

**Itaúsa Europa – Investimentos,
Sociedade Gestora de Participações Sociais, Unipessoal, Lda.**

Pillar 3 Disclosures

2016

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1. Introduction

Itaúsa Europa - Investimentos, SGPS, Unipessoal, Lda. ("IEI" or the "Company") is the ultimate financial holding company based in the European Union ("EU") of Itau BBA International plc (the "Bank" or "IBBAInt"), a public limited company incorporated under the Laws of England and Wales, registered with company number 7425398, authorised by the Prudential Regulation Authority (the "PRA") and regulated by the Financial Conduct Authority (the "FCA") and by the PRA. IEI is the sole shareholder of the Bank.

IEI is a "SGPS" incorporated under the Portuguese Law, pursuant to which it is legally defined as pure holding company. The corporate purpose of the company is strictly limited to the holding of participations in other companies. The only participation IEI holds is the 100% interest in the Bank.

In this context, the disclosures below have been prepared by IBBAInt, and cover IBBAInt and its subsidiaries (together the "IBBAInt Group" or the "Itau BBA UK Group"), except for section 8 – Capital adequacy which reflects the regulatory capital resources and requirements on a consolidated basis of IEI ("IEI Group").

This document has been reviewed and approved by the Company's Board of Directors.

2. The Three Pillars of the Basel II Accord and its developments

The Basel Accord was implemented in the European Union ("EU") via the Capital Requirements Directive ("CRD"), which was designed to ensure the financial soundness of credit institutions (banks and building societies) and certain investment firms. The CRD framework known as Basel II introduced the concept of three 'pillars'. Pillar I sets out the minimum capital requirements firms will be required to meet for credit, market and operational risk. Under Pillar 2, firms and supervisors have to take a view on whether a firm should hold additional capital against risks not covered in Pillar I and must take action accordingly. Pillar 3 aims to improve market discipline by requiring firms to publish certain details of their risks, capital and risk management.

The Basel II Accord was updated in 2010 to strengthen the global capital and liquidity rules following the financial crisis, through a number of reforms collectively known as Basel III. This has been implemented in the European Union through a new Directive and a Regulation collectively known as the Capital Requirements Directive IV ("CRD IV")¹ which took effect from 1 January 2014.

The Basel Committee on Banking Supervision (BCBS) published the revised Pillar 3 disclosure standards in January 2015 to enhance the comparability, quality and consistency of institutions' regulatory disclosures to the market. The European Banking Authority (EBA) issued its Guidelines on disclosure requirements under Part Eight of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential

¹ The CRD IV legislation consists of: Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Capital Requirements Regulation ("CRR")) and Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD).

requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Capital Requirements Regulation (“CRR”) in December 2016 to apply from 31 December 2017. The implementation of the new international standards in the EU will be made via an amendment to the existing disclosure requirements in the CRR, in particular through a legislative proposal by the European Commission published in November 2016 and currently being considered by the European Parliament and Council of EU.²

3. Background to Pillar 3 disclosures

These disclosures cover the IBBAInt Group. .

The IBBAInt Group’s ultimate parent company is Itaú Unibanco Holding S.A., a Brazilian corporation which, together with its consolidated subsidiaries, form the “Itaú Group”. This holding company is subject to the regulation and supervision of the Central Bank of Brazil (“BACEN”).

The main rules for capital allocation have been changing so as to adapt to the international standards. The information contained in this document refers to the IBBAInt Group and is not necessarily indicative of the Itaú Group as a whole. Investors, stakeholders or other users seeking information on capital adequacy, risk exposure and risk management policies of the Itaú Group should consult its public disclosures.

The qualitative and quantitative information contained in this document represents the position of the IBBAInt Group as of 31 December 2016. Any amendments to IBBAInt’s operating model and risk management procedures that have occurred following this date are not discussed in this document.

This document does not constitute a set of financial statements. The IBBAInt Group 2016 audited financial statements (the “IBBAInt Consolidated Annual Report 2016”) are prepared in accordance with the International Financial Reporting Standards (“IFRS”), as issued by the International Accounting Standards Board (“IASB”) and as endorsed by the EU. Information disclosed in IBBAInt Consolidated Annual Report 2016 will not necessarily be consistent with information disclosed in this document, as some definitions used in this document refer to the regulatory view and may differ from the accounting definitions.

These disclosures have not been audited by the external auditors except where the information is equivalent to that included in the IBBAInt Consolidated Annual Report 2016. The information and figures herein have been subject to internal verification by the relevant areas of the Bank.

This document has been reviewed and approved by IEI’s Board of Directors.

4. Overview of IBBAInt legal structure

IBBAInt is a public limited company incorporated under the Laws of England and Wales, registered with company number 7425398, authorised by the Prudential Regulation Authority (the “PRA”) and regulated by the Financial Conduct Authority (the “FCA”) and by the PRA.

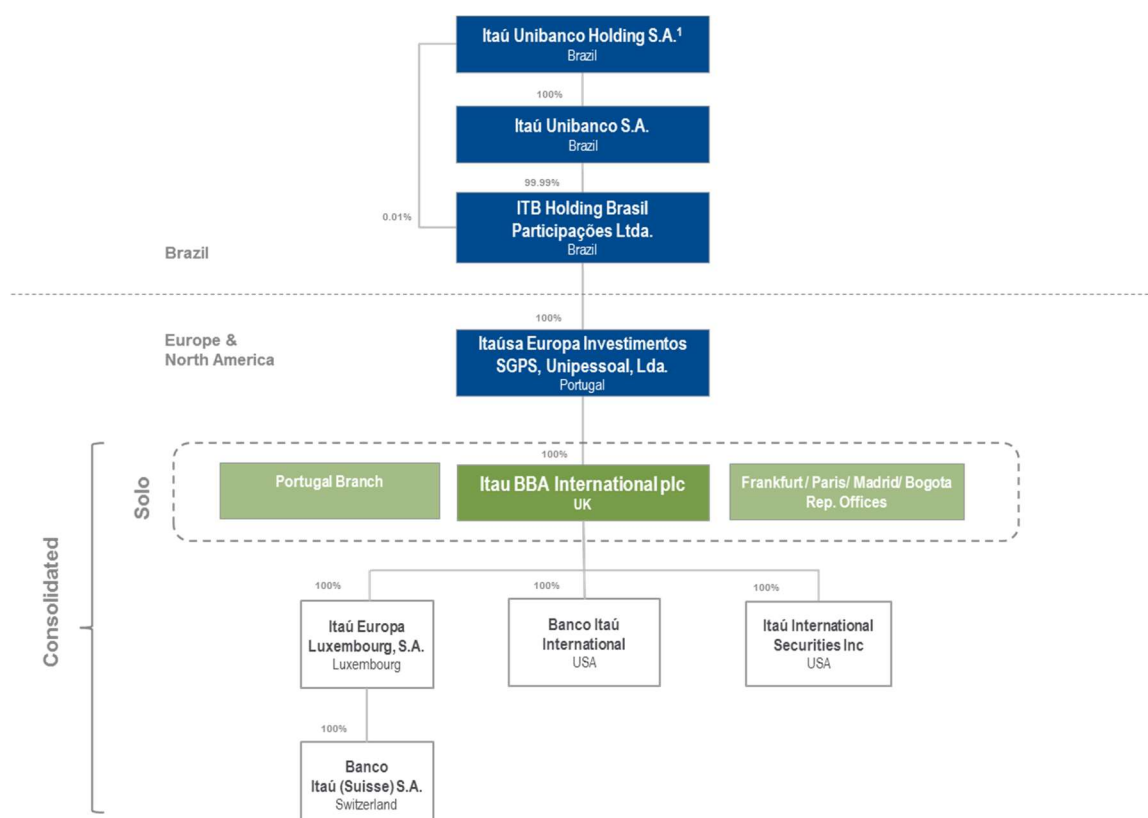
The Bank is a wholly owned subsidiary of Itaúsa Europa - Investimentos, SGPS, Unipessoal, Lda., a Portuguese holding company (“Itaúsa Europa”). Itaúsa Europa is indirectly owned by Itaú Unibanco Holding S.A., a publicly

² Please refer to the European Commission COM(2016) 850 final, available on <http://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/COM-2016-850-F1-EN-MAIN.PDF>

listed joint stock company with its head office in Brazil which owns, inter alia, Itaú Unibanco S.A. (its commercial banking arm) and Banco Itaú BBA S.A. (its investment banking arm). Itaú Group is the largest Latin American financial conglomerate with more than 90 thousand employees and operations in 19 countries throughout the Americas, Asia and Europe.

IBBAInt has overseas banking subsidiaries in the United States of America (“USA”) (Miami) and in Switzerland (Zurich) and a non-banking subsidiary in Luxembourg. These subsidiaries, together with IBBAInt, comprise the IBBAInt Group, as shown in the chart below:

Simplified Corporate Structure



5. IBBAInt Group

The IBBAInt Group’s business model is structured on the basis of two segments of business activity: Corporate & Investment Banking (“CIB”) and International Private Banking (“IPB”).

In the UK, the Bank operates in the CIB, where the strategic focus is on large economic groups and cross-border business between developed markets, in particular between developed markets and Latin America.

IBBAInt owns private banking subsidiaries in the USA and Switzerland, which are the primary delivery channel for the IPB activities of the Itaú Group: Banco Itaú International, headquartered in Miami, and Banco Itaú Suisse S.A., headquartered in Zurich.

The focus of both CIB and IPB is on cross-border business between Latin America and the northern hemisphere (primarily Europe and the USA), taking advantage of the Itaú Group's market leadership in Brazil and its increasing penetration in Latin America.

IBBAInt Group is regulated by the PRA (at the level of the EU parent – Itaúsa Europa – Investimentos, SGPS, Unipessoal, Lda.). It includes all the entities that form part of the accounting consolidation group. As at 31 December 2016, there were no entities which were deducted from IBBAInt Group's capital resources. The IBBAInt Group calculates capital requirements in accordance with the regulatory capital requirements of the PRA, the CRD IV legislation and associated guidance.

6. Governance arrangements

Set out below is a summary of the key governance arrangements in place at IBBAInt. Specific arrangements with regard to risk governance are described in section 7 (Risk management framework) below.

Board of Directors (the “Board”)

IBBAInt operates under a unitary board structure, whereby one body – the Board – provides the overall leadership for the Bank, setting its directions and major policies, appointing and supervising executive top management and ensuring compliance with relevant laws and regulations.

The Board exercises oversight of the Bank's subsidiaries, while respecting the independent legal, regulatory and governance responsibilities which apply to their respective local boards of directors. Given its regulatory responsibilities for the consolidated financial health of the Group, the Board is kept informed of and monitors all material risks and issues that might affect the Group through regular reporting by the top management, including from the risk, compliance and internal audit functions.

The Board may exercise all of IBBAInt's powers. In particular, the Board has reserved powers to approve:

- a) the Bank's strategy and review of its delivery;
- b) the Risk appetite;
- c) the Liquidity Risk appetite - as outlined in the Individual Liquidity Adequacy Assessment Process (“ILAAP”) report, reviewed annually;
- d) the Capital Plan - as outlined in the Internal Capital Adequacy Assessment Process (“ICAAP”) report, reviewed annually; and
- e) the Bank's Recovery Plan and Resolution Pack.

The Board is composed of Group Non-Executive Directors, Independent Non-Executive Directors and Executive Directors.

The following directors held office throughout 2016 and to the date of approval of this report, except where otherwise indicated:

Director	Role	Appointment	Resignation
Candido Botelho Bracher	Chairman Non-Executive	September 2012	December 2016
Alberto Fernandes	Non-Executive	September 2012	
Eduardo Mazzilli de Vassimon	Non-Executive Chairman	May 2013 December 2016	
Flavio Augusto Aguiar de Souza	Non-Executive	December 2015	
Gay Huey Evans	Non-Executive*	September 2012	
Jean-Marc Etlin	Non-Executive	May 2016	
Paulo Jorge dos Santos Lopes	Executive	September 2012	
Renato Lulia Jacob	Executive CEO	September 2012 January 2016	
Ricardo Villela Marino	Non-Executive	September 2012	
Robert Mark Pickering	Non-Executive*	September 2012	

* Gay Huey Evans and Robert Mark Pickering are independent non-executive directors in light of the independence criteria set out by the UK Governance code.

Except as indicated below, the other directorships held by the directors are within the Itaú Group.

As of 31 December 2016, the non-executive directors holding additional directorships in organisations outside the Itaú Group which pursue commercial objectives were:

- Alberto Fernandes – one additional non-executive directorship;
- Eduardo Vassimon – three additional non-executive directorship;
- Gay Huey Evans – two additional non-executive directorships;
- Jean-Marc Etlin – three additional non-executive directorships and one executive directorship;
- Ricardo Marino – three additional non-executive directorships; and
- Robert Mark Pickering – three additional non-executive directorships

Recruitment policy and diversity on the Board

The Board Remuneration and Nomination Committee (“R&NC”) is responsible for leading the process for new appointments to the Board. The R&NC shall regularly evaluate the balance of skills, knowledge and experience on the Board, and, in the light of this evaluation, prepare a description of the role and capabilities required for future appointments.

In performing its duties, the Board Remuneration and Nomination Committee must not discriminate on basis of any characteristic protected by applicable law such as race, national origin, gender, religion, disability, age or sexual orientation. Instead, candidates to the Board shall be assessed on their honesty, competence and capabilities to carry out the role. In terms of age, however, the competency assessment may be indirectly discriminatory because for some roles (such as the chairman of the Board or of its committees) due regard shall be given to the candidate’s experience, which, by definition, is acquired over a period of time. Likewise, in some circumstances, in assessing the capabilities of an individual, the national origin or the country of residence may also impact the assessment

insofar as knowledge and experience on a given national market, business and regulatory environment may be linked to the national provenance of the candidate and not fill the skills gap required for the Board.

Although there are no specific and pre-defined targets for the number of women or other groups being appointed to the Board, diversity is taken into account when assessing Board composition and considering Board appointments.

Chairman of the Board and Chief Executive Officer – Separate roles

The roles of the Chairman and the Chief Executive Officer are separate and fulfilled by different individuals.

The Chairman's main responsibility is to provide leadership to the Board and ensure that its functioning is effective (including by setting the agenda and a timely information flow) and fully complies with the legal and regulatory requirements. Promoting an effective communication between executive and non-executive directors is another crucial role attributed to the Chairman.

The Board has delegated to the **Executive Committee** the general management powers necessary or convenient to conduct wholesale banking business, except for those decision-making powers which remain reserved to the Board due to the material significance for the Bank in terms of their strategic, financial or reputational implications and consequences.

The members of the Executive Committee are appointed by the Board and include the Chief Executive Officer (the "CEO"), as Chairman; the Chief Risk Officer (the "CRO"), the Chief Financial Officer and Chief Operating Officer (the "CFO/COO") and the Head of CIB.

Board Committees

The Board level governance structure comprises three Board Committees: the Risk and Capital Committee ("RCC"), the Audit Committee ("AC"), and the Remuneration and Nomination Committee ("R&NC"). These Board committees are established pursuant to terms of reference approved by the full Board.

The Board ensures that there is an appropriate balance of skill, experience, independence and knowledge to enable the Committees to discharge their responsibilities effectively. The members of the Board Committees are required to have adequate time in order to carry out their responsibilities effectively.

Set out below is a brief description of the role of each of the Board Committees:

(i) Risk and Capital Committee

Risk control arrangements at IBBAInt include RCC in charge of providing focused support and advice to the Board on risk and capital adequacy matters.

The main duties of the Committee include:

- a) providing advice and critical review in relation to the ICAAP, the ILAAP, the Recovery Plan and the Resolution Pack documents;
- b) reviewing relevant policy statements and recommending any changes it considers necessary to the Board for approval;

- c) the development of proposals for consideration by the Board in respect of overall risk appetite and tolerance, target capital ratios as well as ensuring both qualitative and quantitative metrics are used to monitor the Bank's risk management performance;
- d) the oversight and the challenge of the day-to-day risk management and oversight arrangements of the executives;
- e) reviewing whether prices of liabilities and assets offered to clients take fully into account the Bank's business model and risk strategy;
- f) reviewing the Bank's capability to identify and manage new risk types;
- g) considering and approving the remit of the risk management function and ensuring it has adequate resources and appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards; and
- h) providing the advice, oversight and challenge necessary to embed and maintain a supportive risk culture throughout the Bank.

The RCC is chaired by a non-executive director of IBBAInt who holds the position of CRO and CFO of Itaú Unibanco, and is composed by at least two independent non-executive directors (one of which is the chairman of the Audit Committee). IBBAInt's CEO, CRO and CFO are mandatory attendees. All remaining Board members may be invited to attend this Committee's meetings.

The Committee meets at least four times a year, with additional *ad hoc* meetings as and when required.

(ii) Audit Committee

The Audit Committee is accountable to the Board of Directors for the oversight of:

- a) the quality and integrity of the accounts;
- b) the effectiveness of the compliance and internal controls (including financial crime prevention) and risk management systems;
- c) internal audit activities; and
- d) external audit activities.

The Audit Committee is required to include at least two independent non-executive directors, all of whom must be financially literate. The members of the Committee are appointed by the Board from among the non-executive directors, with at least one of the members of this Committee being required to have financial expertise. The CFO and the Head of Internal Audit are mandatory attendees of the Committee meetings. The CEO, the CRO, the Head of Compliance and representatives of the Itaú Group Audit Committee and Internal Audit are regularly invited to attend the Committee meetings. The Audit Committee is chaired by an independent director.

The Committee meets at least four times a year, with additional *ad hoc* meetings as and when required.

(iii) Remuneration and Nomination Committee

The R&NC has duties in relation to both remuneration and nomination issues. The Committee is comprised of at least three members, being two independent non-executive directors. The Committee is chaired by a non-executive director who is the head of the Group-wide CIB. The chairman of the RCC is also a member of the R&NC.

Remuneration:

This Committee is required to exercise competent and independent judgment on remuneration policies and practices and the incentives created for managing risk, capital and liquidity pursuant to its terms of reference. The Committee is responsible for directly overseeing the remuneration of executive directors, executive committee members and senior officers in the risk management, compliance and audit functions of the Bank, and of the CEOs and heads of risk and compliance functions of the Bank's IPB subsidiaries. In discharging its responsibilities, the Committee must take into account the long-term interests of shareholders, investors and other stakeholders in the Bank.

Nomination:

This Committee is also responsible for leading the process for new appointments to IBBAInt's Board and making recommendations regarding appointments to the Board taking into account the challenges and opportunities facing the Bank, and what skills and expertise are therefore needed on the Board.

The Committee meets at least twice every year, with additional *ad hoc* meetings as and when required.

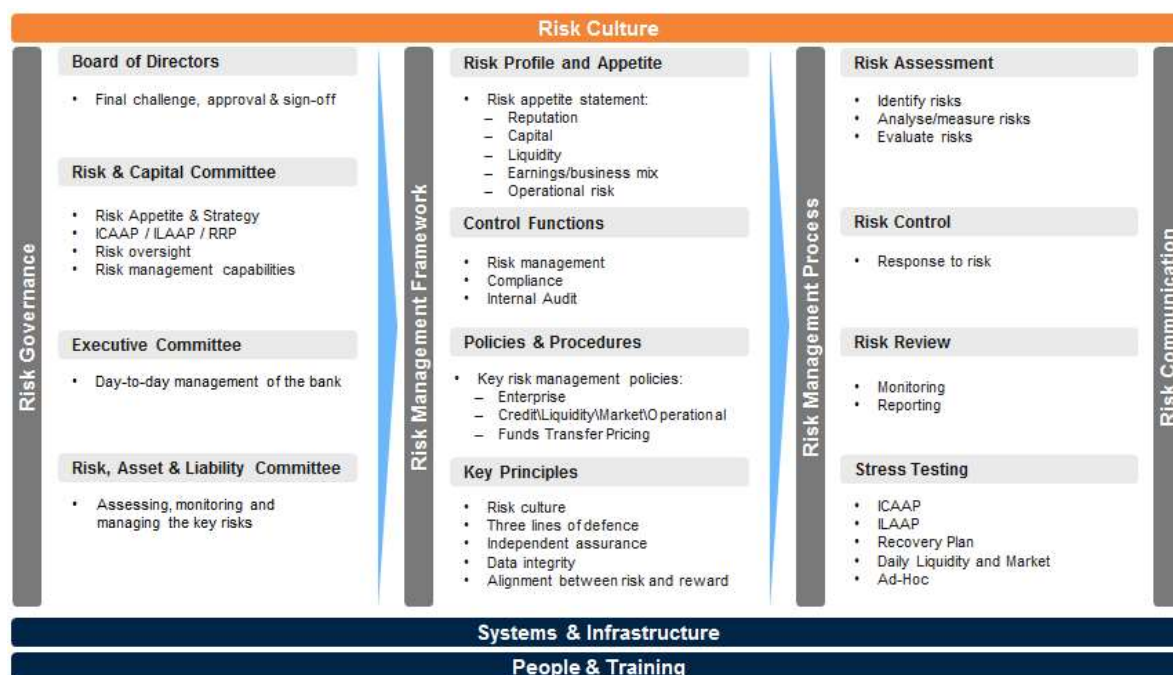
7. Risk management

Risk is an inherent part of the banking business. The Itaú Group regards risk management as an essential instrument for optimising the use of its resources and for selecting the best business opportunities in order to maximise the value creation to shareholders over the long-term. The Bank manages risk within the context of the Itaú Group-wide risk management framework but the Board reviews the overall Itaú Group strategy to ensure it is appropriate for the Bank.

The oversight and direction of the Board is central to the risk management framework. It aims to ensure that appropriate policies, procedures and processes are implemented across the business to control and monitor both the actual and potential risk exposures arising from IBBAInt's operations.

The risk management framework includes oversight bodies for the operational roles and responsibilities, both individual and collective, in the risk management process. This ensures exposed risks are aligned with the Board-approved Risk Appetite and that any unacceptable risk exposures are identified and mitigated, where possible. As an integral part of all organisational processes, the Bank's risk management aims to be inclusive, systematic, structured and timely.

The chart below shows the key components of the overall Bank's risk management framework.



Risk Culture

The Itaú Group has identified four main principles specifically designed to encourage the expected behaviours in terms of risk management. The four principles of Itaú Group's risk culture emphasise the individual and collective responsibility of all employees for maintaining a long-term perspective, with a focus on business sustainability, as follows:

- Consciously taking risks:
 - assess all kinds of risks that can impact clients and the business;
 - understanding and awareness of existing risks – including credit, market, liquidity, operational and reputational risks – and identifying, in a proactive and structured manner, the risks that may arise in the short, medium and long-term;
 - access to internal and external information to make informed decisions, whilst maintaining ethical and business principles.
- We discuss risks:
 - encourage people to share relevant information that creates opportunities for more effective risk management;
 - openly discuss risks and risk appetite in internal meetings, whether bringing good or bad news for all businesses and functions, in a sincere, open, constructive and respectful manner – because it is essential for improving decision-making and risk management.
- We act on risks:
 - systematically reduce the risks that exceed the risk appetite;

- address the root causes, through products, processes, services or behaviour. On identifying these risks, act assertively, without complications, always applying ethical principles, as well as the internal and external rules applicable to Itaú Group, constantly seeking to ensure the durability of the organisation.
- We are all risk managers:
 - individual and collective responsibility for all when it comes to business risks, regardless of position, department or role;
 - not acting alone, keeping management informed and always working alongside the business, support and control departments, without delegating responsibility when it comes to risk management;
 - ultimately, a leading role for everyone when it comes to risk management.

By way of presentations, training, workshops and other ongoing initiatives, the Itaú Group Risk Culture Programme aims to further disseminate the four principles above, reinforcing acceptable risk-taking behaviour and raising risk awareness throughout the Itaú Group.

Risk Governance

The governance arrangements with a particular relevance for risk and capital management are set at both Board and Executive levels³:

- **Board level** – The Board has overall responsibility for ensuring that the Bank maintains an effective risk management framework, having reserved powers to approve: (i) the Bank's strategy and review of its delivery; (ii) the Risk Appetite; (iii) the Capital and Liquidity Plans; and (iv) the appointment and removal of the CRO.
- **Executive level** – Under the authority of the Board, the Executive Committee is responsible for day-to-day management of risks in compliance with the Board-approved Risk Appetite. The Executive Committee shall ensure that the Board-approved Risk Appetite is translated into risk limits and embedded into strategic and financial planning, decision-making processes and compensation decisions, being required to oversee the implementation of the risk policies, procedures and systems, and ensure that the management and, in particular, the individuals responsible for risk management have expertise and knowledge to accomplish the risk management function.

Board Assurance

The Board considers that the governance arrangements and the risk management framework of the Bank are effective to provide assurance that the risk management systems put in place are adequate with regard to the Bank's current profile and strategy.

Risk Management Framework

³ For further details of the Bank's governance arrangements, please refer to section 6 above.

Risk Profile and Appetite

The Group's risk profile and appetite are underpinned by a business model that focuses primarily on:

- Wholesale, cross-border banking for Northern Hemisphere and Latin American corporate clients;
- International private banking for Latin American high net-worth individuals.

Supported by the Bank's risk culture, the Board is committed to:

- Act in accordance with the highest ethical standards and in strict compliance with regulations;
- Seek solid results with low volatility and steady growth through a strategy based upon sustainable client relationships, appropriate pricing of risks, sound sources of funding and adequate use of capital.

The Board has agreed upon a definition of Risk Appetite to limit the total level of risk exposure that it is prepared to accept in pursuit of strategic objectives aligned to those of the wider Itaú Group. The Risk Appetite comprises a set of overarching and supporting statements, to facilitate embedding the principles into business decision-making and to reinforce a strong risk culture across the organisation.

In order to ensure its risk tolerance is effectively interacting with the business strategy and that risk-taking activities in breach of these metrics are identified, escalated and addressed in a timely manner, the Bank has defined quantitative measures across the following dimensions:

a. Reputation

- We shall protect our reputation with our clients, investors, employees, regulators and shareholders, through ethical behaviour, proper business conduct and compliance with the letter and spirit of the regulations;

b. Capital

- We shall maintain enough capital to protect the Bank against a severe recession or others sources of financial stress;

c. Liquidity

- Our liquidity shall support extended periods of funding stress through a sound and appropriate funding structure;

d. Earnings and business mix

- Our businesses shall be based on an appropriate range of clients and products within our core markets, with low appetite for volatility of results and a conservative selection of risks;

e. Operational risk

- We shall have adequate systems, controls and staff to safely manage our businesses and to identify and control operational risk events that may negatively impact our business strategy and our operations.

Control Functions

The risk management framework of the Bank is based on the adoption of the “Three Lines of Defence” model, pursuant to which the various functions, distributed across the “three lines”, play specific and pre-defined roles and responsibilities in order to effectively manage the risks inherent to the Bank’s activities:



First line of defence – Business & Operational Management

The first line of defence lies with business managers, support areas and risk-takers within the organization. They are required to (i) act in accordance with internal risk policies and limits and in compliance with applicable laws and regulations; (ii) develop adequate procedures to ensure risk policies compliance; and (iv) cooperate with the control functions (Risk Management, Compliance and Internal Audit), not interfering with their independent duties.

As part of their responsibilities, they are also required to implement procedures and controls to mitigate risks and to immediately escalate breaches and material risk exposures to the CRO and to the senior management.

Second line of defence – Risk and Compliance

The second line of defence is primarily performed by Risk Management and Compliance functions. They are responsible for risk oversight, policies' compliance monitoring and guidance. They define the methodology and policies for identifying, assessing, monitoring and reporting risks.

Third line of defence – Internal Audit

Internal Audit is an independent function and reports directly to the Board Audit Committee. Their role includes an independent and objective review of the first two lines of defence to provide assurance to the Board that the Bank's activities are in line with the Risk Appetite, regulatory and legal requirements.

Internal Audit should also evaluate the need to supplement its own independent assessment with expertise from third parties to provide a comprehensive independent view of the effectiveness of the risk management and adherence to approved risk limits.

Policies and Procedures

The risk management framework is also supported by policies and procedures. The Enterprise Risk Management policy sets forth the overall approach to risk management for the IBBAInt Group. It describes the key governance and accountability arrangements in place to promote a strong risk culture across the Bank, and the principles and practices to achieve effective risk management in compliance with regulatory requirements and best practices.

The key risks listed below are managed in accordance with specific risk policies and procedures consistent with the general approach set out in the Enterprise Risk Management policy:

- Credit risk: the risk of losses arising from a borrower or counterparty to fulfil their respective financial obligations.
- Liquidity and funding risk: the risk of not having sufficient financial resources to meet obligations as they fall due, or only being able to secure resources at excessive cost. It occurs as a result of imbalances between tradable assets and falling due liabilities, tenor and/or currency mismatches.
- Market risk: the risk of losses resulting from adverse changes in in the value of positions arising from movements in market prices across commodity, credit, equity, foreign exchange rates and interest rates risk factors.
- Operational risk: the risk of losses resulting from inadequate or failed internal processes, people and systems, or from external events, including legal, information security, reputational and conduct risks.

The risk management framework is designed to capture limit breaches and allow for the prompt report of such breaches to senior management so that appropriate follow-up actions are taken.

Risk Management Process

The risk management process comprises:

- Risk assessment – identify, analyse, measure, evaluate risks
- Risk control – response to risks
- Risk review – monitoring and reporting
- Stress testing – periodic (ICAAP, ILAAP, Recovery Plan), daily (Market and Liquidity Risk) and ad-hoc stress tests (scenarios linked to specific events or portfolios)

Stress testing as a firm-wide process involves various areas within the Bank. Scenarios, results and triggered decisions are discussed at management level (Risk, Assets and Liabilities Committee) and reported to the Board Risk and Capital Committee.

Management of Credit Risk

Credit risk refers to the possibility of losses associated with: (i) the failure by the borrower, issuer, or counterparty to fulfil their respective financial obligations under agreed terms, (ii) the depreciation of the credit agreement arising from the deterioration of the borrower's rating, (iii) the reduction of gains or remuneration, (iv) the benefits granted upon renegotiation or (v) debt recovery costs.

The Group establishes limits, risk mitigation mechanisms and processes to monitor and control risks inherent to clients, portfolio concentrations and the impacts of potential changes in the economic environment. Credit risk is

monitored on an ongoing basis and limits and mitigation mechanisms are subject to periodical review. Limits are set by taking into consideration credit risk, country risk and industry risk.

Credit risk management aims at maintaining the quality of the credit portfolio at levels that are consistent with the Bank's risk appetite. To that end, each business unit is required to:

- Follow up and closely monitor the portfolios under its responsibility;
- Grant credit in accordance with the authority levels, market conditions, macroeconomic prospects, changes in markets and products and the effects of sector and geographic concentrations; and
- Manage credit risk by adopting actions that provide sustainability to its business.

The Bank's credit policy is based on internal factors, such as: client rating criteria, performance and evolution of the portfolio, default levels, return rates, and the allocated economic capital; and on external factors, related to the economic environment, interest rates, market default indicators, inflation and changes in consumption.

The concentrations on economic sectors, largest debtors, and geographic region are continuously monitored, hence allowing preventive measures to be taken to avoid the breach of the relevant limits. Credit proposals are analysed on a case-by-case basis through a clearly defined approval governance.

The credit risk control is carried out by an independent and specialised function, duly segregated from the commercial areas. The main responsibilities of the credit risk control function are to:

- Identify, measure, report, monitor and control the Bank's credit portfolio key risks;
- Coordinate the process of preparation, regular review and approval of credit risk policies;
- Ensure that all clients and counterparties to which credit limits are assigned have their risk levels assessed; and
- Monitor Credit Risk Appetite compliance.

In assessing the credit rating of wholesale transactions, the key factors taken into account are the economic and financial condition of the counterparty, its cash-generating capabilities, the economic group to which it belongs and the current and prospective situation of the economic sector and geography in which it operates. Each credit proposal is analysed individually through the approval governance in place at the Bank and the wider Itaú Group. To measure credit risk IBBAInt takes into account the probability of default by the borrower, issuer or counterparty, the exposure at default, past losses from default and concentration of borrowers. Quantifying these risks components is part of the lending process, portfolio management and definition of limits. Models are independently validated, to ensure the accuracy and keep the calibration of the parameters, to be used as tools to quantify these factors, and contribute to more exact decision-making process.

For the Private Banking segment, credit exposures are collateralised by deposits, highly liquid investments or a combination of both.

Management of Counterparty Credit Risk

Counterparty credit risk is the risk of losses arising from the default of the counterparty to derivatives, margin lending, securities lending, repurchase and reverse repurchase or long settlement transactions before final settlement of the transaction's cash flows and where the exposure at default is crucially dependent on market

factors. Additionally, the Bank includes the risk of deterioration of the credit quality of the counterparty in its risk assessment.

Managing, monitoring and controlling the counterparty credit risk arising from derivative financial instruments and other complex financial instruments, as well as from operations with variable indexes, is an integral part of the credit risk management structure in place at the Bank.

Calculation of counterparty credit risk is based on models that allow for an active management of counterparty limits and capital allocation. For derivatives, the potential financial exposure for a transaction up to maturity is used to quantify the relevant credit risk and to determine the credit limits assigned to each counterparty.

Management of Liquidity and Funding Risk

Liquidity and Funding risk is defined as the possibility of not having sufficient financial resources to meet obligations as they fall due, or only being able to secure resources at excessive cost. It occurs as a result of imbalances between tradable assets and falling due liabilities, tenor and/or currency mismatches.

Key principles underlying liquidity and funding risk control are as follows:

- Maintain an adequate level of liquidity resources and a safe and sound funding profile to ensure short-, medium- and long-term obligations under both normal and stressed conditions;
- Invest liquid funds in a manner which emphasises the need for security of principal and ease of conversion to cash; and
- Comply with the applicable regulatory requirements and guidelines.

The Board determines the liquidity and funding risk management strategy in the context of:

- The overall business strategy;
- The liquidity risk appetite; and
- The strategic demands of liquidity and funding disclosed in the business plan.

An independent risk and management control function is responsible for measuring, monitoring and reporting the liquidity risk exposures against the prescribed limits on a daily basis, ensuring the appropriate escalation process. The liquidity risk management and control process is subject to periodic reviews in order to reflect the best market practices, and continuous improvement over time.

The Bank has a comprehensive liquidity and funding risk management framework for managing its liquidity and funding risk, built on policies and governance structures (risk committees), ensuring that the Board-approved Liquidity Risk Appetite is translated into the strategic and day-to-day management of risks and decision-making processes. This framework is established in line with the Itaú Group-wide risk management framework, and also aims to ensure that business is conducted in compliance with regulatory requirements and applicable laws.

Liquidity risk is prudently managed by:

- Considering a set of stress scenarios covering name-specific, market-wide and a combination of both scenarios that contemplate short-term and prolonged periods of illiquidity that may impact the risk exposure and the quantity and quality of liquidity resources and our funding profile;

- Assessing the adequacy of liquidity resources and funding profile vis-à-vis the risks that may crystallise during different types of stress scenarios and their sufficiency to withstand any other disruptions that may arise from deficiencies in our systems and controls; and
- Determine an appropriate size for the liquidity buffer, stable sources of funding and survival period, given the risk tolerance, during a severe but plausible liquidity stress period (varying in magnitude and in duration).

The Bank maintains its liquidity surplus under both internal and regulatory frameworks at an efficient level, monitoring on a daily basis the key liquidity risk drivers, reassessing the nature and severity of its stress scenarios and adjusting its liquidity resources accordingly. Breaches of risk appetite limits are discussed, amongst executives of business and risk control areas, immediately reported to the members of the Risk Assets and Liabilities Committee, with a plan for complying with the limits, and escalated to the Board Risk and Capital Committee.

The liquidity and funding risk management activities that IBBAInt undertakes also include monitoring a range of market and internal EWIs on a daily basis, identifying early emerging signs of liquidity risk in the market or specific to the business. The EWIs enable senior management to take pre-emptive steps to address the stress, including activation of the Contingent Funding Plan or Recovery Plan, if necessary.

Management of Market risk

Market risk refers to the possibility of losses resulting from fluctuations in the market values of positions held by the Bank, most typically caused by variations in foreign exchange rates, interest rates, equity prices, index prices and commodity prices.

At IBBAInt, market risk management is the process by which management monitors and controls the risk of variations in financial instruments, due to market movements, while aiming to optimise the risk-return ratio through an adequate limits structure, effective risk management models and related management tools.

IBBAInt's market risk management strategy is aimed at balancing corporate business goals, taking into account, among other things:

- Political, economic and market conditions;
- The market risk profile of the portfolio; and
- Expertise within the Itaú Group to support operations in specific markets.

The market risk management framework contemplates specific limits assigned to different levels and classes of market risk (such as interest rate risk, foreign exchange risk, among others) and subject to the governance and hierarchy of executive and board level committees. The limits in place range from aggregated risk indicators at the portfolio level to more granular limits at the individual desk level. The market risk limits framework extends to the risk factor level, with specific limits, and is aimed at improving the process of risk monitoring and understanding as well as preventing risk concentration. Limits and alerts are calibrated based on projections of future balance sheets, performance expectations and in compliance with the Board-approved Risk Appetite and the Bank's risk policies. Limits and alerts are monitored on a daily basis, breaches are reported and discussed within one business day amongst executives of business and risk control areas, the root cause is explained and action plans are defined

and implemented. These breaches and related action plans are also reported to the Board Risk and Capital Committee. Key principles underlying market risk control are as follows:

- All market risk taken should be in line with the Bank's risk-return objectives;
- Through disciplined dialogue, senior management is to be kept informed of the overall market risk profile and its evolution through time;
- There should be transparency as to how the business works to optimise results;
- The market risk control structure should provide early warning mechanisms to facilitate effective risk management, without obstructing the business objectives;
- Concentration risks should be monitored and avoided.

An independent risk and management control function is responsible for measuring, monitoring and reporting the market risk exposures against the prescribed limits on a daily basis, ensuring the appropriate escalation process. The market risk management and control process is subject to periodic reviews to reflect the best market practices, and continuous improvement over time.

The Bank's activity is predominantly characterised by portfolios originated from the banking business and operations related to the management of the institution's balance sheet. As a general rule, this book is intended to be either held to maturity, or sold in the medium and long run; interest and foreign exchange rate derivatives are commonly used to hedge the structural risk.

Market risk exposures take into account a set of financial instruments, including derivatives, composed by different risk factors. The main risk factors measured by the Bank are as follow:

- Interest rates: the risk of losses from transactions subject to interest rates variation;
- Foreign exchange rates: the risk of losses from positions subject to foreign exchange rate variation; and
- Equities/Indexes and Commodities: the risk of losses from transactions subject to equity/Indexes or commodities price variations.

Market risk is managed by a combination of processes, including mark-to-market positions, calculating sensitivity to interest rate variations, Value at Risk ("VaR") modelling and performing stress tests across the portfolio.

Market risk is analysed based on the following key metrics:

- Value at Risk ("VaR"): a statistical metric that quantifies the maximum potential economic loss expected in normal market conditions, considering a defined holding period and confidence level;
- Losses in Stress Scenarios ("Stress Testing"): a simulation technique to evaluate the impact on the assets, liabilities and derivatives of the portfolio, of various risk factors in extreme market situations (based on prospective and historic scenarios);
- Mark-to-Market ("MtM") exposure: cumulative exposure of currency risk factor calculated at market value;
- Stop Loss: metrics that trigger a management review of positions if the accumulated losses in a given period reach specified levels;

- Sensitivity (“DV01” or “Delta Variation Risk”): impact on the market value of cash flows when a 1 basis point change is applied to current interest rates or on the index rates.

Management of Operational risk

Operational Risk is the risk arising from people, systems and processes through which a company operates. It also includes other classes of risk, such as fraud, legal risks, physical or environmental risks (e.g. terrorism; natural disasters) and reputation risks (e.g. conduct risks).

For categorisation purposes, IBBAInt uses the definitions of operational risk adopted by the Basel Committee, as follows: internal frauds; external frauds; employee practices and workplace safety; clients, products & business practices; damage to physical assets; business disruption & system failures; and execution, delivery & process management.

The operational risk control is carried out by an independent and specialised function, duly segregated from the commercial areas.

The operational risk management framework is composed of three sequential steps:

- Risk Assessment
 - process mapping performed between the first and second lines of defence where the Bank’s key processes and operational risks are identified and mapped;
 - classification of the risks identified based on the inherent impact (financial, operational, legal/regulatory and reputational) were these risks to materialise;
- Risk Control
 - based on the risk classification, the first line of defence sets out an adequate response, which may include: implementing improvements to the process, running periodical tests on the key controls that mitigate the risk, establishing additional indicators to be monitored, or take no action;
- Risk Review
 - development of risk indicators ensures that the operational risks identified and assessed are monitored and controlled within the limits tolerated; and
 - regular operational risk analysis is disseminated across the Bank through reports discussed with the relevant areas and within the relevant risk committees.

Within the scope of this ongoing monitoring, the Operational Risk team considers: the issues identified by internal and external audit, the daily events and weaknesses identified by the first line of defence, the action plans defined when performing the risk response, the operational losses and the key risk and performance indicators.

Risk Communication

Management promotes an open communication culture encouraging the immediate escalation of actual or emerging risks and allows for continuing focus on prudent risk management. The Board and senior management receive appropriate risk information on a periodic basis.

8. Capital adequacy

Capital resources

Under PRA supervision, the IEI Group is required to maintain a minimum ratio of total capital resources to capital requirements. The same consolidation scope is used by the IEI Group for both accounting and regulatory purposes, which means that the group of companies and risks that are part of the regulatory analysis is the same as the ones presented on the IEI Group financial statements ("IEI Consolidated Annual Report 2016").

Notes 25, 26 and 27 to the IEI Consolidated Annual Report 2016 provide additional information and disclosure regarding the main features of Common Equity Tier 1 items.

The table below summarises the components of regulatory capital as at 31 December 2016. During the past exercise IEI and all its regulated subsidiaries complied with all of the imposed capital requirements to which they are subject.

Table 1: Capital resources

USD m	31.12.16	31.12.15
Common equity tier 1 capital	999	953
Permanent share capital	702	702
Share premium	132	132
Profit and loss account and other reserves	240	199
Intangible assets	(74)	(79)
Prudent valuation adjustments	(1)	(1)
Tier 2 capital	8	10
Total regulatory capital	1,007	963
Total capital requirements	441	423
Risk-weighted assets (RWA) ¹	5,510	5,283
Common equity tier 1 ratio	18.1%	18.0%
Total capital ratio	18.3%	18.2%

¹ Total capital requirements x 12.5

The table below shows Tier 2 capital issued by instrument and provides particular key terms and conditions. Regulatory Tier 2 capital amounts are different from the ones recorded under IFRS due to the PRA specific eligibility requirements.

Table 2: Summary of terms and conditions of capital resources

USD m	31.12.16		31.12.15	
	Regulatory balance	IFRS balance	Regulatory balance	IFRS balance
Subordinated Loan	4	30	10	30
General Credit risk adjustments	4	4	-	-
Total Tier 2	8	34	10	30

Regulatory Capital Requirements

The IEI Group calculates capital requirements in accordance with the rules and guidance set out by the PRA and the European Banking Authority. This section describes IEI Group Pillar 1 capital requirements.

Where it is not separately shown, counterparty credit risk is within credit risk.

The following table shows IEI Group capital requirements as at 31 December 2016:

Table 3: Total capital requirements by risk type

USD m	31.12.16	31.12.15
Credit Risk	393	377
Counterparty Credit Risk	5	7
Market Risk	8	3
Interest rate risk	2	2
Foreign exchange risk	6	1
Settlement Risk	-	-
Credit valuation adjustment (CVA)	1	2
Operational Risk	34	33
Total	441	423

The IEI Group's overall minimum capital resources requirement under Pillar 1 is calculated by adding the credit risk charge (standardised approach) and the counterparty credit risk charge (MtM method) to that required for market risk (debt instruments and foreign-exchange risk requirement) and the operational risk element (basic indicator approach).

The table below provides the risk weighted assets by IFRS balance sheet asset type.

Notwithstanding the fact that the basis of consolidation for both accounting and regulatory purposes is the same, some balances are subject to specific regulatory adjustments prescribed by the CRD IV, such as adjustments to account for differences in IFRS and regulatory netting, and items treated as regulatory capital deductions.

Table 4: IFRS Balance sheet and risk weighted assets by type

USD m	31.12.16			31.12.15		
	Balance sheet amount	Average weight	Risk weighted assets (RWA)	Balance sheet amount	Average weight	Risk weighted assets (RWA)
Assets						
Cash and Balances at central banks	844	0.0%	-	1,561	0.0%	-
Loans and advances to Banks	984	56.5%	556	936	24.9%	233
Loans and advances to customers	4,476	89.4%	4,000	4,682	87.2%	4,082
Securities non-trading book	799	0.3%	2	621	0.0%	-
Securities trading book	163	0.0%	-	106	0.0%	-
OTC and market derivatives	138	45.7%	63	224	38.8%	87
Embedded derivatives	100	0.0%	-	319	0.0%	-
Property, plant and equipment	16	100.0%	16	18	100.0%	18
Goodwill and intangible assets	90	0.0%	-	93	0.0%	-
Investment in associates	-	-	-	26	100.0%	26
Tax assets	19	78.9%	15	18	105.6%	19
Other assets	31	100.0%	31	40	100.0%	40
Total Assets	7,660	61.1%	4,683	8,644	52.1%	4,505
Guarantees	133	68.4%	91	185	60.5%	112
Commitments	437	45.8%	200	436	42.9%	187
Total Off-Balance Sheet	570	51.1%	291	621	48.1%	299
Total RWA for Credit Risk	8,230	60.4%	4,974	9,265	51.9%	4,804
Credit Risk capital requirement			398			384

Despite being presented as having an average risk weight of 0%, goodwill, intangible assets and deferred tax assets that rely on future profitability are excluded from the calculation of the credit risk exposure value as they are deducted from regulatory capital under the CRD IV.

Analysis of Credit Risk

CAPITAL REQUIREMENTS FOR CREDIT RISK AND EXPOSURES

The table below summarises credit risk information and shows original exposure, exposure after Credit Risk Mitigation ("CRM"), Risk Weighted Assets ("RWAs") and the related capital requirements. Exposures before CRM are further analysed by geography and residual maturity.

It should be noted that the regulatory criteria used for defining exposures is different from the accounting criteria used for defining assets.

Table 5: Exposure values (original and after CRM), RWAs and capital requirements by exposure class

USD m	31.12.16							
	Year-end				Average			
	Original exposure value	Exposure value after CRM	RWA	Capital requirements	Original exposure value	Exposure value after CRM	RWA	Capital requirements
Exposure class								
Standardised approach								
Central governments or central banks	1,774	1,774	2	0	1,970	1,970	1	0
Institutions	1,247	1,491	696	56	1,515	1,809	801	64
Corporates	5,591	5,128	4,206	336	5,728	5,203	4,224	338
Retail	-	-	-	-	-	-	-	-
Secured by mortgages on immovable property	6	6	6	0	7	7	7	1
Exposures in default	-	-	-	-	-	-	-	-
Equity exposures	-	-	-	-	20	20	20	2
Other items	144	144	64	5	166	166	82	7
Total	8,762	8,543	4,974	398	9,406	9,174	5,134	411

USD m	31.12.15							
	Year-end				Average			
	Original exposure value	Exposure value after CRM	RWA	Capital requirements	Original exposure value	Exposure value after CRM	RWA	Capital requirements
Exposure class								
Standardised approach								
Central governments or central banks	2,297	2,297	-	-	1,785	1,785	-	-
Institutions	1,040	1,387	409	33	986	1,420	391	31
Corporates	6,089	5,516	4,282	343	6,350	5,597	4,346	348
Retail	-	-	-	-	-	-	-	-
Secured by mortgages on immovable property	8	8	8	1	9	9	9	1
Exposures in default	-	-	-	-	-	-	-	-
Equity exposures	26	26	26	2	26	26	26	2
Other items	159	159	79	6	162	162	78	6
Total	9,619	9,393	4,804	384	9,317	8,999	4,849	388

Table 6: Geographic distribution of credit exposure

USD m						
Exposure value after CRM	Europe	South America	North America	Central America and Caribbean	Other countries	Total
As at 31 December 16						
Standardised approach						
Central governments or central banks	256	557	957	-	4	1,774
Institutions	446	45	209	790	1	1,491
Corporates	1,302	1,624	972	1,156	74	5,128
Retail	-	-	-	-	-	-
Secured by mortgages on immovable property	6	-	-	-	-	6
Exposures in default	-	-	-	-	-	-
Equity exposures	-	-	-	-	-	-
Other items	28	-	116	-	-	144
Total	2,038	2,226	2,254	1,946	79	8,543

USD m						
Exposure value after CRM						
As at 31 December 15						
Standardised approach						
Central governments or central banks	567	266	1,460	-	4	2,297
Institutions	591	90	158	541	7	1,387
Corporates	1,430	1,977	699	1,312	98	5,516
Retail	-	-	-	-	-	-
Secured by mortgages on immovable property	8	-	-	-	-	8
Exposures in default	-	-	-	-	-	-
Equity exposures	26	-	-	-	-	26
Other items	38	-	121	-	-	159
Total	2,660	2,333	2,438	1,853	109	9,393

Table 7: Residual maturity breakdown of credit exposure

USD m					
Exposure value after CRM					
As at 31 December 16					
Standardised approach					
Central governments or central banks	177	742	-	855	1,774
Institutions	659	591	37	204	1,491
Corporates	1,976	2,003	1,149	-	5,128
Retail	-	-	-	-	-
Secured by mortgages on immovable property	-	-	6	-	6
Exposures in default	-	-	-	-	-
Equity exposures	-	-	-	-	-
Other items	-	-	-	144	144
Total	2,812	3,336	1,192	1,203	8,543

USD m					
Exposure value after CRM					
As at 31 December 15					
Standardised approach					
Central governments or central banks	75	600	51	1,571	2,297
Institutions	722	428	30	207	1,387
Corporates	1,931	2,499	1,086	-	5,516
Retail	-	-	-	-	-
Secured by mortgages on immovable property	-	-	8	-	8
Exposures in default	-	-	-	-	-
Equity exposures	-	-	-	26	26
Other items	-	-	-	159	159
Total	2,728	3,527	1,175	1,963	9,393

CREDIT RISK MITIGATION

The IEI Group uses a range of techniques to mitigate credit risk under the standardised approach. Where credit risk mitigation is available in the form of an eligible guarantee or credit derivatives, the risk weight of the protection provider is considered in the amount of the protection it provides.

For exposures fully or partially covered by eligible financial collateral, the value of the exposure is adjusted under the Financial Collateral Simple Method.

The following table shows the CRM by exposure class under the standardised approach as of December 2016.

Table 8: Standardised approach – credit risk mitigation by exposure class

USD m As at 31 December 16	Exposures covered by eligible financial and other collateral	Exposures covered by credit derivatives or guarantees	Exposure value after CRM
Standardised approach			
Central governments or central banks	118	-	1,774
Institutions	75	-	1,491
Corporates	1,228	113	5,128
Retail	-	-	-
Secured by mortgages on immovable property	-	-	6
Exposures in default	-	-	-
Equity exposures	-	-	-
Other items	-	-	144
Total	1,420	113	8,543

USD m As at 31 December 15	Exposures covered by eligible financial and other collateral	Exposures covered by credit derivatives or guarantees	Exposure value after CRM
Standardised approach			
Central governments or central banks	105	-	2,297
Institutions	49	-	1,387
Corporates	1,688	50	5,516
Retail	-	-	-
Secured by mortgages on immovable property	-	-	8
Exposures in default	-	-	-
Equity exposures	-	-	26
Other items	-	-	159
Total	1,842	50	9,393

CREDIT QUALITY ANALYSIS OF STANDARDISED EXPOSURES

Credit Rating Agencies

In order to determine the RWAs for calculating the credit risk charge, the IEI Group has adopted the standardised approach, where the credit risk derives among other factors from external ratings provided by External Credit Assessment Institutions (“ECAIs”). The PRA determines which agencies may be used to determine such ratings and therefore the correct risk weights. Based on that guidance the IEI Group has chosen the Standard & Poor’s, Moody’s and Fitch Ratings.

The following table describes the relationship of ECAIs’ long-term external credit ratings and the correspondent credit categories (denominated as credit quality steps) for risk-weight purposes.

Table 9: Relationship of long-term external credit ratings to credit quality steps

Credit Quality Step	Moody’s	Fitch	S&P
Credit Quality Step 1	Aaa to Aa3	AAA to AA-	AAA to AA-
Credit Quality Step 2	A1 to A3	A+ to A-	A+ to A-
Credit Quality Step 3	Baa1 to Baa3	BBB+ to BBB-	BBB+ to BBB-
Credit Quality Step 4	Ba1 to Ba3	BB+ to BB-	BB+ to BB-
Credit Quality Step 5	B1 to B3	B+ to B-	B+ to B-
Credit Quality Step 6	Caa1 and below	CCC+ and below	CCC+ and below

The following table shows the relationship between the credit quality steps and the correspondent risk weights under the standardised approach.

Table 10: Credit quality steps and risk weights

Credit Quality Step	Corporates	Institutions (Includes Banks)			Sovereigns
		Sovereign Method	Maturity <= 3 months	Maturity > 3 months	
Credit Quality Step 1	20%	20%	20%	20%	0%
Credit Quality Step 2	50%	50%	20%	50%	20%
Credit Quality Step 3	100%	100%	20%	50%	50%
Credit Quality Step 4	100%	100%	50%	100%	100%
Credit Quality Step 5	150%	100%	50%	100%	100%
Credit Quality Step 6	150%	150%	150%	150%	150%

The table below shows original exposure broken down by exposure class and credit quality step.

Table 11: Credit quality step analysis of original exposure and capital deductions

USD m	Credit Quality Step 1	Credit Quality Step 2	Credit Quality Step 3	Credit Quality Step 4	Credit Quality Step 5	Credit Quality Step 6	Credit quality step unrated	Total	Deducted from Capital Resources
Original exposure value									
As at 31 December 16									
Standardised approach									
Central governments or central banks	1,183	3	10	550	-	-	28	1,774	-
Institutions	102	337	130	648	-	-	31	1,248	-
Corporates	26	25	264	739	424	34	4,079	5,591	-
Retail	-	-	-	-	-	-	-	-	-
Secured by mortgages on immovable property	-	-	-	-	-	-	6	6	-
Exposures in default	-	-	-	-	-	-	-	-	-
Equity exposures	-	-	-	-	-	-	-	-	-
Other items	-	-	-	-	-	-	144	144	-
Total	1,311	365	404	1,937	424	34	4,288	8,763	-
USD m									
Original exposure value									
As at 31 December 15									
Standardised approach									
Central governments or central banks	2,013	3	5	265	-	-	11	2,297	-
Institutions	17	575	305	110	-	-	33	1,040	-
Corporates	-	55	294	1,310	100	437	3,893	6,089	-
Retail	-	-	-	-	-	-	-	-	-
Secured by mortgages on immovable property	-	-	-	-	-	-	8	8	-
Exposures in default	-	-	-	-	-	-	-	-	-
Equity exposures	-	-	-	-	-	-	26	26	-
Other items	-	-	-	-	-	-	159	159	-
Total	2,030	633	604	1,685	100	437	4,130	9,619	-

The table below shows exposure after CRM, broken down by exposure class and credit quality step.

Table 12: Credit quality step analysis of exposure after CRM and capital deductions

USD m	Credit Quality Step 1	Credit Quality Step 2	Credit Quality Step 3	Credit Quality Step 4	Credit Quality Step 5	Credit Quality Step 6	Credit quality step unrated	Total	Deducted from Capital Resources
Exposure value after CRM									
As at 31 December 16									
Standardised approach									
Central governments or central banks	1,183	3	10	550	-	-	28	1,774	-
Institutions	107	360	160	802	-	-	62	1,491	-
Corporates	37	104	196	698	351	34	3,708	5,128	-
Retail	-	-	-	-	-	-	-	-	-
Secured by mortgages on immovable property	-	-	-	-	-	-	6	6	-
Exposures in default	-	-	-	-	-	-	-	-	-
Equity exposures	-	-	-	-	-	-	-	-	-
Other items	-	-	-	-	-	-	144	144	-
Total	1,327	467	366	2,050	351	34	3,948	8,543	-
USD m									
Exposure value after CRM									
As at 31 December 15									
Standardised approach									
Central governments or central banks	2,013	3	5	265	-	-	11	2,297	-
Institutions	19	587	338	124	-	-	319	1,387	-
Corporates	14	88	222	1,252	100	263	3,577	5,516	-
Retail	-	-	-	-	-	-	-	-	-
Secured by mortgages on immovable property	-	-	-	-	-	-	8	8	-
Exposures in default	-	-	-	-	-	-	-	-	-
Equity exposures	-	-	-	-	-	-	26	26	-
Other items	-	-	-	-	-	-	159	159	-
Total	2,046	678	565	1,641	100	263	4,100	9,393	-

ACCOUNTING IMPAIRMENT

The following tables show total loans and advances to customers and banks, past due and impaired loan balances, split by asset type and by geographic distribution. The information presented is consistent with the IEI Consolidated Annual Report 2016, and therefore follows the IFRS as adopted by the EU.

Table 13: Analysis of impaired and past due exposures and allowance for impairment by asset class

USD m	Neither Past due nor Impaired	Past Due but not Impaired	Impaired Loans		Allowance for Impairment	Total
As at 31 December 16			Specific	General		
Loans to Banks	984	-	-	-	-	984
Corporate loans	2,781	-	6	-	(11)	2,776
Other loans	1,700	-	-	-	-	1,700
Total	5,465	-	6	-	(11)	5,460
USD m	Neither Past due nor Impaired	Past Due but not Impaired	Impaired Loans		Allowance for Impairment	Total
As at 31 December 15			Specific	General		
Loans to Banks	936	-	-	-	-	936
Corporate loans	3,175	-	8	-	(12)	3,171
Other loans	1,509	2	-	-	-	1,511
Total	5,620	2	8	-	(12)	5,618

Table 14: Geographic distribution of impaired and past due exposures and allowance for impairment

USD m	Neither Past due nor Impaired	Past Due but not Impaired	Impaired Loans		Allowance for Impairment	Total
As at 31 December 16			Individually	Collectively		
Europe	1,277	-	-	-	(1)	1,276
South America	1,528	-	6	-	(8)	1,526
North America	642	-	-	-	(2)	640
Central America and Caribbean	1,954	-	-	-	-	1,954
Other countries	64	-	-	-	-	64
Total	5,465	-	6	-	(11)	5,460

USD m	Neither Past due nor Impaired	Past Due but not Impaired	Impaired Loans		Allowance for Impairment	Total
As at 31 December 15			Individually	Collectively		
Europe	1,666	-	-	-	(2)	1,664
South America	2,163	1	8	-	(10)	2,162
North America	634	-	-	-	-	634
Central America and Caribbean	1,083	1	-	-	-	1,084
Other countries	74	-	-	-	-	74
Total	5,620	2	8	-	(12)	5,618

The following table describes the movement on impairment during the past two exercises.

Table 15: Movement on impairment and the amounts taken against profit and loss

USD m	31.12.16	31.12.15
	Allowance for Impairment	
Starting Period	(12)	(12)
Exchange and other adjustments	-	1
Amounts written off	-	-
Amounts charged against profit	1	(1)
Ending Period	(11)	(12)

The following table shows the impairment allowance by exposure class as of December 2016.

Table 16: Analysis of impairment allowance by exposure class

USD m	Impairment
Regulatory impairment allowance	
Standardised approach	
Central governments or central banks	-
Institutions	-
Corporates	(5)
Retail	-
Secured by mortgages on immovable property	-
Exposures in default	(6)
Equity exposures	-
Other items	-
Total as at 31 December 16	(11)
Standardised approach	
Central governments or central banks	-
Institutions	-
Corporates	(4)
Retail	-
Secured by mortgages on immovable property	-
Exposures in default	(8)
Equity exposures	-
Other items	-
Total as at 31 December 15	(12)

Analysis of Counterparty Credit Risk

COUNTERPARTY CREDIT RISK EXPOSURE

The IEI Group calculates Counterparty Credit Risk ("CCR") using the MtM method.

Under the MtM method, exposures are subject to appropriate netting and collateral offsets and require adjustment for market driven movements that may lead to increased replacement cost at the time of default (potential future credit exposure).

The following table shows counterparty credit risk for derivative exposures.

Table 17: Counterparty credit exposure

USD m Mark to Market Method Net derivative credit exposure	Gross Positive Fair Value of Contracts	Potential Future Credit Exposure	Netting Benefits	Net Current Credit Exposure	Collateral Held	Net Derivatives Credit Exposure
Counterparty Credit Risk	138	248	(227)	159	(33)	126
Total as at 31 December 16	138	248	(227)	159	(33)	126
Counterparty Credit Risk	224	324	(339)	209	(42)	167
Total as at 31 December 15	224	324	(339)	209	(42)	167

CREDIT DERIVATIVE NOTIONALS

The table below shows the notional values of credit derivatives, credit default swaps (“CDS”) and total return swaps (“TRS”), of own credit portfolio. With regards to intermediation activities, the IEI Group currently does not engage in such activities, all credit derivatives are entered into for hedging purposes and are part of the IEI Group’s own Credit Portfolio.

Table 18: Notional amounts of credit derivative transactions

USD m Credit derivative product type	Own Credit Portfolio		
	Protection bought	Protection sold	Total
Credit Default Swaps	40	781	821
Total Return Swaps	4	-	4
Total as at 31 December 16	44	781	825
Credit Default Swaps	62	997	1,059
Total Return Swaps	6	-	6
Total as at 31 December 15	68	997	1,065

The Credit Derivatives used for managing the banking book decreased USD 216m as protection seller. Such decrease was in line with the shrink of structured notes issuances. Note 20 to the IEI Consolidated Annual Report 2016 provides additional information and disclosure regarding structured notes issuances.

Analysis of Market Risk

CAPITAL REQUIREMENTS FOR MARKET RISK

The IEI Group holds capital for the market risk arising from exposures classified as trading for regulatory purposes. Such capital allocation is calculated according to the standardised approach.

The table below breaks down the elements of capital requirements and RWAs under the market risk framework set out in the CRR.

Table 19: RWAs and capital requirements for market risk

USD m	Risk weighted	Capital requirements
Market risk		
Interest rate PRR	25	2
Foreign currency PRR	75	6
Total as at 31 December 16	100	8
Market risk		
Interest rate PRR	25	2
Foreign currency PRR	13	1
Total as at 31 December 15	38	3

CREDIT VALUATION ADJUSTMENT

The CRR introduced a new regulatory capital charge to cover the risk of mark-to-market losses on expected counterparty risk to derivatives: Credit Valuation Adjustment (CVA).

The CVA measures the risk from MtM losses due to deterioration in the credit quality of a counterparty to over-the-counter derivative transactions. It is a complement to the counterparty credit risk charge that accounts for the risk of outright default of a counterparty.

Table 20: Credit valuation adjustment capital charge

USD m	EAD post-CRM	Risk weighted	Capital requirements
Standardised CVA capital charge			
CVA capital charge	44	13	1
Total as at 31 December 16	44	13	1
Standardised CVA capital charge			
CVA capital charge	59	25	2
Total as at 31 December 15	59	25	2

Analysis of Operational Risk

The operational risk requirement under Pillar 1 is calculated using the Basic Indicator Approach. This uses a proxy of 15% of the average of the three year net interest income and net non-interest income to calculate a capital charge for operational risk.

The following table details the IEI Group's operational risk RWAs.

Table 21: Risk weighted assets for operational risk

USD m	31.12.16	31.12.15
	Risk weighted assets	
Operational risk		
Basic indicator approach	422	413
Total	422	413

Analysis of Countercyclical Capital Buffer

CRD IV as implemented in the UK includes a transitional period, during which the Financial Policy Committee (“FPC”) is responsible for deciding whether countercyclical capital buffer (“CCyB”) rates set by EEA States should be recognised and for taking certain decisions about third country rates, including whether a higher rate should be set for the purposes of UK institutions calculating their CCyB.

In March 2016 the FPC announced an increase of the countercyclical capital buffer (“CCyB”) for the UK to 0,5%, but in July 2016 the FPC over-ruled this announcement deciding to maintain the 0% CCyB for UK exposures.

The following table discloses relevant information for the calculation of the countercyclical buffer.

Table 22: Geographical distribution of credit exposures relevant for the calculation of the CCyB

USD m	General credit exposures	Trading book exposures		Own funds requirements				Own funds requirements weights	Countercyclical capital buffer rate
	Exposure value for SA	Sum of long and short positions of trading book exposures for SA	Value of trading book exposures for internal models	of which: General credit exposures	of which: Trading book exposures	of which: Securitisation exposures	Total		
Breakdown by country:									
Norway	10,000	-	-	800	-	-	800	0.02	1.5%
Sweden	13,186	-	-	1,055	-	-	1,055	0.04	1.5%
Hong Kong	-	-	-	-	-	-	-	-	0.625%
Total	23,186	-	-	1,855	-	-	1,855	0.06	

Table 23: Amount of institution-specific CCyB

USD m	Amount
Total risk exposure amount	5,522,673
Institution specific countercyclical capital buffer rate	0.006%
Institution specific countercyclical capital buffer requirement	348

Analysis of Leverage Ratio

The leverage ratio calculation below uses the end-point CRR definition of Tier 1 capital for the numerator and the CRR definition of leverage exposure. The reduction in the balance sheet drove the improvement in the leverage ratio during the period.

Table 24: Leverage Ratio

USD m	31.12.16	31.12.15
Leverage exposure		
Securities financing transactions (SFTs)	208	-
Derivatives	348	690
Off-balance sheet items	570	621
Others assets	7,217	8,101
Asset amount deducted - Tier 1 capital - fully loaded definition	(75)	(79)
Total leverage exposures	8,269	9,333
Fully loaded Tier 1 capital	999	953
Fully loaded leverage ratio	12.08%	10.21%

9. Remuneration disclosures

Decision-making process for determining the Remuneration Policy

The Board, upon the advice of the R&N Committee,⁴ is responsible for approving a Remuneration Policy for the Bank.

Remuneration Policy

The Remuneration Policy aims to ensure consistency with the human resources management policies of Itaú Group, as well as alignment to, and compliance with, the remuneration requirements, to the extent applicable, of the UK Remuneration Code set out in Chapter 19D of the Financial Conduct Authority's Senior Management Arrangements, Systems and Controls Sourcebook ("SYSC 19D Remuneration Code") and the Remuneration Part of the Prudential Regulation Authority's Rulebook (the "PRA Remuneration Code", and together with the SYSC 19D Remuneration Code, the "UK Remuneration Codes") and the related guidance issued by the Financial Conduct Authority and the Prudential Regulation Authority. For the purposes of the UK Remuneration Code, the Bank is a proportionality level three firm.

The general objectives of this policy are:

- a) to foster an organisational culture based on merit, as translated by a focus on performance (sustainable results and growth), and reflecting uniform, consistent, measurable and balanced remuneration criteria;

⁴ See section 6 ("Governance arrangements") for further details on the R&N.

- b) to value individual performance and contribution to the Bank's global results, taking into account factors such as technical skills, initiative, differentiated performance, effort, commitment to ethical and human values, accountability in compliance with the adopted risk management policy, the rules applicable to the activity and loyalty in the pursuance of the Bank's long-term interests;
- c) to enable the attraction, retention and loyalty of talent with high potential to contribute towards the achievement of the Bank's objectives, across the various functions to be achieved through the offer of a competitive remuneration package that takes into account the practices in the reference markets where the Bank's business activities are developed.

In addition to these general objectives, the policy also aims to ensure appropriate compliance with the applicable rules and guidance. In applying these principles and in establishing this policy, the Bank takes due consideration of its size, internal organisation and the nature, scope and complexity of its activities (the proportionality principle).

Remuneration of the members of the Board other than the Executive Directors

The remuneration of the non-executive members of the Board, as applicable, consists of fixed remuneration only, subject to the below, the amount of which is determined taking into account market and Group practices so as to ensure that it is consistent with normal remuneration levels for similar functions.

The Group non-executive members of the Board may not be remunerated for their functions in the Bank.

The remuneration of non-executive directors shall be determined by the Chairman and the CEO. No director shall be involved in any decisions as to their own remuneration.

Remuneration of the Executive Directors

Fixed remuneration

Fixed remuneration will primarily reflect the Executive Director's professional experience and organisational responsibilities. The level of fixed remuneration shall be sufficient to allow the operation of a fully flexible policy on variable remuneration components, including the possibility to pay no variable remuneration either to all the Executive Directors - due to the insufficiency or unsustainability of the results obtained - or to individual Executive Directors who, after being subject to the respective performance assessment processes, are found not to have made an adequate contribution.

The Executive Directors are eligible for similar benefits to those granted to the Bank's other employees (including health insurance, pension and life assurance) in accordance with the Bank's policy and the rules of the relevant benefit schemes in force from time to time.

Variable remuneration

The Executive Directors may be eligible to receive discretionary variable remuneration which shall take into consideration the added value or overall contribution to the Group.

Link between pay and performance

The variable remuneration of the Executive Directors is subject to an assessment of their individual performance and takes into account quantitative and qualitative factors as follows:

- a) leadership capacity;
- b) sound and prudent management;
- c) the achievement of financial results and non-financial objectives, namely through a long-term vision aligned to the interests of the shareholders; and
- d) compliance with the regulations applicable to the Bank's activity, implementation of recommendations issued by the control functions (Risk Management, Compliance and Internal Audit) and adherence to the high ethical standards and culture of the Group.

Risk and performance adjustments

The determination of individual variable remuneration awards shall not be based solely on the assessment of individual performance but shall also take into account any relevant current and future risks. Where appropriate this may lead to awards being reduced, including to nil, to properly reflect risks and/or to reflect subdued or negative financial performance of the Bank, the Bank's consolidation group or the relevant business unit.

The Risk, Compliance and Audit functions shall each report on any risk failings and any current and future risks, at the level of the Bank, the Bank's consolidation group, the relevant business unit or the employee, and any such reports of risk failings or risks shall be taken into account in the assessment of individual performance and/or the determination of individual variable remuneration awards as referred to above.

In determining any discretionary awards of variable remuneration, account will be taken of any current and future risks facing the Bank, including taking into account the cost and quantity of the Bank's capital and liquidity requirements. Where appropriate, this may lead to awards being reduced including, if necessary, to nil, to properly reflect risks and/or to reflect subdued or negative performance of the Bank.

Variable remuneration shall not be awarded to the extent that any such award would materially affect the Bank's solvency ratio or in any way jeopardise the continuity and sustainability of the Bank's future activity and/or lead to a breach of the Bank's capital or liquidity requirements.

Remuneration of employees – design and structure

Fixed remuneration shall reflect an individual's role, experience and technical skills, and will also take account of market practice and the need to recruit, develop and retain talent. Benefits may include health insurance for the employees and their dependents, pension and life assurance, in accordance with the Bank's policy and the rules of the relevant benefit schemes in force from time to time

The level of fixed remuneration shall be sufficient so as to allow the operation of a fully flexible policy on variable remuneration, including the possibility to pay no variable remuneration either to all the Bank's employees - due to the insufficiency or unsustainability of the results obtained - or to individual employees who, after being subject to the respective performance assessment processes, are found not to have made an adequate contribution.

Employees may also be eligible for the payment of wholly discretionary variable remuneration, which is conditional upon the Bank and/or the area of activity in which the employee is engaged achieving adequate and sustainable results, and also upon the performance and individual contribution of the employee to the achievement of those results.

Individual performance of employees is assessed in accordance with methodologies established by the Bank, with the input of the Head of Human Resources, and approved by the Executive Committee, and may vary depending on the area of activity in which the employee is engaged.

The general objective of the assessment processes is to determine differentiation of performance and contribution based on merit, understood as the achievement of results and the manifestation of skills that strengthen the Bank's and the Group's culture.

For the assessment of the functional groups engaged in business execution and risk-taking, the performance indicators will be primarily of an economic and financial nature, based on an adequate weighting of the global results and the results more directly linked to the respective department units.

As regards the remaining activities, namely control and support activities, the factors to be taken into account will be mainly linked to the quality and effectiveness of controls, the meeting of deadlines, innovation, and the improvement and efficiency of processes generating value for the businesses. The financial results considered in the assessment of employees in control and operational support areas should be the global results only and their assessment should not depend on the individual results of the areas which they control or to which they provide technical and operational support.

Manner and conditions of payment of variable remuneration

For the purposes of the UK Remuneration Codes, the Bank is a proportionality level three firm. As such, the Bank is able to disapply some of the provisions of the UK Remuneration Codes, such as the requirement to defer vesting of minimum portions of variable remuneration and payment in financial instruments. Notwithstanding that, the Remuneration Policy provides for deferral arrangements, as well as payment in financial instruments, as further explained below.

Once the amount of the variable remuneration to be attributed to each Executive Director or employee has been determined and approved, its payment shall be made in accordance with the following rules and conditions:

Any variable remuneration of staff whose corporate title is Managing Director or above is paid:

- 50% upfront in cash; and
- 50% in the form of an instrument on deferred terms, the value of which is linked to the value of the preference shares of Itaú Unibanco Holding S.A., consisting of three tranches, each representing one third of the amount of variable remuneration deferred.

A proportion of the variable remuneration of the remaining staff whose total cash remuneration is in excess of certain thresholds will also be deferred over 3 years. The amount of the variable remuneration to be deferred will be proportional to the level of total remuneration and the area in which the employee is engaged, and may reach up to 50% (fifty percent) of the variable remuneration awarded.

Conditions leading to the non-payment, reduction or suspension of the deferred variable remuneration, either in cash or in instruments

The variable component of remuneration shall not be paid or may be reduced or suspended.

In the event that the Bank determines, at its absolute discretion, that the payment of any deferred variable remuneration is not sustainable according to the financial situation of the Itaú Group, the Bank consolidation group (the "Consolidation Group") and/or the Bank, or is not justified on the basis of the performance of any of the Itaú Group, the Consolidation Group, the Bank, the relevant business unit or the employee, the Bank may determine that the amount of any deferred variable remuneration that shall become payable may be reduced (including to nil).

Without limitation, the Bank's discretion to reduce (including to nil) the amount of any deferred variable remuneration may be exercised where the Bank determines that:

- a) the employee participated in, or was directly or indirectly responsible, for conduct (including by omission) which resulted in significant losses (including both direct financial losses and indirect losses, including without limitation, through reputational damage) to the Itaú Group, the Consolidation Group or the Bank;
- b) the employee failed to meet appropriate standards of fitness and propriety;
- c) there is reasonable evidence, at the Bank's discretion, that the employee committed an act or omission which constitutes misbehaviour or a material error;
- d) the Itaú Group, the Consolidation Group or the Bank, or any business unit in which the employee works, has suffered a material downturn in its financial performance; and/or
- e) the Itaú Group, the Consolidation Group or the Bank, or any business unit in which the employee works, has suffered a material failure of risk management.

Quantitative disclosures

The remuneration disclosure consists of remuneration awarded for 2016, including fixed remuneration and the upfront and deferred components of variable remuneration awarded for the year. Note 36 to the Annual Report 2016 provides additional information and disclosure regarding staff costs in 2016.

The disclosures apply to those categories of staff whose professional activities have a material impact on the Bank's risk profile, including senior managers and other material risk takers who are in lower levels of management below the Board of Directors and the Executive Committee. The material risk takers are collectively referred to as "Code Staff" and have been identified in accordance with the European Commission's technical standards with respect to criteria to identify material risk takers (Commission Delegated Regulation 604/2014) (the "European Technical Standards"). The number of individuals identified as Code Staff is 47.

Code Staff aggregate quantitative information on remuneration broken down by business area:

CIB: USD 10,987,901

IPB⁵: USD 14,983,068

Code staff aggregate quantitative information on remuneration, broken down by senior management and Code Staff:

Senior managers: USD 9,428,572

Other Code Staff: USD 16,542,397

10. Basis and frequency of disclosures

In accordance with FCA and PRA requirements, IEI will publish Pillar 3 disclosures at least annually. The disclosures are published on www.itausaeuropa.eu.

⁵ Due to the timing of the IPB's grant process, certain variable remuneration awards that may be made to certain Code Staff of the IPB (who are Senior Management and Staff) have not been made by the date of the disclosure, the maximum value of that additional variable remuneration that could be awarded would be USD 1,943,047.

Appendix A – Disclosure on asset encumbrance

Asset encumbrance arises from collateral pledged against secured funding and other collateralised obligations.

USD m					
Template A – Assets		Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of non-encumbered assets	Fair value of non-encumbered assets
		010	040	060	090
010	Assets of the reporting institution	624		7,038	
030	Equity instruments	-	-	15	15
040	Debt securities	79	79	870	870
120	Other assets	-		394	

USD m			
Template B – Collateral received		Fair value of encumbered collateral received or own debt securities issued	Fair value of collateral received or own debt securities issued available for encumbrance
		010	040
130	Collateral received by the reporting institution	-	1,750
150	Equity instruments	-	-
160	Debt securities	-	-
230	Other collateral received	-	-
240	Own debt securities issued other than own covered bonds or ABSs	-	-

USD m			
Template C – Encumbered assets/collateral received and associated liabilities		Matching liabilities, contingent liabilities or securities lent	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered
		010	030
010	Carrying amount of selected financial liabilities	288	353