ANNUAL REPORT & FINANCIAL STATEMENTS 2018

APS bank

MISSION STATEMENT

TO BE THE COMMUNITY BANK IN MALTA BY MAKING THE BANKING EXPERIENCE SIMPLER AND MORE PERSONAL, INSPIRED BY OUR COMMITMENT TO SOCIAL, ECONOMIC AND ENVIRONMENTAL PROGRESS, WHILE PROVIDING OUR STAKEHOLDERS WITH OPPORTUNITIES TO GROW.

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BANK INFORMATION

DIRECTORS

Frederick Mifsud Bonnici, Chairman
Victor E. Agius (Appointed on 15 October 2018)
Joseph C. Attard (Appointed on 26 July 2018)
Franco Azzopardi
Laragh Cassar
Alfred DeMarco
Arthur Galea Salomone (Resigned on 26 July 2018)
Victor Gusman
Frederick F. Micallef (Resigned on 26 July 2018)
Michael Pace Ross
Martin Scicluna

COMPANY SECRETARY

Mario Felice (Resigned on 1 July 2018)
Graziella Bray (Appointed on 1 July 2018)

REGISTERED OFFICE

APS Bank plc
APS Centre
Tower Street
Birkirkara, BKR 4012
Malta

Registration Number: C2192

WEBSITE

www.apsbank.com.mt

SENIOR MANAGEMENT

Marcel Cassar, Chief Executive Officer
(EXCO[1], MANCO[1], MCC[1], BCC[2], TIC[2], CC[2], ALCO[2], *RC[2], GCC[2], RMC[2]*)

Giovanni Bartolotta, Chief Risk Officer
(CC[1], EXCO[2], MANCO[2], ALCO[2], MCC[2], *RC[2], BCC[2]*)

Jonathan Caruana, Chief Technology Officer
(TIC[2], EXCO[2], MANCO[2])

Hervé Delpech, Chief Strategy Officer
(TIC[2], EXCO[2], MANCO[2], *GCC[2]*)
with effect from 1 April 2019, previously Head of Strategy & Marketing

Noel McCarthy, Chief Financial Officer
(BCC[2], TIC[2], EXCO[2], MANCO[2], ALCO[2], MCC[2], *RC[2]*)

Wilhelm Attard, Head of Operations
(MANCO[2])

Raymond Bonnici, Head of Human Capital
(EXCO[2], MANCO[2], *RMC[2]*)

Anthony Buttigieg, Head of Banking
(EXCO[2], MANCO[2], CC[2], MCC[2], *BCC[2]*)

Edward Calleja, Head of Risk
(MANCO[2], ALCO[2], *MCC[2], RC[2], BCC[2]*)

Alexander Camilleri, Head of Support
(MANCO[2])

Joseph Farrugia, Head of Compliance
(MANCO[2], CC[2])

Marvin Farrugia, Head of Asset-Liability Management
(ALCO[1], MANCO[2])

Nives Grixti, Head of Legal
(EXCO[2], MANCO[2], *MCC[2], GCC[2]*)

Josef Portelli, Head of Investment Management
(MANCO[2], ALCO[2], *RC[2]*)

Richard Scerri, Head of Internal Audit

[1] Denotes Committee chairmanship.

[2] Denotes Committee memberships (non-voting is shown in italics).

Board Credit Committee (BCC), Governance and Conduct Committee (GCC), Remuneration Committee (RMC), Risk Committee (RC), Technology and Innovation Committee (TIC), Executive Committee (EXCO), Management Committee (MANCO), Compliance Committee (CC), Assets-Liabilities Committee (ALCO), Management Credit Committee (MCC).

Other Management members, not listed above, sit on the Management Credit Committee, Compliance Committee and Assets-Liabilities Committee.

BOARD OF DIRECTORS

1. FREDERICK MIFSUD BONNICI

Chairman and Non-Executive Director (GCC[1], RMC[1])

Mr Mifsud Bonnici was appointed Chairman of APS Bank Limited in 2017. Mr Mifsud Bonnici spent over 42 years with PricewaterhouseCoopers. He is a non-executive director of De Raekt Malta Holdings Limited and De Raekt Malta Investments Malta Limited. He is Chairman of the Malta Airport Foundation as well as non-executive Director and Chairman of Blevins Franks Trustees Limited and Blevins Franks Gamma Limited. He is a Fellow of the Institute of Chartered Accountants in England & Wales and a Certified Public Accountant. He has also been a senior lecturer at the University of Malta for 30 years.

2. VICTOR E. AGIUS

Non-Executive Director (BCC[1], RC[2])

Mr Agius was appointed to the Board in 2018 after a diverse career in international investment, banking and development project finance. This included 23 years at the World Bank Group in Washington DC, over three years with the EBRD and 17 years with the Council of Europe Development Bank in London. His work comprised extensive field mission leadership responsibilities to over sixty countries in Africa, East Asia, MENA, Europe and of the Former Soviet Union. Mr Agius graduated with a BA Hons. (Economics) from the Royal University of Malta, an MBA from Manchester Business School and completed Senior Executive Finance and Banking programs at the Wharton School of Finance and at the Stanford Graduate School of Business.

3. JOSEPH C. ATTARD

Non-Executive Director (TIC[1], RC[2], BCC[2])

Dr Ing. Attard was appointed on the Board in 2018. He has over 25 years of local and international experience in the Information and Communication Technology (ICT) sector. He is currently the Chief Technical Officer of GO plc. Between 2007 and 2015 he was the Chief Technology Officer of Emirates International Telecommunications LLC. Amid 1997 and 2007, he held senior positions at Maltacom plc. Dr Ing. Attard holds a B.Elec.Eng.(Hons) degree from the University of Malta, an MSc (in Operational Telecommunications) from the University of Coventry (U.K) and a Ph.D. (in Telecommunications Engineering) from University College London (U.K.). Since 2002 he has regularly lectured at University College London on ICT related topics.

4. FRANCO AZZOPARDI

Non-Executive Director (AC[1], RC[2], TIC[2])

Mr Azzopardi was appointed to the Board in 2008. He is a professional director and a registered fellow member of the UK Institute of Directors. He serves on the Boards of Directors; Audit and Risk Committees of both listed and private companies in various sectors including banking, insurance, software and logistics. He is CEO of the leading logistics company in Malta. He previously spent 27 years working in public practice, ten of which with Deloitte Haskins and Sells, and later in a firm he co-founded in 1990. He holds an MSc degree in Finance from the University of Leicester (UK) and is a fellow member of Malta Institute of Accountants, serving on the Council since 2007. He was also elected and served as President of the Institute for the term 2015-2017.

5. LARAGH CASSAR

Non-Executive Director (GCC[2], RMC[2], TIC[2])

Dr Cassar was appointed to the Board in 2016. Throughout her career, Laragh has gained vast experience in many areas of practice including banking, investment services, asset management, capital markets and corporate law restructuring. She commenced her professional career as an advocate in 2003 having joined Camilleri Preziosi as an associate. She was admitted to partnership in 2009, where she held this position until 2015 when she founded the firm 'Camilleri Cassar Advocates'. She is often appointed by the Faculty of Laws of the University of Malta to supervise and examine LLD and MA Financial Services thesis. Dr Cassar obtained a degree in law from the University of Malta in 2002 and a Master of law in Banking and Finance from the University of London in 2003.

6. ALFRED DEMARCO

Non-Executive Director (RC[2], BCC[2])

Mr DeMarco was appointed to the Board in May 2016. He is an associate of the Institute of Financial Services, London (ACIB) and holds a degree in economics from the University of London. He is a central banker by profession with more than forty years' experience at the Central Bank of Malta (CBM). He progressed through senior executive positions at the Bank including that of Director of the Economics and External Relations Division. He was appointed Deputy Governor in April 2010, a position he held until end-March 2015.

7. VICTOR GUSMAN

Non-Executive Director (GCC[2], RMC[2], TIC[2])

Mr Gusman was appointed to the Board in 2012. He is currently the Administrative Secretary of the Diocese of Gozo. During the 35 years at the helm of the Lemco Group, he led the administration team of a workforce of over 650 with manufacturing basis in Italy and Poland and a sales force operating in 34 countries. He gained experience in dealing with a workforce composed of various nationalities, servicing international companies with custom made products to accommodate their own products and brands. He was central in dealing with Government Departments for the supply of specialised requirements in their Hardware and manufacturing sectors, negotiating with Unions in Italy and Poland.

8. MICHAEL PACE ROSS

Non-Executive Director (AC[2], GCC[2])

Mr Pace Ross was appointed to the Board in 2015. He is currently the Administrative Secretary of the Archdiocese of Malta, following his appointment by Archbishop Charles J. Scicluna. He previously served as Director General of the National Statistics Office for six years, sitting on a number of national and European committees, including the European Statistical Advisory Committee (ESAC). Mr Pace Ross is a Council member of the Malta Employers Association (MEA). He is also a Board member on the Voluntary Solidarity Fund, a charity which embraces core values inspired by and aligned with the Catholic social teachings on solidarity. Mr Pace Ross also sits on the Board of a listed company.

9. MARTIN SCICLUNA

Non-Executive Director (RC[1], AC[2])

Mr Scicluna was appointed to the Board in 2013. Since 2012, he has held a number of directorship appointments in banking, asset management and insurance companies licenced in Malta. He started his banking career with Mid-Med Bank in 1976. In 1996, he joined Midland Bank, which later became HSBC Bank Malta plc., where he held various senior executive posts. Latterly, as Head of Premier and Wealth Management, his responsibilities comprised all investment advisory and regulated product sales distribution. He also served on several boards for HSBC Malta subsidiaries and on the bank's Audit Committee. Mr Scicluna is an Associate of the Chartered Institute of Bankers, holds a Diploma in Financial Studies and was elected as a Fellow of the Institute of Financial Services in 1999.

[1] Denotes Board Committee chairmanship.
[2] Denotes Board Committee memberships.
Board Committees: Audit Committee (AC), Board Credit Committee (BCC), Governance and Conduct Committee (GCC), Remuneration Committee (RMC), Risk Committee (RC), Technology and Innovation Committee (TIC)


APS bank

CHAIRMAN'S STATEMENT

CHAIRMAN'S STATEMENT

2018 has been a challenging year for the local banking sector. A continuing low interest rate regime, a strong competitive environment, an ever increasing regulatory burden and a whole range of issues relating to human resources, ranging from recruitment of skilled and experienced personnel to training and staff retention, present a formidable list of challenges to any management body both in its supervisory and management functions. All this coupled with the objective of strengthening and promoting the Bank to retain existing customers and as an attractive alternative to potential new customers, and to meet future challenges and growth made it even tougher. In this huge task, I believe the Bank's senior management ably led by the Chief Executive Officer have done a remarkable job. The figures speak for themselves as amply explained in the CEO's review.

It must also be said that the costs of compliance with new and changing regulation are increasing unrelentingly. No doubt regulation has many benefits and beneficiaries, however, to be effective and efficient, a regulatory regime and detailed regulations need to be developed in the context of constant and regular constructive dialogue between the regulator and the regulated. The current review of the main regulator in financial services is welcome. No doubt attention will be given to recommendations made by international bodies to improve on our current performance. Certainly, appropriate dialogue will result in more effective compliance than as at present. I would like here to address briefly the issue related to customer on-boarding. A regulated entity has to take cognisance of AML and CFT regulations promulgated by the regulator, its own risk appetite, the standards and risk appetite of the international banks it deals with on behalf of its customers and, last but not least, the effect that all this has on the customer who is only interested in getting on with his transactions. I believe most of these issues can be addressed more effectively if there is a better dialogue between regulators and regulated.

Bank Performance

Malta's economy remained buoyant with an enviable growth rate, driven particularly by the property and tourist sectors; the former, no doubt, also spurred by the Gaming industry. These conditions helped APS Bank achieve and exceed its operational targets. Our lending portfolio grew by 28% compared with last year resulting in an increase in market share. This has been complemented by our success in sourcing new deposits including from outside the country at competitive rates. Furthermore, our cost to income ratio increased only marginally which is very satisfactory considering the pressures outlined already, i.e. increasing salaries and compliance costs, and the ambitious programme we have embarked on to improve the Bank, particularly with regard to the customer experience.

At the end of the year, a new three-year Business Plan covering the period 2019-2021 was approved encompassing an emphasis on customer centricity, the development of Human Resources, process re-engineering, digitalisation, the strengthening of the Risk and related control functions and various upgrades to the IT infrastructure. The strong financial position of the Bank at 31 December 2018 is a good starting point for the implementation of the new Business Plan and gives us the confidence to meet future challenges. The Plan also includes a capital development programme to ensure that the Bank remains well capitalised and comfortably above the required statutory capital ratios.

The dividend for the year is also being increased, reflecting the improved performance and to align it better with expected investor considerations.

The Board

During the year, two new directors were appointed replacing Dr Arthur Galea Salomone and Mr Frederick Micallef, who had served the Bank with loyalty, expertise and strong commitment for many years. I especially thank them for their notable contribution to the Bank. I welcome the new Board members: Mr Victor Agius and Dr. Ing. Joseph Attard. Victor Agius, an international economist with qualifications in Financial Management of Banking Institutions, has over 40 years' senior credit experience at the World Bank, EBRD and the Council of Europe Development Bank, including at principal and director levels. Dr. Ing. Attard is a Telecommunications, IT and Media specialist and is currently Chief Technical Officer with GO plc. Since joining the Board, they have already contributed significantly in their areas of expertise.

The Board aspires to observe the highest standards of ethical conduct and integrity and has ensured that such high standards have been incorporated in the three-year Strategy and Business Plan for the entire Bank.

Looking ahead

The recent decision by the ECB to offer again cheap loans to Eurozone banks, signalling that it would keep interest rates at historic lows until next year, suggests a perception of mounting risks to the global economy. Malta has in recent years managed to avoid the extremes of the global experience and therefore, perhaps, one need not be unduly concerned. However, if there is a pullback arising from such uncertainties as Brexit, trade wars and a slowdown in China, some impact on tourism and financial services may be expected. One also needs to comment on the practical consequences of the deterioration of Malta's reputation internationally which, in a globalised economy, will not turn away unless quick and drastic action is taken. Furthermore, the expected completion of substantial property developments over the next year or two may dampen some of the growth drivers of the recent past, in terms of speed of growth in property rentals and sales.

We expect some of our more important customer–oriented IT projects to be completed during 2019, helping to enhance the Bank's competitive offering. Today, we have a highly-dedicated, well-qualified and experienced workforce, sharpening our commitment to improve our service levels to our loyal customer base. This places APS Bank in a position to ensure that its performance in 2019 will again be satisfactory.

Finally, on behalf of my fellow directors, I wish to thank the shareholders of the Bank for their continued, constant support throughout the year.

F. Mifsud Bonnici
Chairman

21 March 2019

CEO'S REVIEW

In last year's Annual Report I concluded my Review by listing five areas that I had singled out for special focus during 2018, namely:

1. **Improving the quality and diversification of the income statement in an environment with continued pressure on spreads;**
2. **Gaining further market share on a sustained basis, as our base of relationships and product range continues to widen;**
3. **Continuing the transformation at various levels, organisational, network and processes, without affecting the efficiency ratio and optimising on costs;**
4. **Improving further governance, risk and compliance infrastructure, particularly in the face of regulatory and accounting game-changers like IFRS 9, PSD 2, MIFID 2 and GDPR; and**
5. **Above all, producing a bold and visionary 2019-2021 Business Strategy which will also embrace the capital planning required to scale the Bank up to the next level.**

So it is appropriate that my Review this year should cover these areas which between them capture the intense rhythm and scale of activity that is taking place at APS Bank. The Review is an opportunity to present a clear and fairly detailed point of view about what we've been doing, the things we believe really matter and what we think it all means for our business. Whether the reader is a customer, a shareholder, an employee or a stakeholder in the broader community, it is an opportunity to transmit the strategy of the Bank, the actions that support the strategy and the successes and challenges that we experience.

First, it gives me once again great pleasure to report another year of record growth and profit. This was achieved thanks to sustained tailwinds from a strongly performing Maltese economy despite signs of slowdown elsewhere in Europe. The low interest rate environment continued to present challenges for banks to find acceptable returns in a highly dynamic risk landscape. Nevertheless, APS Bank's business model again delivered excellent results in a year characterised by the continuation of our transformation journey.

Income strategy: quality, diversification and performance

In an environment that continued to be marked by exceptionally low or negative interest rates, a year that can be described as a 'perfect storm' of increased regulatory obligations, a fast-moving risk panorama and pressures on costs, especially people, Malta was one of the best performing European players, in terms of growth, employment and budget management.

We are again pleased to report a record performance at both Group and Bank levels, with activity also reaching all-round record levels. Group Operating Income expanded by 4.6%, from €42.8 million to €44.7 million (Bank: by 6.3% to €45.7 million) and Pre-tax Profit increased by 1.5%, from €18.4 million to €18.6 million (Bank: by 7.7% to €19.7 million). This result was achieved on the back of continued growth in business momentum and heavy investment in people, technology, network transformation, functional and process reorganisation.

We are satisfied to note a strong performance in the main income constituents, namely Net Interest Income (up by 15.3% on 2017) and Fees and Commissions (up by 24.7%). Households and home finance remained the largest source of credit activity, however 2018 saw more diversification taking place towards commercial real estate and a growing book of overseas syndicated loan participations. Correspondingly, the Bank operated within very prudent Liquidity Coverage Ratios (LCR) of 143% and 197% during the year under review, substantially above the minimum regulatory requirement. Similarly, the Net Stable Funding Ratios (NSFR) ranged between 128% and 133%, also way over the regulatory minima. Our funding diversification strategy returned liquidity levels without necessarily compensating spreads – on the contrary, Central Bank of Malta and other bank balances continued to attract negative interest throughout the year under review.

Cost-Efficiency at 50.8% was higher than the 47.9% of 2017, as pressures on personnel, operating and compliance expenses are not expected to abate any time soon. It should be underlined that realised gains in excess of €2 million on the transfer of securities to form the APS Diversified Bond Fund in 2017 were not repeated in 2018. On the other hand, the Group results reflect a net, unrealised negative fair value movement in the performance of Bond Fund during the year under review.

Overall credit quality at Bank level continued to improve, with NPLs to Gross Loans reducing significantly from 4.2 % in 2017 to 3.8% in 2018. The stock of NPLs maintained a fair distribution across sectors, with Construction & Real Estate (38%) and Manufacturing (19%) being the main components. A prudent credit loss experience (ECL estimated at 12 bp for 2018) and sustained recovery efforts also resulted in lower net impairment provisions compared to the previous year.

The Group's ROE remained strong at 9.7% (2017: 10.9%) while Balance Sheet growth was robust, with total assets increasing by 26.4% to €1.89 billion. At 13.94% (Bank: 13.59%), the Group Total Capital ratio, consisting primarily of Tier 1 equity, is down from last year (16.53% and 15.99% for Group and Bank, respectively) yet still affording an adequate headroom above the regulatory minimum. As anticipated last year, a Capital Development Plan has now been formulated, discussions with our shareholders have taken place and the first phase of a Rights Issue is planned for the second quarter of 2019.

More numbers and statistics from the 2018 financial results can be found in the 'Financial Statements' section of the Annual Report. This Review is not meant to delve into performance indicators in more detail, however the message that these numbers transmit is that amidst a competitive and challenging environment, the Bank has been able to draw on its market strengths and maximise on the business and revenue opportunities that they offer.

Gaining market share and widening the product range

Growth in 2018 was spurred by deposit raising and lending activity which grew by 34.7% and 28.1% respectively over 2017. It is the Bank's strategy to increase its market share through strategic, selective business development through an operating model which continues to be centred around three main product segments, namely Personal, Business and Investments.

We are pleased to note that our liability management targets for 2018 were surpassed as we managed to attract a healthy mix of institutional and retail funds at a pace that was pretty consistently spread throughout the year. This included new product offerings, such as the 'Triple One Euro Term Deposit' as well as targeted products in US Dollar and Sterling. A new retail source also originated pursuant to the authorisation received from Bafin in May 2018 for the Bank to passport its services in Germany. Despite the record increase in deposits, funding remained highly diversified with no single relationship or source exceeding 4% of the base.

The Bank also continued to make inroads in commercial activity while maintaining our place as a favourite home loan institution in Malta, with 61.6% of the total loan portfolio remaining directed to individual and family home financing. APS Bank remains the household name for residential financing despite stiff competition in this segment. We are pleased to note that the Directive on Borrower-Based Measures due to be issued by the Central Bank of Malta later this year should be timely to address vulnerabilities that may be arising because of heating in the residential real estate market. The Bank has nevertheless remained a competitive albeit selective player in the financing of commercial and residential real estate developments, hotel and office accommodation, the markets for which continue to be particularly buoyant.

We have also continued to promote with interest eco-friendly and sustainable energy projects, as well as the education, health-care and retirement segments, including in partnership with other financial institutions. In 2018 we further strengthened our collaboration with the University of Malta by investing in a portable presence ('Green Space') on the Tal-Qroqq campus. Further initiatives of support to specific University faculties and departments also took place and more are planned for 2019. We continue to be actively interested in the opportunities we see in the personal lending segment and retirement and pensions solutions where we especially see a market gap. We await developments in legislation and regulation to take forward new products and schemes in this important market. Moreover, the agreements signed with the European Investment Fund in 2016 also supported the Bank in extending credit facilities to micro and small and medium-sized entities (MSMEs) and small mid-caps on funded as well as unfunded [the InnovFin SME Guarantee scheme (#investEU)] terms and at concessionary conditions.

In 2018 we continued to diversify our credit risk, particularly in terms of geography, industry and maturity. The small ticket activity of participations in short-term trade-related facilities, sourced from banks of good repute and experience in this area, was maintained. We also continued to expand our book of syndicated loan participations of medium term duration originated by quality international names, reaching €70 million in approved facilities (€62.4 million disbursed at end-2018) spread over sectors such as manufacturing, wholesale & retail, transport/communication, health and social work.

We are also proud to be maintaining our leading position as providers of social banking services, through a concessionary home loan scheme launched in April 2017 in collaboration with the Malta Government and social welfare agencies. Discussions are at an advanced stage to further support Government on other important initiatives, such as the re-launch of the Home Equity Sharing Scheme and an Affordable Housing Project. We are also collaborators of micro-credit schemes for the *Fondazzjoni Vittmi tal-Użura,* Malta Microfinance and Asylum Seekers and are working at improving our offering further in these areas. During the last quarter the Bank launched its Basic Payment Account, in line with the requirements of the Payment Accounts Regulations.

2018 also saw further work taking place on the reorganisation of the investment distribution and advisory service across the branch network, partly in preparation of more stringent requirements arising from the introduction of the MIFID 2 regulations. ReAPS Asset Management Limited, the wholly-owned investment management subsidiary which manages the APS Funds SICAV, was further organised during the year under review and a stronger management structure is now in place. A first-time 3-year business plan recently approved for ReAPS should see this outfit better realise its objectives as a manager of retail funds under the UCITS regime, promoting further the APS Group philosophy of encouraging savings through fair investment products offered to the community at large. We are confident that the strengthening of the Group's investment management capabilities, including in the risk and compliance functions, and the plans to introduce new products to the market, will deliver results in 2019.

Continuing the transformation

The year under review saw further results being achieved in the network transformation programme. After the successful roll-out of the new offices on Sliema Tower Road and Valletta Republic Street, which now also houses the Legal Contracts Unit on two of its floors, work was started and completed on the transformation of the Victoria, Gozo and Mosta offices. We are grateful to our staff for providing an uninterrupted service throughout the period of works, to our customers for their patience and understanding and to our contractors for the efficient turnaround. The final phase of the Mosta transformation is taking place in the first months of 2019 with a major upgrade to the façade. Once again the branch layouts – based on designs of UK-based international firm I-AM, which was entrusted with the transformation strategy of the branch network - are modern, create an innovative, contemporary experience for our customers and introduce more digital interaction and space for meetings. For 2019 we plan to transform our Swatar branch and to finish a new branch in Qormi, replacing the existing facilities which have been outgrown by the market demands.

We extended to take up further office footprint at the Swatar Head Office to accommodate the larger teams made up of permanent as well as project and temporary staff. A larger board-room and modern canteen and dining facilities for staff were finished early in the year under review. Further important projects are planned for the coming months, including new meeting rooms and a new, multi-purpose conference room/auditorium. Works on the new Central Document Repository and Archiving Building in Marsa are close to completion while proposals submitted for the Digitisation project, which will be complimenting it, have been evaluated and awarded.

As anticipated in last year's Review, in July the Bank switched on its new offsite data centre, designed to meet its growing system and business requirements besides serving as Disaster Recovery Centre. This leading-edge facility is aligned with international data centre best practices for security, ergonomics, redundancy and resiliency whilst respecting the environment. We are proud to note that construction and finishing work was overseen by the Bank's Support Department, who prepared the site with all required facilities to host the suite of servers – a complex project requiring meticulous planning, hard work, professionalism and dedication, as well as coordination from our esteemed technology partners.

Concurrently in the backrooms intense activity has been taking place to meet deadlines for the roll-out of our omni-channel solution in the summer of 2019, which will include mobile banking, an improved internet banking experience and other digital channels. The design and implementation of this major project, entrusted to NF Innova, part of New Frontier Group, is in testing stage and a soft 'family and friends' launch is taking place in March. We are confident and excited about the new experience that 'myAPS', as the solution will be branded, will deliver to our customers. We are also on schedule to finally start the roll-out of an enhanced cards offering later in 2019. Work on developing our PSD2/Open Banking platform is also progressing at a brisk pace, as are various other projects mandated by regulatory and compliance obligations. The list of projects is practically endless and overarching everything is the need to ensure that procedures are simplified and processes made as efficient as possible. Ultimately our aim is that of permitting customers to access our range of financial products and services from a variety of channels and through a more consistent interaction with our banking franchise across various touch points.

No transformation is possible without an engaged and motivated workforce. During the year under review there were increases in staff across all strata of the Bank, reflecting the strengthening of functions and positions as well as more business and growth. The professional job evaluation exercise concluded late in 2018 has helped to recognise better the job requirements and responsibilities, leading also to improved rewards for individual competences and experience.

As stated in past Reviews, we do not look at the higher payroll as an increase in overheads but as one of the choicest investments we can make. Our slogan 'Being the employer of choice' is the statement underscoring the belief that all our plans and ambitions depend on our ability to attract and retain the best talent and skills, while offering a well-defined vision, common culture and the best employment conditions. In 2018 we further refined the organisation structure, making it more modern and responsive to current trends while at the same time opening new paths for career progression. By widening further our horizons in search of the best talent, we are also making the Bank more international, enriching the overall fabric and culture of the Bank. We also continued to make available very generous programmes to promote staff engagement, including coaching, training and education opportunities, family-friendly work arrangements, schemes assisting with home and content financing and other rewards & incentives structures. The Undergraduate Work Placement scheme gained further momentum in 2018, various staff development and training programmes, local and overseas, are in place and e-learning facilities were stepped up. A Sports Committee was set up in addition to the Social Activities Committee, enriching the welfare calendar of staff and their families.

We firmly believe that our employees are our best resource and want to create for them a relationship that goes beyond employment, an environment based on the wholesome development of the self. We pride ourselves at offering an environment for our staff where high career ambitions and work-life balance both have a place.

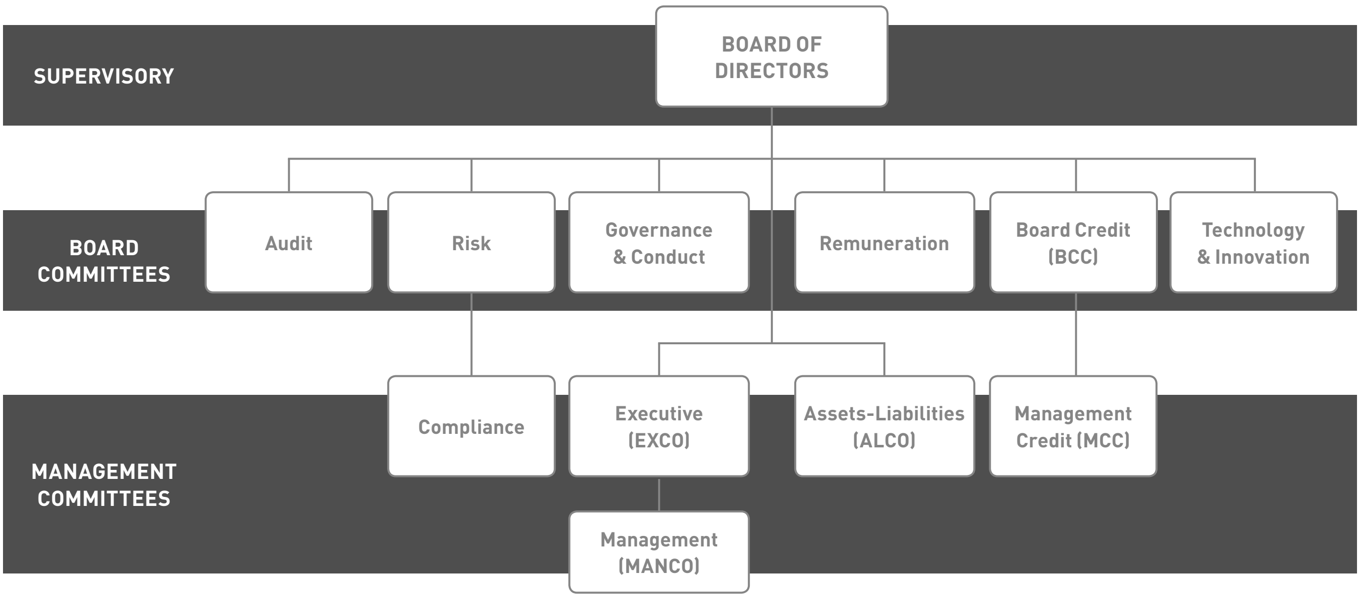
Once again, I cannot reiterate enough that APS Bank will remain a customer-friendly bank and our agenda for digital transformation will always be built around the value of human interaction to deliver a simpler, personal experience.

Strengthening the governance, risk and compliance infrastructure

Maltese banks, and APS Bank nonetheless, are not immune to the challenges facing our industry, arising from new technologies, increased regulation and evolving risk 'hotspots'. These are in turn changing customer behaviours and creating new competitive pressures, requiring us to respond by investing continuously in the governance framework as well as our various lines of defences, at the same remaining customer-centric in our business approach. 2018 was especially a demanding one, also because of regulatory and accounting overloads like IFRS 9, PSD 2, MIFID 2 and GDPR - just to mention some of the main game-changers. Strengthening of AML controls, risk assessment and KYC processes also continue to feature on the agenda, as Malta's financial system faces increased scrutiny from regulatory and supervisory bodies. These journeys call for expert and experienced staff, particularly at senior and professional levels which in a domestic environment of full employment further creates pressure on talent cost and availability.

2018 saw further reinforcement of the Bank's governance and organisation structure, with new functions, positions and reporting lines being set in place and emphasis made on strengthening the main control functions. Risk, Compliance, Audit and Legal departments were re-organised following senior appointments and additional human resources and tools being deployed. Even more importantly, we are conscious of the importance of imbuing a superlative risk culture across all lines of the Bank, bolstering, among others, our defences against cyber risk, hazards from financial and economic crime and operational and reputational risk. We believe that these measures are necessary to make sure that our business growth is always as safe as possible. We are also taking an opportunistic view to seek diversification whenever possible, which is important for the soundness of our business model.

In the third quarter the Board of Directors approved a structure of Board and Management committees which continued to improve on what was already a strong arrangement of Bank corporate governance. The new structure, which was accompanied by detailed terms of reference and composition requirements for each committee, is set out below:



Strategy 2019-2021

Early into the new year and wasting no time, the Bank's Strategy Department started working on the new 2019–2021 Business Plan which, from the word 'go', engaged various levels of the organisation, from the Board of Directors to more junior staff. Various meetings, including offsite events with external consultants, went into developing the Plan. The final product, the fruit of ten months of intensive market analysis, consultation and discussion, provides key strategic direction for the years ahead. APS Bank's renewed mission is to make the banking experience simpler and more personal, inspired by a commitment to social, economic and environmental progress while providing all stakeholders with opportunities to grow.

The vision is now captured by the simple slogan: 'to be the community Bank in Malta'. The process has also seen the Bank sharpening its core values, placing a focus on:

a) excellence, that is being outstanding of extremely good at what we do internally and externally, taking ownership and delivering the best which is what our customers deserve and expect;
b) authenticity, that is being true to one's own personality, spirit or character, understanding and trusting while acting always with integrity;
c) passion, showing eagerness for an idea, proposal or cause, bringing high energy levels into what we do, being inspiring by leading and caring;
d) inclusiveness, meaning that we welcome differences, respect diversity, actually leveraging on different perspectives and backgrounds, building on them for the good of all; and
e) contemporary, meaning that we need to be relevant to our time, in sync with the world, testing, learning, adopting and sharing – pushing the boundaries to make things better.

Going forward these beliefs will be anchored in every product and service that we provide and every channel we operate. Equally relevant, 'Strategy 2019-2021' continues to build on APS Bank's role as a leading Corporate Social Responsibility (CSR) player, as 2018 amply showed. Our support went to a large number of projects, such as: 'Time to care' photo competition, 'It pays to go green' sustainability campaign, various art and photographic exhibitions, the first Readathon organised by the National Literacy Agency and the President's Trust, the 'Schranz Family of Arts' exhibition at Fort St Elmo, support to a number of charitable foundations and campaigns and a vast programme of financial support to various projects in the arts, conservation and culture. The Bank was again the title sponsor of one of Malta's main theatre and music events in the calendar – APS Teatru Unplugged.

The full Plan, a document running into almost 200 pages, also contains the ambitions and financial targets for the coming years, which continue to anticipate opportunities for sustained growth, revenue generation and profit. Critical to the Plan is the Bank's ability to raise additional capital in order to support its future business requirements and it is again reassuring that active discussion is taking place on the 2018 - 2022 Capital Development Plan presented to the shareholders.

The next steps

Last year I gave a personal, contemporary interpretation of the 'APS' acronym, that of an 'Alternative, Progressive and Superior' organisation, forward-looking in its product range, market reach and governance standards. Becoming an increasingly important bank for the Maltese system places on us challenges as well as responsibilities – and our 2019-2021 Business Plan is the roadmap to deliver all that in the right balance. It is a Plan that belongs to all of us at APS and will only be effective to the extent that we make it our very known – but also communicating it to all our stakeholders.

So with a larger sense of responsibility comes the recognition that in these times of rapid and dynamic disruption in 'banking' as we knew it, we must embrace and promote change and must also play a role in addressing its broader consequences. The digital revolution is creating fantastic challenges but also opening up unprecedented avenues of opportunity. It is also radically altering the very nature of work. We see 2019 as a year of transition and consolidation for our transformation journey, leading to a more contemporary bank by 2020/2021. And in a world that increasingly places pressure on banks to serve their customers digitally, we continue to believe in a bank that remains personal and relevant for every one of our customers.

Sincerely,
Marcel Cassar

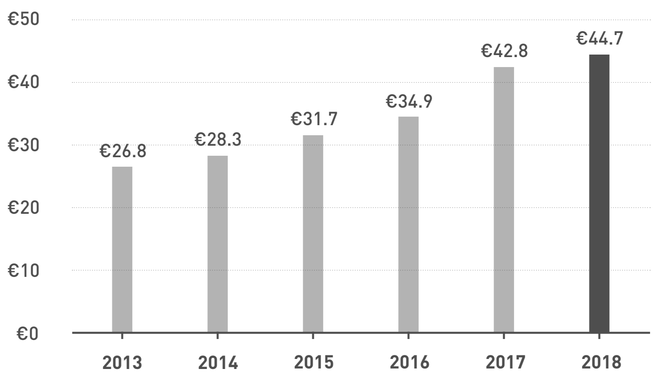

APS
bank

FINANCIAL STATEMENTS

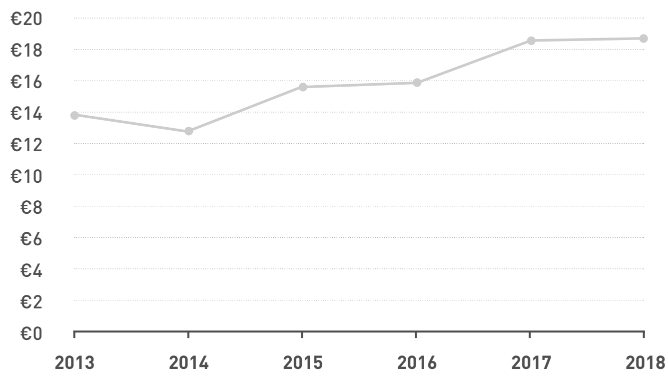
DIRECTORS' REPORT

The Directors present their report together with the audited financial statements of APS Bank Group and APS Bank Limited for the year ended 31 December 2018.

Group's Operating income (€million)



Group's Profit before Tax (€ million)



Principal Activities

APS Bank Group (the 'Group') comprises APS Bank Limited (the 'Bank'), its subsidiary ReAPS Asset Management Limited, and APS Funds SICAV p.l.c. which consists of three sub-funds: the APS Regular Income Ethical Fund and the APS Income Fund, both of which are associates of the Bank (the 'Associates'), and the APS Diversified Bond Fund being a subsidiary of the Bank.

The Bank is incorporated as a private limited liability company under the Companies Act (Cap. 386 of the Laws of Malta). It is licensed by the Malta Financial Services Authority (the 'MFSA') to carry out the business of banking and investment services in terms of the Banking Act (Cap. 371 of the Laws of Malta) and the Investment Services Act (Cap. 370 of the Laws of Malta) respectively. The Bank is also enrolled in the Tied Insurance Intermediaries List in terms of the Insurance Intermediaries Act (Cap. 487 of the Laws of Malta).

Over the years, the Bank has established itself to be one of the leading service providers in the financial services industry, employing an average of 372 employees and functioning through a strategic and dynamic network of branches and outlets across Malta and Gozo.

Subsidiaries and Associates

ReAPS Asset Management Limited is a wholly owned subsidiary of the Bank, which was incorporated in October 2016 as a private limited liability company in terms of the Companies Act and is licenced by the MFSA to perform investment management services under the Investment Services Act. As the Investment Manager of APS Funds SICAV p.l.c., during the reporting period, the Company registered a profit before tax of €0.2 million and a total net asset base of €0.8 million.

APS Funds SICAV p.l.c. was incorporated in January 2008 and is licensed by the MFSA as a collective investment scheme under the Investment Services Act. The company operating under the Retail UCITS Scheme consists of three sub-funds, namely the APS Income Fund, the APS Regular Income Ethical Fund and the APS Diversified Bond Fund. As at end of December 2018, the total assets under management for APS Funds SICAV p.l.c. stood at €149.9 million, decreasing marginally by €5.0 million, or 3.3% occurring through trading losses throughout the course of the year.

Financial Performance

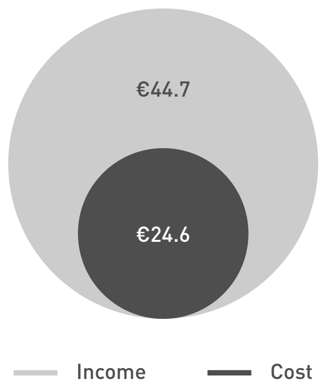
As of 31 December 2018, the Group posted a profit before tax of €18.6 million, further improving by 1.5% over the previous year with a return on average equity of 10.1%. Last year has been particularly marked by a one-off gain realised from the sale of financial instruments. If we exclude the effect of gains and losses arising on financial instruments, net profit before tax increased by 28.6% on the preceding year. This shows how the Group is further solidifying its position with another year of strong financial performance. The Group continued strengthening its market position within the community by aiming its focus on customer-centricity, governance, system processes and investment in capital expenditure. Moving forward, with the upcoming Business Plan 2019-2021 the Group aims to provide a simpler, more personalised experience to its customers to sustain its long-term profitability.

Operations

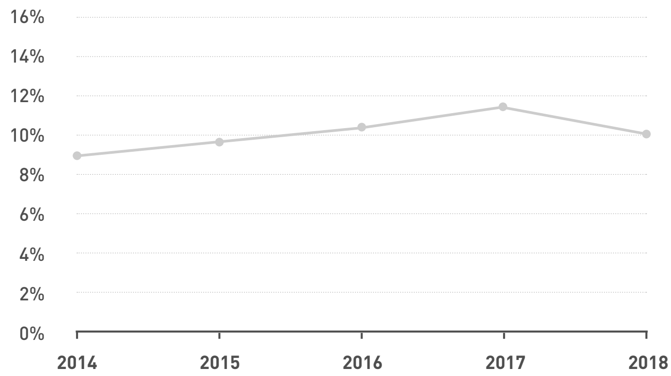
Net interest income registered for 2018 was €37.8 million, an increase of 15.3% when compared to the €32.8 million of 2017. A key pillar hereof was the interest receivable on Loans and Advances to Customers rising by €8.9 million or 27.9%, mainly driven by the increase in lending portfolio, both in mortgage and commercial lending. Interest Payable rose by 26.7% or €2.6 million yet still outweighed by the increase in the interest income. This was mainly attributable to the augmented level of deposits, which supported its lending activity.

Fees and Commission Income generated from banking activities increased by 24.7% reaching €6.2 million. The Group's continuous expansion in its operations and its efforts to strengthen its position in investment services positively affected these results. As at end of year, the Group experienced an unrealised loss of €0.7 million arising from movements in market values of financial instruments held in its Subsidiary. As reported in last year's annual statement, the Group's net gains on financial instruments stood at €3.3 million, including the one-off gain stemming from the sale of financial instruments invested as seed capital in the Bank's subsidiary, the APS Diversified Bond Fund.

Group's Cost to Income (€ million)



Group's Return on Average Equity (after tax)



The Group maintained its operating expenses at a prudent level with operating expenses totalling €24.6 million, 9.9% higher than previous year. The ongoing commitment towards the Group's workforce resulted in staff costs being the main contributor. Simultaneously, the Group kept on investing heavily in its infrastructure and the implementation of various systems which are scheduled to be fully operational in 2019 whilst further strengthening its compliance functions to ensure robust governance to protect the business. Further pursuing its Branch Transformation projects, the Group aims to attain a newly modernised retail experience throughout its entire branch network as to ultimately enhance customer experience. As a result, the Bank registered a cost-to-income ratio of 55.0%, which increased marginally when considering the same ratio reported in 2017. Nevertheless, this is still deemed satisfactory, with the Group continuously seeking to improve its cost-efficient management strategies so as to maximise its return over the years.

Net impairment charge reported for the year was €1.6 million when compared to the recorded figure of €2.5 million for 2017. This further supports the Group's prudent approach to lending especially when taking into account the introduction of IFRS 9 and the implementation of the Expected Credit Losses model, which superseded the previously adopted model of impairment losses.

Statement of Financial Position

Total asset base expanded by €394.8 million over December 2017, representing an increase of 26.4%, reaching a balance of €1.9 billion. This was mainly driven by the growth of €149.0 million, from the Loans and Advances to Households and Individuals. Commercial lending followed, with a further expansion of €107.0 million, with the accommodation services industry being the major contributor in this regard. Further enhancing its diversification strategy, the Group's syndicated loans portfolio registered further growth reaching a balance of €62.4 million. Along the years, the Bank strived to continuously diversify its product concentration. This is portrayed through growth in loans and advances almost recording the same increase between home loans and commercial loans. Non-Performing Loans declined to 3.8% from the preceding year, hence affirming the Group's prudent approach to lending.

The growth in the Group's lending portfolio was supported by the substantial increase in customer deposits, reaching €1.7 billion, consequently expanding by €424.7 million. This is a result of an increase in customer base and increased balances with existing customers.

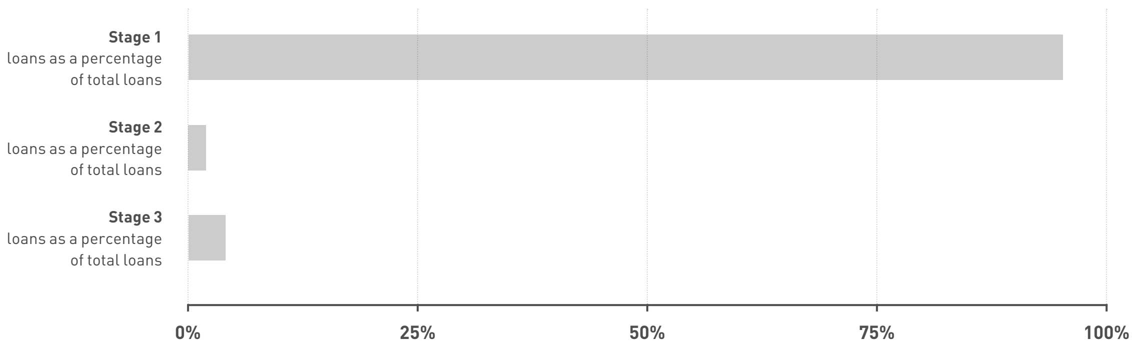
Capital and Liquidity Management

The Group's CET1 capital ratio reported for December 2018 was 13.94%, prevailing to be above the regulatory minimum. The Group's strong performance further contributed to maintain an adequate capital position. Capital planning and budgeting are always key elements on the Group's agenda. As part of supporting its long-term strategy, the Bank included in its Business Plan a capital development plan targeted to further strengthen its capital, hence allowing the Group to respond to new business opportunities and be well placed for future growth.

The liquidity requirement also remains a key aspect within the Group's programme especially when considering the ever challenging and competitive environment. While the attraction of various sources of funding and the expansion of lending services dominated the banking activity during the course of 2018, the Group pursued to conduct the necessary assessments to strike a sustainable balance between profitability and liquidity. As at the end of the year under review, the Liquidity Coverage Ratio (LCR) stood at 173.9%, remaining well above the regulatory threshold and within the Group's risk appetite.

For 2018, the Board of Directors are proposing a gross final dividend of 7.59 cents per share.

Group's loans credit quality



Principal Risks and Uncertainties

The successful management of risk is essential to enable the Group to achieve its objectives. The ultimate responsibility for risk management rests with the Bank's directors, who evaluate the Group's risk appetite and formulate policies for identifying and managing such risks. The principal risks and uncertainties facing the Group are included below:

(a) Market and competition

The Group operates in a competitive environment and faces competition from various other entities. Technological developments also have the ability to create new forms of quickly evolving competition. An effective, coherent and consistent strategy to respond to competitors and changing markets enables the Bank to sustain its increase in market share and its profitability. The Group continues to focus on service quality and performance in managing this risk.

(b) Legislative pressures

The Group is subject to numerous laws and regulations covering a wide range of matters. Failure to comply could have financial or reputational implications and could materially affect the Group's ability to operate. The Group has embedded operating policies and procedures to ensure compliance with existing legislation.

(c) Talent and skills

Failure to engage and develop the Group's existing employees or attract and retain talented employees could hamper the Group's ability to deliver in the future. Regular reviews are undertaken of the Group's resource requirements.

(d) Brand and reputation risk

Damage to the Group's reputation could ultimately impede the Group's ability to execute its corporate strategy. To mitigate this risk, the Group strives continually to build its reputation through a commitment to sustainability, transparency, effective communication and best practices. The Group works to develop and maintain its brand value.

(e) Economic and market environment

The Group is susceptible to changing market conditions in the broader economy within which it operates. A significant economic decline could impact on the Group's ability to continue to attract and retain customers. Demand for the Group's products can be adversely affected by weakness in the wider economy which are beyond the Group's control. This risk is evaluated as part of the Group's strategy process covering the key areas of investment and development and updated regularly throughout the year. The Group continues to make significant investment in innovation. The Group regularly reviews its pricing structure to ensure that its products are appropriately placed within the markets in which it operates.

(f) Technology and business interruption

The Group relies on information technology in all aspects of the business. In addition, the service that the Group offers to its customers are reliant on complex technical infrastructure. A failure in operation of the Group's key systems or infrastructure could cause a failure of service to its customers, thus negatively impacting its brand, and increased costs. The Group makes significant investment in technology infrastructure to enable it to continue to support the growth of its business and has a robust selection and monitoring process of third-party providers. The Group also invests in technology infrastructure which enables it to reduce cyber risk. The Group also organises regular business continuity exercises to ensure ongoing readiness of key systems and sites.

(g) Supply chain

The Group relies on a number of third parties and outsourced suppliers to support its supply chain. A significant failure within the supply chain could adversely affect the Group's ability to deliver products and services to its customers. A robust supplier selection process is in place with appropriate ongoing management and monitoring of key suppliers.

(h) Customer service

The Group's revenues are at risk if it does not continue to provide the level of service expected by its customers. The Group's commitment to customers is embedded in its values. The relevant employees undertake intensive training programmes to ensure that they are aware of, and abide by, the levels of service that are required by the company's customers.

(i) Financial risk management

Note 42 to the financial statements provides details in connection with the Group's financial risk management objectives and policies and the financial risks to which it is exposed.

(j) Significant judgements and estimates

Note 2.3 to the financial statements provides details in connection with the inherent uncertainties that surround the preparation of the financial statements and which require significant estimates and judgements.

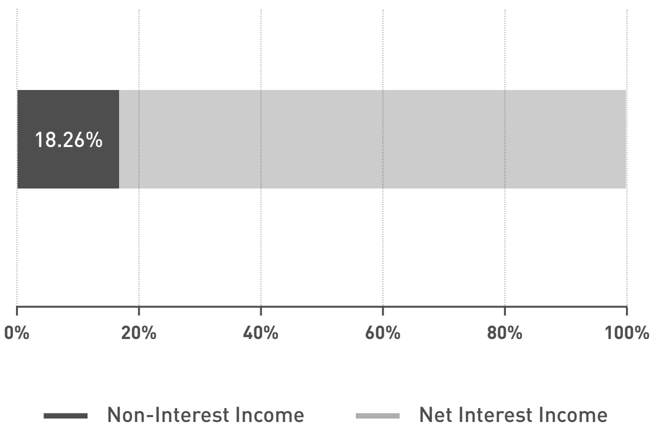
(k) Contingent liabilities

Note 37 to the financial statements provides details in connection with the Group's contingent liabilities.

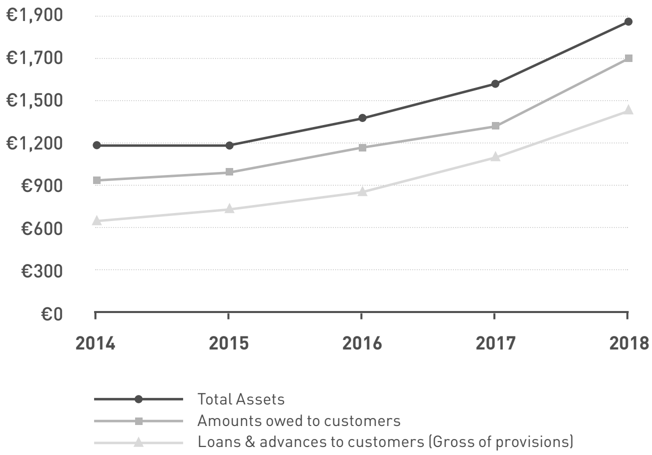
Outlook

Following up on 2017, the Group continued on its journey in achieving its mission of long-term growth and sustainable profitability, with various projects being resumed and others commenced during the course of 2018. Both placed emphasis on the enhancement of its governance and risk management, whilst striving to supply its clientele with the best service that

Group's Non-Interest Income to Net Interest Income



Group's Growth over a 5-Year Period (€million)



exceeds their expectations, thereby building towards the Bank's re-invented vision of being *"The Community Bank in Malta"*. With the new Business Plan commencing in 2019, the Group will be focusing on attaining its vision and mission through a framework of three key principles namely, engage with its communities, consolidate its backbone and innovate. Further supporting these principles is the launch of the Omni-Channelling solution being implemented in the forthcoming year seeking to further enhance the customer experience.

Looking ahead to 2019, at our distinctive core values, solid governance and diversification model the Group has geared itself up to more success. Simultaneously, the Group is currently undergoing a process in converting itself into a public limited company (p.l.c). This will aid in addressing its funding requirements for the near future whilst delivering long-term value to all its stakeholders. Together with the underlying drivers of our culture aligned towards our business strategy, we are confident it will take the Group's brand to the next level.

Directors' Responsibilities for the Financial Statements

The Companies Act, Cap. 386 of the Laws of Malta requires the Directors to prepare financial statements for each financial year that give a true and fair view of the state of affairs of the Group at end of each financial year and of its profit or loss for that financial year in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union ('EU').

The Directors are responsible for ensuring that:

- Appropriate accounting policies have been consistently applied and supported by reasonable and prudent judgments and estimates.
- Financial statements have been drawn up in accordance with International Financial Reporting Standards as adopted by the EU.
- The financial statements are prepared on the basis that the Group must be presumed to be carrying on its business as a going concern.
- Account has been taken of income and charges relating to the accounting period, irrespective of the date of receipt or payment.

The Directors are responsible for ensuring that proper accounting records are kept which disclose with reasonable accuracy at any time, the financial position of the Group and which enable them to ensure that the financial statements comply with the Companies Act, Cap. 386 of the Laws of Malta and the Banking Act, Cap. 371 of the Laws of Malta.

The Directors are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Disclosure in Terms of the Sixth Schedule to the Companies Act, Cap. 386 of the Laws of Malta

During the year ended 31 December 2018, no shares in the Bank were:

- Purchased by it or acquired by it by forfeiture or surrender or otherwise.
- Acquired by another person in circumstances where the acquisition was the Bank's nominee, or by another with the Bank's financial assistance, the Bank itself having a beneficial interest.
- Pledged or made subject to other privileges, to a hypothec or to any other charge in favour of the Bank.

Standard Licence Conditions

In accordance with Standard Licence Condition 7.28 of the Investment Services Guidelines issued by the MFSA, licence holders are required to disclose any regulatory breaches of the Standard Licence Conditions in their annual report. During the year under review, there were no such regulatory breaches nor were any regulatory sanctions imposed on the bank by the MFSA.

Auditors

Deloitte Audit Limited have signified their willingness to continue in office as auditors of the Group and a resolution proposing their reappointment will be put to the Annual General Meeting.

The Directors' report was authorised for issue by the Board of Directors and was signed on its behalf by:

F. Mifsud Bonnici
Chairman

F. Azzopardi
Director

21 March 2019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CAPITAL ADEQUACY & RISK DISCLOSURES REPORT

The objective of this report is to implement the Additional Regulatory Disclosures for APS Group, as referred to in Banking Rule BR/07/2014 - *Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised Under the Banking Act 1994,* and governed by Part Eight of the Capital Requirements Regulation (CRR) No. 575/2013.

1 Introduction

This report is not subject to external audit, with the exception of any disclosures which are equivalent to those made in the 2018 financial statements which adhere to International Financial Reporting Standards as adopted by the EU (EU IFRSs). However, this report has been subject to comprehensive internal review and it has been approved by the Group's Risk Committee and its Board of Directors (hereafter referred to as 'the Board'). This information is published annually. The Group is satisfied that internal verification procedures ensure that these Additional Regulatory Disclosures present a fair and accurate picture.

2 Risk Governance

Responsibility for risk management lies at all levels within the Bank through a three lines of defence model. Business units, as the first line of defence, are responsible for identifying, assessing and mitigating the risks to which the Group is exposed in the respective operating units. The management of the various forms of risk is then co-ordinated and monitored by the second line of defence, namely the Risk and Compliance Departments. The Internal Audit Department, as the third line of defence, provides independent assurance to the Board.

The Risk and Compliance Departments are headed by the Chief Risk Officer who reports directly to the Risk Committee. The Risk Committee establishes and ensures the implementation of the Group's risk management and compliance strategy, systems and policies. The Committee is composed of five Non-Executive Directors (one of whom chairs the Committee) while the Chief Executive Officer, Chief Risk Officer, Chief Financial Officer, Head Risk and Head Investment Management are non-voting members of the Committee. The Risk Committee meets regularly to monitor the assessment of risk and ensures that policies are in place in line with the Group's risk appetite, as set by the Board. Policies, including revisions to existing ones, are recommended to the Board for approval, unless the Board specifically delegates this authority to other Committees.

The Risk Department maintains a comprehensive enterprise-wide view of the risks facing the Group and ensures that these are within the Risk Appetite set by the Board. The Group's Risk Appetite is reviewed and approved by the Board through the annual review of its Risk Appetite Statement. The Risk Department is responsible for bringing to the attention of the Risk Committee emerging risks and material changes to existing risks within the Group's risk profile, including as part of the business planning process, to ensure that Management operates within the risk appetite approved by the Board. Subsequently, it is the role of the Chairperson of the Risk Committee to report to the Board on such updates. As the second line of defence, the Risk Department operates independently of the Bank's business activities vested in the first line of defence. The Department comprises:

- **Credit Risk Management Unit (CRMU):**
  The CRMU, which is responsible for Credit Risk Management, is vested with the following main responsibilities:

i. Drafting and reviewing the Credit Risk Policy, duly supported by the underlying procedures, in line with the Bank's Risk Appetite;
ii. Independent evaluation/recommendation of credit proposals presented by first line of defence;
iii. Ensuring that the Credit Portfolio is diversified, sound and consistent with the Bank's Credit Risk Policy;
iv. Monitoring of key risk indicators for credit risk and pursuing escalation procedures when appropriate;
v. Maintaining the credit rating framework and system development and compliance with regulations;
vi. Identifying performing from non-performing credit facilities and relative provisioning;
vii. Ensuring that the Bank's lending principles are consistent with the Regulations and Banking Rules;
viii. Developing and adhering to the NPL Reduction Plan, which is the responsibility of the Recovery Function of the Bank;
ix. Ensuring compliance with the credit regulatory reporting framework.

- **Enterprise Risk Management Unit (ERMU):**
  The ERMU's objective is to articulate and champion the Risk Appetite set by the Board and ensure that business functions operate within this framework. The Unit continuously seeks to enhance the Bank's risk-awareness and culture which are considered a key element of effective risk management. The ongoing update of the Risk Register resides with the ERMU through collaboration with other Departments within the Bank. The compilation and submission of the Internal Capital and Liquidity Adequacy Assessment Process and Recovery Planning Process falls under the remit of this function. The ERMU performs regular sensitivity analyses and stress testing encompassing all material risks facing the Bank. The management of credit risk within the investments portfolio, liquidity and funding risk and market risk are also the responsibility of the ERMU.

- **Operational Risk Management Unit (ORMU):**
  The main areas of focus of the ORMU are IT and Cyber Risk, Operational Risk Governance, Business Continuity Management and Bank Insurance cover. The unit is responsible for compiling the quarterly operational losses and near misses report, upholding a current and tested business continuity plan as well as maintaining a comprehensive and effective insurance cover for all insurable bank risks not related to specific products.

The Compliance function is constituted as follows:

- Regulatory Compliance:
  This Unit covers all licensable activities, thus including Banking, Investment Services and Insurance Intermediation. Hence, it keeps under constant review local and EU based regulatory developments and assesses potential impacts on the Group's daily activities. Furthermore, the Unit's remit also includes the Data Protection capacity, overseen by the Data Protection Officer, and the handling of customer complaints with specific emphasis on all matters which are referred to the appropriate regulatory body i.e. the Office of the Arbiter for Financial Services (OAFS).

- Financial Crime Compliance:
  This Unit essentially covers all Anti-Money Laundering (AML) and Combating the Funding of Terrorism (CFT) initiatives/ controls and Sanctions monitoring. It also acts as the Subject Matter Expert for the branch network, back office functions and Senior Management.

- Customer Profiling:
  This Unit is involved in the on-boarding and periodical reviews of all personal and non-personal client profiles with specific reference to corporate entities and high risk clients. It is also involved in assessment exercises which may potentially lead to declining or exiting a customer relationship.

From an internal governance perspective, the Compliance Function is overseen by the Compliance Committee which meets on a regular basis. The purpose of this Committee is to ensure implementation of the Bank's compliance strategy, systems and policies, as determined and delegated by the Risk Committee. One of the responsibilities of the Compliance Committee is to ensure that prescribed regulations, rules, policies, guidelines and procedures are being followed and also anticipated – as may be appropriate. This includes oversight of major compliance projects, client data reviews, KYC and transaction monitoring tools.

The following sections provide an overview of each material risk to which the Group is exposed, including the risk mitigation and capital allocation techniques adopted. The Bank considers the risk of its subsidiary, ReAPS Asset Management Limited, to the extent that this constitutes a material impact on the Group's risk profile. The subsidiary has its own Risk Management and Compliance policies and documented procedures that delineate the risk management and compliance processes, which facilitate reporting to the Risk Committee on the assessment of the subsidiary's risk profile.

3 Credit Risk

This is the possibility that a borrower or counterparty fails to meet his/her obligations in accordance with (or performing according to) agreed terms. Alternatively, losses may result from reduction in asset value arising from actual or perceived deterioration in credit quality. In view of the nature of its business, the Group's financial assets are inherently and predominantly subject to credit risk. Thus, Management has put in place internal control systems to evaluate, approve and monitor credit risks relating to both the investments and the advances portfolios.

The Group has a detailed Credit Risk Policy which lays down the principles for the management of credit risk. The following sections provide a brief outline of the main elements of the Group's credit risk management framework.

3.1 Credit Approval

The Group has a process in place for the approval of new credits, as well as the amendment, renewal and review of existing credits. The Group's credit approval process establishes accountability for decisions taken and designates different levels of authority to approve credits or changes in credit terms as approved by the Risk Committee and the Board of Directors.

Proposals for credit facilities are issued by business units (the first line of defence) and escalated to higher levels for approval, depending on various criteria and types of limits. Credit facilities above a certain amount, or which do not fall under the Bank's lending policies, are proposed to the Credit Risk Unit for evaluation and recommended to the Management Credit Committee (MCC), Board Credit Committee (BCC) and Board depending on the exposure involved or the relative terms and conditions.

The BCC is composed of three Non-Executive Directors together with the Chief Executive Officer and Chief Financial Officer. The Chief Risk Officer, Head Risk and Head Banking are non-voting members of the Committee. The main functions of the BCC relate to the credit risk framework within which credit applications are reviewed, approved, or recommended to the Board. It advises the Risk Committee on credit limits by country, geography and sector, as required by the Bank's credit policy.

In order to fulfil its duties, the BCC is authorised by the Board to delegate certain powers and authorities to the MCC. The MCC receives and reviews credit applications and approves credit limits for customers and transactions, within the parameters set by the BCC in terms of the credit policy and procedures. It refers and recommends to the BCC applications where these exceed its (MCC) limits. The MCC is composed of the Chief Executive Officer, who chairs the meetings, the Chief Financial Officer, Chief Risk Officer, Head Banking, and Senior Manager Retail. Head Risk, Head Legal and Senior Manager Commercial are non-voting members of the Committee. Credit applications that exceed the limit established for the BCC are recommended to the Board for approval.

Counterparty exposures and credit limits with correspondent banks are recommended by the Group's Assets Liabilities Management function to the MCC for its consideration. If in agreement, the MCC approves or recommends these proposals to the BCC depending on the amount requested. The BCC ensures that the Group adopts a sound investment strategy to diversify its revenue streams within an appropriate risk-reward trade-off.

3.2 Credit Analysis

The Group has detailed credit granting processes and criteria to evaluate the credit risk inherent in a borrowing application. The Group also has procedures in place (in adherence to current banking regulation) to identify situations where, in considering an advance, it is appropriate to classify a group of borrowers as connected counterparties and, thus, as a single exposure. As connected accounts are to be grouped and treated as being one exposure, the Group takes into consideration the total facilities at the disposal of connected customers before considering extending further facilities to one of the members forming part of a group of connected customers.

Monitoring and control processes are considered to be of critical importance during the life cycle of a credit facility and contribute towards the maintenance of a sound lending portfolio. To ascertain the current financial conditions of the borrower or counterparty, as well as to keep track of decisions made and the history of the credit, the Group maintains electronic credit profiles and dossiers with all the relevant information and documentation supporting decisions made. The Group applies an automated proprietary credit rating system to differentiate the degree of credit risk inherent in advances extended to its customers. Ratings are used to grade advances with a view to assess the repayment ability of the borrower and to assist in the monitoring and control of credit risk. The credit rating process also provides a basis for the recognition of any non-performing loans and for the assessment of expected credit losses.

3.3 Credit Limits

The Group has established exposure limits at the level of individual borrowers and counterparties, groups of counterparties, maturity, sector and geography. These limits are approved by the above-mentioned Credit Committees, in certain cases the Risk Committee, as well as the Board. The Country Risk Policy puts forward a methodology to align the Bank's exposure to international countries with its risk appetite and the relative country risk (including transfer and convertibility risks). In addition, the Credit Risk Policy also stipulates limits on a sectorial basis. Further detail on the Bank's exposure limits is provided within section 3.5.

3.4 Related Parties

Credit facilities negotiated with related parties are reported to the Board on a quarterly basis and adequately disclosed in the Financial Statements. Requests by related parties for credit facilities which are not at arm's length are to be approved by the BCC and reported to the Board on a quarterly basis.

As part of its duties, the Audit Committee ensures that transactions with related parties are adequately assessed, reviewed and reported to ensure approval at arm's length, in addition to performing other assurance functions as delegated to it by the Board.

3.5 Concentration Risk

The Group is exposed to concentration risk within its advances and investments portfolios (as well as within its deposits portfolios). Concentration risk arises when the Group has significant exposures to a single counterparty, groups of connected counterparties, and counterparties in the same geographic region or from the same sector of activity.

To manage its exposure to concentration risk across its portfolios, the Group adopts an exposure limits system by individual and connected exposures, sector and geography. The Risk Committee and the Board are regularly informed about the exposure of the Group against such limits.

In terms of the CRR, an exposure to a customer or group of connected customers is considered to be a large exposure where its value, before the deduction of eligible credit risk mitigation, is equal to or exceeds 10% of the Group's Own Funds. Large exposures are reported both internally and to the Authority and are monitored continuously to ensure that these do not exceed the regulatory threshold of 25% of the Bank's Own Funds.

The Group also monitors the individual and sectorial concentration index and translates this into an economic capital figure for the purposes of capital allocation as part of its ICAAP.

Exposures by Industry of the Group's advances portfolio broken down by exposure classes are shown in Table 1, while Table 2 shows the residual maturity of the Group's advances portfolio broken down by exposure classes.

Table 1
Exposures by industry of the Group's advances portfolio broken down by exposure class (Gross)

	Financial Institutions €000	Manu-facturing €000	Real Estate €000	Wholesale and Retail €000	Public Sector €000	Other Industries €000	Individuals €000	Total €000
Government	-	-	9,656	-	11,210	113	-	20,979
Real Estate	-	-	-	-	-	330	793,715	794,045
Corporate	75,104	35,960	64,494	38,892	-	136,486	-	350,936
of which SME	*51,928*	*10,865*	*64,494*	*28,847*	-	*110,965*	-	*267,099*
Retail	-	1,455	10,052	8,212	-	17,208	22,302	59,229
of which SME	-	*1,455*	*10,052*	*8,212*	-	*17,208*	-	*36,927*
High Risks Items	-	-	57,551	-	-	-	-	57,551
Exposures in Default	3,793	9,625	18,993	4,985	-	4,210	8,729	50,335
Total	**78,897**	**47,040**	**160,746**	**52,089**	**11,210**	**158,347**	**824,746**	**1,333,075**

Table 2
Residual maturity of the Group's advances portfolio broken down by exposure classes (Gross)

	Less than 3 months €000	Between three months and one year €000	Between one and five years €000	More than five years €000	Total €000
Government	-	2,952	81	17,946	20,979
Home Loans	358	148	5,582	787,957	794,045
Corporate	4	78,105	67,059	205,768	350,936
Retail	12	6,528	10,022	42,667	59,229
High Risks Items	-	4,408	35,311	17,832	57,551
Exposures in Default	12,822	25,151	2,360	10,002	50,335
Total	**13,196**	**117,292**	**120,415**	**1,082,172**	**1,333,075**

3.6 Collateral

The Group generally takes collateral against its loans and advances portfolio, most of which consists of immovable property. These are taken by the Group as a fall-back, hence acting as a secondary source of repayment should the primary source of repayment fail. The security provided does not form the main basis of the lending decision. The Group has to be satisfied, amongst other things, that the primary source of repayment will be reliable and sustainable. In this spirit, the taking of collateral is neither considered a substitute for a comprehensive assessment of the credit application and the corresponding borrower or counterparty, nor can it compensate for insufficient information or deficient primary source of repayment. The Credit Risk Policy of the Bank stipulates inter alia the types of collateral and valuations to be carried out.

Other collateral, which is not tangible, is sought to ensure that the borrowing customer will abide by the terms and conditions of sanction, thereby reducing the default risk associated with the borrowing customer.

The value and type of collateral required depends on an assessment of the credit risk of the counterparty. The main types of collateral held at the end of 2018 are as follows:

	€000
Government and other Guarantees	31,728
Cash or Quasi Cash	23,293
Commercial Real Estate	256,487
Residential Real Estate	796,059
	1,107,567

Collateral held as security for financial assets other than loans and advances depends on the nature of the instrument. Debt securities are generally unsecured, with the exception of covered bonds, which are mainly secured by residential mortgages.

3.7 Expected Credit Loss

In line with IFRS 9, the Group calculates the Expected Credit Loss in respect of the credit facilities and investments portfolios, which is based on the probability of default (PD), loss given default (LGD) and exposure at default (EAD) of each exposure. The Risk Committee is responsible to certify to the Bank's Board that provisioning levels recommended by Management are adequate and in line with the Bank's approved methodologies and the related financial reporting standards.

3.8 Credit Risk Reporting

The Risk Department is responsible for monitoring and reporting on the credit quality of both the advances and investments portfolios. The Risk Department presents regular risk reports to the Board, Risk Committee and Executive Committee. These reports include, but are not limited to, an analysis of credit growth, non-performing exposures, value at risk and concentration risk.

3.9 Capital Requirement

The Group adopts the Standardised Approach (as per Regulation No. 575/2013 - Capital Requirements Regulation (CRR)) for the purposes of calculating the risk-weighted exposures to credit risk. For rated investments within its investment portfolio, the Group adopts credit ratings assigned by reputable credit rating agencies to establish the credit quality of all exposure classes, that is, institutions, government and corporate debt securities. For unrated investments and exposures within the advances portfolio, risk weights are assigned in accordance with the CRR. The Standardised Approach is based on the assumption that the Group's portfolio is sufficiently granular, as this methodology has been calibrated for internationally active banks. For this reason, the Group also allocates additional capital to cover concentration risk under Pillar 2 (Section 3.5). Further information on the Bank's risk-weighted exposure to credit risk is provided in Section 9.

4 Market Risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates, and prices of equities, bonds and commodities.

The Group's exposure to market risk is limited since its trading portfolio is minimal. This is consistent with the Group's Risk Appetite. In accordance with the CRR, it is therefore exempted from the trading book capital requirements.

The Group's exposure to market risk is mainly related to:

i. Interest rate risk – the risk that the Group's financial position and cash flow is exposed to unfavourable movements in interest rates.
ii. Foreign exchange risk – the risk that the Group's financial position and cash flow is exposed to unfavourable movements in foreign exchange rates.

The Group had an investment of €1.5 million in equities at the end of 2018. The risk associated with this exposure is not considered to be material.

The Assets and Liabilities Committee (ALCO) is primarily responsible for balance sheet management and pricing policies. Towards this, it reviews financial information and assesses the impact of various types of risks—related to changes in interest rates, exchange rates and the market—on the Bank's profitability and financial statements. The members of the ALCO are the Head ALM (Chair), Chief Executive Officer, Chief Finance Officer, Chief Risk Officer, Head Risk, Head Investment Management and Senior Manager Finance.

4.1 Interest Rate Risk in the Banking Book

The Group is mainly exposed to interest rate risk in the banking book (IRRBB) which arises from the Bank's non-trading activities. The Group has an Interest Rate Risk Policy approved by the Board, which sets out a comprehensive risk management process that identifies, measures, monitors and controls interest rate risk exposures, whilst also ensuring appropriate oversight by Senior Management, Board-appointed committees and ultimately the Board, to confirm that this risk is consistent with its risk appetite.

Interest rate risk is measured from two perspectives – the earnings perspective and economic value perspective. Both of these perspectives are complementary in understanding and assessing IRRBB. Earnings measures capture the short-term effect of interest rate changes on the Group's earnings. On the other hand, economic value measures capture the long-term effect of interest rate changes, which is a key aspect in defining a business strategy and keeping an adequate level of capitalisation in the long term.

The management of Interest Rate Risk through the Earnings Perspective

The ALCO is responsible for maintaining an effective balance between the assets and liabilities of the Bank. The net interest margin is the main driver of the Group's profitability. Therefore, the primary objective of ALCO is to ensure that there exists an appropriate margin between interest receivable and interest payable. Consequently, ALCO must ensure that the pricing of assets and liabilities supports an adequate net interest margin. In pricing commercial facilities Management is guided by the Bank's credit pricing model which takes into consideration loan characteristics, such as, the loan term, amount, capital requirement and collateral.

The Group also monitors its resilience to interest rate shocks by adopting a capital approach using the Duration Gap Analysis. This methodology is based on offsetting the interest-sensitive long and short positions in each time band, resulting in a single short or long position in each time band. This is the interest rate gap. Assets and liabilities are then re-priced according to a 100 basis points parallel shift in the yield curve over a period of one year. These are then netted off to determine the total impact of the assumed interest rate shift. At 31 December 2018, the resulting impact on the Group's net interest income following a 100 basis points parallel movement in interest rates over a period of one year amounts to €1,602k, as per note 42.5. This is within the Group's Risk Appetite.

The Group uses simulation modelling on a quarterly basis to monitor the sensitivity of projected net interest income for the subsequent twelve months. The model simulates a 25 basis points parallel shift in interest rates and the impact on cash flows and the resulting income streams. The parallel shift is assumed to take place on the first day of the following month, or following maturity in the case of debt securities, fixed rate loans and term deposits. At 31 December 2018, an increase in interest rates by 25 basis points leads to an increase of €408k in projected net interest income, while a decline in interest rates by 25 basis points leads to decline of €1.38m in projected net interest income, as per note 42.5. These fall within the Group's Risk Appetite.

The management of Interest Rate Risk through the Economic Value Perspective

The Interest Rate Risk Policy establishes a limit where the Group's economic value must not decline by more than 20% of Own Funds as a result of a sudden and unexpected parallel shift in interest rates of 200 basis points. In line with the CRD IV, in the event that the decline in economic value is greater than 20% of Own Funds, the Bank is required to inform the regulator. During 2018, the resulting impact on the Group's economic value was at all times well within the established regulatory requirement and within the Group's risk appetite.

During 2018 the European Banking Authority (EBA) issued revised guidelines on the management of interest rate risk arising from non-trading book activities. The Group embarked on a project to re-align the measurement of its exposure to interest rate risk with these guidelines, which come into force from 30 June 2019.

4.2 Foreign Exchange Risk

The Group's financial assets and liabilities are predominantly held in Euro. The Foreign Exchange Risk Policy puts forth a framework for identifying, measuring, managing and reporting on the Bank's exposure to this risk. The Policy clearly outlines the structure, responsibilities and controls for the management of foreign exchange risk and sets limits, on the level of exposure by currency and in total, which are monitored regularly. The Enterprise Risk Management Unit is responsible for carrying out sensitivity analyses showing the impact on the Bank's financial position as a result of an adverse/favourable movement in all currencies against the Euro. Capital is allocated for the Bank's exposure to foreign exchange risk in line with the Basic Method stipulated by the CRR. Further information on the Bank's risk-weighted exposure to foreign exchange risk is provided in Section 9.

5 Operational Risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems, or from external events. The Operational Risk Policy sets forth a framework for the identification, management, monitoring and reporting on the Group's exposure to this risk. The Policy also seeks to continuously enhance the Group's operational risk management culture.

When internal controls fail, operational risk can inflict damage to reputation, have legal or regulatory implications, and/or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through its control framework and by monitoring and responding to potential risks, it is able to manage operational risks effectively. Controls include appropriate segregation of duties, ensuring that Staff Members have appropriate expertise and training and regular verification and reconciliation of transactions and accounts.

The Policy clearly sets out the responsibilities for the management of operational risk, as well as the operational risk management process to ensure that the operational risk level is aligned with the Group's risk appetite.

The Group maintains a database to regularly record and quantify operational losses and near miss events, reported by the first line of defence and co-ordinated and analysed by the Operational Risk Management Unit, in order to promote a culture of cooperation, communication and continuous improvement where lessons are learnt from incidents and near misses. The Bank embarked on an operational risk register compilation project for the identification and evaluation of operational risk through process and risk mapping, with a view to assess inherent operational risks and residual operational risks after the application of the relevant mitigating actions and controls.

The Group also has a Business Continuity Plan (BCP) in place, which is regularly updated and provides a standard procedure that must be followed in the eventuality that a disruption affects its operations, to ensure that resumption of core services and critical functions is carried out in an efficient and prioritised manner. The likelihood and/or impact of particular events may also be mitigated through the Group's comprehensive insurance coverage strategy.

5.1 IT and Cyber Risk

The Bank continues to capitalise on IT within its activities and strengthen its online presence, whilst cognisant of the evolving cyber threats landscape. The Bank maintains zero tolerance to events that could compromise the confidentiality and integrity of data, as well as the availability of its IT systems.

The Technology and Innovation Committee (TIC) provides the Bank's Board with oversight and direction over the Bank's Information, Communications and Technology programmes including innovation initiatives. The TIC is composed of four NEDs, one of whom chairs the Committee, together with the Chief Executive Officer, Chief Financial Officer, Chief Technology Officer and Chief Strategy Officer.

In this complex operating environment, the Bank has embarked on an extensive programme to update its information and cyber security operating frameworks, continue implementation of avant-garde information security tools, partnering with industry specialists to be fully equipped to prevent information security and cyber threats and to be agile to respond to security threats with minimal disruption on the Bank's operations.

The Risk Department, as the second line of defence, includes dedicated (and separate) functions for Information Security Governance, reporting directly to the CRO, and IT and Cyber Risk oversight.

5.2 Capital Requirement

The Group allocates capital for operational risk in line with the Basic Indicator Approach as regulated by the CRR. Further information on the Bank's risk-weighted exposure to operational risk is provided in Section 9.

6 Liquidity and Funding Risk

Liquidity risk is the risk that the Group cannot meet its financial obligations as they fall due in the short term and medium term, either at all or without incurring unacceptable losses.

Funding risk is the risk that the Group cannot meet its financial obligations as they fall due in the medium to long term, either at all or without increasing funding costs unacceptably. Funding risk can also be seen as the risk that its assets are not stably funded in the medium and long term.

The Group manages this risk by seeking to match the maturities of assets and liabilities. The management of liquidity and funding is governed by a detailed Liquidity and Funding Risk Policy. This Policy establishes clear lines of responsibility, limits and guidance on the measurement and monitoring of the Group's net funding requirements. The Asset Liability Management Unit is responsible for implementing the Policy; whereas ALCO is responsible for monitoring and ensuring the implementation of and adherence with the Policy, as well as ensuring consistency with the Bank's Risk Appetite. It also ensures that adequate liquidity is held to meet both expected and unexpected commitments. This Policy includes a detailed Liquidity Contingency Plan which addresses the strategy for handling liquidity crises and includes procedures for covering cash flow shortfalls in emergency situations.

Through the Internal Liquidity Adequacy Assessment Process (ILAAP), the Group ensures that it maintains, at all times, liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. Thus, the ILAAP serves as a key decision making tool in liquidity and funding management. The latest ILAAP, compiled in line with EBA Guidelines, concluded that the Bank maintains adequate levels of liquidity buffers and adequate funding. The document is reviewed in detail by the Bank's Internal Audit Department and Risk Committee and subsequently presented to the Board for approval. Following Board approval, the ILAAP Report is submitted to the regulator.

The Group funds loans primarily through sourcing retail deposits. At 31 December 2018 the Group's Loan-to-Deposit ratio, computed in line with the methodology adopted by the EBA, was equal to 92.1% which is in line with the Bank's risk appetite. Moreover, the Group has a level of stable deposits which acts as a virtually permanent source of liquidity. The Group also has a portfolio of highly marketable assets that can be easily liquidated in the event of any unforeseen cash flow requirements.

The Liquidity Coverage Ratio (LCR) measures the Group's liquidity buffer to its net liquidity outflows over a 30 calendar days' stress period. The Bank reports this ratio to the regulator. During 2018 the Bank's LCR fluctuated consistently above the applicable minimum requirement of 100% and, at 31 December 2018, stood at 174%.

The Net Stable Funding Ratio (NSFR) measures the amount of stable funding available to a financial institution against the required amount of stable funding. The NSFR is subject to an observation period until a binding minimum standard is introduced by the Authorities. The Bank officially reports information on its funding structure to the regulator on a quarterly basis. In addition, the Bank monitors its NSFR in line with Basel III Rules. As for the LCR, the NSFR was consistently above 100% during 2018.

7 Reputation Risk

Reputation is considered by the Group to be its most valuable intangible asset and is governed by a detailed Reputation Risk Policy.

The Bank has zero-tolerance to maximising profitability at the detriment of its reputation and standing, as profits are not the primary objective that the Group follows.

Moreover, the Group has a number of systems and techniques in place to mitigate reputation risk; including a Board succession policy, a detailed risk management system, a business continuity plan, the Code of Conduct, established credit granting criteria, sound investment parameters and anti-money laundering procedures. During 2018 the Bank strengthened further its governance through various actions which include the introduction and revision of various policies including the Nomination and Succession Policy, Conflicts of Interest Policy, Anti-Bribery and Anti-Corruption Policy, Risk Management Policy, Operational Risk Policy and Information Security and Cyber Risk Policy.

8 Other Risks

The Group has a detailed risk management system which covers other risks not mentioned above; such as legal, strategic, residual and systemic risks. The Group has established risk management policies governing the management and mitigation of these risks, which policies are approved by the Risk Committee and Board.

9 Capital

9.1 Capital Planning

Capital planning is a crucial element of the Group's business planning process. The Group examines both the current and future capital requirements in line with its Risk Appetite and strategic business objectives, in order to establish its near and long-term capital needs, capital expenditures required for the foreseeable future, target capital levels and potential sources of capital. Capital planning is the responsibility of the ALCO.

Furthermore, as part of its capital planning process, the Bank takes into consideration the requirements of Banking Rule BR/15/2015 – *Capital Buffers of Credit Institutions Authorised Under Banking Act 1994,* which introduced a number of capital buffers. These buffers entered into force as from January 2016, with full application by January 2019. The Group is on track to fully implement the CRD IV capital requirements by January 2019.

As an integral part of the Group's business planning process, the Risk Department performs a detailed analysis of the capital requirements over the medium- and long-term. This involves compiling scenario analysis and stress testing exercises to evaluate the impact of the Bank's strategic growth on its risk profile, whilst also taking into consideration regulatory requirements. The impact of business objectives on the Group's risk profile is also evaluated as part of the annual budgeting process.

9.2 Capital Adequacy

The Group's capital is mainly composed of Common Equity Tier 1 (CET 1) instruments, as defined by the CRR. Further information on the main features and terms and conditions of the Group's capital instruments is provided in note 42.7.

The Group adopts the Standardised Approach (as per the CRR and Banking Rule BR/08/2012 – Capital Adequacy of Credit Institutions Authorised Under the Banking Act 1994) for the purposes of calculating its risk-weighted exposure to credit risk. The minimum regulatory capital allocation to credit risk is calculated at 8% of the credit risk-weighted exposures.

For the purposes of allocating capital to cover foreign exchange risk, the Group adopts the Basic Method (as per the CRR and Banking Rule BR/08/2012 – *Capital Adequacy of Credit Institutions Authorised Under the Banking Act 1994).* The capital allocation for foreign exchange risk is therefore equal to 8% of the higher of the sum of the Group's net short or net long positions.

The Group adopts the Basic Indicator Approach (as per the CRR and Banking Rule BR/04/2013 – *Capital Requirements of Credit Institutions Authorised Under Banking Act 1994)* for the purposes of allocating a capital charge to cover operational risk. Under this approach a 15% charge is applied on average operating income for the previous three financial years.

The Group's capital ratios are regularly monitored and reported to Executive Management, ALCO, Risk Committee and Board. The following table discloses the Group's capital position at 31 December 2018. The book values, risk-weighted exposures and capital requirements by exposure class have been provided for the Group only, as the difference between the capital requirement of the Bank and the Group is immaterial. Capital allocation is based on the methods highlighted above. Further information on the Bank's capital position is provided in note 42.7.

Table 3
The Group's risk-weighted exposures and capital requirements

31 December 2018	Book Value €000	Risk Weighted Exposure €000	Capital Allocation €000
Standardised Approach - Credit Risk			
Sovereign	362,267	7,490	599
Institutions	95,280	28,642	2,291
Corporates	443,802	279,478	22,358
Retail	62,418	45,661	3,653
Home loans	793,713	317,757	25,421
Exposures in default	28,225	33,884	2,711
Items associated with particular high risk	59,661	89,492	7,159
Collective investment undertakings	23,968	19,368	1,549
Equity exposures	1,523	1,523	122
Other assets	36,963	42,687	3,415
	1,907,820	**865,982**	**69,278**
Basic Indicator Approach			
Operational Risk		72,462	5,797
Basic Method			
Foreign Exchange Risk		167	13
		938,611	**75,088**
Total Own Funds		**130,888**	
Capital Adequacy Ratio		**13.94%**	
Capital Conservation Buffer		1.875%	

9.3 Internal Capital Adequacy Assessment Process

The Bank performs an Internal Capital Adequacy Assessment Process (ICAAP) in compliance with the Pillar II requirements of Banking Rule BR/12/2014 – *The Supervisory Review Process of Credit Institutions Authorised Under the Banking Act 1994* and the CRR. This key decision-making tool is of utmost importance for keeping the Board of Directors informed about the Bank's ongoing risk assessment, the mitigation measures adopted and their impact on the capital requirements.

The Bank's ICAAP is based on the principle of proportionality set out in the above-mentioned Banking Rule, and adopts a combination of quantitative capital and adequate systems and controls in fulfilment of these requirements. The production of the ICAAP is led by the Risk Department, taking into consideration the Bank's Risk Appetite and underlying risk profile, as well as the external environment.

In this exercise, the Bank's capital requirements are set at a starting point of zero. A structured and comprehensive assessment and quantification of all the material risks are performed. This involves an analysis to determine whether the minimum regulatory requirements for Pillar I risks are sufficient to cover the Bank's credit, operational and market risk. Since the minimum regulatory requirement for credit risk was calibrated for internationally diversified banks and the Bank's operations are concentrated locally, additional capital is allocated to account for individual and sectoral concentration. This capital allocation is based on the results of an index-based model. For prudence purposes, the Bank allocates an extra portion of capital to operational risk to account for the rapid growth in its operations. The Bank also assesses and measures other risks to determine its capital requirements, namely:

- Interest rate risk in the banking book using the economic value approach; and
- A detailed analysis of controls and mitigation techniques for other risks, particularly reputation, legal, strategic, systemic and residual risks.

The latest ICAAP, which concluded that the Bank is adequately capitalised, was reviewed in detail by the Bank's Internal Audit Department and by the Risk Committee, and subsequently presented to the Board of Directors for approval. Following Board approval, the ICAAP Report was submitted to the regulator.

9.4 Leverage

The CRR introduced the Leverage Ratio, which measures the relationship between a bank's Tier 1 Capital and its on- and off-balance sheet exposures.

The Board of Directors approved the Bank's Leverage Risk Policy, the purpose of which is to set forth a framework for comprehensively identifying, managing, monitoring and reporting on leverage and the risk of excessive leverage. The Bank's leverage ratio is regularly reported to and monitored by the Executive Management, Risk Committee and Board. During 2018 the Bank's leverage ratio remained well above the regulatory minimum requirement of 3% and within the Bank's risk appetite. At 31 December 2018 the Group's leverage ratio stood at 6.86%.

REMUNERATION REPORT

Remuneration Governance

As from 1 September 2018, the Governance Committee, which until then also convened as Remuneration Committee, was reconstituted as the Governance and Conduct Committee and a separate Remuneration Committee was formed for that purpose.

Membership and meetings

The members of the Governance Committee until 31 August 2018 were:

– Arthur Galea Salomone – Chair (retired on 26 July 2018)
– Laragh Cassar
– Michael Pace Ross
– Victor Gusman
– Marcel Cassar (non-voting)

The Governance Committee met on four occasions during the period until 31 August 2018 and these meetings were attended by all members of the Committee. For the first four meetings the Governance Committee had the remit to convene itself as a Remuneration Committee.

The members of the Remuneration Committee with effect from 1 September 2018 are:

– Frederick Mifsud Bonnici – Chair
– Victor Gusman
– Laragh Cassar
– Marcel Cassar (non-voting)
– Ray Bonnici (non-voting)

No meetings of the Remuneration Committee were held until the end of year under review.

Remuneration Policy Statement

The approval of the Bank's Remuneration Policy is the responsibility of the Board of Directors (hereafter referred to as the "Board"). The Remuneration Policy (hereafter the "Policy") of APS Bank Limited and its subsidiaries (hereafter referred to as "APS Group") includes all categories of staff including senior management, risk takers and staff engaged in control functions. The application of the principles of Directive 2013/36/EU and of the EBA Guidelines on sound remuneration policies set out in this Policy take into account the nature and scale of APS Group and the complexity of its activities.

The Policy aims to enable APS Group to exercise a competent and independent judgement on its remuneration practices and its incentives created for managing risk. Its objective is to attract, retain and motivate high quality staff members and to ensure that staff compensation is aligned with the Bank's values, performance business strategy and prudent risk taking. The Bank's Remuneration Policy distinguishes between basic pay, performance bonus and other benefits and therefore has two main components – Fixed and Variable.

Fixed Remuneration

The base salary provides a predictable base level of income reflecting each staff member's level of responsibility, capabilities, skills and experience. Base salaries are reviewed annually, and increases are granted in line with performance and when a staff member assumes increased responsibilities or significantly deepens knowledge and expertise. Base salaries may also be reviewed when there is a material change in the remuneration levels of comparable roles in the respective market.

Variable Remuneration

Staff members may have a variable component to their remuneration in addition to their fixed remuneration. The relation between fixed and variable remuneration shall not exceed twenty five (25) per cent of the fixed component for each individual.

The variable portion is clearly connected to the work and performance of the staff member, the performance of his/her business unit and the overall performance of the Bank and its subsidiaries. The goals are based on factors that support APS Group's long-term strategy and business objectives.

Staff in Control Functions are adequately compensated in accordance with their own objectives and not directly tied to the results of any business unit. They are judged on their success in developing appropriate policies, developing effective risk management controls and procedures, monitoring risk and building control systems.

Bonuses related to individual performance are based on both quantitative and qualitative targets. Qualitative criteria considers (i) adherence to the applicable regulatory framework, (ii) treating customers fairly and (iii) the on-going provision of a high quality service to customers. Performance bonus and profit sharing schemes promote teamwork and encourage all staff members to perform to the best of their abilities, for their mutual benefit and the long-term sustainable success of APS Group.

APS Group ensures that bonuses are fair, transparent, easy to understand and based on the Bank's Business Plan and Annual Budgets. Any variable remuneration, be it monetary or non-monetary, outside the parameters of the Policy is referred to the Remuneration Committee for approval.

Variable remuneration does not include "clawback' provisions. APS Group does not offer buy out contracts, supplementary pension or other pension benefits and share options. Schemes relating to early termination are established within the Collective Agreement. There is also no remuneration that is subject to deferral.

During the year ended 31 December 2018, there were no new sign-on and severance payments made either to directors or members of the senior management of the Group.

The Remuneration Policy is reviewed internally on a regular basis and is updated when required. An updated Remuneration Policy was approved by the Board on 5 December 2017.

Identified Staff

The target population defined as Identified Staff for the purposes of this report (excluding those allocated to the Supervisory function) represents 13% of the total number of employees in the Group. Identified staff were determined in line with the Regulatory Technical Standard EU604/2014 regarding qualitative and appropriate quantitative criteria that came into force in June 2014 in order to identify the core categories of staff whose professional activities have a material impact on an institution's risk profile and includes:

– Non-executive directors that are responsible for providing a monitoring role;
– Senior management that are also responsible for certain business units; and
– Senior management responsible for business units/business lines of Finance, Support and Human Capital, as well as those responsible for internal audit and risk management functions.

For the purposes of remuneration, Identified Staff have been aggregated and split into business areas according to the European Banking Authority ("EBA") guidelines on the remuneration benchmarking exercise EBA/GL/2014/08 dated 16 July 2014. The tables in the sections that follow include total fixed and variable remuneration and the number of beneficiaries per and within each business area.

Non-Executive Directors

Non-executive Directors are non-employees and receive a fee for their services as Directors. They are not eligible to receive a base salary, fixed pay allowance, benefits, pension or any variable pay. Non-executive Directors are entitled to participate in a health insurance scheme.

The remuneration of the Chairman and the Non-Executive Directors of APS Bank and its subsidiaries is proposed by the Governance Committee and approved by the shareholders at the Annual General Meeting. Their remuneration is of a fixed fee and set at a level which:

- broadly reflects the rest of the market;
- reflect the competencies and contribution required; and
- reflect the extent of responsibilities and the number of board meetings and committee membership/s.

The table below includes Directors' Fees and Board Committees Fees received by the Chairman and ten non-executive Directors who held office during the financial year 2018. The total number of non-executive Directors at year end was eight as two Directors retired from office and two new Directors were appointed during 2018.

	€
As Chairman	50,000
As Chair of Board Credit Committee Jan – Oct 2018	14,000
As Directors and Members of Committees	195,434
	259,434

Senior Management, Material Risk Takers (MRTs) and other Identified Staff

The Chief Executive Officer makes a proposal regarding the remuneration of Senior Management, i.e. Chief Officers and Heads, to the Remuneration Committee for approval by the Committee. In considering the level of remuneration, the Chief Executive Officer ensures that it is in line with the Remuneration Policy and makes a clear distinction between fixed and variable remuneration. Remuneration of other MRTs and Identified Staff is managed by the Senior Management in terms of the Remuneration Policy, including the provisions of the Collective Agreement.

Basic fixed remuneration reflects relevant professional experience and organisational responsibility as set out in the staff member's position description. Variable remuneration reflects a sustainable and risk adjusted performance in excess of that required to fulfil the staff member's role and responsibilities. The factors that determine the extent a staff member shall participate in a bonus distribution shall include:

- reward for personal performance (both results and behaviour);
- performance of the Bank – achievement of planned profit targets;
- performance of the Department and Unit/Branch;
- adherence to all internal policies and procedures; and
- performance relative to risk and capital usage.

The remuneration plan for all other staff members, i.e. except for Senior Management, is governed by the Bank's Collective Agreement, with a clear distinction between fixed and variable remuneration.

The variable remuneration is arrived at by calculating 10% of the excess over a pre-determined benchmark profit before tax based on 10% of the Bank's own funds at the beginning of the year under evaluation. Upon the recommendation of the CEO, the Board also authorises additional variable remuneration outside the structures of the Collective Agreement where this is especially merited.

The table below includes total fixed and variable remuneration for all thirty-nine Identified Staff, excluding non-executive directors, during the financial year 2018:

	€	%
Fixed remuneration	2,321,451	90
Variable remuneration	266,737	10
	2,588,188	**100**

The table below shows total fixed and variable remuneration for Identified Staff during the financial year 2018 broken down by business area, senior management and members of staff whose actions have a material impact on the risk profile of the institution.

	Management Function	Portfolio Management and Wealth Management	Retail Banking	Asset Liability Management	Corporate Functions	Independent Control Functions
Senior Management						
Number of Identified Staff	15					
Total Fixed Remuneration (€)[1]	1,340,054					
Total Variable Remuneration (€)	147,501					
Material Risk Takers (non-senior management)						
Number of identified staff		5	3	3	5	8
Total fixed remuneration (€)[1]		199,933	159,230	77,523	230,689	314,022
Total variable remuneration (€)		24,826	29,867	6,827	24,684	33,032
Total						
Number of identified staff	**15**	**5**	**3**	**3**	**5**	**8**
Total fixed remuneration (€)[1]	**1,340,054**	**199,933**	**159,230**	**77,523**	**230,689**	**314,022**
Total variable remuneration (€)	**147,501**	**24,826**	**29,867**	**6,827**	**24,684**	**33,032**

[1] Total fixed remuneration comprises non-cash benefits specifically company car allowance.

CORPORATE GOVERNANCE STATEMENT

The Board of Directors (the "Board" or "Directors") of APS Bank Ltd (the "Bank") is committed to uphold the highest standards of corporate governance and to promote the Bank's culture, values and behaviours. The Annual Report includes the extent to which the Bank has adopted the 'Corporate Governance Guidelines for Public Interest Companies' (the "Guidelines") as well as the effective measures taken to ensure compliance with such Guidelines, and this in the interest of portraying to the stakeholders the commitment to excellence in corporate governance.

Guideline 1: The Board

The Board promotes the well-being of the Bank and is responsible for its general governance, its proper administration and management and the general supervision of its affairs. The Board is committed to continually improving its practices so that it can effectively discharge its role and responsibilities as the Bank's needs evolve. An overview of the Board's composition and evolving key governance practices follows.

During the year under review the Board continued to embrace the principles enunciated in the Board Charter, which serves as a guidance to the Board and its Committees in the exercise of their responsibilities. The Charter elaborates on the duties of the Directors and sets out in detail the key governance principles adopted by the Bank and the manner in which the Directors are expected to execute their powers and responsibilities, covering such areas as independence, conflicts of interest and conduct and performance at meetings.

As at the date of this Statement, the Board is currently composed of nine non-executive Directors, including the Chairman. As provided on page II, during the period under review two Directors, namely Dr Arthur Galea Salomone and Mr Frederick Micallef, retired during the Annual General Meeting that was held on 26 July 2018. On the same day Dr Ing. Joseph C. Attard was appointed as Director. Mr Victor E. Agius was appointed on 15 October 2018.

The Board seeks to have an appropriate mix of skills, expertise and experience to enable it to deal with current and emerging opportunities and issues and to effectively review the performance of management. Details of the current experience, qualifications and dates of appointment are also provided on pages IV to V. Appointment of Directors takes place following a rigorous and transparent selection process conducted by the Governance & Conduct Committee in terms of the Joint ESMA and EBA Guidelines on the Assessment of the Suitability of Members of the Management Body and Key Function Holders. This process is based on merit, taking into account the skills, experience and diversity needed on the Board in terms of the Bank's strategic direction. Once a candidate is nominated, an Assessment of Management Body is carried out at Board level that includes background checks as to fitness and properness.

The Board delegates specific responsibilities to the Committees it set up, explained in more detail hereunder.

As from the 2018 Annual General Meeting, the Board is assisted by a Company Secretary who forms part of the Bank's full-time staff complement. This followed a reorganisation that created the General Counsel Department, which includes a Company Secretarial Unit, which in turn oversees Corporate Governance and Investor Relations responsibilities. All Directors have access to the Company Secretary. In matters relating to the Board, the Company Secretary reports directly to the Chairman.

Guideline 2: The Chairman of the Board

The Chairman is appointed by the shareholders from amongst the Directors. He is responsible for leading the Board and setting its agenda for meetings, ensuring that the Directors receive precise, timely and objective information so that they can properly execute their duties, while encouraging their active engagement at meetings and on issues of a complex or contentious nature. The Chairman holds a non-executive function and is independent from the Chief Executive Officer, who in turn has executive powers, to ensure clear division of responsibilities at executive level.

Guideline 3: The Directors

The Bank's Articles of Association contain detailed provisions as to the manner of appointment and retirement of Directors. Directors hold office from the close of the Annual General Meeting at which they are appointed until the end of the subsequent General Meeting, at which they become eligible for re-election.

Each Director is expected to be an active participant in a Board that functions effectively as a whole. The Board balances longer-serving Directors with a deep knowledge of the Bank's operations and history, and newer Directors with fresh insights. The combined and varied knowledge and competences permit the Board to function properly in a dynamic environment. All Directors hold office in a non-executive capacity while they also actively participate in committees of the Board.

As at the date of this Statement, the Bank's Directors in office as from the 2018 Annual General Meeting, hold the following number of directorships, other than that as Director of the Bank or its subsidiaries:

Frederick Mifsud Bonnici – 2;
Victor E. Agius – Nil;
Joseph C. Attard – Nil;
Franco Azzopardi – 7;
Laragh Cassar – 4;
Alfred De Marco – 1;
Victor Gusman – 2;
Michael Pace Ross – 1;
Martin Scicluna – 5.

In terms of the 'Evaluation Policy and Procedure', at least once a year an evaluation takes place to assess the Board's performance and that of its individual Directors. The evaluation of a Director's performance is an integral part of the process for recommending or otherwise a Director's continuation in office. In 2018 an internal evaluation took place comprising a questionnaire that related to the Board as a whole and a self-assessment evaluation. Summarily, the evaluation looked into the respective roles and responsibilities of the Board and its Committees; the adequacy of the Board's processes; the sufficiency of reporting to the Board and the robustness of discussion at strategy and operational level.

All Board Directors have exposure to good corporate governance practices and are committed to acting ethically.

Guidelines 4 and 5: The Responsibilities of the Board and Board Meetings

The Board conducts itself in a manner which ensures effective execution of its functions to set strategy and formulate policy as well as to exercise stewardship and oversight.

The Board meets regularly, typically on the last Thursday of the month and meetings are preceded by a more casual, offsite gathering on the eve of each meeting, usually over dinner, where Directors have the opportunity to discuss the Agenda informally. During the year under review, the Board met 15 times. Directors are knowledgeable of their expected time commitment towards the Bank. During 2018, all meetings were attended by the large majority of Directors and the average rate of attendance was of 96.5%. Further meetings are held if required for the Board to discharge its duties effectively.

The Board approves and oversees the implementation of the Bank's strategic objectives and sets the Bank's risk tolerance through policy approval. Board agendas invariably include discussions and decisions on strategic matters, detailed update presentations by the CEO, structured reporting from the Committees and Subsidiaries, open discussion with Management on business and risk topics as well as regulatory briefings and updates. After each Board Meeting, Minutes are drawn up by the Company Secretary and circulated to all Directors. Minutes faithfully record the attendance of Directors at said Meetings, matters discussed, the discussion and considerations made and decisions taken.

Committees

During the period under review, the Board of Directors continued to strengthen the respective roles and responsibilities of the Board and Management Committees. The Governance Committee has been renamed 'Governance & Conduct Committee' with a wider mandate to oversee 'Conduct' issues. Concurrently a new, separate Remuneration Committee was created with its remit now focused to a standalone Committee and no longer falls under that of the Governance & Conduct Committee. Similarly, a revised mandate was given to the IT Steering Committee which now focuses more on 'Technology & Innovation'. A Compliance Committee was also created as a Management committee reporting to the Risk Committee, with a remit that covers compliance controls, on-boarding and exiting of customer relationships and a range of regulatory compliance matters. Due to the enlarged Senior Management presence as a result of continued organisational growth, the Executive Committee, which meets at least monthly, was separated from the Management Committee, which continues to meet weekly.

Each Committee has its own Terms of Reference, setting out the Committee's mandate, scope and working procedure. Minutes are kept of all the business transacted in the course of Committee meetings. All Directors have access to Committee papers and Minutes, which are also tabled at Board meetings. Committee Chairs report on Committee business at the subsequent Board meetings.

During the year under review the Board also continued to strengthen its oversight of the Bank's subsidiary, ReAPS Asset Management Limited, with additional reporting obligations implemented at Board level.

Board Committees:

1. **Audit Committee:**

The role of the Audit Committee is to monitor the financial reporting process, including the audit of the annual accounts and review of any interim reporting, to review proposed transactions by the Bank with related parties and to oversee the standards/performance of the Internal Audit Unit, whilst approving and monitoring its Audit Plan. The Committee also monitors the effectiveness of the internal control environment and accounting framework. It considers the adequacy of contingency plans for processing and production of financial information. The Audit Committee reviews the external auditor's independence, in particular the provision of additional services to the Bank and liaises between external auditors, internal audit, the Board and Management.

2. **Risk Committee:**

The Risk Committee recommends the Bank's risk profile and proposes its risk appetite statement for approval by the Board of Directors, whilst periodically reviewing the Bank's risk management framework. It reviews strategic decisions, including new products and markets, acquisitions, and disposals, from a risk perspective while it keeps sight of regulatory and market developments and how these can impact on the Bank's risk appetite. The Risk Committee approves risk policies, limits and delegations, including those of the Credit Committees. It has a wide mandate for risk oversight, including credit risk, market risk, operational risk, technology/cyber risk, concentration risk, liquidity risk as well as compliance matters. The Committee considers impairment and provisioning recommendations as prepared by Management and recommends them for adoption, risk reporting in the financial statements and the process of compilation of reports such as ICAAP, ILAAP and Recovery Plans, amongst others.

3. **Governance & Conduct Committee:**

The Governance & Conduct Committee acts as first point of reference on Board governance policies and procedures, codes of conduct and conflicts of interest. The Committee oversees the structure and performance of the Bank's committees, whilst itself performing the function of Nomination Committee, besides steering the process of directors' evaluation, both individually and collectively as a Board. The Committee considers and approves senior executive appointments and assesses the performance of the CEO. With respect to Conduct, the Committee oversees the brand, valued behaviours and reputation of the Bank, by covering the review of brand positioning, the Bank's culture, compliance with stated values and reputational risk management.

4. **Board Credit Committee:**

The Board Credit Committee (or 'BCC') receives and reviews credit applications and approves credit limits for customers and transactions, within the parameters set by the Board in terms of the credit policy procedures. It also receives and reviews updates/amendments to approved facilities and approves, or delegates approval, for deviations as the case may be. The BCC considers and advises the Risk Committee on credit limits and/or any matter for approval (e.g. country, geographic, segment limits) when this is required according to the Bank's credit policy. The BCC may delegate its limits to the Management Credit Committee, composed only of Management.

5. **Remuneration Committee:**

The Remuneration Committee is responsible for informing, advising and supporting the Board of Directors on the design, revision and implementation of the Remuneration Policy. Within the ambit of that Policy, it is also responsible for considering specific remuneration arrangements and schemes.

6. Technology & Innovation Committee:

The Technology & Innovation Committee oversees management with regard to IT-related risks, security and business continuity plans. It intervenes with the Board to secure sponsorships and support for the main IT strategic decisions & projects. The Technology & Innovation Committee provides strategic leadership through a steady flow of innovative ideas that will serve as a catalyst for innovation at the Bank as well as monitoring IT project implementation.

Management Committees:

1. **Executive Committee:**

The Executive Committee (or 'EXCO') acts as consultative body and advisor to the CEO on matters such as strategy, operations and business. It reviews and debates relevant items before consideration by the Board/Board Committees and escalates key issues. The focus of EXCO meetings and deliberations is on the four Ps, namely Performance, Products, Projects and People, and these four broad areas describe adequately the coverage of this Committee. It approves capital commitments and transactions within its delegated authority and recommends for Board approval the annual capital and revenue budgets, monitors KPIs, KRIs and financial performance on an ongoing basis. The EXCO has first line of oversight of the control frameworks, receiving and considering reports of operational reports, including serious service/product complaints and/or incidents.

2. **Management Committee**

The Management Committee brings together the most senior levels of management, essentially Chief Officers and Heads, in a weekly forum where all members share updates about their respective areas of responsibility, work plans as well as matters or items of significant interest. The Management Committee reports into the EXCO, with which it also works very closely especially because all members are common. Meetings of the Management Committee are characterised by their regular frequency, tour-de-table style and informality, which serves to instil a high degree of communication and collaboration between the members.

3. **Assets & Liabilities Committee:**

The Assets and Liabilities Committee (or 'ALCO') is generally responsible for the asset liability management ('ALM') strategy, policy, surveying of market developments, including the Bank's Base Rate and funding strategy. It monitors interest rate, liquidity and currency risks and determines treasury strategy accordingly. Liquidity management and contingency planning are another important area of focus of ALCO and in the determination of liquidity strategy. The scope and attention of the ALCO are also on optimising capital allocation in terms of ALM strategy and regulatory requirements. The ALCO instigates the development of new treasury (funding and lending) products and approves and monitors the Bank's Funds Transfer Pricing (FTP) framework and its components, monitors implementation and reviews results. It also regularly appraises Bank performance in terms of ALM strategy.

4. **Management Credit Committee:**

The Management Credit Committee (or 'MCC') receives and reviews credit applications and approves credit limits for customers and transactions, within the parameters set by the BCC in terms of the credit policy and procedures. It refers and recommends to the BCC limit applications where these exceed its (MCC) limits. The Committee receives and reviews updates/amendments to approved facilities and approves, or delegates approval, for deviations as the case may be, and considers and advises the BCC on credit limits and/or any matter for approval that is within its (BCC) competence.

5. **Compliance Committee**

The Compliance Committee ensures that prescribed regulations, rules, policies, guidelines and procedures are being followed and also anticipated in advance. It also acts as a decision point for business acceptance, on-boarding and dismissal of customers, in line with the Bank's on-boarding and exit policies. It ensures that the Bank's Compliance function takes a holistic as well as balanced view of compliance risk. The Compliance Committee reports to the Risk Committee.

Guideline 6: Information and Professional Development

Upon appointment, all Directors are offered familiarisation of the Bank by the Chairman and CEO. During 2018 a more formal, customised induction programme started to be provided to new Directors by the Company Secretary. This includes providing an overview of the Bank's Memorandum and Articles of Association, Board Charter and key policies and practices relevant to the Board. The induction programme also includes briefings from the CFO, CRO and Heads of business and support department. Access to the services and resources of the Bank, including, where necessary, independent professional advice at the Bank's expense, are also available.

During the year under review the Board underwent collective training in various areas mainly concerning governance, risk, digital innovation and regulatory matters. Individual Board members also attend specific training and seminars from time to time, according to the topic and subject matter covered. Directors are also kept abreast by Management on aspects that help them in the professional discharge of their functions as Board and Committee members. The high standards of continuing professional development embedded in the Bank's culture run across the entire organisation and include the Board.

The Board members were also involved in the formulation of the 2019-2021 Business Plan and engaged in various offsite events, with Management and external consultants, that served to enrich the outcome and quality of the final Plan. Close liaison with members of Management also takes place specifically at the levels of Board committee chairs, particularly in the areas of Risk and Audit, where this is required because of independence considerations.

Guideline 7: Relations with Shareholders

The shareholders are served with the statutory notice to attend the Annual General Meeting which is normally held during the second quarter of the year. The notice contains all the resolutions proposed for approval by the Annual General Meeting, where the Annual Report and Audited Financial Statements are approved. The Board also considers the Annual Report to be an effective document which contains detailed information about the Bank's performance and can therefore serve as a medium for interested parties, not least the shareholders, to find out more about the Bank in a transparent fashion.

The Board also recognises the importance of maintaining a regular dialogue with its majority shareholders, being AROM Holdings Ltd (Archdiocese of Malta) and the Diocese of Gozo. This ensures a flow of communication about the Bank's strategy and updates on performance. These meetings are conducted in a structured manner and also include meetings with the full Board.

On a periodic basis, meetings with staff, intermediaries, analysts and institutions are also held where information about the Bank's progress, activities and financial performance is disseminated. These encounters are very useful as they enable the Bank to reach out to a wider band of stakeholders. The presentation of the annual financial results is one particular opportunity where the shareholders are also invited to receive a detailed appraisal of the Bank's performance and outlook for the current year.

Guideline 8: Conflicts of Interest

Each Director is expected to act to the highest standards of ethical behaviour and fiduciary duties. The Directors are aware of their obligation to avoid conflicts of interest and their responsibility to act in the interest of the Bank and its shareholders as a whole irrespective of which shareholder nominated him/her to the Board.

The Board Charter contains specific sections dealing with conflicts of interest, starting with the general precept that Directors should take all reasonable steps to avoid such situations. However, from time to time, actual or potential conflicts of interest may arise in which case it needs to be ensured that these are managed properly by the Board and the interested Director, as also provided in the amended Conflicts of Interest Policy. Directors are required to inform the Board of any matter that may result or has already resulted in a conflict of interest. A record of such declaration is entered into the Bank's minute books and the said Director is precluded from voting in any resolution concerning a matter in respect of which he/she has declared a direct or indirect interest.

Guideline 9: Corporate Social Responsibility

The Board of Directors encourages that sound principles of corporate social responsibility are adhered to and integrated into the core business ethos of the Bank and embedded into the Bank's day-to-day culture and operations. As a result, the Bank is a prominent supporter of various CSR initiatives at both national and community level aimed at contributing to economic, societal, environmental and cultural development.

Through its endorsement of a variety of such priorities and programmes, the Bank promotes positive social change as well as a sense of common good. Details of the main CSR milestones achieved during 2018 are elaborated upon in other parts of the Annual Report.

INDEPENDENT AUDITOR'S REPORT

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of APS Bank Limited (the Bank) and the consolidated financial statements of the Bank and its subsidiaries (together, the Group), set out on pages 23 to 97, which comprise the statements of financial position as at 31 December 2018, and the statements of profit or loss and other comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank and the Group as at 31 December 2018, and of the Bank's and the Group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and have been properly prepared in accordance with the requirements of the Companies Act (Cap.386) and the Banking Act (Cap.371).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank and the Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (IESBA Code) together with the Accountancy Profession (Code of Ethics for Warrant Holders) Directive* (Maltese Code) that are relevant to our audit of the financial statements in Malta, and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code and the Maltese Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion. In conducting our audit, we have remained independent of the Bank and the Group and have not provided any of the non-audit services prohibited by article 18A (1) of the Accountancy Profession Act (Cap. 281).

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. The key audit matters described below pertain to the audit of both the individual and consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Impairment of loans and advances to customers

On 1 January 2018, a new accounting standard for financial instruments (IFRS 9) became effective, which introduced the requirement for the impairment provision on loans and advances to customers to be based on expected credit losses at the date of the statement of financial position, rather than basing the provision on incurred losses at that date as previously applied under the preceding accounting standard (IAS 39). Transitional rules in the new standard regulate the change in the basis of assessment of the impairment provision. This is a significant change and is a matter of applied estimation and judgement by the directors that is material to the financial statements. At 31 December 2018 the Group and Bank reported total gross loans and advances of EUR1,270,685,000 and EUR16,802,000 of expected credit loss provisions.

Key judgements and estimates in respect of the timing and measurement of expected credit losses (ECL) include:

- Grouping of assets by extent of potential impairment (stage 1, 2, or 3) using criteria in accordance with the accounting standard;
- Accounting interpretations and modelling assumptions used to build the models that calculate the ECL;
- Completeness and accuracy of data used to calculate the ECL;
- Inputs and assumptions used to estimate the impact of multiple economic scenarios;
- Completeness and valuation of post model adjustments (management overlays);
- Measurements of individually assessed provisions including the assessment of multiple scenarios; and
- Accuracy and adequacy of the financial statement disclosures.

Our audit response to address the risk of material misstatement arising from this change in accounting requirements comprised the following:

- As IFRS 9 was adopted at the beginning of the financial year, we performed audit procedures on the opening balances to gain assurance on the transition from IAS 39. This included evaluating the accounting interpretations for compliance with IFRS 9 and testing the adjustments and disclosures made on transition by the Group and Bank.
- We tested the design and operating effectiveness of the Group's and Bank's key controls across the processes relevant to the ECL calculation. These Group and Bank processes included model governance, the allocation of assets into stages, data accuracy and completeness, preparation of multiple economic variables and scenarios, post model adjustments, individual provisions and disclosures:
  - We reviewed the composition of the Group's and Bank's project working group and also reviewed the minutes of meetings held, where the inputs, assumptions and adjustments to the ECL were discussed and approved.
  - We challenged the criteria used to allocate an asset to stage 1, 2 or 3 in accordance with IFRS 9. We tested assets in stage 1, 2 and 3 to verify that they were allocated to the appropriate stage.
  - To verify data quality, we tested the data used in the ECL calculation by reconciling to source systems. To test credit monitoring, we recalculated the risk ratings (credit gradings) for a sample of performing loans.
  - With the support of our internal modelling specialists, we tested the assumptions,

- inputs and formulas used. This included assessing the appropriateness of model design and formulas used, considering alternative modelling techniques and recalculating the Probability of Default, Loss Given Default and Exposure at Default for a sample of models.
  - We assessed whether the macroeconomic variables were appropriate for the model, such as GDP, unemployment and inflation rates. With the support of our modelling specialists we challenged the correlation and impact of the macroeconomic factors to the ECL.
  - We assessed the completeness and appropriateness of post model adjustments and recalculated a sample.
- We performed an overall assessment of the ECL provision levels by stage to determine if they were reasonable considering the Group and Bank's portfolio, risk profile, credit risk management practices and the macroeconomic environment. We considered trends in the economy and industries to which the Group and Bank are exposed.
- For a sample of individually impaired loans we evaluated the specific circumstances of the customer, including latest available information, the basis for measuring the impairment provision, and whether key judgements were appropriate. We re-performed management's impairment calculations, which were largely based on the expected recovery from collateral held. We tested the valuation of collateral challenging subjective estimates by referring to actual historical recovery data.
- We assessed the adequacy and appropriateness of disclosures for compliance with the accounting standards, including disclosure of the transition from IAS 39.

The Group and Bank's disclosures about impairment are included in Notes 2.3, 10, 15 and 42, which include the directors' assessment of the adequacy of the impairment provisions. Notes in relation to transition to IFRS 9 have been disclosed in note 2.2.

Information Other than the Financial Statements and the Auditor's Report Thereon

The directors are responsible for the other information. The other information comprises the following - Bank information, Board of Directors, Directors' Report, Capital adequacy and risk disclosures report, Remuneration report, Corporate governance statement and Five year summaries, the Chairman's statement and the CEO's review. However, the other information does not include the individual and consolidated financial statements and our auditor's report thereon.

Except for our opinion on the Directors' Report in accordance with the Companies Act (Cap. 386), our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

With respect to the Directors' Report, we also considered whether the Directors' Report includes the disclosure requirements of article 177 of the Companies Act (Cap. 386).

In accordance with the requirements of sub-article 179(3) of the Companies Act (Cap. 386) in relation to the Directors' Report on pages 2 to 5, in our opinion, based on the work undertaken in the course of the audit:

- The information given in the Directors' Report for the financial year for which the financial statements are prepared is consistent with those financial statements; and
- The Directors' Report has been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Directors' Report.

Responsibilities of the directors and the Audit Committee for the Financial Statements

As explained more fully in the Statement of directors' responsibilities on page 5, the directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Companies Act (Cap.386) and the Banking Act (Cap.371), and for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Bank's and the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Bank and the Group or to cease operations, or have no realistic alternative but to do so.

The directors have delegated the responsibility for overseeing the Bank's and the Group's financial reporting process to the Audit Committee.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the 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 financial statements.

In terms of article 179A(4) of the Companies Act (Cap. 386), the scope of our audit does not include assurance on the future viability of the audited entity or on the efficiency or effectiveness with which the directors have conducted or will conduct the affairs of the entity.

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 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 Bank's and the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' 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 the Bank's and the Group's ability 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 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 Bank or the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the 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 the Audit Committee 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 the Audit Committee 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 the Audit Committee, we determine those matters that were of most significance in the audit of the 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.

Report on Other Legal and Regulatory Requirements

Additional matters on which we are required to report pursuant to the Banking Act (Cap. 371)

In our opinion:

- Proper accounting records have been kept so far as it appears from our examination thereof;
- The financial statements are in agreement with the accounting records; and
- We have obtained all the information and explanations which, to the best of our knowledge and belief, are necessary for the purpose of our audit.

Matters on which we are required to report by exception pursuant to the Companies Act (Cap. 386) in addition to those reported above.

We have responsibilities to report to you if in our opinion:

- Proper returns adequate for our audit have not been received from branches not visited by us; or
- The financial statements are not in agreement with the returns.

We have nothing to report to you in respect of these responsibilities.

Auditor tenure

We were first appointed to act as statutory auditor of the Bank and its Group by the members of the Bank on 27 July 2017 for the financial year ended 31 December 2017, and were subsequently reappointed as statutory auditor by the members of the Company on an annual basis. The period of total uninterrupted engagement as statutory auditor of the firm is 2 financial years.

Consistency of the audit report with the additional report to the Audit Committee

Our audit opinion is consistent with the additional report to the Audit Committee in accordance with the provisions of article 11 of the EU Audit Regulation No. 537/2014.

Sarah Curmi as Director
in the name and on behalf of
Deloitte Audit Limited

Registered auditor
Mriehel, Malta.

21 March 2019

STATEMENTS OF PROFIT OR LOSS

For the year ended 31 December 2018

		The Group		The Bank	
		2018	2017	2018	2017
	Note	€000	€000	€000	€000
Interest receivable and similar income:					
On loans and advances, balances with the Central Bank of Malta and treasury bills	(3)	40,947	31,861	40,940	31,861
On debt securities:					
Measured at amortised cost (2017: held-to-maturity)		3,643	4,256	3,643	4,256
Amortisation on premiums and discounts on debt securities measured at amortised cost (2017: held-to-maturity)		(477)	(296)	(477)	(296)
Measured at fair value through profit or loss (FVTPL)		1,020	186	22	74
Other debt securities		5,858	7,748	5,858	7,748
Amortisation on premiums and discounts on other debt securities		(1,028)	(1,359)	(1,028)	(1,359)
	(3)	9,016	10,535	8,018	10,423
Total interest receivable and similar income		49,963	42,396	48,958	42,284
Interest payable	(4)	(12,149)	(9,592)	(12,182)	(9,592)
Net interest income		37,814	32,804	36,776	32,692
Dividend income	(5)	575	214	1,604	656
Fees and commission income		6,179	4,956	6,120	5,390
Gains/(losses) on foreign exchange	(6)	260	299	446	418
Net (losses)/gains on financial instruments	(7)	(674)	3,349	153	3,356
Other operating income		565	1,128	565	436
Operating income		44,719	42,750	45,664	42,948
Personnel expenses	(8)	(13,534)	(11,148)	(13,534)	(11,148)
Fees and commission expenses	(9)	(405)	(554)	(405)	(554)
Other administrative expenses	(9)	(8,763)	(8,780)	(8,616)	(8,617)
Amortisation of intangible assets	(26)	(774)	(840)	(773)	(840)
Depreciation of property and equipment	(25)	(1,099)	(1,041)	(1,099)	(1,041)
Net operating profit before associates' results & impairment gains & losses		20,144	20,387	21,237	20,748
Share of results of associates, net of tax	(22)	38	441	-	-
Operating profit before impairment gains and losses		20,182	20,828	21,237	20,748
Net impairment losses	(10)	(1,555)	(2,470)	(1,555)	(2,470)
Profit before tax		18,627	18,358	19,682	18,278
Income tax expense	(11)	(6,043)	(5,250)	(5,974)	(5,190)
Profit for the year		12,584	13,108	13,708	13,088
Profit for the year attributable to:					
Equity holders of the parent		12,610	13,110	13,708	13,088
Non-controlling interest		(26)	(2)	-	-
		12,584	13,108	13,708	13,088

STATEMENTS OF COMPREHENSIVE INCOME

For the year ended 31 December 2018

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Profit for the year	**12,584**	13,108	**13,708**	13,088
Other comprehensive income:				
Items that may be reclassified subsequently to profit or loss:				
Change in fair value on available-for-sale financial assets	**-**	(2,406)	**-**	(2,406)
Release of fair value on disposal of available-for-sale financial assets	**-**	(4,070)	**-**	(4,070)
Change in fair value on debt instruments measured at fair value through other comprehensive income (FVTOCI)	**(4,432)**	-	**(4,432)**	-
Release of fair value on disposal of debt instruments measured at fair value through other comprehensive income (FVTOCI)	**(183)**	-	**(183)**	-
Deferred income tax relating to the components of other comprehensive income	**879**	1,195	**879**	1,195
Other comprehensive loss for the year, net of tax	**(3,736)**	(5,281)	**(3,736)**	(5,281)
Total comprehensive income for the year, net of tax	**8,848**	7,827	**9,972**	7,807
Total comprehensive income attributable to:				
Equity holders of the parent	**8,910**	7,829	**9,972**	7,807
Non-controlling interest	**(62)**	(2)	**-**	-
	8,848	7,827	**9,972**	7,807

STATEMENTS OF FINANCIAL POSITION

As at 31 December 2018

		The Group		The Bank	
		2018	2017	**2018**	2017
	Note	**€000**	€000	**€000**	€000
ASSETS					
Cash and Balances with Central Bank of Malta	(13)	**175,408**	89,539	**174,511**	86,449
Cheques in course of collection		**69**	39	**69**	39
Loans and advances to banks	(14)	**50,384**	33,246	**49,384**	32,246
Loans and advances to customers	(15)	**1,253,883**	998,377	**1,253,883**	998,377
Syndicated loans	(16)	**61,610**	26,213	**61,610**	26,213
Derivative financial instruments	(17)	**822**	3,008	**822**	3,008
Financial assets at FVTPL	(18)	**36,241**	37,045	**879**	942
Other debt and fixed income instruments	(19)	**251,040**	252,324	**251,040**	252,324
Equity and other non-fixed income instruments	(20)	**1,272**	1,793	**1,272**	1,793
Investment in subsidiaries	(21)	**-**	-	**40,250**	40,250
Investment in associates	(22)	**17,748**	18,224	**14,887**	14,887
Non-Current assets held for sale	(23)	**2,600**	-	**2,600**	-
Investment properties	(24)	**1,860**	4,203	**1,860**	4,203
Property and equipment	(25)	**22,286**	17,706	**22,286**	17,706
Intangible assets	(26)	**5,861**	5,093	**5,858**	5,089
Deferred tax assets	(27)	**3,853**	2,985	**3,853**	2,985
Other receivables	(28)	**6,293**	6,650	**5,845**	6,122
TOTAL ASSETS		**1,891,230**	1,496,445	**1,890,909**	1,492,633
LIABILITIES					
Amounts owed to banks	(29)	**74,473**	111,132	**74,473**	111,132
Derivative financial instruments	(17)	**822**	3,008	**822**	3,008
Amounts owed to customers	(30)	**1,650,308**	1,225,576	**1,653,309**	1,226,382
Current tax		**1,389**	198	**1,321**	138
Other liabilities	(31)	**11,892**	9,530	**11,892**	9,530
Accruals	(32)	**10,102**	10,598	**10,077**	10,533
TOTAL LIABILITIES		**1,748,986**	1,360,042	**1,751,894**	1,360,723
EQUITY					
Issued capital	(33)	**57,605**	57,605	**57,605**	57,605
Share premium	(34)	**1,770**	1,770	**1,770**	1,770
Revaluation reserve	(35)	**12,398**	15,896	**12,398**	15,896
Retained earnings	(36)	**68,478**	60,032	**67,242**	56,639
Attributable to equity holders of the parent		**140,251**	135,303	**139,015**	131,910
Non-controlling interest		**1,993**	1,100	**-**	-
TOTAL EQUITY		**142,244**	136,403	**139,015**	131,910
TOTAL LIABILITIES AND EQUITY		**1,891,230**	1,496,445	**1,890,909**	1,492,633
MEMORANDUM ITEMS					
Contingent liabilities	(37)	**23,269**	10,834	**23,269**	10,834
Commitments	(38)	**711,160**	552,000	**711,160**	552,000

The financial statements on pages 23 to 97 were authorised for issue by the Board of Directors on 21 March 2019 and were signed by:

F. MIFSUD BONNICI
Chairman

F.AZZOPARDI
Director

M. CASSAR
Chief Executive Officer

N. MCCARTHY
Chief Financial Officer

STATEMENTS OF CHANGES IN EQUITY

For the year ended 31 December 2018

THE GROUP	Attributable to the equity holders of the parent							
	Issued capital €000	Share premium €000	Revaluation reserve €000	Dividend reserve €000	Retained earnings €000	Total €000	Non-controlling interest €000	Total equity €000
FINANCIAL YEAR ENDED 31 DECEMBER 2018								
Balance at 1 January 2018								
As previously reported	57,605	1,770	15,896	-	60,032	135,303	1,100	136,403
Effect of change in accounting policy upon first time adoption of IFRS 9 (note 2.2)	-	-	238	-	(364)	(126)	-	(126)
Adjusted balance at 1 January 2018	**57,605**	**1,770**	**16,134**	**-**	**59,668**	**135,177**	**1,100**	**136,277**
Profit for the year	-	-	-	-	12,610	12,610	(26)	12,584
Other comprehensive loss	-	-	(3,736)	-	-	(3,736)	-	(3,736)
Total comprehensive (loss) / income	**-**	**-**	**(3,736)**	**-**	**12,610**	**8,874**	**(26)**	**8,848**
Dividends paid (note 12)	-	-	-	-	(3,676)	(3,676)	(32)	(3,708)
Retained earnings adjustment due to tax	-	-	-	-	(124)	(124)	-	(124)
Net share capital issued in subsidiary company	-	-	-	-	-	-	951	951
Balance at 31 December 2018	**57,605**	**1,770**	**12,398**	**-**	**68,478**	**140,251**	**1,993**	**142,244**
FINANCIAL YEAR ENDED 31 DECEMBER 2017								
Balance at 1 January 2017	**57,605**	**1,770**	**21,177**	**1,188**	**47,648**	**129,388**	**-**	**129,388**
Profit for the year	-	-	-	-	13,110	13,110	(2)	13,108
Other comprehensive loss	-	-	(5,281)	-	-	(5,281)	-	(5,281)
Total comprehensive (loss) / income	**-**	**-**	**(5,281)**	**-**	**13,110**	**7,829**	**(2)**	**7,827**
Reversal of retained earnings on liquidation of subsidiary	-	-	-	-	36	36	-	36
Net share capital issued in subsidiary company	-	-	-	-	-	-	1,102	1,102
Dividends paid (note 12)	-	-	-	(1,188)	(762)	(1,950)	-	(1,950)
Balance at 31 December 2017	**57,605**	**1,770**	**15,896**	**-**	**60,032**	**135,303**	**1,100**	**136,403**

THE BANK	Issued capital €000	Share premium €000	Revaluation reserve €000	Dividend reserve €000	Retained earnings €000	Total €000
FINANCIAL YEAR ENDED 31 DECEMBER 2018						
Balance at 1 January 2018						
As previously reported	57,605	1,770	15,896	-	56,639	131,910
Effect of change in accounting policy upon first time adoption of IFRS 9 (note 2.2)	-	-	238	-	(364)	(126)
Adjusted balance at 1 January 2018	**57,605**	**1,770**	**16,134**	**-**	**56,275**	**131,784**
Profit for the year	-	-	-	-	13,708	13,708
Other comprehensive loss	-	-	(3,736)	-	-	(3,736)
Total comprehensive (loss) / income	**-**	**-**	**(3,736)**	**-**	**13,708**	**9,972**
Dividends paid (note 12)	-	-	-	-	(2,617)	(2,617)
Retained earnings adjustment due to tax	-	-	-	-	(124)	(124)
Balance at 31 December 2018	**57,605**	**1,770**	**12,398**	**-**	**67,242**	**139,015**
FINANCIAL YEAR ENDED 31 DECEMBER 2017						
Balance at 1 January 2017	57,605	1,770	21,177	1,188	44,313	126,053
Profit for the year	-	-	-	-	13,088	13,088
Other comprehensive loss	-	-	(5,281)	-	-	(5,281)
Total comprehensive (loss) / income	**-**	**-**	**(5,281)**	**-**	**13,088**	**7,807**
Dividends paid (note 12)	-	-	-	(1,188)	(762)	(1,950)
Balance at 31 December 2017	**57,605**	**1,770**	**15,896**	**-**	**56,639**	**131,910**

STATEMENTS OF CASH FLOWS

For the year ended 31 December 2018

	Note	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
OPERATING ACTIVITIES					
Interest and commission receipts		**47,976**	37,955	**47,713**	37,696
Interest and commission payments		**(11,426)**	(9,892)	**(12,182)**	(9,592)
Cash paid to employees and suppliers/depositors		**(22,699)**	(17,420)	**(22,633)**	(17,333)
Operating profit before changes in operating assets and liabilities		**13,851**	10,643	**12,898**	10,771
(Increase)/decrease in operating assets					
Loans and advances to customers		**(292,617)**	(221,199)	**(292,617)**	(221,199)
Loans and advances to banks		**-**	11,362	**-**	11,362
Reserve deposit with Central Bank of Malta		**(3,360)**	(1,494)	**(3,360)**	(1,494)
Cheques in course of collection		**(30)**	3	**(30)**	3
Other assets		**(14)**	(257)	**-**	-
Increase/(decrease) in operating liabilities					
Amounts owed to customers		**423,796**	126,691	**423,919**	126,820
Amounts owed to banks		**(441)**	74,510	**(441)**	74,510
Other liabilities		**5,730**	(994)	**5,686**	(1,168)
Cash from/(used in) operating activities before tax		**146,915**	(735)	**146,055**	(395)
Income tax paid		**(5,071)**	(5,302)	**(5,011)**	(5,302)
Net cash flows from/(used in) operating activities		**141,844**	(6,037)	**141,044**	(5,697)
INVESTING ACTIVITIES					
Dividends received		**596**	126	**1,604**	588
Interest income from debt securities		**9,546**	12,074	**9,546**	12,074
Purchase of financial assets measured at amortised cost		**(38,997)**	-	**(38,997)**	-
Purchase of held-to-maturity financial assets		**-**	(155)	**-**	(155)
Proceeds on maturity of financial assets measured at amortised cost		**25,174**	-	**25,174**	-
Purchase of debt instruments measured at FVTOCI		**(6,617)**	-	**(6,617)**	-
Purchase of available-for-sale debt instruments		**-**	(12,584)	**-**	(12,584)
Proceeds on disposal of debt instruments measured at FVTOCI		**16,023**	-	**16,023**	-
Proceeds on disposal of available-for-sale financial assets		**-**	79,412	**-**	79,412
Purchase of financial assets at FVTPL		**(30,124)**	(38,595)	**(184)**	(502)
Proceeds on disposal of financial assets at FVTPL		**26,741**	2,766	**221**	2,350
Proceeds on disposal of equity and other non-fixed income instruments		**397**	2,055	**397**	2,055
Investment in subsidiary		**-**	-	**-**	(40,000)
Purchase of property, equipment and intangible assets		**(7,543)**	(4,064)	**(7,543)**	(4,059)
Proceeds on disposal of property and equipment		**7**	31	**7**	31
Net cash flows (used in)/from investing activities		**(4,797)**	41,066	**(369)**	39,210
FINANCING ACTIVITIES					
Dividends paid		**(2,135)**	(1,478)	**(2,617)**	(1,950)
Amounts paid on redemption of units in subsidiary		**(64)**	(50)	**-**	-
Net proceeds from issue of units in subsidiary		**1,017**	1,152	**-**	-
Net cash flows used in financing activities		**(1,182)**	(376)	**(2,617)**	(1,950)
Net increase in cash and cash equivalents		**135,865**	34,653	**138,058**	31,563
Cash and cash equivalents at 1 January		**75,113**	40,460	**72,023**	40,460
Cash and cash equivalents at 31 December	(40)	**210,978**	75,113	**210,081**	72,023

NOTES TO THE FINANCIAL STATEMENTS

1. CORPORATE INFORMATION

APS Group comprises APS Bank Limited, APS Consult Limited (liquidated), ReAPS Asset Management Limited and APS Diversified Bond Fund (a sub-fund of APS Funds SICAV p.l.c.).

APS Bank Limited is incorporated and domiciled in Malta as a limited liability company under the Companies Act, Cap. 386 of the Laws of Malta. ReAPS Asset Management Limited, a fully owned subsidiary of the Bank was incorporated in October 2016 as a private limited liability company under the Companies Act, Cap. 386 of the Laws of Malta. It is licensed by the Malta Financial Services Authority to provide investment services in terms of the Investment Services Act, Cap. 370 of the Laws of Malta and the investment services licence issued by the MFSA. APS Funds SICAV p.l.c. is licensed by the Malta Financial Services Authority as a Collective Investment Scheme under the Investment Services Act, Cap. 370 of the Laws of Malta.

The registered office of APS Bank Limited is APS Centre, Tower Street, Birkirkara, BKR 4012 and the registration number is C2192.

The principal activities of the Group are described in the Directors' report on page 2.

2. SIGNIFICANT ACCOUNTING POLICIES

2.1 BASIS OF PREPARATION

The consolidated and separate financial statements have been prepared on a historical cost basis, except for derivative financial instruments, certain financial assets and investment property, which have been measured at fair value. The consolidated and separate financial statements are presented in Euro (€), and all values are rounded to the nearest thousand (€000) except when otherwise indicated.

The Group presents its statement of financial position in order of liquidity.

Statement of compliance

The consolidated and separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU and comply with the provisions of the Banking Act, Cap. 371 and the Companies Act, Cap. 386 of the Laws of Malta.

Basis of consolidation

The consolidated financial statements comprise the financial statements of APS Bank Limited, its subsidiaries for the year ended 31 December 2018, which together are referred to as the 'Group'. Subsidiaries are fully consolidated from the date on which the Group achieves control and continue to be consolidated until the date that such control ceases. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee).
- Exposure, or rights, to variable returns from its involvement with the investee.
- The ability to use its power over the investee to affect its returns.

Generally, a majority of voting rights results in control to the extent that such substantive rights provide the investor with the current ability to direct the relevant activities of the investee. When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement with the other vote holders of the investee.
- Rights arising from other contractual arrangements.
- The Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income (OCI) are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance.

The financial statements of the subsidiaries are prepared for the same reporting period as the parent company. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies in line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises the related assets (including goodwill), liabilities, non-controlling interest and other components of equity while any resultant gain or loss is recognised in profit or loss. Any investment retained is recognised at fair value.

During the prior year, APS Consult Limited was liquidated and any assets and liabilities consolidated at December 2016 were derecognised.

2.2 CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

Standards, interpretations and amendments to published standards, which are effective in the current year

In the current year, the Group and the Bank have applied the following:

IFRS 9 Financial Instruments

In the current year, the Group and the Bank have adopted IFRS 9 as issued by the IASB in July 2014, with a date of initial application of 1 January 2018. The Group and the Bank did not early adopt any previous versions of IFRS 9 in previous periods. IFRS 9 is applied retrospectively and replaces IAS 39 *Financial Instruments: Recognition and Measurement.*

As permitted by the transitional provisions of IFRS 9, the Group and the Bank elected not to restate comparative figures and these continue to be reported under IAS 39. In terms of this election, any adjustments to the carrying amounts of financial assets and liabilities at the date of initial application are recognised in opening equity.

IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7 'Financial Instruments: Disclosures'. Consequently, for notes disclosures, the consequential amendments to IFRS 7 have also only been applied to the current period as permitted by IFRS 7. The comparative period notes disclosures continue to include only those disclosures made in the prior year.

In accordance with the transitional provisions of the Standard, the Group and the Bank have not applied the requirements of IFRS 9 to instruments that had already been derecognised at 1 January 2018.

The adoption of IFRS 9 has resulted in changes in the accounting policies for classification and measurement of financial assets and financial liabilities and impairment of financial assets.

The Group and the Bank do not designate any of their assets, liabilities or other items in a hedge relationship for accounting purposes and accordingly the changes introduced by IFRS 9 in this respect do not affect these financial statements.

Set out below are disclosures relating to the impact of the adoption of IFRS 9 on the Group and the Bank. Further details of the specific IFRS 9 accounting policies applied in the current period (as well as the previous IAS 39 accounting policies applied in the comparative period) are described in more detail below. The relevant changes in the estimation techniques or significant assumptions made during the reporting period as a result of the adoption of IFRS 9 are described in the significant accounting policies and in the remaining notes to the financial statements.

(a) Classification and measurement of financial instruments

Financial assets

IFRS 9 includes three principal classification categories for financial assets: measured at amortised cost, FVTOCI and FVTPL. IFRS 9 eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

The measurement category and the carrying amount of financial assets in accordance with IAS 39 and IFRS 9 at 1 January 2018 are compared as follows:

The Bank	IAS 39		IFRS 9	
Financial Assets	Measurement Category	Carrying Amount €000	Measurement Category	Carrying Amount €000
Cash and Balances with Central Bank of Malta	Amortised cost (Loans and receivables)	86,449	Amortised cost	86,449
Loans and advances to banks	Amortised cost (Loans and receivables)	32,246	Amortised cost	32,246
Loans and advances to customers	Amortised cost (Loans and receivables)	998,377	Amortised cost	998,717
Syndicated loans	Amortised cost (Loans and receivables)	26,213	Amortised cost	25,784
Derivative financial assets	FVTPL	3,008	FVTPL	3,008
Debt securities	Available-for-sale	179,549	FVTOCI	179,549
	Held-to-maturity	72,775	Amortised cost	72,738
	FVTPL	910	FVTPL	910
Equity instruments	Available-for-sale	1,793	FVTOCI	1,793
	FVTPL	32	FVTPL	32

There are no substantial differences between the financial assets of the Group and the Bank other than the fact that the Group also has additional financial assets measured at FVTPL of €36,103k.

Held-to-maturity investments and loans and receivables classified in terms of IFRS 9 as measured at amortised cost

Financial assets that were previously classified as held-to-maturity investments or loans and receivables are classified in terms of IFRS 9 as financial assets measured at amortised cost if they meet these two conditions:

- the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

In accordance with the transitional provisions of IFRS 9, the Group assessed the business model in which the financial assets are held on the basis of the facts and circumstances at 1 January 2018 and the resulting classification is being applied retrospectively irrespective of the Group's business model in prior reporting periods. Accordingly, there was no change in the carrying amount of these instruments at 1 January 2018 as a result of the new classification in terms of IFRS 9.

In terms of IFRS 9, the Group applies an Expected Credit Loss (ECL) model as opposed to an incurred credit loss model under IAS 39. In accordance with the transitional provisions of IFRS 9, where possible, the Group used reasonable and supportable information that was available without undue cost or effort to determine the credit risk of the instruments at the date these were initially recognised and compared that to the credit risk at 1 January 2018, taking into consideration the low credit risk exemption for debt securities and the 30 days rebuttable presumption for the remaining financial assets. The change to the loss allowance at 1 January 2018 as a result of the new impairment model in terms of IFRS 9 is quantified below.

Available-for-sale debt financial assets classified in terms of IFRS 9 as FVTOCI

Debt instruments that were previously classified as available-for-sale investments are classified in terms of IFRS 9 as debt instruments measured at FVTOCI if they meet these two conditions:

- the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling the financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

In accordance with the transitional provisions of IFRS 9, the Group assessed the business model in which the debt instruments are held on the basis of the facts and circumstances at 1 January 2018 and the resulting classification is being applied retrospectively irrespective of the Group's business model in prior reporting periods. Accordingly, there was no change in the carrying amount of these instruments at 1 January 2018 as a result of the new classification in terms of IFRS 9.

In terms of IFRS 9, the Group applies an ECL model as opposed to an incurred credit loss model under IAS 39. In accordance with the transitional provisions of IFRS 9, where possible, the Group used reasonable and supportable information that was available without undue cost or effort to determine the credit risk of the instruments at the date these were initially recognised and compared that to the credit risk at 1 January 2018, taking into consideration the low credit risk exemption. The change to the loss allowance at 1 January 2018 as a result of the new impairment model in terms of IFRS 9 is quantified below.

Available-for-sale equity financial assets classified in terms of IFRS 9 as FVTOCI

The Group has elected to designate those equity instruments that were previously classified as available-for-sale investments and that are not held for trading as FVTOCI in terms of IFRS 9.

In accordance with the transitional provisions of IFRS 9, the Group made this designation on the basis of the facts and circumstances at 1 January 2018 and the resulting classification is being applied retrospectively.

Accordingly, there was no change in the carrying amount of these instruments at 1 January 2018 as a result of the new classification in terms of IFRS 9. The cumulative fair value movement previously recognised in other comprehensive income in connection with these assets will not be reclassified subsequently to profit or loss in terms of IFRS 9.

FVTPL debt financial assets classified in terms of IFRS 9 as FVTPL

Debt investments that were previously designated as FVTPL are classified in terms of IFRS 9 as financial assets measured at FVTPL if they meet these two conditions:

- the financial asset is part of a portfolio of financial assets that is managed and whose performance is evaluated on a fair value basis; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Accordingly, there was no change in the carrying amount of these instruments at 1 January 2018 as a result of the new classification in terms of IFRS 9.

FVTPL equity financial assets classified in terms of IFRS 9 as FVTPL

Equity instruments that were previously designated as FVTPL continue to be measured at FVTPL in terms of IFRS 9.

Accordingly, there was no change in the carrying amount of these instruments at 1 January 2018 as a result of the new classification in terms of IFRS 9.

Derivative financial assets classified in terms of IFRS 9 as FVTPL

Derivative financial assets that were previously classified as FVTPL continue to be measured at FVTPL in terms of IFRS 9.

Accordingly, there was no change in the carrying amount of these instruments at 1 January 2018 as a result of the new classification in terms of IFRS 9.

Financial liabilities

There were no changes to the classification and measurement of financial liabilities. All financial liabilities continue to be measured at amortised cost using the effective interest method. Embedded derivatives in financial liability host contracts which are not closely related are separately accounted for and measured at fair value with gains and losses being recognised in profit or loss, with the financial liability host contract being measured at amortised cost using the effective interest method.

The Group / The Bank	IAS 39		IFRS 9	
Financial Liabilities	Measurement Category	Carrying Amount €000	Measurement Category	Carrying Amount €000
Amounts owed to banks	Amortised cost	111,132	Amortised cost	111,132
Amounts owed to customers	Amortised cost	1,226,382	Amortised cost	1,226,382
Derivative financial liabilities	FVTPL	3,008	FVTPL	3,008

No substantial difference exists between financial liabilities of the Group and the Bank.

(b) **Reconciliation of IAS 39 and IFRS 9 classifications and carrying amount**

The following table reconciles the carrying amounts of financial assets, from their previous measurement category in accordance with IAS 39, to their new measurement categories upon transition to IFRS 9 on 1 January 2018:

The Bank	IAS 39 carrying amount 31-Dec-17 €000	Changes due to: Reclassifications €000	Remeasurements due to loss allowance €000	IFRS 9 carrying amount 01-Jan-18 €000
Amortised cost				
Cash and balances with Central Bank of Malta:				
Opening balance under IAS 39 and closing balance under IFRS 9	86,449	-	-	86,449
Loans and advances to banks:				
Opening balance under IAS 39 and closing balance under IFRS 9	32,246	-	-	32,246
Loans and advances to customers:				
Opening balance under IAS 39 and closing balance under IFRS 9	998,377	-	340	998,717
Syndicated loans:				
Opening balance under IAS 39 and closing balance under IFRS 9	26,213	-	(429)	25,784
Debt Securities – held-to-maturity				
Opening balance under IAS 39 – held-to-maturity	72,775	-	-	-
Reclassification to amortised cost (IFRS 9)	-	(72,775)	-	-
Closing balance under IAS 39 – held-to-maturity	-	-	-	-
Debt Securities – amortised cost				
Opening balance under IFRS 9 – amortised cost	-			
Reclassification from held-to-maturity (IAS 39)	-	72,775	-	-
Closing balance under IFRS 9 – amortised cost	-	-	(37)	72,738
Total financial assets measured at amortised cost	**1,216,060**	**-**	**(126)**	**1,215,934**
FVTPL				
Derivative financial assets:				
Opening balance under IAS 39 and closing balance under IFRS 9	3,008	-	-	3,008
Debt securities:				
Opening balance under IAS 39 and closing balance under IFRS 9	910	-	-	910
Equity instruments:				
Opening balance under IAS 39 and closing balance under IFRS 9	32	-	-	32
Total financial assets measured at FVTPL	**3,950**	**-**	**-**	**3,950**
FVTOCI				
Debt securities – available-for-sale:				
Opening balance under IAS 39 – available-for-sale	179,549	-	-	-
Reclassification to FVTOCI (IFRS 9)	-	(179,549)	-	-
Closing balance under IAS 39 – available-for-sale	-	-	-	-
Equity instruments – available-for-sale:				
Opening balance under IAS 39 – available-for-sale	1,793	-	-	-
Reclassification to FVTOCI (IFRS 9)	-	(1,793)	-	-
Closing balance under IAS 39 – available-for-sale	-	-	-	-
Debt securities – FVTOCI				
Opening balance under IFRS 9 – FVTOCI	-	-	-	-
Reclassification from available-for-sale (IAS 39)	-	179,549	-	-
Closing balance under IFRS 9 - FVTOCI	-	-	-	179,549
Equity instruments – FVTOCI				
Opening balance under IFRS 9 – FVTOCI	-	-	-	-
Reclassification from available-for-sale (IAS 39)	-	1,793	-	-
Closing balance under IFRS 9 - FVTOCI	-	-	-	1,793
Total financial assets measured at FVTOCI	**181,342**	**-**	**-**	**181,342**

There are no substantial differences between the financial assets of the Group and the Bank other than the fact that the Group also has additional financial assets measured at FVTPL of €36,103k.

(c) Reconciliation of IAS 39 and IFRS 9 provisions

The following table reconciles the prior period's closing impairment allowance measured in accordance with the IAS 39 incurred loss model to the new impairment allowance measured in accordance with the IFRS 9 expected loss model at 1 January 2018:

The Group / The Bank Measurement Category	Impairment provision under IAS 39 31-Dec-17	Reclassification	Effect of IFRS 9 in retained earnings	ECL under IFRS 9 01-Jan-18
	€000	€000	€000	€000
Loans and receivables (IAS 39) / Financial assets at amortised cost (IFRS 9)				
Loans and advances to customers	16,395	-	(340)	16,055
Syndicated loans	-	-	429	429
Total	**16,395**	**-**	**89**	**16,484**
Held-to-maturity (IAS 39) / Financial assets at amortised cost (IFRS 9)				
Debt securities	-	-	37	37
Available-for-sale (IAS 39) / Financial assets at FVTOCI (IFRS9)				
Debt securities	-	-	238	238
Grand Total	**16,395**	**-**	**364**	**16,759**

The additional ECL allowance of €364,265 is charged against the respective asset, except for the allowance of €238,143 in relation to the debt instruments measured at FVTOCI, previously classified as available-for-sale investments since these investments are already measured at fair value. Consequently, the adjustment of €238,143 is recognised against the revaluation reserve.

(d) Impact of transition on equity

The cumulative effect of initially applying IFRS 9 on 1 January 2018, amounts to a decrease of €364,265 in retained earnings and an increase of €238,143 in the revaluation reserve and is presented in the Statement of Changes in Equity. This adjustment is arising from the following financial statement line items;

The Group / The Bank Impact of changes in accounting policies at 1 January 2018	As previously reported	IFRS 9 adjustments	As restated
	€000	€000	€000
Loans and advances to customers	998,377	340	998,717
Syndicated loans	26,213	(429)	25,784
Other debt and fixed income instruments	252,324	(37)	252,287
Total effect on net assets		**(126)**	
Revaluation reserve	(15,896)	(238)	(16,134)
Retained earnings	(60,032)	364	(59,688)
Total effect on equity		**126**	

The effect on the Bank's net assets and equity is in line with the above, with the Bank's retained earnings at 1 January 2018 decreasing from €56,639k to €56,275k and its revaluation reserve at 1 January 2018 increasing from €15,896k to €16,134k.

As further disclosed in notes 15 and 16, the prior year figures for loans and advances to customers in the Statement of Financial Position were restated by presenting syndicated loans separately in the Statement of Financial Position since the Group and the Bank treat these financial assets as a separate class.

(e) Presentation of comparative information

Where applicable, the presentation of comparative information in the Statement of Profit and Loss has been restated retrospectively for the amended presentation requirements in IAS 1 Presentation of Financial Statements. The effect of the restatement in the comparative period of the line items presented in the Statement of Profit or Loss as a result of IAS 1 (as amended by IFRS 9) is summarised overleaf;

	The Group Effect on 2017 €000	The Bank Effect on 2017 €000
Interest receivable and similar income on debt securities	(10,535)	(10,423)
Interest receivable and similar income on held-to-maturity debt securities	3,960	3,960
Interest receivable and similar income on debt securities measured at FVTPL	186	74
Interest receivable and similar income on other debt securities	6,389	6,389
Profit for the year	-	-

IFRS 15 Revenue from Contracts with Customers

In May 2014, the IASB issued IFRS 15 "Revenue from Contracts with Customers". The standard is the result of a convergence project between the IASB and the FASB. IFRS 15 specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18 'Revenue', IAS 11 'Construction Contracts' and a number of revenue-related interpretations. Application of the standard is mandatory for all IFRS reporters and it applies to nearly all contracts with customers: the main exceptions being leases, financial instruments and insurance contracts.

IFRS 15 Clarifications Revenue from Contracts with Customers

In April 2016, a clarification was issued with the Amendments to the Revenue Standard, IFRS 15 Revenue from Contracts with Customers, clarify some requirements and provide additional transitional relief for companies that are implementing the new Standard.

Standards, interpretations and amendments to published standards as endorsed by the EU that are not yet effective

Up to the date of approval of these financial statements, certain new standards, amendments and interpretations to existing standards have been published but are not yet effective for the current reporting period and which have not been adopted early.

IFRS 16 Leases (effective for financial years beginning on or after 1 January 2019)

During January 2016, the IASB issued a new standard IFRS 16 "Leases". The new standard brings most leases on-balance sheet for lessees under a single model, eliminating the distinction between operating and finance leases. Lessor accounting however remains substantially unchanged (except for a requirement to provide enhanced disclosures) and the distinction between operating and finance leases is retained. IFRS 16 supersedes IAS 17 'Leases' and related interpretations. IFRS 16 is effective for periods beginning on or after 1 January 2019. Early application is permitted for companies that also apply IFRS 15 Revenue from Contracts with Customers.

The directors have assessed the impact that this standard will have on the financial statements and this is considered as not being material.

Standards, interpretations and amendments to published standards that are not yet endorsed by the European Union

The following standards, interpretations and amendments have been issued by the IASB but not yet endorsed by the EU, except as disclosed below:

- IFRS 17 – Insurance Contracts (effective for financial years on or after 1 January 2021)
- IAS 19 (Amendment) – Plan Amendment, Curtailment or Settlement (effective for financial years on or after 1 January 2019)
- IAS 28 (Amendment) – Long-term Interest in Associates and Joint Ventures (effective for financial years on or after 1 January 2019), which is endorsed by the EU
- IFRS 3 (Amendments as part of the Annual Improvements to IFRS Standards 2015 – 2017 cycle) – Business Combinations (effective for financial years on or after 1 January 2019)
- IFRS 11 (Amendments as part of the Annual Improvements to IFRS Standards 2015 – 2017 cycle) - Joint Arrangements (effective for financial years on or after 1 January 2019)
- IAS 12 (Amendments as part of the Annual Improvements to IFRS Standards 2015 – 2017 cycle) – Income Taxes (effective for financial years on or after 1 January 2019)
- IAS 23 (Amendments as part of the Annual Improvements to IFRS Standards 2015 – 2017 cycle) – Borrowing costs (effective for financial years on or after 1 January 2019)
- IFRS 3 (Amendment) – Definition of a Business (acquisitions that occur on or after the 1 January 2020)
- The Conceptual Framework and Amendments to References to the Conceptual Framework in IFRS Standards
- IAS 1 and IAS 8 (Amendment) – Definition of material (effective for financial years on or after 1 January 2020)
- IFRS 9 Amendment - Prepayment Features with Negative Compensation (effective for financial years beginning on or after 1 January 2019) – endorsed by the EU
- IFRIC 23 Uncertainty over income tax treatments (effective for financial years beginning on or after 1 January 2019) – endorsed by the EU

The changes resulting from these standards, interpretations and amendments are not expected to have a material effect on the financial statements of the Group.

2.3 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest and similar income and expense

Interest income and expense are recognised in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts, excluding expected credit losses, through the expected life of the financial instrument, or where appropriate, a shorter period, to that instrument's gross carrying amount on initial recognition.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate.

Fees and commission

The Group earns fee and commission income from a diverse range of services it provides to its customers. Fees and commissions that are earned from services provided to customers are accrued for over that period. These fees include commission income, custody and other management and advisory fees. Other fee and commission income is recognised on completion of underlying transactions in the relevant period.

Dividend income

Dividend income from investments is recognised when the right to receive income is established, which is generally when shareholders approve the dividend.

Net gains on financial instruments

Net gains on financial instruments include realised gains and losses on disposal of financial instruments and unrealised gains and losses on financial assets at FVTPL. Realised gains and losses on disposal of financial assets at FVTPL represent the difference between an instrument's carrying amount and disposal amount and are recognised on the value date of transaction. Unrealised gains and losses on financial assets at FVTPL represent changes in fair value of financial instruments during the year and up to the reporting date.

Foreign currency translation

The consolidated financial statements are presented in Euro, which is the Group's presentation currency and the functional currency of the Bank. Transactions in foreign currencies are initially recorded by the Group entities at their respective functional currency spot rates at the date the transaction first qualifies for recognition. Transactions in foreign currencies are translated at the rate of exchange prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date. Differences arising on settlement or translation of monetary items are recognised in profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of recognition.

Financial assets and liabilities

Initial recognition and measurement

Financial assets and financial liabilities are recognised when the entity becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the Group commits to purchase or sell the asset.

At initial recognition, the Group measures a financial asset or financial liability at its fair value plus or minus in the case of a financial asset or financial liability not at FVTPL, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions. Transaction costs of financial assets and financial liabilities carried at FVTPL are expensed immediately in profit or loss.

Derecognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired; or
- the Group has transferred its rights to receive cash flows from the asset, or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and
- either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a 'pass-through' arrangement, and has neither transferred nor retained substantially all of the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset.

A financial liability is derecognised when the obligation under the liability is discharged, cancelled or expired.

Offsetting financial instruments

Financial assets and financial liabilities could be offset and the net amount is presented in the Statement of Financial Position only if there is a currently legally enforceable right to offset the recognised amounts and there is an intention either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Comparative year

Financial assets

Prior to the adoption of IFRS 9, the Group classified its financial assets at initial recognition in accordance with IAS 39 Financial Instruments – Recognition and Measurement.

In the comparative year, the significant accounting policies for financial assets were as follows:

For purposes of subsequent measurement financial assets are classified in four categories:

- Financial assets at FVTPL;
- Loans and receivables;
- Held-to-maturity investments;
- Available-for-sale financial assets.

Financial assets at FVTPL

Financial assets at FVTPL include financial assets held for trading and financial assets designated upon initial recognition at FVTPL. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Financial assets at FVTPL are carried in the Statement of Financial Position at fair value with net changes in fair value presented as net gains on financial instruments (note 7b). Interest earned or incurred is accrued in interest income using the EIR, while dividend income is recorded in dividend income when the right to the payment has been established.

Loans and receivables

This category is relevant to the Group and applies mostly to loans and advances to banks and loans and advances to customers.

Loans and advances to banks and loans and advances to customers include non-derivative financial assets at fixed or determinable payments that are not quoted in an active market, other than:

- Those that the Group intends to sell immediately or in the near term and those that the Group upon initial recognition designates at FVTPL.
- Those that the Group, upon initial recognition, designates as available-for-sale.
- Those for which the Group may not recover substantially all of its initial investment, other than because of credit deterioration.

After initial measurement, loans and receivables are subsequently measured at amortised cost using the effective interest rate (EIR) method, less allowance for impairment. The losses arising from impairment are recognised in the Statement of Profit or Loss in net impairment losses. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of EIR.

Held-to-maturity financial investments

Held-to-maturity financial investments are non-derivative financial assets with fixed or determinable payments and fixed maturities, which the Group has the intention and ability to hold to maturity. After initial measurement, held-to-maturity financial investments are subsequently measured at amortised cost using the EIR less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR. The amortisation is included in interest receivable and similar income in the Statement of Profit or Loss. The losses arising from impairment of such investments are recognised in the Statement of Profit or Loss in net impairment losses.

If the Group were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available-for-sale. Furthermore, the Group would be prohibited from classifying any financial asset as held-to-maturity during the following two years.

Available-for-sale financial investments

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for-sale are those which are neither classified as held-for-trading nor designated at FVTPL. Debt securities in this category are those which are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity or in response to changes in the market conditions.

After initial measurement, available-for-sale financial investments are subsequently measured at fair value. Unrealised gains and losses are recognised directly in equity (Other Comprehensive Income) and credited to the revaluation reserve. When the investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the Statement of Profit or Loss in net gains on financial instruments. Where the Group holds more than one investment in the same security they are deemed to be disposed of on a first-in first-out basis.

Interest earned whilst holding available-for-sale financial assets is reported as interest income using the EIR. Dividends earned whilst holding available-for-sale financial investments are recognised in the Statement of Profit or Loss when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the Statement of Profit or Loss in net impairment losses and removed from the revaluation reserve.

Impairment of financial assets

The Group assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (an incurred loss event) and the loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

Financial assets carried at amortised cost

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If it is determined that no objective evidence of impairment exists for an individually assessed financial asset, the asset is included in a group of financial assets with similar credit risk characteristics and that group of financial assets is collectively assessed for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised, are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss on loans and receivables and held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original EIR (i.e. the EIR computed at initial recognition). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Loans, together with the associated allowances, are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group. If, in a subsequent period, the amount of the estimated impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reduced by adjusting the allowance account, to the extent that the carrying value of the asset does not exceed its amortised cost at the reversal date. If a future write-off is later recovered, the recovery is credited to the Statement of Profit or Loss.

Available-for-sale financial investments

For available-for-sale financial investments, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a 'significant' or 'prolonged' decline in the fair value of the investments below its cost. 'Significant' is evaluated against the original cost of the investment and 'prolonged' against the period in which the fair value has been below its original cost. Where there is evidence of impairment, the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the Statement of Profit or Loss, is removed from Other Comprehensive Income and recognised in the Statement of Profit or Loss. Impairment losses on equity investments are not reversed through the Statement of Profit or Loss; increases in their fair value after impairment are recognised directly in other comprehensive income.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the Statement of Profit or Loss. Future interest income is based on the reduced carrying amount of the asset and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Interest income is recorded as part of interest receivable and similar income. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognised in the Statement of Profit or Loss, the impairment loss is reversed through the Statement of Profit or Loss.

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and the future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loans' original EIR.

Current year

In the current year, the significant accounting policies in terms of IFRS 9 for financial assets are as follows:

Classification and subsequent measurement

From 1 January 2018, the Group has applied IFRS 9 and classifies its financial assets in the following principal categories:

- FVTPL;
- FVTOCI; or
- Amortised cost

Consequently, all recognised financial assets are subsequently measured in their entirety at either amortised cost or fair value. Derivatives embedded in hybrid contracts that contain financial asset hosts within the scope of IFRS 9 are not separated; instead, the hybrid contract is classified and subsequently measured in its entirety at either amortised cost or fair value.

Classification and subsequent measurement of financial assets depend on:

i. the Group's business model for managing the asset; and
ii. the cash flow characteristics of the asset.

Business model assessment

The business model reflects how the Group manages its financial assets in order to achieve a particular business objective. That is, whether the Group's objective is solely to hold assets to collect the contractual cash flows from assets or both to collect the contractual cash flows and to sell the assets. If neither of these is applicable i.e. financial assets are held for trading purposes or financial assets are managed and their performance is evaluated on a fair value basis, then the financial assets that meet the Solely Payment of Principal and Interest (SPPI) criterion are classified as part of 'other' business model and measured at FVTPL.

The Bank's business model does not depend on management's intentions for an individual instrument, therefore the business model assessment is performed at a higher level of aggregation rather than on an instrument-by-instrument basis. Factors considered by the Group in determining the business model for a group of assets include;

- the stated policies and objectives for the portfolio and the operation of those policies in practice, including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
- how the performance of the portfolio is evaluated and reported to the Group's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed; and
- past experience i.e. the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

SPPI

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and to sell, the Group assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In assessing whether the contractual cash flows are solely payments of principal and interest, the Group considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Group will consider:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms; and
- features that modify consideration for the time value of money - e.g. periodic reset of interest rates.

Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset fails the SPPI test.

Financial assets with embedded derivatives are considered in their entirety, when determining whether their cash flows are solely payment of principal and interest. If the hybrid contract contains a host that is a financial asset, then the Group assesses the entire contract as described in the financial assets section above for classification and measurement purposes.

All of the Group's retail loans and certain fixed-rate corporate loans contain prepayment features. A prepayment feature is consistent with the SPPI criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable compensation for early termination of the contract.

In addition, a prepayment feature is treated as consistent with this criterion if:

- a financial asset is acquired or originated at a premium or discount to its contractual par amount,
- the prepayment amount substantially represents the contractual par amount plus accrued (but unpaid) contractual interest (which may also include reasonable compensation for early termination); and
- the fair value of the prepayment feature is insignificant on initial recognition.

The Group reclassifies financial assets when and only when the business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and none occurred during the period.

Debt instruments

Amortised cost

Debt financial assets which are held within a business model whose objective is to hold assets for collection of contractual cash flows where those cash flows give rise on specified dates to cash flows that are SPPI, and that are not designated at FVTPL, are measured at amortised cost.

Appropriate allowances for ECL are recognised in profit or loss in accordance with the Group's accounting policy on ECL. The amortised cost of a financial asset is the amount at which the financial asset is measured at initial recognition minus the principal repayments, plus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount, adjusted for any loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any loss allowance. Interest income from these financial assets is included in 'interest receivable and similar income' using the effective interest rate method.

Financial assets classified in this category are principally as follows – Cash and bank balances, loans and advances to banks and customers and certain debt and fixed income instruments.

FVTOCI

Debt financial assets that are held within a business model whose objective is achieved by both collection of contractual cash flows and sale of the assets, where those cash flows give rise on specified dates to cash flows that are solely payments of principal and interest, and that are not designated at FVTPL, are measured at FVTOCI.

Appropriate allowances for ECL are recognised in profit or loss in accordance with the Group's accounting policy on ECL. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortised cost which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in 'net gains on financial instruments'. Interest income from these financial assets is included in 'interest receivable and similar income' using the effective interest rate method. Certain debt and other fixed income instruments are being classified in this category.

FVTPL

Debt financial assets that are not classified as measured at amortised cost or FVTOCI are measured at FVTPL. Certain debt and other fixed income instruments are being classified in this category.

In addition, on initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVTOCI, as FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise. The Group did not designate any of its debt financial assets in terms of this requirement.

A gain or loss on a debt investment that is subsequently measured at FVTPL is recognised in profit or loss and presented in the profit or loss statement within 'net gains on financial instruments' in the period in which it arises. Interest income from these financial assets is included in 'interest receivable and similar income' using the effective interest rate method.

Equity instruments

The Group subsequently measures all equity investments at FVTPL, except where the Group's management has elected, at initial recognition, to irrevocably designate an equity investment at FVTOCI unless the instrument is held for trading. The Group's policy is to designate equity investments as FVTOCI when those investments are held for purposes other than to generate investment returns.

When the FVTOCI election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Dividends, when representing a return on such investments, continue to be recognised in profit or loss as 'dividend income' when the Group's right to receive payments is established.

Gains and losses on equity investments at FVTPL are included in the 'net gains on financial instruments' line in the Statement of Profit or Loss.

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward-looking ECL model. This requires considerable judgement over how changes in economic factors affect ECLs, which are determined on a probability-weighted basis.

The Group assesses on a forward-looking basis the ECL associated with;

- debt financial assets carried at amortised cost and FVTOCI, comprising mainly debt and other fixed income securities, loans and advances to customers and banks, syndicated loans and balances with CBM
- irrevocable loan commitments and financial guarantee contracts issued.

The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- the time value of money; and
- reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

IFRS 9 requires a loss allowance to be recognised at an amount equal to either 12-month ECLs or lifetime ECLs. Lifetime ECLs are the ECLs that result from all possible default events over the expected life of a financial instrument, whereas 12-month ECLs are the portion of ECLs that result from default events that are possible within the 12 months after the reporting date. The Group recognises loss allowances at an amount equal to lifetime ECLs, except in the following cases, for which the amount recognised will be 12-month ECLs:

- financial assets, including debt investment securities that are determined to have low credit risk at the reporting date. The Group considers a debt security to have low credit risk when its credit risk rating is equivalent to the definition of 'investment-grade';
- and other financial instruments for which credit risk has not increased significantly since initial recognition.

The credit risk note provides more detail of how the ECL allowance is measured. Loss allowances for ECL are presented as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts, generally, as a provision;
- where a financial instrument includes both a drawn and an undrawn component, and the Group cannot identify the ECL on the loan commitment component separately from those on the drawn component, the Group presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component and;
- debt instruments measured at FVTOCI: no loss allowance is recognised in the Statement of Financial Position because the carrying amount of these assets is their fair value. However, the loss allowance is recognised in Other Comprehensive Income and accumulated in the fair value reserve.

Under IFRS 9, no impairment loss is recognised on equity investments and other financial instruments measured at FVTPL.

Modification of loans

The Group sometimes renegotiates or otherwise modifies the contractual cash flows of loans to customers. When this happens, the Group assesses whether this modification results in derecognition. A modification results in derecognition when the new terms are substantially different to the original terms. The Group does this by considering, among others, the following factors:

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay;
- Whether any substantial new terms are introduced;
- Significant extension of the loan term when the borrower is not in financial difficulty;
- Significant change in the interest rate;
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Group derecognises the original financial asset and recognises a 'new' asset at amortised cost and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Group also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, and the Group recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate.

Collateral valuation

The Bank uses collateral to mitigate its risks on financial assets. The collateral comes in various forms such as cash, securities, guarantees and real estate. The fair value is generally assessed at a minimum at inception date. However, some collateral, for example cash or securities, is valued monthly. To the extent possible, the Group uses active market data for valuing collateral. Non-financial collateral, such as real estate, is valued based on data provided by external valuers to the extent that they continue to be recognised.

Financial Liabilities

Subsequent measurement

The measurement of financial liabilities depends on their classification, as described below:

Amounts owed to banks and to customers

Financial liabilities are classified according to the substance of the contractual arrangements entered into. Amounts owed to banks and amounts owed to customers are subsequently measured at amortised cost using the EIR method.

Derivative financial instruments

Derivatives are subsequently re-measured at fair value.

All derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative.

In terms of IAS 39, derivatives embedded in other financial instruments are treated as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract, and the host contract is not itself held for trading or designated at FVTPL. The embedded derivatives separated from the host are carried at fair value with changes in fair value recognised in the Statement of Profit or Loss.

Under IFRS 9, derivatives embedded in hybrid contracts that contain financial asset hosts within the scope of IFRS 9 are not separated; instead, the hybrid contract is classified and subsequently measured in its entirety at either amortised cost or fair value. Derivatives embedded in hybrid contracts that contain financial liability hosts within the scope of IFRS 9 continue to be accounted for in the same manner as previously accounted for under IAS 39.

Modification of financial liabilities

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability at fair value. The difference in the respective carrying amounts is recognised in the Statement of Profit or Loss.

The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the cash flows of the original financial liability. In addition, other qualitative factors, such as the currency that the instrument is denominated in, changes in the type of interest rate, new conversion features attached to the instrument and change in covenants are also taken into consideration. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Financial guarantee contracts and loan commitments

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and others on behalf of customers to secure loans, overdrafts and other banking facilities.

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the financial statements at fair value, being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of (i) the amortised premium and (ii) the amount of the loss allowance determined in accordance with IFRS 9 (2017 - the best estimate of the expenditure required to settle any financial obligation) arising as a result of the financial guarantee. Any increase in the liability relating to financial guarantees is taken to the Statement of Profit or Loss.

Loan commitments are firm commitments to provide credit under pre-specified terms and conditions.

Loan commitments provided by the Group are considered for loss allowance determined in accordance with IFRS 9 (2017 – the best estimate of the expenditure required). The Group has not provided any commitment to provide loans at a below-market interest rate, or that can be settled net in cash or by delivering or issuing another financial instrument.

For loan commitments and financial guarantee contracts, the loss allowance would be recognised as a provision. However, for contracts that include both a loan and an undrawn commitment and the Group cannot separately identify the ECL on the undrawn commitment component from those on the loan component, the ECL on the undrawn commitment are recognised together with the loss allowance for the loan. To the extent that the combined ECL exceed the gross carrying amount of the loan, the ECL are recognised as a provision.

Equity

An equity instrument is any contract that evidences a residual interest in the assets of the company after deducting all of its liabilities. Equity instruments are recorded at the proceeds received, net of direct issue costs. Redemptions or refinancing of equity instruments are recognised as changes in equity.

Ordinary shares issued by the company are classified as equity instruments.

Repurchase and reverse repurchase agreements

Securities sold under agreements to repurchase at a specified future date are not derecognised from the Statement of Financial Position as the Group retains substantially all of the risks and rewards of ownership. The corresponding cash received is recognised in the consolidated Statement of Financial Position as an asset with a corresponding obligation to return it, including accrued interest as a liability within cash collateral on securities lent and repurchase agreements, reflecting the transaction's economic substance as a loan to the Group. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of agreement using the EIR.

Conversely, securities purchased under agreements to resell at a specified future date are not recognised in the statement of financial position. The consideration paid, including accrued interest, is recorded in the Statement of Financial Position, within cash collateral on securities borrowed and reverse repurchase agreements, reflecting the transaction's economic substance as a loan by the Group. The difference between the purchase and resale prices is recorded in net interest income and is accrued over the life of the agreement using the EIR.

If securities purchased under agreement to resell are subsequently sold to third parties, the obligation to return the securities is recorded as a short sale within financial liabilities held for-trading and measured at fair value with any gains or losses included in net gains on financial instruments.

Property and equipment

All property and equipment is stated at cost less accumulated depreciation and accumulated impairment in value, if any. Depreciation is calculated using the straight line method to write off the cost of each asset to its residual value over its estimated useful economic life. Changes in the expected useful life are accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The annual rates used for this purpose are:

	%
Building	1.0
Computer equipment	12.5 – 25.0
Other	5.0 – 20.0

Works of art and land are not depreciated by the Group.

Property and equipment is derecognised upon disposal or when no future economic benefits are expected from its use. Any gain or loss arising on de-recognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the Statement of Profit or Loss in the year the asset is derecognised. The asset's residual value, useful life and method is reviewed, and adjusted if appropriate, at each financial year end.

Intangible assets

Intangible assets comprise computer software. An intangible asset is recognised only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Group. Intangible assets are initially measured at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

Intangible assets are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset is reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets is recognised in the Statement of Profit or Loss in the expense category consistent with the function of the intangible asset.

Amortisation is calculated using the straight-line method to write down the cost of computer software to its residual value over its estimated useful life of 4 – 8 years.

Development costs

Development costs on an individual project are recognized as an intangible asset when the Group can demonstrate:

- The technical feasibility of completing the intangible asset so that the asset will be available for use or sale.
- Its intention to complete and its ability to use or sell the asset.
- How the asset will generate future economic benefits.
- The availability of resources to complete the asset.
- The ability to measure reliably the expenditure during development.

Following initial recognition of the development expenditure as an asset, the asset is carried at cost less any accumulated amortisation and accumulated impairment losses. Amortisation of the asset begins when development is complete and the asset is available for use. It is amortised over the period of expected future benefit. During the period of development, the asset is tested for impairment annually.

Investment properties

Investment properties are stated initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value, which reflects market conditions at the reporting date. Gains or losses arising from changes in the fair values of investment properties are included in the Statement of Profit or Loss in the period in which they arise, including the corresponding tax effect. Fair values are determined based on an annual evaluation performed by an accredited external independent valuer.

Investment properties are derecognised when either they have been disposed of or when they are permanently withdrawn from use and no future economic benefit is expected from their disposal. The difference between the net disposal proceeds and the carrying amount of the asset is recognised in the Statement of Profit or Loss in the period of derecognition.

Impairment of non-financial assets and investments in subsidiaries and associates

The Group assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or Cash Generating Unit's fair value less costs to sell and its value in use. Where the carrying amount of an asset or Cash Generating Unit exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. Impairment losses are recognised in the Statement of Profit or Loss in those expense categories consistent with the function of the impaired asset.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used.

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the recoverable amount is estimated. A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. If that is the case, the carrying amount of the asset is increased to its recoverable amount. The reversal is limited so that the carrying amount of the asset does not exceed the recoverable amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the Statement of Profit or Loss.

After such a reversal the depreciation charge is adjusted in future periods to allocate the asset's revised carrying amount, less any residual value, on a systematic basis over its remaining useful life.

Investments in subsidiaries

Investments in subsidiaries are accounted for at cost less any accumulated impairment losses in the separate financial statements of the Bank.

Investment in associates

The Group

The Group's investment in its associates is accounted for using the equity method. An associate is an entity over which the Group has significant influence.

Under the equity method, the investment in an associate is initially recognised at cost in the Statement of Financial Position. The carrying amount of the investment is adjusted to recognise changes in the Group's share of net assets of the associate since acquisition date. Goodwill relating to the associates is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

The Statement of Profit or Loss reflects the Group's share of the results of operations of the associates. When there has been a change recognised directly in the equity of the associates, the Group recognises its share of any changes and discloses this, when applicable, in the Statement of Changes in Equity. Unrealised gains and losses resulting from transactions between the Group and the associates are eliminated to the extent of the interest in the associates.

The Group's share of profit or loss of associates is shown on the face of the Statement of Profit or Loss. This is the profit attributable to equity holders of the associate and, therefore, represents profit after tax and non-controlling interests in the subsidiaries of the associate.

The financial statements of the associate are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on its investment in its associate. The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the loss in the share of results of associate in the Statement of Profit or Loss.

Upon loss of significant influence over the associate, the Group measures and recognises any retaining net of tax investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognised in the Statement of Profit or Loss.

The Bank

The investment in associates is stated in the separate financial statements of the Bank at cost less any accumulated impairment losses. Provision is made where in the opinion of the Directors; there is a permanent diminution in value. Income from the investments is recognised only to the extent of the distributions received by the Bank.

Dividends payable on ordinary shares

Dividends payable on ordinary shares are recognised in the period in which they are approved by the Group's shareholders.

Taxation

Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the reporting date. Current income tax relating to items recognised directly in equity is recognised in equity and not in the Statement of Profit or Loss.

Deferred income tax

Deferred income tax is provided using the liability method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax liabilities are recognised for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred income tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

The carrying amount of deferred income tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilised. Unrecognised deferred income tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred income tax relating to items recognised directly in equity is recognised in equity and not in the Statement of Profit or Loss. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Retirement benefit costs

The Group contributes towards the government pension defined contribution plan in accordance with local legislation and to which it has no commitment beyond the payment of fixed contributions. These obligations are recognised as an expense in the Statement of Profit or Loss as they accrue. The Group does not contribute towards any retirement benefit plans.

Other liabilities

Liabilities for other amounts payable are carried at cost which is the fair value of the consideration to be paid in the future for goods and services received, whether or not billed to the Group.

Cash and cash equivalents

For the purpose of the Statement of Cash Flows, cash and cash equivalents comprise:

- Cash in hand and deposits repayable on call or short notice or with a contractual period to maturity of less than three months, with any bank or financial institution;
- Short-term highly liquid investments which are readily convertible into known amounts of cash without notice, subject to an insignificant risk of changes in value and with a contractual period of maturity of less than three months; and
- Advances to/from banks repayable within three months from the date of the advance.

Provisions, contingent liabilities and contingent assets

Provisions are recognised when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Provisions are measured at the Directors' best estimate of the expenditure required to settle the present obligation at the end of the reporting period. If the effect of the time value of money is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. Provisions are not recognised for future operating losses.

A contingent liability is (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or (b) a present obligation that arises from past events but is not recognised because: (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability. Contingent liabilities are not recognised. Contingent liabilities are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote. A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. Contingent assets are not recognised. Contingent assets are disclosed where an inflow of economic benefits is probable.

Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards incidental to ownership to the lessee. All other leases are classified as operating leases. Lease classification is made at the inception of the lease, which is the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease.

Rentals payable under operating leases, less the aggregate benefit of incentives received from the lessor, are recognised as an expense in profit or loss on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user's benefit.

Fair value measurement

The Group measures certain financial instruments and certain non-financial assets at fair value at each reporting date as disclosed in the Basis of Preparation.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability or, in the absence of a principal market, in the most advantageous market for the asset or liability. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The fair value for financial instruments traded in active markets at the reporting date is based on their quoted price or binding dealer price quotations without any deduction for transaction costs. Securities defined in these financial statements as 'quoted' are traded in an active market.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 - Quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- Level 2 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;
- Level 3 - Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

External valuers are involved for valuation of non-financial assets like investment property. Selection criteria of valuer include market knowledge, reputation, independence and whether professional standards are maintained.

At each reporting date, the Advances Division verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to relevant documents.

Significant accounting judgements, estimates and assumptions

In the process of applying the Group's accounting policies, management is required to make judgements, estimates and assumptions that affect the amounts recognised or disclosed in the financial statements. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods.

Management has made the following judgements and estimates which have the most significant effect on amounts recognised in the consolidated financial statements:

Accounting for investments in which the Group holds less than 20% voting power

At 31 December 2018, the Group directly held 15.74% (2017: 15.48%) interest in APS Income Fund and 17.83% (2017: 17.78%) interest in APS Regular Income Ethical Fund.

The Group assessed whether it has significant influence over the investees and concluded that significant influence can be clearly established upon considering the following factors:

- Representation in the board of directors.
- Participation in policy-making processes.
- Material transaction between the investee and the Bank.
- Provision of technical information and management services.

Therefore, the Group continues to account for its investment in APS Income Fund and APS Regular Income Ethical Fund as an associate under the equity method.

Fair value of investment properties

The Group carries its investment properties at fair value, with changes in fair value being recognised in the Statement of Profit or Loss. The Group engaged an independent valuation specialist to assess fair value at 31 December 2018 and 31 December 2017. For investment properties, the valuation specialist determines the most appropriate methodology (market/income approach) depending on the nature of the property.

Deferred tax assets

Deferred tax assets are recognised in respect of tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Judgement is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies (note 27).

Impairment losses on loans and advances

The Group reviews its individually significant loans and advances at each reporting date to assess whether an impairment loss should be recorded in the Statement of Profit or Loss. In particular, management's judgment is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Under IAS 39, loans and advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances, are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but the effects of which are not yet evident. The collective assessment takes account of data from the loan portfolio and judgments to the effect of concentrations of risks and economic data. The impairment loss on loans and advances is disclosed in more detail in note 10.

The critical judgements in the process of introducing IFRS 9 are explained in note 42.3.2 ECL measurement.

Impairment of other debt and fixed income securities (2017: and equity investments)

The Group reviews its debt investments measured at FVTOCI (2017: available-for-sale debt investments) and its debt investments measured at amortised cost (2017: held-to-maturity investments) at each reporting date to assess whether they are impaired. This requires similar judgment as applied to the individual assessment of loans and advances.

Up to 31 December 2017 and in terms of IAS 39 the Group also records impairment charges on available-for-sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is significant or prolonged requires judgment. In making this judgment, the Group evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investment is less than its cost. Equity instruments designated at FVTOCI upon initial recognition in terms of IFRS 9 are not tested for impairment. There were no impairment losses brought forward at 1 January 2018 in respect of these investments.

Current Year

In terms of IFRS 9, the Group made other critical judgements and estimates, which are explained in note 42.3.2 ECL measurement.

3. INTEREST RECEIVABLE AND SIMILAR INCOME

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
On loans and advances to banks	313	102	306	102
On loans and advances to customers	40,634	31,759	40,634	31,759
	40,947	31,861	40,940	31,861
On debt securities:				
Measured at amortised cost (2017: held-to-maturity)	3,643	4,256	3,643	4,256
Amortisation on premiums and discounts on debt securities measured at amortised cost (2017: held-to-maturity)	(477)	(296)	(477)	(296)
Measured at FVTPL	1,020	186	22	74
Other debt securities	5,858	7,748	5,858	7,748
Amortisation on premiums and discounts on other debt securities	(1,028)	(1,359)	(1,028)	(1,359)
	9,016	10,535	8,018	10,423
	49,963	42,396	48,958	42,284

In respect of the comparative period, interest receivable on loans and advances to customers is netted off with €880K in respect of interest accrued on impaired loans and advances to customers (note 15).

4. INTEREST PAYABLE

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
On amounts owed to banks	572	55	572	55
On amounts owed to customers	11,577	9,537	11,610	9,537
	12,149	9,592	12,182	9,592

5. DIVIDEND INCOME

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
From equity shares held in local and foreign entities and collective investment schemes	575	214	1,604	656

During the year the Group recognised dividend income of €4K on equity instruments designated at FVTOCI upon initial recognition which were derecognised during the year and €27K on equity instruments designated at FVTOCI upon initial recognition which are still held at year end.

6. GAINS / (LOSSES) ON FOREIGN EXCHANGE

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Net unrealised / realised gain on foreign exchange	260	299	446	418

7. NET (LOSSES) / GAINS ON FINANCIAL INSTRUMENTS

a) Net realised gains on disposal of debt instruments measured at FVTOCI (2017: available-for-sale)

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Realised gains on disposal of debt instruments at FVTOCI (2017: available-for-sale)	140	3,281	140	3,281

b) Net changes in fair value of financial assets at FVTPL

Unrealised net fair value movements on financial assets at FVTPL	(961)	(72)	(7)	(65)
Realised gains on disposal of financial assets at FVTPL	147	140	20	140
	(814)	68	13	75
	(674)	3,349	153	3,356

8. PERSONNEL EXPENSES

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Wages and salaries (short-term):				
- key management personnel	2,541	1,303	2,541	1,303
- other staff	10,205	9,209	10,205	9,209
Social security costs	788	636	788	636
	13,534	11,148	13,534	11,148

The average number of employees employed during the year was as follows:

	The Group		The Bank	
	2018	2017	2018	2017
Managerial	81	59	81	59
Senior officers and officers	282	255	282	255
Others	9	9	9	9
	372	323	372	323

9. OTHER ADMINISTRATIVE EXPENSES

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Remuneration payable to the auditors for:				
- the audit of financial statements	**92**	52	**78**	41
- tax advisory services	**6**	7	**4**	5
- other non-audit services	**14**	-	**8**	-
Directors' emoluments (i)	**282**	252	**259**	228
Insurance	**1,089**	810	**1,089**	810
Professional fees	**1,270**	1,604	**1,189**	1,557
Repairs and maintenance	**1,242**	1,731	**1,242**	1,731
Telecommunications	**425**	366	**425**	366
Office operating expenses	**2,388**	2,167	**2,383**	2,160
Card and other financial charges	**99**	170	**99**	170
Others	**1,856**	1,621	**1,840**	1,549
	8,763	8,780	**8,616**	8,617
Fees and commission expenses	**405**	554	**405**	554
	9,168	9,334	**9,021**	9,171

(i) Directors' emoluments are split as follows:

	The Bank
	2018
	€
Frederick Mifsud Bonnici	
- as Chairman's remuneration	50,000
- as Chair of Board Credit Committee	14,000
Victor E. Agius (appointed on 15 October 2018)	8,250
Joseph C. Attard (appointed on 26 July 2018)	13,851
Franco Azzopardi	29,000
Laragh Cassar	22,000
Alfred DeMarco	22,333
Arthur Galea Salomone (resigned on 26 July 2018)	14,875
Victor Gusman	22,000
Frederick F. Micallef (resigned on 26 July 2018)	13,125
Michael Pace Ross	23,000
Martin Scicluna	27,000
	259,434

Total Directors' emoluments (excluding Chairman) amount to €195,434 out of which €99,000 were paid in relation to Directors' fees and €96,434 were in relation to Committee fees. Each Director receives the amount of €12,750 yearly as honoraria for sitting on the Board of Directors. The non-executive directors do not receive pension entitlements from the Group.

10. NET IMPAIRMENT LOSSES

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Charge for the year:				
- collective impairment	**827**	589	**827**	589
- individual impairment	**5,200**	2,679	**5,200**	2,679
- bad debts written off	**528**	1,258	**528**	1,258
	6,555	4,526	**6,555**	4,526
Reversal of write-downs:				
- collective impairment	**(663)**	-	**(663)**	-
- individual impairment	**(4,337)**	(2,056)	**(4,337)**	(2,056)
	(5,000)	(2,056)	**(5,000)**	(2,056)
Net impairment losses	**1,555**	2,470	**1,555**	2,470

	The Group/ The Bank
	2018
	€000
Loans and advances to customers:	
Charge for the year	
- Stage 1	230
- Stage 2	316
- Stage 3	5,200
- Bad debts written off	528
	6,274
Reversal of write downs	
- Stage 1	(513)
- Stage 2	(150)
- Stage 3	(4,337)
	(5,000)
Net impairment losses	
- Stage 1	(283)
- Stage 2	166
- Stage 3	1,391
	1,274
Syndicated loans:	
- Stage 1	259
- Stage 2	92
- Stage 3	-
	351
Debt securities at amortised cost:	
- Stage 1	12
- Stage 2	-
- Stage 3	-
	12
Debt securities at FVTOCI:	
- Stage 1	(82)
- Stage 2	-
- Stage 3	-
	(82)
Net impairment losses	**1,555**

11. INCOME TAX EXPENSE

The major components of income tax expense recognised in profit and loss for the years ended 31 December 2018 and 2017 are:

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Current income tax	6,263	5,539	6,194	5,479
Deferred income tax	(220)	(289)	(220)	(289)
Income tax expense	6,043	5,250	5,974	5,190

A reconciliation between tax expense and the product of accounting profit multiplied by the applicable tax rate in Malta of 35% (2017: 35%) for the years ended 31 December 2018 and 2017 is as follows:

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Profit before tax	18,627	18,358	19,682	18,278
Theoretical tax expense at 35%	6,519	6,425	6,889	6,397
Tax effect of:				
- Non-taxable sale of investments	(41)	(1,148)	(41)	(1,148)
- Income taxed at lower rates of tax	(528)	(129)	(528)	(129)
- Depreciation not recovered by way of capital allowance	51	53	51	53
- Others	42	49	(397)	17
Income tax expense	6,043	5,250	5,974	5,190

12. DIVIDENDS PAID AND PROPOSED

	The Bank	
	2018	2017
	€000	€000
Final gross of income tax for 2017: 5.48 cents per share (2016: 3.96 cents per share)	2,527	1,827
Final net of income tax for 2017: 3.56 cents per share (2016: 2.58 cents per share)	1,642	1,187
Interim gross of income tax for 2018: 3.25 cents per share (2017: 2.55 cents per share)	1,500	1,173
Interim net of income tax for 2018: 2.12 cents per share (2017: 1.66 cents per share)	975	763

During the year the Group`s subsidiaries paid dividends amounting to €1,091,380 to its shareholders.

The Directors propose that a gross dividend of 7.59 cents per ordinary share will be paid to ordinary shareholders. This dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. The total gross dividend to be paid is €3,500,000. Shareholders have an option to receive cash or scrip dividend.

13. CASH AND BALANCES WITH CENTRAL BANK OF MALTA

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Cash in hand (note 40)	**10,387**	13,089	**9,490**	9,999
Balances with Central Bank of Malta (excluding reserve deposit) (note 40)	**151,611**	66,400	**151,611**	66,400
Reserve deposit with Central Bank of Malta	**13,410**	10,050	**13,410**	10,050
	175,408	89,539	**174,511**	86,449

Deposits with the Central Bank of Malta represent mandatory reserve deposits and are not available for use in the Group's day-to-day operations. Included in this balance is an amount of €1,400,000 (2017: €1,400,000) pledged in favour of the MFSA's Depositors' Compensation Scheme (note 19).

During the year ended 31 December 2018 the Bank has been compliant with the reserve deposit requirement (2017: the same).

14. LOANS AND ADVANCES TO BANKS

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Repayable on call and at short notice (note 40)	**49,384**	32,246	**49,384**	32,246
Placements with other banks not repayable at short notice	**1,000**	1,000	**-**	-
	50,384	33,246	**49,384**	32,246
Analysed by currency:				
- Euro	**17,537**	9,324	**16,537**	8,324
- Foreign	**32,847**	23,922	**32,847**	23,922
	50,384	33,246	**49,384**	32,246

15. LOANS AND ADVANCES TO CUSTOMERS

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Repayable on call and at short notice	**79,689**	88,015	**79,689**	88,015
Term loans and advances	**1,190,996**	926,757	**1,190,996**	926,757
Gross loans and advances (i)	**1,270,685**	1,014,772	**1,270,685**	1,014,772
Less: allowance for impairment losses (ii)	**(16,802)**	(16,395)	**(16,802)**	(16,395)
Net loans and advances	**1,253,883**	998,377	**1,253,883**	998,377

	The Group/TheBank
	€000
Balance at 31 December 2017 in terms of IAS 39	998,377
Adjustments upon initial adoption of IFRS 9 (note 2.2)	
Adjustment for ECL allowance	340
Balance at 1 January 2018 in terms of IFRS 9	**998,717**

The prior year figures for loans and advances to customers in the Statements of Financial Position and in this note were restated by presenting syndicated loans separately in the Statement of Financial Position and in note 16 since the Group and the Bank treat these financial assets as a separate class of financial assets.

15. LOANS AND ADVANCES TO CUSTOMERS (Continued)

(i) Gross loans and advances analysed by currency

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
- Euro	**1,262,901**	1,000,627	**1,262,901**	1,000,627
- Foreign	**7,784**	14,145	**7,784**	14,145
	1,270,685	1,014,772	**1,270,685**	1,014,772

(ii) Impairment allowance for loans and advances to customers

	The Group / The Bank
	€000
Balance at 31 December 2017 in terms of IAS 39	16,395
Adjustments upon initial adoption of IFRS 9 (note 2.2)	
Adjustment for ECL allowance	(340)
Balance at 1 January 2018 in terms of IFRS 9	**16,055**

A reconciliation of the allowance for impairment losses for loans and advances to customers is as follows:

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
At 1 January – as previously reported	**16,395**	14,303	**16,395**	14,303
Adjustments upon initial adoption of IFRS 9 (note 2.2)	**(340)**	-	**(340)**	-
At 1 January – adjusted	**16,055**	14,303	**16,055**	14,303
Charge/(Reversal) for the year:				
- Collective (note 10)	**(116)**	589	**(116)**	589
- Individual (note 10)	**863**	623	**863**	623
- Accrued interest (note 3)	**-**	880	**-**	880
At 31 December	**16,802**	16,395	**16,802**	16,395
- Individual impairment losses	**16,047**	12,966	**16,047**	12,966
- Collective impairment losses	**755**	3,429	**755**	3,429
	16,802	16,395	**16,802**	16,395

15. LOANS AND ADVANCES TO CUSTOMERS (Continued)

	Stage 1	Stage 2	Stage 3	
	12-moth ECL	Lifetime ECL	Lifetime ECL (but not POCI)	Total
	€000	€000	€000	€000
Loss allowance at 1 January 2018	620	251	15,184	16,055
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	(52)	-	-	(52)
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	(19)	(19)
Write-offs	-	-	(528)	(528)
New financial assets originated or purchased	129	23	1,875	2,027
Financial assets derecognised during the period	(173)	(11)	(1,047)	(1,231)
Increase / Decrease due to change in Credit Risk	(187)	155	582	550
Loss allowance at 31 December 2018	**337**	**418**	**16,047**	**16,802**

With the individually assessed allowance for impairment losses at 31 December 2017 is included an amount of €5,791,137 which has been netted off against interest receivable.

Concentration of loans and advances to customers
The following table shows the risk concentration by industry for loans and advances to customers, gross of provisions:

The Group / The Bank	2018	2017
	€000	€000
Agriculture	**11,637**	8,572
Fishing	**12,144**	9,444
Mining and quarrying	**34**	46
Manufacturing	**21,997**	20,646
Electricity, gas and water supply	**3,940**	2,870
Construction	**81,268**	58,392
Wholesale and retail trade	**42,418**	32,266
Hotels and restaurants, excluding related construction activities	**73,228**	28,506
Transport, storage and communication	**4,733**	4,019
Financial intermediation	**73,897**	70,618
Real estate, renting and business	**78,420**	65,534
Professional, scientific and technical	**7,650**	7,185
Administrative and support services	**8,626**	6,684
Public administration	**11,210**	11,607
Education	**10,709**	8,556
Health and social work	**4,085**	4,507
Community, recreational and personal service activities	**3,364**	2,946
Households and individuals	**821,325**	672,374
	1,270,685	1,014,772

16. SYNDICATED LOANS

The Group / The Bank	2018 €000	2017 €000
Manufacturing	**25,043**	9,203
Wholesale and retail trade	**10,000**	-
Transport, storage and communication	**9,500**	4,500
Financial intermediation	**5,000**	5,000
Public administration	**2,622**	2,510
Health and social work	**10,225**	5,000
Gross syndicated loans (i)	**62,390**	26,213
Less: allowance for impairment loss (ii)	**(780)**	-
Net syndicated loans	**61,610**	26,213

	€000
Balance at 31 December 2017 in terms of IAS 39	26,213
Adjustments upon initial adoption of IFRS 9 (note 2.2)	
Adjustment for ECL allowance	(429)
Balance at 1 January 2018 in terms of IFRS 9	**25,784**

(i) Gross loans and advances analysed by currency

	2018 €000	2017 €000
- Euro	**59,768**	23,703
- Foreign	**2,622**	2,510
	62,390	26,213

(ii) Impairment allowance for syndicated loans

	Stage 1 12-moth ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL (but not POCI) €000	Total €000
Loss allowance at 1 January 2018	429	-	-	429
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	(92)	92	-	-
Transfer to Stage 3	-	-	-	-
Write-offs	-	-	-	-
New financial assets originated or purchased	483	-	-	483
Financial assets derecognised during the period	-	-	-	-
Increases/decreases due to change in credit risk	(132)	-	-	(132)
Changes in model/risk parameters	-	-	-	-
Foreign Exchange and other movements	-	-	-	-
Loss allowance at 31 December 2018	**688**	**92**	**-**	**780**

The prior year figures for loans and advances to customers in the Statements of Financial Position and in note 15 were restated by presenting syndicated loans separately since the Group and the Bank treat these financial assets as a separate class of financial assets.

17. DERIVATIVE FINANCIAL INSTRUMENTS

	The Group / The Bank	
	2018	2017
	€000	€000
Derivative assets, designated at fair value through profit or loss, not designated as hedges	822	3,008
Derivative liabilities, designated at fair value through profit or loss, not designated as hedges	822	3,008

The table below shows the fair values of derivative financial instruments recorded as assets and liabilities together with their notional amount. The notional amount represents the basis upon which changes in the value of derivatives are measured. Notional amount indicates the volume of outstanding transactions as at the year end.

The Group / The Bank	Notional 2018 €000	Assets 2018 €000	Liabilities 2018 €000	Notional 2017 €000	Assets 2017 €000	Liabilities 2017 €000
Over the counter derivatives:						
Equity/commodity-index warrants purchased	49,475	822	-	49,475	3,008	-
Equity/commodity-index warrants written	(49,475)	-	822	(49,475)	-	3,008
	-	822	822	-	3008	3,008

The Group's exposure under the derivative contracts is closely monitored as part of the overall management of market risk.

18. FINANCIAL ASSETS AT FVTPL

Financial investments at FVTPL were made as follows:

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Fixed income instruments and collective investment schemes	36,241	37,013	879	910
Equity and other non-fixed income instruments	-	32	-	32
	36,241	37,045	879	942
Analysed by currency:				
- Euro	27,305	25,228	879	942
- Foreign	8,936	11,817	-	-
	36,241	37,045	879	942
Carrying value				
At 1 January	37,045	3,321	942	3,321
Disposals	(21,954)	(2,802)	(240)	(2,802)
Acquisitions	22,127	36,633	184	502
Increase/(decrease) in fair values	(977)	(107)	(7)	(79)
	36,241	37,045	879	942

The above financial assets are mandatorily measured at FVTPL in terms of IFRS 9.

19. OTHER DEBT AND FIXED INCOME INSTRUMENTS

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Held-to-maturity	**-**	72,775	**-**	72,775
Available-for-sale	**-**	179,549	**-**	179,549
At amortised cost	**85,905**	-	**85,905**	-
FVTOCI	**165,184**	-	**165,184**	-
Gross other debt and fixed income instruments (i)	**251,089**	252,324	**251,089**	252,324
Less: allowance for impairment losses (ii)	**(49)**	-	**(49)**	-
Net other debt and fixed income instruments	**251,040**	252,324	**251,040**	252,324

(i) Gross other debt and fixed income instruments

Held-to-maturity	**The Group**	**The Bank**
	€000	**€000**
Balance at 31 December 2017 in terms of IAS 39	72,775	72,775
Adjustments upon initial adoption of IFRS 9 (note 2.2)		
Reclassification to financial assets measured at amortised cost	(72,775)	(72,775)
Balance at 1 January 2018 in terms of IFRS 9	-	-

	The Group		The Bank	
Held-to-maturity	**2018**	2017	**2018**	2017
	€000	€000	**€000**	€000
Issued by public bodies:				
- Local government	**-**	62,851	**-**	62,851
Issued by other issuers:				
- Foreign government	**-**	9,255	**-**	9,255
- Foreign others	**-**	669	**-**	669
	-	9,924	**-**	9,924
Total	**-**	72,775	**-**	72,775

Available-for-sale	**The Group**	**The Bank**
	€000	**€000**
Balance at 31 December 2017 in terms of IAS 39	179,549	179,549
Adjustments upon initial adoption of IFRS 9 (note 2.2)		
Reclassification to FVTOCI	(179,549)	(179,549)
Balance at 1 January 2018 in terms of IFRS 9	-	-

19. OTHER DEBT AND FIXED INCOME INSTRUMENTS (Continued)

Available-for-sale	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
Issued by public bodies:				
- Local government	-	61,953	-	61,953
- Foreign government	-	20,634	-	20,634
	-	82,587	-	82,587
Issued by other issuers:				
- Local banks	-	1,875	-	1,875
- Foreign banks	-	17,646	-	17,646
- Foreign others	-	77,395	-	77,395
- Local others	-	46	-	46
	-	96,962	-	96,962
Total	-	179,549	-	179,549

Amortised cost	The Group €000	The Bank €000
Balance at 31 December 2017 in terms of IAS 39	-	-
Adjustments upon initial adoption of IFRS 9 (note 2.2)		
Reclassification from held-to-maturity investments	72,775	72,775
Additional ECL allowance	(37)	(37)
Balance at 1 January 2018 in terms of IFRS 9	**72,738**	**72,738**

Amortised cost	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
Issued by public bodies:				
- Local government	37,779	-	37,779	-
Issued by other issuers:				
- Foreign government	47,626	-	47,626	-
- Foreign other	500	-	500	-
	48,126	-	48,126	-
Total	85,905	-	85,905	-

FVTOCI	The Group €000	The Bank €000
Balance at 31 December 2017 in terms of IAS 39	-	-
Adjustments upon initial adoption of IFRS 9 (note 2.2)		
Reclassification from available-for-sale investments	179,549	179,549
Balance at 1 January 2018 in terms of IFRS 9	**179,549**	**179,549**

19. OTHER DEBT AND FIXED INCOME INSTRUMENTS (Continued)

FVTOCI (Continued)	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
Issued by public bodies:				
- Local government	53,322	-	53,322	-
- Foreign government	19,711	-	19,711	-
	73,033	-	73,033	-
Issued by other issuers:				
- Local banks	504	-	504	-
- Foreign banks	22,027	-	22,027	-
- Foreign other	69,573	-	69,573	-
- Local other	47	-	47	-
	92,151	-	92,151	-
Total	165,184	-	165,184	-
Total debt and other fixed income instruments	251,089	252,324	251,089	252,324
Analysed by currency:				
- Euro	214,507	215,810	214,507	215,810
- Foreign	36,582	36,514	36,582	36,514
	251,089	252,324	251,089	252,324
Unamortised premiums on debt and other fixed income instruments	4,720	5,503	4,720	5,503

	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
Listing status:				
- Listed on Malta Stock Exchange	91,652	126,725	91,652	126,725
- Listed elsewhere	158,937	124,930	158,937	124,930
- Unlisted	500	669	500	669
	251,089	252,324	251,089	252,324

Available-for-sale Carrying value	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
At 1 January – as previously reported	179,549	249,928	179,549	249,928
IFRS 9 reclassification to financial assets measured at FVTOCI (note 2.2)	(179,549)	-	(179,549)	-
At 1 January - adjusted	-	249,928	-	249,928
Redemptions and disposals	-	(76,131)	-	(76,131)
Acquisitions	-	14,518	-	14,518
Amortisation	-	(1,355)	-	(1,355)
Change in fair value	-	(5,552)	-	(5,552)
Exchange adjustments	-	(1,859)	-	(1,859)
	-	179,549	-	179,549

Held-to-maturity Carrying value	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
At 1 January – as previously reported	72,775	72,916	72,775	72,916
IFRS 9 reclassification to financial assets measured at amortised cost (note 2.2)	(72,775)	-	(72,775)	-
At 1 January - adjusted	-	72,916	-	72,916
Redemptions and disposals	-	-	-	-
Acquisitions	-	155	-	155
Amortisation	-	(296)	-	(296)
Exchange adjustments	-	-	-	-
	-	72,775	-	72,775

19. OTHER DEBT AND FIXED INCOME INSTRUMENTS (Continued)

FVTOCI	The Group		The Bank	
Carrying value	2018	2017	2018	2017
	€000	€000	€000	€000
At 1 January – as previously reported	-	-	-	-
IFRS 9 reclassification from available-for-sale	179,549	-	179,549	-
At 1 January – adjusted	179,549	-	179,549	-
Redemptions and disposals	(15,883)	-	(15,883)	
Acquisitions	7,027	-	7,027	-
Amortisation	(1,054)		(1,054)	-
Change in fair value	(4,047)	-	(4,047)	-
Exchange adjustments	(408)	-	(408)	-
	165,184	-	165,184	-

At amortised cost	The Group		The Bank	
Carrying value – Gross of ECL allowance	2018	2017	2018	2017
	€000	€000	€000	€000
At 1 January – as previously reported	-	-	-	-
IFRS 9 reclassification from held-to-maturity	72,775	-	72,775	-
At 1 January - adjusted	72,775	-	72,775	-
Redemptions and disposals	(25,175)	-	(25,175)	-
Acquisitions	38,782	-	38,782	-
Amortisation	(477)	-	(477)	-
	85,905	-	85,905	-
Total	251,089	252,324	251,089	252,324

(ii) Impairment allowance for other debt and fixed income instruments

	Stage 1	Stage 2	Stage 3	
Debt securities at amortised cost	12-moth ECL	Lifetime ECL	Lifetime ECL (but not POCI)	Total
	€000	€000	€000	€000
Loss allowance at 1 January 2018	37	-	-	37
Movements in loss allowance				
New financial assets originated or purchased	23	-	-	23
Financial assets derecognised during the period	(3)	-	-	(3)
Increases/(decreases) due to change in credit risk	(8)	-	-	(8)
Loss allowance at 31 December 2018	**49**	**-**	**-**	**49**

Eligible debt instruments with a nominal value of €146,475,471 (2017: €121,066,549) have been pledged against the provision of credit lines by the Central Bank of Malta, under the usual terms and conditions applying to such agreements. Financial assets with a nominal value of €5,250,000 (2017: €5,250,000) have been pledged in favour of the MFSA's Depositors' Compensation Scheme, as follows:

The Group / The Bank	2018	2017
	€000	€000
Deposit with Central Bank of Malta (note 13)	1,400	1,400
Debt instruments with local government	3,850	3,850
	5,250	5,250

20. EQUITY AND OTHER NON-FIXED INCOME INSTRUMENTS

Available-for-sale	The Group €000	The Bank €000
Balance at 31 December 2017 in terms of IAS 39	1,793	1,793
Adjustments upon initial adoption of IFRS 9 (note 2.2)		
Reclassification to equity instruments designated at FVTOCI	(1,793)	(1,793)
Balance at 1 January 2018 in terms of IFRS 9	-	-

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Listing status:				
- Listed on Malta Stock Exchange	-	1,511	-	1,511
- Unlisted	-	282	-	282
	-	1,793	-	1,793

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Carrying value				
At 1 January – as previously reported	**1,793**	4,119	**1,793**	4,119
IFRS 9 reclassification to equity instruments designated at FVTOCI (note 2.2)	**(1,793)**	-	**(1,793)**	-
At 1 January – as adjusted	-	4,119	-	4,119
Disposals	-	(2,479)	-	(2,479)
Acquisitions	-	47	-	47
Increase in fair value	-	106	-	106
	-	1,793	-	1,793

FVTOCI	The Group €000	The Bank €000
Balance at 31 December 2017 in terms of IAS 39	-	-
Adjustments upon initial adoption of IFRS 9 (note 2.2)		
Reclassification from available-for-sale	1,793	1,793
Balance at 1 January 2018 in terms of IFRS 9	**1,793**	**1,793**

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Listing status:				
- Listed on Malta Stock Exchange	**963**	-	**963**	-
- Unlisted	**309**	-	**309**	-
	1,272	-	**1,272**	-

20. EQUITY AND OTHER NON-FIXED INCOME INSTRUMENTS (Continued)

FVTOCI (Continued)	The Group		The Bank	
Carrying Value	2018	2017	2018	2017
	€000	€000	€000	€000
At 1 January – as previously reported	-	-	-	-
- IFRS 9 reclassification from available-for-sale	1,793	-	1,793	-
At 1 January – as adjusted	1,793	-	1,793	-
- Disposals	(276)	-	(276)	-
- Acquisitions	28	-	28	-
- Decrease in fair value	(273)	-	(273)	-
	1,272	-	1,272	-

These are equity investments which are not held for trading.

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Available-for-sale				
Sector:				
Monetary financial institutions	-	149	-	149
Non-MMF Investment Funds	-	301	-	301
Public non-financial corporations	-	1,143		1,143
Private non-financial corporations	-	200	-	200
	-	1,793	-	1,793

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
FVTOCI				
Sector:				
Monetary financial institutions	80	-	80	-
Public non-financial corporations	964	-	964	-
Private non-financial corporations	228	-	228	-
	1,272	-	1,272	-

When launching new sub-funds, the Bank invests an amount as seed capital. The Bank never increases or decreases the investment and has no intention of disposing of such investments. Therefore, these investments are classified as FVTOCI.

During the year under review (2017: the same) the Group has revised its business model and concluded that these type of investments do not form part of its core business. Given that the market conditions were favourable, the Group decided to dispose of a number of equity instruments. The fair value of the equity instruments measured at FVTOCI derecognised during the year was €426,900 (2017: €2,119,996). The cumulative gains generated from the disposal of these instruments was of €99,528 (2017: €677,364).

21. INVESTMENT IN SUBSIDIARIES

The Bank	2018 €000	2017 €000
Cost		
At 1 January	40,250	305
Dissolution of subsidiary	-	(55)
Increase in investments	-	40,000
At 31 December	40,250	40,250

Name	Country of incorporation	% equity interest 2018	% equity interest 2017	Cost 2018 €000	Cost 2017 €000
APS Diversified Bond Fund 40,000,000 ordinary shares at €1.00 (2017: 40,000,000 ordinary shares at €1.00)	Malta	95.03	97.32	40,000	40,000
ReAPS Asset Management Limited 250,000 ordinary shares at €1.00 (2017: 250,000 ordinary shares at €1.00)	Malta	100.00	100.00	250	250
				40,250	40,250

	APS Diversified Bond Fund 2018 €000	APS Diversified Bond Fund 2017 €000	ReAPS Asset Management Limited 2018 €000	ReAPS Asset Management Limited 2017 €000
Current assets	40,200	41,094	773	591
Non-Current assets	-	-	3	4
Current liabilities	(68)	(53)	(287)	(234)
Net assets value	40,132	41,041	489	361
Income	(490)	15	1,108	692
Expenses	(281)	(76)	(912)	(521)
(Loss)/profit before tax	(771)	(61)	196	171
Tax	-	-	(69)	(60)
(Loss)/profit after tax	(771)	(61)	127	111

22. INVESTMENT IN ASSOCIATES

The Group

The following table illustrates summarised financial information of APS Income Fund and APS Regular Income Ethical Fund:

	APS Income Fund		APS Regular Income Ethical Fund	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Current assets	**79,486**	81,571	**30,641**	32,728
Current liabilities	**(189)**	(207)	**(148)**	(174)
Net assets value	**79,297**	81,364	**30,493**	32,554
Carrying amount of the Group's investment	**12,481**	12,595	**5,437**	5,788

	APS Income Fund		APS Regular Income Ethical Fund	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Income	**2,536**	2,886	**(696)**	1,375
Expenses	**(769)**	(829)	**(403)**	(414)
Finance cost	**(1,694)**	(1,644)	**(568)**	(569)
Profit before tax	**73**	413	**(1,667)**	392
Tax	**(404)**	(421)	**(45)**	(44)
(Loss)/profit after tax	**(331)**	(8)	**(1,712)**	348
Group's share of (loss)/profit for the year	**(221)**	262	**259**	179

The following table illustrates the movements in the carrying amount of investment in associates during the year:

	2018	**2017**
	€000	€000
Carrying amount of the investment at 1 January	**18,224**	18,256
Share of associate's results, net of tax	**38**	441
Dividend distribution	**(514)**	(473)
Carrying amount of the investment at 31 December	**17,748**	18,224

The associate had no contingent liabilities or capital commitments at 31 December 2018 (2017: the same).

The fair value of the investment in associate at 31 December 2018 amounted to €17,918,288 (2017: €18,383,199).

The following are quoted market prices of the associate at end of December 2018 and December 2017 and represent Level 1 investments in the fair value hierarchy:

	APS Income Fund	
	2018	**2017**
	€	€
Accumulator	**179.0534**	175.9104
Distributor	**126.1875**	127.3622

22. INVESTMENT IN ASSOCIATES (Continued)

The following sub-fund is not quoted and represents a Level 2 investment in the fair value hierarchy:

	APS Regular Income Ethical Fund	
	2018	2017
	€	€
Accumulator Class A	**1.3243**	1.3731
Distributor Class B	**1.0872**	1.1573
Accumulator Class C	**1.3206**	1.3703
Distributor Class D	**1.0856**	1.1563

The Bank

Name	Country of incorporation	% equity interest 2018	% equity interest 2017	Cost 2018 €000	Cost 2017 €000
APS Funds SICAV p.l.c.	Malta				
1,199 founder shares at €1.00					
(2017: 1,199 founder shares at €1.00)		**99.99***	99.99*	**1**	1
APS Income Fund	Malta				
98,853.14 units at €100.01					
(2017: 98,853.14 units at €100.01)		**15.74**	15.48	**9,886**	9,886
APS Regular Income Ethical Fund	Malta				
5,000,000 units at €1.00					
(2017: 5,000,000 units at €1.00)		**17.83**	17.78	**5,000**	5,000
				14,887	14,887

*The 99.99% equity interest pertains solely to the Bank's share in the total founder shares of APS Funds SICAV p.l.c.

APS Income Fund and APS Regular Income Ethical Fund are both sub-funds of APS Funds SICAV p.l.c. The Company is recognised under the laws of Malta as a multi-fund public limited liability company with variable share capital pursuant to the Companies Act. The Company and its sub-funds are authorised in terms of the Investment Services Act (Cap. 370, Laws of Malta) as an open-ended collective investment scheme qualifying as a Maltese UCITS , and licensed and regulated by the MFSA.

23. NON CURRENT ASSETS HELD-FOR-SALE

	The Group / The Bank	
	2018	2017
	€000	€000
At 1 January	**-**	-
Property reclassified as held-for-sale	**2,600**	-
At 31 December	**2,600**	-

The Bank entered into a promise of sale agreement on one of its investment properties at a selling price of €2,600,000. The actual deed will take place during the financial year ending 2019.

24. INVESTMENT PROPERTIES

The Group's investment property consists of commercial property and residential properties in Malta. At 31 December 2018 and 2017 the fair values of investment properties held by the Group were as follows:

	The Group		The Bank	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
At 1 January	**4,203**	3,793	**4,203**	3,793
Additions for the year	**-**	50	**-**	50
Subsequent expenditure	**-**	100	**-**	100
Property reclassified as held-for-sale	**(2,600)**	-	**(2,600)**	-
Fair value movement	**257**	260	**257**	260
At 31 December	**1,860**	4,203	**1,860**	4,203

During the year the Bank reclassified one of its investment properties as held-for-sale, after entering into a promise of sale with a value of €2,600,000 (Note 23).

25. PROPERTY AND EQUIPMENT

The Group	Land and Buildings	Computer Equipment	Other	Total
	€000	€000	€000	€000
Cost				
At 1 January 2017	13,264	5,206	12,408	30,878
Additions	1,158	1,294	2,161	4,613
Reclassification	-	(213)	213	-
Disposals	-	(30)	(285)	(315)
At 31 December 2017	14,422	6,257	14,497	35,176
Additions	2,022	1,415	2,243	5,680
Disposals	-	-	(64)	(64)
At 31 December 2018	**16,444**	**7,672**	**16,676**	**40,792**
Depreciation				
At 1 January 2017	1,937	4,539	10,255	16,731
Charge for the year	152	305	584	1,041
Reclassification	-	(77)	77	-
Disposals	-	(18)	(284)	(302)
At 31 December 2017	2,089	4,749	10,632	17,470
Charge for the year	146	245	708	1,099
Disposals	-	-	(63)	(63)
At 31 December 2018	**2,235**	**4,994**	**11,277**	**18,506**
Net Book Value				
At 31 December 2018	**14,209**	**2,678**	**5,399**	**22,286**
At 31 December 2017	12,333	1,508	3,865	17,706
At 1 January 2017	11,327	667	2,153	14,147

	2018	2017
	€000	€000
Future capital expenditure:		
- Authorised by the Directors and contracted	**396**	1,082
- Authorised by the Directors but not yet contracted	**4,783**	7,593
	5,179	8,675

25. PROPERTY AND EQUIPMENT (Continued)

The Bank	Land and Buildings €000	Computer Equipment €000	Other €000	Total €000
Cost				
At 1 January 2017	13,264	5,199	12,410	30,873
Additions	1,158	1,294	2,161	4,613
Reclassification	-	(213)	213	-
Disposals	-	(23)	(287)	(310)
At 31 December 2017	14,422	6,257	14,497	35,176
Additions	2,022	1,415	2,243	5,680
Disposals	-	-	(64)	(64)
At 31 December 2018	**16,444**	**7,672**	**16,676**	**40,792**
Depreciation				
At 1 January 2017	1,937	4,531	10,258	16,726
Charge for the year	152	305	584	1,041
Reclassification	-	(77)	77	-
Disposals	-	(10)	(287)	(297)
At 31 December 2017	2,089	4,749	10,632	17,470
Charge for the year	146	245	708	1,099
Disposals	-	-	(63)	(63)
At 31 December 2018	**2,235**	**4,994**	**11,277**	**18,506**
Net Book Value				
At 31 December 2018	**14,209**	**2,678**	**5,399**	**22,286**
At 31 December 2017	12,333	1,508	3,865	17,706
At 1 January 2017	11,327	668	2,152	14,147

	2018 €000	2017 €000
Future capital expenditure:		
- Authorised by the Directors and contracted	**396**	1,082
- Authorised by the Directors but not yet contracted	**4,783**	7,593
	5,179	8,675

The gross carrying amount of any fully depreciated property and equipment that is still in use at 31 December 2018 was of €15,035,462 (2017: €11,481,946).

26. INTANGIBLE ASSETS

	The Group Computer software €000	The Bank Computer software €000
Cost		
At 1 January 2017	13,042	13,042
Additions	1,872	1,868
At 31 December 2017	14,914	14,910
Additions	1,542	1,542
At 31 December 2018	**16,456**	**16,452**
Amortisation		
At 1 January 2017	8,981	8,981
Charge for the year	840	840
At 31 December 2017	9,821	9,821
Charge for the year	774	773
At 31 December 2018	**10,595**	**10,594**
Net book value		
At 31 December 2018	**5,861**	**5,858**
At 31 December 2017	5,093	5,089
At 1 January 2017	4,061	4,061

	2018 €000	2017 €000
Future capital expenditure:		
- Authorised by the Directors and contracted	**885**	1,141
- Authorised by the Directors but not yet contracted	**6,157**	2,307
	7,042	3,448

The gross carrying amount of any fully amortised intangible assets that is still in use at 31 December 2018 was of €8,958,340 (2017: €8,703,492).

27. DEFERRED TAX ASSETS

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Fair value movements in investment securities	(1,197)	(1,956)	(1,197)	(1,956)
Fair value movements on investment properties	(148)	-	(148)	-
Impairment allowance for loans and advances to customers	6,154	5,739	6,154	5,739
Impairment allowance for investment securities	43	-	43	-
Excess of capital allowances over depreciation	(999)	(798)	(999)	(798)
	3,853	2,985	3,853	2,985

Deferred tax arising on the fair value movements on investment securities, amounting to €878,334 was credited (2017: €1,194,914 credited) directly in Other Comprehensive Income. For other movements' details refer to note 11.

28. OTHER RECEIVABLES

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Accrued income	4,826	5,204	4,826	5,204
Prepayments and other receivables	1,467	1,446	821	759
Amounts due from subsidiaries	-	-	198	159
	6,293	6,650	5,845	6,122

29. AMOUNTS OWED TO BANKS

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
With agreed maturity dates or periods of notice, by remaining maturity:				
- 3 months or less but not repayable on demand (note 40)	404	36,622	404	36,622
- over 3 months but less than 1 year but not repayable on demand	7,059	7,500	7,059	7,500
- Over 1 year	67,010	67,010	67,010	67,010
	74,473	111,132	74,473	111,132
Analysed by currency:				
- Euro	74,079	109,677	74,079	109,677
- Foreign	394	1,455	394	1,455
	74,473	111,132	74,473	111,132

30. AMOUNTS OWED TO CUSTOMERS

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Term deposits	784,587	544,330	787,087	545,091
Repayable on demand	865,721	681,246	866,222	681,291
	1,650,308	1,225,576	1,653,309	1,226,382
Analysed by currency:				
- Euro	1,570,396	1,149,921	1,573,397	1,150,727
- Foreign	79,912	75,655	79,912	75,655
	1,650,308	1,225,576	1,653,309	1,226,382

31. OTHER LIABILITIES

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Other liabilities	11,892	9,530	11,892	9,530

32. ACCRUALS

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Accrued interest payable	5,608	5,132	5,608	5,132
Other accruals	4,494	5,466	4,452	5,400
Amounts due to subsidiaries	-	-	17	1
	10,102	10,598	10,077	10,533

33. ISSUED CAPITAL

	The Group / The Bank	
	2018	2017
	€000	€000
Authorised		
60,000,000 ordinary shares of €1.25 each (2017: same)	75,000	75,000
Issued and fully paid		
46,083,840 ordinary shares of €1.25 each (2017: same)	57,605	57,605

	Number of shares	Number of shares
	000	000
At 31 December	46,084	46,084

The Bank's major shareholders are AROM Holdings Limited and the Diocese of Gozo which hold 83.33% and 16.67% of the share capital, respectively. The accounts of APS Bank Limited are included in the consolidated financial statements of AROM Holdings Limited, a copy of which can be obtained from the Registry of Companies. The ultimate controlling party of APS Bank Limited is the Archdiocese of Malta.

The registered office of AROM Holdings Limited and the Archdiocese of Malta is Archbishop's Curia, St. Calcedonius Square, Floriana.

34. SHARE PREMIUM

	The Group / The Bank	
	2018	2017
	€000	€000
Balance at beginning and end of year	1,770	1,770

The share premium reserve is not available for distribution.

35. REVALUATION RESERVE

The revaluation reserve is used to record movements in the fair value of financial statements measured at FVTOCI (2017 – available-for-sale equity shares and debt securities), net of deferred taxation thereon. The revaluation reserve is not available for distribution.

36. RETAINED EARNINGS

The retained earnings represent retained profits. The amount is available for distribution to shareholders subject to qualification as realised profits in accordance with the requirements of the Companies Act, Cap. 386 of the Laws of Malta. In accordance with the revised Banking Rule BR/09/2013, which became applicable as from 31 December 2013, the Bank has set aside in 2015 the amount of €45,400 from the planned dividend distributions. No amounts were required to be allocated during 2017 and 2018. The full appropriation has been made, despite the fact that the Authority granted a transitory period of three years for the initial appropriation of funds to the Reserve for General Banking Risks.

37. CONTINGENT LIABILITIES

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Guarantees	22,762	8,666	22,762	8,666
Other contingent liabilities	507	2,168	507	2,168
	23,269	10,834	23,269	10,834

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit and guarantees. The measurement of these instruments is disclosed in the accounting policies.

The majority of contingent liabilities are backed by corresponding obligations from third parties. There were no significant law suits against the Group and the Bank at 31 December 2018 and 31 December 2017.

38. COMMITMENTS

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Undrawn formal standby facilities, credit facilities and other commitments to lend	711,160	552,000	711,160	552,000

39. OPERATING LEASES

	The Group / The Bank	
	2018	2017
	€000	€000
Minimum lease payments under operating leases recognised as an expense for the year	402	317

At the end of the reporting period, the Bank had outstanding commitments under non-cancellable operating leases, which fall due as follows:

	2018	2017
	€000	€000
Within one year	444	349
Between one and five years	1,275	1,263
Over five years	1,641	1,669
	3,360	3,281

Operating lease payments represent rentals payable by the Group for certain buildings. The leases for the buildings have varying terms ranging from 6 years to 20 years and certain leases have a renewable clause. A number of leases also have an escalation clause within the lease amount increasing generally based on the Property Price Index, Retail or Consumer Price Index.

40. NOTES TO THE STATEMENTS OF CASH FLOWS

	The Group		The Bank	
	2018	2017	2018	2017
	€000	€000	€000	€000
Cash in hand (note 13)	10,387	13,089	9,490	9,999
Balances with Central Bank of Malta (excluding reserve deposit) (note 13)	151,611	66,400	151,611	66,400
Loans and advances to banks (repayable within 3 months) (note 14)	49,384	32,246	49,384	32,246
Amounts owed to banks (note 29)	(404)	(36,622)	(404)	(36,622)
Cash and cash equivalents included in the statements of cash flows	210,978	75,113	210,081	72,023

41. RELATED PARTY DISCLOSURES

The Group structure

These consolidated financial statements of the Group include the financial statements of APS Bank Limited, its subsidiaries and associates as follows:

		Country of incorporation	Note	% equity interest 2018	2017
APS Regular Income Ethical Fund (sub-fund of APS Funds SICAV p.l.c)	Associate	Malta	22	17.83	17.78
APS Income Fund (sub-fund of APS Funds SICAV p.l.c.)	Associate	Malta	22	15.74	15.48
ReAPS Asset Management Limited	Subsidiary	Malta	21	100.00	100.00
APS Diversified Bond Fund (sub-fund of APS Funds SICAV p.l.c.)	Subsidiary	Malta	21	95.03	97.32

The registered office of APS Funds SICAV p.l.c., APS Regular Income Ethical Fund, APS Income Fund, APS Diversified Bond Fund and ReAPS Asset Management Limited is APS Centre, Tower Street, Birkirkara, BKR 4012.

During the course of its normal banking business, the Bank conducts business on commercial terms with its subsidiaries, associates, shareholders, key management personnel and other related parties.

41. RELATED PARTY DISCLOSURES (Continued)

Related party transactions

The following table provides the total amount of transactions, which have been entered into by the Bank with the subsidiaries and associates for the relevant financial year:

Related parties	Year	Income from related parties €000	Expenses charged to / (by) related parties €000	Amounts owed by related parties €000	Amounts owed to related parties €000
Subsidiaries					
APS Diversified Bond Fund	**2018**	**-**	**33**	**-**	**2,500**
APS Diversified Bond Fund	2017	-	-	-	472
ReAPS Asset Management Limited	**2018**	**845**	**-**	**198**	**488**
ReAPS Asset Management Limited	2017	434	-	159	334
Associates					
APS Income Fund	**2018**	**-**	**58**	**-**	**5,024**
APS Income Fund	2017	97	366	-	8,935
APS Regular Income Ethical Fund	**2018**	**-**	**3**	**-**	**219**
APS Regular Income Ethical Fund	2017	134	24	-	19,391

Transactions with key management personnel of the Bank/Group

(a) Compensation of key management personnel of the Bank/Group

The amounts disclosed in note 8 and 9 are recognised as an expense during the reporting year and are paid to key management personnel of the Group. These only include short-term employee benefits. (2017: the same).

(b) Other transactions with directors:

	2018 €000	2017 €000
Loans and advances	**287**	83
Commitments	**400**	7

The above facilities do not involve more than the normal risk of repayment or present other unfavourable features and were made in the ordinary course of business on substantially the same terms as for comparable transactions with persons of a similar standing, or where applicable, other employees.

(c) Transactions with executive employees:

	2018 €000	2017 €000
Loans and advances	**2,030**	1,638
Commitments	**174**	123

41. RELATED PARTY DISCLOSURES (Continued)

Transactions with other related parties	Balances at 31.12.2018	Interest payable 2018	Balances at 31.12.2017	Interest payable 2017
	€000	€000	€000	€000
Amounts due from other related parties:				
Shareholders and entities with common directorship	7,219	231	7,184	248
Amounts due to other related parties:				
-Shareholders	29,295	611	27,700	671
-Key management personnel	922	4	561	2
-Other related parties	25,170	296	12,385	98

Included in the amounts due to shareholders, are deposits of €250,000 (2017: €250,000) held as collateral for loan commitments and overdraft facilities granted to related parties. Also included are term deposits of €11,383,597 (2017: €12,163,496), which bear interest at the prevailing Bank rates. Furthermore, the amounts due from other related parties includes a secured element of €7,204,075 and €14,451 as unsecured.

For the year ended 31 December 2018, the Bank did not require to provide for impairment of receivables relating to amounts due from related parties (2017: the same).

No guarantees were received by related parties as at end of December 2018 (2017: the same). Special guarantees given to related parties amount to €235,132 (2017: €229,532)

42. RISK MANAGEMENT

42.1 INTRODUCTION

42.1.1 Risk management framework

The Board of Directors (hereafter referred to as "the Board") has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established the Risk Committee. The Risk Committee proposes the risk appetite statement for approval by the Board and ensures implementation of the Group's risk management and compliance strategy, systems and policies. The Group's Risk Appetite Statement articulates the types and level of risk that the Group is willing to take in the pursuit of the strategic objectives. The risk management policies and systems are reviewed regularly to reflect changes in market conditions and the Group's activities.

The Group's risk governance framework ensures oversight of and accountability for the effective management of risk. Responsibility for risk lies at all levels within the Bank through a three lines of defence model. Business units, as the first line of defence, are responsible for identifying, assessing and mitigating the risks to which the Group is exposed in the respective operational function. The management of the various forms of risk is then coordinated and monitored by the Risk and Compliance functions. The Internal Audit Department, as the third line of defence, provides independent assurance to the Board on the adequacy of the risk management framework.

The key risks to which the Group is exposed are detailed below:

42.2 Fair values

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities;
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable;
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

The level within which the fair value measurement is categorised is determined based on the lowest level of input that is significant to fair value measurement.

The reporting of fair values is intended to guide users as to the amount, timing and certainty of cash flows.

42. RISK MANAGEMENT (Continued)

42.2 FAIR VALUES (Continued)

Fair value measurement hierarchy of the Bank's assets and liabilities is as follows:

The Group	Fair value measurement hierarchy			
	Level 1	Level 2	Level 3	Total
	€000	€000	€000	€000
Assets at 31 December 2018				
Investment properties (Note 24)				
- Residential properties	-	-	460	460
- Commercial property	-	-	1,400	1,400
Non-current assets held-for-sale	-	-	2,600	2,600
Derivative assets not designated as hedges (Note 17)	-	822	-	822
Financial assets at FVTPL (Note 18)				
- fixed income instruments and collective investment schemes	36,241	-	-	36,241
- equity and other non-fixed income instruments	-	-	-	-
FVTOCI				
- other debt and fixed income instruments (Note 19)	165,184	-	-	165,184
- equity and other non-fixed income instruments (Note 20)	963	-	309	1,272
Total	**202,388**	**822**	**4,769**	**207,979**
Liabilities at 31 December 2018				
Derivative liabilities not designated as hedges (Note 17)	-	822	-	822
Total	**-**	**822**	**-**	**822**

The Group	Fair value measurement hierarchy			
	Level 1	Level 2	Level 3	Total
	€000	€000	€000	€000
Assets at 31 December 2017				
Investment properties (Note 24)				
- Residential properties	-	-	2,803	2,803
- Commercial property	-	-	1,400	1,400
Derivative assets not designated as hedges (Note 17)	-	3,008	-	3,008
Financial assets at FVTPL (Note 18)				
- debt and other fixed income investments	37,013	-	-	37,013
- equity and other non-fixed income instruments	32	-	-	32
Available-for-sale financial assets				
- other debt and fixed income instruments (Note 19)	179,549	-	-	179,549
- equity and other non-fixed income instruments (Note 20)	1,511	-	282	1,793
Total	**218,105**	**3,008**	**4,485**	**225,598**
Liabilities at 31 December 2017				
Derivative liabilities not designated as hedges (Note 17)	-	3,008	-	3,008
Total	**-**	**3,008**	**-**	**3,008**

42. RISK MANAGEMENT (Continued)

42.2 FAIR VALUES (Continued)

The Bank	Level 1 €000	Fair value measurement hierarchy Level 2 €000	Level 3 €000	Total €000
Assets at 31 December 2018				
Investment properties (Note 24)				
- Residential properties	-	-	460	460
- Commercial property	-	-	1,400	1,400
Non-current assets held-for-sale	-	-	2,600	2,600
Derivative assets not designated as hedges (Note 17)	-	822	-	822
Financial assets at FVTPL (Note 18)				
- fixed income instruments and collective investment schemes	879	-	-	879
- equity and other non-fixed income instruments	-	-	-	-
FVTOCI				
- other debt and fixed income instruments (Note 19)	165,184	-	-	165,184
- equity and other non-fixed income instruments (Note 20)	963	-	309	1,272
Total	**167,026**	**822**	**4,769**	**172,617**
Liabilities at 31 December 2018				
Derivative liabilities not designated as hedges (Note 17)	-	822	-	822
Total	**-**	**822**	**-**	**822**

The Bank	Level 1 €000	Fair value measurement hierarchy Level 2 €000	Level 3 €000	Total €000
Assets at 31 December 2017				
Investment properties (Note 24)				
- Residential properties	-	-	2,803	2,803
- Commercial property	-	-	1,400	1,400
Derivative assets not designated as hedges (Note 17)	-	3,008	-	3,008
Financial assets at FVTPL (Note 18)				
- debt and other fixed income investments	910	-	-	910
- equity and other non-fixed income instruments	32	-	-	32
Available-for-sale financial asstes				
- other debt and fixed income instruments (Note 19)	179,549	-	-	179,549
- equity and other non-fixed income instruments (Note 20)	1,511	-	282	1,793
Total	**182,002**	**3,008**	**4,485**	**189,495**
Liabilities at 31 December 2017				
Derivative liabilities not designated as hedges (Note 17)	-	3,008	-	3,008
Total	**-**	**3,008**	**-**	**3,008**

There were no reclassifications made within the fair value hierarchy and there were no changes in valuation techniques used by the Bank during the year.

Property held by the Group and the Bank was valued by an independent architect. Commercial property was valued using the investment method, whereby the potential rental value estimated to be in the range of €130 and €160 per square metre (2017: €125 and €150 per square metre) of this property was estimated and then capitalized using a yield of 6% which has been deemed to be fair and reasonable. Furthermore, the potential increased floor area of the property as allowed by the Planning Authority was also taken into consideration.

In 2017, one of the residential properties was valued using a comparative sales method adjusted for the specific attributes of the property which is under construction. The fair value of the second residential property was established by using the results of two separate valuation methods. The first method was the comparative sales method for all units forming part of the residential complex and the second method was replacement cost. The value obtained from both of these valuations in 2017 ranged between €270 and €300 per square metre.

In 2018, the residential property was valued using a comparative sales method adjusted for the specific attributes of the property which is in need of a refurbishment.

The Bank's objective is to dispose of the properties in an orderly fashion to reduce or repay outstanding claims and accordingly their current use is not necessarily the highest and best use in terms of IFRS 13.

Significant increases (decreases) in estimated market rates per square metre in isolation would result in a significantly higher (lower) fair value of the properties.

As at the end of 31 December 2018 (2017: the same) the Group has no restrictions on the realisation of investment properties in Note 24.

As disclosed in Note 24, the fair value movement on property held by the Group and the Bank amounted to €257k for 2018 (2017: €260k) and is included in the following line item – Other operating income.

Derivative assets not designated as hedges

The last valuation for derivative instruments was made on 31 December 2018 (2017: 31 December 2017) on the basis of observable inputs using a discounted cash flow model by applying appropriate yield curves at the balance sheet date.

Financial assets at FVTPL – fixed income instruments and collective investments schemes

All of the Group's financial assets at FVTPL are carried at market value using available quoted market prices.

Financial assets at FVTOCI (2017: available-for-sale financial assets)

Fair values of debt and equity instruments classified in this category are generally based on quoted market prices, if available.

Derivative liabilities not designated as hedges

The last valuation for derivative instruments was made on 31 December 2018 (2017: 31 December 2017) on the basis of observable inputs using a discounted cash flow model by applying appropriate yield curves at the balance sheet date.

Other financial instruments

The amounts stated for cash balances, balances with the Central Bank of Malta and loans and advances to banks which are repayable on call and at short notice are highly liquid assets. The Directors regard the amounts shown in the Statement of Financial Position for these items as reflecting their fair value in that these assets will be realised for cash in the immediate future. The fair value of the placements with other banks not repayable at short notice is not materially different from their carrying amount since these carry an arm's length rate of interest which is reflective of conditions at year end. The fair value was determined using a Level 2 valuation technique.

At the reporting date debt securities classified at amortised cost amounted to €85.9 million (2017: held-to-maturity investments amounted to €72.8million). Their market value amounted to €93.1 million (2017: €82.6 million) (Level 1), whilst their nominal value amounted to €81.6 million (2016: €71.6 million). For other details refer to Note 19.

Loans and advances to customers are stated at the amounts contractually due less provision to reflect the expected recoverable amounts. Their carrying amount is not deemed to differ materially from their fair value as these are re-priced to take into consideration changes in both the Bank's base rate and credit margins. The fair value measurement is classified as Level 2.

Amounts owed to banks and customers are mainly deposit liabilities. Of this category of liability, 76% (2017: 79%) have contractual re-pricing within one year, whilst 24% (2017: 21%) re-prices between one year and over. For demand deposits and term deposits within one year, fair value is taken to be the amount payable on demand at the reporting date. For term deposits after one year with a carrying amount of €412.7 million (2017: €217.4 million), fair value is €412.7 million (2017: €217.4 million). All term deposits at different maturities were revalued to reflect the current interest rates. The fair value measurement is classified as Level 2.

The reconciliation of Level 3 fair value measurements of financial instruments is disclosed below.

	2018 €000
Opening balance at 1 January	282
Disposals	-
Acquisitions	28
Fair value movements	(1)
Closing balance at 31 December	**309**

42. RISK MANAGEMENT (Continued)

42.3 CREDIT RISK

Credit Risk is the possibility that a borrower or counterparty fails to meet its obligations in accordance with (or performing according to) agreed terms, causing a financial loss, including losses resulting from a reduction in portfolio value arising from actual or perceived deterioration in credit quality.

Credit risk arises mainly from inter-bank, commercial and consumer loans and advances, and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as financial guarantees, letters of credit, endorsements and acceptances.

The Group is also exposed to credit risk arising from investments in debt securities and other financial instruments arising from its trading and investment activities including non-equity portfolio assets and derivatives as well as settlement balances with market counterparties, reverse repurchase agreements and balances with CBM.

The Group has a detailed Credit Risk Policy, which lays down the principles for the management of credit risk. The Group manages and controls its exposure to credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and connected entities, as well as by geographical and industry concentrations.

The Group has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision. The credit quality review process aims to allow the Group to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

42.3.1 Credit Risk Measurement

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties.

42.3.1.1 Credit Risk Grading

The Group allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. The Group uses these grades in identifying significant increases in credit risk under IFRS 9. Credit risk grades are a primary input into the determination of the term structure of PD for exposures.

The Group use internal rating models tailored to the various categories of counterparty. Borrower and loan specific information collected at the time of application (such as the level of collateral for retail exposures and turnover and industry type for wholesale exposures) is fed into this rating model. This is supplemented with external data such as information from the credit risk register. In addition, the models enable management overlay by the responsible person, to be fed into the final internal credit rating for each exposure. This allows for considerations which may not be captured as part of the other data inputs into the model.

The following are additional considerations for each type of portfolio held by the Group:

Retail

After the date of initial recognition, for retail business, the payment behaviour of the borrower is monitored on a periodic basis to develop a behavioural score. Any other known information about the borrower which impacts their creditworthiness, such as unemployment and previous delinquency history, is also incorporated into the internal credit rating system.

Wholesale

For wholesale business, the rating is determined at the borrower level. A relationship manager will incorporate any updated or new information/credit assessments into the credit system on an ongoing basis. In addition, the relationship manager will also update information about the creditworthiness of the borrower every year from sources such as public financial statements. This will determine the updated internal credit rating.

Treasury

For debt securities in the Treasury portfolio, external rating agency credit grades are used. These published grades are continuously monitored and updated. The PDs associated with each grade are determined based on historical realised default rates, as published by an external credit rating agency.

Syndicated Loans

Similar to debt securities, syndicated loans are rated using an external rating agency credit grades. Again, these credit grades are frequently reviewed and monitored for immediate update where necessary.

The Group's internal gradings for loans and advances comprise of nine (9) rating levels including three (3) default classes, whilst the remaining rating levels represent exposures not in default. Each rating category is assigned a stage under IFRS 9, where the PDs differ according to which stage, the rating category falls under.

For debt securities and syndicated loans, PDs are obtained from market data provided by a third party. PDs are assigned to the instruments, according to their external credit rating, region and sector. The risk of default increases exponentially at each higher credit risk rating. This means that the difference in the PD between an A and A- rating grade is lower than the difference in the PD between a B and B- rating grade.

42.3.2 ECL Measurement

IFRS 9 outlines a 'three-stage' model for impairment based on changes in credit quality since initial recognition as summarised below:

- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Group.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. Please refer to note 42.3.2.1 for a description of how the Group determines when a significant increase in credit risk has occurred.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Please refer to note 42.3.2.2 for a description of how the Group defines credit-impaired and default.
- Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis. Please refer to note 42.3.2.3 for a description of inputs, assumptions and estimation techniques used in measuring the ECL.
- A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward looking information. Note 42.3.2.4 includes an explanation of how the Group has incorporated this in its ECL models.

Further explanation is also provided in note 42.3.2.5 on how the Group determines appropriate groupings when ECL is measured on a collective basis.

The following diagram summarises the impairment requirements under IFRS 9:

Change in credit quality since initial recognition

Stage 1	Stage 2	Stage 3
Initial Recognition	Significant increase in credit risk since initial recognition	Credit-impaired assets
12 month Expected Credit Loss	Lifetime Expected Credit Loss	Lifetime Expected Credit Loss

The key judgements and assumptions adopted by the Group in addressing the requirements of the standard are discussed in the following notes.

42.3.2.1 Significant increase in Credit Risk (SICR)

Under IFRS 9, when determining whether the credit risk (i.e. risk of default) on a financial instrument has increased significantly since initial recognition, the Group will consider reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information and analysis based on the Group's historical experience, expert credit assessment and forward-looking information.

The main judgements that will be made by the Group in identifying whether a significant increase in credit risk has occurred for an exposure are as follows:

- For loans and advances to customers and banks, the Group's internal credit risk grades will be used to assess whether there has been a significant increase in credit risk, performed by comparing the internal credit risk grades as at reporting date with the internal credit risk grades on initial recognition.
- For the investments' portfolio and balances with CBM, the Group will apply the low credit risk simplification to all its exposures, thus to the extent that these investments are considered to be low credit risk, they are not subject to the significant increase in credit risk assessment.
- In assessing whether there has been a significant increase in credit risk since initial recognition of a loan commitment, the Group considers changes in the risk of a default occurring on the loan to which a loan commitment relates; for financial guarantee contracts, the Company considers the changes in the risk that the specified debtor will default on the contract.

Assessing whether credit risk has increased significantly since initial recognition of a financial instrument requires identifying the date of initial recognition of the instrument, together with its internal grading/credit rating on initial recognition. For certain revolving facilities (e.g. overdrafts), the date when the facility was first entered into, could be a long time ago. Modifying the contractual terms of a financial instrument may also affect this assessment, as discussed in Note *2.3 Modification of loans.*

Determining whether credit risk has increased significantly

The Group has established a framework that incorporates both quantitative and qualitative information to determine whether the credit risk on a particular financial instrument has increased significantly since initial recognition. The framework aligns with the Group's internal credit risk management process.

The criteria for determining whether credit risk has increased significantly will vary by portfolio and will include a backstop based on delinquency.

Quantitative Criteria:

For financial instruments other than the Group's investment portfolio, the Group will presumptively consider that a significant increase in credit risk occurs when the borrower is more than 30 days past due on its contractual payments. The Group will determine days past due by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. In assessing whether a financial instrument has experienced a SICR, the Group also considers non-payments on connected accounts of the same issuer to the Group, which exceed 30 days.

Qualitative Criteria:

Using its expert credit judgement and, where possible, relevant historical experience, the Group may determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

If the borrower meets one or more of the following criteria, the internal grading of the credit facility falls due to a significant increase in credit risk i.e. transition to Stage 2:

- Excesses over an overdraft limit become fairly frequent and/or exceed the 30 days past due (latter automated in the core banking system).
- A few cheques returned unpaid.
- Review of borrowing accounts overdue.
- Trading losses that indicate a negative financial trend leading to an unsound financial position
- A significant downgrade from a superior credit rating.
- Significant decrease in collateral value which is expected to increase risk of default (for bullet repayment loans only, such as commercial property-for-resale and/or residential Bridge Loans repayable from sale of the same collateral)
- Early signs of cash flow/liquidity problems such as delay in servicing of trade creditors/loans and/or non-collection of debtors/amounts due.

The assessment of SICR incorporates forward-looking information and is performed on a regular basis. More detail is provided in note 42.3.2.4.

The Group monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- The criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- The average time between the identification of a significant increase in credit risk and default appears reasonable; and
- Exposures are not generally transferred directly from 12-month ECL measurement (Stage 1) to credit-impaired (Stage 3).

The Group has used the low credit risk exemption for the investments' portfolio in the year ended 31 December 2018, meaning that such financial instruments were not subject to SICR test.

42.3.2.2 Definition of Default and credit impaired

Under IFRS 9, the Group will consider a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held);
- with respect to loans and advances to customers, the borrower is more than 90 days past due on any material credit obligation to the Group. Overdrafts are considered past due once the customer has either exceeded a sanctioned limit or has been advised of a limit that is smaller than the current balance outstanding; or
- with regards to the investments' portfolio, a payment by the counterparty or issuer is more than 30 days past due.

This definition is largely consistent with the definition that will be used for regulatory purposes.

In assessing whether a borrower is in default, the Group will consider indicators that are:

- qualitative: e.g. breaches of covenant;
- quantitative: e.g. overdue status and non-payment of another obligation of the same issuer to the Group; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

At each reporting date, the Group assesses whether financial assets carried at amortised cost, debt financial assets carried at FVTOCI, loan commitments and financial guarantees are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Group on terms that the Group would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of three months. This period of three months has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions.

42.3.2.3 Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit impaired.

Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

PD estimates are estimates at a certain date, which, for loans and advances to customers, loan commitments and financial guarantees, are calculated based on statistical rating models and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally-compiled data comprising both quantitative and qualitative factors. PDs are estimated considering the contractual maturities of exposures and estimated prepayment rates. They are adjusted to reflect forward-looking information as described below.

Market data, obtained from a third party service provider, is used for the PD of the investments portfolio, balances with CBM and loans and advances to banks.

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based on the history of recovery rates of claims, adjusted by the cure rates, against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset. LGD estimates are calibrated for different economic scenarios and, for real estate lending, to reflect possible changes in property prices. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Group derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract, including amortisation and prepayments. The EAD of a financial asset is the gross carrying amount at default. For lending commitments and financial guarantees, the EAD considers the amount drawn, as well as potential future amounts that may be drawn or repaid under the contract, which will be estimated based on historical observations and forward-looking forecasts. For some financial assets, the Group determines EAD by modelling the range of possible exposure outcomes at various points in time using scenario and statistical techniques.

ECLs are a probability-weighted estimate of credit losses and are measured as follows:

- financial assets that are not credit-impaired at the reporting date: the present value of all cash shortfalls i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive;
- financial assets that are credit-impaired at the reporting date: the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn irrevocable loan commitments: the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and
- financial guarantee contracts: the present value of the expected payments to reimburse the holder less any amounts that the Group expects to recover.

Subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Group measures ECLs considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for risk management purposes, the Group considers a longer period. The maximum contractual period extends to the date at which the Group has the right to require repayment of an advance or terminate a loan commitment or guarantee.

For retail overdrafts and certain corporate revolving facilities that include both a loan and an undrawn commitment component, the Group measures ECLs over a period longer than the maximum contractual period if the Group's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Group's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are risk managed on an individual basis; these facilities are however collectively assessed for IFRS 9 purposes. Although the Group can cancel these facilities with immediate effect, this contractual right is not enforced in the normal day-to-day management, but rather only when the Group becomes aware of an increase in credit risk at the facility level. This longer period will be estimated taking into account the credit risk management actions that the Group expects to take and that serve to mitigate ECLs. These include a reduction in limits and cancellation of the facility.

42.3.2.4 Forward Looking Information

Under IFRS 9, the Group incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since initial recognition and its measurement of ECLs. The assessment of significant increase in credit risk and the calculation of ECL, both incorporate forward-looking information. The Group performs a historical analysis and identifies the key economic variables affecting credit risk and expected credit losses for each portfolio. These economic variables and their associated impact on the PD, EAD and LGD may vary by financial instrument. The Group performs expert judgement in this process.

A third party provider has been engaged to provide, on a regular basis, the forecasted macro-economic scenarios covering a ten-year time horizon. The 'base line' scenario represents the most-likely outcome and is the same scenario considered by the Group for the purposes of strategic planning and budgeting. Apart from the 'base line' scenario, the Group considers two other macro-economic scenarios, which represent more optimistic and more pessimistic outcomes.

As with any macro-economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of uncertainty and, therefore, the actual outcomes may be significantly different to those projected. The Group considers these forecasts to represent its best estimate of the possible outcomes.

The Group has identified key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has analysed relationships between macro-economic variables and credit risk and credit losses. These key drivers include inflation rates, unemployment rates and GDP forecasts.

42.3.2.5 Grouping shared risk characteristics

For expected credit loss provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous. In performing this grouping, there must be sufficient information for the group to be statistically credible. The characteristics and any supplementary data used to determine groupings are outlined below;

- Product type (e.g. residential/buy to let mortgage, credit cards);
- Credit risk grades;
- Industry – taking into consideration external information;
- LTV ratio band;
- Repayment type (e.g. bullet cash flow type);
- Collateral type; and
- Geographic region of exposure.

The Group has classified the existent portfolios into the following groups;

1. Loans and advances to customers;
   a. Mortgages
   b. Personal
   c. Commercial
   d. Accommodation and Food
   e. Construction
2. Loans and advances to Banks;
3. Debt instruments; and
4. Syndicated loans

The groupings are subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

42.3.3 Credit Risk Exposure

42.3.3.1 Maximum exposure to credit risk without taking account of any collateral and other credit enhancements

With respect to financial instruments which expose the Group to credit risk, the maximum exposure equals the carrying amount of these instruments, except for loan commitments and financial guarantees.

Credit risk exposures relating to the statement of financial position assets and off-balance sheet items are as follows:

	The Group Maximum exposure		The Bank Maximum exposure	
	2018	2017	**2018**	2017
	€000	€000	**€000**	€000
Cash and balances with Central Bank of Malta (excluding cash in hand)	**165,021**	76,450	**165,021**	76,450
Cheques in course of collection	**69**	39	**69**	39
Loans and advances to banks	**50,384**	33,246	**49,384**	32,246
Loans and advances to customers (net)	**864,162**	703,302	**864,162**	703,302
Loans and advances to corporate entities (net)	**389,721**	321,288	**389,721**	321,288
Syndicated loans (net)	**61,610**	26,226	**61,610**	26,226
Derivative financial instruments	**822**	3,008	**822**	3,008
Other debt and fixed income instruments (net)	**251,040**	252,324	**251,040**	252,324
Financial assets at FVTPL	**36,241**	37,045	**879**	942
Other receivables	**6,293**	6,650	**5,845**	6,122
At 31 December	**1,825,363**	1,459,578	**1,788,553**	1,421,947
Credit risk exposures relating to off-balance sheet items are as follows:				
Financial guarantees and other contingent liabilities	**23,269**	10,834	**23,269**	10,834
Commitments	**711,160**	552,000	**711,160**	552,000
At 31 December	**734,429**	562,834	**734,429**	562,834

42. RISK MANAGEMENT (Continued)

42.3 CREDIT RISK (Continued)

42.3.3.2 Concentration of Risk

The Group Concentrations of risk	Financial Institutions €000	Manufac -turing €000	Real Estate €000	Wholesale and Retail Trade €000	Public Sector €000	Other Industries €000	Individuals €000	Total €000
Cash and balances with Central Bank of Malta (excluding cash in hand)	165,021	-	-	-	-	-	-	165,021
Cheques in course of collection	69	-	-	-	-	-	-	69
Loans and advances to banks	50,384	-	-	-	-	-	-	50,384
Loans and advances to customers (gross)	73,928	21,996	160,746	42,089	11,210	135,969	824,747	1,270,685
Syndicated loans (gross)	5,000	25,043	-	10,000	2,622	19,725	-	62,390
Derivative financial instruments	822	-	-	-	-	-	-	822
Other debt and fixed income instruments (gross)	40,899	13,282	3,526	13,563	159,912	19,907	-	251,089
Financial assets at FVTPL	10,679	777	-	-	14,952	9,833	-	36,241
Other receivables	-	-	-	-	-	6,293	-	6,293
At 31 December 2018	**346,802**	**61,098**	**164,272**	**65,652**	**188,696**	**191,727**	**824,747**	**1,842,994**
Financial guarantees and other contingent liabilities	2,384	260	12,666	1,439	-	4,765	1,755	23,269
Commitments	51,268	2,108	145,995	17,032	4,129	92,422	398,206	711,160
At 31 December 2018	**53,652**	**2,368**	**158,661**	**18,471**	**4,129**	**97,187**	**399,961**	**734,429**

The Group Concentrations of risk	Financial Institutions €000	Manufac -turing €000	Real Estate €000	Wholesale and Retail Trade €000	Public Sector €000	Other Industries €000	Individuals €000	Total €000
Cash and balances with Central Bank of Malta (excluding cash in hand)	76,450	-	-	-	-	-	-	76,450
Cheques in course of collection	39	-	-	-	-	-	-	39
Loans and advances to banks	33,246	-	-	-	-	-	-	33,246
Loans and advances to customers (gross)	68,298	21,788	122,686	32,228	9,097	88,368	672,294	1,014,759
Syndicated loans (gross)	5,000	9,216	-	-	2,510	9,500	-	26,226
Derivative financial instruments	3,008	-	-	-	-	-	-	3,008
Other debt and fixed income instruments (gross)	37,247	15,100	4,070	17,877	156,224	21,806	-	252,324
Financial assets at FVTPL	16,551	984	-	826	12,812	5,840	-	37,013
Other receivables	-	-	-	-	-	6,650	-	6,650
At 31 December 2017	**239,839**	**47,088**	**126,756**	**50,931**	**180,643**	**132,164**	**672,294**	**1,449,715**
Financial guarantees and other contingent liabilities	2,662	390	1,387	1,486	-	3,528	1,381	10,834
Commitments	35,416	3,153	115,677	16,666	4,705	72,299	304,084	552,000
At 31 December 2017	**38,078**	**3,543**	**117,064**	**18,152**	**4,705**	**75,827**	**305,465**	**562,834**

42. RISK MANAGEMENT (Continued)
42.3 CREDIT RISK (Continued)

42.3.3.2 Concentration of Risk (Continued)

The Bank

Concentrations of risk	Financial Institutions €000	Manufac -turing €000	Real Estate €000	Wholesale and Retail Trade €000	Public Sector €000	Other Industries €000	Individuals €000	Total €000
Cash and balances with Central Bank of Malta (excluding cash in hand)	165,021	-	-	-	-	-	-	165,021
Cheques in course of collection	69	-	-	-	-	-	-	69
Loans and advances to banks	49,384	-	-	-	-	-	-	49,384
Loans and advances to customers (gross)	73,928	21,996	160,746	42,089	11,210	135,969	824,747	1,270,685
Syndicated loans (gross)	5,000	25,043	-	10,000	2,622	19,725	-	62,390
Derivative financial instruments	822	-	-	-	-	-	-	822
Other debt and fixed income instruments (gross)	40,899	13,282	3,526	13,563	159,912	19,907	-	251,089
Financial assets at FVTPL	-	-	-	-	879	-	-	879
Other receivables	-	-	-	-	-	5,845	-	5,845
At 31 December 2018	**335,123**	**60,321**	**164,272**	**65,652**	**174,623**	**181,446**	**824,747**	**1,806,184**
Financial guarantees and other contingent liabilities	2,384	260	12,666	1,439	-	4,765	1,755	23,269
Commitments	51,268	2,108	145,995	17,032	4,129	92,422	398,206	711,160
At 31 December 2018	**53,652**	**2,368**	**158,661**	**18,471**	**4,129**	**97,187**	**399,961**	**734,429**

The Bank

Concentrations of risk	Financial Institutions €000	Manufac -turing €000	Real Estate €000	Wholesale and Retail Trade €000	Public Sector €000	Other Industries €000	Individuals €000	Total €000
Cash and balances with Central Bank of Malta (excluding cash in hand)	76,450	-	-	-	-	-	-	76,450
Cheques in course of collection	39	-	-	-	-	-	-	39
Loans and advances to banks	32,246	-	-	-	-	-	-	32,246
Loans and advances to customers (gross)	68,298	21,788	122,686	32,228	9,097	88,368	672,294	1,014,759
Syndicated loans (gross)	5,000	9,216	-	-	2,510	9,500	-	26,226
Derivative financial instruments	3,008	-	-	-	-	-	-	3,008
Other debt and fixed income instruments (gross)	37,247	15,100	4,070	17,877	156,224	21,806	-	252,324
Financial assets at FVTPL	-	205	-	-	705	-	-	910
Other receivables	-	-	-	-	-	6,122	-	6,122
At 31 December 2017	**222,288**	**46,309**	**126,756**	**50,105**	**168,536**	**125,796**	**672,294**	**1,412,084**
Financial guarantees and other contingent liabilities	2,662	390	1,387	1,486	-	3,528	1,381	10,834
Commitments	35,416	3,153	115,677	16,666	4,705	72,299	304,084	552,000
At 31 December 2017	**38,078**	**3,543**	**117,064**	**18,152**	**4,705**	**75,827**	**305,465**	**562,834**

42.3.3.2 Concentration of Risk (Continued)

Collateral and other credit enhancements

The Group employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation. Of the total loans and advances to customers, 87.16% (2017: 84.34%) were collateralised.

The Group prepares a valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically. The principal collateral types for loans and advances are:

- Cash and securities;
- Government guarantees;
- Mortgages over residential properties, with the substantial majority being situated in Malta;
- Charges over business assets such as premises, inventory and accounts receivable; and
- Charges over financial instruments such as debt securities, equities and insurance policies.

Longer-term finance and lending to corporate entities are generally secured, however, revolving personal credit facilities are, generally, unsecured.

Collateral held as security for financial assets other than loans and advances depends on the nature of the instrument. Debt securities are generally unsecured, with the exception of covered bonds, which are mainly secured by residential mortgages.

The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period.

It is the Group's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the Group does not occupy repossessed properties for business use. During the year the Bank entered into a promise of sale on one of its Investment Properties with a value of €2,600,000 (Note 24).

The Group also makes use of master netting agreements with counter parties. At 31 December 2018 and 31 December 2017 there were no financial assets or liabilities arising from these agreements.

A portion of the Group's financial assets originated by the mortgage business has sufficiently low 'loan to value' (LTV) ratios, which results in no loss allowance being recognised in accordance with the Group's expected credit loss model. The carrying amount of such financial assets is €767 million at 31 December 2018.

The group closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below.

The Group / The Bank

31 December 2018	Gross Exposure €000	Impairment allowance €000	Carrying amount €000	Fair value of collateral held €000
Credit-impaired assets				
Loans to individuals:				
– Overdraft	2,089	1,358	731	745
– Credit Cards	-	-	-	-
– Term Loans	2,847	1,184	1,663	2,067
– Mortgages	6,269	1,312	4,957	5,153
Loans to corporate entities				
– Large corporate entities	-	-	-	-
– Small and medium-sized enterprises (SMEs)	39,130	12,193	26,937	29,022
– Other	-	-	-	-
Total credit-impaired assets	**50,335**	**16,047**	**34,288**	**36,987**

The Group / The Bank

The following table shows the distribution of LTV ratios for the Group's mortgage and term loans credit-impaired portfolio:

Mortgage portfolio- LTV distribution	Credit-impaired (Gross carrying amount)
	€000
Lower than 50%	2,937
50 to 60%	176
60 to 70%	203
70 to 80%	305
80 to 90%	1,094
90 to 100%	990
Higher than 100%	564
Total	**6,269**

42. RISK MANAGEMENT (Continued)

42.3 CREDIT RISK (Continued)

42.3.3.3 Credit quality

Comparative Year

The Group's and the Bank's exposure to financial assets, as rated by external credit rating agencies are presented below:

The Group **At 31 December 2017**	**Balances with CBM**	**Derivative Financial Instruments**	**Financial assets at FVTPL**	**Debt securities**	**Loans and advances to banks**	**Total**
	€000	**€000**	**€000**	**€000**	**€000**	**€000**
AAA	-	-	2,441	7,624	-	10,065
AA+ to AA-	-	-	202	21,393	1,164	22,759
A+ to A-	76,450	3,008	1,062	174,586	27,477	282,583
Lower than A-	-	-	18,878	47,657	3,605	70,140
Unrated	-	-	14,430	1,064	1,000	16,494
	76,450	3,008	37,013	252,324	33,246	402,041

The Bank **At 31 December 2017**	**Balances with CBM**	**Derivative Financial Instruments**	**Financial assets at FVTPL**	**Debt securities**	**Loans and advances to banks**	**Total**
	€000	**€000**	**€000**	**€000**	**€000**	**€000**
AAA	-	-	-	7,624	-	7,624
AA+ to AA-	-	-	202	21,393	1,164	22,759
A+ to A-	76,450	3,008	286	174,586	27,477	281,807
Lower than A-	-	-	422	47,657	3,605	51,684
Unrated	-	-	-	1,064	-	1,064
	76,450	3,008	910	252,324	32,246	364,938

Loans and advances to customers by internal rating based on the Banking Rules

The following table provides a detailed analysis of the credit quality of the Group's and Bank's lending:

	2017 €000
Neither past due nor impaired	944,964
Past due but not impaired	38,485
Impaired	31,310
	1,014,759

Analysis of financial assets that are neither past due nor impaired by internal credit rating

The Group / The Bank	2017 €000
Regular	927,927
Watch List	4,604
Sub-Standard	8,217
	940,748

42.3.3.3 Credit quality (Continued)

Analysis of financial assets that are past due but not impaired

Past due loans and advances include those that are only past due by a few days. An analysis of past due loans by age but not specifically impaired is provided below:

The Group / The Bank	2017 €000
Past due up to 29 days	9,357
Past due 30-59 days	9,391
Past due 60-89 days	564
Past due over 90 days	19,173
	38,485

Individually impaired gross loans by segment

The Group / The Bank	2017 €000
Personal	7,366
Business	36,088
	43,454

Rescheduled loans and advances to customers that would otherwise be past due totalled €3,261,898.

Information on impaired and past due facilities by significant industry and by significant geographical area, as required by BR/07/2014 – Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised under the Banking Act 1994, is not being disclosed because given the Bank's small loan portfolio, the identity of clients may be easily inferred from such information.

Current Year

The following table sets out information about the credit quality of financial assets measured at amortised cost and FVTOCI. Unless specifically indicated, for financial assets, the amount in the table represents gross carrying amounts.

Explanation of the terms 12-month ECL, lifetime ECL and credit-impaired are included in the previous notes discussed.

The Group / The Bank **31 December 2018**	**12-month ECL €000**	**Lifetime ECL not credit-impaired €000**	**Lifetime ECL credit-impaired €000**	**Total €000**
Loans and advances to customers - amortised cost				
Grade 1-4: Low risk	1,202,105	-	-	1,202,105
Grades 5-6: Watch & substandard	-	18,245	-	18,245
Grade 7: Doubtful	-	-	21,774	21,774
Grade 8: Classified	-	-	28,561	28,561
Loss allowance	(337)	(418)	(16,047)	(16,802)
Carrying amount	**1,201,768**	**17,827**	**34,288**	**1,253,883**
Debt securities - amortised cost				
Investment grade	85,405	-	-	85,405
Sub Investment grade	500	-	-	500
Loss Allowance	(49)	-	-	(49)
Carrying amount	**85,856**	**-**	**-**	**85,856**
Debt securities - FVTOCI[2]				
Investment grade	163,899	-	-	163,899
Sub Investment grade	1,285	-	-	1,285
Carrying amount	**165,184**	**-**	**-**	**165,184**
Syndicated loans				
Investment grade	5,000	-	-	5,000
Sub Investment grade	52,390	5,000	-	57,390
Loss allowance	(688)	(92)	-	(780)
Carrying amount	**56,702**	**4,908**	**-**	**61,610**

[2] No loss allowance is recognised in the Statement of Financial Position for debt instruments measured at FVTOCI as the amount is at fair value.

42.3.4 Loss Allowance

Current Year

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stage 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period and the consequent "step up" (or "step down") between 12 month and Lifetime ECL.
- Additional allowance for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period.
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models.
- Impacts on the measurements of ECL due to changes made to models and assumptions.
- Discount unwind within ECL due to passage of time, as ECL is measured on a present value basis.
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements.
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period.

The Group / The Bank Loans and advances to customers at amortised cost	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL (but not POCI) €000	Total €000
31 December 2017 under IAS 39	3,369	60	12,966	16,395
Adjustment upon initial application of IFRS 9 (note 15)	(2,749)	191	2,218	(340)
Loss allowance at 1 January 2018 under IFRS 9	**620**	**251**	**15,184**	**16,055**
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	(52)	-	-	(52)
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	(19)	(19)
Write-offs	-	-	(528)	(528)
New financial assets originated or purchased	129	23	1,875	2,027
Financial assets derecognised during the period	(173)	(11)	(1,047)	(1,231)
Increase / Decrease due to change in Credit Risk	(187)	155	582	550
Loss allowance at 31 December 2018	**337**	**418**	**16,047**	**16,802**

The Group / The Bank Debt securities at amortised cost	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL (but not POCI) €000	Total €000
31 December 2017 under IAS 39	-	-	-	-
Adjustment upon initial application of IFRS 9 (note 19)	37	-	-	37
Loss allowance at 1 January 2018 under IFRS 9	**37**	**-**	**-**	**37**
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Write-offs	-	-	-	-
New financial assets originated or purchased	23	-	-	23
Financial assets derecognised during the period	(3)	-	-	(3)
Increases/decreases due to change in credit risk	(8)	-	-	(8)
Changes in model/risk parameters	-	-	-	-
Loss allowance at 31 December 2018	**49**	**-**	**-**	**49**

42.3.4 Loss Allowance (Continued)

The Group / The Bank Debt securities at FVTOCI	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL (but not POCI) €000	Total €000
31 December 2017 under IAS 39	-	-	-	-
Adjustment upon initial application of IFRS 9 (note 19)	238	-	-	238
Loss allowance at 1 January 2018 under IFRS 9	**238**	**-**	**-**	**238**
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Write-offs	-	-	-	-
New financial assets originated or purchased	5	-	-	5
Financial assets derecognised during the period	(20)	-	-	(20)
Increases/decreases due to change in credit risk	(66)	-	-	(66)
Changes in model/risk parameters	-	-	-	-
Loss allowance at 31 December 2018	**157**	**-**	**-**	**157**

The Group / The Bank Syndicated loans	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL (but not POCI) €000	Total €000
31 December 2017 under IAS 39	-	-	-	-
Adjustment upon initial application of IFRS 9 (note 16)	429	-	-	429
Loss allowance at 1 January 2018 under IFRS 9	**429**	**-**	**-**	**429**
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	(92)	-	-	(92)
Transfer to Stage 2	-	92	-	92
Transfer to Stage 3	-	-	-	-
Write-offs	-	-	-	-
New financial assets originated or purchased	483	-	-	483
Financial assets derecognised during the period	-	-	-	-
Increases/decreases due to change in credit risk	(132)	-	-	(132)
Changes in model/risk parameters	-	-	-	-
Foreign Exchange and other movements	-	-	-	-
Loss allowance at 31 December 2018	**688**	**92**	**-**	**780**

42. RISK MANAGEMENT (Continued)

42.3 CREDIT RISK (Continued)

42.3.4 Loss Allowance (Continued)

The following tables further explain changes in the gross carrying amount of each portfolio to help explain their significance to the changes in the loss allowance for the same portfolio as discussed above:

The Group / The Bank	**Stage 1**	**Stage 2**	**Stage 3**	
Loans and advances to customers at amortised cost	**12-month ECL**	**Lifetime ECL**	**Lifetime ECL (but not POCI)**	**Total**
	€000	**€000**	**€000**	**€000**
Gross carrying amount at 1 January 2018	938,933	21,683	54,155	1,014,771
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	117	-	-	117
Transfer to Stage 2	-	(1,097)	-	(1,097)
Transfer to Stage 3	-	-	105	105
Write-offs	-	-	(528)	(528)
New financial assets originated or purchased	316,559	2,833	5,951	325,343
Financial assets derecognised during the period	(91,996)	(3,495)	(8,563)	(104,054)
Increase / Decreases due to changes in Credit Risk	38,492	(1,679)	(785)	36,028
Gross carrying amount at 31 December 2018	**1,202,105**	**18,245**	**50,335**	**1,270,685**

The Group / The Bank	**Stage 1**	**Stage 2**	**Stage 3**	
Debt securities at amortised cost	**12-month ECL**	**Lifetime ECL**	**Lifetime ECL (but not POCI)**	**Total**
	€000	**€000**	**€000**	**€000**
Gross carrying amount at 1 January 2018	72,775	-	-	72,775
Movements in Loss allowance				
Transfers:	-	-	-	-
Transfer to Stage 1	-	-	-	-
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Write-offs	-	-	-	-
New financial assets originated or purchased	38,399			38,399
Financial assets derecognised during the period	(24,973)			(24,973)
Changes to modifications that did not result in derecognition	(296)	-	-	(296)
Changes in model/risk parameters	-	-	-	-
Foreign Exchange and other movements	-	-	-	-
Gross carrying amount at 31 December 2018	**85,905**	**-**	**-**	**85,905**

The Group / The Bank	**Stage 1**	**Stage 2**	**Stage 3**	
Syndicated loans	**12-month ECL**	**Lifetime ECL**	**Lifetime ECL (but not POCI)**	**Total**
	€000	**€000**	**€000**	**€000**
Gross carrying amount at 1 January 2018	26,213	-	-	26,213
Movements in Loss allowance				
Transfers:				
Transfer to Stage 1	(5,000)	-	-	(5,000)
Transfer to Stage 2	-	5,000	-	5,000
Transfer to Stage 3	-	-	-	-
Write-offs	-	-	-	-
New financial assets originated or purchased	36,177	-	-	36,177
Financial assets derecognised during the period	-	-	-	-
Changes in model/risk parameters	-	-	-	-
Foreign Exchange and other movements	-	-	-	-
Gross carrying amount at 31 December 2018	**57,390**	**5,000**	**-**	**62,390**

42. RISK MANAGEMENT (Continued)
42.3 CREDIT RISK (Continued)

42.3.4 Loss Allowance (Continued)

Comparative Year
Analysis of loans and advances to customers that are performing or non-performing exposures

Non-performing exposures are those that satisfy either or both of the following criteria:

a) Material exposures which are more than 90 days past-due;
b) The borrower is assessed as unlikely to pay its credit obligations in full without realization of collateral, regardless of the existence of any past-due amount or of the number of days past due.

Forbearance measures occur when a borrower is about to face difficulties in meeting its financial commitments, due to financial difficulties.

The following table provides a detailed analysis of the impairment allowances on the exposures of the Group's and Bank's lending portfolio:

Impairment Allowances on Total/Forborne Exposures The Group / The Bank	Total 2017 €000	of which forborne 2017 €000
Performing		
Neither past due nor impaired	3,377	19
Past due <90days, but not impaired	52	1
Non-performing		
Past due >90 days, but not impaired	2,690	822
Impaired	10,276	3,663
Total allowances	**16,395**	**4,505**

Analysis of loans and advances to customers that are performing or non-performing exposures
The following table provides a detailed analysis of the performing and non-performing exposures of the Group's and Bank's lending portfolio:

The Group / The Bank	Total 2017 €000	of which forborne 2017 €000
Performing		
Neither past due nor impaired	966,974	3,294
Past due < 90days, but not impaired	23,528	3,690
Non-performing		
Past due >90 days, but not impaired	19,173	7,401
Impaired	31,310	16,152
Total gross/forborne exposures	**1,040,985**	**30,537**

42. RISK MANAGEMENT (Continued)

42.3 CREDIT RISK (Continued)

42.3.5 Write-off Policy

The Group writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include:

- ceasing enforcement activity; and
- situations where the Group's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full.

The Group does not have any enforcement activities on written-off activities, meaning that the Group does not seek to recover amounts which is legally owed in full, once these are written off.

42.3.6 Modification of Financial Assets

The Group sometimes modifies the terms of loans provided to customers. The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value.

Under IFRS 9, when the terms of a financial asset are modified but the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- internal grading/credit rating at the reporting date based on the modified terms; with
- internal grading/credit rating on initial recognition at the original contractual terms.

The Group renegotiates loans and advances to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Group's forbearance policy, loan forbearance is granted on a selective basis if:

- the debtor is currently in default on its debt or if there is a high risk of default;
- there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms; and
- the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, revision of interest rate, or changing the timing of interest payments. Both retail and corporate loans are subject to the forbearance policy. The appropriate committee, depending on the facility amount and type of facility, reviews reports on forborne facilities on a regular basis.

For financial assets modified as part of the Group's forbearance policy, the credit grading will reflect whether the modification has improved or restored the Group's ability to collect interest and principal and the Group's previous experience of similar forbearance action. As part of this process, the Group will evaluate the borrower's payment performance against the modified contractual terms and consider various behavioural indicators.

Generally, forbearance is a qualitative indicator of default and credit impairment and expectations of forbearance are relevant to assessing whether there is a significant increase in credit risk. Following forbearance, a customer needs to demonstrate consistently good payment behaviour over a period of one year before the exposure is no longer considered to be in default/credit-impaired.

42.4 LIQUIDITY RISK

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or other financial assets. It arises because of the possibility that the Group might be unable to meet its payment obligations when they fall due. To limit this risk, the Group has arranged for diversified funding sources. The Group also manages this risk by matching the maturities of assets and liabilities.

The Group maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow.

The disclosures made in the financial statements showing maturities are intended to show the timing of cash flows arising from assets and liabilities.

The table below classifies the assets and liabilities into relevant maturity groupings, based on the remaining period to the contractual maturity date. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date it could be required to pay and the table below does not reflect the expected cash flows indicated by its deposit retention history.

42. RISK MANAGEMENT (Continued)

42.4 LIQUIDITY RISK (Continued)

The Group At 31 December 2018	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Assets						
Cash and balances with Central Bank of Malta	175,408	-	-	-	-	175,408
Cheques in course of collection	69	-	-	-	-	69
Loans and advances to banks	49,384	1,000	-	-	-	50,384
Loans and advances to customers (net)	15,144	101,297	97,039	1,040,403	-	1,253,883
Syndicated loans (net)	-	-	22,536	39,074	-	61,610
Derivative financial instruments	-	3	717	102	-	822
Other debt and fixed income instruments (net)	3,633	36,106	98,552	112,749	-	251,040
Financial assets at FVTPL	-	656	7,598	21,517	6,470	36,241
Equity and other non-fixed income instruments	-	-	-	-	1,272	1,272
Investment in associates	-	-	-	-	17,748	17,748
Other assets	3,227	1,162	185	1,719	36,460	42,753
	246,865	140,224	226,627	1,215,564	61,950	1,891,230
Liabilities and equity						
Amounts owed to banks	404	7,059	67,010	-	-	74,473
Derivative financial instruments	-	3	717	102	-	822
Amounts owed to customers	1,002,209	302,371	296,564	49,164	-	1,650,308
Other liabilities	3,448	1,179	1,974	395	16,387	23,383
Equity	-	-	-	-	142,244	142,244
	1,006,061	310,612	366,265	49,661	158,631	1,891,230
Gap	**(759,196)**	**(170,388)**	**(139,638)**	**1,165,903**	**(96,681)**	**-**

The Group At 31 December 2017	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Assets						
Cash and balances with Central Bank of Malta	89,539	-	-	-	-	89,539
Cheques in course of collection	39	-	-	-	-	39
Loans and advances to banks	32,246	1,000	-	-	-	33,246
Loans and advances to customers (net)	22,935	93,697	64,484	817,248	-	998,364
Syndicated loans (net)	-	12	7,510	18,704	-	26,226
Derivative financial instruments	-	-	1,492	1,516	-	3,008
Other debt and fixed income instruments (net)	253	37,685	113,252	101,134	-	252,324
Financial assets at FVTPL	-	1,474	4,495	16,614	14,462	37,045
Equity and other non-fixed income instruments	-	-	-	-	1,793	1,793
Investment in associates	-	-	-	-	18,224	18,224
Other assets	4,165	1,361	89	1,034	29,988	36,637
	149,177	135,229	191,322	956,250	64,467	1,496,445
Liabilities and equity						
Amounts owed to banks	30,200	13,922	67,010	-	-	111,132
Derivative financial instruments	-	-	1,492	1,516	-	3,008
Amounts owed to customers	805,347	209,856	152,727	57,646	-	1,225,576
Other liabilities	634	1,840	2,469	387	14,996	20,326
Equity	-	-	-	-	136,403	136,403
	836,181	225,618	223,698	59,549	151,399	1,496,445
Gap	**(687,004)**	**(90,389)**	**(32,376)**	**896,701**	**(86,932)**	**-**

The Bank At 31 December 2018	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Assets						
Cash and balances with Central Bank of Malta	174,511	-	-	-	-	174,511
Cheques in course of collection	69	-	-	-	-	69
Loans and advances to banks	49,384	-	-	-	-	49,384
Loans and advances to customers (net)	15,144	101,297	97,039	1,040,403	-	1,253,883
Syndicated loans (net)	-	-	22,536	39,074	-	61,610
Derivative financial instruments	-	3	717	102	-	822
Other debt and fixed income instruments (net)	3,633	36,106	98,552	112,749	-	251,040
Financial assets at FVTPL	-	-	483	396	-	879
Equity and other non-fixed income instruments	-	-	-	-	1,272	1,272
Investment in subsidiaries	-	-	-	-	40,250	40,250
Investment in associates	-	-	-	-	14,887	14,887
Other assets	2,581	1,162	185	1,719	36,655	42,302
	245,322	138,568	219,512	1,194,443	93,064	1,890,909
Liabilities and equity						
Amounts owed to banks	404	7,059	67,010	-	-	74,473
Derivative financial instruments	-	3	717	102	-	822
Amounts owed to customers	1,005,210	302,371	296,564	49,164	-	1,653,309
Other liabilities	3,380	1,179	1,974	395	16,362	23,290
Equity	-	-	-	-	139,015	139,015
	1,008,994	310,612	366,265	49,661	155,377	1,890,909
Gap	**(763,672)**	**(172,044)**	**(146,753)**	**1,144,782**	**(62,313)**	**-**

The Bank At 31 December 2017	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Assets						
Cash and balances with Central Bank of Malta	86,449	-	-	-	-	86,449
Cheques in course of collection	39	-	-	-	-	39
Bank Balances	-	-	-	-	-	-
Loans and advances to banks	32,246	-	-	-	-	32,246
Loans and advances to customers (net)	22,935	93,697	64,484	817,248	-	998,364
Syndicated loans (net)	-	12	7,510	18,704	-	26,226
Derivative financial instruments	-	-	1,492	1,516	-	3,008
Other debt and fixed income instruments (net)	253	37,685	113,252	101,134	-	252,324
Financial assets at FVTPL	-	-	708	202	32	942
Equity and other non-fixed income instruments	-	-	-	-	1,793	1,793
Investment in subsidiaries	-	-	-	-	40,250	40,250
Investment in associates	-	-	-	-	14,887	14,887
Other assets	3,478	1,361	89	1,034	30,143	36,105
	145,400	132,755	187,535	939,838	87,105	1,492,633
Liabilities and equity						
Amounts owed to banks	30,200	13,922	67,010	-	-	111,132
Derivative financial instruments	-	-	1,492	1,516	-	3,008
Amounts owed to customers	805,726	210,283	152,727	57,646	-	1,226,382
Other liabilities	574	1,840	2,470	387	14,930	20,201
Equity	-	-	-	-	131,910	131,910
	836,500	226,045	223,699	59,549	146,840	1,492,633
Gap	**(691,100)**	**(93,290)**	**(36,164)**	**880,289**	**(59,735)**	**-**

42. RISK MANAGEMENT (Continued)

42.4 LIQUIDITY RISK (Continued)

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2018 and 31 December 2017 based on contractual undiscounted repayment obligations:

The Group At 31 December 2018	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Liabilities						
Amounts owed to banks	404	7,059	67,010	-	-	74,473
Derivative financial instruments	-	3	717	102	-	822
Amounts owed to customers	1,004,272	303,546	298,538	49,560	-	1,655,916
Other Liabilities	3,448	1,179	1,974	395	16,387	23,383
	1,008,124	**311,787**	**368,239**	**50,057**	**16,387**	**1,754,594**

The Group At 31 December 2017	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Liabilities						
Amounts owed to banks	30,200	13,922	67,010	-	-	111,132
Derivative financial instruments	-	-	1,492	1,516	-	3,008
Amounts owed to customers	806,543	212,546	155,616	58,034	-	1,232,739
Other Liabilities	634	1,840	2,469	387	14,996	20,326
	837,377	**228,308**	**226,587**	**59,937**	**14,996**	**1,367,205**

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2018 and 31 December 2017 based on contractual undiscounted repayment obligations:

The Bank At 31 December 2018	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Liabilities						
Amounts owed to banks	404	7,059	67,010	-	-	74,473
Derivative financial instruments	-	3	717	102	-	822
Amounts owed to customers	1,007,273	303,546	298,538	49,560	-	1,658,917
Other liabilities	3,380	1,179	1,974	395	16,362	23,290
	1,011,057	**311,787**	**368,239**	**50,057**	**16,362**	**1,757,502**

The Bank At 31 December 2017	Less than three months €000	Between three months and one year €000	Between one year and five years €000	More than five years €000	Others €000	Total €000
Liabilities						
Amounts owed to banks	30,200	13,922	67,010	-	-	111,132
Derivative financial instruments	-	-	1,492	1,516	-	3,008
Amounts owed to customers	806,164	212,119	155,616	58,034	-	1,231,933
Other liabilities	574	1,840	2,465	387	14,930	20,196
	836,938	**227,881**	**226,583**	**59,937**	**14,930**	**1,366,269**

42. RISK MANAGEMENT (Continued)

42.4 LIQUIDITY RISK (Continued)

Off – Balance sheet items

To meet the financial needs of customers, the Group and the Bank enter into various commitments and contingent liabilities. Even though these obligations are not recognised on the statement of financial position (being, off-balance sheet items), they are subject to credit risk and are, therefore, part of the overall risk of the Group and the Bank.

The Group / The Bank	Not later than one year 2018 €000	2017 €000
Loan commitments	**711,160**	522,000
Guarantees, acceptance and other financial facilities	**23,269**	10,834
	734,429	532,834

Asset encumbrance

In accordance with Appendix 3 of BR07/2014 - *Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised under the Banking Act 1994* and the CRR, credit institutions shall ensure compliance with the provisions of the EBA Guidelines on Disclosure of Encumbered and Unencumbered Assets.

The Group's encumbered assets relate to debt securities which are pledged in favour of the European Central Bank for the purposes of existing and potential long term re-financing operations and also cash in favour of the Depositor Compensation Scheme.

The Group Assets at 31 December 2018	Carrying amount of encumbered assets €000	Fair value of encumbered assets €000	Carrying amount of unencumbered assets €000	Fair value of unencumbered assets €000
Equity instruments	-	-	19,020	1,524
Debt securities	148,644	155,820	138,637	108,773
Other assets	1,400	-	1,583,529	-
Assets of the reporting institution	**150,044**	**155,820**	**1,741,186**	**110,297**

The Group Assets at 31 December 2017	Carrying amount of encumbered assets €000	Fair value of encumbered assets €000	Carrying amount of unencumbered assets €000	Fair value of unencumbered assets €000
Equity instruments	-	-	20,017	2,044
Debt securities	140,408	150,197	148,961	114,551
Other assets	1,400	-	1,185,657	-
Assets of the reporting institution	**141,808**	**150,197**	**1,354,635**	**116,595**

42. RISK MANAGEMENT (Continued)

42.4 LIQUIDITY RISK (Continued)

The Bank Assets at 31 December 2018	Carrying amount of encumbered assets €000	Fair value of encumbered assets €000	Carrying amount of unencumbered assets €000	Fair value of unencumbered assets €000
Equity instruments	-	-	56,409	1,524
Debt securities	143,185	150,361	108,735	108,773
Other assets	1,400	-	1,581,180	-
Assets of the reporting institution	**144,585**	**150,361**	**1,746,324**	**110,297**

The Bank Assets at 31 December 2017	Carrying amount of encumbered assets €000	Fair value of encumbered assets €000	Carrying amount of unencumbered assets €000	Fair value of unencumbered assets €000
Equity instruments	-	-	56,930	2,044
Debt securities	138,732	148,521	114,534	114,551
Other assets	1,400	-	1,181,037	-
Assets of the reporting institution	**140,132**	**148,521**	**1,352,501**	**116,595**

In the above table, the unencumbered assets disclosed under *Other Assets* include loans and advances, cash and short- term funds, property, plant and equipment, tax assets and other assets.

The table below discloses the liabilities associated with the Bank's encumbered assets.

	The Group		The Bank	
Encumbered assets/collateral received and associated liabilities at 31 December 2018	Matching liabilities €000	Encumbered Assets €000	Matching liabilities €000	Encumbered Assets €000
Carrying amount of selected financial liabilities	**799,985**	**150,044**	**799,985**	**144,585**

	The Group		The Bank	
Encumbered assets/collateral received and associated liabilities at 31 December 2017	Matching liabilities €000	Encumbered Assets €000	Matching liabilities €000	Encumbered Assets €000
Carrying amount of selected financial liabilities	**773,137**	**141,808**	**773,137**	**140,132**

42.5 MARKET RISK

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates, and the prices of equities, bonds and commodities.

The Group's exposure to market risk is mainly in the form of interest rate risk and foreign exchange risk. The risk associated with the Group's exposure in equities is not considered to be material. Also, as disclosed in Note 17, the Bank enters into derivative contracts to economically hedge against movement in certain cash flows on financial liabilities having embedded derivatives which are separately accounted for.

42.5.1 Interest rate risk

Interest rate risk is the risk of the exposure of the Group's financial condition to unfavourable movements in interest rates. The Group manages its exposure to interest rate risk using duration gap analysis, simulation modelling and interest rate repricing gaps.

Duration Gap Analysis

The Group also monitors its resilience to interest rate shocks by adopting a capital approach using the Duration Gap Analysis. This methodology is based on offsetting the interest-sensitive longs and shorts in each time band, resulting in a single short or long position in each time band. This is the interest rate gap. Assets and liabilities are then re-priced according to a 100 basis points parallel shift in the yield curve over a period of one year. These are then netted off to determine the total impact of the assumed interest rate shift.

42. RISK MANAGEMENT (CONTINUED)

42.5 MARKET RISK (Continued)

42.5.1 Interest rate risk (Continued)

	2018 €000	2017 €000
Net effect for a twelve-month period	1,602	500

Projected net interest income

A principal part of the Group's management of interest rate risk is to monitor the sensitivity of projected net interest income under varying interest rate scenarios (simulation modelling). For simulation modelling, the business uses a combination of scenarios relevant to local businesses and local markets.

The table below sets out the impact on future net interest income of a 25 basis points shift in all yield curves on the first day of the following year based on current financial statement position/risk profiles:

	Increase/ decrease in basis points	Effect on profit before tax €000
2018	**+25**	**408**
	-25	**(1,380)**
2017	+25	140
	-25	(1,114)

The carrying amount of assets and liabilities that carry a variable interest rate is €1.2 billion and €866 million respectively (2017: €887 million and €681 million).

Impact of Interest Rate Risk on Economic Value

The Group also monitors the estimated impact of an immediate 200 basis points increase in yields on its economic value. Economic Value is defined as the present value of the expected future cash flows to be generated by the investment portfolios. The resulting impact is expressed as a percentage of the Group's Own Funds.

42.5.2 Currency risk

Currency risk is the risk of the exposure of the Group's financial position and cash flow to unfavourable movements in foreign exchange rates.The Group's financial assets and liabilities are substantially held in Euro. Limits are set on the level of exposure, both by individual currency and in total. The exposure is also monitored through regular sensitivity analysis.

The aggregate amount of assets and liabilities denominated in foreign currencies translated into Euro are as follows:

	2018			
	USD €000	GBP €000	Other €000	Total €000
Assets	**20,152**	**44,880**	**11,446**	**76,478**
Liabilities	**20,141**	**44,880**	**11,290**	**76,312**

	2017			
	USD €000	GBP £000	Other €000	Total €000
Assets	8,506	44,532	12,428	65,466
Liabilities	8,516	44,533	12,304	65,353

The minimal currency exposure is not expected to leave any significant impact on the Group's income.

42.6 OPERATIONAL RISK

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through its control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access controls, authorisation and reconciliation procedures, staff education and assessment processes, including internal audit verifications.

42. RISK MANAGEMENT (Continued)

42.7 CAPITAL MANAGEMENT

The primary objective of the Group's capital management is to ensure that the Group complies with regulatory capital requirements and has adequate capital to support its business and to maximise shareholder value. The Group manages its capital structure and makes adjustments to it in the light of regulatory developments, changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

During the current financial year, the Group continued to perform the Internal Capital Adequacy Assessment Process (ICAAP), in compliance with Banking Rule BR/12/2014 - The Supervisory Review Process of Credit Institutions Authorised Under the Banking Act 1994, as mandated by the Capital Requirements Directive. The objective of the ICAAP is to inform the Board of Directors of the ongoing assessment of the Group's risks, how the Group mitigates those risks and how much capital is necessary having considered other mitigating factors. This process takes into consideration Pillar I risks, as well as other material risks (Pillar II risks) including concentration risk, interest rate risk and reputational risk. Thus, the ICAAP serves as a key decision-making tool. The ICAAP demonstrated that the Group is well capitalised. The document was approved by the Board of Directors and submitted to the MFSA.

Further information on the Group's capital position may be found in the updated Capital Adequacy and Risk Disclosures Report which is prepared in line with the Pillar III requirements of Banking Rule BR/07/2014 – Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised Under the Banking Act, and governed by the Capital Requirements Regulation.

The capital adequacy ratio measures the Group's own funds as a percentage of the total risk-weighted assets and off-balance sheet items. The ratio for the year under review has been prepared in compliance with the Capital Requirements Regulation and Capital Requirements Directive IV requirements. During the year under review, the Group has complied with the externally imposed capital requirements. The table below summarises the composition of regulatory capital and the ratios of the Group as at the reporting date.

	The Group 2018 €000	The Group 2017 €000	The Bank 2018 €000	The Bank 2017 €000
Adjusted book value	**1,907,820**	1,502,614	**1,907,498**	1,498,804
Risk weighted amounts:				
Credit risk calculation - standardised approach				
Total assets and off-balance sheet items	**865,982**	699,174	**866,086**	696,133
Operational risk - basic indicator approach				
15% of the three year adjusted average operating income	**72,462**	63,154	**72,821**	63,940
Foreign exchange risk				
8% of the capital requirement of the net short or long position, whichever is the higher	**167**	134	**167**	134
Total credit, operational and foreign exchange risk	**938,611**	762,462	**939,074**	760,207
Tier 1 Capital	**130,888**	122,881	**127,659**	118,392
Tier 2 Capital	**-**	3,179	**-**	3,179
Total Own Funds	**130,888**	126,060	**127,659**	121,571
Capital Adequacy Ratio				
Tier 1 Ratio	**13.94%**	16.12%	**13.59%**	15.57%
Total Capital Ratio	**13.94%**	16.53%	**13.59%**	15.99%

In July 2013 the EBA issued the *'Final Draft Implementing Technical Standard on Disclosure for Own Funds by Institutions under Articles 437 (2) and 492(5) of Regulation (EU) 575/2013 (CRR)'*. This draft ITS provides a set of templates, thereby increasing transparency regarding the regulatory capital of European institutions and facilitating cross-jurisdictional comparisons. During the period from 1st January 2014 to 31 December 2017, which covers the phasing-in of the regulatory adjustments, institutions are required to complete the transitional disclosure template.

* The original own funds calculation comprises retained earnings which are adjusted to exclude the amount specified in favour of the Depositor's Compensation Scheme Reserve in line with the legislation (note 19).

42. RISK MANAGEMENT (Continued)

42.7 CAPITAL MANAGEMENT (Continued)

The Group	2018 €000	2017 €000
Common Equity Tier 1 (CET1) capital	130,888	122,881
CET1 capital: instruments and reserves	136,971	131,152
Capital instruments and the related share premium accounts	59,375	59,375
Retained earnings	61,505	53,081
Accumulated other comprehensive income	12,398	15,896
Funds for general banking risk	1,700	1,700
Non-controlling interest	1,993	1,100
CET1 capital: regulatory adjustments	(6,083)	(8,271)
Intangible assets	(5,861)	(5,092)
Regulatory adjustments relating to unrealised gains and losses pursuant to Articles 467 and 468 of Regulation (EU) No 571/2013	-	(3,179)
Regulatory adjustments due to the requirements for prudent valuation pursuant to Article 4 of Delegated Regulation (EU) 2016/101	(222)	-
Tier 2 capital	-	3,179
Regulatory adjustments applied to Tier 2 in respect of amount subject to pre-CRR treatment and transitional treatments subject to phase-out as prescribed in Regulation (EU) No 575/2013 (i.e. CRR residual amounts)	-	3,179
Total Capital	130,888	126,060
Total Risk Weighted Assets	938,611	762,462
Capital Ratios		
CET1 Capital Ratio	13.94%	16.12%
Total Capital Ratio	13.94%	16.53%
Amounts below the thresholds for deduction:		
Direct and indirect holdings of the capital of financial sector entities where the institution does not have significant investments in those entities (not included in CET 1 capital)	7,271	9,105

42. RISK MANAGEMENT (Continued)

42.7 CAPITAL MANAGEMENT (Continued)

The Bank	2018 €000	2017 €000
Common Equity Tier 1 (CET1) capital	**127,659**	118,392
CET1 capital: instruments and reserves	**133,741**	126,660
Capital instruments and the related share premium accounts	**59,375**	59,375
Retained earnings	**60,268**	49,689
Accumulated other comprehensive income	**12,398**	15,896
Funds for general banking risk	**1,700**	1,700
Non-controlling interest	**-**	-
CET1 capital: regulatory adjustments	**(6,082)**	(8,268)
Intangible assets	**(5,858)**	(5,089)
Regulatory adjustments relating to unrealised gains and losses pursuant to Articles 467 and 468	**-**	(3,179)
Regulatory adjustments due to the requirements for prudent valuation pursuant to Article 4 of Delegated Regulation (EU) 2016/101	**(224)**	-
Tier 2 capital	**-**	3,179
Regulatory adjustments applied to Tier 2 in respect of amount subject to pre-CRR treatment and transitional treatments subject to phase-out as prescribed in Regulation (EU) No 575/2013 (i.e. CRR residual amounts)	**-**	3,179
Total Capital	**127,659**	121,571
Total Risk Weighted Assets	**939,074**	760,207
Capital Ratios		
CET1 Capital Ratio	**13.59%**	15.57%
Total Capital Ratio	**13.59%**	15.99%
Amounts below the thresholds for deduction:		
Direct and indirect holdings of the capital of financial sector entities where the institution does not have significant investments in those entities (not included in CET 1 capital)	**7,271**	9,105

42. RISK MANAGEMENT (Continued)

42.7 CAPITAL MANAGEMENT (Continued)

In line with the CRR, the following table discloses the main features and the terms and conditions of Bank's Tier 1 instruments.

Capital Instruments Main Features	
Issuer	APS Bank Ltd
Unique identifier	N/A
Governing law(s) of the instrument	Maltese law
Regulatory treatment	
Transitional CRR rules	CET 1
Post-transitional CRR rules	CET 1
Eligible at solo/(sub-)consolidated/ solo&(sub-)consolidated	Solo & consolidated
Instrument type	Ordinary shares
Amount recognised in regulatory capital	57,605
Nominal amount of instrument	57,605
Issue price	N/A
Redemption price	N/A
Accounting classification	Shareholder's equity
Original date of issuance	9 September 2013*
Perpetual or dated	Perpetual
Original maturity date	No
Issuer call subject to prior supervisory approval	No
Optional call date, contingent call dates and redemption amount	No
Subsequent call dates, if applicable	No
Coupons / dividends	
Fixed or floating dividend/coupon	Floating
Coupon rate and any related index	N/A
Existence of a dividend stopper	No
Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary
Fully discretionary, partially discretionary or mandatory (in terms of amount)	Fully discretionary
Existence of step up or other incentive to redeem	No
Noncumulative or cumulative	Non-cumulative
Convertible or non-convertible	Non-convertible
Write-down features	No
Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Subordinated to creditors and depositors
Non-compliant transitioned features	No

*Various, latest date of capital injection was 9 September 2013.

Full Reconciliation of Own Funds Items to Audited Financial Statements of the Group at 31 December 2018 is presented below:

The Group	Balance sheet in accordance with IFRS €000	Reconciling items €000	Balance sheet in accordance with regulatory scope €000
Issued capital (note 33)	57,605	-	57,605
Share premium (note 34)	1,770	-	1,770
Revaluation reserve (note 35)	12,398	-	12,398
Retained earnings (note 36)	68,480	(14,185)	54,295
of which general banking reserves (note 36)	1,700	-	1,700
of which general reserve	1	-	1
Dividend reserve	-	-	-
Intangible assets (note 26)	5,861	-	5,861

FIVE YEAR SUMMARIES

STATEMENTS OF PROFIT OR LOSS

The Group	2018 €000	2017 €000	2016 €000	2015 €000	2014 €000
Interest receivable and similar income	**49,963**	42,396	38,867	38,784	38,026
Interest payable	**(12,149)**	(9,592)	(10,865)	(13,173)	(15,880)
Net interest income	**37,814**	32,804	28,002	25,611	22,146
Other operating income	**6,905**	9,946	6,894	6,094	6,178
Total operating income	**44,719**	42,750	34,896	31,705	28,324
Other operating charges	**(24,575)**	(22,363)	(18,972)	(17,182)	(15,494)
Share of results of associate, net of tax	**38**	441	828	1,754	1,142
Net impairment losses	**(1,555)**	(2,470)	(988)	(706)	(1,201)
Profit before tax	**18,627**	18,358	15,764	15,571	12,771
Income tax expense	**(6,043)**	(5,250)	(4,820)	(5,568)	(3,835)
Profit for the year	**12,584**	13,108	10,944	10,003	8,936

The Bank	2018 €000	2017 €000	2016 €000	2015 €000	2014 €000
Interest receivable and similar income	**48,958**	42,284	38,867	38,784	37,409
Interest payable	**(12,182)**	(9,592)	(10,865)	(13,173)	(15,898)
Net interest income	**36,776**	32,692	28,002	25,611	21,511
Other operating income	**8,888**	10,256	7,393	6,691	5,703
Total operating income	**45,664**	42,948	35,395	32,302	27,214
Other operating charges	**(24,427)**	(22,200)	(18,961)	(17,176)	(15,401)
Net impairment losses	**(1,555)**	(2,470)	(988)	(706)	(1,194)
Profit before tax	**19,682**	18,278	15,446	14,420	10,619
Income tax expense	**(5,974)**	(5,190)	(4,820)	(5,568)	(3,835)
Profit for the year	**13,708**	13,088	10,626	8,852	6,784

THE GROUP'S STATEMENTS OF FINANCIAL POSITION

	2018	2017	2016	2015	2014
	€000	€000	€000	€000	€000
ASSETS					
Cash, treasury bills and balances with Central Bank of Malta	10,387	13,089	6,464	6,832	5,927
Balances with Central Bank of Malta	165,021	76,450	29,956	9,165	8,370
Cheques in course of collection	69	39	42	1,970	2,185
Loans and advances to banks	50,384	33,246	60,162	43,027	49,951
Loans and advances to customers	1,253,883	998,377	806,011	695,800	623,631
Syndicated loans	61,610	26,213	-	-	-
Derivative financial instruments	822	3,008	3,164	3,560	3,872
Financial assets at FVTPL	36,241	37,045	3,321	3,815	16,106
Other debt and fixed income instruments	251,040	252,324	322,844	297,959	356,404
Equity and other non-fixed income instruments	1,272	1,793	4,119	3,348	2,448
Investment in associates	17,748	18,224	18,256	17,926	11,171
Non-current assets held-for-sale	2,600	-	-	-	-
Investment properties	1,860	4,203	3,793	3,965	4,147
Property and equipment	22,286	17,706	14,147	13,394	13,813
Intangible assets	5,861	5,093	4,061	3,137	2,091
Current tax	-	-	39	209	1,150
Deferred tax assets	3,853	2,985	1,502	2,076	682
Other receivables	6,293	6,650	6,673	5,278	5,890
TOTAL ASSETS	1,891,230	1,496,445	1,284,554	1,111,461	1,107,838
LIABILITIES					
Amounts owed to banks	74,473	111,132	36,204	35,327	78,568
Derivative financial instruments	822	3,008	3,164	3,560	3,872
Amounts owed to customers	1,650,308	1,225,576	1,099,115	942,921	892,829
Current tax	1,389	198	-	-	-
Other liabilities	11,892	9,530	8,418	3,630	3,914
Accruals and deferred income	10,102	10,598	8,265	8,224	8,807
TOTAL LIABILITIES	1,748,986	1,360,042	1,155,166	993,662	987,990
EQUITY					
Issued capital	57,605	57,605	57,605	57,605	57,605
Share premium	1,770	1,770	1,770	1,770	1,770
Revaluation reserve	12,398	15,896	21,177	18,739	19,062
Retained earnings	68,478	60,032	47,648	38,654	30,444
Dividend reserve	-	-	1,188	1,031	763
Non-controlling interest	1,993	1,100	-	-	10,204
TOTAL EQUITY	142,244	136,403	129,388	117,799	119,848
TOTAL LIABILITIES AND EQUITY	1,891,230	1,496,445	1,284,554	1,111,461	1,107,838
MEMORANDUM ITEMS					
Contingent liabilities	23,269	10,834	6,112	5,606	5,328
Commitments	711,160	552,000	379,078	209,567	211,470

FIVE YEAR SUMMARIES

THE BANK'S STATEMENTS OF FINANCIAL POSITION

	2018 €000	2017 €000	2016 €000	2015 €000	2014 €000
ASSETS					
Cash, treasury bills and balances with Central Bank of Malta	**9,490**	9,999	6,464	6,832	5,927
Balances with Central Bank of Malta	**165,021**	76,450	29,956	9,165	8,370
Cheques in course of collection	**69**	39	42	1,970	2,185
Loans and advances to banks	**49,384**	32,246	60,162	43,027	49,314
Loans and advances to customers	**1,253,883**	998,377	806,011	695,800	623,631
Syndicated loans	**61,610**	26,213	-	-	-
Derivative financial instruments	**822**	3,008	3,164	3,560	3,872
Financial assets at FVTPL	**879**	942	3,321	3,815	3,483
Other debt and fixed income instruments	**251,040**	252,324	322,844	297,959	356,404
Equity and other non-fixed income instruments	**1,272**	1,793	4,119	3,348	2,448
Investment in subsidiaries	**40,250**	40,250	305	55	5,055
Investment in associates	**14,887**	14,887	14,887	14,887	9,887
Non-current assets held-for-sale	**2,600**	-	-	-	-
Investment properties	**1,860**	4,203	3,793	3,965	4,147
Property and equipment	**22,286**	17,706	14,147	13,394	13,811
Intangible assets	**5,858**	5,089	4,061	3,137	2,091
Current Tax	**-**	-	39	209	1,150
Deferred tax assets	**3,853**	2,985	1,502	2,076	682
Other receivables	**5,845**	6,122	6,690	5,294	5,605
TOTAL ASSETS	**1,890,909**	1,492,633	1,281,507	1,108,493	1,098,062
LIABILITIES					
Amounts owed to banks	**74,473**	111,132	36,204	35,327	78,568
Derivative financial instruments	**822**	3,008	3,164	3,560	3,872
Amounts owed to customers	**1,653,309**	1,226,382	1,099,406	942,973	895,156
Current Tax	**1,321**	138	-	-	-
Other liabilities	**11,892**	9,530	8,415	3,627	3,892
Accruals and deferred income	**10,077**	10,533	8,265	8,224	8,796
TOTAL LIABILITIES	**1,751,894**	1,360,723	1,155,454	993,711	990,284
EQUITY					
Issued capital	**57,605**	57,605	57,605	57,605	57,605
Share premium	**1,770**	1,770	1,770	1,770	1,770
Revaluation reserve	**12,398**	15,896	21,177	18,739	19,062
Retained earnings	**67,242**	56,639	44,470	35,637	28,578
Dividend reserve	**-**	-	1,031	1,031	763
TOTAL EQUITY	**139,015**	131,910	126,053	114,782	107,778
TOTAL LIABILITIES AND EQUITY	**1,890,909**	1,492,633	1,281,507	1,108,493	1,098,062
MEMORANDUM ITEMS					
Contingent liabilities	**23,269**	10,834	6,112	5,606	5,328
Commitments	**711,160**	552,000	379,078	209,567	211,470

THE GROUP'S STATEMENTS OF CASH FLOWS

	2018 €000	2017 €000	2016 €000	2015 €000	2014 €000
Net cash flows from / (used in) operating activities	**141,844**	(6,037)	45,742	(36,463)	24,197
Investing activities					
Dividends received	**596**	126	211	190	373
Interest income from debt securities	**9,546**	12,074	13,121	14,833	16,105
Purchase of debt and other fixed income instruments	**(45,614)**	(12,739)	(72,594)	(40,163)	(79,730)
Proceeds on maturity and disposal of debt and other fixed income instruments	**41,197**	79,412	50,630	95,388	64,570
Purchase of financial assets at FVTPL	**(30,124)**	(38,595)	(2,582)	(1,090)	(16,643)
Proceeds on disposal of financial assets at FVTPL	**26,741**	2,766	3,041	1,307	14,499
Purchase of equity and other non-fixed income instruments	**-**	-	(807)	(617)	(359)
Proceeds on disposal of equity and other non-fixed income instruments	**397**	2,055	169	-	369
Purchase of property and equipment	**(7,543)**	(4,064)	(3,413)	(2,272)	(2,557)
Proceeds on disposal of property and equipment	**7**	31	17	-	3
Net cash flows (used in) / from investing activities	**(4,797)**	41,066	(12,207)	67,576	(3,370)
Financing activities					
Dividends paid	**(2,135)**	(1,478)	(1,294)	(928)	(2,288)
Net proceeds from non-controlling interest for shares in subsidiaries	**(64)**	(50)	-	-	4,727
Proceeds from issue of share capital	**1,017**	1,152	-	-	-
Net cash flows (used in) / from financing activities	**(1,182)**	(376)	(1,294)	(928)	2,439
Net increase in cash and cash equivalents	**135,865**	34,653	32,241	30,185	23,266
Cash and cash equivalents at 1 January	**75,113**	40,460	8,219	(21,966)	(45,232)
Cash and cash equivalents at 31 December	**210,978**	75,113	40,460	8,219	(21,966)

FIVE YEAR SUMMARIES

THE BANK'S STATEMENTS OF CASH FLOWS

	2018 €000	2017 €000	2016 €000	2015 €000	2014 €000
Net cash flows from / (used in) operating activities	**141,044**	(5,697)	45,742	(36,463)	25,721
Investing activities					
Dividends received	**1,604**	588	710	787	808
Interest income from debt securities	**9,546**	12,074	13,121	14,833	16,105
Purchase of debt and other fixed income instruments	**(45,614)**	(12,739)	(72,594)	(40,163)	(79,730)
Proceeds on maturity and disposal of debt and other fixed income instruments	**41,197**	79,412	50,630	95,388	64,570
Purchase of equity and other non-fixed income instruments	**-**	-	(807)	(617)	(359)
Proceeds on disposal of equity and other non-fixed income instruments	**397**	2,055	169	-	366
Purchase of financial assets at FVTPL	**(184)**	(502)	(2,582)	(1,090)	(6,029)
Proceeds on disposal of financial assets at FVTPL	**221**	2,350	3,041	1,307	6,656
Purchase of property and equipment	**(7,543)**	(4,059)	(3,413)	(2,272)	(2,557)
Proceeds on disposal of property and equipment	**7**	31	17	-	3
Investment in subsidiaries	**-**	(40,000)	-	-	-
Net cash flows (used in) / from investing activities	**(369)**	39,210	(11,708)	68,173	(167)
Financing activities					
Dividends paid	**(2,617)**	(1,950)	(1,793)	(1,525)	(2,288)
Net cash flows (used in)/from financing activities	**(2,617)**	(1,950)	(1,793)	(1,525)	(2,288)
Net increase in cash and cash equivalents	**138,058**	31,563	32,241	30,185	23,266
Cash and cash equivalents at 1 January	**72,023**	40,460	8,219	(21,966)	(45,232)
Cash and cash equivalents at 31 December	**210,081**	72,023	40,460	8,219	(21,966)

ACCOUNTING RATIOS

The Group	2018 %	2017 %	2016 %	2015 %	2014 %
Net interest income and other operating income to total assets	**2.4**	2.9	2.7	2.9	2.6
Operating expenses to total assets	**1.3**	1.5	1.5	1.5	1.4
Cost to income ratio	**55.0**	52.3	54.4	54.2	54.7
Profit before tax to total assets	**0.98**	1.2	1.2	1.4	1.2
Return on average capital employed after tax *	**10.1**	11.5	10.6	10.0	9.4
Profit after tax to equity *	**9.7**	10.9	10.1	10.1	8.9

	2018	2017	2016	2015	2014
Shares in issue (thousands)	**46,084**	46,084	46,084	46,084	46,084
Net assets per share *	**282c**	261c	235c	215c	197c

The Bank	2018 %	2017 %	2016 %	2015 %	2014 %
Net interest income and other operating income to total assets	**2.4**	2.9	2.8	2.9	2.5
Operating expenses to total assets	**1.3**	1.5	1.5	1.5	1.4
Cost to income ratio	**53.5**	51.7	53.6	53.2	56.6
Profit before tax to total assets	**1.0**	1.2	1.2	1.3	1.0
Return on average capital employed after tax *	**11.2**	11.8	10.6	9.6	7.9
Profit after tax to equity *	**10.8**	11.3	10.1	9.2	7.6

	2018	2017	2016	2015	2014
Shares in issue (thousands)	**46,084**	46,084	46,084	46,084	46,084
Net assets per share *	**275c**	252c	228c	208c	193c

* Return on average capital employed, profit after tax to equity and net assets per share are calculated on equity excluding the revaluation reserve.

Return on average capital employed before tax of the Bank is calculated as the return as a percentage of the 12 months ending equity balances. The average capital employed of the Group is calculated as the average of the opening and closing equity balances.