To listen to our clients, to be flexible, fast, simple and convenient, to use modern technologies, and to constantly improve the level of service are the formula for Alfa-Bank’s success. This approach has kept Alfa-Bank at the top of Russia’s private banks for years and results in an increase in its number of clients annually: persons, individual entrepreneurs, and legal entities.

ALFA-BANK 2017

branches and offices 762
employees 25 340
corporate clients 420 000
retail clients 14,4
net profit, USD million* 798
equity, USD million* 6 382
loan portfolio, USD million 28 562
total assets, USD million 44 728

* For the purposes of this report, the term «Alfa-Bank» is used to describe ABH Financial Limited and its subsidiaries.
ALFA-BANK’S AWARDS IN 2017

01.2017
Alfa-Bank named No.1 book-runner amongst Russian banks in 2016
Alfa-Bank was No.1 book-runner amongst Russian banks and No.4 amongst global actors on the CIS syndicated loan market, according to the news agency Bloomberg.

02.2017
S&P Global Ratings upgrades outlook on Alfa-Bank’s ratings from stable to positive
On February 20, 2017, S&P Global Ratings upgraded the outlook on Alfa-Bank from stable to positive and affirmed its "BB" long-term rating. The agency indicated strengthened capitalization of the bank and improved its capital buffers achieved by the USD 700 mln issue of perpetual subordinated Eurobonds in late 2016. The agency believes that Alfa-Bank will demonstrate higher profitability and asset quality than comparable Russian private banks over the next two years.

03.2017
Fitch Ratings upgrades outlook on Alfa-Bank’s ratings from negative to stable
On March 30, 2017, Fitch Ratings upgraded the outlook on Alfa-Bank’s ratings from negative to stable and affirmed its Long-Term Issuer Default Rating at “BB+”. The revision reflects the agency’s opinion that the pressure on Alfa-Bank’s asset quality and performance has been reduced due to general economic stabilization in Russia.
Alfa-Bank’s ratings, which are the highest amongst Russian private banks, are based on its well-developed business, substantial clientele, which includes the biggest and most reliable state-run and private companies, strong management, and its history of successfully dealing with crises on the Russian market.

04.2017
Alfa-Bank leads in Financial Sphere Award
Alfa-Bank won in 6 categories in the Financial Sphere Annual Innovations and Financial Achievements Award established by the journal Bankovskoye Obozrenie (Banking Review). Mikhail Povaly, ex-member of the Alfa-Bank Executive Board and Head of Retail Business, was named Person of Retail. Alfa-Bank’s Private Banking won in the “New Russian Private” category, which was introduced first time this year. Irina Elistratova, Director of Alfa-Bank’s BI Center, was declared the winner in the IT Head category. In addition, Alfa-Bank was victorious in the Reporting Implementation and Marketing

04.2017
Bank releases best corporate journal, employs best editor
Alfa-Bank was evaluated positively by corporate media market journals, winning the Best Corporate Media 2017 contest. The journal Alfa-Navigator was elected Best Corporate Journal, and Corporate Media Chief Editor, Mikhail Ivanov, was named Best Corporate Media Editor. The contest was hosted by the Russian Association of Communication Directors and Corporate Publishing. More than 150 companies from all over the CIS competed in 20 categories. The contest’s expert board comprised authoritative specialists in the publishing business and corporate PR.

05.2017
Moody’s Investors Service upgrades Alfa-Bank’s Baseline Credit Assessment to ba2 from ba3
On May 24, 2017, Moody’s Investors Service upgraded Alfa-Bank’s Baseline Credit Assessment (BCA) and adjusted BCA to ba2 from ba3 and affirmed the “Ba2” long-term local- and foreign-currency senior unsecured debt and deposit ratings with a “Stable” outlook. The upgrade reflected the agency’s opinion that Alfa-Bank’s financial indicators have improved and Moody’s expects them to remain stable in the long-term.

05.2017
Alfa-Bank first again in terms of Forex turnover in Central and Eastern Europe
Alfa-Bank’s Forex business has been the biggest in Central and Eastern Europe for two years in a row, according to the annual rating by the Euromoney portal. The bank occupied 23th place in the global rating alongside major investment banks and funds. This position reinforces the excellent choice made by the bank’s current clients and offers potential clients new opportunities to obtain support from Alfa-Bank for their foreign economic activity. The Forex market survey by Euromoney magazine is the only acknowledged Forex market rating.
06.2017
Private banking clients name Alfa-Private best banking brand in 2017, according to Frank Research Group
Alfa-Bank was a laureate in the Best Banking Brand nomination by private banking clients in 2017, according to the Frank Research Group research company. The survey covered 17 banks controlling 75% of the Russian wealth management service. Frank RG Private Banking Rating is an annual rating of banks offering private banking services in Russia; it is based on a profound analysis of major indicators and offers made to wealthy clients. A uniform rating of compliance with the criteria of the classic wealth management model was presented in 2017.

07.2017
Alfa-Bank website named best for small business by Markswebb
The Markswebb Rank&Report analytical agency assessed the efficiency of Russian bank websites as channels for settlement and cash services for small business. The Alfa-Bank website was recognized as the best for opening an account.
The best website was chosen by three types of potential clients: prospective entrepreneurs, incumbent entrepreneurs, and accountants participating in the choice of the bank for opening an account.

08.2017
Expert RA assigns credit rating ruАА to Alfa-Bank
On August 29, 2017, RAEX Rating Agency (Expert RA) assigned credit rating ruАА to Alfa-Bank. The rating outlook is stable. This rating more than meets regulatory requirements, including those associated with the deposit of federal budget funds, which requires that a financial entity is rated by both Expert RA and the Analytical Credit Rating Agency (ACRA). Alfa-Bank was the first systematically important bank to receive an ACRA rating in November 2016. Expert RA believes that Alfa-Bank, a systematically important bank and the largest Russian private bank, occupies solid positions in lending and retail and corporate banking, and surpasses other private banks in terms of individual deposits and retail demand accounts. The agency praised the bank's operating income diversification and the high level of operating expenses coverage by net interest and fee and commission income. The broad geography of operations and the bank's highly diverse clientele and corporate loan portfolio by sectors contributed to the positive rating. The agency also approved of the efficient risk management system, the high quality corporate governance, and the positive public credit history, including over a decade of attracting subordinated bonds, as well as perpetual loan participation notes, on global capital markets. The agency's analysts recognized the good liquidity cushion and the bank's access to a broad range of additional liquidity sources.

09.2017
Alfa-Bank shareholders, top managers rank highly in Top 1000 Russian Managers rating
Alfa-Bank’s shareholders and top managers ranked highly in the Top 1000 Russian Managers rating by the Russian Managers Association and the publishing house, Kommersant. Once again, Member of the Board of Directors, Mikhail Fridman, and Chairman of the Alfa-Bank Group’s Board of Directors ABH Holdings S.A., Petr Aven, were named the “leading businessmen and managers of strategic enterprises creating the Russian economy’s image.”
Alfa-Bank ex-Chief Executive Officer, Alexey Marey, headed the rating of private bank top managers.
The Co-Head of Alfa-Bank’s Corporate Investment Bank, Maxim Pershin, ranked second in the relevant rating.
Leonid Ignat, Alfa-Bank’s ex-Head of Corporate Communications, again topped the list of private bank corporate and public relations directors, and Mikhail Grishin was the best among legal department directors.
Alfa-Bank’s CFO, Alexey Tchoukhlov, ex-Head of Information Technologies, Martin Pletsky, ex-Human Resources Director, Shlomit Gruman-Navot, and Marketing Director, Oksana Belyaveva, were also listed in the relevant Top 3 ratings.
The Top 1000 Russian Managers rating has been annually published for 18 years and is regarded as an impartial evaluation of the professional reputation of top Russian managers.

09.2017
Alfa-Bank wins Visa international awards for security and focus on clients
Alfa-Bank won the 2016 Visa Global Service Quality Award of the Visa international payment system for the provision of high-quality operational services to its clients who are Visa cardholders. For the fourth time in a row, the bank won in the Best International Risk Efficiency and Chargeback Effectiveness categories. Alfa-Bank was named the best one among the 21,000 member banks of the Visa international payment system.
The Best International Risk Efficiency nomination is based on the minimal ratio of frauds to the total number of transactions amid the highest number of approved transactions. The winner needs to establish a correct and optimal risk-monitoring mechanism with the best level of successful transactions. The Chargeback Effectiveness nomination is based on the processing of client claims relating to transactions and their reimbursement.

09.2017
Alfa-Private named top private bank in Forbes rating
Alfa-Bank has been named the top private bank in the Forbes annual rating of banks offering private banking services and was ranked third in the general rating. This is an improvement by one position since 2016.
Moody’s Investors Service upgrades Alfa-Bank’s rating from Ba2 to Ba1

On October 31, 2017, Moody’s Investors Service upgraded Alfa-Bank’s local-currency long-term deposit rating and local- and foreign-currency senior unsecured debt ratings to Ba1 from Ba2. The agency affirmed the bank’s Ba2 foreign-currency deposit ratings that are constrained by the foreign-currency deposit ceiling of Russia. The outlook on these ratings was stable.

The agency noted an improvement in the bank’s asset quality in the first half of 2017: the bank managed to reduce the share of non-performing loans from the peak level of 12.7% in late 2015 to 9.2%. The lower cost of risk and funds significantly improved the bank’s profitability: in 2016 the bank reported 1.5% return on average assets with a further increase to 2.2% (annualised ratio) in the first half of 2017. The lower cost of risk and funds significantly improved the bank’s profitability: in 2016 the bank reported 1.5% return on average assets with a further increase to 2.2% (annualised ratio) in the first half of 2017. The agency recognized the high level of capital adequacy and liquidity supported by the constantly growing deposit base: the share of liquid assets stood at 28% of Alfa-Bank’s total assets.

Alfa-Bank wins Best Private Banking Russia Wealth & Money Management Awards 2017

The Wealth & Finance magazine has announced the winners of Wealth & Money Management Awards 2017. Alfa-Private of Alfa-Bank, the only Russian bank nominated for the award, was named the winner in the Best Private Banking Russia category.

The Wealth & Money Management Awards 2017 recognize dedicated and selfless work in the field of asset management, financial planning, private banking for high net worth individuals, and specialized banking services.

Alfa-Bank leads by individual entrepreneur current account opening

Alfa-Bank has been named one of the top 3 banks in terms of easy and convenient processes associated with current accounts opening for small business. The Markswebb Rank & Report analytical agency ranked Alfa-Bank second in terms of the length of interaction with the bank: it took slightly more than 30 minutes to open the account, which included a meeting with the client manager.

The mystery shopper research was carried out in June-August 2017. Mystery shoppers opened individual entrepreneur accounts in 20 Russian banks and recorded the entire process, from filing an application online to the moment the client’s current account was opened and the Internet banking service was connected. The account opening process was evaluated according to four criteria, namely: the possibility to open the account without visiting a bank office, the total time spent interacting with the bank, the overall complexity of interaction with the bank, and the overall waiting time for the bank’s response (excluding days off).

Alfa-Private of Alfa-Bank has won the client award in SPEAR’S Russia Wealth Management Awards 2017, Russia’s only private banking and wealth management award, and was thereby recognized as the best Russian wealth management and corporate bank.

It was the 9th SPEAR’S Russia Wealth Management Awards ceremony. The award is an analogue of the UK’s SPEAR’S Wealth Management Awards which is awarded annually by the journal SPEAR’S UK in London. The award’s organizers include the journal SPEAR’S Russia and the website PBWM.ru.

Alfa-Direct wins Digital Heights Award

The Alfa-Direct mobile application has won the Digital Heights Award in the Best Financial Management and Reporting System category. The award ceremony took place at Skolkovo Techno-Park on December 14.

Digital Heights is the national IT award recognizing the best domestic efficiency solutions. The jury included representatives of big and medium business, civil servants, venture investors, employees of government funds supporting business, and the media. The jury assessed the importance of the problem addressed and the efficiency of its solution.

The award is supported by the Russian Economic Development Ministry, the Russian Communications and Mass Media Ministry, the Russian Presidential Academy of National Economy and Public Administration, and Skolkovo Techno-Park.

Forbes named Mikhail Fridman Businessman of the Year

The business magazine has acknowledged the 2017 investment activity of Mikhail Fridman. Mr. Fridman is the only entrepreneur to be named Businessman of the Year by Forbes for a second time.

Five years ago, Mr. Fridman was chosen as the principal organizer of the sale of a 50% stake in TNK-BP to Rosneft for USD 28 bln. The LetterOne Holding was established in Luxembourg in 2013 for investing these funds in the West. LetterOne closed two major deals in 2017: it bought the UK healthy food chain, Holland & Barrett, for USD 2.3 bln, and invested USD 3 bln in Pamplona Capital Management’s new fund.
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We are pleased to present Alfa-Bank's Annual Report 2017: last year was yet another successful period in the development of our financial institution. The Bank again demonstrated a growth in key financial performance indicators and proved its status as the largest private bank in the country. In accordance with IFRS, Alfa-Bank's net profit increased by 1.5 times and amounted to USD 798 mln, while net interest income grew by 26.9% and net fee and commission income went up 33.4%. The number of our clients also increased significantly.

The success of the entire Bank means the success of every business block. All business lines achieved impressive results in 2017 by following the common strategy and gaining additional advantages through efficient cooperation. Alfa-Bank was the only private bank to be named among the country's top 10 financial institutions working with large business. This chiefly owed to the Corporate Investment Bank's team. Our work with medium and regional businesses boosted operating profit significantly and resulted in a considerable increase in the number of active clients. The Mass Business block surpassed its targets and showed excellent performance in terms of profit growth.

As for our work with retail clients, remarkable results were achieved not only by Retail Bank, whose share hit a historic maximum of 3.11% at the end of the year, but also by Alfa Private, which was established as a separate unit interacting with the premium segment and which we expect will become the best bank service for Russian-speaking affluent clients in the near future.

Alfa-Bank has always been a high-tech bank; there is no doubt that this is the only efficient model in our fast and mobile world. Our retail and corporate clients are already able to perform many operations using a single instrument — their phone. This enables us to actively broaden the geography of our services, and we were certainly doing so last year. It is now possible to become an Alfa-Bank client even in regions where the Bank has no presence. We want to be closer to our clients and to provide convenient services wherever and whenever they are required.

Alfa-Bank will never cease to develop, and so our plans for the future are ambitious. We aim to double our business within several years. We do not doubt that we will achieve our goals because we are sure we are on the right track. To listen to our clients, to be flexible, fast, simple and convenient, to use modern technologies, and to constantly improve the level of service are the formula for Alfa-Bank's success. This approach has kept Alfa-Bank at the top of Russia's private banks for years and results in an increase in its number of clients annually: individuals, entrepreneurs, and legal entities.
Alfa-Bank Entities

Abakan
Airmetyevsk
Angarsk
Arkhangelsk
Achinsk
Balashikha
Barnaul
Belgorod
Berdsk
Biisk
Buzuluk
Vladivostok
Vladimir
Volgograd

Alfa-Bank subsidiaries and partners geographic coverage:

Alfa Capital Markets
(Branch of Alfa Capital Holdings (Cyprus) Limited)
UK, London
Amsterdam Trade Bank N.V.
Netherlands, Amsterdam
Alfa Capital Holdings (Cyprus) Ltd.
Cyprus, Nicosia
Alfa-Bank Kazakhstan
Almaty, Astana, Aktau, Karaganda, Ust-Kamenogorsk, Uralsk
MESSAGE FROM ACTING CHIEF EXECUTIVE OFFICER

Assessing the results of 2017, I would like to begin by saying that Alfa-Bank successfully accomplished its strategic task of raising its significance as a leading actor in the national financial market. All key indicators of our financial activity improved, confirming the Bank’s leadership as the biggest private bank in Russia.

If we talk about specific figures, they prove this assessment: in accordance with IFRS, Alfa-Bank’s net profit grew by 1.5 times and amounted to USD 798 mn in 2017, net interest income increased by 26.9% and net fee and commission income by 33.4%. Furthermore, we supplemented the growth of our loan portfolio with an improvement in its quality: under IFRS, share of overdue loans for more than 90 days decreased to 2.3%, which is one of the lowest indicators in the Russian banking market and achieved unique rates of soft collection in Retail Business — 96.8%.

Alfa-Bank’s business units also achieved their goals and increased their share in market segments crucial to the Bank — retail and affluent client service and mass and medium corporate business, and retained steady positions and an adequate risk portfolio in the large corporate business segment.

Another important feature of last year was the high degree of employees’ involvement in every process, which improved the quality of banking services and client satisfaction generally and also had a positive influence on the number of the Bank’s active clients.

Alfa-Bank’s successes were particularly impressive in light of the increasing competition between banks. The government’s presence in the banking sector has been growing amid a reduction in the number of large private banks, which has increased pressure on the business margin and influenced the behavior of market majors. The intense activity of non-financial entities, which continue to gain a foothold in the market of financial companies, should also be taken into account. This is especially true of technological companies offering modern and innovative approaches to classic financial products.

The Bank’s development strategy relies on its competitive edge and takes into account specific features of other entities. It will thus be especially important in the predicted climate. Alfa-Bank monitors the market situation closely, which enables it to deal with the pressure coming from other banks and non-financial entities. This is reflected in the results of last year.

As for the five-year strategy of Alfa-Bank, it is our aim to double the number of active clients in Retail Bank, and to at least double the number of clients in Mass and Medium Corporate Business segments. As a result, the Bank’s share and significance on the market will double compared to 2016 and the number of active clients will reach 10 million by 2022. Importantly, our strategy implies high business efficiency, cost to income ratio of at the level of not more than 50% and its further reduction, and expected rate of return on equity from 12% to 15%.

We intend to achieve these goals by actively implementing modern technologies at each level of our business and an innovative approach to information technologies. Innovations are helping us to do more with fewer resources and to simultaneously improve client service, rendering it easier, faster, and more convenient. Modern technologies give us a competitive edge over non-financial entities, which tend to be high-tech and provide fast client service. Alfa-Bank also boasts these advantages and supplements them with its expertise as the leading private bank of the country, its strict compliance with regulations, its stable reputation, and the trust of millions of clients.

It is a challenging task for any company to win the trust of clients, so the Bank not only preserves but constantly bolsters the loyalty of its clientele by encouraging more entities and individuals to become of its brand. We create remarkable and positive client experiences and this sets us apart from our rivals; we have a better understanding of clients’ needs and provide a faster response to their wishes, even the hidden ones. Our client service strategy is based on adjusting to their needs, which tends to be high-tech and provide fast client service. Alfa-Bank also boasts these advantages and supplements them with its expertise as the leading private bank of the country, its strict compliance with regulations, its stable reputation, and the trust of millions of clients.

Another priority is maximum accessibility of our products and services via mobile devices. The world will soon be one where clients perform every significant action by means of a mobile phone whenever and wherever it is convenient. The Bank is no exception, which means such services should be accessible via a mobile gadget 24/7. It is our task to give clients remote access to every routine operation while retaining the possibility to do so in a Bank office.
Finally, Alfa-Bank prioritizes a high level of client service and further improvement of client experience at every point of contact, whether it be the classic Bank office, or the call center, or the mobile application. Every channel of interaction between the Bank and the client should be consistent, stable and satisfying. The use of state-of-the-art technologies is an important component of this work, since technical support of external communication channels and internal processes is vital to upholding a safe client service and the rapid and efficient accomplishment of tasks. We aim to use technologies to improve all aspects of the Bank's activity, both external — pertaining to products and interaction with clients, and internal — that is, processes which are invisible to our clients.

In addition, we are focused on optimizing and simplifying cooperation between all units involved and creating cross-block teams, which cuts expenses in comprehensive projects and provides faster and better solutions to any problem we may face.

As for the performance of particular business blocks, every single one was successful last year. Corporate Investment Bank exceeded targets in every priority area and reaffirmed Alfa-Bank's stable position amongst Russia's top 10 banks working with big business. The Bank's corporate credit portfolio grew by 15.3%, net interest income practically doubled, and the share on the corporate lending market increased to 4.20%. While developing its business, the Bank did a lot to manage current liabilities and successfully resolved complex situations with distressed clients, offering solutions which were favorable to both the Bank and the client themselves.

The Bank's strategic focus on client needs was especially noticeable in investments. Thanks to our cooperation with U.S. investment funds and European partner banks, we have been able to provide a plethora of opportunities for international financing and investment in international assets.

Our investment capacities have been further expanded by the Alfa-Investments project, which will enable our clients to buy investment products in just 1 or 2 clicks with their mobile phone. We expect the project to be as fruitful as the update of our Alfa-Direct mobile terminal, which was recognized as the best market solution in several contests held throughout 2017.

Our Medium and Regional Corporate Business segments were no less successful last year: operational revenue grew by one and a half times, and the number of active clients increased by 43% in Medium Corporate Business and by 38% in Regional Corporate Business. Importantly, most of our operational revenue was risk-free thanks to the excellent quality of the Bank's transaction business.

In addition, Mass Business revenue significantly exceeded last year's targets and increased the market share by 1.3%, averaging 6.1% across the country. The block markedly increased its clientele to more than 360,000 companies and individual entrepreneurs as of the yearend. Alfa-Kassa and onsite acquiring were landmark projects of 2017. Alfa-Bank considers these areas to be extremely promising and intends to increase its share on the trade-acquiring market to 7% three years from now. The establishment of the Compliance Risk Department was important for work with mass clients. We monitor compliance with all laws and regulations very closely, and the new department will treat every case with even greater care to ensure compliance and to avoid mistakes. Due to the number of client operations and the general scope of our work, the Bank has automated many processes.

Retail business has always been a priority of Alfa-Bank, which aims to become the principal bank of an ever-increasing number of clients. 2017 was no exception. We successfully broadened our interaction with existent clients and attracted new ones by offering products inherent to every person's life (such as cards with additional benefits, or family accounts) and improving quality of life (for instance, mortgage loan programs), by developing technologies which moved current operations to our clients' mobile phones, and by invariably maintaining a high level of service. Financial performance indicators of the block prove that our strategy has been successful: the net revenue of the block has grown, as has the total market share for all types of products. As of late 2017, the Bank had over 14 mln retail clients.

The emergence of a separate business block, Alfa Private, which provides comprehensive service to affluent clientele, was another of last year’s successful projects. This is evident from the 1.5 times growth of assets managed by the business block. Today we can offer our affluent clients in Moscow and regions all products of the Bank and its partners, as well as unique remote access and, naturally, uninterrupted service 24/7. We are confident that we will soon be providing the best service for Russian-speaking clients in this segment both inside and outside Russia.

A focus of 2017 was the successful use of Alfa-Bank's status as the first regional partner of the FIFA World Cup™ to further develop our client database. The effort will continue in 2018. Last year, the Bank, an official bank of FIFA World Cup 2018™, issued a card with the exclusive design of the FIFA World Cup Trophy and launched numerous special projects enabling many clients to attend Cup matches. Our Bank is an ambassador of football in the business community; this status demonstrates that the culture of a successful bank is a culture of victory and, of course, a team culture. We set ambitious tasks and achieve them as a team, and football inspires the successful continuation of our joint activities.

The importance of teamwork is a specific feature of Alfa-Bank's corporate culture, in addition to the constant professional development of our employees. The Bank recruited many young specialists in 2017 and their youth certainly doesn't hamper their success or their ability to make valuable contributions. Alfa-Bank offers the perfect chance for professional development and career growth; it listens to the ideas of its employees, and encourages each of them to speak up. This attitude is appreciated, as demonstrated by the reduction in employee outflow last year.

A number of managers joined us in 2017. The appointment of Michael Tuch as Head of Retail Business was a significant event for the Bank. Tuch is very experienced in developing financial retail products in the biggest companies of our country; he is a top-notch professional. We are confident that his appointment has strengthened our team and hope that Retail Bank will be even more successful under Michael's supervision. Darya Kozyreva, who has many years of banking experience, accepted a position as Head of Corporate Communications.

We will continue to work hard over the coming years, as we have serious objectives to meet. Alfa-Bank is driven to be even more efficient and high-tech in order to do so. We aim to further develop banking technologies and to bring the best Western models and standards to Russia in order to use them for the benefit of our clients and to enhance the client experience.

In the short term, our key task for 2018 is to continue sustainable development and to increase revenue while maintaining our current strategic focus. Once again, next year will be a year of growth in retail and mass business. We are already doubling our share on the market while steadily maintaining profitability, which is a key objective that Alfa-Bank has set for itself for the next few years.
RATIONALE: Alfa-Bank is the only private bank in Russia amongst the top ten financial institutions interacting with big corporate business thanks to its competitive edge: flexibility, capacity for fast decision-making, and high efficiency.
OVERVIEW OF RUSSIAN ECONOMY AND BANKING SECTOR

World economy in 2017

In 2017, the world economy was influenced by a number of factors which will dictate global developments in the coming years. Firstly, global growth rates accelerated from an average of 3.3% y/y in 2012-16 to 3.6% y/y in 2017 and, according to forecasts, will reach 3.9% y/y in 2018 (see Fig. 1). The better growth outlook is attributable to improving trends in developed countries, supported by the monetary easing of previous years and the recent recovery in the financial markets. The US markets, in particular, showed steady growth in 2017: the S&P 500 advanced by 19% and the Dow Jones increased by 25%. European markets also saw growth, albeit at a slower pace — the StoxxEuro600 rose by 8% last year. The market growth was driven, to a large extent, by tech stocks: the NYSE FANG+ index, which includes Facebook, Apple, Netflix and Google, has advanced by 58% since the beginning of 2017 (see Fig. 2).

Secondly, an important factor supporting the global economic recovery last year was the general shift in favor of softer budget policy. US tax reforms, which came into effect in 2018, are expected...
OVERVIEW OF RUSSIAN ECONOMY AND BANKING SECTOR

Fig. 3. US GDP and budget deficit, % y/y and % GDP

Sources: FED, US Dep. of Agriculture, Alfa-Bank

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<th>GDP, % y/y</th>
<th>Budget deficit, GDP, % y/y (RHS)</th>
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<tbody>
<tr>
<td>2007</td>
<td>1.5%</td>
<td>-3.2%</td>
</tr>
<tr>
<td>2008</td>
<td>2.3%</td>
<td>-3.5%</td>
</tr>
<tr>
<td>2009</td>
<td>2.7%</td>
<td>-3.7%</td>
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<tr>
<td>2010</td>
<td>2.5%</td>
<td>-4.1%</td>
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<tr>
<td>2011</td>
<td>2.1%</td>
<td>-4.4%</td>
</tr>
<tr>
<td>2012</td>
<td>2.1%</td>
<td>-4.8%</td>
</tr>
<tr>
<td>2013</td>
<td>2.0%</td>
<td>-5.1%</td>
</tr>
</tbody>
</table>

Fig. 4. Corporate profit tax rates by countries, 2017 and 2020-25, %

Sources: OECD, Alfa-Bank

- USA: 21% (2017), 14% (2020-25)
- France: 25% (2017), 19% (2020-25)
- Japan: 31% (2017), 24% (2020-25)
- Australia: 30% (2017), 23% (2020-25)
- Norway: 31% (2017), 25% (2020-25)
- UK: 35% (2017), 33% (2020-25)

to drive US economic growth going forward. As a result, the IMF recently revised upwards the country’s 2018 GDP growth outlook from 2.3% y/y to 2.7% y/y and upgraded the projection for 2019 from 1.9% y/y to 2.5% y/y (see Figure 3). There is similar rhetoric emanating from the EU, where countries are unveiling proposals to cut corporate tax rates: at the end of December 2017, the French President, Emmanuel Macron, confirmed plans to slash corporate profit tax from 33% currently to 25% by 2022; and the UK Prime Minister, Teresa May, announced a plan to cut the corporate profit tax rate there from 19% currently to 17% by 2020 (see Fig. 4). Since the end of 2017, discussions have been underway in Germany to reduce corporate profit tax. Thirdly, the acceleration in global economic growth offered an avenue to end monetary easing. In 2017, the Federal Reserve raised its key policy rate three times to end the year at 1.25-1.50%. The Bank of Canada increased its interest rate twice last year from 0.5% to 1.0%; while the Bank of England hiked its policy rate from 0.25% to 0.50% in 2016-17. The plan envisages cutting the Fed balance sheet by approximately USD 400 bn in 2018 and by a further USD 600 bn annually thereafter to the end of 2021, or until a level of USD 2.2 tn is achieved (see Fig. 5). The ECB has not yet announced plans to taper its policy (see Fig. 6), but it has already scaled-back its asset purchase program, reducing it by half from EUR 60 bn
Fourthly, the specter of trade restrictions surfaced in 2017. Protectionism poses a substantial risk to world economic development in the coming years: the US is currently considering the introduction of trade restrictions on approximately 1,300 Chinese products, amounting to around USD 50 bn, which constitutes 10% of annual US imports from China. In response, China is threatening to introduce restrictions on 106 US products (cars, petrochemicals as well as soybeans), representing around 30% of the value of Chinese imports from the US. Meantime, President Donald Trump has responded by requesting an additional list of products be drawn up for potential trade restrictions, amounting to a total value of USD 100 bn. Tit-for-tat threats between the world's two-largest economies is creating a high level of uncertainty and may impede global economic growth by damaging existing value-added chains.

Finally, the global economy remains burdened by the unresolved problem of indebtedness. Although the issue of excessive debt burdens in some countries and bad loans in others did not come into the focus of international experts in 2017, the problem cannot simply be swept under the carpet. As of end-2017, the debt burden of the G20 countries totaled a staggering USD 135 tn, almost double that of 2007, when it amounted to an aggregate of only USD 80 tn. Corporate debt, including S&P 500 companies, has increased two-fold since 2010. The number of corporate defaults globally continued to grow steadily and totaled 162 in 2016 (up from 113 in 2015), the highest level since 2009. This problem is country-specific; cumulative debt in China exceeded 230% of GDP last year. Although lending growth is providing short-term stimulus to the Chinese economy, in essence, it is simply delaying a much-needed adjustment; high debt levels pose a risk, which could damage future Chinese growth.

Russia: economy returns to growth

After two years of recession, which cost 2.7% of GDP, the Russian economy returned to a growth trajectory in 2017. According to initial government forecasts, the Russian economy was projected to expand at 2.0-2.1% y/y last year, however a second estimate by Rosstat in April confirmed Russian economic growth at 1.5% y/y only in 2017.

The problem for the Russian economy, however, is not just the modest scale of the growth recovery, but the high level of instability prevalent in the growth indicators. According to the latest estimate, GDP growth accelerated to 2.5% y/y in the second quarter of last year; however, by 4Q17, the pace of growth had decelerated to just 0.9% y/y. This erratic growth pattern is also
in fixed capital investments. In the second quarter of 2017, this indicator grew by 5.0% y/y, but already by the following quarter, it had decelerated to 2.2% y/y. A similar situation can be observed in industrial production, where output unexpectedly fell by 1.7% y/y in 4Q17 (see Fig. 7). This came despite the fact that, traditionally, the final months of the year generally see an uptick in growth driven by budget support.

The structure of the growth is also a cause of concern: last year’s statistics pointed to a strong concentration of growth in several segments of the economy. Firstly, commodity extraction remained the driving force of industrial production growth as well as investment growth. Despite Russia’s participation in the OPEC+ production cut agreement, the commodity extraction sector demonstrated the highest level of growth in 2017 (+2.0% y/y) and was among the top-four fastest growing economic segments since 2013. At the same time, growth in manufacturing output was just slightly positive at 0.2% y/y in 2017 (see Fig. 8). Commodity extraction accounted for around half of last year’s investment growth. Secondly, there are structural concerns related to the increased share of the state in the economy. Around 30% of Russia’s investment recovery last year was attributable to just two regions, where investment activity was driven by state residential (Moscow city) and infrastructure (Crimea) projects.
It is worth mentioning that despite the aforementioned weakness in the economic indicators and in spite of the Russian presidential elections, the government managed to maintain a highly balanced and prudent budget policy. In 2017, federal budget expenditure contracted by 0.4% y/y. Another important achievement by the government last year was its success in tax collections. According to Finance Ministry estimates, around RUB 1 tn, or 40%, of the extra tax revenues in 2017 were the result of improved government efficiency in tax administration. Budget revenue growth helped to reduce the consolidated budget deficit to 1.5% of GDP vs. a 2.6% of GDP deficit in 2013-16; the consolidated non-oil budget deficit also recovered to 8.1% of GDP vs. a 10.2-10.6% of GDP range recorded since 2013 (see Fig. 9). As of end-2017, the federal budget breakeven oil price had declined to USD 67/bbl from USD 78/bbl in 2016. Thanks to the budget rule, which dictates that additional budget revenues above USD 40/bbl must be channeled towards savings, the Finance Ministry managed to purchase USD 14 bn of foreign currency last year. As a result, the National Welfare Fund, which now consolidates all government savings, totaled USD 65 bn as of end-2017 (see Fig. 10). Monetary policy remained moderately tight in 2017. Over the course of last year, the CBR continued to cut its key policy rate toward equilibrium. As a result, the key rate was reduced from 10% at the start of the year to 7.75% by the year-end. The rate cut took place under a strong deceleration in inflation, which came significantly lower than its targeted level of 4%, having reached 2.5% y/y in 2017.

That said, one should not forget the significant contribution of the deflationary trend in the food segment as a result of the bumper harvests of 2016 and 2017. The deceleration of inflation is an indisputable achievement of CBR policy that will enable the Central Bank to gradually move to neutral monetary policy, i.e. bring the key nominal rate to neutral position of 6-7% in 2018.

Banking sector consolidation continues

The pick-up in economic growth in 2017 created a solid backdrop for the recovery in loan activity. The retail loan portfolio grew by 13% y/y in 2017. In a positive development, the non-mortgage loan segment began to recover from May 2017, ending a two-year period of contraction (-14%) that had started in March 2015. In the mortgage segment, growth remains stable and reached 17% y/y in 2017 (see Fig. 11), supported by a series of cuts in the CBR key policy rate during last year.

However, the structural weaknesses discussed in the previous section had a negative effect on the corporate loan portfolio. As of end-2017, the corporate loan portfolio had stopped shrinking, although it remained stagnant and two divergent trends emerged in the foreign currency and ruble-denominated segments. Almost up to the end of 2017, companies actively deleveraged...
from the forex segment: the foreign currency loan portfolios of Russian banks contracted by 24% y/y in December 2017 vs. a 39% decline in 2015; as of end-2017, it amounted to only USD 101 bn in nominal terms, vs. USD 134 bn in 2016, and USD 165 bn in 2015. Regarding the ruble loan book, a recovery in demand started in August 2017, which neutralized the shrinking forex part of the corporate loan portfolio. As of year-end 2017, ruble loans grew by 11% y/y (see Fig. 12). However, as the acceleration of the ruble portfolio was combined with a slowdown in economic growth, it looks likely that the pick-up in lending activity could reflect corporate preferences in favor of ruble-denominated loans prior to a possible tightening of sanctions.

The relatively tight monetary policy implemented by the CBR (key rate of 7.25% as of March 2018) ensured a stable deposit base growth. In 2017, retail deposits increased by 7% y/y, including 12% y/y growth in ruble-denominated deposits. Corporate accounts demonstrated more moderate growth rates, adding 2% y/y in 2017; while corporate ruble-denominated deposits delivered strong growth of 9% y/y. Due to a steady inflow of deposits and limited lending activity, the banking sector is operating in an environment of excess liquidity, which is being sterilized by the CBR. At the start of 2017, the CBR sterilized around RUB 0.5-1.0 tn of banks’ liquidity and by the end of 2017 that figure had grown to RUB1.6-2.0 tn.

That said, the key watch factor of 2017 was the restructuring of three large private banks, which were taken under the umbrella of the Banking Sector Consolidation Fund (BSCF), owned by the CBR. The banking sector cleanup launched in 2013 continued in 2017. As a result, the number of banks has dropped from 897 in 2013, to 575 in 2016, and 517 as of end-2017 (last year the number of banks was reduced by 58). However, in the second half of 2017, this process started to affect a number of large privately-owned banking groups for the first time. During this period, the CBR entered the capital of three large privately-owned banks — Otkritie, B&N and Promsvyazbank — which accounted for around 5% of total banking assets, as of end-2017, 2-3% of the credit market and 3-5% of the deposit market (see Figure 13). Concerns over the stability of private banking groups has also led some clients to transfer their accounts to state banks, expanding the large state presence in the sector. As a result, the share of state banks (excluding the newly created BSCF) in corporate lending grew to 71%, while their share of corporate and retail deposits expanded to 63% (see Figure 14). The key question for the coming years is the ability of the CBR to exit the capital of the rescued banks, and whether it can sell these assets to private investors. So far, the foreign presence in the sector is decreasing and private banks are experiencing strong competition from state-owned institutions, thus making the task ahead more challenging.
DETERMINATION: Alfa-Bank is always ready to negotiate with clients and reach an understanding on problems of any complexity. This policy bolsters the Bank's potential and position of a creditor on the Russian market of borrowings.
CORPORATE INVESTMENT BANKING

In 2017, we were successful in dealing with companies representing large corporate business. This was evidenced by our annual financial performance. The net profit target was exceeded, while the net profit was USD 968 mln according to IFRS; and the Bank’s share of the corporate lending market increased while the corporate loan portfolio grew by 15.3% to USD 24,152 m and the share of the corporate lending market increased to 4.20% compared with 3.60% in early 2017. The net interest income of the Corporate-Investment Banking actually doubled to reach USD 1,222 mln. It is worth noting the high quality of the loan portfolio. The share of corporate loans overdue more than 90 days is one of the lowest in the market and is 2.0% in 2017 compared to 4.6% in 2016 according to consolidated IFRS financial statements. At the same time, coverage of this overdue debt with reserves is 120%.

Despite the difficulties related to increase in share of government in financial market, the Corporate Division expects to see the same positive results in 2018, if not better; ensuring greater return on the assets already currently available, making the most of the internal and external market opportunities to achieve a further increase in the corporate lending portfolio and riskless income, as well as ensuring a several-fold increase in transactions involving shareholders.

Assessing the market situation in the area of large corporate business financing in 2017, it is worth noting that there were no serious changes in the market from the previous year. The characteristic trends of the past several years, related to customer base diversification, continued. The share of the fee based income also remained on the increase, as well as high-margin complex structured finance transactions and special focus on improving efficiency and adaptability to the banking business. The regulator became even more significant in the life of the Bank, and the competition with the banks wholly or partially owned by the government, which have considerable administrative leverage and financial resources, became even tougher. Today, in certain cases, the Bank of Russia employs a more flexible approach to dealing with such banks both in the context of provisioning as well as in complying with various restrictions. Alfa-Bank is the only private bank in Russia to be one of the ten leaders working with large corporate businesses, despite the above-mentioned complications. This is thanks to its competitive advantages: flexibility, fast decision-making and high efficiency.

Lending to Large Businesses

Last year, lending to large businesses was more active compared to the previous period, as the stable market situation encouraged it. It is worth noting that macroeconomic factors enabled us to be more positive with regard to the business valuation of existing and potential customers. The Bank continued to cooperate with its long-standing partners, increased its presence in the priority business sectors and financed new reliable corporate customers.

Under the loan facility agreement, Alfa-Bank has lent RUB 17.5 bn for 5 years to VimpelCom Holdings B.V., a subsidiary of VEON Ltd. The funds will be used to refinance the current loan debt of VimpelCom Holdings B.V. and for the general corporate objectives. Alfa-Bank has been successfully cooperating with VEON Ltd and VimpelCom Holdings B.V., its subsidiary, for a long time. Therefore, the signing of this agreement is indicative of a strengthening of the long-term relations between the companies.

In 2017, Alfa-Bank and PAO Sberbank also completed a transaction to make a syndicated loan available to Integra Group. The latter received funding totaling RUB 8.7 bn for 5 years to VimpelCom Holdings B.V., a subsidiary of VEON Ltd. The funds will be used to refinance the current loan debt of VimpelCom Holdings B.V. and for the general corporate objectives. Alfa-Bank has been successfully cooperating with VEON Ltd and VimpelCom Holdings B.V., its subsidiary, for a long time. Therefore, the signing of this agreement is indicative of a strengthening of the long-term relations between the companies.

In 2017, Alfa-Bank and PAO Sberbank also completed a transaction to make a syndicated loan available to Integra Group. The latter received funding totaling RUB 8.7 bn for the re-structuring of its current obligations to participating banks with provision of additional recourse financing. The timeframe for performance of all syndicated loan commitments was 6 years, thus enabling the company to significantly extend the terms of the current loan obligations and obtain more funds to replenish its working capital. We look forward to a long relationship with the company and intend to continue our cooperation in the debt financing area.

The Bank actively develops financing of leasing companies. Last year, Alfa-Bank opened a new loan facility for PAO TransFin-M, a leasing company. The company received a RUB 8.5 bn loan facility for up to two years, which is secured by railway cars. The disbursed funds will be used to develop the borrower’s new leasing projects. It is already the fourth loan facility disbursed by Alfa-Bank to PAO TransFin-M, and the total credit limit approved for the companies is about...
RUB 15 bn. The credit limit increase takes the cooperation between the Bank and this market leaders in leasing services in Russia to the next level.

As a result of financing provided by Alfa-Bank, TransFin-M successfully implements its development strategy in the railway sector and related industries. Some of the funds borrowed under the above loan facility have been already used to purchase rock handlers for coal mining in Kuzbass. This area has been under development by TransFin-M since last August and today coal miners are provided with a range of logistic services for the extraction and transportation of coal from the open-pit mine to the railway station.

AO “ALFA-BANK” and AO Etalon LenSpetsSMU (member of Etalon Group) have signed the Loan Facility Agreement for RUB 3 bn. The Loan Facility matures within 5 years and the loan proceeds are made available for a period of up to 4 years and may be used, inter alia, to finance working capital. Alfa-Bank and Etalon Group have been cooperating for a number of years and will look forward to continuing their cooperation.

Alfa-Bank has traditionally been a strong player in the metallurgy sector. In 2017, the Bank provided financing of USD 200 mln to an enterprise belonging to EVRAZ Group — Nizhnetagilskiy Metallurgichesky Kombinat JSC (EVRAZ NTMK). The Bank has been cooperating with EVRAZ — one of the largest industrial groups in Russia — for more than 10 years. A reliable borrower, it has chosen Alfa-Bank as its long-standing financial partner thanks to Alfa-Bank’s fast decision-making and efficient disbursing of amounts comparable to loans issued by the major state banks.

Repayment of Delinquent Debt

In 2017, there was a significant effort aimed at delinquent debt collection and settlement agreements with regard to non-performing loans. Successes were achieved thanks to macroeconomic changes and, first and foremost, to the lowering and stabilization of the USD/RUB exchange rate. This development enabled many companies to repay debts or at least begin this process as their financial standing became more stable. Despite the continuing sanctions against Russia, the country has retained its access to the global capital market. The third contributing factor, which is no less important than the first two, is the expertise of the Bank officers responsible for delinquency-related negotiations. All this has resulted in the reduction of the delinquency amount.

Thus, last March, Alfa-Bank and JSC Uralvagonzavod Research and Production Corporation (UVZ) announced the final resolution of the issue of principal debt repayment by UVZ entities to the Bank. In 2017, UVZ subsidiary — ChTZ-UralTrac LLC — transferred the funds to repay the principal under its loan facility agreements, and in late 2016 the liabilities of Uraltransmash JSC were paid off. The total debt of UVZ subsidiaries to the Bank has been settled.

In addition, Alfa-Bank and Evgeny Giner, the President of PFC CSKA, have settled the issue of delinquency in full by entering into a Settlement Agreement between Alfa-Bank and the following defendants at court proceedings: LLC Eleks-Polyus Kar, LLC Chudovsky Farfor and LLC Start-Aviansentr. The settlement agreement outlines delinquent debt restructuring on mutually acceptable terms and the debt repayment period deemed convenient for the borrower — until 2023 —has been approved. All contentious issues have been resolved to the satisfaction of both parties and all current court cases related to such indebtedness have been closed.

Last year, a settlement agreement was approved between Alfa-Bank and entities of Alexey Kholin, the former owner of Yugra Bank. The agreement indicates that parties decided to fulfill the previously-outlined obligations.

These developments are further evidence of the Bank’s flexible policy towards its clients, its willingness to negotiate and its ability to establish mutual understanding when resolving issues, no matter how complex. We are confident that such a policy reinforces the Bank’s capacity and partnership positions as a lender on the Russian debt capital market.

Risk-Free Business

The development of risk-free business is still of great importance to the Bank. All targets were reached by the end of 2017, moreover, we managed to exceed the targets. Thanks to the continued growth of our customer base, the net fee based income increased by 36.4% on last year, totaling USD 442 mln. The portion of net fee-based income in the operating profit before provisioning reached a record high at 35.8% in late 2017, reflecting the Bank’s strategy to increase the stable risk-free income and enhancing the role of transactional business.

Customer relations in this sector, as well as in the lending area, are organized across all phases and levels. We are satisfied with the achieved results and intend to meet our targets in the next year. We also have many new project ideas, the implementation of which will considerably increase the fee based income earned by the Bank. We are planning both the development of risk-free business by means of customer acquisition and the development and implementation of new technological solutions in this area.

With regard to new technological solutions, it is worth mentioning blockchain pilots with Alfa-Bank involvement. Blockchain technology offers new opportunities for the corporate sector as a whole as it can change the money transfer market fundamentally, provide rapid clearing of payments, reduce transaction costs of all participants and optimize liquidity of interbank settlements. Despite the fact such transactions are not yet treated as a focus area by the Corporate Bank, we are actively testing the business model as we consider that there are excellent prospects and wish to respond to the growing interest of companies in this technology.

The first steps were made last year. MegaFon, Alfa-Bank and Sberbank were the first in Russia to make a payment using blockchain technologies. The payment transaction for RUB 1 mln was made between MegaFon and MegaLabs, its subsidiary, under the existing revolving loan facility agreement. The electronic transactions were exchanged via the decentralized computer network comprised of nodes interfacing on the basis of Hyperledger Fabric protocol of IBM Blockchain
Last year Alfa-Bank and S7 Airlines declared the launch of the innovative blockchain platform to automate trading activities. The technology sped up (several-fold) and streamlined payments between the airline and its largest agent in ticket-selling. S7 Airlines will not preclude new partners from joining the project, and aviation-related companies — suppliers of in-flight catering, fuel and airport services — may be the first to join. In December 2016, S7 Airlines together with Alfa-Bank used its LC transaction to test blockchain, and this transaction was the first of its kind to be executed in Russia.

In autumn 2017, M.Video, Russia’s major retail seller of electronics and home appliances, together with Sberbank Factoring and Alfa-Bank, announced the creation of an open ended consortium focused on the commercial use of blockchain-based technologies in the financial sector. The consortium members launched the open blockchain platform for factoring operations, which is capable of connecting an unlimited number of banks and factoring companies while maintaining confidentiality of transaction-related information. The platform has already proved effective in the partnership between M.Video, Sberbank Factoring and Alfa-Bank. It considerably reduced operating costs, and sped up and enhanced the security of factoring payments. Alfa-Bank and its partners successfully implemented the connectivity to the deliveries verification system shared by multiple partners and banks and thereby successfully launching the networking commercial blockchain platform in Russia.

Sector Priorities

Alfa-Bank’s corporate customers include companies engaged in various types of business and in leading positions in multiple economic sectors. There remain industries where the customer business increase is of paramount importance for us. 2017 sector priorities did not differ from those we had set for several years. This included the export sector, import substitution industries, in particular the agricultural and industrial sector, and petrochemistry, the transport and logistics sector, and industries of high priority for ordinary customers, such as pharmaceutics and retail trade.

Lending to enterprises of the agricultural and industrial sector is one of the Bank’s priority areas. Owing to the expertise of its team and working arrangements with the Ministry of Agriculture of Russia, Alfa-Bank provides consultancy support to its clients. Alfa-Bank also takes part in the financing of investment projects in this area, M&A transactions, and lends to exporters and processors. Currently the Bank has over 1,200 corporate customers in the agricultural and industrial sector. The largest holdings include: Prodo, Step, Rusagro Group, Solnechnye Produkty and Siberian Agrarian Group. From the beginning to the middle of 2017, Alfa-Bank’s loan portfolio in the agrarian and industrial sector grew two-fold and reached USD 2 bn. Taking into account guarantees and trade financing, it reached a total of USD 2.5 bn.
RESULT: In 2017, Alfa-Bank again demonstrated a growth of key financial indicators and confirmed its leadership as the biggest private bank in the country.
INVESTMENT BUSINESS

In 2017, Investment Banking performed strongly thanks to the favorable market environment which had not been predicted. As these positive dynamics had not been foreseen, the Bank had not assumed an aggressive position on the market, however, it reviewed its strategy over the course of the year as opportunities arose.

Last year, the Investment Banking maintained and enhanced its cooperation with US investment funds. This is a significant competitive advantage of Alfa-Bank, which we intend to continue to develop. In cases where material restrictions on dealing with local brokers have been introduced for western funds, we manage to bypass the best part of such restrictions and strengthen our position in the Russian market by means of active cooperation with Auerbach Grayson, a US brokerage company. Joint projects between the Bank and Auerbach Grayson became possible after the companies entered into a cooperation agreement in 2015. Auerbach Grayson represents institutional investors in cross-border markets in 98 countries, and in Russia it cooperates with Alfa-Bank. In 2016, Alfa-Bank, together with the US brokerage company Auerbach Grayson, organized an investment mission of the US investment funds to Russia. The mission focused principally on the assessment of opportunities and prospects for financial investments in Russian assets. The partnership with Auerbach Grayson, whose clients are large US investment funds, provided the Bank with additional opportunities for arranging IPO/SPO transactions.

We consistently orient ourselves to our clients' needs and desires. As such, the necessary efforts have already been made in order to provide efficient services to foreign (primarily, the US) institutional investors. In addition, in 2017, in order to meet the needs of private investors, Investment Banking increased the number of analysts in the group responsible for equity capital markets. The Bank is capable of providing all necessary services to investors at a very high level, including detailed market research.

Alfa-Direct

In 2017, Alfa-Direct mobile terminal was announced the best on the market multiple times. Our successes are also evidenced by our financial performance — based on the year-end results, the subdivision in charge of Alfa-Direct functioning exceeded its target by 20%.

The Alfa-Direct mobile application was the winner of the Digital Peaks Award in the category of Best System in the area of Financial Management and Financial Reporting. Digital Peaks is the national award in the IT area fostering the best domestic solutions aimed at improving efficiency. The award is supported by the Ministry of Economic Development of the Russian Federation, Ministry of Communications and Mass Media of the Russian Federation, Russian Presidential Academy of National Economy and Public Administration under the President of the Russian Federation, Skolkovo Technology Park. The expert jury consists of representatives of large and medium businesses, civil officers and venture investors, as well as representatives of mass-media and the state foundation for the support of entrepreneurship. The high score awarded by the jury recognizes the high efficiency of the application designed to meet the objectives.

Alfa-Direct's awards are an important achievement signifying the recognition of its successes in Investment Banking digitization. When developing the application, we relied on cutting edge concepts of customer focus and employed state-of-the-art technologies. The development of the Alfa-Investments portal is the next step in digital investment banking for a more active offering of investment products to clients of Retail Banking and Alfa-Private.

In 2017, a sustained effort was made to improve the efficiency of Investment Banking, rendering it the fastest at opening broker accounts on the Russian market. Alfa-Bank clients can do this remotely via Alfa-Click, the e-banking system. It takes the Bank a few minutes, only one day is needed to register at the Exchange, and then our clients are able to execute transactions with any tools at the Moscow or St.-Petersburg stock exchanges via a mobile phone or computer. Clients have the opportunity to undertake free training in Alfa-Direct or to select the solutions which are a perfect fit for those who are new to the market – the robo-trader functionality or a personal broker service.
Late last year, Alfa-Bank launched the online securities trading service integrated into the Alfa-Mobile retail application, where the Investments tab was introduced. The updated Alfa-Mobile application enables remote trading in government bonds, eurobonds and corporate bonds of issuers such as Sberbank and Evraz, VTB and Gazprom, Federal Loan Bonds, monitoring of the yield on securities, and tracking of coupon yield accrual. The minimum threshold for purchasing RR denominated securities is RUB 1,100. When trading in US dollars, the threshold is USD 1,800, thus providing access to the stock market for a vast number of nonprofessional investors who currently make active use of the Bank's application. In the current climate, where the yield of deposits is falling, we see an increase in client interest in such facilities offered by financial markets and have created a very simple online investment service which enables our clients to obtain a high yield.

Corporate Finance

In 2017, the corporate finance team actively analyzed the partners' offers in order to select the most promising startups for investment. Two favorable decisions were made on the basis of the analysis.

Another important event last year was the decision regarding cooperation with Natixis, a French bank, on joint activity aimed at raising international investment capital for Russian companies in the area of M&A and structured products. Natixis is a corporate investment bank belonging to BPCE, the French financial group, which is one of the French market leaders with financial assets amounting to EUR 420 bn and a capital of EUR 15 bn. The financial group has one of the highest ratings among the European Banks (Standard & Poor's — A, Fitch — A, Moody's — A2). Currently, the Bank manages assets of EUR 832 bn. The partnership enabled Alfa-Bank to offer access to international companies for company acquisition or sale, and provided it with access to new complex infrastructure projects. Alfa-Bank, together with Natixis, offers its clients a wide range of financial capabilities encompassing international bank financing arrangements, the raising of investment capital managed by financial investors and relevant partners, security placement and sale in international stock markets, fund raising against securities, asset purchase/sale arrangements and investments in international assets and companies.

Debt Capital Markets

Alfa-Bank has been a Russian debt capital market leader for many years. In 2017, it arranged the placement of seven issues of Russian RR bonds for corporate customers amounting to RUB 40.4 bn and two issues of eurobonds for corporate customers totaling USD 1.3 bn.

Last year, Alfa-Bank was the underwriter and co-arranger of a successful RUB 5 bn issue of exchange-traded bonds of AO Etalon LenSpetsSMU. During request collection, the investors' demand exceeded the issue amount more than four-fold. The final coupon rate to maturity was established at the level of 8.95% p. a. — considerably lower than the initial benchmark of 9.4%—9.65%. Alfa-Bank has been co-operating with AO Etalon LenSpetsSMU for many years.

Such a placement is a significant development in the bond market and may be treated by other companies as a benchmark.

In the spring of 2017, Alfa-Bank arranged placing of exchange-traded bonds, series EO-06, issued by Trubnyaia Metalurgicheskaya Kompaniya PAO for the total amount of RUB 5 bn with a coupon rate of 9.75% p. a. and an initial benchmark of 10.10%-10.40% p. a. During placing, the marketing range was revised down four times. This transaction was the second joint transaction by Alfa-Bank and TMK in the Russian debt market. This time, as before, there was considerable interest by investors: the market demand exceeded the total issue amount more than three times. In addition, the Bank arranged the issues of RR bonds for Baltic Leasing, PAO Rosseti, SFO Lokoservis Finans LLC, JSC Air-Telecom Holding, and eurobonds for the State Transport Leasing Company and Polus.

Liaising with Other Divisions

Cooperation with other business divisions is of great importance. Investment Banking is not an exception, involving close work with colleagues from Corporate Banking, Retail and, of course, Alfa Private, promoting a considerable profit increase. Last year, cooperation between the divisions became even more active. We launched a joint operation with colleagues in charge of middle corporate business. A large number of clients in this segment signed derivative transactions agreements. Sale of Investment Banking products to Alfa Private clients is of paramount importance. Last year, the Bank placed Exchange-traded Structured Bonds for the first time, and this was the first structured product developed specially for Alfa Private.

Plans and Forecasts for 2018

The beginning of 2018 was challenging for investment business. We will therefore maintain our cautious approach while continuing to focus on our clients' activities. Nevertheless, we are planning to execute a number of major transactions, including in the M&A area, several new types of structured financing transactions, and the full-scale launch of the Alfa-Investment portal for all types of tools and products. Our objective is to become a leader in the investment service market. Currently, we provide services to the customer base of all divisions of our Bank, rendering us a unique subdivision. In 2018, we will continue to focus on enhancement of our cooperation with other divisions. And, finally, we actively introduce new technologies in the investment business and schedule the implementation of the first phase (out of two) of digitization of operational activities of the Investment Banking, thus laying the groundwork for fast and flexible customer services over the next five years.

Regarding relations with large corporate business, the division has the serious and ambitious objective to earn maximum profit for Alfa-Bank. We are confident that we will attain our objectives, as we have the resources, experience and the strongest team in the market that has been able to achieve the best results for a number of years. And 2018 will not be an exception.
RATIONALE: Alfa-Bank priorities have been unwavering for years: these are client centrisim, technology, quality risk management, and operational efficiency.
Mobility and dynamism are an indisputable advantage for any business. Alfa-Bank is ready and intends to modify its approach to the developing products and will optimize processes to fully meet client expectations and needs.

The year 2017 was an interesting one in terms of market challenges, and productive in terms of interaction with our clients and establishment of new partnerships. New approaches improved our understanding, anticipation, and rapid response to client needs. We are confident that Alfa-Bank not only provides advanced financial solutions and quality instruments to its clients but also helps develop their business. Numerous successful cases of clients who successfully fulfilled the most daring business development plans in collaboration with us are testament to this.

The decision to establish a new business line, Small and Medium Corporate Bank, which combined Mass Business and Medium Regional Corporate Business blocks, was a keynote event of 2017 and highly significant for the entire corporate segment of Alfa-Bank. The new structure will give us a chance to achieve the ambitious goal of enlarging our share on the market.

The principal objective of the unification of our blocks is an integral distribution model, which will enable our team to work as fast as possible and minimize losses. In addition, we will preserve the combined block’s expertise and reach our common goals.

Medium and Regional Corporate Business

Alfa-Bank’s interaction with medium and regional business has been intensifying year on year. Last year, the Bank continued its successful development of this segment, and improved every indicator significant to business. Importantly, the number of active clients in the Medium Corporate Business segment (legal entities with a yearly income between RUB 350 mln and 3.5 bn) and the Regional Corporate Business segment (legal entities with a yearly income between RUB 3.5 bn and RUB 10 bn) increased by 43% and 41%, respectively. It was achieved thanks to our systemic approach to attracting new clients — an approach designed by sales teams in Moscow and branches over recent years. The Bank’s market share by the number of customers grew to 18% in Medium Corporate Business and 33% in Regional Corporate Business.

Further evidence of our successful performance is the growth of operating profit by nearly 50% in both segments. Operating profit of medium corporate business reached USD 133 mln, while regional corporate business posted operating profit of USD 66 mln. Importantly, about half our operating profit was risk-free. A further increase in risk-free revenue is the priority of all banks working with corporate business.

In 2017, the Bank boosted both clearing and credit business, thanks to more stable macroeconomic situation, decrease in key interest rate and a favorable market condition created by the revocation of many bank licenses by the regulator and financial rejuvenation procedures. Concerted efforts of credit and client teams produced commendable results in both segments: the credit portfolio of the Medium Corporate Business grew by approximately a third, from USD 269 mln to USD 348 mln, while Regional Corporate Business doubled its operations, from USD 0.6 bn to USD 1.3 bn.

Products and Services for Medium and Regional Corporate Business Clients

The block significantly expanded the range of products in 2017. New products and solutions for corporate clients of the Bank responded to market needs. Clients were given the opportunity to open a deposit and apply for a loan online, without submitting documents to a Bank office.

Letters of credit for real estate developers were also in demand. When a letter of credit is opened, the buyer of an apartment credits a certain sum to a special account in the Bank: the money is transferred to the real estate developer only after the purchase is registered and the real estate developer fulfills its obligations under the letter of credit.

Another important event of 2017 was the launch of a new service for clients searching for counterparties. This is a joint project of the Bank and the international company Opportunity Network, which gives Russian business access to the international B2B platform, Opportunity Network. This platform finds commercial partners, attracts investment, and facilitates asset sales and purchase and real estate operations across the globe. Opportunity Network currently unites about 14,000 owners and top managers from 128 countries. The overall value of offers available to platform users is USD 86 bn.

Connection to Opportunity Network is possible only via major banks, such as Intesa Sanpaolo, CaixaBank, Eurobank, Citizens Bank, BCI and Eurobank, which ensures the reliability of platform users and their information. Alfa-Bank is the first Russian partner of the international Opportunity Network.
Network. We are expecting the platform to be popular with Russian enterprises seeking to go beyond local markets.

Conferences and coaching events

In 2017, Alfa-Bank continued to host client conferences for legal entities in Moscow and regions. Over a hundred conferences took place, and the most popular themes were: compliance with Federal Law No 115-FZ “On Combating Legalization (Laundering) of Proceeds from Crime and Financing of Terrorism”, diligent cash handling, and foreign economic activity.

For the second year in a row, the Bank organized an educational event and a discussion for medium business heads, the CEO Forum. Reset, which addressed efficient development models of the sector.

The forum involved owners and top managers of successful companies, and Skolkovo experts and professors, among them the founder of KupiVIP.ru and Carprice and a member of the Alfa-Bank Board of Directors, Oscar Hartmann, President of the Moscow School of Management Skolkovo, Andrei Sharonov, acting Alfa-Bank Chief Executive Officer, Alexei Tchoukhliev, the founder and General Director of the company Simple, Maxim Kashirin, and other corporate executives.

Plans for 2018

The Medium and Regional Corporate Business segment has equally ambitious plans for 2018: we expect to increase the number of our active clients, legal entities, by 30%, and achieve a 50% increase in operating profits of both segments. We expect to achieve every objective and actively increase our revenue by developing relations with client companies and attracting new clients to Alfa-Bank.

Mass Business

Alfa-Bank achieved a lot in every key area of interaction with small business. Its share on the market grew 1.3% to 6.9% and soared to 20% in certain cities where the Bank is present. According to management statements, net profit totaled USD 194 bn in 2017, which was almost 30% higher than planned. Commission revenue amounted to USD 292 mln. The credit portfolio, including leasing, tripled to USD 255 mln. The number of Mass Business clients increased by 20% to more than 366,000 companies and individual entrepreneurs, and client activity stood at 83%.

Small Business Market in 2017

The Small Business Plus survey, which has been conducted by Alfa-Bank jointly with the international research center MARC since 2015, shows that economic expectations of entrepreneurs are negative and seasonal. However, the appraisal made in late 2017 displayed a minor improvement in the business climate and economic stabilization.

Small businesses are going to raise profitability by drawing new clients and cutting their costs. The biggest concern of businessmen is taxes, which have become Number One problem in every segment. Another trend is automation of business processes. The issue was increasingly mentioned by entrepreneurs in 2017, and 68% of them said they would be investing in technologies.

A further difficulty confronted by small business in 2017 was the replacement of cash registers as outlined by amendments to Federal Law No 54-FZ dated May 22, 2003, “On the Use of Cash Register Equipment for Cash and/or Electronic Settlements”.

It is possible that these factors contributed to the low number of new companies. According to the Unified Register of Small and Medium Businesses, the number of small companies (including individual entrepreneurs) grew insignificantly in 2017 (about 200,000 new companies and individual entrepreneurs) to slightly more than 6 mln.

We are monitoring all these changes on the small business market and adjusting our activity to contend with market challenges and to meet needs of businessmen.

Main changes and areas of block’s activity

Alfa-Bank is set to considerably increase its presence in the segment of the small and medium business by broadening its range of products and by combining all services required by businessmen under a single brand.

Alfa-Kassa

In 2016, we successfully launched the pilot project, Alfa-Kassa, and decided to expand its scope. In order to do this, Alfa-Bank acquired a share in the financial technology company, PAYMETECH CYPRUS LIMITED, a mobile acquiring service. Our cooperation resulted in the appearance of a new range of products for settlements between small businesses and buyers of their goods and services: POS-set Alfa-Kassa, mobile acquiring service Pay-Me, and equipment adjustment, installation, and maintenance services.

We plan to expand our presence on the market of online cash registers and attract new clients by offering a package solution which includes all the tools needed by an efficient business.

Onsite acquiring

In line with our logic that the entire range of business services should develop as a single brand, we continued to actively explore the new area of onsite acquiring in 2017.

About 3 million companies are operating on the market of retail trade and services. According to Rosstat, about 70% of Russia’s trade turnover falls on small business, mostly individual entrepreneurs, and this market has a huge potential. However, the availability of acquiring services is rather low (from 30% to 40%, according to various estimates). A lot of preparation was done in 2017 to start trade acquiring: a team led by a major acquiring market actor was formed, partner agreements were concluded, and a concept for entering the market and gaining a foothold was developed. Over the next three years, Alfa-Bank intends to increase its share on the trade acquiring market to 7% by ensuring rapid delivery of terminals to clients, integration of a majority of small businesses, and by offering a package solution which includes all the tools needed by an efficient business.
Client experience

In 2017, we placed particular emphasis on service quality and satisfying our client needs. Improving client experience was treated as a separate area, and the Service Directorate was set up. We developed a service concept and principles to improve client experience, and structured our work according to client feedback. Mass Business’ approach to client feedback was recognized as efficient and was used in interacting with clients of other blocks.

As a result, the principles of recruitment and basic training were modified. The individual supervisor launching plan was supplemented with a section on client experience and relevant assignments.

In order to implement successful personnel training practices of the block throughout the Bank, a special training program was developed so that any Bank employee, including those in cross-functional units, could immerse themselves in the client experience. The program kicked off in all regions and Moscow in late 2017.

Compliance control

Seeking to comply with the regulator’s requirements under Federal Law No 115-FZ dated August 7, 2001, “On Combating Legalization (Laundering) of Proceeds from Crime and Financing of Terrorism”, and to reduce the outflow of bona-fide clients, the Mass Business block created the Compliance Risk Department.

Compliance has a regulatory function in the Bank; it is a sort of ‘conductor’ of the requirements set by the Russian Central Bank. The Compliance Directorate fulfills the mission, but it is rather detached from the business. The block’s department is a link between business and the Compliance Directorate whose specialists have a profound knowledge of every nuance of business and the requirements of the Central Bank. This formula enables an individual approach to every situation and prevents mistakes from being made in cases of dubious operations.

The format indicated that higher efficiency required automation of many internal bank processes. We successfully automated some processes in 2017 and decided to continue our efforts in 2017.

Online distribution

In 2017, the block launched another project based on the Remote City pilot; the latter began in 2016 with the design of an online distribution model for attracting small business clients via online channels and ensuring their remote access to all bank products and services. Remote City exclusively targeted clients in regions where Alfa-Bank does not maintain physical presence. The online distribution model is applicable to all clients in any populated locality of Russia.

We managed to create cross-cutting processes which can be used by any bank block. The online distribution models will substantially cut the cost of attracting new clients and expand our client base.

Value stream

In 2016 and 2017, the Mass Business block applied a new approach to organizing its processes—the value stream.

The principal objective of the value stream is to design products and solutions based on client needs, rapidly improve via feedback, and stream values back to clients as quickly as possible.

Taking into account the positive results and efficiency of the value stream principle, Mass Business decided to apply a similar approach to Bank products as a whole: there are plans to combine product development for all client segments into a single center — a product factory — in 2018.

Product range and processes

Interaction with business novices and small companies was a priority of the block in 2017. For instance, we inaugurated a new package of services for small and new business called Na Start (Ready). The package opens an account and connects the online bank free of charge, and the monthly service fee is only 490 rubles; there is no fee charged if no account transactions are performed.

Another new package of services launched in 2017 is called Vsy chto nado (All you may need). The target group is companies with high financial activity that make settlements with Russian and foreign partners.

The Notarius (Notary) package was launched in February 2017 to open transaction and deposit accounts for notaries in rubles. There is no fee for opening and servicing a deposit account of a notary. A monthly service fee depends on the region; it varies from RUB 1,700 to 2,000 , and stands at RUB 59 per month if there are no account transactions. There is a 25% discount if an advance payment for six months is made, and a 35% discount is offered for payments made 12 months in advance.

In March 2017, Alfa-Bank adjusted the process of account opening for individual entrepreneurs; now an account can be opened in the space of 30 minutes. The process became fully automated in July; it was possible to open the account instantaneously in the first visit to a Bank office without the preliminary processing of documents.

The analytical agency, Markswebb Rank & Report, recognized the account opening process in Alfa-Bank as one of the best in terms of convenience and simplicity. Alfa-Bank held the second position in the rating with of the lowest time of interaction with the bank. The Alfa-Bank website topped efficiency rating of Russian banks’ websites as channels selling settlement-and-cash services to small business in terms of transaction account approval.

In 2017, Alfa-Bank launched the FIFA loyalty program, not only for retail clients, but also for individual entrepreneurs and legal entities. Any client could join the program by pressing a button in the mobile or Internet bank, score points for routine transactions, and exchange them for tickets to matches of the FIFA World Cup 2018TM, sports attributes, and souvenirs. About 80,000 clients joined the program in 2017. The efficiency of this loyalty program is demonstrated
not only by the number of participants but also by the gradual increase in the profile of program participants. The program will continue in 2018.

Back in 2016, Alfa-Bank began the Universal Employee project, the purpose of which was to enable any employee to offer service to private and corporate clients. The pilot project proved successful and was implemented in all Bank offices dealing with cash transactions in early 2017. Individual entrepreneurs and legal entities were able to credit cash to a transaction account in any bank office with a cashier in April 2017.

As for the range of credit products, we launched a new product, Business Credit, in 2017. This is an unsecured loan of up to RUB 10 mln. Our management of the overdraft interest rate was also adjusted: from now on, the rate depends on the number of years businessmen, businesswomen or companies have been Alfa-Bank’s clients. There is an individual rate for every client; the longer the client has been with the Bank, the smaller loan rate. The minimal annual rate is 15%, while the maximum rate is 18%.

Mobile bank and Internet bank

In 2017, Alfa-Bank developed and launched a new Internet bank, Alfa-Business Online, which can use any operating system (Windows, Mac, Linux) and can be adjusted to tablet computers and smart phones. Convenient navigation makes it possible to receive a balance in two clicks, sign the register of payments, easily find a payment in the history and repeat it, order a statement signed by the Bank’s electronic signature, and donate money to a charity.

Advanced technologies and integration with various online accountancy, CRM and ERP services give clients access to the calculation of tax payments and submission of reports. The new Internet bank enables clients to open a deposit account within several minutes all by themselves.

In December 2017, the new Internet bank’s NPS reached 72%, which was higher than the NPS of the previous version.

A lot of effort was put into updating the mobile bank, Alfa Business Mobile. Users were granted access to information on topics such as the change of tariff, fast transfers between client accounts, the search for an entity by name among Russian counteragents for transaction purposes, balance export in IC, CSV, and PDF formats; balance sending and downloading; viewing of commission fees and all account transactions in the payment history; temporary card blocking and unblocking, opening of additional transaction accounts in various currencies, etc.

Mobile banking penetration grew by 10% in 2017. The number of active users increased by 65,000 to 155,000, and the number of payments conducted via the mobile bank nearly tripled.

Nowadays, mobility and dynamism are an indisputable advantage for any business, and entrepreneurs are well aware of this. Seeking to meet the expectations of our clients and make their interaction with the Bank as convenient as possible, we intend to give them full access to account management via a smart phone or a tablet computer. A key task of the Bank’s team is to adjust the Alfa-Business Mobile functions to a version compatible with computers.

Non-financial services

Alfa-Bank not only offers modern financial solutions and account management instruments to small companies but also helps clients develop their business. The Bank designed a unique ecosystem, a community where entrepreneurs find partners, suppliers, and potential clients. Federal partners of the Client Club are market leaders who work across the country and offer exclusive terms to Alfa-Bank’s clients. These include Yandex.Direct, HeadHunter, BeeLine, Kontur, Microsoft, Target.Mail.ru, and Findolog. Eight more companies joined in 2017. For instance, Megagroup offered Bank clients free design of a corporate website or an online store, as well as annual service and a one-year CRM as a gift.

As we are striving to help entrepreneurs develop their business, we organized 193 coaching events across Russia in 2017, including 17 Alfa Business Week forums, 29 accounting conferences, 42 industry seminars, 89 business breakfasts with partners, 13 webinars on various subjects, and three master classes. The events involved 17,000 clients of ours and 4,500 companies and businessmen who are yet to become our clients. All the events were focused on practice. The average NPS of our events stood at 80%- a definitive indicator of the success of these efforts.

Alfa-Bank is traditionally focused on charity: we actively participate in diverse charity projects and give our clients a chance to do the same. One such project is the Alfa Cash Ultra affinity card, launched in 2016. Businessmen who hold and use this card are helping children: Alfa-Bank transfers 0.39% of the sum of every transaction to the Life Line Fund. A total of 16 million rubles were transferred to the Fund in 2017. The money was spent on helping 15 children with severe disabilities.

Another charity project was launched at the Alfa Business Week business forum, which became a member of the corporate club, Plus One Life, of the Life Line Fund. There was a charity auction at every event: entrepreneurs were given the opportunity to buy a ball of the FIFA World Cup 2018 signed by all the speakers. 17 balls were sold for a total of RUB 160,000. RUB 1,198,500 were transferred to the fund over the course of the year. Money was transferred online, using a mobile terminal installed on the stage.

Forecasts and plans for 2018

Competition on the market of business services for small business will continue to grow in 2018. Alfa-Bank is ready and intends to modify its approach to developing products and will optimize processes to fully meet client expectations and needs.

Financial performance indicators and the market share will determine Mass Business’ success in 2018. In order to satisfy our appetite for market share, we will continue to interact with the client segment (micro-businesses and self-employed citizens) which were low priorities for the Bank prior to 2017 due to economic considerations: the way our processes were organized rendered these clients loss-making. In 2018, we will design processes and value offers that created a segment in this segment and fully satisfy clients’ needs for bank products and services. We have a plan as to how to achieve this goal: we will launch a vast promotion campaign, design package solutions for this client segment and, as we have said before, modify and optimize our processes. We will automate our operations and shift them to the digital space.

Our range of products will be optimized and areas such as acquiring, Alfa-Kassa, and credit products will continue to develop.
DETERMINATION: Be better, faster, more convenient and efficient than rivals and guarantee best-available service to clients; this is how Alfa-Bank maintains leadership on the market.
RETAIL BANKING

2017 was very successful for Retail Business. The block’s financial result grew from USD 297 mln in 2016 to USD 359 mln in 2017 under consolidated IFRS financial statements. The market share of retail demand accounts reached 9.2%. The overall market share of retail accounts reached a historic level of 3.11% at the end of the year, compared to 2.73% the year before. The overall value of individual accounts exceeded USD 15 bn at the end of the year, including USD 8.7 bn worth of demand accounts, which grew by 23% year-on-year. The Bank had more than 14 mln retail clients as of the end of 2017.

The Bank was more active in retail lending in 2017, which had an effect on the credit portfolio of Retail Business. The portfolio grew by 47% year-on-year to USD 4.4 bn. The Bank ranked third on the credit card market with a portfolio totaling USD 1.4 bn according to IFRS; the segment demonstrated a year-on-year growth of 26%. The consumer loan portfolio went up from USD 406 mln to USD 665 mln. The cash loan portfolio expanded by 65% and stood at USD 2.1 bn at the end of the year. Importantly, despite the increase in the loan portfolio, its quality is improved. According to the consolidated IFRS financial statements, the share overdue loans for 90+ days amounted to 4.1% in 2017. In 2017 a new approach was applied: the write-off date was moved from day 181 to day 541. Excluding the effect of new approach, the level of NPLs 90-180 days decreased to 0.9%.

Market Situation

The retail portfolio of Russian banks grew by more than 12.7%, reaching RUB 12.2 trln in 2017. We are witnessing the banking sector’s recovery from the stagnation of the previous years: in 2016, domestic retail banking grew by only 1.1%. Positive trends emerged against the backdrop of the reduction of the Central Bank’s key rate, from 10% to 7.75% over the course of the year. The mortgage loan market was very dynamic and grew by 15% year-on-year, while the credit card market increased by 11.4%. Alfa-Bank was monitoring market trends and focusing on most popular products. For instance, it began to actively develop the mortgage loan segment last year.

Retail Bank’s Product Range

Most individuals using Alfa-Bank services also use services of other financial institutions. In order to be the principal bank of such clients, we need to become a part of their everyday life and make Alfa-Bank’s services inherent — without pushing it onto them. Mortgage loans are a product which contributes to this goal. Such loans satisfy the basic need for a comfortable living space.

Last year, Alfa-Bank modified the retail sector development strategy and made mortgage loans a focus of its lending program. The interest in mortgage loans is logical: the product has been a key driver of the growth in bank credit portfolios over recent years, and Alfa-Bank seeks to be one of the Top 5 on this market. Alfa-Bank launched mortgage loan programs on primary and secondary housing markets and offered refinancing to clients of other banks in Moscow and St. Petersburg. There are also plans to open mortgage loan centers in the regions. The mortgage loan rate in Russia has dropped to the lowest ever level. By contrast, the share of real estate deals based on mortgage loans is soaring.

Bank cards are another product which serves the daily needs of every individual. As the official bank of the FIFA World Cup 2018™, Alfa-Bank issued a card with an exclusive design of the FIFA World Cup Trophy in 2017 in collaboration with Visa, which is one of the six global partners of FIFA and a global payment system. The card features the Visa Pay Wave technology, which makes payments easier than ever before. The unique advantage of this card is that any holder can score points by conducting routine operations and exchange them for tickets to matches of the FIFA Confederations Cup 2017 and the FIFA World Cup 2018. Card holders can also exchange their points for sporting souvenirs of the FIFA World Cup 2018, and enjoy other exclusive opportunities provided by Visa and Alfa-Bank. Russia has millions of football fans, and many of them are Alfa-Bank clients. Thanks to this initiative, they have a unique opportunity to enjoy this world-class sporting event, hosted by Russia for the first time ever, in new and exciting ways.

Alfa-Bank pays special attention to young clients, and the Next card remains a trendy product. Alfa-Bank has updated it and now offers cash-back. The Next debit card boasts features which are highly popular with young people, such as the Mastercard contactless payment technology. The technology is implemented in a bank card and a stylish bracelet with an inbuilt microchip.
Card holders can use the Alfa-Mobile application for free and communicate with the Bank via an online chat - a feature which is important to the younger generation.

In the same vein, Alfa-Bank, the game division of Mail.Ru Group, and the Gratz Bonus loyalty program presented special bank cards for gamers, Warface and Game@mail.Ru, in 2017. Card holders receive cash-back on any purchases, as well as special bonuses and in-game gifts from Mail.Ru Group games. Bank cards with gamer loyalty programs are increasingly popular, considering that the active gaming community in Russia is nearly 46 mln, and most of these people regularly spend money on virtual entertainment. Game card holders can spend cash-back on regular or virtual purchases.

In 2017, Alfa-Bank gave its clients the opportunity to open a family account in a mobile application and manage money together, in order to increase the efficiency of family spending. The joint account for a married couple is an alternative to storing cash at home, which can be unsafe and inconvenient. The Bank offers a handy tool, which helps to avoid such situations, raises spending efficiency, and assists in planning the family budget. Every time money on the family account is spent, the Alfa Mobile application records the purchase, irrespective of who makes it. What's more, every client receives his or her own family account statement.

Retail Technologies

Alfa-Bank is reputed to be one of the most high-tech banks in the market; every year it does a lot to maintain this reputation and to meet client expectations. Technologies expanding and facilitating the interaction between clients and the Bank via safe electronic channels are high on the agenda of retail business. Our mobile bank knows a lot about its clients, including with regard to their needs and lifestyle. This is what clients expect from their principal bank. We realize this and adjust our products and services to their wishes.

In 2017, we updated the Alfa-Mobile bank, which has become the principal finance management tool for many of our clients. Last year we stopped taking a commission fee in Alfa-Mobile, which attracted new active users to the mobile application. The application now boasts more operations, which can be conducted without visiting a bank office. In 2017, we added functions to open and manage deposits, activate a card, modify a pin code, and make a request for an account statement or balance. The limits on payments and transfers made in the mobile bank were raised.

Last year, Alfa-Bank inaugurated a convenient payment planning service. Our clients do not have to worry about financial affairs any more: all they have to do is plan the required transactions, and the application will remind them of the need to make the payment. We offer a convenient budget management tool (PFM) to our clients, who are now able to plan their budget several months in advance and to assess future expenses by category based on information from previous months.

We now also provide our clients who don't possess bank cards with the ability to repay their loans using cards of other banks via Alfa-Mobile, while clients repaying loans to other banks can do so using the mobile application and the number of their loan agreement. Clients can also request the issuance of a preapproved credit card or loan via the mobile application. In the case of a loan, money is instantly transferred to the account of the client, who does not need to make a call or visit a bank office. The new Product of the Year, the family account, can also be opened in Alfa-Mobile and managed through this application.

Finally, a new section has appeared in Alfa-Mobile ahead of the FIFA World Cup 2018: it deals with FIFA bonuses and client privileges (which can be exchanged), and the number of transfers and priority passes.

Client Feedback and Interaction

The successful development of any business is now impossible without a profound understanding of client expectations and a rapid response to client needs. Readiness to recommend Alfa-Bank to family and friends and to leave a positive comment on social networks depends on a client's impression of a particular product, their satisfaction with their visit to a bank office, or their communication with the Client Support Center.

Without feedback, the Bank cannot continue to consistently raise the level of client satisfaction, manage client experience, and improve products and services. Clients enthusiastically share their impressions. They understand that the Bank is ready to address their problems, hence client experience is improving and client loyalty is growing as a result.

Teamwork

The Retail Business leadership was reshuffled and the management strengthened, and new remarkable leaders with extensive professional experience joined us last year. All these transformations made the block even more successful. Our team was restructured in order to provide a better response to business needs and maximise the efficiency of interaction between employees.

In 2017, emphasis was placed on raising the efficiency of every employee and improving their knowledge of our clients. Client information could be used to improve the range of bank products, communications and processes, as well as our interaction with our clients via every channel.

Plans for 2018

In 2018, the Retail Bank will concentrate on increasing its share in the lending market, first and foremost in the segment of credit cards. It will also launch the comprehensive mortgage loan program proposed in 2017. Our products will not be limited to lending. We will do a lot to upgrade the product range, so that our clients can choose the products they need, quickly and easily.

Next year, we will also give the technological capacities of Retail Bank a complete facelift, placing particular importance on the Alfa-Mobile application. It is our goal to increase the number of active users and the frequency of use of this application. We will integrate new convenient services, which will boost the demand.

To be better, faster, more convenient and more efficient than our rivals, and to guarantee high-end service to our clients: these are the mandatory ingredients of our success. The third priority area of the Bank is to increase the efficiency of internal processes, interaction with employees, and the development of corporate culture based on the ability of employees to observe their performance and the Bank's services and products through our clients' eyes. This gives us a better understanding of those for whom we work day in, day out. It also helps us to continue to upgrade our services and provide top-notch service - service of Alfa-Bank quality - as we have been doing for over 20 years.
RESULT: In 2017, Alfa-Bank strengthened its market position via teamwork and again proved the efficiency of its business model by expanding client base and lending operations and improving quality of its assets.
We become even more transparent and communicative with clients under the Alfa Private brand. Over a thousand new clients chose the updated Alfa-Private offer in 2017.

ALFA PRIVATE

The affluent and private banking unit was rebranded as Alfa Private and separated from Retail Business in April 2017. The Bank was aware that such clients and their families required services of higher quality. Efficient solutions for affluent clients combine classic banking service with products from different areas, including the Investment Bank, management, insurance, leasing, and other companies of the group and its partners. Global practice proves that it is better to use a specialized platform for meeting the needs of such clients, and Alfa Private now provides this platform. It offers better solutions to clients whose cost and quality may vary depending on tools offered by the Bank and its partners. For instance, in 2017 Alfa-Private actively developed portfolio investment consulting, lending, and wealth structuring and management services.

Results of 2017

Last year was not an easy one for the banking industry, yet our private banking services were as popular as ever. The reason is simple: our main asset is the confidence of our partners. Alfa-Bank has laid the foundations for special relationships over a decade of operation in this segment. Alfa-Private is now even more transparent and communicative. In 2017, we organized meetings with the bank’s CEO and regular events for our clients, their families and proxies on the subjects of information security, artificial intelligence, and other topical aspects of technological development. A series of innovative solutions were implemented, VR block-chain seminars were arranged, and one of our offices implemented a biometric identification system.

We prioritize feedback, so we started discussing ideas on how to develop our service and products with a group of clients in 2017. This practice will continue in 2018. The level of participation in these meetings prove that our work is highly important for our clients, especially in such a rapidly changing environment.

Innovative technologies for client interaction and remote access to Bank products give Alfa Private its competitive edge. The expertise of our Bank and its key partners, Investment Bank and the Alfa Capital management company, reinforce our leadership in technological solutions offered to clients. Convenient daily service and the ability to manage one’s capital remotely 24/7/365 are primary needs of every affluent person living and working in Russia and frequently visiting other countries.

Alfa-Bank has been investing heavily in innovative infrastructure, which provides families with a convenient way of managing their budgets, even the most complicated ones. More than 80% of our operations are conducted online, via remote access channels. This includes our mobile application and the exclusive telebanking service for our private banking clients. A short time ago we implemented unique account management by proxies. As a rule, private banking clients interact with the Bank to manage their daily affairs via proxies. Unlike companies, earlier, proxies had no remote access to accounts of their beneficiaries. They now enjoy this option, and it seems to have resolved an inconvenience previously experienced by our clients.

Our work has yielded tangible financial results: assets managed by Alfa Private grew 150% in 2017, and more than 90% of growth comprised client money from state-run and Western banks. The investment portfolio of affluent clients doubled in 2017. Last year, we fulfilled the three-year plan handed down to our business in 2016. We did not aspire to a significant increase in clientele and focused on quality development of relations with existing clients. Regardless, over 1,000 new clients still chose the updated Alfa Private offer in 2017.

An average check of our target family is close to USD 5 mln, which is higher than the market’s average. An average check of our clients in Russian federal centers is much higher, which has a positive effect on the overall result.

Regional Business Development

Alfa Private is actively attracts clients both in Moscow and in regions. Currently, only 50% of our business is concentrated in Moscow, while regional business accounts for the rest. In some
cities, including Novosibirsk, the market share of Alfa Private is as high as 50%. This model helps diversify the client base and improve business stability. Regional clients, who rarely visit Moscow, receive the service they need any time from Alfa Private.

We believe in the potential of the regional market and the demand for private banking services in the format we are offering: it combines quality portfolio expertise, ability to accomplish tasks set by our clients, and broad remote access to services. We are ready to develop new formats of interaction with our clients outside Moscow in 2018; our clients will be serviced in the Client Coverage format without opening an office.

Alfa Private Team

In 2017, we focused primarily on the development of skills and competences of our team. The team is our second most valued possession after our clients. We put a lot of effort into training and developing our financial consultants, who are an essential part of our relations with our clients. It is our goal to provide world-class expertise. Therefore, we run regular coaching programs addressing keynote trends in tax laws and other legislation, compliance, and management of compliance and portfolio risks.

Together with the Moscow School of Management Skolkovo, we launched a unique professional development program for personal bankers, Future Private Banker Today, in 2017. The program is based on research done by the Skolkovo Wealth Management and Philanthropy Center, polls of Russian businessmen and their entourage, and studies on the mentality and perception of capital owners. The first course involved 30 of our financial consultants.

In addition, Alfa Private implemented a system of compulsory employee certification. All existing employees were certified in 2017, and new employees were either certified prior to or at the time of their recruitment. Our focus on service and feedback has been constant. The Alfa Private call-center embedded state-of-the-art client service information technologies, which is a significant result of these efforts.

In 2017, the block updated its approach to portfolio expertise. The initiative led to the founding of an investment consulting division and a team of portfolio managers. The product committee, which chose products to become part of the portfolio of private banking clients, reached its full capacity in 2017. Financial consultants were powered by the expertise of investment consultants, who are tasked with helping clients form individual investment portfolios. We reorganized the operational model of the team interacting with clients, grouped financial consultants into teams, designated roles to team members to improve the quality of daily client service, and enabled financial consultants to focus on more complex tasks. Entire team works for our clients and their families, which renders our service consistent and of a very high quality, ensuring high-end expert support whenever necessary.

Forecast for 2018

We have daring and ambitious plans for 2018. We are doing everything we can to provide the best private banking service to our Russian-speaking clients both in Russia and other parts of the world, which means we will be competing against global banks. We will therefore continue to develop our team, our competences, and technologies in the field of investment, together with our partners in open architecture. We are aware that this is an ambitious goal, but we are confident that we will achieve it. We have no doubt that we can continue to make the lives of our affluent clients, their families, and proxies easier and much more comfortable.
RESULT: Constant development, modification, and innovations are aimed at a convenient and long-term relationship with our clients.
The joint work of Operational and IT blocks is a logical consequence of digitalization of the banking industry. The boundaries between them are being erased, yet the primary objective remains unchanged: to maintain stability, to ensure reliability.

OPERATIONS AND INFORMATION
TECHNOLOGY DEPARTMENTS

Operational Block

The Operational Block performed highly in 2017: all targets were surpassed, and some indicators were at a record high. For instance, we achieved the highest ever arrear collection rate of 96.8%. We continued to raise the block’s efficiency and achieved impressive results: 2016 indicators were exceeded by 14%. The block implemented many interesting projects which improved client service and fostered the Bank’s positive image. Also, we did a great deal to meet other priorities, such as minimization of operational risks and broadening of personnel knowledge.

Market challenges of 2017 resulted mostly from regulator activity, which continued to raise the bar for banks. Norms are substantially modified year upon year, and last year was no exception. It should be noted that Alfa-Bank prepares for new requirements in advance and always manages to reconcile its processes with current norms, which is part of our competitive edge.

Another important feature of Alfa-Bank’s Operational Block is its pioneering approach, in addition to the ability to monitor rivals and rapidly implement new technologies emerging on the financial market. For example, Alfa-Bank, a leader of banking technologies in Russia, was the first in the country in 2017 to begin the issuance of digital statements with electronic signatures to legal entities and individual entrepreneurs. Our bank was also the first to start using the SWIFT gpi service which increases the speed, transparency, and predictability of trans-border payments of our clients. The unique payment information service became available to all Alfa-Bank clients in January 2018.

These are elements of our dedicated effort to improving client convenience, availability of state-of-the-art technologies, and provision of assistance to the Bank’s clients in carrying out their financial tasks.

Raising Client Service Quality

Optimization of the cash order system is an illustrative example of client service projects implemented in 2017. Alfa-Bank developed a mobile application for clients to use to order cash, choose the type of banknotes and the bank office to collect it, and submit relevant documents online. The mobile platform instantaneously transmits the information to the system, which automatically forms cash orders, and the cash collection service delivers the money to the chosen office. More than 50% of our clients use the service, making cash orders convenient and precise and saving them a lot of time.

Another important event of 2017 is the implementation of the practically instantaneous opening of accounts for individual entrepreneurs the first time they visit a bank office. Alfa-Bank are able to select electronic document flow and sign documents required for opening an account with an electronic signature.

Our interaction with payroll clients has evolved greatly. After examining client experiences closely, we completely redesigned our processes, reduced time loss, and ruled out the possibility of error, rendering the service faster and easier. Payroll clients can now open an account in the space of one day. Optimization of processes will continue in 2018.

The Bank also switched to electronic document flow in the interaction with Mass Business Clients in 2017. As a result, the settlement processes and the signing of documents have become faster.

Pilot Projects

The Operational Block launched a variety of pilot projects in 2016, and some were furthered and completed in 2017. Two projects involved the testing of robots, both digital and physical. Alfa-Bank is expecting to significantly expand its business in the coming years, which means the workload of operational offices will grow. Instead of increasing the number of employees, we will be using digital robots to perform routine tasks. The block is actively implementing digital robots. The testing of a physical robot in our cash processing center has not yet been successful, however we believe we can use this robot or its analogues in our cash processing centers after making some key improvements in the near future.
Audio technologies used in the debt collection process are another pilot project that proved successful in 2017. Our robot calls clients and enquires whether they are ready to pay debts. If the answer is positive, the information is immediately transmitted to the system, and if the answer is negative, Bank employees begin communicating with the client. Such audio technologies have a lot of potential, as they can reduce the call center workload. Hence, we are closely monitoring innovations in this area and testing solutions which we deem to be useful or promising.

A pilot project using chat-bots for personnel training purposes was launched in 2017. The chat-bot was implemented for front office specialists interacting with payroll clients. It should be noted that the system does not use standard scripts: artificial intelligence analyzes our bases and provides the correct answer to the question. This system assists new employees in processing the masses of information that they receive when they start. It also saves time for senior personnel: the chat-bot serves its purpose in providing new employees with support, whether it be a simple consultation or a frequently asked question.

Another solution tested in 2016 consisted of local teams of software developers deployed at operational centers of the Bank. The project proved extremely successful in 2017: the investment in our programming group paid off by at least 300% and boosted the completion of minor assignments. The IT Department addresses global tasks, which means minor assignments have a low priority and can take a long time to accomplish. The group of software developers stationed at operational centers in Ulyanovsk and Barnaul deals with minor projects. Our team is evolving from a purely instrumental unit into a center of robotics expertise, which operational centers are in great need of. A further task is identifying paper documents. We have also been doing well in this area. New technology has been implemented for payroll projects and this has markedly increased our efficiency. Some 40% of documents are now automatically identified. We are expecting this percentage to markedly grow by the end of 2018.

In 2017, we expanded our team in order to enable developers to accomplish more tasks and propose new solutions for automating local processes. We are confident that the combination of resources which the IT and Operational Blocks have at hand could significantly raise our efficiency. Employees of both blocks are working together and have a better understanding of their needs and capacities; as a result, new solutions are developed faster and more successfully.

Assistance in optimizing the processes of business units is an important mission of the Operational Block. The Alfa-Credit 2.0 platform was designed in 2017 to implement electronic document flow in relations with big corporate business. The number of paper documents was reduced, the interface of our workstations demonstrated that nobody is perfect, and indicates the areas to work on.

Arrear Collection

In 2017, the Operational Block achieved a record level of arrear collection, of 96.8%. We did a lot to maximise the efficiency of employees responsible for this sector. Firstly, we worked together with Retail Business to improve the quality of contacts. Our surveys helped minimize the operator waiting time and technological downtime. We believe we have achieved the ideal balance between employee workload and client convenience. As a result, the efficiency of arrear collection has grown and is maintained at a very high level.

Teamwork

Employee skills of the Operational Block are constantly being developed: the better an employee performs, the more efficient the entire block is. In 2017, we replaced classic formal tests with personalized ones, depending on the position, functions, duties, and areas of responsibility of our employees. The format of our tests has also changed: multiple-choice assignments were supplemented with business cases, in which employees needed to find a solution and decide on how to respond to a concrete situation. Tests of this kind demonstrate to employees where they can solve problems independently, and where they should seek additional knowledge or experience. Weaknesses are analyzed, and skills are developed.

Another interesting innovation of 2017 is the employee quiz which appears on the monitor from time to time after the employee starts their computer. In contrast to annual tests, such testing methods provide operative information on the level of employee skills. The supervisor sees who gives the right answer to the “question of the day” and who does not, and decides which issues the team should address. A pilot has been rolled out and the tests will be a standard tool for constant testing of personnel skills in 2018.

A new index of the assessment of the knowledge of expertise center employees, the Client Digital Design Product (CDDP), was implemented in 2017. The assessment parameters were dictated by the needs of the market: our employees have to understand client needs, be familiar with the capacities of modern technologies and process design basics, and master product design tools. Employees assessed themselves according to four parameters of theoretical knowledge and practical skills at the beginning of the year; the self-assessment was done again at the end of the year. The average score in the block more than doubled over the course of the year. This is a very useful initiative, which professionally develops our employees, demonstrates that nobody is perfect, and indicates the areas to work on.

With regard to training programs, we should not forget that we are helping both employees and clients acquire new knowledge. The areas where most mistakes are made are identified, and we help minimize these mistakes. For instance, our clients, legal entities, often make mistakes in dealing with tax or other payments. We have prepared a comic book which reminds them of what they should do to deliver the money to the addressee.

Training videos for clients is another popular format; we made some of those videos by request. New banknotes with a face value of 200 and 2,000 rubles emerged in 2017, and we made a special video on this subject. There was also a video for accountants of our payroll clients which suggested ways of spending less time on payroll accounting. Our regional clients are also able to send their cashiers to our coaching seminars.

Such training aides not only reduce the work load of Bank employees but also raise the level of client satisfaction. We will continue preparing such materials, and will choose the themes together with our clients.
Interaction with IT Department

The joint work of the Operational and IT Blocks is a logical consequence of the banking industry’s digitalization. There is no doubt that close ties between these two blocks are key to achieving perfect results. Exchange of practices between their employees and combined expertise solves the most complex tasks more efficiently. It is impossible to separate technologies from processes, and hence IT specialists need to understand the essence of processes requiring automation, and Operational Block employees need to be familiar with the capacities of new technologies. Several joint teams were created in 2017 in the agile format, and their results are impressive.

Plans for 2018

In 2018, we have the important task ahead of us of cutting the cost price of processes, drawing more clients, and maintaining a high level of customer experience. We are analyzing the most labor-intensive and expensive processes and working on their maximum optimization. The Operational Block achieved its goal of instantly opening accounts for individual entrepreneurs in 2017. We will seek to make this process cheaper for the Bank in 2018. Another area where cost price needs to be reduced is cash handling. Of course, we are expecting requests from our business blocks which will help optimize their essential processes and accomplish the tasks set by the client influx.

The Digital Economy government program presents another challenge. The Bank strives to be a leader of Russia’s digital transformation. We actively participate in the integration process, which will yield a unified identification and authentication system enabling Bank clients and non-clients to open accounts and conduct transactions by means of biometric parameters, without visiting a bank office. The Bank is an active member of the Association of Financial Technologies. We are testing a pilot system of fast payments, blockchain-based letters of credit, and other innovations.

No matter how the Bank evolves, the Operational Block must ensure the stability of all its processes. This is a huge responsibility; the smooth operation of the Bank is crucial to its image and client satisfaction, and therefore the number of individuals and legal entities who choose Alfa-Bank as their financial partner. It is our primary objective to maintain stability wherever necessary and not to forget the need for constant development, modification, and beneficial innovation.

IT Block

Alfa-Bank is a technological leader of the Russian financial market, and IT support is growing more important year upon year. Our Bank deserves to be called ‘digital’ - a quality which is now mandatory for the successful operation of any financial institution.

What do we mean by ‘digital bank’? On one hand, it means client convenience, fast and understandable processes which assist clients to achieve their goals and even anticipate their wishes. On the other hand, the Bank needs to optimize its operational costs: reduce the cost price of transactions, facilitate processes, implement electronic document flow, etc. These are the two pillars of the functioning of a modern bank.
Important projects of 2017

Ediny Front (Single Front) topped the list of most significant projects implemented last year to interact with our clients through every available channel. Another important project was the implementation of SAP solutions in preparing tax reports, which automated preparation of individual income tax, broker, and deposit operation statements.

About 30 solutions were implemented in 2017 in order to automate our work with loan debts, including the collection of data. They rendered the process more efficient for the bank and clearer and faster for the client.

Many projects optimized the activity of Retail Bank, including the Unified CRM. Previously, the Bank had many disconnected client databases and systems which automated interaction with clients. The Sales Force Automation (SFA) system was commissioned in 2017. The project involved about 50 people, both IT specialists and representatives of business units, who merged these separate databases into one.

Alfa-Bank is working together with other banks to design a biometric system which will be launched before July 1, 2018. In the summer, Alfa-Bank will register its clients in the Unified System of Identification and Authentication (USIA) by means of personal identification and it will collect biometric data which will be stored in the centralized database of Rostelecom, the USIA operator. Banks will access the unified storage and use the biometric parameters of their clients for identification purposes. We have the important task of developing an application to collect and transfer the data and authenticate clients on the basis of this information. The Bank will develop the necessary equipment and implement software for collecting biometric information and registering clients in the USIA by July, in order to take part in the project with other participating banks.

The core of the banking system, comprising A6C Equation and the integration bus, was upgraded in 2016-2017. Modernization of our hardware and software tripled the system’s productivity and created productivity reserves for the next three to five years of the Bank's development.

IT and business blocks. Merger between Alfa Lab and IT

Many IT functions have recently been reassigned to business blocks, while the IT unit has been supervising their implementation. Business units are responsible for many operations, and our role is evolving from one of construction to architecture: we make sure that the same function is not repeated multiple times, and decide on how to connect functions and to designate elements within one business.

An important event of 2017 was the merger of three IT development units (development for Mass Business, Retail Bank, and Corporate Bank) into one, and the attachment of developers from Alfa Laboratory. Since then, we have developed unified standards and approaches to technologies, combined management structures, and established more efficient control of the development process.

The integration of Alfa Laboratory into the IT unit drew many new professionals to our team; their average age is under 30. This is a major advantage, as we are now seen as a Bank with a young and energetic approach, in addition to our extensive development experience. In addition, Alfa-Lab raised the level of motivation and

enlivened the team, pulling down the barriers between IT and business. New technologies penetrate business processes, and classic IT known for quality development helps implement Alfa Lab’s ideas on a high level.

The understanding of our block’s role evolved in 2017, and the IT block began to operate according to business unit rules. For instance, the practice of industrial contracts was put into place, and the obligations of the IT department and business lines were defined. These contracts were adjusted on a quarterly basis, as was the appraisal of the contract fulfillment by both sides. All contracts were completed to 75-90% by the end of the year. This practice will continue, as it helps to control the interaction between blocks, achieve better results, reach contract objectives, and enhance the synergy between business units and IT.

Interaction with Operations Unit

The line between IT and Operations Unit has been gradually disappearing, as only IT can help Operations Unit achieve its objectives. The only way to reduce costs is to adjust the process of digitalization and develop a strategy of technological transformations, and this is IT’s responsibility.

In 2017, our unit combined forces with the Operations Unit to launch a robotization project: a center of innovative technologies was established in Ulyanovsk. It is the home of the Robotics Process Automation (RPA) team, a group of IT specialists from Operations Unit who are the strategic partners of our block. These experts optimize processes, robotize, and implement AI projects, while solving local but no less important tasks.

The third area where collaboration between the Operations Unit and IT yielded impressive results was in projects aimed at improving client service quality, primarily by accelerating and facilitating processes, for instance, the opening of accounts and the creation of a unified front office for all clients. Joint work with business lines is important for interaction with clients, as they are more aware of the needs of the companies and individuals they work with.

Plans for 2018

IT is moving closer to business with every year; this is a general trend on the financial market which, on the one hand, improves the efficiency of our work and, on the other hand, makes it more complex. It is our goal to provide maximum support to our business partners, and to implement successful projects and constantly raise the efficiency of the IT service, while managing the increased pressure from business.

The Bank will be undergoing serious transformations and adjusting its strategy in 2018, which tasks IT with conducting a successful transformation without loss. In addition, the IT block will help business lines develop a business architecture strategy which is essential for efficient performance. Another priority of next year is our work with mobile devices, which have become an integral part of the lives of individuals and companies. This means we should do the utmost to enable our clients to use their mobile devices to complete their financial tasks. We will also continue to outsource, rendering the Bank more flexible and innovative, while maintaining a high level of IT security. The reliable and smooth operation of all banking systems is our primary objective.
PRINCIPAL FACTORS OF RISK IN BANK ACTIVITY

The Bank prioritizes the management of financial risks. It seeks to maintain an optimal risk-to-profitability ratio, including an acceptable level of risk appetite. The Bank is continuously improving risk management as a key element of its development strategy. The Bank’s risk management is based on principles compliant with Russian laws, international standards, and the best available risk management practices. The Bank has implemented the Internal Capital Adequacy Assessment Process (ICAAP) of the financial institution and the Bank Group. The Bank carries out capital adequacy planning on the basis of stress-testing of capital adequacy and significant risks. The Bank exploits its capacity to increase profitability and expand business, while constantly monitoring risk levels to minimize and contain losses that could occur in the course of its activity.

The Bank’s risk management relies on the improvement of internal methodology and risk management processes as ways of maintaining and strengthening its position on the market of banking services. The Bank develops and upgrades risk and capital management techniques in the areas of internal credit risk models and relevant infrastructure and IT systems. The Bank applies established risk management practice covering financial risks (emphasis is placed on the management of significant risks, such as the non-retail credit risk, the counter-agent credit risk, and the retail credit risk), market risks, operational risks, liquidity risks, interest rate risks, and risks of concentration in non-retail credit risk management.

Risk management consists of risk assessment, determination of risk limits, monitoring, control, accountability, and internal risk management processes. The Bank manages risks by implementing three independent lines of defense in the absence of a conflict of interest.

Implementation of ICAAP of Bank, Bank Group


The ICAAP is a regular cyclic process, which comprises the following stages:

- Identification of inherent and significant risks — the assessment of risks’ significance.
- Assessment of significant risks — the quantitative assessment of every significant risk.
- Aggregation of significant risks — the establishment of an aggregate of significant risks.
- Capital allocation and planning — the establishment of rates of capital adequacy and aggregate exposure within risk appetite.
- Monitoring, control, minimization, and reporting — the continuous control and reporting of significant risks, risk appetite, and capital adequacy, and notification on various management levels.
- Monitoring of procedure efficiency — the verification of the efficiency of risk and capital management methods and controlling procedures.

The Bank’s principal risk and capital management documents have been approved by the Board of Directors, such as the Risk and Capital Management Strategy (including risk appetite information), the Significant Risk Management Procedure, the Procedure of the Elaboration, Approval, Validation, and Implementation of Bank Risk Management Methods and Quality Risk Assessment Models, and the Financial Stability Recovery Plan (in case of significant deterioration of financial status). The Executive Board has approved the Alfa-Bank Methodology of the Calculating Capital Adequacy and Aggregate Exposure, the Procedure of Capital Adequacy Planning and Assessment, the Methodology of Capital Adequacy Stress-testing within the ICAAP, the Procedure of Establishing Capital Limits within the ICAAP, and documents imposing upper limits in significant risk management.

On the Bank Group’s level, the Bank Board of Directors approved the Bank Group’s Risk and Capital Management Strategy (including information regarding the Bank Group’s risk appetite), and the Executive Board approved the Methodology of Establishing Types of Risks Significant to the Bank Group, the Procedure of Capital Adequacy Planning and Assessment of the Bank Group (including the procedure of establishing capital limits of the Group), the Methodology of Exposure Assessment of the Bank Group, the Methodology of Capital Adequacy Stress-testing within the ICAAP of the Bank Group, and documents establishing upper limits to manage significant risks of the Bank Group.

Risk Management: Organizational Structure

The Bank’s system of collegial risk management bodies comprises the Board of Directors, the Board of Directors’ Audit Committee, the Board of Directors’ Staff and Remuneration Committee, the Executive Board, the Strategic Risk Committee, the Asset and Liability Management Committee, the Credit Committees, including the Chief Credit Committee, the Credit Committee, and the Retail Credit Committee, the Corporate Investment Bank Default Committee, the Operational Risk Management Committee, and others. The Executive Board, the Audit Committee, and the Staff and Remuneration Committee are accountable to the Board of Directors, while the Strategic Risk Committee and other risk management committees are subordinate to the Executive Board.
Fundamentals of Bank’s Risk and Capital Management Strategy

The Risk and Capital Management Strategy deals with the elaboration and implementation of the ICAAP. The Strategy aims to establish the fundamental principles of the Bank’s system of management of significant risks and capital in implementing the ICAAP. This is imperative for efficient risk-centered management, the fulfillment of the Bank’s development plans (the development strategy) approved by the Board of Directors, and the provision and protection of the interests of the Bank’s clients and shareholders.

The Risk and Capital Management Strategy:
- Lays a foundation of the significant risk management system;
- Describes the concept of three independent lines of defense;
- Describes functions and responsibilities of management bodies, committees, and units of the Bank in the risk and capital management process;
- Determines key provisions of the Bank’s significant risk management strategy;
- Determines the approach to risk appetite, its indicators and upper (signal) values;
- Determines the approach to the assessment of exposure rates and risk aggregation methods;
- Describes principles of the Bank’s capital planning and management, plans the structure of capital and risks;
- Determines the approach to stress-testing and the stress scenario;
- Determines the procedure of ICAAP reporting and notification of management bodies of non-compliance with limits, achievement of signal values, and measures taken to remedy these situations.

The Bank implements the following procedures as part of the risk and capital management system:
- Determines the approach to the ICAAP’s elaboration and implementation and principles of significant risk and capital management;
- Determines risk appetite;
- Determines significant risks;
- Plans the structure of capital adequacy and risks;
- Aggregates capital requirements and implements relevant methods;
- Organizes the stress-testing process;
- Monitors the ICAAP’s implementation as part of the regular reporting process;
- Verifies the efficiency of the ICAAP’s implementation.

Credit Risk

The Bank defines credit risk as a principal risk; this is the risk of inability of a borrower/counterparty to fully repay a debt in due time. Credit risk exists in the form of non-retail credit risk, retail credit risk, and counterparty credit risk.

The Bank assesses and manages non-retail and retail credit risks by means of internal rating models of the credit risk assessment, including those consistent with the requirements of the Basel Committee on Banking Supervision (BCBS) adjusted by the Russian Central Bank (hereinafter referred to as Basel II).

Non-retail Credit Risk

The non-retail credit division of the Risk Management Directorate oversees the exposure to credit risks posed by clients: legal entities and financial institutions. The Bank follows the general principles of credit risk management, depending on the client’s segment.

In order to increase the efficiency of credit risk management, the Bank divides the non-retail credit portfolio into the following pools:
- Current credits, including those with technical overdue and those which have been overdue for up to 14 days.
- Watch list, including credits showing early signs of impairment.
- Non-performing credits, including credits showing signs of impairment and overdue for more than 14 days.
- Defaulted credits overdue for more than 90 days or showing other signs of default, irrespective of the rating.

The credit policy establishes a system of limits on the non-retail credit risk (including the limits on concentration of credit risks to the Bank’s capital, the limits on concentration of credit risks in the Bank’s credit portfolio, the limits on lending concrete borrowers/groups of related borrowers, the limits on operations with counterparties, and administrative limits), controls compliance with the limits, and establishes the course of action in case where limits or their signal values are exceeded.

The limits are regularly monitored and reviewed. Limits on credit risks are approved according to established procedure. The risk of one borrower, including banks and non-banking financial entities, has additional limits covering balance and non-balance risks, and daily settlement limits on trading instruments such as forex forwards. Compliance with limits on accepted risks is monitored on a daily basis. The borrower’s credit quality is assessed, credit decisions are made, and limits are set on the borrower, including those derived from Basel II, by assessing the default and the internal rating using internal models.

The Bank develops its approach to lending to borrowers by approving a credit policy, which determines the decision-making powers of committees with regard to risk level and a special system of authorization for large transactions. Quality borrowers — Russian companies — are the target lending segment.

The Bank’s credit committees approve limits on credit risk operations. Depending on the significance of a credit risk, decisions on transactions with corporate clients are approved by either the Chief Credit Committee or the Credit Committee. The upper limits on risk are approved by the Executive Board. Committees hold weekly meetings which involve representatives of the Corporate
Investment Bank, the Legal Affairs Department, the Treasury, and other units. Occasionally, the limits/transactions approved by the Chief Credit Committee also require the authorization of the Executive Board or the Board of Directors (depending on the period and/or amount of the credit). The Four Eyes program imposes joint personal limits on employees of the Corporate Investment Bank and the Risk Management Directorate according to the decisions made by the Executive Board. Personal jurisdiction of employees is set by the Executive Board. The Executive Board also makes decisions regarding the writing off of uncollectable debts.

Non-retail Credit Risk. Credit Process and Risk Assessment

The approach to corporate lending is based on a standard underwriting procedure (with due account of the borrower’s segment), which includes verification of the solvency of the potential borrower, the quality of the offered collateral, and the compliance of the deal’s structure with the Bank’s policy and limits; internal ratings are awarded on the basis of statistical models, internal procedures, and Basel II.

Basel II standards are applied at every stage of the corporate lending process:
- assessment of solvency, collateral management, pricing, improvement of internal methodology;
- approach to segmentation;
- integration of internal rating models into the solvency assessment and credit decision-making process;
- credit monitoring; monitoring of operation of internal models;
- identification of default;
- non-performing debts’ management process.

The Corporate Credit Directorate eyes a potential deal, focusing on the analysis of financial stability, adequacy of money flow, long-term stability, credit history, competitive edge, and quality of the collateral. The borrower is awarded an internal rating after the risks are assessed. Internal rating is based on financial, non-financial, and other significant information. Client ratings are used both in the credit process and for pricing purposes.

The Risk Management Directorate analyzes a credit request, verifies the correctness of the awarded rating, and presents an opinion. The opinion of the Risk Management Directorate and the financial analysis of the client are submitted for consideration by the relevant credit committee. Credit committees analyze credit requests in order to set a credit limit based on the information of the collateral. The borrower is awarded an internal rating after the risks are assessed. Internal ratings are regularly monitored and submitted to relevant collegial bodies as part of risk reports.

Clients are divided into the following categories, depending on their credit rating:
- **First-class borrower.** A borrower with the minimal risk of default on credit; as a rule, such borrowers have few debts/high financial stability, often have access to state support, and are usually included in low-risk segments of the credit portfolio.
- **Good/quality borrower.** A borrower with a low or acceptable risk of default on credit; such borrowers have low financial stability, operate in high-risk industries, and demonstrate warning signs of a worsening financial position.
- **Potentially unstable borrower.** A borrower with a considerable risk of default on credit; such borrowers usually have acceptable financial stability and operate in high-risk industries or have a deteriorating financial position and operate in stable industries.
- **Unstable borrower.** A borrower with a high risk of default on credit; as a rule, such borrowers have low financial stability, operate in high-risk industries, and demonstrate warning signs of a worsening financial position.
- **Impaired borrower.** A borrower who defaults on the credit for reasons of: (a) substantial financial difficulties; (b) breach of the agreement, for instance, the failure to pay or a significant delay in paying the interest or the principal debt; (c) the creditor’s allowances are economically or legally related to the financial problems of the borrower; (d) possible bankruptcy or other kinds of financial reorganization of the borrower.

Non-retail Credit Risk. Monitoring.

In the course of routine activity, the Bank constantly analyzes the level of its exposure to credit risk. Credit risk is managed by regular analysis of the ability of current and potential borrowers to pay the interest and the principal debt, as well as by modifying credit limits if necessary. Credit risk is also managed using collaterals and the guarantees of companies and individuals.

Should the borrower’s solvency worsen or negative signs appear, the client is put on the Watch List and monitored for signs of a possible future impairment of creditworthiness.

The relevant credit committee receives information on creditworthiness dynamics in order to carry out analysis and control. The Bank regularly monitors the condition of the businesses of its clients, analysis of their sales, the dynamics of the margin, and the credit portfolio. Client ratings are regularly monitored and submitted to relevant collegial bodies as part of risk reports.

Limits on risk concentration by portfolio are verified weekly, and concentration reports are submitted to the Chief Credit Committee; situations in which the concentration is nearing the upper limit are described. The Chief Credit Committee makes sure that the impact of new operations on the risk concentration by portfolio complies with the Bank’s risk appetite and the structure of portfolio limits.

The Bank pays close attention to non-performing credits and submits weekly reports to the Chief Credit Committee. The Corporate Debt Collection Directorate also analyzes non-performing credits on a weekly basis. The analysis includes payment prospects, impoundment of collateral, debt collection claims, and additional collateral requirements.

Non-retail Credit Risk. Control. The Bank has developed a system of risk control, which applies to all deals posing a credit risk. The purpose of control to ensure strict compliance with internal policies and procedures.
The Bank uses control mechanisms to maintain risk management efficiency. The mechanisms include: (a) regular reports on the condition of portfolios and regular notifications of the relevant committee, (b) definition of main principles of the credit policy on the department’s level, (c) regular analysis of the need to review policy principles, (d) elaboration of lending principles to ensure a disciplined and focused approach to decision making, (e) decision-making based on statistical data, and (f) constant monitoring of the credit process by the Risk Management Directorate and the Internal Audit Department for the purpose of efficiency assessment and relevant adjustments.

Non-retail Credit Risk. Credit Risk Reduction. The Bank employs a broad range of methods to reduce the credit risk and manages loss factors such as the probability of default, losses caused by default, and default exposure, as well as factors of systemic risk of the entire portfolio.

The borrower’s ability to service the possible credit is assessed. The Bank accepts various types of collaterals, sureties of legal entities and individuals, and bank guarantees, as means of risk reduction.

The Bank actively manages the credit risk. The monitoring procedures applied by the Bank enable timely awareness of the scope of risk and ensure that measures are taken to deal with operations showing signs of impairment. These measures include risk reduction, additional collaterals, restructuring, and other tools, depending on the situation. The limits on concentration of credit risks ensure portfolio diversification and prevent excessive levels of concentration.

The risk premium based on the probability of the client’s default is included in the risk assessment and pricing process. It provides a fair compensation for the amount of credit risk accepted by the Bank.

The Bank is constantly improving IT systems to support the implementation of risk management practices consistent with Basel II (including internal rating, and management of data quality, collaterals, and default recognition processes).

Development of the risk management system consistent with Basel II is a key task of the Bank in the field of non-retail credit risk models. The Bank assigns internal and external resources for the development of the approach to the credit rating based on internal assessment models, the system of risk indicators and a risk strategy. It also reviews the credit decision-making matrix, and approaches to collateral management and debt collection, bolsters the IT base, and implements data quality management system as prescribed by the Russian Bank and Basel II.

Counteragent Credit Risk

Analysis of the counteragent credit risk is carried out by the counteragent division of the Non-Retail Risk Department. The counteragent credit risk is managed according to limits imposed on concentration, counterparties and groups of counterparties depending on the type of operations, the level of risk, and the urgency of operation. The limits are consistent with the Bank’s decision-making procedures.

A key factor of limit-setting on counteragent credit risks is the financial status of a counteragent. The status is assessed by means of internal rating models calculating the probability of default by the Basel requirements, as well as expert tools based on financial reports, market quotations, and media reports.

Should the operation involve securities, the counteragent's financial status is assessed in addition to an analysis of the collateral (unless it is cash) in terms of the amount, volatility of cost, and liquidity. In order to further monitor the collateral’s sufficiency, collateral marginal parameters are established (for instance, the initial discount, the margin call that enables the Bank to demand that the debt be reduced or the collateral be enlarged within the period prescribed by the agreement, and the knockout level on which the Bank may start selling the collateral on the market). Also, the counteragent credit risk is lowered by means of liquidation netting agreements (mutual claims and liabilities in a package of deals, which improve the risk profile through diversification) and protect the Bank’s interests should the counteragent fail to fulfill or improperly fulfill its obligations under the agreement.

Retail Credit Risk

The retail risk is managed by the Retail Risk Department, the Retail Credit Committee (Retail Business and Affluent and Private Banking clients), the Mass Business Risk Management Unit, and the Chief Credit Committee (Mass Business clients).

The Retail Risk Unit of the Risk Management Directorate oversees credit risks posed by products such as credit cards, cash loans, target consumer loans, car loans, and mortgage loans, while the Mass Business Risk Management Unit oversees products offered to mass business entities (individual entrepreneurs and legal entities established consistent with Russian laws and reporting annual revenue of no more than 360 million rubles), as well as individuals owning mass business enterprises.

The policies of retail and mass business credits establish the principles of retail and mass business risk management, as well as their identification, assessment, monitoring and control, including portfolio management and divided responsibility associated with managing retail risk. The Bank's credit risk management policy seeks to form a portfolio with minimal volatility. The purpose of the mass business credit policy is to form a homogenous portfolio of standard credits. Differentiated approaches to managing retail and mass business risks achieve the target profitability-to-risk ratio.

The Retail Credit Committee approves the retail credit policy, parameters of retail credit products and prices (interest rates, commission fees, and penalties), the lending process, and main procedures for controlling retail business risks. The committee holds monthly meetings.
PRINCIPAL FACTORS OF RISK IN BANK ACTIVITY

The Chief Credit Committee approves the mass business lending policy, parameters of credit products, the lending process, and main procedures of control mass business risks. The committee holds weekly meetings. The Asset and Liability Management Committee sets prices on mass business products (interest rates, commission fees, and penalties).

Retail and Mass Business Credit Risk. Credit Process and Risk Assessment. The decision-making process in mass business and retail lending is founded on principles of standardization and automation of procedures, including manual verification of information about the applicant, and automated risk assessment processes.

The automatic risk assessment employs statistical models (scoring) based on the analysis of the existent credit portfolio and features of borrowers. The scoring includes information from the questionnaire, the history of client-Bank relations, and information from external sources (for instance, the Credit History Bureau and results of the analysis of the activity of mass business enterprises, in cases where the mass business credit risk is assessed). The credit risk is assessed by means of internal models based on the internal rating and scoring models of other types (including a model which assesses the probability of fraudulent actions of the borrower, etc.).

The Bank regularly monitors stability and efficiency of risk assessment processes and statistical models, and makes adjustments whenever necessary.

Retail and Mass Business Credit Risk. Monitoring. The Risk Management Unit of the Risk Management Directorate monitors retail portfolios on a regular basis. Monitoring encompasses the approval/denial rates by product/client segment, overdue payments (both long and accidental), migration indicators (overdue payment balance by overdue payment groups); collection demands and payment promises for monitoring the collection efficiency; losses of previous periods by product and issuance dates; special pilot programs; write-off indicators for every product portfolio; repayment rates per product portfolio; stability of risk assessment procedures; assessment results by product, and efficiency of segmentation procedures. The Bank prioritizes the risk-adjusted margin in order to optimize the profitability of the retail and mass business portfolios.

Procedures of retail and mass business lending are sporadically modernized to match economic conditions and validation recommendations. Modifications may involve changing the ‘cut-off’ criteria, credit limits, debt coefficients, verification standards, and minimal borrower approval procedures.

Retail and Mass Business Credit Risk. Control. In order to establish efficient control over the retail and mass business credit risk, the Bank sets target values of key retail and mass business credit risks and regularly monitors them. Reports on key risk indicators and information on exceeded target values are submitted to management bodies and relevant committees of the Bank, which make medium and long-term decisions regarding the retail and mass business credit portfolio with the aim of maintaining these indicators within the prescribed limits.

Retail and Mass Business Credit Risk. Credit Risk Reduction. Increased efficiency of retail credit repayment is achieved by the Risk Management Unit of the Risk Management Directorate. They employ statistical models which identify credits posing a high risk of impairment and carry out optimal debt collection procedures in a timely manner. Procedures may include interaction with the borrower via various communication channels, audio, printed, and SMS notifications, and debt refinancing to reduce the debt burden of the borrower. Debt collection procedures are activated if there is information about the deteriorating financial position of a mass business enterprise from external and/or internal sources (borrower/guarantor/turnover on the borrower’s bank accounts) or overdue credit payments.

The efficiency of applied statistical models and payment procedures is monitored by the Mass Business Risk Management Unit and the Retail Risk Unit of the Risk Management Directorate. This is achieved by implementing retail and mass business credit risk monitoring processes according to regular internal reports.

Market Risk

The Bank assesses market risks, i.e. the risk associated with the changing value of Bank positions caused by new market indicators: stock quotations and indexes, currency exchange rates, book prices on precious metals and commodities, and interest rates.

The Market Risk Management Unit, the Treasury, the Asset and Liability Management Committee manage the market risk.

The Bank assesses the market risk of the trading portfolio as required by the Central Bank’s Regulation No 511-P dated 03.12.2015, “On the Procedure for Market Evaluation by Credit Institutions” (hereinafter referred to as Regulation No 511-P) to comply with the mandatory requirements on banks’ activity as outlined by Ordinance No 180-I.

The Bank manages market risks according to principles outlined in the Bank’s internal documents, including the Policy for Market Risk Management as approved by the Executive Board.

The exposure of the Bank’s trading book to market risk is managed using limits on the Bank’s risk metric and the list of permissible instruments put together by the Asset and Liability Management Committee. The Bank uses the following metric to assess market risk to the trading book: the amount of losses in a stress scenario, the value of risk-weighted assets, one-day 99% VaR, and the value of an open security position.

The bank determines the VaR metric with the A% reliability level and the t-day horizon as a value expressed in monetary units that does not exceed with a given probability A% a decrease in the position value during the next t days under the assumption of a ‘normal’ market, and uses this metric with a view to limiting the market risk.
Market risk assessment methods are prescribed by internal documents:
- Methods of preparing and submitting aggregate market risk reports consistent with the Russian Central Bank’s Regulation No 511-P dated December 3, 2015;
- Methods of stress-testing market risks consistent with Alfa-Bank’s ICAAP;
- Historical methods of Alfa-Bank’s VaR market risk assessment.

The Asset and Liability Management Committee sets limits to contain the market risk to the Bank book, such as limits on the interest rate metric, and limits on the size of an open currency position.

**Stock (Quotation) Risk Management.** The stock risk is the risk associated with losses incurred by an unfavorable change in quotations of securities (including those assigning management rights) in the trading portfolio and derivatives influenced by factors linked to the issuer of securities and financial derivatives (the special stock issuer risk), and general fluctuations of market prices on financial instruments (the general stock risk).

In order to carry out quantitative assessment of risks to the Bank’s financial instruments in the trading position of investment business, the Bank imposes limits on the size of an open position, the amount of risk according to Regulation No 511-P, and VaR limits: The stock risk is one of the risks assessed using these metrics.

**Forex Risk Management.** The forex risk is a probability that loss will occur as a result of an unfavorable change in exchange rates of foreign currencies and/or precious metal prices in positions denominated in foreign currencies and/or precious metals. In order to minimise the forex risk, the Bank implements the Russian Central Bank’s Ordinance No 178-I dated 28.12.2016, “On the Amount (Limits) of Open Currency Positions, their Assessment Methods, and Specifics of Supervision of Compliance by Credit Organizations” and sets limits on the sum of open currency positions at an amount of 20% of the Bank’s equity capital in each currency and the balancing positions, and signal values of the market risk metric consistent with Regulation No 511-P, and VaR limits. The forex risk is one of the risks assessed using these metrics.

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The Asset and Liability Management Committee established the following internal direct and indirect limits on the currency position of the Bank:
- Limits and signal values of VaR market risk metrics (1-day horizon, 99% reliability level), which includes the calculation of the Bank’s currency position;
- Limits and signal values of the market risk metric consistent with Regulation No 511-P, which includes the calculation of the Bank’s currency position.
- The internal limits are controlled at the prescribed intervals by relevant units of the Risk Management Directorate and the Treasury.

**Interest Rate Risk**

The Bank is exposed to the interest rate risk due to the nature of its activity — there is a risk of deterioration of the Bank’s financial position caused by a reduction of capital, income, and cost of assets as a result of a change in market interest rates.

The interest rate risk is a combination of two factors: 1) fluctuations in interest rates which, in cases of a certain structure of the Bank’s balance, may cause substantial losses for the Bank or change the value of its capital; 2) uncertain maturity before revision of the Bank’s interest rates on assets and liabilities (non-zero repricing gap) derived from the Bank’s ability to attract and place resources consistent with the market situation and the right of the borrower (creditor) to prematurely terminate its agreement with the Bank (the period before revision is unclear, which increases dependence on the dynamics of interest rates).

Two families of metrics are used as interest rate risk indicators:

1) Indicators of exposure of the Bank capital’s economic value to changing interest rates (DEV(E(ALL)), SSP(ALL), ASP(ALL)):
   - DEV(E(ALL)) — is an integral metric of exposure of the economic value of the Bank’s capital to interest rate shocks standardized by the Basel Committee.
   - SSP(ALL) — is an integral metric of exposure of the economic value of the Bank’s capital to an increase of the sovereign spread (profitability of Russian bonds denominated in a particular foreign currency exceeding market indicators (rates) denominated in this currency).
   - ASP(ALL) — is an integral metric of exposure of the economic value of the Bank’s capital to an increase of the Alfa-spread (the Bank’s credit spread).

2) Indicators of exposure to the expected net interest income of the Bank on the one-year horizon to a change of interest rates (DNIM(ALL), SSEAR(ALL), ASEAR(ALL)):
   - DNIM(ALL) — an integral indicator of exposure of the Bank’s expected net interest income on the one-year horizon to interest rate shocks standardized by the Basel Committee.
   - SSEAR(ALL) — an integral indicator of exposure of the Bank’s expected net interest income on the one-year horizon to an increase of the sovereign spread (profitability of Russian bonds denominated in a particular foreign currency exceeding market indicators (rates) denominated in this currency).
   - ASEAR(ALL) — an integral indicator of exposure of the Bank’s expected net interest income on the one-year horizon to an increase of the Alfa-spread (the Bank’s credit spread).

The limits and signal values are set by the Asset and Liability Management Committee. The metrics are calculated weekly according to the status of assets and liabilities at least 10 days from the calculation date by currency. The Asset and Liability Management Committee uses methods of calculation of interest rate risk metrics and significant factors in order to calculate the interest rate risk metric.
All assumptions made in interest rate risk assessment methods are described in the Procedure for the Management of Interest Rate Risk of AO "Alfa-Bank", a list of assets and liabilities of the bank book exposed to the interest rate risk; interest rate shocks assessed in interest rate risk metrics; periods before the revision of interest rates of the Bank's assets and liabilities exposed to the interest rate risk; and formulas for calculating interest rate risk metrics used to assess demand account probabilities and to calculate maturity of assets (liabilities) and their costs.

Consistent with the current Interest Rate Policy and the Interest Rate Management Procedure, the Bank makes adjustments whenever signal values of interest risk metrics are exceeded. The procedure adjusts the level of interest rate risk whenever the current limits on interest rate risk are exceeded.

The Treasury acts to:
- Conclude deals on financial markets for the purpose of complying with the limits;
- Adjust transfer pricing rates and attraction/allocation interest rates;
- Take additional measures prescribed by the Asset and Liability Management Committee, for instance, ban operations breaching the limits on the interest rate risk.
- Whenever the Treasury's jurisdiction is insufficient, it may submit one or several of the following issues for consideration by the Asset and Liability Management Committee:
  - Adjustment of attraction/allocation interest rates;
  - Adjustment of current allocation funding priorities;
  - Regulatory ban on operations breaching the limit on interest rate risk.

### Liquidity Risk

The liquidity risk is the risk that the Bank is unable to finance its operations, i.e. enlarge assets and meet mature liabilities without incurring losses which threaten the Bank's financial stability.

The Treasury and the Risk Management Directorate manage the liquidity risk. The Asset and Liability Committee monitors the liquidity risk.

Liquidity risk management addresses various manifestations of the risk:
- **Liquidity risk gap** — a gap between crediting and debiting sums and dates (incoming and outgoing money flows);
- **Unforeseen demand risk** — a consequence of unforeseen demands, which may require more resources than expected;
- **Market liquidity risk** — a probability of losses incurred from selling assets due to the impossibility of closing positions amid insufficient market liquidity or trading volume;
- **Funding risk** — the risk associated with a potential change in funding costs affecting the Bank's future revenue;
- **Norm violation risk** — the risk of a breach of norms/indicators/liquidity metrics established by the Russian Central Bank and the Bank's collegial bodies in the daily activity of the Bank;
- **Concentration risk** — the risk of a significant deterioration in physical or normative liquidity caused by an unbalanced structure of assets and liabilities, including a high level of dependence of the Bank's passive base on one/several clients or sources of funding in a certain currency or a certain period.

The Bank maintains a steady funding base, which includes amounts payable on deposits of legal entities and individuals, securities, amounts payable to other banks, and appropriate diversified portfolios of liquid assets enabling a timely response to unforeseen liquidity demands.

While managing liquidity, the Bank constantly:
- Analyzes the level of liquid assets for meeting mature liabilities;
- Ensures access to various sources of funding;
- Adjusts plans in case of funding problems;
- Controls the compliance of the balance-sheet liquidity ratio with legislative requirements.

The Bank manages liquidity risk by monitoring compliance with various liquidity limits and metrics:
- Compliance with the Russian Central Bank's liquidity requirements are monitored daily. These include: (a) the instant liquidity ratio (N2), the ratio of highly liquid assets to demand liabilities; (b) the current bank liquidity ratio (N3), the ratio of liquid assets to liabilities within a 30-day maturity period; (c) the long-term liquidity ratio (N4), the ratio of the entire long-term debt to the Bank to the Bank's equity capital and liabilities on deposit accounts, credits received and other debt liabilities with maturities exceeding 1 year;
- Daily monitoring is carried out of the short-term liquidity ratio calculated according to the Russian Central Bank's Regulation No 421-P dated 30.05.2014 "On the Procedure for Calculating the Liquidity Coverage Ratio" (Basel III) (hereinafter referred to as Regulation No 421-P) and the short-term liquidity requirement N26 of the Bank Group according to Regulation No 510-P dated 28.12.2015 "On the Procedure for Calculating the Liquidity Coverage Ratio (Basel III) of Systemically Important Credit Institutions";
- The structural liquidity ratio N28 of the Bank Group is calculated monthly according to Regulation No 596-P dated 26.07.2017 "On the Procedure for Calculating the Structural Liquidity Ratio (Net Stable Funding Ratio) of Systemically Important Banks (Basel III)."
- Provision of an appropriate portfolio of short-term liquid assets, mostly liquid securities on the Russian Central Bank's Lombard List (HTM and HFS security portfolios), bank deposits, and other interbank instruments;
- Control of the amount of short-term interbank credits covering the asset liability/maturity gap;
- Monitoring of the daily liquidity position and regular liquidity stress-testing in various scenarios, that is, both in standard and in crisis market conditions. The Treasury controls the compliance with liquidity limits imposed by the Asset and Liability Management Committee under the "survival period" crisis scenario. The "survival period" is the number of calendar days where the Bank has positive liquidity in a stress scenario. Monitoring is carried out for all currencies and separate types of currencies: rubles, foreign currencies;
- Assessment of the Bank's market position using the funding cost metric, which compares costs of the Bank to those of its principal rivals;
- Compliance of funding sources' concentration with target values: monitoring of compliance...
The operational risk is the risk that the Bank incurs losses as a result of the unreliable and flawed internal management procedures, unscrupulous conduct of employees, failures of information or other systems, or external events. Operational risk includes the legal risk and the regulatory risk, but excludes the strategic risk and the reputation risk.

The operational risk is managed using a set of procedures which identify, assess, monitor, report, control and/or minimize implications.

The following instruments are used to identify and assess operation risks:

- Analysis of new processes;
- Collection and analysis of events posing an operational risk to the Bank;
- Collection and analysis of events posing an operational risk to other credit institutions;
- Risk control self-assessment (RCSA);
- Key risk indicators (KRI);
- Operational risk scenario analysis (stress-testing).

The analysis of new processes stipulates the identification and assessment of new potential operational risks to processes, products or systems of the Bank at the stage of their creation and implementation.

Events which pose an operational risk are collected and analyzed in order to carry out an objective assessment of losses the Banks would incur from the occurrence of operational risks. Once causes of events posing operational risk are analyzed and measures are implemented to minimize the operational risk, prevent a recurrence of events posing this risk, improve internal processes, raise efficiency, or implement new methods of control.

Events posing the operational risk to other credit institutions are collected and analyzed in order to monitor new operational risks existing in the banking industry and as a source of additional information for the assessment of operational risks to the Bank.

Risk control self-assessment is performed by the Bank’s units in order to identify and assess operational risks inherent in their activity, assessment of the efficiency of current methods of control over identified operational risks, and elaboration and implementation of measures to minimize identified operational risks.

The system of key risk indicators enables the Bank to control and forecast the level of principal operational risks, rapidly identify and react to events increasing the level of the operational risk, and prevent the occurrence of operational risks and losses of the Bank.

The scenario analysis (stress-testing) of operational risks aims to identify potential implications of rare and unlikely events posing operational risk which may cause substantial damage to the Bank. The scenario analysis enables the Bank to implement measures in a timely manner to prevent the occurrence of the scenario or to minimize its consequences.

Heads of the Bank’s units are responsible for containing operational risks under their jurisdiction. The Operational Risk Management Unit of the Risk Management Directorate analyzes and assesses results of the system of operational risk management of the Bank’s units, organizes the implementation of the operational risk management system of the Bank as a whole, controls the operational risk management system, provides professional assistance to employees of the units at various stages of operational risk management (identification, assessment, minimization, control, and monitoring), provides methodological support to units, trains personnel in the field of operational risks, and provides comprehensive consultations on the analysis of risks to processes and the assessment of risks' actuality and probability and the existent methods of control.

A decision on accepting operational risks is made by the Operational Risk Management Committee and the Executive Board as part of operational risk appetite for the current calendar year.

The amount of operational risk is calculated for the purpose of regulatory assessment of capital adequacy in accordance with the Russian Central Bank's Regulation No 346-P dated 03.11.2009 "On the Procedure for Calculating the Amount of Operational Risk." The approach prescribed by Ordinance No 3624-U and recommended by the Basel Committee on Banking Supervision is used for internal management of the operational risk.

Key methods of the operational risk minimization by the Bank are:

- Elaboration of procedures for operations (deals), segregation of powers and reporting of operations (deals), which rule out the emergence of the operational risk;
- Ensuring compliance with these procedures;
- Automation of banking technologies and information security systems.

A principal criterion of the expediency of measures minimizing the operational risk is the economic effect of the operational risk reduction — the cost of control should not exceed the possible losses. Whenever the internal control system fails to cope with the operational risk, and the elimination of this operational risk is not a reasonable option, control may be supplemented with the reassignment of risk to a third party, i.e. outsourcing or insurance. The Bank has a comprehensive financial-institution insurance plan.
Risk of Losing Business Reputation (Reputation Risk)

The risk of losing business reputation (reputation risk) is the risk that losses are incurred as a result of the Bank’s negative image in the eyes of shareholders, counterparties, oversight agencies, and other interested sides which may have a negative impact on the Bank’s ability to maintain current and/or establish new business relations or to ensure constant access to sources of funding.

The Bank has a corporate ethics code which declares its mission and corporate values. The Bank operates on the principle of timely and quality fulfillment of its obligations to clients and partners, and strict compliance with laws and norms of business ethics. The Bank ensures a full and reliable system of public disclosures in mass media and on its website.

Strategic Risk

Strategic risk is the risk of an unfavorable change in various internal and external factors, which may prevent the Bank from accomplishing its strategy.

The Bank controls strategic risk with managerial decisions based on the analysis of the current and prospective situation in the banking sector, levels of risk, actions of the Bank’s rivals, and possibilities of HR, financial, and technical support for pending modifications. The Bank assesses these parameters in order to plan its product range, tariff policy, development of branches and asset-and-liability management, including interest rate management, and qualitative and quantitative development parameters.

The Bank relies on the Strategic Development Unit and the Strategy Management Committee for this purpose. The strategic planning process includes the elaboration of a three-year strategic plan approved by the Board of Directors. The risk of losses caused by mistakes (flaws) in the Bank’s activity and development strategy is insignificant. The Board of Directors approved a development strategy for 2018-2021.

Stress-Testing

As part of internal procedures assessing capital adequacy, the Bank assesses capital adequacy for significant types of risk under stress at least once a year. The purpose of stress-testing is to assess the potential impact on the Bank’s financial stability under a stressful change of internal or external factors in exclusive but probable events. The Bank tests its ability to maintain financial stability amid an economic crisis and stress — significant risks that may harm its financial stability. The amount of capital sufficient to cope with all types of significant risks and the sufficiency of available capital are calculated.

The Bank develops an approach to stress-test every significant type of risk, taking into account the specifics of the Bank’s operational activity, the amount of capital needed to compensate for possible losses, etc. Capital adequacy is stress-tested by aggregating results of stress-tests of significant types of risks. The Bank uses the stress-testing results to develop measures which can be applied to potential stress scenarios.

The Bank comes up with a unified macroeconomic scenario of exclusive but probable events that can harm or destroy its business reputation. Scenarios are based on specifics and areas of the Bank’s activity. A crisis scenario includes crises of previous periods and hypothetical events. Key external macroeconomic factors of the stress scenario are Russia’s GDP, the dollar/ruble exchange rate, the oil price, and the key rate. A number of additional external factors are also taken into account.

The Bank constantly modifies, revises, and supplements the risk management approaches, including the approaches to stress-testing of capital adequacy. By the end of 2017, the annual stress-testing process had resulted in the modification and improvement of the stress-testing methods of credit and concentration risks. Updated stress-testing methods were implemented in 2018. Stress-testing scenarios and results were approved by the Board of Directors.
The Bank is complying with the principles of the Corporate Management Code recommended for application by the Russian Central Bank (The Russian Central Bank’s Letter No 06-52/2463 dated 10.04.2014 “On the Corporate Management Code”).

For the purpose of maintaining and improving corporate management standards, the Bank’s Corporate Management Code was approved at an extraordinary meeting of shareholders in 2013 (Protocol No 02-2013 dated 02.12.2013) developed consistent with current Russian laws, normative acts of the Russian Central Bank, and the Corporate Management Code recommended by the Russian Central Bank.

Alfa-Bank’s Corporate Management Code is an internal normative document laying down fundamental principles, rules, and standards of corporate government, on which the Bank relies in its activity. The Code regulates the following areas: protection of rights and lawful interests of the Bank’s shareholders, organization of the activity of the Board of Directors, determination of the system of remuneration of members of the Board of Directors, executive bodies, and other key managers of the Bank, strategic management, coordination of risk management and organization of internal control, information disclosure, and a procedure for significant corporate actions.

Consistent with the Code, the Bank pledges to be guided with the following general principles of corporate management in its activity:
- Compliance with laws, other normative acts, the Bank’s Charter and internal documents;
- Provision and protection of rights of the Bank’s shareholders;
- Equal (consistent with normative acts) attitude to the Bank’s shareholders;
- Accountability of the Board of Directors to the Bank’s shareholders;
- Strategic management of the Bank’s activity by the Board of Directors;
- Efficient control of the activity of the Bank’s executive bodies by the Board of Directors;
- Ability of executive bodies to operate reasonably, in good faith, and exclusively in the Bank’s interests for the purpose of efficient management of the Bank’s current activity and accountability of executive bodies to the Board of Directors, and the Bank’s shareholders;
- Provision of the creation and efficient functioning of the risk management system and the Bank’s internal control;
- Provision of timely and full disclosure of reliable information about the Bank;
- Openness and transparency of significant corporate actions on the condition of the provision and protection of rights of the Bank’s shareholders.

Shareholders’ Rights and Equality

The Bank provides rights of its shareholder and equal conditions for their use. The procedure of convening, preparing, and holding a general meeting of shareholders is regulated by the Regulation on the General Meeting of Shareholders approved by a general meeting of the Bank’s shareholders (Protocol No 01-2016 of the General Meeting of Shareholders dated 29.06.2016).

Shareholders have an equal and fair access to the Bank’s revenue by means of dividends. The Bank could abstain from paying dividends in case this payment, although it does not formally breach the law, would be economically unfounded and create a false impression of the Bank’s activity.

The protection of property rights of a shareholder and the free disposal of shares are ensured with the Bank’s choice of registrar, AO Independent Registrar Company, which is highly reputed and possesses streamlined and reliable technologies efficiently accounting of property titles and ensuring the implementation of shareholders’ rights.

Bank’s Board of Directors

The Board of Directors executes strategic management of the Bank, organizes bank risk management, supervises the creation and functioning of an efficient internal control system, controls the activity of the Bank’s executive bodies, and performs other key functions. The Board of Directors is accountable to the general meeting of shareholders.

The Regulation on the Board of Directors determines rights and duties of members of the Board of Directors, the procedure for preparing and holding meetings of the Board of Directors, and requirements to members of the Board of Directors, including high professional and business reputation, skills and experience, enabling them to assess information about the Bank’s activity and the market situation for the purpose of professional judgments on banking operations.

A new edition of the Regulation on the Board of Directors was approved in 2017 (Protocol of the General Meeting of Shareholders No 02-2017 dated 28.06.2017). The Regulation was reconciled with the latest adjustments to the Bank Charter, and procedures for holding meetings and in-absentia votes of the Board of Directors were specified.
As of late 2017, the Board of Directors had ten members, including three ultimate beneficial owners (Fridman M.M., Aven P.O. and Kosogov A.N.), and independent member Hartmann O. who operates on the basis of criteria of the Corporate Management Code recommended by the Russian Central Bank. The Board of Directors believes this composition prevents a conflict of interest between the Bank, shareholders, and clients.

The activity of the Board of Directors is supervised by the Chairman, who organizes the work, convenes and chairs meetings of the Board of Directors, sets the agenda and form of meetings of the Board of Directors, signs protocols of meetings of the Board of Directors, chairs general meetings of shareholders, signs a contract with the Chief Executive Officer on behalf of the Bank, and executes other functions envisaged by the Federal Law on Joint Stock Companies, the Bank Charter, and the Regulation on the Board of Directors. Whenever the chairman of the Board of Directors is absent, his functions are performed by the first deputy chairman of the Board of Directors, and in the absence of the latter the work is done by a member of the Board of Directors designated to do so by the Board of Directors.

For the purpose of preliminary consideration of keynote issues of the Bank’s activity, the Board of Directors formed two (2) theme committees in 2014, namely the Audit Committee tasked with assisting in the Board of Directors’ efficient control of the financial and economic activity of the Bank, and the Staff and Remuneration Committee assisting in the recruitment of skilled employees and providing incentives for their successful performance.

The Board of Directors establishes main guidelines for the Bank’s long-term activity, in particular, approves the Bank's strategy and considers the progress of its fulfillment. In 2017, the Bank was operating under the strategic plan for 2017-2019 (Protocol of the meeting of Board of Directors No 14-2016 dated 21.10.2016). In the course of the annual revision of the Bank’s strategy, the Bank’s strategic plan for 2018-2021 was approved in October 2017 (Protocol of the meeting of the Board of Directors No 15-2017 dated 31.10.2017).

The Board of Directors plays a key role in the prevention, identification, and settlement of internal conflicts between management bodies, shareholders, and employees of the Bank. The Board of Directors approved the Procedure for Preventing a Conflict of Interest in the Bank, which prevents the emergence of a conflict of interest in the process of the Bank’s activity. The Board of Directors also approved the Corporate Ethics Code of AO Alfa-Bank (Protocol of the meeting of the Board of Directors No 21-2015 dated 15.12.2015), whose purpose is to lay down standards of the Bank’s activity and employee conduct aimed to maintain ethical standards, quality service and customer convenience, higher profitability, financial stability and efficiency of the Bank, its subsidiaries and affiliates. The Code was posted on the Bank’s website for the general public. The Bank’s employees and members of management bodies were personally familiarized with the Code.

The Compliance Directorate is monitoring the implementation of the Code in the Bank. In fulfillment of the Code’s requirements, the Bank has developed and approved the Regulation on Terms and Procedure for Interested-Party Transactions by Employees of OAO Alfa-Bank and/or their Affiliates (Appendix 1 to Bank Order No 1206 dated 03.12.2010), Bank Order No 980 dated 24.08.2012 on the Participation of Employees of OAO Alfa-Bank in Management of Any Legal Entities Unaffiliated to Alfa-Bank Bank Group, and the Anti-corruption and Anti-bribery Regulation (Appendix 1 to Bank Order No 1704 dated 30.12.2015).


Remuneration of Members of Board of Directors, Executive Bodies, and Other Key Managers

The Bank’s principles of short- and long-term remuneration are based on the Bank’s profitability, and the amount of remuneration is sufficient for recruiting and keeping skilled personnel.

In 2015, the Board of Directors (Protocol of the meeting of the Board of Directors No 02-2015 dated 16.03.2015) approved the Staff Policy, a system of principles and norms aimed at forming human capital consistent with the Bank’s strategy and mission. In 2017, the Board of Directors reiterated the existent Staff Policy. In 2016, the Board of Directors approved a new edition of the Bank’s Remuneration Policy (protocol of the meeting of the Board of Directors No 13-2016 dated 06.10.2016), which regulates the terms and procedure of remuneration of the Bank staff. Prior to that, the documents were considered by the Staff and Remuneration Committee of the Bank’s Board of Directors.

The Board of Directors also approved the Regulation on Remuneration and Compensation of Expenses Members of the Board of Directors Have in the Fulfillment of their Duties, defining general principles, criteria, and procedure for remunerating members of the Board of Directors and compensation of expenses related to the fulfillment of their duties.

Risk Management and Internal Control System

The Bank has developed an efficient system of risk management and internal control aimed at maintaining an acceptable level of risks and achieving the Bank’s goals.
Risk Management: Organizational Structure

The Bank’s system of collegial risk management bodies comprises the Board of Directors, the Board of Directors’ Audit Committee, the Board of Directors’ Staff and Remuneration Committee, the Executive Board, the Strategic Risk Committee, the Asset and Liability Management Committee, the Credit Committees, including the Chief Credit Committee, the Credit Committee, and the Retail Credit Committee, the Corporate Investment Bank Default Committee, the Operational Risk Management Department, and others. The Executive Board, the Audit Committee, and the Staff and Remuneration Committee are accountable to the Board of Directors, while the Strategic Risk Committee and other risk management committees are subordinated to the Executive Board.

Corporate management chart:

Audit Commission - General Meeting of Shareholders
Bank’s Board of Directors
Staff and Remuneration Committee — Audit Committee
Chief Executive Officer
Bank’s Executive Board
SRC, CCC, CC, RCC, Counterparty Subcommittee, ALMC, ORMD, other

The Board of Directors is tasked with organizing the risk and capital management system in general, controlling the implementation and efficiency of the Internal Capital Adequacy Assessment Process (ICAAP) by means of regular ICAAP reports, and approving capital adequacy and stress testing plans, the Bank’s strategy, the Bank’s risk and capital management strategy, risk appetite, and the procedure for managing significant risks.

The Board of Directors’ Audit Committee is tasked with assessing the efficiency of current risk management and internal control procedures, controlling their reliability, and proposing ways of their improvement to the Board of Directors.

The Staff and Remuneration Committee of the Board of Directors is tasked with giving preliminary consideration, analyzing, and preparing proposals to the Board of Directors on regulating the recruitment and remuneration of employees essential to the Bank’s risk management system, and elaborating and improving the Bank’s internal remuneration documents.

The Executive Board is tasked with elaborating the risk management policy based on the Bank’s risk and capital management strategy, approving risk and capital management and stress testing procedures, supervising risk reduction measures and monitoring the optimal ratio of the Bank’s goals to the capital profitability level required by shareholders and the Bank’s risk appetite, ensuring the implementation of the ICAAP, maintaining a higher-than-minimal level of capital adequacy, and processing ICAAP reports.

The Strategic Risk Committee (SRC) is the senior committee in the risk management system. It establishes and regulates the risk management system, determines the Bank’s risk policy and strategy, considers and adjusts the risk management system and principles for the purpose of higher efficiency, approves methods and models of qualitative risk assessment and validation reports, and controls validation of internal models of quantitative risk assessment.

The Chief Credit Committee (CCC) considers and adjusts principles of the credit policy before it is approved by the Executive Board, establishes limits and accepts non-retail credit risks under its jurisdiction approved by the Executive Board, and controls compliance of the credit portfolio’s quality with the approved policy.

The CCC Sub-committee on Capital Market Counterparties establishes credit risk limits on counterparties and security issuers under its jurisdiction.

The Credit Committee (CC) establishes limits on non-retail clients in various types of operations to the extent of the CC limits.

The Retail Credit Committee (RCC) addresses aspects of the retail business strategy, considers the retail credit policy, controls the retail credit risk in the context of reports, and approves retail credit risk management processes under its jurisdiction.

The Asset and Liability Management Committee (ALMC) is tasked with managing market risks, interest rate risks of banking operations, and liquidity risks, optimizing the structure of the Bank’s balance for the purpose of maximum profitability amid the limited risk, establishing aggregate limits on market risks, interest rate risks of banking operations, and liquidity risks, and approving models and methods of their elaboration.

The Operational Risk Management Committee (ORMC) ensures management of operational risks, considers acceptance of operational risks to the limit established by the Executive Board, monitors the operational risk level, and approves measures, procedures, and techniques of identification, assessment, monitoring, control, prevention, and minimization of operational risks.

The Risk Management Directorate subordinated to the Chief Risk Officer bears responsibility for the operation of the risk management system, provides general risk management, and ensures the application of unified identification, assessment, management principles and methods, and relevant notification of the Bank’s administration. The Risk Management Directorate operates consistent with the Regulation on the Risk Management Directorate and comprises the following units: the Non-Retail Risk Department (the Methodology, Modeling, and Risk Reporting Unit; the Industry and Regional Project Risk Analysis Unit; the Industry and Moscow Region Project Risk Analysis Unit; the Counterparties Unit; the Market Risk Management Unit); the Mass Business Risk Management Unit; the Retail Risk Department; the Operational Risk Management Unit; and the Integrated Risk Management Center (the Validation Unit, and the Risk Reporting and Control Department).
The Audit Commission; Management bodies (the general meeting of shareholders, the Bank’s Board of Directors, the Annual report 2017 Alfa-Bank Annual report 2017Alfa-Bank Consistent with the Bank’s statutory and internal documents, internal control is exercised by:

- methodology of recognition of a default and recovery of retail borrowers. The methodology is uncollectable. A third party, a collection agency, could be engaged in the collection process on debt servicing, collection of credit arrears, and identification of debts which are written off as the Operational Block’s Retail Service Department is tasked with measures towards resuming.

The Retail Risk Department lays down retail arrear management rules. The Collection Unit of Risk by Means of Internal Ratings.” It recognizes defaults consistent with an internal document Central Bank’s Regulation No 483-P dated 06.08.2015 “On the Procedure for Calculating Credit The Default Committee of Corporate Investment Bank was established consistent with the Russian laws, normative acts of the Russian Central Bank, and internal documents regulating professional activity on the stock market, Russian laws protecting rights and lawful interests of stock market investors, Russian advertising laws, and internal documents regulating professional activity on the stock market; A structural unit controlling compliance with Federal Law No 224-FZ dated August 7, 2001, “On the Suppression of Money Laundering and Terrorism Financing”; A stock market professional controller — an employee designated to control compliance of the Bank’s professional activity on the stock market with Russian stock market laws, normative acts of the federal executive authority in the field of the stock market, Russian laws protecting rights and lawful interests of stock market investors, Russian advertising laws, and internal documents regulating professional activity on the stock market; A structural unit controlling compliance with Federal Law No 224-FZ dated July 27, 2010, “On Countering the Illegal Use of Insider Information and Market Manipulation and on Modifying Certain Legislative Acts of Russia”; Other units and employees acting consistent with their office duties and jurisdiction established by the Bank’s internal documents.

There is internal audit for the purpose of systematic independent assessment of the reliability and efficiency of the risk management and internal control system, and corporate management practices.

Internal audits are held by a separate structural unit, the Internal Audit Department, which is accountable to the Board of Directors.

The Internal Audit Department operates on the principles of independence, impartiality, competence, and professional approach, continuous activity and neutrality, and on the basis of Russian laws, normative acts of the Russian Central Bank, and internal audit standards set by

The Chief Risk Officer bears responsibility for organizing and controlling the Bank’s risk management process, the creation and development of the Bank’s risk management system, the oversight of the Bank’s current risk profile, and assessment of the sufficiency of risk management resources with due account of the complexity, interconnection, and scope of the Bank’s risks, risk appetite, and strategy.

The non-retail credit risk is managed by the Non-Retail Risk Department (the Methodology, Modeling, and Risk Reporting Unit; the Industry and Regional Project Risk Analysis Unit; the Industry and Moscow Region Project Risk Analysis Unit; the Counterparties Unit; the Market Risk Management Unit) and non-retail credit committees (the CCC and the CC); the CCC has the upper hand in this field. Retail credit risk is managed by the Retail Risk Department and the Retail Credit Committee in the area of Retail Business and Affluent and Private Banking blocks, and the Mass Business Risk Management Unit and the CCC in the area of mass business. Market risk is managed by the Market Risk Management Unit, the Treasury, and the Asset and Liability Management Committee (ALMC). Operational risk is managed by the Operational Risk Management Unit and the Operational Risk Management Committee (ORMC). Risk control (middle office) is also exercised by the Risk Management Directorate (via the Risk Reporting and Control Department). The Treasury, the Risk Management Directorate, and the ALMS manage and control liquidity and interest rate risks.

The Corporate Debt Collection Directorate (CDCD) is fully independent from the Risk Management Directorate; it prepares proposals on ways of dealing with arrears, including collection strategies, elaborates corporate arrear collection solutions, and presents them for the CCC’s consideration. The CDCD implements the approved strategy. It includes the block of the Chief Executive Officer and is accountable to the CCC. The CCC recognizes debts as distressed.

The Default Committee of Corporate Investment Bank was established consistent with the Russian Central Bank’s Regulation No 483-P dated 06.08.2015 “On the Procedure for Calculating Credit Risk by Means of Internal Ratings.” It recognizes defaults consistent with an internal document on default and recovery of non-retail borrowers.

The Retail Risk Department lays down retail arrear management rules. The Collection Unit of the Operational Block’s Retail Service Department is tasked with measures towards resuming debt servicing, collection of credit arrears, and identification of debts which are written off as uncollectable. A third party, a collection agency, could be engaged in the collection process on the basis of an agency contract. Criteria of retail borrowers’ default are set by AO Alfa-Bank’s methodology of recognition of a default and recovery of retail borrowers. The methodology is approved by the RCC.

Consistent with the Bank’s statutory and internal documents, internal control is exercised by:

- Management bodies (the general meeting of shareholders, the Bank’s Board of Directors, the Bank’s Executive Board, and the Chief Executive Officer);
- The Audit Commission;
the International Standards for the Professional Practice of Internal Auditing and the Ethics Code of the Institute of Internal Auditors. The head of the Internal Audit Department is appointed, relieved of duties, and transferred by the Chief Executive Officer on the basis of decisions made by the Board of Directors. The Board of Directors approves work plans and reviews reports of the Internal Audit Department.

The Internal Control Department identifies, reports, and monitors regular (compliance) risk in the Bank; this is the risk of incurring losses from the failure to comply with Russian laws, internal documents of a credit institution, and the imposition of sanctions and/or other measures by supervisory bodies. The Regulation on the Internal Control Department gives a detailed description of the functions of internal control.

Bank Information Disclosure, Information Policy

The Bank discloses information about its activity in accordance with Russian laws on the principles of reliability, regularity, and rapidity, and a balance between the Bank's transparency and observation of its lawful interests.

For the purpose of transparency, timeliness, and completeness of the Bank’s information disclosure, an easy access of shareholders to the Bank’s documents, and designation of employees responsible for the disclosure of the Bank’s information, the Bank has a package of documents regulating the information policy:

- The Regulation on the Interaction between Units in the Information Disclosure by AO “Alfa-Bank” as an Issuer of Securities;
- The list of Bank insider information
- The Regulation on the Interaction between Units in the Disclosure of Bank Insider Information;
- The Regulation on Commercial and Banking Secrets, and the Bank’s Proprietary Information;
- The list of information designated as commercial and banking secrets and the Bank’s proprietary information consistent with relevant laws.


The Bank provides information and documents at the request of shareholders on the equal and unhindered access principles.

Significant corporate actions

Consistent with the Corporate Management Code, the Bank primarily views the following actions as significant corporate actions:

- The Bank’s reorganization;
- Modification (lessening or increase) of the Bank’s charter capital;
- Significant modification of the Bank’s Charter;
- Significant deals;
- Listing and delisting of the Bank’s shares.

The segregation of powers of the Bank’s management bodies in making decisions on significant corporate actions is a key element of the corporate management system aimed at protecting lawful interests and rights of the Bank’s shareholders and assets.

The Bank’s management bodies ensure shareholders’ involvement in decisions on significant corporate actions in accordance with Russian laws and the Bank’s Charter.

The Bank created a system of interaction between units in the field of significant corporate actions. The Bank’s units are doing their best to comply with the procedure for the conclusion of deals and submit those deals for approval by the Bank’s relevant management bodies.

Information about significant corporate actions of the Bank is disclosed in the procedure established by Russian laws.

The Bank’s Internal Audit Service assessing the efficiency of the internal control system may hold selective inspections of the compliance with the decision-making procedure in effect for significant corporate actions.
Alfastrakhovanie Insurance Group

“Alfastrakhovanie” Group is one of the largest Russian insurance companies with a universal insurance services portfolio, including both complex programs for business protection and wide range of insurance products for individuals. According to its license, “Alfastrakhovanie” offers more than 100 products, including life insurance.

“Alfastrakhovanie” is widely represented in the regions of Russia, operates in more than 270 regional offices and has over 25 million private customers across the country.

The “Alfastrakhovanie” Group includes “Alfastrakhovanie PLC”, “Alfastrakhovanie-Life” LLC, “Alfastrakhovanie-OMS” LLC, “Medicine Alfastrakhovanie” LLC.

In 2017, the market share of “Alfastrakhovanie” was 9.9%, the company's fees reached RUB 288.6 bn (RUB 125 bn except OMI - obligatory medical insurance). The company was the second largest Russian insurer on the market (except OMI — obligatory medical insurance). The company “Alfastrakhovanie-OMS” with a market share of 10% is among the five largest participants in the compulsory health insurance system. In 2017, online sales (via website alfastrah.ru) reached a record value of more than RUB 19 bn.

“Alfastrakhovanie” Group has a reputation for being a reliable and stable company. Today, with its obligations, the Group responsible for their own funds — RUB 17.2 bn, the Authorized capital of the company amounts to RUB 7.5 bn.

Key projects

“Alfastrakhovanie” was the first on the Russian's insurance market to produce a number of products that meet the requirements of a modern client.

The “Alfastrakhovanie mobile application” was launched in 2015. This is a free service for our clients, which allows them to declare damages, prolong their insurance policy, make an appointment to see a doctor or call for help from anywhere in the world by clicking “SOS”. In 2017, almost half a million people were using the app.

“Alfa-health Center” is a project of the network of medical centers launched by the Group “Alfastrakhovanie” in 2009, providing quality medical services to residents of 12 cities of Russia: Moscow, Nizhny Novgorod, Yekaterinburg, Tyumen, Rostov-on-Don, Kirov, Saratov,Samara, Yaroslavl, Murmansk, Perm and Berezniki.

At the beginning of 2018, “Alfastrakhovanie” came up with AlfaCyber. This policy will minimize the financial and information risks of almost any business or company that is subjected to cyberattacks.

In August 2017, “Alfastrakhovanie” in partnership with the Moscow school of management SKOLKOVO and RBC information holding, launched an educational project for clients and partners of “Alfastrakhovanie” in the field of risk management entitled ‘Risk Institute’.

Awards and prizes

In 2017, the international agency Fitch Ratings confirmed the financial stability rating of the insurer “Alfastrakhovanie” at the level of “BB” on an international scale. The rating outlook is “stable”.

Also in 2017, the Russian Agency Expert RA confirmed the highest ruAA reliability rating assigned to “Alfastrakhovanie” in 2003 (‘Exceptionally high level of reliability’, the outlook on the rating is “stable”). In 2018, Expert RA raised the rating of the company to the level of ruAA+ reliability. In 2015, RAEX (Expert RA) revised the highest rating of reliability and quality of a++ services, and in September 2016 confirmed the exceptionally high level of reliability and quality of “Alfastrakhovanie-OMS” services. The Agency's experts assessed the quality and stability of the company at an exceptionally high level.

“Alfastrakhovanie” has taken 168 place in a ranking of the largest companies in the country composed of RBC. It also entered the rating of the 600 largest companies of Russia and the top five leaders in the insurance industry from RAEX and publishing house ‘Kommersant’. According to the results of 2017, “Alfastrakhovanie” was awarded the highest reliability assessment based on the results of research conducted by the Analytical center of the National Rating Agency in cooperation with the insurance broker company, Industrial.
In 2015-2017, the work of ‘Alfastrakhovanie’ Group was awarded a number of professional awards and prizes. For many years, managers of the company have occupied leading positions in the authoritative annual rating of “Top 1000 Russian Managers”, a joint project of the Association of Managers of Russia and Kommersant publishing house.

In May 2015, “Alfastrakhovanie” passed the international certification and was awarded of certificate of the international quality management system ISO 9001-2011. In October 2016, General Director of “Alfastrakhovanie”, Vladimir Skvortsov, and General Director of “Alfastrakhovanie-OMS”, Andrey Ryzhakov, joined the Presidium of the SRO on the basis of VSS, and Ilya Kabachnik, Deputy General Director and Director of Aviation Insurance of “Alfastrakhovanie”, joined the Public Council of the Federal Air Transport Agency.

In 2017, “Alfastrakhovanie” was recognized for the third time in a row as the best insurance company of the year in Russia by the British magazine World Finance.

In March 2018, the company won the “Bank of the Year” award from the portal Banki.ru in the “Best Insurance Company of the Year” nomination. “Alfastrakhovanie” also topped the national rating Agency of insurance news (ASN). The company was awarded the fifth annual Travelers ‘Choice award by TripAdvisor in the category “Favorite travel insurance company” and took third place in the ranking of successful insurers of legal entities for 2015, according to the portal Compare.ru. Expert RA rating agency recognized “Alfastrakhovanie” as the market leader in travel insurance and banking risks, and Tripsta international online travel agency confirmed its status as the leader, deeming ‘Alfastrakhovanie’ to be the company with the highest level of trust among Russian travelers.

The application ‘Group Mobile’ has received three awards as part of the largest competition of mobile applications in the world entitled ‘The Golden App 2016’.

‘Alfastrakhovanie’ is among the top 1000 successful suppliers from B2B-Center, Russia’s largest system of electronic bidding for corporate procurement.

As a result of its successful development of business in Siberia, the company was named “Reliable partner” and received an award in the competition “Novosibirsk Brand” for stability and professionalism. In 2017, the product ‘I Choose health!’ from ‘Alfastrakhovanie-OMS’ received the golden award for ‘Kuzbass quality’ in a competition for the best quality of services in Kuzbass.

Clients


Social activities and support for social projects

‘Alfastrakhovanie’ Group is a member of the following unions:

- All-Russian Union of Insurers
- Russian Union of Motor Insurers
- Russian Association of Aviation and Space Insurers
- National Union of Insurers of Responsibility
- National Union of Agricultural Insurers
- Association of Managers of Russia
- Russian Union of Travel Industry
- Environmental Insurance Associations
- Russian Grain Union
- Association of International Road Carriers
- Chamber of Commerce and Industry of the Russian Federation
- Moscow chamber of Commerce and industry
- Union of Marine Insurers

In 2017, “Alfastrakhovanie” was the general partner of the three-year celebration of the Active Citizen Project, an electronic voting platform launched with the support of the Moscow government. “Alfastrakhovanie” has been cooperating for many years with Life Line Foundation, which saves seriously ill children. The company annually supports the Foundation’s initiatives, including “Someone’s life — not a trifle!” which raises money to help children, as well as “Celebration of life” and the “Red nose — Good heart” and Charity race-5275.
Alfa Capital

Alfa Capital Management Company LLC

Alfa Capital Management Company LLC is one of the largest asset management companies in Russia, with a history dating back to 1992. Alfa Capital key businesses are personalized asset management for individual and corporate clients (including individual investment account strategies), as well as management of mutual funds and institutional clients’ assets.

Alfa Capital’s assets under management increased by 35% and exceeded RUB 260 bn as of March 31, 2018, staging a growth of more than six-fold over the past five years. The bulk of the assets, 94%, are individual clients’ funds, which makes Alfa Capital the leader among non-bank companies in the retail sector. Alfa Capital serves more than 1 mln individual clients.

Alfa Capital turned 25 in 2017 and marked the anniversary with a record high volume of assets under management as well as net attraction, management efficiency and number of clients.

Alfa Capital was the first to launch online sales of its products among Russian asset management companies. In 2017, Alfa Capital developed a robo-advisor service and several other cutting edge online services aimed at making online operations quicker and more user-friendly.

ACM at a Glance

Alfa Capital has been a leading asset management firm in Russia for more than 25 years

Assets under management exceed RUB 260 bn as of March 31, 2018

Alfa Capital — the first to launch online sales of its products among Russian asset management companies

Alfa Capital is among the top 11 largest management companies by assets under management and it leads the market by retail clients’ funds under trust management and comes second in mutual funds’ assets, RAEX data reveals

The Alfa Capital team unites highly qualified professionals with many years of expertise in Russia and abroad, including in the emerging markets

Alfa Capital boasts a “А++” rating (Exceptionally high/the highest level of reliability and service quality) assigned by RAEX (Expert RA) Russian rating agency

Alfa Capital is among the top 10 largest asset management companies and comes second in open-end mutual funds and interval mutual funds’ assets (RUB 35.09 bn as of December 31, 2017). Alfa Capital demonstrates the highest growth rates among assets management firms.
**FINANCIAL STATEMENTS**

**Extracts from the Auditor’s Report**

To the Shareholders and Board of Directors of ABH Financial Limited

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of ABH Financial Limited (the “Company”) and its subsidiaries (the “Group”) as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (“IFRS”).

**Responsibilities of management and those charged with governance for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the ability of the Group to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the financial reporting process of the Group.

**Auditor’s responsibilities for the audit of the consolidated financial statements**

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor’s report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the internal control of the Group.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on ability of the Group to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

**25 February 2018**

Moscow, Russian Federation
### ABH FINANCIAL LIMITED
#### CONSOLIDATED STATEMENT OF FINANCIAL POSITION

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>31 December 2017</th>
<th>31 December 2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>5,114</td>
<td>4,344</td>
</tr>
<tr>
<td>Mandatory cash balances with central banks</td>
<td>327</td>
<td>263</td>
</tr>
<tr>
<td>Trading securities</td>
<td>1,201</td>
<td>1,840</td>
</tr>
<tr>
<td>Repurchase receivables relating to trading securities</td>
<td>191</td>
<td>29</td>
</tr>
<tr>
<td>Due from other banks</td>
<td>4,075</td>
<td>3,000</td>
</tr>
<tr>
<td>Loans and advances to customers</td>
<td>27,742</td>
<td>22,762</td>
</tr>
<tr>
<td>Investments</td>
<td>4,374</td>
<td>3,691</td>
</tr>
<tr>
<td>Repurchase receivables relating to investments</td>
<td>115</td>
<td>243</td>
</tr>
<tr>
<td>Other financial assets</td>
<td>649</td>
<td>1,219</td>
</tr>
<tr>
<td>Other assets</td>
<td>399</td>
<td>331</td>
</tr>
<tr>
<td>Premises and equipment</td>
<td>541</td>
<td>524</td>
</tr>
<tr>
<td>Deferred tax asset</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td><strong>TOTAL ASSETS</strong></td>
<td>44,728</td>
<td>38,247</td>
</tr>
<tr>
<td><strong>LIABILITIES</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Due to other banks</td>
<td>2,050</td>
<td>3,428</td>
</tr>
<tr>
<td>Customer accounts</td>
<td>29,552</td>
<td>21,721</td>
</tr>
<tr>
<td>Debt securities issued</td>
<td>3,624</td>
<td>3,580</td>
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<tr>
<td>Other debt</td>
<td>388</td>
<td>323</td>
</tr>
<tr>
<td>Subordinated debt</td>
<td>1,357</td>
<td>1,534</td>
</tr>
<tr>
<td>Other financial liabilities</td>
<td>858</td>
<td>1,479</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>509</td>
<td>417</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>8</td>
<td>31</td>
</tr>
<tr>
<td><strong>TOTAL LIABILITIES</strong></td>
<td>38,346</td>
<td>32,513</td>
</tr>
</tbody>
</table>

### ABH FINANCIAL LIMITED
#### CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>EQUITY</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share capital</td>
<td>1,265</td>
<td>1,265</td>
</tr>
<tr>
<td>Perpetual loan participation notes</td>
<td>695</td>
<td>701</td>
</tr>
<tr>
<td>Fair value reserve for investments available for sale</td>
<td>10</td>
<td>6</td>
</tr>
<tr>
<td>Revaluation reserve for premises</td>
<td>55</td>
<td>69</td>
</tr>
<tr>
<td>Cumulative translation reserve</td>
<td>(1,167)</td>
<td>(1,275)</td>
</tr>
<tr>
<td>Retained earnings</td>
<td>5,457</td>
<td>4,948</td>
</tr>
<tr>
<td>Net assets attributable to the Company's owners</td>
<td>6,315</td>
<td>5,714</td>
</tr>
<tr>
<td>Non-controlling interests</td>
<td>67</td>
<td>20</td>
</tr>
<tr>
<td><strong>TOTAL EQUITY</strong></td>
<td>6,382</td>
<td>5,734</td>
</tr>
<tr>
<td><strong>TOTAL LIABILITIES AND EQUITY</strong></td>
<td>44,728</td>
<td>38,247</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest income</td>
<td>3,225</td>
<td>2,705</td>
</tr>
<tr>
<td>Interest expense</td>
<td>(1,486)</td>
<td>(1,335)</td>
</tr>
<tr>
<td>Expenses directly attributable to leasing and deposit insurance</td>
<td>(62)</td>
<td>(45)</td>
</tr>
<tr>
<td>Net margin</td>
<td>1,677</td>
<td>1,325</td>
</tr>
<tr>
<td>Provision for loan impairment</td>
<td>(10)</td>
<td>(296)</td>
</tr>
<tr>
<td>Net margin after provision for loan impairment</td>
<td>1,667</td>
<td>1,029</td>
</tr>
<tr>
<td>Fee and commission income</td>
<td>1,225</td>
<td>905</td>
</tr>
<tr>
<td>Fee and commission expense</td>
<td>(379)</td>
<td>(271)</td>
</tr>
<tr>
<td>Gains less losses arising from trading securities</td>
<td>(19)</td>
<td>(44)</td>
</tr>
<tr>
<td>Gains less losses arising from interest based derivatives</td>
<td>(3)</td>
<td>(4)</td>
</tr>
<tr>
<td>Gains less losses arising from foreign currencies</td>
<td>(205)</td>
<td>17</td>
</tr>
<tr>
<td>Gains less losses arising from investments</td>
<td>(9)</td>
<td>54</td>
</tr>
</tbody>
</table>
FINANCIAL STATEMENTS

Gains less losses arising from acquisition of own debts (1) (30)
Other provisions (38) 37
Other operating income 76 27
Operating expenses (1 203) (957)
Profit before tax 1 111 763
Income tax expense (313) (236)
Profit for the year 798 527

Other comprehensive income/(loss):
Items that may be reclassified subsequently to profit or loss:
Available for sale investments:
• Fair value gains less losses (4) 31
• Reclassification adjustments for (gains)/losses included in profit or loss 9 (54)
Effect of translation of the financial statements of foreign operations 329 820
Net change in hedge of net investment in foreign operations (269) (820)
Income tax recorded directly in other comprehensive income 53 166
Items that will not be reclassified to profit or loss:
Revaluation of premises (14) -
Income tax on items that will not be reclassified to profit or loss (4) -
Other comprehensive income for the year 100 143
Total comprehensive income for the year 898 670

Profit is attributable to:
The Company’s owners 796 533
Non-controlling interests 2 (6)
Total comprehensive loss attributable to:
The Company’s owners 896 676
Non-controlling interests 2 (6)
Total comprehensive income for the year 898 670

ABH FINANCIAL LIMITED
CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

<table>
<thead>
<tr>
<th>Attributable to the Company’s owners</th>
<th>In millions of US Dollars</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share capital</td>
<td>1 265</td>
</tr>
<tr>
<td>Perpetual loan participation notes</td>
<td>27</td>
</tr>
<tr>
<td>Fair value reserve for investments</td>
<td>71</td>
</tr>
<tr>
<td>Revaluation reserve for premises</td>
<td>(1 438)</td>
</tr>
<tr>
<td>Cumulative translation reserve</td>
<td>4 407</td>
</tr>
<tr>
<td>Retained earnings</td>
<td>4 332</td>
</tr>
<tr>
<td>Total</td>
<td>12 4 344</td>
</tr>
<tr>
<td>Non-controlling interests</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
</tr>
</tbody>
</table>

Balance as at 1 January 2016
Profit - - - - - 533 533 (6) 527
Other comprehensive income - - (21) - 143 - 143
Total comprehensive income for the year - - (21) - 164 533 676 (6) 670
Realised revaluation reserve - - - (2) - 2 - - -
Contribution from noteholders - 701 - - - - 701 - 701
Changes of non-controlling interests - - - - (1) 6 5 14 19
Balance as at 31 December 2016
Profit - - - - - 796 796 2 798
Other comprehensive income - - 4 (11) 107 - 100 - 100
Total comprehensive income for the year - - 4 (11) 107 796 896 2 898
Realised revaluation reserve - - - (3) - 3 - - -
Discretionary interest payments and redemptions of perpetual loan participation notes - (6) - - - (43) (49) - (49)
Distribution to shareholders - - - - - (250) (250) - (250)
Changes of non-controlling interests - - - - 1 3 4 45 49
Balance as at 31 December 2017
Profit - - - - - 1 265 695 10 55 (1 167) 5 457 6 315 67 6 382
### ABH FINANCIAL LIMITED
#### CONSOLIDATED STATEMENT OF CASH FLOWS

<table>
<thead>
<tr>
<th>In millions of US Dollars</th>
<th>2017</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Cash flows from operating activities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest received</td>
<td>3,211</td>
<td>2,647</td>
</tr>
<tr>
<td>Interest paid, other than on debt securities issued, other debt and subordinated debt</td>
<td>(1,040)</td>
<td>(889)</td>
</tr>
<tr>
<td>Expense directly attributable to leasing and deposit insurance paid</td>
<td>(62)</td>
<td>(45)</td>
</tr>
<tr>
<td>Fees and commissions received</td>
<td>1,220</td>
<td>898</td>
</tr>
<tr>
<td>Fees and commissions paid</td>
<td>(378)</td>
<td>(243)</td>
</tr>
<tr>
<td>Net income received from trading securities</td>
<td>106</td>
<td>28</td>
</tr>
<tr>
<td>Net income received from trading in foreign currencies</td>
<td>(195)</td>
<td>168</td>
</tr>
<tr>
<td>Net income received from interest rate derivatives</td>
<td>14</td>
<td>(4)</td>
</tr>
<tr>
<td>Other operating income received</td>
<td>45</td>
<td>20</td>
</tr>
<tr>
<td>Staff costs paid</td>
<td>(680)</td>
<td>(519)</td>
</tr>
<tr>
<td>Other operating expenses paid</td>
<td>(328)</td>
<td>(285)</td>
</tr>
<tr>
<td>Income tax paid</td>
<td>(213)</td>
<td>(298)</td>
</tr>
<tr>
<td><strong>Cash flows from operating activities before changes in operating assets and liabilities</strong></td>
<td>1,700</td>
<td>1,422</td>
</tr>
<tr>
<td><strong>Changes in operating assets and liabilities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net change in mandatory cash balances with central banks</td>
<td>(49)</td>
<td>(84)</td>
</tr>
<tr>
<td>Net change in trading securities and repurchase receivables</td>
<td>397</td>
<td>(790)</td>
</tr>
<tr>
<td>Net change in due from other banks</td>
<td>(1,012)</td>
<td>(1,490)</td>
</tr>
<tr>
<td>Net change in loans and advances to customers</td>
<td>(4,487)</td>
<td>(1,156)</td>
</tr>
<tr>
<td>Net change in other financial assets and other assets</td>
<td>358</td>
<td>88</td>
</tr>
<tr>
<td>Net change in due to other banks</td>
<td>(1,470)</td>
<td>1,184</td>
</tr>
<tr>
<td>Net change in customer accounts</td>
<td>6,753</td>
<td>2,236</td>
</tr>
<tr>
<td>Net change in other financial liabilities and other liabilities</td>
<td>(498)</td>
<td>487</td>
</tr>
<tr>
<td><strong>Net cash from operating activities</strong></td>
<td>1,692</td>
<td>1,897</td>
</tr>
<tr>
<td><strong>Cash flows from investing activities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Acquisition of investments available for sale</td>
<td>(1,435)</td>
<td>(1,121)</td>
</tr>
<tr>
<td>Proceeds from disposal and redemption of investments available for sale</td>
<td>1,573</td>
<td>1,727</td>
</tr>
<tr>
<td>Acquisition of investments at fair value through profit or loss</td>
<td>(8)</td>
<td>-</td>
</tr>
<tr>
<td>Disposal of investments at fair value through profit or loss</td>
<td>8</td>
<td>(2)</td>
</tr>
<tr>
<td>Acquisition of investments held to maturity</td>
<td>(1,200)</td>
<td>(1,164)</td>
</tr>
<tr>
<td>Proceeds from redemption of investments held to maturity</td>
<td>658</td>
<td>298</td>
</tr>
<tr>
<td>Acquisition of premises, equipment and intangible assets</td>
<td>(116)</td>
<td>(183)</td>
</tr>
<tr>
<td>Proceeds from disposal of premises and equipment</td>
<td>2</td>
<td>9</td>
</tr>
<tr>
<td><strong>Net cash used in investing activities</strong></td>
<td>(518)</td>
<td>(436)</td>
</tr>
<tr>
<td><strong>Cash flows from financing activities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Disposal of non-controlling interest in subsidiary</td>
<td>17</td>
<td>-</td>
</tr>
<tr>
<td>Proceeds from debt securities issued</td>
<td>1,769</td>
<td>685</td>
</tr>
<tr>
<td>Repayment of debt securities issued</td>
<td>(1,841)</td>
<td>(1,297)</td>
</tr>
<tr>
<td>Interest paid on debt securities in issue</td>
<td>(284)</td>
<td>(285)</td>
</tr>
<tr>
<td>Proceeds from subordinated debt</td>
<td>-</td>
<td>57</td>
</tr>
<tr>
<td>Repayment of subordinated debt</td>
<td>(201)</td>
<td>(157)</td>
</tr>
<tr>
<td>Interest paid on subordinated debt</td>
<td>(104)</td>
<td>(123)</td>
</tr>
<tr>
<td>Proceeds from perpetual loan participation notes</td>
<td>-</td>
<td>701</td>
</tr>
<tr>
<td>Interest paid on perpetual loan participation notes</td>
<td>(59)</td>
<td>-</td>
</tr>
<tr>
<td>Repayment of other debt</td>
<td>-</td>
<td>(22)</td>
</tr>
<tr>
<td>Interest paid on other debt</td>
<td>(5)</td>
<td>(4)</td>
</tr>
<tr>
<td><strong>Net cash used in financing activities</strong></td>
<td>(708)</td>
<td>(445)</td>
</tr>
<tr>
<td><strong>Net increase in cash and cash equivalents</strong></td>
<td>466</td>
<td>1,016</td>
</tr>
<tr>
<td>Cash and cash equivalents at the beginning of the year</td>
<td>4,344</td>
<td>3,145</td>
</tr>
<tr>
<td>Effect of exchange rate changes on cash and cash equivalents</td>
<td>304</td>
<td>183</td>
</tr>
<tr>
<td>Cash and cash equivalents at the end of the year</td>
<td>5,114</td>
<td>4,344</td>
</tr>
</tbody>
</table>
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