Bank of Valletta

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BOV/190

COMPANY ANNOUNCEMENT

The following is a company announcement issued by Bank of Valletta p.l.c. pursuant to Malta Financial Services Authority Listing Rules Chapters 8 and 9:

Quote

The Board of Directors of Bank of Valletta p.l.c. (the Bank) has today, the 29 October 2010, approved the audited financial statements for the financial year ended 30 September 2010. The Board resolved that these audited financial statements be submitted for the approval of the shareholders at the forthcoming Annual General Meeting which is scheduled for Thursday, 16 December 2010. A preliminary statement of annual results is being attached herewith in terms of the Listing Rules.

The Board of Directors further resolved to recommend for the approval of the Annual General Meeting:

1. The payment of a final gross dividend of €0.160 per share making for a final net dividend of €0.104 per share which, if approved by the Annual General Meeting, would make for a total gross dividend for the year of €0.235 per share (total net dividend per share €0.15275).

2. A bonus share issue of one (1) share for every five (5) shares held which will be allotted to shareholders on the Bank's share register as at close of business on 12 January 2011[1]. The bonus issue will be funded by a capitalisation of reserves amounting to €40 million.

Application will be made for the necessary authorisations concerning the listing of the bonus share issue on the Malta Stock Exchange.

Shareholders on the Bank's share register, at the Central Securities Depository of the Malta Stock Exchange, as at the close of business on Wednesday 10 November 2010[2] will receive notice of the Annual General Meeting, together with the Financial Statements for the financial year ended 30 September 2010.

The final dividend, if approved at the Annual General Meeting, will be paid on the 17 December 2010 to the shareholders on the Bank's share register at the Central Securities Depository of the Malta Stock Exchange as at the close of business on Wednesday 10 November 2010.

Unquote

Catherine Formosa

Dr. Catherine Formosa B.A., LL.D.
Company Secretary

29 October 2010

[1] Wednesday, 12 January 2011 will include trades undertaken up to and including Friday, 7 January 2011.
[2] Wednesday, 10 November 2010 will include trades undertaken up to and including Friday, 5 November 2010.

Income statements for the year ended 30 September 2010

Basis of Preparation

These figures have been extracted from the Bank of Valletta Group's audited financial statements for the year ended 30 September 2010, as approved by the Directors on 29 October 2010, and are being published in terms of MFSA Listing Rule 9.35.

	The Group		The Bank	
	2010 €000	2009 €000	2010 €000	2009 €000
Interest receivable and similar income:				
- on loans and advances, balances with Central Bank of Malta and treasury bills	146,274	147,813	146,274	147,813
- on debt and other fixed income instruments	73,630	92,252	73,630	92,252
Interest payable	(93,153)	(124,694)	(93,153)	(124,694)
Net interest income	126,751	115,371	126,751	115,371
Fee and commission income	47,365	41,478	43,777	38,516
Fee and commission expense	(3,252)	(3,608)	(5,607)	(5,141)
Net fee and commission income	44,113	37,870	38,170	33,375
Dividend income	730	788	7,900	3,950
Trading profits	22,039	17,236	22,033	17,243
Net gain/(loss) on investment securities and hedging instruments	(2,442)	1,518	(2,442)	1,518
Operating income	**191,191**	**172,783**	**192,412**	**171,457**
Employee compensation and benefits	(50,280)	(48,959)	(49,163)	(48,067)
General administrative expenses	(22,390)	(21,372)	(21,092)	(20,304)
Amortisation of intangible assets	(1,308)	(1,223)	(1,308)	(1,223)
Depreciation	(4,818)	(5,501)	(4,690)	(5,375)
Operating profit before impairment losses	112,395	95,728	116,159	96,488
Net impairment losses	(12,936)	(4,016)	(12,888)	(4,016)
Operating profit	**99,459**	**91,712**	**103,271**	**92,472**
Share of results of associate and jointly controlled entity, net of tax	(542)	(9,894)	-	-
Profit before tax	**98,917**	**81,818**	**103,271**	**92,472**
Income tax expense	(34,945)	(32,403)	(35,030)	(32,293)
Profit for the period	**63,972**	**49,415**	**68,241**	**60,179**
Profit for the period attributable to:				
Equity holders of the Bank	63,447	49,014	68,241	60,179
Non-controlling interest	525	401	-	-
	63,972	**49,415**	**68,241**	**60,179**
Earnings per share	31c7	24c5	34c1	30c1

Statements of comprehensive income for the year ended 30 September 2010

	The Group 2010 €000	The Group 2009 €000	The Bank 2010 €000	The Bank 2009 €000
Profit for the period	63,972	49,415	68,241	60,179
Other comprehensive income				
Available-for-sale investments:				
- change in fair value	4,970	5,541	4,970	5,541
- deferred tax thereon	(1,739)	(1,939)	(1,739)	(1,939)
- change in fair value transferred to profit and loss	(153)	(1,418)	(153)	(1,418)
- deferred tax thereon	53	496	53	496
Property:				
- revaluation decrease	-	(1,000)	-	(1,000)
- deferred tax thereon	-	120	-	120
Other comprehensive income for the period, net of tax	3,131	1,800	3,131	1,800
Total comprehensive income	67,103	51,215	71,372	61,979
Total comprehensive income attributable to:				
Equity holders of the Bank	66,578	50,814		
Non-controlling interest	525	401		
	67,103	**51,215**		

Statements of financial position

as at 30 September 2010

	The Group		The Bank	
	2010 €000	2009 €000	2010 €000	2009 €000
ASSETS				
Balances with Central Bank of Malta, treasury bills and cash	135,773	278,270	135,773	278,270
Financial assets at fair value through profit or loss	963,488	1,101,202	961,370	1,099,763
Investments	1,243,454	1,159,422	1,243,430	1,159,350
Loans and advances to banks	264,965	207,481	264,965	207,481
Loans and advances to customers at amortised cost	3,496,744	3,245,899	3,496,744	3,245,899
Investments in associate and jointly controlled entity	68,689	54,886	52,870	34,025
Investments in subsidiary companies	-	-	1,393	1,393
Intangible assets	4,297	3,853	4,297	3,853
Property, plant and equipment	76,199	77,825	75,844	77,542
Current tax	1,482	-	1,167	-
Deferred tax assets	41,813	41,368	41,813	41,368
Other assets	13,047	8,978	11,802	8,075
Prepayments and accrued income	25,241	37,230	25,236	37,202
Total Assets	**6,335,192**	**6,216,414**	**6,316,704**	**6,194,221**
LIABILITIES				
Financial liabilities at fair value through profit or loss	47,867	36,114	47,867	36,114
Amounts owed to banks	347,369	668,584	347,369	668,584
Amounts owed to customers	5,185,264	4,766,278	5,185,606	4,767,502
Debt securities in issue	25,701	24,936	25,701	24,936
Current tax	187	507	-	583
Other liabilities	73,429	126,574	73,174	126,075
Accruals and deferred income	35,635	41,789	34,891	41,288
Financial liabilities designated for hedge accounting	30,692	20,430	30,692	20,430
Subordinated liabilities	120,000	96,567	120,000	96,567
Total Liabilities	**5,866,144**	**5,781,779**	**5,865,300**	**5,782,079**
EQUITY				
Equity attributable to shareholders of the Bank:				
Called up share capital	200,000	160,000	200,000	160,000
Share premium account	988	988	988	988
Revaluation reserves	24,931	21,810	24,819	21,688
Retained earnings	242,546	251,199	225,597	229,466
	468,465	433,997	451,404	412,142
Non-controlling interest	583	638	-	-
Total Equity	**469,048**	**434,635**	**451,404**	**412,142**
Total Liability and Equity	**6,335,192**	**6,216,414**	**6,316,704**	**6,194,221**
MEMORANDUM ITEMS				
Contingent liability	183,803	167,875	183,803	167,875
Commitments	1,096,124	1,049,013	1,096,124	1,049,013

Statements of changes in equity for the year ended 30 September 2010

The Group	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000	Non Controlling Interest €000	Total Equity €000
	Attributable to Equity holders of the Bank						
As at 30 September 2008	**100,000**	**988**	**20,010**	**271,675**	**392,673**	**717**	**393,390**
Profit for the period	-	-	-	49,014	**49,014**	401	**49,415**
Other comprehensive income							
Available for sale investments:							
- change in fair value, net of tax	-	-	3,602	-	**3,602**	-	**3,602**
- change in fair value transferred to profit or loss, net of tax	-	-	(922)	-	**(922)**	-	**(922)**
Property:							
- revaluation decrease, net of tax	-	-	(880)	-	**(880)**	-	**(880)**
Total other comprehensive income	-	-	1,800	-	**1,800**	-	**1,800**
Total comprehensive income for the period	-	-	1,800	49,014	**50,814**	401	**51,215**
Transactions with owners, recorded directly in equity							
Bonds issue	26,667	-	-	(26,667)	-	-	**-**
Increase in paid up value	33,333	-	-	(33,333)	-	-	**-**
Dividends - final 2008	-	-	-	(5,850)	**(5,850)**	(480)	**(6,330)**
- interim 2009	-	-	-	(3,640)	**(3,640)**	**-**	**(3,640)**
	60,000	-	-	(69,490)	**(9,490)**	(480)	**(9,970)**
As at 30 September 2009	**160,000**	**988**	**21,810**	**251,199**	**433,997**	**638**	**434,635**
Profit for the period	-	-	-	63,447	**63,447**	525	**63,972**
Other comprehensive income							
Available for sale investments:							
- change in fair value, net of tax	-	-	3,231	-	**3,231**	-	**3,231**
- change in fair value transferred to profit or loss, net of tax	-	-	(100)	-	**(100)**	-	**(100)**
Total other comprehensive income	-	-	3,131	-	**3,131**	-	**3,131**
Total comprehensive income for the period	**-**	**-**	3,131	63,447	**66,578**	525	**67,103**
Transactions with owners, recorded directly in equity							
Transfer to retained earnings	-	-	(10)	10	-	-	**-**
Bonus issue	40,000	-	-	(40,000)	-	-	**-**
Dividends - final 2009	-	-	-	(22,360)	**(22,360)**	(580)	**(22,940)**
- interim 2010	-	-	-	(9,750)	**(9,750)**	-	**(9,750)**
	40,000	-	**(10)**	**(72,100)**	**(32,110)**	**(580)**	**(32,690)**
At 30 September 2010	**200,000**	**988**	**24,931**	**242,546**	**468,465**	**583**	**469,048**

Statements of changes in equity

for the year ended 30 September 2010

The Bank	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000
As at 30 September 2008	**100,000**	**988**	**19,888**	**238,777**	**359,653**
Profit for the period	-	-	-	60,179	**60,179**
Other comprehensive income					
Available for sale investments:					
- change in fair value, net of tax	-	-	3,602	-	**3,602**
- change in fair value transferred to profit or loss, net of tax	-	-	(922)	-	**(922)**
Property:					
- revaluation decrease, net of tax	-	-	(880)	-	**(880)**
Total other comprehensive income	-	-	1,800	-	**1,800**
Total comprehensive income for the period	-	-	1,800	60,179	**61,979**
Transactions with owners, recorded directly in equity					
Bonds issue	26,667	-	-	(26,667)	-
Increase in paid up value	33,333	-	-	(33,333)	-
Dividends - final 2008	-	-	-	(5,850)	**(5,850)**
- interim 2009	-	-	-	(3,640)	**(3,640)**
	60,000	-	-	(69,490)	**(9,490)**
As at 30 September 2009	**160,000**	**988**	**21,688**	**229,466**	**412,142**
Profit for the period	-	-	-	68,241	**68,241**
Other comprehensive income					
Available for sale investments:					
- change in fair value, net of tax	-	-	3,231	-	**3,231**
- change in fair value transferred to profit or loss, net of tax	-	-	(100)	-	**(100)**
Total other comprehensive income	-	-	3,131	-	**3,131**
Total comprehensive income for the period	**-**	**-**	**3,131**	**68,241**	**71,372**
Transactions with owners, recorded directly in equity					
Bonus issue	40,000	-	-	(40,000)	-
Dividends - final 2009	-	-	-	(22,360)	**(22,360)**
- interim 2010	-	-	-	(9,750)	**(9,750)**
	40,000	-	**-**	**(72,110)**	**(32,110)**
At 30 September 2010	**200,000**	**988**	**24,819**	**225,597**	**451,404**

The share premium account and the revaluation reserves are non-distributable.

Statements of cash flow

for the year ended 30 September 2010

	The Group		The Bank	
	2010 €000	2009 €000	2010 €000	2009 €000
Cash flows from operating activities				
Interest and commission receipts	202,648	280,592	199,031	277,635
Interest and commission payments	(103,147)	(150,404)	(105,745)	(151,784)
Payments to employees and suppliers	(71,838)	(69,488)	(69,423)	(67,528)
Operating profit before changes in operating assets and liabilities	27,663	60,700	23,863	58,323
(Increase) / decrease in operating assets:				
Loans and advances	(335,809)	(199,473)	(335,761)	(199,473)
Reserve deposit with Central Bank of Malta	(5,088)	9,110	(5,088)	9,110
Fair value through profit or loss financial assets	260,106	278,557	260,106	278,557
Fair value through profit or loss equity instruments	(2,839)	3,506	(2,160)	2,110
Treasury bills with original maturity of more than 3 months	92,213	(54,751)	92,213	(54,751)
Other assets	(4,070)	4,455	(3,727)	4,696
Increase / (decrease) in operating liabilities:				
Amounts owed to customers	418,986	140,894	418,104	140,579
Amounts owed to banks	(240,509)	(284,826)	(240,509)	(284,826)
Other liabilities	(53,435)	67,355	(53,196)	67,114
Net cash from operating activities before tax	157,218	25,527	153,845	21,439
Tax paid	(39,287)	(19,378)	(38,911)	(17,997)
Net cash from operating activities	117,931	6,149	114,934	3,442
Cash flows from investing activities				
Dividends received	5,639	1,788	7,900	3,950
Interest received from held-to-maturity debt and other fixed income instruments	45,745	42,175	45,745	42,175
Investment in associate and jointly controlled entity	(18,845)	(2,754)	(18,845)	(2,754)
Purchase of equity instruments	(953)	-	(953)	-
Purchase of debt instruments	(255,863)	(416,978)	(255,863)	(416,978)
Proceeds from sale of maturity of debt instruments	206,166	199,727	206,120	199,727
Receipts from disposal of property, plant and equipment	(4,946)	(5,651)	(4,744)	(5,586)
Net cash used in investing activities	(23,057)	(181,693)	(20,640)	(179,466)
Cash flows from financing activities				
Proceeds from issue of subordinated bonds	42,295	50,000	42,295	50,000
Repayment of subordinated bonds	(18,862)	-	(18,862)	-
Debt securities in issue	(1,133)	-	(1,133)	-
Dividends paid to bank's equity holders	(32,110)	(9,490)	(32,110)	(9,490)
Dividends paid to non-controlling interests	(580)	(480)	-	-
Net cash from/(used in) financing activities	(10,390)	40,030	(9,810)	40,510
Net change in cash and cash equivalents	84,484	(135,514)	84,484	(135,514)
Effect of exchange rate changes on cash and cash equivalents	20	13	20	13
Net change in cash and cash equivalents	84,464	(135,527)	84,464	(135,527)
	84,484	(135,514)	84,484	(135,514)
Cash and cash equivalent at 1 October	146,365	281,879	146,365	281,879
Cash and cash equivalent at 30 September	**230,849**	**146,365**	**230,849**	**146,365**

Background

In the Bank of Valletta (BOV) Annual Report for the Year ended 30 September 2009 (FY 2009), it was observed that whereas stability and confidence had been restored to the global financial and banking systems, the financial crisis of 2008-2009 had caused significant and potentially lasting damage to the global economy. Governments around the world were facing the challenges of combating high unemployment and a demand for continuing stimulus support against a backdrop of contracting tax revenues. In Malta, signs of the impact of the global recession were evident, albeit at a much more modest level than had been seen elsewhere across Europe.

It was hoped in late 2009 that the growing level of restored confidence that we had seen in the global financial markets would be sustained. At the same time, we recognised that the incipient economic recovery that we were then witnessing was fragile, and that set-backs would be experienced from time to time.

In the event, the first half of the current financial year through to March 2010 saw a continuing restoration of confidence and calm in the financial markets. However, this sense of calm was rudely interrupted in late April 2010, with the eruption of the eurozone debt crisis. The origins of this after-shock to the European financial system can be traced to the severe problems that Greece was facing with its public finances, and the difficulties that it was encountering in financing its considerable deficit. A growing realisation emerged that much of the funding difficulties previously faced by the banking system had been transferred to or assumed by various national state governments, and that questions formerly asked of the banking sector were now being asked of entire economies in the eurozone.

Notwithstanding the €110 billion funding package that was put together for Greece, serious concerns emerged that contagion would take hold, and that the problems being faced by Greece would swiftly move to those "peripheral" eurozone states (Portugal, Spain, Italy, and Ireland) whose public finances were likewise under pressure. At one stage, the future status of the euro itself was being questioned. This "sovereign debt" phase of the financial crisis threatened to feed back into the banking system, given the very substantial holdings of sovereign paper held within the European banking sector.

Public policymakers have adopted a multi-faceted approach to the new problem:-

(i) as noted above, a €110 billion funding package was put together for Greece – a package that secures Greek funding needs through to 2013. This package was made available conditional on the Greek government implementing a severe austerity package and fundamental structural reforms;

(ii) establishing a €750 billion European Financial Stability Facility (EFSF) to reassure financial markets that eurozone countries would have access to funding in the event that credit markets seized up again;

(iii) encouraging governments across Europe to implement stringent austerity measures in order to bring budget deficits under control and restore confidence in the vitally important sovereign debt market;

(iv) carrying out a programme of "stress tests" on almost 100 European banks, with an understanding that Governments would take measures to recapitalise those banks shown to be short of capital;

(v) commencing a long-term programme to strengthen the global banking system through what is referred to as the Basel III process. This process will require banks to hold more capital and maintain higher liquidity buffers; it will also bring more demanding risk weightings to certain asset classes. These Basel III measures, some of them still under discussion, are being phased in over a transition period of several years, due to policy-makers' anxiety that they should not stifle the still fragile economic recovery.

The indications are that the package of measures is holding, although concerns remain that Greece may, at some stage, be forced to restructure its debt because of the unsustainability of its public finances, and the debt burden that has been allowed to build up. This concern has caused spreads on Greek debt to widen markedly – and a contagion effect has been transmitted to Portugal and Ireland. Having taken some time to realise the gravity of the situation, the strong measures taken by the Spanish authorities – including the forced restructuring of the caja de ahorro or savings institutions, appear to have restored some confidence to the markets insofar as Spain is concerned. Fears over Greek debt have also eased a little of late. However, what is clear is that the markets are now very critically differentiating between the various eurozone countries in a manner that was not evident previously – with those countries whose public finances are not being conducted with sufficient rigour facing punitive funding costs - or the prospect of being excluded from the markets altogether.

This new era of austerity in public finances causes new problems or potential further after-shocks to loom – that of the threat of a double dip recession, and with it the prospect of social discontent and political instability. These concerns revolve around the fear that the implementation of the austerity measures – which include severe job cuts, salary and pension reductions or deferrals, and aborted public spending and/or investment programmes - will necessarily impact unemployment levels, consumer confidence and economic growth negatively. We are already seeing political pressures giving rise to growing (trade) protectionist sentiment and tensions relating to comparative currency exchange rates. The euro has recovered somewhat from the dark days of May, and economic growth appears to be holding its head above water – just – but it is early days yet, as many of the austerity programmes have still to be fully implemented.

So, in summary, across the eurozone, we end FY 2010 somewhat less optimistically than we started it, with the fiscal stability of certain countries being questioned – and with it the potential of transferring certain problems back to some parts of the banking sector. It is clear that what we have seen in the second half of FY 2010 has been a severe after-shock of the 2008-2009 financial crisis.

Paradoxically, against the above wider eurozone backdrop, the Maltese economy has performed better than expected. Following a lag effect, and an uncharacteristically short downturn, Malta emerged from the recession in the last quarter of 2009, and registered a 4% growth in GDP in the first half of 2010. This recovery has been due to employment numbers remaining relatively stable, a strong performance from the services sector (including financial services) and, in part, to the continuing availability of credit in the local economy.

Furthermore, returning growth in tourism activity has been an important factor, due to its rapid and widespread knock-on impact into other sectors of the economy. This growth in tourism activity can in the main be attributed to a number of critical strategic decisions taken some while back on opening a number of new routes to competition in the aviation sector. This has resulted in tourist arrivals on a year to date basis being up 12%, a welcome growth statistic that is in stark contrast with the tourist sector experience in most other European destinations. However, domestic consumer demand remains subdued, more due to continuing uncertainty over utility costs than employment concerns. Overall, sentiment in the economy is a little more optimistic than a year ago – once again in marked contrast with much of the rest of Europe. Clearly, the sustainability of Malta's finances are a positive feature, especially when compared to the rest of the eurozone, and have been an important factor that has helped the country during the recessionary phase, and enabled the country to avoid undue disruptions to its financial markets and real economy.

Review of performance

The Bank of Valletta Group has recorded a profit before taxation of €98.9 million for the year ended 30 September 2010. This compares with €81.8 million pre tax profit earned in the previous financial year, an increase in profits of 21%. As can be seen from the table below, the retail and corporate businesses of the Bank have continued to perform well, and we have seen a welcome turnaround in the results from our interests in the insurance sector. The uncertainty in the financial markets in the second half of the year referred to above has resulted in an overall fair value recovery in our Financial Markets book being limited to €1.2 million for the year. The impairment charge for the year has increased by €8.9 million, reflecting the tougher economic environment through which we have been passing.

Our results for the year are summarised in the table below. This table should be read in conjunction with the explanatory notes that follow:

Bank of Valletta Summary Results Year to 30th September	Note	2010 € million	2009 € million
Net Interest Income	(a)	126.7	115.4
Net Commission and Trading Income	(b)	63.2	51.7
Operating Expenses	(c)	(78.8)	(77.1)
Net Impairment Charges	(d)	(12.9)	(4.0)
Net Operating Profit before Fair Value movements	(e)	98.2	86.0
Fair Value movements	(f)	1.2	5.7
OPERATING PROFIT		99.4	91.7
Share of results of jointly controlled and associated companies	(g)	(0.5)	(9.9)
Profit before tax		98.9	81.8

(a) Net Interest Margin

Net Interest Margin for the year of €126.7 million increased by €11.3 million from the €115.4 million earned in FY 2009. With lending rates little changed over the year, this improvement in the interest margin contribution of 9.8% arose from a combination of increased volumes and the time lag effect on the re-pricing of deposits. The European Central Bank (ECB) has not implemented any changes to the historically low reference rate of 1% since May 2009, and net interest margin earnings will remain compressed for so long as rates are maintained at this low level. Given the fragility of the economic recovery, the current thinking is that it is unlikely that the ECB will make any changes to its key reference rate until the second half of 2011 at the earliest.

(b) Net Commission and Trading Income

Net Commission and Trading Income showed strong growth of €11.5 million for the year – up by 22% from the equivalent period to September 2009. This improvement has come from a wide cross-section of business activities; higher foreign exchange volumes, our Cards business (including in particular, the e-commerce sector) showing strong growth, and our various investment related activities (stock-broking, capital markets, bancassurance, funds and wealth management) producing very satisfactory results, as this sector benefited from a marked change in sentiment as investors regained their appetite for the equity and bond markets after the turmoil and disruption of 2008 and 2009.

(c) Operating Expenses

Operating expenses for the year totalled €78.8 million, an increase of just 2.3% over the previous year, reflecting management's continuing focus on cost containment – and the elimination of certain costs through the greater use of the electronic media for statement and other data distribution. Increased technology spend, where we continue to make material investments, and selective specialist recruitment could see a step up in operating cost levels in FY 2011.

(d) Net Impairment charges

As anticipated, and notwithstanding the quicker than expected recovery, the difficult economic conditions of the past two years have had something of a knock-on effect on credit quality in certain sectors. The specific impact to date has remained modest and manageable, and the higher impairment charge for the year has in part come from an increase in the non-specific collective allowance. In this regard, management has adopted a prudent and cautious outlook to certain sectors, at a time when the overall situation for these sectors remains characterised by some uncertainties. Overall credit quality remains satisfactory, but, not unexpectedly given the above factors, we have seen a year on year deterioration in the proportion of non-performing accounts to total loans and advances.

(e) Net Operating Profit

The net operating profit from core corporate and retail banking operations for the year amounts to €98.2 million (2009: €86.0 million). The increase in profits can be largely attributed to the improved net interest income for the reasons explained in (a) above, together with the higher level of commission income earned. These increases have been partly offset by the higher overhead costs and the increased impairment allowance.

(f) Fair Value movements

The results of the first half of the year to 31 March 2010 reported a gain of approximately €6 million on the reversal of the unrealised fair value movements booked in previous periods. However, the sovereign debt issues that emerged in the second half of the year (see above) resulted in uncertainty returning to the capital markets and the widening of spreads on certain issues. This caused the reversal of most of the gains of the first half, and overall the net fair value position for the year showed a modest recovery of just €1.2 million. A further sum of €4.8 million before tax has been credited directly to reserves, representing favourable movements in the value of the available for sale portfolio.

(g) Jointly Controlled and Associated Companies

The Jointly Controlled and Associated Companies represent our insurance sector interests through our holdings in Middlesea Valletta Life Assurance Company Limited (MSV), in which BOV has a direct equity interest of 50%, and in Middlesea Insurance plc (MSI), where our holding increased to 31.08% following the Rights Issue launched in November 2009. The Group's share of loss for the year of €0.5 million is made up as follows:-

	6 months to March 2010 € million	**6 months to Sept 2010 € million**	**FY 2010 € million**	**FY 2009 € million**
MSV share of profit/(loss)	3.7	2.1	5.8	(0.4)
MSI share of loss	(7.3)	1.0	(6.3)	(9.5)
Net loss for the year	(3.6)	3.1	(0.5)	(9.9)

The above charge represents BOV's share of profits and losses on its MSV and MSI holdings based on the audited accounts of these companies for the six months to 31 December 2009 (Middlesea's financial year end), and the unaudited results for the six months ended 30 June 2010. The charge therefore includes the impact on MSI's results of the write off of its entire investment in Progress

Assicurazioni SpA that was taken up in MSI's FY 2009 accounts, following the decision that was taken in early 2010 to wind up the operations of that company.

Since January 2010 and the cessation of its Italian operations, a number of important steps have been taken to reorganise and rehabilitate MSI under the chairmanship of Joseph F X Zahra. New business strategies have been adopted that return MSI to its roots as Malta's leading insurance company, with a clear focus on its role as a customer centric, profitable and progressive domestic insurer. Investment is being made in both HR and IT structures so as to improve efficiency and customer service levels. IIMS (now renamed BEE), a wholly owned subsidiary of MSI, will transit to an exclusively third party service provider to the insurance industry sector, looking to attract further reputable international insurance related operators to Malta's important and growing financial services sector.

Middlesea Valletta, in which the Bank has an economic interest of 65%, has moved rapidly during the year to implement a Board mandated initiative to transform itself into a wholly self-sufficient, stand-alone company, ably led by its CEO David Curmi. A new senior management team has been put in place, with a number of important senior executives having been recruited during the year. MSV has total assets of over €1 billion, a customer base of over 80,000, and shareholders' equity of over €100 million. It is Malta's leading life insurance company by far, and prospects for continuing growth and development are encouraging, both in the life assurance and in the long term savings/pensions areas.

Review of financial position

Throughout the year under review, the Bank has continued to manage its balance sheet in the deliberate and prudent manner that stood it in good stead through the 2008-2009 financial crisis. Liquidity has remained very satisfactory at 41%, and the core Tier I capital ratio is strong at 10.5%. The total capital ratio at the year end stood at 15.0% (September 2009, as restated – 12.5%). This latter ratio was reinforced during the year with the successful €70 million 4.8% 2020 Subordinated Bond issuance, which closed in March 2010. This issue was heavily oversubscribed, attracting more than 6,800 applications aggregating €96 million.

The net Loan to Deposit ratio remains steady at 70%, and the Bank continues to be in the position whereby our loan book is wholly funded by retail liabilities, with no dependence for this purpose on the short term inter-bank or commercial paper markets. Total assets at the end of September 2010 stood at €6.3 billion, much in line with the September 2009 level, while shareholders' equity amounted to €469 million, as compared with €435 million of a year earlier.

Stress Tests and Basel III

During July 2010, the Committee of European Banking Supervisors (CEBS), in collaboration with the European Central Bank (ECB) and local regulatory authorities, carried out a series of "stress tests" on 91 leading European banks. Bank of Valletta, as the largest local banking group, was selected to represent the Maltese banking sector in this test.

The results of the test showed that Bank of Valletta Group enjoys strong capital buffers. When the Bank's balance sheet was "stressed" in accordance with the parameters set by the ECB, our Tier 1 ratio (which is an international benchmark indicator of balance sheet strength), decreased by 1.2 percentage points, reaching the level of 9.3%. This is more than one-and-a-half times higher than the designated 6% "pass mark" set by the ECB, and more than double the current statutory minimum ratio of 4%.

Discussions have been taking place for sometime between the Bank for International Settlements (BIS), international regulators and the Financial Stability Board about what lessons should be learned from the banking crisis of 2008-2009, so as to strengthen regulation to ensure that such an alarming event is never repeated. These proposed changes to regulations to the global banking sector have come to be referred to as "Basel III".

In September 2010 it was announced that agreement had been reached on a series of measures that are directed at raising both the minimum requirement and the quality of bank capital. The regulators are proposing a phased introduction of these new measures over a transition period. This is because they are concerned that the new requirements should not lead to the short term contraction of credit, which could have the effect of stifling the very fragile economic recovery that is currently underway.

Apart from requiring higher minimum Tier 1 “core capital”, over a four year transition period commencing in 2016, banks will also be required to build additional “capital conservation” and “counter-cyclical” buffers. Banks deemed to have inadequate “buffers” will face dividend distribution and bonus payment constraints. Furthermore, although final agreement has yet to be reached, it is also intended to introduce further capital surcharges in respect of “systemically important banks”. Further refinements are also expected shortly relating to leverage and liquidity regulations.

Capital forecasting work carried out internally by Bank of Valletta shows the Bank to be comfortably in excess of the new minimum capital requirements, and an expectation (based on prudent assumptions and on Basel III pronouncements to date) that the Bank will be able to meet the phased additional capital conservation and counter-cyclical buffers without having to resort to any near term capital raising or dividend constraint measures. These forecasts will be kept under constant review as additional regulations emerge.

Credit

During FY 2010 BOV has continued to honour the pledge that it would support the Maltese economy and the business community in a responsible manner through the economic downturn. Loans and advances at the end of FY 2010 stood at €3.6 billion, an increase of €325 million or 10%, since 30 September 2009. Non Performing Loans at the year end stood at 5.2% of the total loan book, compared with a little under 4% a year earlier.

Credit growth has come from carefully selective increases to the business sector, and a continuing demand for home loans, particularly in the first time buyer segment. During the year to 30 September 2010, the Bank approved €229 million of new home loans, of which €181 million were drawn down, both numbers being approximately 15% below FY 2009 demand levels. Credit actually utilised by the business sector over the year increased by €216 million (or 11%). BOV’s Capital Markets team has also been very active in the new issues sector, with the Bank acting as Manager during the year for 7 new issues, which between them raised a total of close to €250 million.

Customer Deposits

During FY 2010, Customer Deposits exceeded a total of €5 billion for the first time in the Bank’s history. Total deposits at the year end of €5.19 billion show an increase of €419 million or 9% since September 2009, with growth being registered throughout the year. Notwithstanding acute competition for deposits and a high level of government and corporate bond issuance activity, FY 2010 has seen BOV sustaining its position as the market leader in the domestic euro-deposit retail and corporate sectors.

The Bank has maintained deposit rates at competitive levels, and brings special products to the market at regular intervals. As noted last year, Malta’s ongoing growth and development as an international financial centre is attracting material money flows, but many of these tend to be more short term and volatile in nature, placing a premium on astute treasury management.

Dividend and Bonus issue

The dividend distribution policy of the Bank has been clearly articulated for a number of years. The Board has long believed that it represents a good and prudent model to follow, in that it secures a fair dividend distribution to shareholders, whilst at the same time enabling the capital base of the Bank to grow. This policy has enabled the Bank to build up its high quality core capital base over the years, and in a manner which has enabled it to withstand the stress tests carried out in July 2010 under the auspices of the ECB. It also places the Bank in a position to meet the more demanding capital requirements that are emerging from the Basel III process, without having to resort to the dividend restraint measures that may be imposed on many other banks.

Accordingly, it is the Board's belief that the "one thirds" policy should be retained at this time, and the Board of Directors is recommending a final gross dividend to our shareholders of €0.16 per share which, taken together with the gross interim dividend of €0.075 per share paid on 28 May, makes for a total gross dividend of €0.235 per share for FY 2010 (FY 2009: €0.20 per share, as adjusted for bonus issue). The total dividend for the year of €0.235 would represent a gross yield of 7.25% by reference to BOV's closing share price of €3.24 as on 30 September 2010. The total dividend will be 2.10 times covered by the post tax profits for the year.

The Board is also recommending, effective 12 January 2011, a bonus issue of 1 share for every 5 shares held. The bonus issue will be funded by a capitalisation of reserves amounting to €40 million. This bonus issue will serve to further increase the permanent capital base of the Bank (from €200 million to €240 million), and will also serve to enhance the affordability and liquidity of the Bank's shares.

The La Valette Multi Manager Property Fund

On 4 August 2010 the La Valette SICAV, Bank of Valletta, Valletta Fund Management (VFM), and Valletta Fund Services (VFS) received the first of a series of judicial protests relating to the La Valette Multi Manager Property Fund (the Fund). Counter-protests categorically rebutting these allegations as being without foundation have been filed by the parties within the Bank of Valletta Group and by the SICAV.

The Bank of Valletta Group does, of course, greatly regret the poor performance of the Fund, and the impact that this has had on our investors, and believes that both the SICAV and VFM have been very open since 2008 in stating that serious difficulties had emerged in connection with the investments made in the Belgravia funds. Indeed, the SICAV, VFM and Insight Investment Management (the appointed investment manager of the Fund) have been working very hard over an extended period of time in seeking to find a resolution to the Belgravia-related problems, and have been taking legal advice and consulting with the regulators in this regard. Bank of Valletta believes that the SICAV and VFM have been open and transparent about the problems concerned, and that no reasonable person could come away from a reading of the various communications relating to the Fund in the SICAV reports, and of the (ongoing) correspondence to shareholders from the SICAV and VFM, without concluding that problems existed and had been disclosed, and that work was being done in an attempt to mitigate matters – work that continues at the time of writing. Therefore, the suggestion that investors in the Fund were in any way misled is most emphatically and categorically rebutted.

Although no allegations *per se* have been made on the question of redemptions, the insinuation has been floated that the level of redemptions experienced by the Property Fund in 2008 were in some way "massive" or "extraordinary", and that the level of redemptions was due to Bank of Valletta staff, family and friends, as well as a number of favoured customers, having been given access to privileged information that enabled them to redeem their holdings in the Fund ahead of its suspension. Such a suggestion is grossly offensive. We regard all the investors in the Fund as valued Bank of Valletta customers, and the Bank would never countenance or tolerate such a breach of trust. The Bank has formally requested that the MFSA concludes its review on redemption activity as a matter of urgency, so that this matter can be laid to rest as soon as possible. We know that this review will demonstrate that the level of redemptions experienced was due to market forces, conditioned by the extreme volatility prevailing at that time, and was absolutely not the result of any privileged information being extended to any particular investor or group of investors. Indeed, a simple comparison with other publicly available information relating to funds operating in Malta has shown that the level of redemptions experienced by the Property Fund in 2008 was very much the norm experienced right across the market. We are also confident that the review will demonstrate that the Bank acted very professionally, and took all reasonable measures to guard the confidentiality of the deliberations that necessarily took place concerning the question of the suspension of dealings in the Fund, and that internal procedures in this regard were respected at all times.

Whereas the Bank fully respects the right of any party to take commercial issue with the company and its subsidiaries, and to engage them in arbitration or litigation, and has no quarrel with any of the parties concerned in this regard, the Bank deplores the irresponsible and unprofessional approach adopted by certain complainants in this matter, who, for reasons best known to them, have chosen an approach that is aimed at calling into question the integrity and *bona fide* of Malta's leading financial institution, and who have made unwarranted and unsubstantiated allegations as part of a campaign that has been replete with indiscriminate half truths, insinuation and innuendo.

The Bank will continue to respect the rights of any party to question and challenge its decisions and actions – but will insist that this is done in the proper and professional manner – and in accordance with established procedures for settling commercial disputes. And, of course, the Bank will face up to and accept its responsibilities if its decisions and actions are found to have been wanting in any respect. This, we submit, is the proper and responsible approach that will be fully in keeping with Malta's aspirations to establish itself as a professional and mature financial services jurisdiction. Furthermore, and as always, the Bank will co-operate fully with the Malta Financial Services Authority on the various lines of enquiry that are taking place. In the meantime, we would caution all concerned about the very material differences between unsubstantiated allegations and/or innuendo and established facts, and of the substantial divide that often exists between one and the other.

Outlook

The Board expects that the general economic environment will continue to be uncertain and fragmented, with different economies and different sectors within economies responding in varying degrees. This recovery will be uneven, slow and erratic, with the possibility of further after-shocks and fears of contagion being encountered along the way. Domestically, tourist arrivals for 2010 to date have been most encouraging, and the services sector has demonstrated strength and resilience. Parts of the local manufacturing sector are also showing signs of a gradual recovery. Ultimately, the restoration of an appetite for long term investment expenditure will determine the pace and sustainability of any rebound. The expectation is that the chronic over-supply on the market will continue to keep property prices subdued for some time to come. A number of large infrastructural projects that are either underway or in the pipeline could give the larger scale construction operators some grounds for optimism, but speed of implementation on the key projects will be critical.

As noted above, the Basel III process will introduce radical changes to strengthen the global banking system, albeit in a phased manner, so as to prevent any recurrence of the terrifying events of late 2008 and early 2009, when the global financial system came perilously close to melt-down – a resolve strongly reinforced by the after-shocks experienced in 2010. These risk based measures to strengthen capital and liquidity requirements are essential, and should be welcomed by all concerned. However, it would be a pity if policy-makers were to succumb to current populist pressures for the application of industry-wide levies or taxes. Such levies would be indiscriminate in nature and effect, and would likely impact the imprudent and the prudent in equal measure. They would therefore bring with them their own form of moral hazard, without necessarily strengthening or safeguarding the financial system as a whole – and would soon degenerate into just another form of taxation.

Elsewhere on the international front, the pressures being faced by the peripheral eurozone states (Greece, Ireland, Portugal, and to a lesser extent Spain), in re-financing their debt, and the ever present threat of contagion, demonstrates the importance of the continuing need for fiscal discipline and rigour to be maintained at government level right across Europe.

The sustainability of public finances in Malta, particularly as compared to that of other eurozone economies, has served the economy well during the latest recessionary phase. Importantly, it has enabled the country to avoid undue disruptions to its financial markets and real economy. The fiscal deficit in 2009 stood at 3.8% of GDP, compared to an average for the euro area countries of over 6%. Malta's debt to GDP ratio likewise remained at under 70% of GDP, which is relatively manageable in the current circumstances. This factor was an important consideration in Malta being able to maintain its credit rating following a recent review. Government has renewed its commitment to fiscal responsibility and sustainability with the recently announced budget, and this is to be welcomed. As in other advanced European economies, apart from dealing with current short term issues, Malta will also shortly have to address a number of important longer term strategic issues, including those arising from marked demographic shifts, and the impact that these will have on Government finances and the economy as a whole.

At Bank of Valletta, we will continue to manage our balance sheet in a prudent and conservative manner, maintaining high liquidity and strong capital ratios. As in the past, we will also aspire to actively manage both sides of our balance sheet in a responsible manner, seeking to meet the reasonable demands and expectations of our depositors and borrowers alike, whilst at the same time being acutely aware of our obligations to our other stakeholders – our shareholders, employees and the wider community.

Conclusion

The Board of Directors would like to express sincere thanks to Tonio Depasquale, the Chief Executive, his senior management team and all the staff of the Bank of Valletta Group for their dedication, commitment and hard work. Their collective efforts have produced the very satisfactory results that have once again been achieved for the financial year just closed. We are also grateful to our many customers for the business they bring, and for the great confidence and trust that they consistently demonstrate in the Group. As has been observed before, BOV's firm commitment to support the Maltese economy as a whole, and to encourage our many customers through the difficult economic circumstances of the past two years have been clearly recognised, acknowledged and appreciated – and has led to business gains and strengthened customer relationships. Finally, we have, as always, maintained a healthy and open dialogue with the regulatory authorities at the MFSA and the Central Bank, and we are grateful to them for their support, wise counsel and advice.

Finally, the Board would like to congratulate Albert Frendo and Michael Galea on their appointments as Chief Officers of the Bank, and the Board is confident that they will prove to be excellent choices. They will take over responsibilities from John Soler (Chief Officer – Credit) and Igino Xuereb (Chief Officer – Operations) respectively. Igino Xuereb retired from the Bank on 1 October 2010, and John Soler will follow suit on 1 December. Both have served the Bank with great distinction for over 40 years, and they will be sorely missed. We are grateful to them for their outstanding contributions, and we wish them every possible success and happiness for the future.

By Order of the Board
29 October 2010

Notice is hereby given that Wednesday 10 November 2010 is the "effective date" for the purposes of Article 2 (f) of the Bank's Articles of Association.

All shareholders appearing on the Bank's Register of Members as at the close of business on Wednesday 10 November 2010 will:

i) receive notice of and be entitled to attend and vote at the Bank's Annual General Meeting scheduled for Thursday 16 December 2010, and

ii) be paid, on Friday 17 December 2010, the final dividend as approved by the Annual General Meeting.

Pursuant to the Malta Stock Exchange Bye-Laws, the Bank's Register of Members as at close of business on Wednesday 10 November 2010 will include trades undertaken up to and including Friday 5 November 2010.