Pillar 3 Disclosures

30 September 2022

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1. Introduction

This report provides an overview of the regulatory capital and risk management practices and exposures of APS Bank and its subsidiaries (hereafter 'the Group') in line with Pillar 3 of the Basel framework. Pillar 3 of the Basel framework aims to promote financial market discipline through regulatory disclosure requirements. These requirements enable market participants to access key information relating to a bank's regulatory capital and risk exposures, in order to increase transparency and confidence about a bank's exposure to risk and the overall adequacy of its regulatory capital.

The Pillar 3 disclosures within this report are prepared in line with 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) II No. 2019/876. To enhance the comparability and consistency of banks' Pillar 3 disclosures, the EBA published guidelines on disclosure requirements under Part Eight of the CRR.

This report is not subject to external audit, however, it has undergone comprehensive internal review as outlined in the Pillar 3 Disclosures Policy. This report has been reviewed by the Chief Risk Officer and approved by the Board of Directors (hereafter referred to as 'the Board'). The Board is satisfied that the internal controls implemented around the preparation of these Additional Regulatory Disclosures are adequate and such disclosures present a fair and accurate picture of the Group's risk profile and capital position.

2. Key Risk Metrics

The Risk Department performs regular risk assessments and stress testing exercises, the results of which are presented to the Board of Directors, Risk Committee and other committees as may be required, including the Assets and Liabilities Committee (ALCO) and the Executive Committee. The Risk Appetite Dashboard, which complements the Risk Appetite Statement, is presented to the Board of Directors on a quarterly basis. These reports provide insight on the Group's risk profile and benchmarks this with the Group's risk appetite and internal limits. These are presented using a RAG approach (also known as "traffic lights"). Early warning signals and excesses are escalated to the Chief Risk Officer, followed by the Risk Committee and the Board of Directors, as deemed applicable, to ensure that the necessary corrective actions are implemented.

The following table summarises the Bank's key regulatory ratios, and their underlying components, for the reporting quarter and the preceding four quarters. These ratios form an integral part of the Bank's strategic planning and risk management framework.

EU KM1 - Key metrics

		Sep-22	Jun-22	Mar-22	Dec-21	Sep-21
	Available own funds (€000)					
1	Common Equity Tier 1 (CET1) capital	227,607	233,693	174,031	176,723	174,623
2	Tier 1 capital	227,607	233,693	174,031	176,723	174,623
3	Total capital	282,238	288,312	228,639	231,320	229,208
	Risk-weighted exposure amounts					
4	Total risk exposure amount	1,499,604	1,422,060	1,367,698	1,378,563	1,342,428
	Capital ratios (as a percentage of risk-weighted exposure amount)					
5	Common Equity Tier 1 ratio (%)	15.18%	16.43%	12.72%	12.82%	13.00%
6	Tier 1 ratio (%)	15.18%	16.43%	12.72%	12.82%	13.00%
7	Total capital ratio (%)	18.82%	20.27%	16.72%	16.78%	17.06%
	Additional own funds requirements to address risks other than the risk of excessive leverage (as a percentage of risk-weighted exposure amount)					
7a	Additional own funds requirements to address risks other than the risk of excessive leverage (%)	4.00%	4.00%	3.70%	3.70%	3.70%
7b	of which: to be made up of CET1 capital (percentage points)	2.25%	2.25%	2.08%	2.08%	2.08%
7c	of which: to be made up of Tier 1 capital (percentage points)	3.00%	3.00%	2.78%	2.78%	2.78%
7d	Total SREP own funds requirements (%)	12.0%	12.0%	11.70%	11.70%	11.70%
	Combined buffer and overall capital requirement (as a percentage of risk-weighted exposure amount)					
8	Capital conservation buffer (%)	2.50%	2.50%	2.50%	2.50%	2.50%
8a	Conservation buffer due to macro-prudential or systemic risk identified at the level of a Member State (%)	-	-	-	-	-
9	Institution specific countercyclical capital buffer (%)	0.00%	0.00%	0.00%	0.00%	0.00%
9a	Systemic risk buffer (%)	-	-	-	-	-
10	Global Systemically Important Institution buffer (%)	-	-	-	-	-
10a	Other Systemically Important Institution buffer (%)	0.125%	0.125%	0.125%	0.06%	0.06%
11	Combined buffer requirement (%)	2.64%	2.63%	2.63%	2.56%	2.56%
11a	Overall capital requirements (%)	14.64%	14.63%	14.33%	14.26%	14.26%
12	CET1 available after meeting the total SREP own funds requirements (%)	8.19%	9.65%	6.09%	6.42%	6.50%

	Leverage ratio					
13	Total exposure measure	3,198,985	3,149,505	2,977,556	2,871,279	2,777,939
14	Leverage ratio (%)	7.11%	7.42%	5.84%	6.15%	6.29%
	Additional own funds requirements to address the risk of excessive leverage (as a percentage of total exposure measure)					
14c	Regulatory minimum leverage ratio requirement (%)	3.00%	3.00%	3.00%	3.00%	3.00%
	Liquidity Coverage Ratio					
15	Total high-quality liquid assets (HQLA) (Weighted value -average)	514,187	495,721	466,941	443,370	432,858
16a	Cash outflows - Total weighted value	402,518	384,888	371,161	359,090	351,705
16b	Cash inflows - Total weighted value	58,994	56,196	61,044	56,904	58,957
16	Total net cash outflows (adjusted value)	343,524	328,693	310,117	302,185	292,749
17	Liquidity coverage ratio (%)	149.43%	150.51%	150.99%	147.28%	148.05%
	Net Stable Funding Ratio					
18	Total available stable funding	2,548,536	2,483,686	2,377,648	2,288,589	2,241,123
19	Total required stable funding	1,892,401	1,777,060	1,681,725	1,682,802	1,637,977
20	NSFR ratio (%)	134.67%	139.76%	141.38%	136.00%	136.82%

3. Capital Management

The Group continuously aims at building and sustaining a strong capital base and at applying it efficiently throughout its activities to reach its strategic objectives, optimise shareholder value whilst ensuring the sustainability of its business model and risk profile. A strong and prudent capital base is one of the pillars of the Group's business model and maintaining adequate capital ratios will continue being key to enable the Group to steer through the currently challenging economic conditions.

Capital planning is a crucial pillar 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.

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, which are part of the Internal Capital Adequacy Assessment Process (ICAAP). 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.

3.1. Capital Instruments

The Group' capital is composed of Common Equity Tier 1 (CET 1) and Tier 2 capital instruments, as defined by the CRR. CET 1 capital is the highest quality capital and, therefore, the most effective in absorbing losses. The Group's capital is mainly composed of CET 1 capital, which primarily consists of ordinary share capital and retained earnings. In June 2022 the Bank issued its first public offering worth €65,800,000, hence strengthening further its capital position. Further information on the Initial Public Offering is provided in Note 10 to the Condensed Interim Financial Statements for June 2022 which are available on the Bank's website.

In November 2020, the Bank joined the list of issuers on the Malta Stock Exchange with the listing of the €55,000,000 3.25% APS Bank plc Unsecured Subordinated Bonds 2025-2030. The subordinated bond qualifies as Tier 2 Capital, which ranks after the claims of all depositors (including financial institutions) and all other creditors.

3.2. Capital Requirements

In accordance with the CRR, the Group calculates its capital requirements for Pillar 1 risks using the following approaches:

- The Standardised Approach 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.
- The Standardised Approach for the purposes of calculating its risk-weighted exposure to foreign exchange risk. 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 Basic Indicator Approach for the purposes of calculating its risk-weighted exposure to operational risk. Under this approach, a 15% capital charge is applied on the average operating income for the previous three financial years.

The following table discloses the Bank's risk weighted assets and capital requirements as at 30 September 2022 for each exposure class in line with the CRR, and the respective Pillar 1 capital requirement based on the methods outlined above.

EU OV1 – Overview of total risk exposure amounts

		RWA		Minimum Capital requirements
		Sep-22 €000	Jun-22 €000	Sep-22 €000
1	**Credit risk (excluding counterparty credit risk)**	**1,394,502**	**1,316,957**	**111,560**
2	*Of which: standardised approach*	*1,394,502*	*1,316,957*	*111,560*
	Central government or central banks	*12,856*	*10,894*	*1,029*
	Multilateral development banks	*2,006*	*2,086*	*160*
	Institutions	*17,919*	*26,561*	*1,434*
	Corporates	*414,907*	*368,631*	*33,192*
	Retail	*54,493*	*53,673*	*4,359*
	Secured by mortgages on immovable property	*624,084*	*597,980*	*49,927*
	Exposures in default	*77,683*	*80,517*	*6,215*
	Items associated with particular high risk	*81,815*	*73,760*	*6,545*
	Covered bonds	*1,761*	*191*	*141*
	Claims in the form of CIU	*26,926*	*25,856*	*2,154*
	Equity exposures	*325*	*327*	*26*
	Other Assets	*79,727*	*76,481*	*6,378*
19	**Market risk**	**15**	**16**	**1**
20	*Of which: standardised approach*	*15*	*16*	*1*
23	**Operational risk**	**105,087**	**105,087**	**8,407**
24	*Of which basic indicator approach*	*105,087*	*105,087*	*8,407*
29	**Total**	**1,499,604**	**1,422,060**	**119,968**

The Bank is required to meet a total SREP capital requirement (TSCR) of 12%, consisting of 8.0% minimum Pillar 1 requirement and a 4.0% Pillar 2 requirement (P2R). In line with the Capital Requirement Directive (CRD V), which came into force in June 2021, banks may partially use capital instruments that do not qualify as Common Equity Tier 1 (CET1) capital, for example Additional Tier 1 or Tier 2 instruments, to meet the P2R.

Banking Rule BR/15/2015 – *Capital Buffers of Credit Institutions Authorised Under Banking Act 1994* requires institutions to maintain capital buffers over and above the Pillar 1 requirements. In accordance with this Rule, the Group maintains a Capital Conservation Buffer (CCB), a Countercyclical Capital Buffer (CCyB) and an Other-Systemically Important Institutions (O-SII) buffer. The capital buffers (collectively referred to as the Combined Buffer Requirement) are to be met from Common Equity Tier 1 capital and, if the minimum buffer requirements are breached, the Group might be subject to capital distribution constraints. Further information on the Group's capital buffer requirements is provided in tables 'EU CC1' and 'EU CCyB1' below

As at 30 September 2022, the Bank's Tier 1 and Total Capital Ratios stood at 15.2% and 18.8%, respectively, thereby above the respective applicable regulatory minima.

4. 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 the Group's assets are not stably funded in the medium and long term.

The Liquidity Coverage Ratio (LCR) measures the Bank's liquidity buffer to its net liquidity outflows over a 30 calendar days stress period. The Bank reports this ratio to the MFSA on a monthly basis. The Bank's LCR remained consistently above the applicable minimum requirement of 100% and stood at 137% as at 30 September 2022 (compared to 168% as at 30 June 2022).

The movement in the LCR during the third quarter of 2022 is attributed to a decline in the liquidity buffer, and an increase in net cash outflows.

The Bank's liquidity buffer is classified into:

- Level 1 assets (94%), which include withdrawable central bank reserves and central government assets; and
- Level 2 assets (6%), which include regional government or public sector entity assets and corporate debt securities with a credit rating of BBB- or higher.

The decline in the liquidity buffer was driven mainly by a decline in coins, banknotes and withdrawable central bank reserves (Level 1 assets). During the reporting period excess cash was invested in High Quality Assets (debt securities) which classify as Level 1 and Level 2A. Net cash outflows increased during the reporting period mainly due to an increase in customer deposits.
The table overleaf discloses quantitative information on the Bank's LCR for each of the four calendar quarters, starting December 2021 and ending September 2022. The figures are calculated as the simple averages of month-end observations over the twelve months preceding the end of each quarter. The difference between the Group and the Bank's LCR is immaterial. Given that the Bank does not have another 'material currency'[1], other than the Euro, the Bank reports the LCR in the reporting currency (Euro).

[1] Banks are required to assess the LCR by material currencies. A currency is considered to be a 'material currency' if the aggregate liabilities denominated in that currency amount to, or exceed, 5% of the bank's total liabilities.

EU LIQ1 - Quantitative information of Liquidity Coverage Ratio (LCR)

		Total unweighted value (average)				Total weighted value (average)			
Quarter ending on		Sep-22 €000	Jun-22 €000	Mar-22 €000	Dec-21 €000	Sep-22 €000	Jun-22 €000	Mar-22 €000	Dec-21 €000
Number of data points used in the calculation of average		**12**	**12**	**12**	**12**	**12**	**12**	**12**	**12**
High-quality liquid assets									
1	Total HQLA					514,187	495,721	466,941	443,370
Cash outflows									
2	Retail deposits and deposits from small business customers, of which:	1,289,795	1,231,114	1,172,738	1,117,192	93,324	88,423	83,668	77,875
3	*Stable deposits*	*923,618*	*889,662*	*855,250*	*822,731*	*46,180*	*44,483*	*42,762*	*41,137*
4	*Less Stable deposits*	*366,177*	*341,452*	*317,488*	*294,461*	*47,144*	*43,940*	*40,906*	*36,738*
5	Unsecured wholesale funding, of which:	485,561	453,659	430,121	409,523	246,212	232,429	222,104	213,425
7	*Non-operational deposits (all counterparties)*	*485,561*	*453,659*	*430,121*	*409,523*	*246,212*	*232,429*	*222,104*	*213,425*
9	Secured wholesale funding					-	-	-	-
10	Additional requirements, of which:	817,818	818,545	819,246	826,770	59,938	59,371	59,799	61,944
13	*Credit and liquidity facilities*	*817,818*	*818,545*	*819,246*	*826,770*	*59,938*	*59,371*	*59,799*	*61,944*
14	Other contractual funding obligations	3,045	4,678	5,890	6,564	3,044	4,665	5,590	5,846
15	Other contingent funding obligations	3,149	1,616	-	-	-	-	-	-
16	**Total Cash Outflows**					402,518	**384,888**	**371,161**	**359,090**
Cash Inflows									
18	Inflows from fully performing exposures	65,584	62,996	67,936	64,441	56,929	54,204	58,513	54,855
19	Other cash inflows	2,065	1,991	2,531	2,050	2,065	1,991	2,531	2,050
20	**Total Cash Inflows**	**67,649**	**64,987**	**70,467**	**66,491**	58,994	**56,195**	**61,044**	**56,905**
Total Adjusted Value									
21	**Liquidity buffer**					**514,187**	**495,721**	**466,941**	**443,370**
22	**Total net cash outflows**					**343,524**	**328,693**	**310,117**	**302,185**
23	**Liquidity Coverage Ratio (%)**					**149.4%**	**150.51%**	**150.99%**	**147.28%**

The Net Stable Funding Ratio (NSFR) measures the amount of stable funding available to a financial institution against the required amount of stable funding. Under CRR II, institutions are required to maintain a NSFR of at least 100%. Given that the Bank does not have a 'material currency'[2], other than the Euro, the Bank reports the NSFR in the reporting currency (Euro), regardless of the actual denomination of assets, liabilities and off-balance sheet items. All liabilities with a residual maturity of one year or more shall be subject to a 100% ASF factor, unless otherwise specified in CRR II.

At 134.7%, the Bank's NSFR was above the regulatory minimum requirement and within the Bank's risk appetite as at 30 September 2022. The ratio remained relatively stable during the third quarter of 2022 (Jun-22: 139.8%).

[2] Banks are required to assess the NSFR by material currencies. A currency is considered to be a 'material currency' if the aggregate liabilities denominated in that currency amount to, or exceed, 5% of the bank's total liabilities.

EU LIQ2 - Net Stable Funding Ratio

		Unweighted value by residual maturity				
		No Maturity	< 6 months	6 months to <1 year	> 1 year	Weighted Value
		€000	€000	€000	€000	€000
Available stable funding (ASF) Items						
1	Capital items and instruments	-	-	-	307,450	307,450
2	*Own funds*	-	-	-	307,450	307,450
4	Retail deposits		1,585,897	131,124	305,685	1,907,675
5	*Stable deposits*		*1,064,725*	*68,654*	*204,654*	*1,281,365*
6	*Less stable deposits*		*521,172*	*62,470*	*101,031*	*626,310*
7	Wholesale funding		589,398	61,064	73,147	313,220
9	*Other wholesale funding*		*589,398*	*61,064*	*73,147*	*313,220*
11	Other liabilities	-	22,030	2,082	19,150	20,191
13	*All other liabilities and capital instruments not included in the above categories*		*22,030*	*2,082*	*19,150*	*20,191*
14	**Total available stable funding (ASF)**					**2,548,536**
Required stable funding (RSF) Items						
15	Total high-quality liquid assets (HQLA)					20,794
17	Performing loans and securities:		78,915	122,265	2,083,979	1,584,352
19	*Performing securities financing transactions with financial customer collateralised by other assets and loans and advances to financial institutions*		*39,783*	*29,414*	*84,820*	*103,506*
20	*Performing loans to non- financial corporate clients, loans to retail and small business customers, and loans to sovereigns, and PSEs, of which:*		*10,375*	*80,244*	*614,889*	*559,002*
21	*With a risk weight of less than or equal to 35% under the Basel II Standardised Approach for credit risk*		*889*	*5,840*	*44,815*	*32,495*
22	*Performing residential mortgages, of which:*		*9,936*	*11,717*	*1,384,270*	*919,517*
23	*With a risk weight of less than or equal to 35% under the Basel II Standardised Approach for credit risk*		*9,594*	*8,254*	*1,339,693*	*879,724*
24	*Other loans and securities that are not in default and do not qualify as HQLA, including exchange-traded equities and trade finance on-balance sheet products*		*18,821*	*890*	-	*2,327*
26	Other assets:	-	30,934	10,261	213,168	243,532

27	*Physical traded commodities*					
31	*All other assets not included in the above categories*		*30,934*	*10,261*	*213,168*	*243,532*
32	Off-balance sheet items		891	73,523	792,722	43,723
33	Total Required Stable Funding (RSF)					1,892,401
34	Net Stable Funding Ratio (%)					134.67%