BOV

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BOV/387

COMPANY ANNOUNCEMENT

The following is a Company Announcement issued by Bank of Valletta p.l.c. pursuant to the Listing Rules, issued by the Listing Authority

Quote

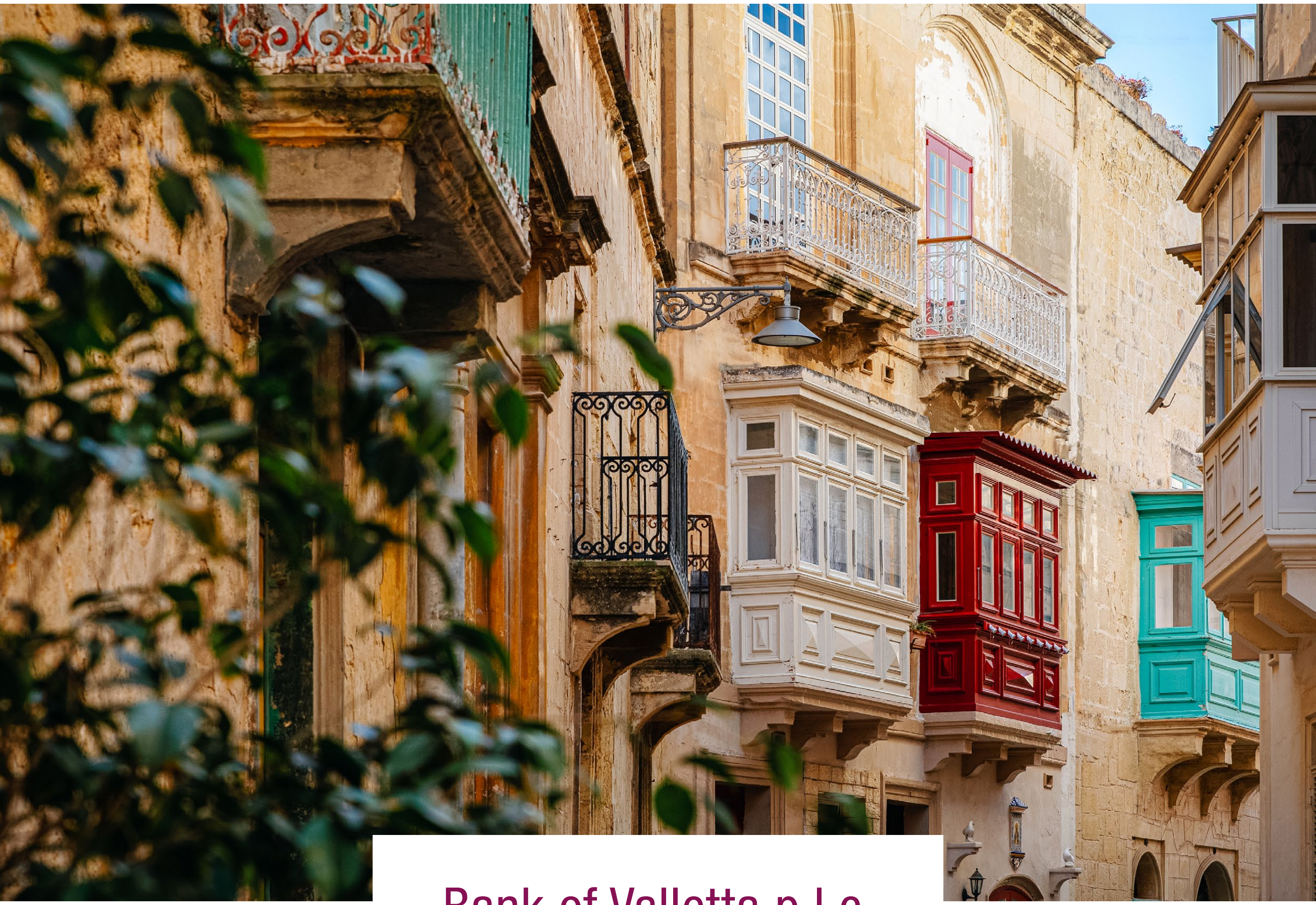
Reference is made to Company Announcement BOV386 issued on 3 April 2020. Besides the link provided therein, Bank of Valletta p.l.c. Annual Report and Accounts for the financial year ending 31 December 2019 are being enclosed herein with this Company Announcement.

Unquote

Dr. Ruth Spiteri Longhurst B.A., LL.D.
Company Secretary

6 April 2020

Registered Office: 58, Triq San Żakkarija, Il-Belt Valletta VLT 1130 - Malta Registration Number: C 2833
Bank of Valletta p.l.c. is a public limited company licensed 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).
Bank of Valletta p.l.c. is an enrolled tied insurance intermediary of MSV Life p.l.c. MSV Life is authorised by the Malta Financial Services Authority to carry on long term business of insurance under the Insurance Business Act 1998.
Bank of Valletta p.l.c. is authorised to act as a trustee by the Malta Financial Services Authority.



Bank of Valletta p.l.c.

Annual Report & Financial Statements

2019

BOV

Bank of Valletta

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COMPANY SECRETARY

Ruth Spiteri Longhurst

EXECUTIVE COMMITTEE

Rick Hunkin (Chief Executive Officer)
Ernest John Agius (Chief Operations Officer)
Joseph Agius (Chief Technology Officer)
Miguel Borg (Chief Risk Officer)
Kenneth Farrugia (Chief Business Development Officer)
Albert Frendo (Chief Credit Officer)
Elvia George (Chief Finance Officer)
Anthony Scicluna (Chief Officer Human Resources and Ethics)

Rudolph Gatt (Secretary)

AUDITORS

KPMG

LEGAL ADVISORS

Camilleri Preziosi

NOTICE OF MEETING

In view of the current COVID-19 scenario and in order for the Bank to safeguard the health and safety of its shareholders, employees and other stakeholders the date of the Annual General Meeting, originally planned for 15 May 2020, is being postponed. A new date will be advised in due course, via a Company Announcement.

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Board of Directors and Group Company Secretary

Taddeo Scerri
Chairman

NED *

Taddeo Scerri was appointed Chairman of the Bank in December 2016. Mr Scerri had been serving as Director of the Bank as from April 2013. Mr Scerri chaired the Bank's Audit Committee and was a member of the Bank's Remuneration Committee and of the Asset Liability Management Committee. He currently chairs the Board's Nominations and Governance Committee. Until end 2019 he also used to chair the Remuneration Committee and the Credit Committee. As from 2018 he was appointed director of Mapfre MiddleSea Insurance plc and was recently appointed director of MAPFRE MSV Life p.l.c (subject to regulatory approval). A qualified accountant by profession, Mr Scerri was the managing partner of RSM Malta until his retirement in 2015. He was also chairman of the local UEFA Clubs Licensing Board and a member of the Malta Football Association's Finance Committee.

Stephen Agius
Director

NED *

Appointed to the Board in December 2016. Stephen Agius is currently a member of the Nominations and Governance Committee and of the Remuneration Committee. During 2019 he was also a member of the Audit Committee. Mr Agius works as Chief Operating Officer at Mater Dei Hospital where he is responsible for strategy formulation and execution; and the day to day operations of the hospital. For five years, Mr Agius served as member of the board of directors of Enemalta p.l.c. and Engineering Resources Limited. Prior to his current role, Mr Agius occupied various positions where he was responsible for a number of large scale projects both locally and abroad in areas related to enterprise resource planning, business intelligence, business transformation and process modelling. Mr Agius is also a visiting senior lecturer at the University of Malta where he lectures Big Data Analytics and Social Media Marketing Strategy. He studied computer science and information systems and gained an honours Bachelor degree from the University of Greenwich (UK) followed by an MBA in e-Business from the University of Malta.

Alan Attard
Director

NED

Appointed to the Board in December 2016 and resigned on 1 January 2020. Alan Attard was a member of the Compliance and Crime Prevention Committee and the Risk Management Committee. He joined the Bank in 1987. For the past fifteen years, he has held various managerial positions including serving as branch manager of several branches. At present, Mr Attard is the branch manager of Floriana branch which is classified as one of the Bank's premier branches. In July 2015, he was elected as trustee on the board of trustees of the BOV Employees' Foundation serving as secretary to the said board and then as chairman between 2018 and 2019.

Paul V Azzopardi
Director

NED *

Appointed to the Board in December 2016 and resigned on 15 February 2020. Paul V Azzopardi was the chairman of the Compliance and Crime Prevention Committee, deputy chairman of the Risk Management Committee and member of the Audit Committee. He set up and managed Azzopardi Financial Services between 1989 and 2006 and subsequently worked in investments in Ontario, Canada, as director and portfolio manager. Mr Azzopardi was sponsoring and corporate stockbroker of the Bank from 1992 until 2006, and also served in the same roles for the funds of BOV Asset Management Limited and other companies. He is the author of "Behavioural Technical Analysis", two other books on investments and contributes regularly to the press. Mr Azzopardi lectured at the University of Malta and the School of Continuing Studies, University of Toronto. He holds a first degree in accountancy from the University of Malta, an MBA from the University of British Columbia, is a Fellow of the Malta Institute of Accountants and a Certified Public Accountant. Mr Azzopardi was also Director of BOV Asset Management Limited until he resigned in February 2020.

Miguel Borg
Director

ED

Appointed to the Board in August 2017. Miguel Borg is the Chief Risk Officer and an Executive Director of Bank of Valletta plc. He serves as the Deputy Chairman of the Executive Committee (previously referred to as the Management Board) and chairs both the Credit Committee and the Internal Control & Risk Management Committee of BOV. In 2019, Mr Borg was a member of the Ethics Committee. Mr Borg is a Director of BOV Asset Management Ltd and chairs the Risk Committee of the company. He also chairs the Risk Committee of MAPFRE MSV Life plc. Mr Borg is also Chairman of the Central Co-Operative Fund. Prior to joining the Bank, he worked at the Central Bank of Malta. Mr Borg holds a Masters in Economics and is a member of a number of international risk management associations. He lectures at the University of Malta.

James Grech
Director

NED

Appointed to the Board in 2004 till 2008. Re-appointed to the Board by the shareholders in the respective AGMs in December 2014 to date. Mr Grech's career commenced as a management accountant with a local accounting firm. He later joined the Bank in 1998 and is currently the Executive Head of Foreign Bank Relationships Department reporting to the Chief Officer Treasury. During the reporting year, he was a member of the Bank's Risk Management Committee and of the Credit Committee. Mr Grech is also a director of other local companies, Non Executive Chairman of Malta Industrial Parks Limited and a recognised member of the Institute of Directors (UK). Mr Grech holds an Honours Degree in Management and a Masters in Business Administration from Henley Management College (UK). His dissertation focused on the effectiveness of Board Performance and Corporate Governance. Mr Grech has lectured on Financial Services at the Malta College of Arts, Science and Technology, and on Corporate Governance at the University of Malta.

Alfred Lupi
Director

NED *

Appointed to the Board in December 2015 and currently chairs the Audit Committee and is a member of the Remuneration Committee. In 2019, he used to chair the Ethics Committee and was also a member of the Credit Committee and the Compliance and Crime Prevention Committee. Mr Lupi is an accountant by profession, with a degree in economics. He was chief financial officer in two major companies in Malta and the Executive Chairman of Pavi Shopping Complex p.l.c. Mr Lupi was a non-executive director of the Central Bank of Malta, chairing its Audit Committee and also served as Acting Governor. For a number of years Mr Lupi chaired the Accountancy Board and was subsequently a member of its Quality Assurance Oversight Committee. Mr Lupi has held a number of board appointments mainly in the financial sector.

Mario Mallia
Director

ED

Appointed to the Board in July 2017 and resigned in December 2019. Mario Mallia joined the Bank in September 1979 and was appointed as the Bank's Chief Executive Officer in January 2016. Mr Mallia has carried out various other executive roles at the Bank, including those of Chief Finance Officer, Chief Risk Officer and Chief Operations Officer. Up until the date of his retirement, Mr Mallia was chairman of the BOV Management Board and the Asset Liability Management Committee. He was a member of the Credit Committee and Ethics Committee, and also a director on the board of MAPFRE MSV Life p.l.c. Mr Mallia graduated in accountancy from the University of Malta, held the Certified Public Accountant warrant and was a Fellow of the Malta Institute of Accountants.

Rick Hunkin
Director

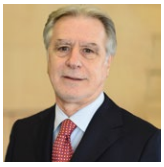
ED

Appointed to the Board on 1 January 2020 as Executive Director. Mr Hunkin is the Bank's Chief Executive Officer and is a vastly experienced financial services executive who has worked in all aspects of retail, commercial and corporate banking for over 35 years. Having started his career at NatWest and then LloydsTSB, he has since covered a wide span of organisations and held seats on the Boards of several UK financial services companies including Tesco Bank, Cheltenham and Gloucester, Goldfish Bank, GE Money and National Bank of New Zealand. Post the 2007/08 crisis Rick was one of a small senior group hired to resolve issues at Northern Rock and subsequently joined the Executive team leading the establishment of Williams & Glyn (part of the RBS EU remediation programme). Prior to joining BOV, he was Chief Risk Officer of Chetwood Financial. Mr Hunkin chairs the BOV Executive Committee (previously referred to as the Management Board) and the Asset Liability Management Committee and is also a member of various management committees. Mr Rick Hunkin, holds a Masters in Business Administration from Manchester University and a Financial Studies Diploma - a degree level qualification obtained via the Chartered Institute of Bankers and Sheffield Hallam University. He has been elected a Fellow of the Chartered Institute of Banking in both England and Scotland (FCIB, FCIBS) for services to Banking and Education.

Anita Mangion
Director

NED *

Appointed to the Board in December 2016. In 2019 Anita Mangion was a member of the Remuneration Committee and deputy chairperson of the Compliance and Crime Prevention Committee. Ms Mangion is currently a member of the Audit Committee. Ms Mangion is an experienced Business and IT Consultant. Her area of specialisation is Technology Intrapreneurship. During the last seventeen years she consulted to such effect, different local and international entities in various sectors as well as start-ups, where she successfully drove critical projects to completion and implemented sustainable profitable frameworks. Ms Mangion graduated in Executive MBA (eBusiness); B.Com. Management Hons and B.Sc. Business and Computing from the University of Malta. Additionally, she studied Business and IT at Indiana University (USA), and Technology Entrepreneurship and New Business Operations at the University of Malta in joint collaboration with Oxford University (UK). For four years, Ms Mangion served as board director at Malta Industrial Parks Limited (MIP). At MIP she was also entrusted to oversee the Tenders Committee, was a member of the Audit Committee and chaired the ICT Steering Committee.



Antonio Piras
Director

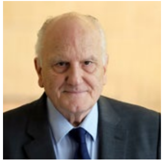
NED *

Appointed to the Board in December 2016. Mr Antonio Piras is currently the chairman of the Remuneration Committee and a member of the Risk Management Committee. He was previously a member of the Audit Committee. Mr Piras occupies the role of deputy chairman of the board and the deputy chairman of the Audit and Risk Committee of Banca UBAE (Rome). He was previously director of the boards of Iacobucci Aerospace HF (Rome) and vice chairman of Eurofidi Soc. Consortile Garanzia Fidi s.c.a.r.l. (Turin). Until 2014, he was the CEO of Equitalia Centro S.p.A (Florence) and chairman and CEO of other companies of Equitalia Group. In 1971 he started his career at UniCredit Group, former Credito Italiano, holding various key roles in the Italian commercial network until 1997. In 1998, Mr Piras was appointed as CEO of UniCredit Factoring (Milan), Deputy General Manager of Banca dell'Umbria, chairman and CEO of Pekao Leasing Sp.z.o.o (Warsaw) and Leasing Fabryczny Sp.z.o.o (Lublin), CEO of UniRiscossioni S.p.A. (Turin), all companies held by UniCredit, from where he ended his career as Senior Executive Vice President in 2009.

Joseph M Zrinzo
Director

NED *

Appointed to the Board in December 2013 and resigned on 1 September 2019. Up until he relinquished his post of Director, Joseph M Zrinzo chaired the Board's Risk Management Committee. Mr Zrinzo was also a member of the Audit Committee and deputy chairman of the Nominations and Governance Committee. He also serves as a member of the BOV Arts Committee. Mr Zrinzo currently serves as managing director of a group of family companies, as board director of other local companies, committee member of the Cultural Heritage Advisory Committee and is an active member of philanthropic associations. Over the years, Mr Zrinzo served as director on boards of various local and international companies. He was a founder member of the Malta Shareholders' Association and has vast experience of international trade.



Alfred Mifsud
Director

NED *

Appointed to the Board in December 2019. From 2015 to 2017 Mr Mifsud was Deputy Governor of the Central Bank of Malta, with main responsibilities of the monetary policy and banking operations. Prior to that, Mr Mifsud was Chairman of Crystal Finance Investments Limited, a position he held for 15 years. From 1992 to 1996 he was a Governor on the Board of Malta Financial Services Centre which now is MFSA. From 1996 to 1998, Mr Mifsud was Chairman of Mid-Med Bank. He holds a Masters in Business Administration from Sheffield Hallam University and a Financial Studies Diploma by the former Chartered Institute of Bankers. Mr Mifsud presently chairs the Bank's Risk Management Committee and is a member of the Audit Committee and of the Compliance and Crime Prevention Committee.

Diane Bugeja
Director

NED *

Appointed to the Board in December 2019. Dr Bueja is a lawyer by profession practicing primarily in financial services law, financial regulation and anti-financial crime compliance. She is currently a Senior Associate at Camilleri Preziosi Advocates. Prior to joining Camilleri Preziosi, Diane held the post of Senior Manager at a Big Four audit firm, working in Malta and in London. She subsequently joined the enforcement departments of the UK Financial Conduct Authority and the Malta Financial Services Authority. Diane holds a Ph.D in law from King's College London and a M.Sc from the London School of Economics and Political Science. She is also a visiting lecturer at the University of Malta. Dr Bugeja currently chairs the Bank's Compliance and Crime Prevention Committee and is a member of the Risk Management Committee and Nominations and Governance Committee.

Ruth Spiteri Longhurst
Group Company Secretary

Appointed Group company secretary in April 2016. Previously she occupied the post of executive head of the compliance unit within the Bank. Dr Spiteri Longhurst is also the company secretary of MAPFRE MSV Life p.l.c., BOV Asset Management Limited and BOV Fund Services Limited. Dr Spiteri Longhurst graduated Doctor of Laws from the University of Malta in 2001 and obtained Master of Arts in Financial Services in 2004. Dr Ruth Spiteri Longhurst has been employed with the Bank for the past eighteen years.

ED	Executive Director
NED	Non-executive Director
*	Independent

Chairman's Statement

Taddeo Scerri

BOV again delivered a strong financial performance in 2019

BOV again delivered a strong financial performance in 2019, which sees the Bank strengthen its capital reserves and return to the payment of a dividend.

The Board has overseen a strategy which has sought to deliver a safe and stronger bank. This included the strengthening of governance, risk management and controls. Good progress is being made on these fronts, although the work and costs will continue through into 2020, as we are only part way through a major Transformation Programme in this respect. The Bank has considerably enhanced the skills and capabilities at Board and management levels including more experienced NEDs and a new CEO.

The strong results have been delivered in the midst of a cybercrime attack, regulatory challenges, de-risking and the ongoing lawsuits, all whilst executing an extensive IT system migration. Looking ahead, the COVID-19 pandemic, the legacy litigation cases and the ongoing transformation costs will make 2020 another challenging year.

STRONGER CAPITAL POSITION

The Bank substantially strengthened its core capital ratios in 2019 – this was after taking into account the substantial transformation expenses and the further increase in litigation provisioning.

The Board gives priority to long-term stability over short-term return. We managed to build significant capital buffers as a result of the capital enhancement program that we started some years ago. Profit retention, the proactive management of risk weighted assets and issue of new capital instruments markedly increased capital reserves.

We delivered a CET1 ratio of 19.5%, an increase of 120bps. This is a strong capital position with a significant buffer above the regulatory minimum requirements and gives us protection against a range of uncertainties. We regularly monitor and stress test our capital position.

In terms of share price, the Board again focuses on the long term rather than short run movements. A mismatch is noted between the current share price and the underlying fundamentals of the Bank. The remedial actions being taken will help to further strengthen these fundamentals, especially in uncertain times ahead.

Our aim is to reward our shareholders with a sustainable and stable dividend, while ensuring sufficient capital buffers to weather stress scenarios. The Board will strive to maintain an appropriate balance between the strengthening of capital and an equitable return to shareholders.

This year the Board proposes to the shareholders a total gross dividend of 2.64 cents per share, subject to regulatory approval. This is equivalent to a total net dividend of 1.71 cents per share.

BOV is closely monitoring the situation and constantly assessing the impact of the COVID-19 pandemic on the capital position of the Group. The European Central Bank announced measures that will allow banks to operate temporarily below the level of capital defined by the regulatory buffers.

At this early stage of the pandemic, it is very difficult to estimate the potential impact of COVID-19 on the Bank's capital position. In recent years, the Bank built up a material capital buffer prudently exceeding the regulatory capital requirements. Nevertheless, there are uncertainties on both the duration of the crisis and the scale of the impact. Some degree of mitigation will be forthcoming dependent upon what local national or EU measures are implemented.

STRATEGY AND TRANSFORMATION

2019 was the year where the Bank made major strides in executing its strategic transformation.

We successfully rolled out the new Core Banking System. This was a three-year strategic transformation initiative that simplified the IT architecture with re-engineered core processes. At the same time, we enhanced our digital product suite by introducing a new version of the Bank's Mobile Banking App and BOV Pay.

The Bank is progressing well with the remediation plan to enhance its internal controls. We took robust measures to address the issues highlighted by the ECB in their 2018 on-site inspection. We developed a new Risk Appetite Framework, enhanced corporate governance, developed a structured strategic framework and enhanced the resources and capabilities in the control functions. All of these initiatives were implemented in consultation and agreement with the ECB. In the coming months, we will continue to work on measures to enhance the compliance culture and capabilities.

BOARD MEMBERSHIP

During the year, I commissioned an independent Board evaluation that provided useful input on the strengthening of the Bank's governance arrangements. We are committed to have the right balance of skills and experience within the Board, both at an individual and on a collective basis.

There were a number of Board changes in 2019 and early 2020. Joseph Zrinzo, Alan Attard and Paul Azzopardi retired from the Board. I am very grateful for their valuable service and dedication. Alfred Mifsud and Diane Bugeja were co-opted as Independent Non-Executive Directors in line with the amendments approved during the last Annual General Meeting. The co-option will enhance the skills of the Board especially in the area of risk management and compliance. Rick Hunkin, in his capacity as CEO, joined the Board as an Executive Director. I am sure the new directors will enrich the Board's collective capabilities with their experience and balance of skills.

The sudden and untimely passing of Mario Mallia, less than two months after his retirement from the Bank, shocked the financial community. Mario gave forty years of dedicated service to BOV, rising through the ranks of the company to the position of CEO and Executive Director. He will be remembered for his intellect, integrity, professionalism and kindness. Under his stewardship, the Bank achieved ambitious milestones in a testing environment. He was the architect of a multi-year transformation project, laying the foundations for long-term stability, sustainability and value creation. BOV mourns the loss of a true gentleman.

LITIGATION

We have always been preparing for the possibility that the Deiulemar case, a legacy of a trust structure from 2009, could be decided against the Bank in the court of first instance.

The Bank has very recently obtained new and independent confirmation of existing advice that the claim is without merit.

Our aim is to reward our shareholders with a sustainable and stable dividend

However the intensity of public pressure in Torre Annunziata may play a decisive role in the first instance ruling, regardless of the actual merit. We are fully committed to exercising all our legal rights at every instance and court, fully expectant that ultimately we will receive a fair hearing.

In May 2019, the Bank filed proceedings against the State of Italy before the European Court of Human Rights in Strasbourg with a view to safeguarding its fundamental right to a fair hearing in this matter in terms of the European Convention on Human Rights.

The other main claim relates to the Swedish Pension Agency (SPA), being the sole investor in Falcon Fund SICAV. No legal proceedings have been initiated by the SPA. Recently both parties agreed to mediation in London.

While there were positive developments on the two main litigation claims, the Board cautiously decided to increase litigation provision by a further €25 million to €100 million. This in order to be in a position to defend our rights to the highest level, and to guard against stress risks.

Finally in relation to the Property Fund, the Bank appealed the Arbiter decision that ordered the Bank and other service providers to pay the sum of €3.4 million plus interest and charges. Following the favourable judgement delivered by the Court of Appeal in December 2019, the Bank is no longer deemed to have an exposure on this case in view that this recent court decision is likely to be reflected in any similar outstanding cases.

BOV IN THE COMMUNITY

Bank of Valletta continues to provide significant support for the development of the Maltese society. The Bank is proud to operate a comprehensive CSR programme, setting a benchmark for other local companies, and invests a considerable portion of its profits back into the community for the benefit of current and future generations.

Bank of Valletta's CSR programme supports a wide spectrum of community activities across the arts and culture, heritage, environment, sports, education and philanthropy.

In 2019 Bank of Valletta pledged its commitment to three projects that will have a notable positive social impact:

- Through a partnership with the Marigold Foundation - BOV in the Community, we made a significant contribution to Caritas for the refurbishment and modernisation of its male quarters at the San Blas Therapeutic Community. The premises underwent a complete renovation and it now has been totally transformed and offers a safe and dignified environment to individuals following the delicate residential drug rehabilitation programme.

- The second noteworthy project which we are excited to support is the transformation of the former Adelaide Cini Institute in Santa Venera into the first state-of-the-art palliative care complex in Malta – the St Michael Hospice Project. Statistics show that cancer is currently affecting one in every three people and palliative care has never been as important as it is today. The whole floor area of the property totals 11,000 square metres and is expected to host its first patients by 2021.

- The third project that we are proud to be supporting and covers both educational and humanitarian causes, is the development of a multi-sensory room for children within a wide spectrum of behavioural and learning difficulties.

The multi-sensory room will be hosted within the Esplora building in Kalkara and it will give equal opportunities for children to experience the joy of learning and experimentation.

A number of philanthropic activities are supported both by the Bank as an organisation but also by the Bank's staff who organise multiple activities throughout the year to raise funds and donate their time towards such causes.

Bank of Valletta continued to support a number of major events and initiatives in conjunction with the Malta Community Chest Fund and supported local major NGOs and other organisations in the sphere of arts and culture, restoration projects and the environment. We remain a strong supporter of the sporting scene with the Bank being associated with football, basketball, waterpolo, sporting initiatives for youths with SportMalta and other initiatives on a community level.

LOOKING AHEAD

2020 is another challenging year. The unfolding impact of the COVID-19 pandemic, MONEYVAL's evaluation report on Malta, legacy litigation cases, transformation costs and persistent low/negative interest rate environment present a challenging environment. BOV's resilient business model and strong buffers will cushion the impact, although profitability will be affected.

We will continue with the transformation programme. We will continue to work to strengthen the foundations and control environment of the Bank. Our strategic focus will be on business lines that sit well within our re-defined risk appetite and we will strive to achieve greater efficiency in delivering these and therefore keep costs under control and sustain revenue growth.

Our success depends on our customers and we need to adapt to meet their evolving needs. The new strategic approach will focus on the development of efficient and cost-effective channels, simplified products and an enhanced customer experience.

I would like to thank my fellow directors, the dedicated employees, the shareholders and all our customers for their crucial support.

After seven years as Director, half of which as Chairman, I have decided to withdraw from the Board and focus more on my personal life and family. The 15th May 2020 will be my last day as Chairman and member of the Board.

Looking back, I am proud of our achievements during some turbulent times. Together we have built a stronger, safer and more sustainable institution that has the capacity and resources to service and support the Maltese economy. At the same time it continues to effectively balance the needs and aspirations of all its stakeholders. I have no doubt that the Board, Executives and dedicated employees will continue to build on these strong grounds in the years ahead.

It has been a privilege to serve as Chairman of BOV.

Taddeo Scerri
Chairman
18 March 2020

CEO's Commentary

Rick Hunkin

The Group reported pre-tax profit of €89.2 million

A PIVOTAL YEAR TOWARDS A SAFER, STRONGER BANK

Although 2019 presented many challenges for the Bank, it is pleasing to be able to report on a strong set of results for Bank of Valletta. This performance enables us to strengthen our capital position as we build upon a significant de-risking programme, supported by tangible improvements in our risk, governance and control frameworks.

The key highlights of our financial performance are a reported profit before tax of €89.2 million (which compares with €71.2 million for 2018). Profit attributable to shareholders of €63.5 million result in an earnings per share of 10.9 cents compared to 8.8 cents last year.

Adjusting for an additional contingent liability provision of €25 million (2018: €75 million) and additional costs associated with our transformation programme of €23.9 million, underlying profit is €138.1 million (2018: €146.2 million). This reflects a reduction of only 6% year-on-year, at a time when the Bank has significantly reduced higher risk areas of the business and is reflective also of a positive local economy which has sustained demand for credit.

The balance sheet has continued to grow, with gross advances to customers 1.9% higher than 2018 at €4.7 billion. Deposits are also up by 2.1%, which reflects growth from our local retail economic activity, offsetting substantial reductions in deposits held by international clients.

To deliver on our strategy of a safer, stronger bank, we have invested heavily in de-risking our portfolio through a new risk appetite, increased controls and tighter policies, and remediating any past control failings. This required an investment of €23.9 million during 2019, and it is likely that we will need to continue investing during 2020 to provide all stakeholders with increasing confidence we are moving towards our overall aim.

Similarly, our aim is to remove the overhang of contingent liabilities and BOV has been putting great focus on closing these out. The historic property fund issue has been settled in the Bank's favour and closed, mediation discussions are underway with the Swedish Pension Authority and the Bank has received additional very strong legal opinion regarding its position around Deiulemar. Although we are increasing our provision in respect

The strong performance of the local economy had a positive impact on the results of the Group

of these collectively, this reflects our determination to defend the Bank's interest to the maximum level whilst looking for opportunities to bring early closure wherever possible.

As we move through 2020 our initial focus will remain on making BOV safer and stronger, but will increasingly move to a greater customer focus, simplification and streamlining as we begin to build on our successful core banking migration. From this our next strategy phase will move to supporting business growth and cost efficiency from a strong platform.

FINANCIAL PERFORMANCE OF THE GROUP

The strong performance of the local economy had a positive impact on the results of the Group. Malta recorded GDP growth of 4.4% in real terms in 2019[1]. The Central Bank of Malta forecasts good economic prospects for the coming years, although growth rates are expected to be lower than the record rates seen in previous years. Employment continued to grow, with the Labour Force Survey[2] estimating growth of 4.5% for the third quarter of 2019 over the same period for the previous year.

Group operating income of €249.8 million comprised net interest margin (€152.9 million), fee income (€73.8 million), trading and dividend income (€18.1 million) and fair value gains on investments (€5.0 million). The net interest margin and fee income are both below those recorded in FY2018, while trading income remained at last year's level and fair value gains registered an increase.

Pre-tax profit for FY 2019 was €89.2 million compared to €71.2 million last year. This figure is net of litigation provisions and represents a post-tax return on equity of 6.2% (2018: 5.3%) which compares well with the average return for Eurozone banks.

Pre-tax profit, as stated before the litigation provision of €25 million and transformation costs of €23.9 million, was €138.1 million, down by 6% when compared to €146.2 million for 2018.

Net interest margin, representing 61% of operating income, remains the Bank's main revenue source. The net interest margin continues to be under stress within the current context of surplus liquidity and low to negative yields.

The positive income from strong growth in the credit business was offset by declining return on treasury investments as higher yielding assets matured and negative interest paid on higher liquidity levels. The increase in negative interest paid was partly mitigated by the lower cost of long-term borrowings as maturing bonds were partially replaced with a new issue at a lower coupon rate.

Net commission income decreased by 9% and this is a result of the Bank exiting higher risk business areas as part of the de-risking initiatives, the introduction of new regulation which impacted the sale of investment products and the non-repeat of a one off gain of €3 million recognised in 2018. Trading and exchange earnings are in line with the previous year as growth

[1] National Statistics Office – News Release 034/2020

[2] National Statistics Office - Labour Force Survey Q3/2019

Gross advances increased by €88 million and stood at €4.7 billion at the year end

from local business more than offset reduced trading from international clients. Fair value gains arose mostly on equity holdings with €5 million recorded in the Profit and Loss and a further €4.7 million resulting through reserves – Fair Value through Other Comprehensive Income (FVOCI).

The share of profit from investment in insurance interests is almost double that of the previous year as both the life and the non-life business reported improved performance which was also influenced by positive market movements.

Total expenses for the year amounted to €163.0 million and include additional costs of €23.9 million relating to the ongoing Transformation Programme. The Group continued investing in human resources, especially in areas relating to risk management, Anti-Money Laundering (AML) and other control functions. The roll-out of a number of new IT systems and upgrades as well as the final phase of the implementation of the Core Banking Transformation (CBT) programme resulted in higher IT-related costs. The cost to income ratio stood at 61.4% (2018: 49.1%) or 52.4% when the costs relating to the Transformation Programme are excluded.

During 2019, a net impairment reversal of €11.6 million (2018: €10.8 million) was recorded. The proactive stance towards debt management resulted in further recoveries being made in respect of non-performing loans previously written off. This, together with the Group's continued focus on improving the credit quality of its credit portfolios, resulted in an improvement of the NPL ratio from 5.3% last year to 4.6% at 31 December 2019.

BALANCE SHEET STRENGTH

At the year end, the Group's balance sheet comprised total assets of €12.3 billion, which is marginally up year-on-year. Customer deposits remain the main source of funding, representing 86% of total assets. De-risking initiatives carried out during the year resulted in substantial reductions in international corporate deposits which were down by 24%. This reduction was offset by increases in resident deposits, mostly retail, as the economic activity generated by the local economy meant that more liquidity was channelled into banks.

The Bank's customer deposits are up by €214.8 million or 2.1% and amount to €10.6 billion. The increase in deposits was primarily in the short term, low yield category.

Gross advances increased by €88 million and stood at €4.7 billion at the year end. While some early prepayments were experienced in the business lending book, the strong demand for home loans was sustained during the year and a 6% growth was recorded on this portfolio. Demand for personal lending was also buoyant. Despite the growth in the loan book, the advances to deposit ratio, at 44.2%, remains on the low side and in line with 2018 levels.

The Group's investment book at the end of 2019 stood at €3.1 billion, a reduction of €244 million over the prior year. Excess liquidity was channelled into short term funds which had a negative impact on the Profit and Loss in view of negative rates applied by the ECB and other prime banks.

The Group's equity base increased to €1.1 billion, an increase of 6.9% over last year. The Group's CET 1 and capital adequacy ratios stand at 19.5% and 23.1% respectively (2018: 18.3%, 21.1%).

We are steadfast in our commitment to strengthen the capital buffers while distributing appropriate cash dividends to our shareholders. The Bank has built up material capital buffers, which is the result of a focused capital enhancement program based on profit retention, proactive management of risk-weighted assets and issue of new capital instruments.

REVIEW OF KEY BUSINESS AREAS

Personal Banking

Personal customers are by far the Bank's largest customer segment, and we are adapting our business models and delivery channels in line with changing demographics and shifts in behavioural trends. On the digital front, we provided our customers with a new version of the Bank's mobile banking app, which offers a better customer experience and improved security features.

To support cashless payments, the Bank launched the new BOV Mobile app alongside facilitating mobile-to-mobile payments. The smartphone is increasingly becoming the primary digital banking tool for many customers, and the Bank now provides the 'BOV Signatures' app as part of the BOV Mobile suite of services, giving customers the option to do away with any hardware token, previously used to log into Internet Banking. Customers can now authorise transactions on both BOV's internet and mobile platforms using just their smartphone.

Millennials continue to be an important market segment for the Bank. During 2019, Bank of Valletta launched its BOV Club 2019, its most popular package specifically designed for students embarking on post-secondary or tertiary education. New BOV Club members or students renewing their BOV Club package received significant benefits ranging from free gifts to a wide selection of carefully selected items at highly discounted prices.

As well as our digital offering, we understand that our customers also want access to banking services at a convenient time for them. We therefore introduced new opening hours for the Bank's network of branches, which are a closer fit to our customers' busy schedules. The change in opening hours also enhanced the ability of our branch staff to process customers' applications, resulting in faster response times and increased efficiency. Bank of Valletta is proud to operate the largest branch network on the island, servicing the needs of residents across Malta and Gozo.

Lending

The Bank remained highly active in both the retail and commercial businesses, recording a healthy increase in its credit portfolio, with aggregate net growth of around €88 million, equivalent to a year-on-year increase of 1.9%. The positive results were mainly in the retail arm which grew by more than 6% over the year.

Over €480 million of funds were extended to nearly nine hundred local businesses, to support their plans for expansion and development, demonstrating the Bank's commitment towards the business community. The funds benefitted a variety of traditional and emerging economic sectors as the Bank continues to diversify its portfolio. A number of sizeable repayments took place during the year resulting in a marginal net drop in the overall commercial portfolio.

The Bank continued to widen its product offering and enhance access to finance for SMEs and family businesses. In conjunction with the European Investment Fund (EIF), the Bank topped up the funds available for the SME Initiative scheme (JAIME) by nearly €20 million. This product proved to be extremely attractive and in demand by local SMEs. To date the Bank has extended €61 million of funding under this scheme to six hundred and twenty customers. We are pleased to note that micro SMEs were the highest beneficiaries of this scheme with 81% of total number of facilities being granted to this critical customer segment.

The successful implementation of Risk Sharing Instruments in recent years has been very popular with the local business community. This led the Bank to hold discussions with the Malta Development Bank (MDB), resulting in the launch of two new products: the 'SME Invest' and the 'BOV Family Business Transfer Facility'. The SME Invest product has a portfolio capacity of €50 million and was received very well with nearly €15 million sanctioned from six months of its launch. The 'BOV Family Business Transfer Facility' was designed to facilitate the smooth transfer of family businesses from one generation to the next while ensuring proper governance and care of hard-earned assets.

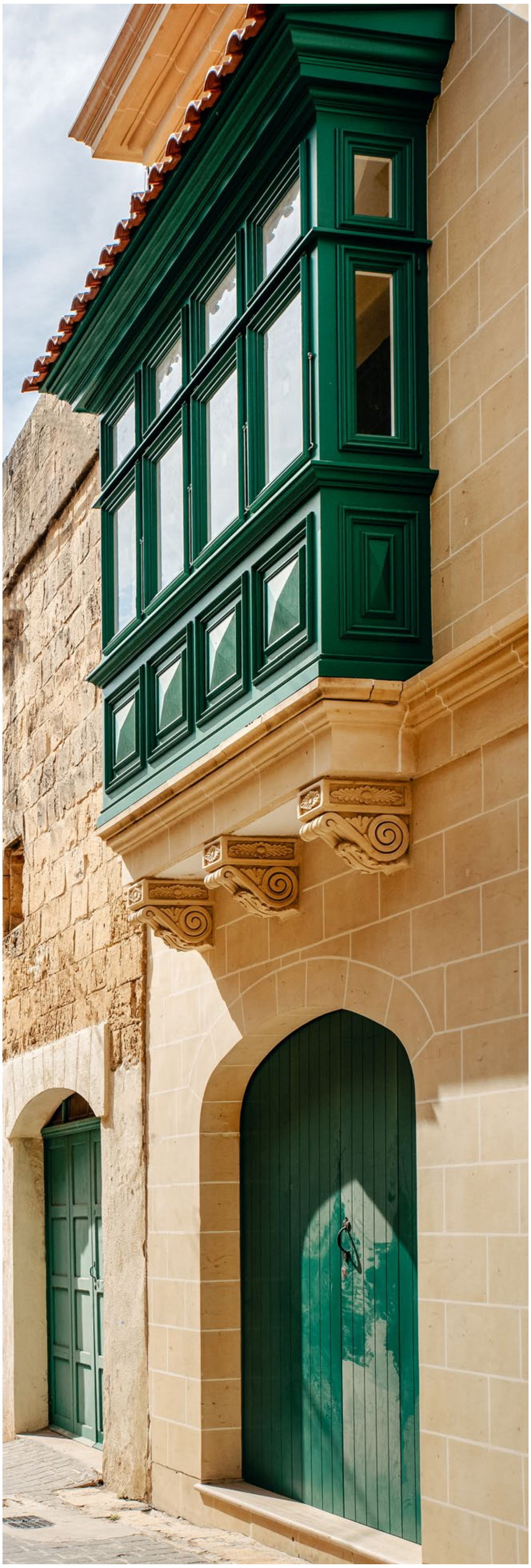
The consumer finance segment proved to be very active with the Bank underwriting more than €400 million in new funds over a twelve-month period. Despite the highly competitive landscape and the increased regulation on residential property lending, also brought about by the CBM Directive 16, the Bank continued to consolidate its position in the market through a net growth of over €135 million. This was a direct result of the Bank's customer-centric approach and the widening of the product suite to cater for specific needs of different customer segments. This approach also saw the Bank recently launch the BOV Studies+ product which assists students in furthering their studies up to doctorate level. The scheme has been well-received with more than half of the allocated funds taken up within three months of launch.

During 2019, local property prices increased by 6.3%. Property price inflation has abated amid concerns of the market overheating, an increase in the supply of properties for sale and for rent and the introduction of macroprudential policies by the CBM.

The improvements registered over past years in the Bank's asset quality was sustained in 2019, with further curtailment of the non-performing ratio and the forbearance ratio on both commercial retail portfolios. Indeed the NPL ratio, now standing at 4.6% is the lowest ratio registered in the last ten years. This was achieved as a result of the Bank's prudent loan granting processes and consistent monitoring thereafter.

Investment Services / Fund Management

The Bank provides its customers with a comprehensive suite of investment products managed by Bank of Valletta Asset Management, the Bank's fully owned asset management as well as a range of bancassurance investment solutions that have been developed through MAPFRE MSV Life Plc, a joint partnership between Bank of Valletta Plc and MAPFRE Middle Sea Insurance Plc. During the period under review, the Bank has remained highly active in the investment services space. Through the Bank's branch network, customers are provided with a robo-advisory service which has been designed to align the customers' risk profile which are thereon linked to a choice of



three strategies to reflect their conservative, balanced or growth driven investment objectives.

On the other hand, the Bank has a dedicated network of Investment Centres where customers are provided with bespoke financial advice insofar as their investment portfolios are concerned. Moreover, for its premium customers, the Bank's Wealth Management Unit provides specialist open architecture discretionary and advisory portfolio management services.

<u>De-Risking</u>

The Bank has now reached the tail end of winding down its Trusts business. The Bank is also well on its way to ending its Third-Party Fund Custody business. During 2019 the Bank terminated thousands of international personal and corporate customer relationships which no longer fit within its risk appetite, and is concluding a review and remediation of all of its international clients.

The past year saw the launch of another significant project – the file review of the Bank's retail customer base. The Customer Acceptance Policy (CAP) had been revised in 2018 to reflect that the Bank is no longer entertaining relationships with customers that have no nexus with Malta - a criterion which has been articulated in clear and objective terms. After eighteen months of application, the CAP is now being further refined, along with other supporting policies. Customer on-boarding is also being reviewed with a view of expediting new customer account opening, whilst ensuring higher levels of control.

CONCLUSION

Our short term priority is to continue to focus on finalising our transformation, and to build the base for a better, stronger Bank of Valletta. As we progress this year, our increasing attention will turn to improving customer service, delivering growth and simplifying our processes for customers and staff. Although 2020 will still see some headwinds on cost, completion of a forward looking strategy built on customers, efficiency and service will position us well for the future.

As our Chairman covers in his report, the present situation around Corona Virus is a significant concern and BOV will continue to do all we can to ensure the welfare and protection of all our staff and customers. In what will be uncertain times over the next few months, we will work with Government and all regulatory bodies, constantly reviewing our position, to ensure we can also best support the local economy in such unusual circumstances.

I thank our many customers for whom we are their bank of choice, our shareholders for their unrelenting trust and support, the supervisory authorities with whom we have a close working relationship, my management team and all our employees for their unrelenting efforts towards Bank of Valletta.

I am writing this as Bank of Valletta's new CEO, having taken up my position on 1st January this year. My predecessor, Mario Mallia, oversaw the Bank last year, and indeed had served the Bank for 40 years before retiring. His sad and untimely death in February 2020 came as a shock to us all. Bank of Valletta will be forever in his debt for such unyielding loyalty, commitment and valuable contribution.

Finally, I refer to Deo Scerri's decision to withdraw from the Board in order to focus more on his personal life and family. Deo has been a leader of our Business for over 7 years and has made a massive contribution to the Bank. On behalf of all staff, I thank him and wish him well for the future.

Rick Hunkin
Chief Executive Officer
18 March 2020

Executive Committee

Mario Mallia
Chief Executive Officer up until December 2019

Appointed to the Board in July 2017 and resigned in December 2019. Mario Mallia joined the Bank in September 1979 and was appointed as the Bank's Chief Executive Officer in January 2016. Mr Mallia has carried out various other executive roles at the Bank, including those of Chief Finance Officer, Chief Risk Officer and Chief Operations Officer. Up until the date of his retirement, Mr Mallia was chairman of the BOV Management Board and the Asset Liability Management Committee. He was a member of the Credit Committee and Ethics Committee, and also a director on the board of MAPFRE MSV Life p.l.c. Mr Mallia graduated in accountancy from the University of Malta, held the Certified Public Accountant warrant and was a Fellow of the Malta Institute of Accountants.

Rick Hunkin
Chief Executive Officer

Rick Kunkin was appointed to the Board as Executive Director and as the Bank's Chief Executive Officer on 1 January 2020.

He is a vastly experienced financial services executive who has worked in all aspects of retail, commercial and corporate banking for over 35 years. Having started his career at NatWest and then LloydsTSB, he has since covered a wide span of organisations and held seats on the Boards of several UK financial services companies including Tesco Bank, Cheltenham and Gloucester, Goldfish Bank, GE Money and National Bank of New Zealand. Post the 2007/08 crisis Rick was one of a small senior group hired to resolve issues at Northern Rock and subsequently joined the Executive team leading the establishment of Williams & Glyn (part of the RBS EU remediation programme). Prior to joining Bank of Valletta, he was Chief Risk Officer of Chetwood Financial.

Mr Hunkin chairs the BOV Executive Committee and the Asset Liability Management Committee and is also a member of various management committees.

Mr Rick Hunkin, holds a Masters in Business Administration from Manchester University and a Financial Studies Diploma - a degree level qualification obtained via the Chartered Institute of Bankers and Sheffield Hallam University. He has been elected a Fellow of the Chartered Institute of Banking in both England and Scotland (FCIB, FCIBS) for services to Banking and Education.

Miguel Borg
Chief Risk Officer

Appointed to the Board in August 2017. Miguel Borg is the Chief Risk Officer and an Executive Director of Bank of Valletta plc. He serves as the Deputy Chairman of the Executive Committee (previously referred to as the Management Board) and chairs both the Credit Committee and the Internal Control & Risk Management Committee of BOV. In 2019, Mr Borg was a member of the Ethics Committee. Mr Borg is a Director of BOV Asset Management Ltd and chairs the Risk Committee of the company. He also chairs the Risk Committee of MAPFRE MSV Life plc. Mr Borg is also Chairman of the Central Co-Operative Fund. Prior to joining the Bank, he worked at the Central Bank of Malta. Mr Borg holds a Masters in Economics and is a member of a number of international risk management associations. He lectures at the University of Malta.

Elvia George
Chief Finance Officer

Elvia George is the Chief Finance Officer of the Group, a post she has occupied since May 2008. In this role she is responsible for all the core areas of Finance, Management Reporting and the published Group Financial Statements as well as other areas within the Group.

Ms George is a member of various committees and boards within and outside the Group including voluntary organisations. She is a certified public accountant, graduating with first class honours in accountancy from the University of Malta and a Fellow of the Malta Institute of Accountants. Besides lecturing at the University of Malta, where her area of expertise is accounting for financial institutions, she also supervises a number of students in their dissertation during their final year of the professional degree of the Masters in Accountancy or for an MA in Financial Services. Ms George is involved with the Malta University Examination Panel and has also served as a member of the Accountancy Board for a number of years.

Kenneth Farrugia
Chief Business Development Officer

Kenneth Farrugia joined the Bank in 1985 and has since occupied various positions within the Group. Mr Farrugia currently holds the post of Chief Business Development Officer and sits on the Executive Committee.

Mr Farrugia is amongst others responsible for the improvement of the Bank's market position, as well as the achievement of financial growth and long-term strategic business goals. He currently sits on the Board of Directors of BOV Asset Management Limited, and is also a director on the board of the Vilhena Funds SICAV p.l.c. Mr Farrugia is a Fellow of the Institute of Sales and Marketing Management in the UK.

Anthony Scicluna
Chief Officer Human Resources & Ethics

Anthony Scicluna was appointed as Chief Officer Ethics and Employee Development in 2016, and became a member of the Management Board (now Executive Committee) in November 2019. As Chief Officer Ethics and Employee Development, Mr Scicluna is responsible for the Group's human resources, training, ethics and employee professional development.

Mr. Scicluna joined the Bank in 1984 and mainly held positions within the bank's branch network, finance and internal audit. Between 2005 and 2013 he was responsible for the Bank's Group Internal Audit. Mr Scicluna is a certified public accountant and holds a practicing certificate in auditing. He is a Fellow of the Malta Institute of Accountants and also holds an honours degree in Business Management from the University of Malta. Mr Scicluna is a member of various committees within and outside the Group.

Albert Frendo
Chief Credit Officer

Albert Frendo is an accountant by profession and is responsible for the stewardship of the Credit Function. His career at the Bank spans over thirty years with wide ranging experience in cost management and financial reporting, risk management and credit finance. For twelve years, he headed the Bank's Risk Function and was later assigned with the management of the Bank's overall Credit Portfolio, responsible for a number of key credit areas including Corporate, SME, Consumer and Trade Finance, Collections and Collateral Management. He was entrusted to launch Risk Sharing Instruments in Malta aimed at SMEs including JEREMIE, CIP, SMEG, SME Initiative (JAIME) and SME Invest. Mr Frendo is a member of the Bank's Executive Committeeand a number of management committees. He holds a degree in Accountancy from University of Malta and a Masters in Business Administration, with specialization in Management Consulting, from Grenoble Graduate School of Business in France.

Ernest John Agius
Chief Operations Officer

Ernest John Agius was appointed Chief Operations Officer in May 2016. His previous position within the Bank was that of Change Management Executive, responsible for the setting up of the Change Management Function, which incorporates Process Management.

Mr Agius career in the financial services sector spans more than thirty three years during which he has held a number of senior executive positions within the Business and IT. He has vast experience in the Banking Operations, Financial Crime Compliance, and has led major transformation projects involving complex technology.

As Chief Operations Officer, Mr Agius is responsible for the Bank's overall Operations, Facilities Management, Administration, Security, Health & Safety, Procurement, Architect's Services, Customer Service Centre and Investment Operations.

Mr Agius is responsible for the overall business management of projects, including the implementation of Core Banking Transformation programme.

He has been a member of the Management Board (now Executive Committee) since June 2016.

Joseph Agius
Chief Technology Officer

Joseph Agius was appointed Chief Technology Officer in October 2014, and became a member of the Bank of Valletta Management Board (now Executive Committee) in October 2016.

Since joining the Bank in 1985, Mr Agius has garnered over thirty years' experience in IT and Financial Services. In this time, he has been actively involved in the implementation of various mission critical projects, including the recent Core Banking Transformation. In his role as Chief Technology Officer, Mr Agius is responsible for driving the Bank's IT strategy. He is a strong proponent for modernisation in IT, digitalisation and running IT as a business with its inherent business value.

Mr Agius holds an Honours degree in Computer Science from the University of Reading and an MBA in eBusiness from Grenoble Graduate School of Business. He is also a Chartered Engineer and member of the British Computer Society.

Corporate Social Responsibility (CSR)

As one of Malta's largest organisations, we at Bank of Valletta fully recognise our role as a responsible citizen of the Maltese Community. We operate the largest branch network, servicing the banking needs of residents and being very close to the Community in which we operate, supporting its values, its culture and its history. Bank of Valletta is also one of Malta's top employers with a workforce approaching the 2,000 mark.

The aim of our extensive Community Programme is to sustain the society, promote its heritage and its culture, care for our environment and promote a healthy lifestyle, all while ensuring economic growth, both for the country as well as for our institution.

These are some of the initiatives undertaken during 2019 in support of this commitment.

Staff

Our staff are our most valued asset. Their abilities, knowledge and experience are what enables us to give an excellent customer experience, going the extra mile to keep our customers happy. The Bank invests heavily in the training of its staff and thrives to offer the best working conditions. The signing of the new collective agreement is a tangible acknowledgement of the commitment, loyalty and services of the Bank's dedicated workforce.

Arts & Culture

The promotion of local artists remains high on the Bank's agenda. The BOV Joseph Calleja Foundation, a collaboration between Bank of Valletta and The Maltese Tenor assists local performing artists in extending their studies and taking the local music landscape to the next level. The Bank continues to support major artistic initiatives such as the Opera productions at the Manoel Theatre, Teatru Astra and Teatru Aurora, showcasing local talent, some of them scholars of the BOV Joseph Calleja Foundation.

Heritage

'The Return of the Holy Family from Egypt', the 18th century oil painting found at Comino's Chapel is being restored with BOV's support. This work of art is unique as it is the only work of art on the island of Comino. The extensive restoration of The Miraculous Crucifix of 'Ta' Ġieżu' was completed during 2019 as well as the restoration of a Gilt Monstrance Throne (Ġelandra) found at the St Dominic Church of the Annunciation in Birgu. Bank of Valletta will continue to protect our rich cultural heritage to ensure that it will continue to be enjoyed by future generations.

Social

The male quarters at the San Blas Therapeutic Community Centre in the limits of Ħaż-Żebbug were fully refurbished through the support of 'The Marigold Foundation – BOV in the Community' and now offer improved facilities for the holistic rehabilitation programme provided by Caritas (Malta).

The Bank continued to organise social initiatives among its workforce, such as Blood Donation Drives and Dress Down Days to raise funds for various NGOs and initiatives to raise awareness about various local social issues.

Sports

Bank of Valletta firmly believes that exercise is a key element in maintaining a healthy lifestyle. Bank of Valletta continues to support the major sporting organisations in Malta, the Malta Football Association, the Malta Basketball Association and the Aquatic Sports Association of Malta, assisting these associations to organise sporting competitions for various age groups and in various disciplines.

The BOV Sports and Social Club continues to encourage BOV staff members to step up their physical activity through various events and training sessions in different sporting disciplines.

Education

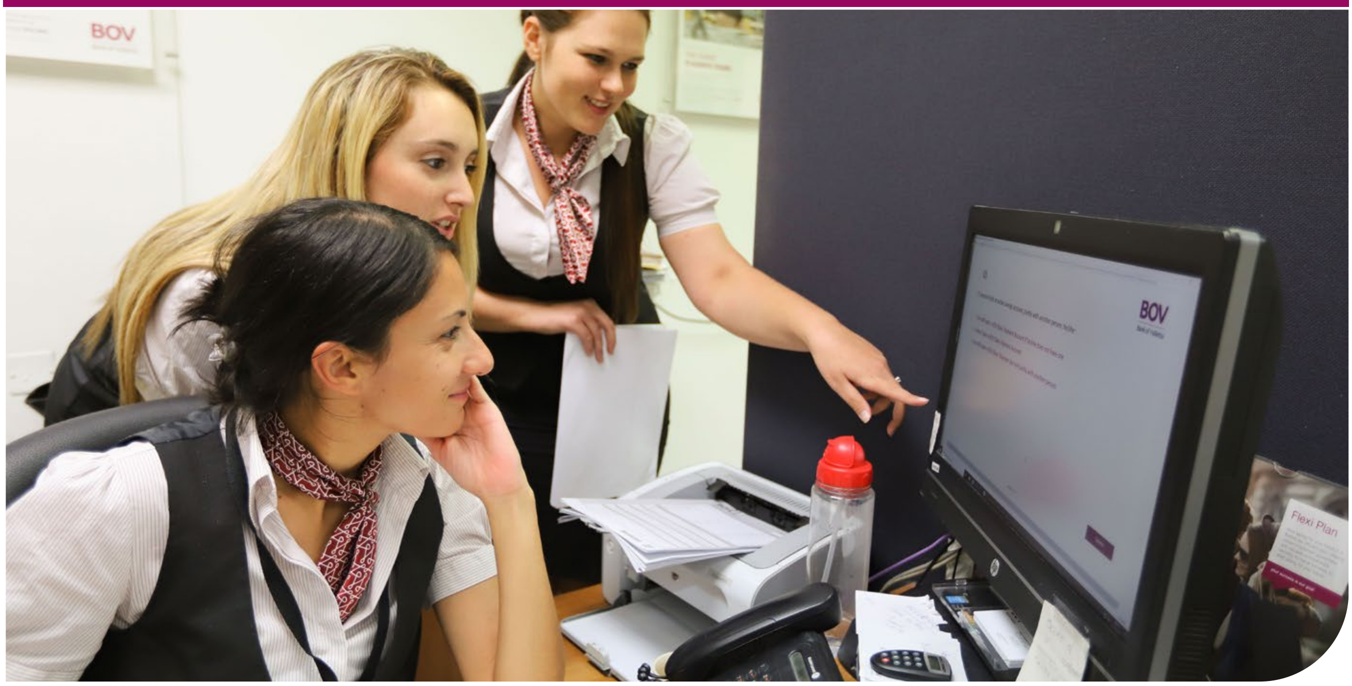
Promoting excellence in education forms an integral part of the Bank's Community Programme. The BOV Prize in Medicine, The BOV Excellence in Engineering Award and the BOV Prize in Science are among the awards supported by BOV enticing students to strive for excellence in their respective fields and become leaders in the near future.

The Bank also introduced BOV Studies Plus+, a new financing solution targeted for individuals seeking further studies through a highly attractive financial solution.

Business

The Bank's largest project of the past few years was the replacement of its Core Banking System. The new Core Banking System is key to the Bank's future sustainability and its ability to continue implementing key innovative business initiatives as well as increased operational efficiency.

The Bank continued to support and expand its collaboration with a number of constituted bodies. The goal behind these partnership is for the Bank to extend financial support to the various activities organised by these organisations and also to make available its professional human resources to the benefit of the members in order to strengthen trade opportunities within the business community in Malta.



Directors' report as at 31 December 2019

The Directors present their 46th Annual Report, together with the audited financial statements of the Bank of Valletta Group (the Group) and the Bank for the Financial Year (FY) ended 31 December 2019.

Principal Activities

The Bank of Valletta Group comprises Bank of Valletta p.l.c. (the Bank) and two subsidiary companies namely BOV Asset Management Limited (BOV AM) and BOV Fund Services Limited (BOV FS). The Group also has two equity-accounted investee companies, MAPFRE Middlesea p.l.c. and MAPFRE MSV Life p.l.c. The Group's principal activities are set out below.

The Group offers banking, financial and investment services and connected activities within the domestic Maltese market. The principal activities of the Bank comprise the following:

1) The receipt and acceptance of customers' monies for deposit in current, savings and term accounts which may be denominated in Euro and other major currencies,

2) The provision of loans and advances to a wide array of customers, and

3) The provision of investment services, covering a comprehensive suite of investment products and services that meet the customers' needs throughout their lifecycle, including stockbroking, advisory and discretionary portfolio management services.

The Group also provides a number of other services, including, bancassurance, corporate advisory, fund management, fund administration, and other services, such as 24-hour internet banking service, issuance of major credit cards, night safe facilities, automated teller machines, foreign exchange transactions, outward and inward payment transfers.

Pursuant to Article 177(2) of the Companies Act (Chapt. 386 of the Laws of Malta) the Directors declare that in mid-2019 the Bank embarked on (i) a transformation programme which revolves around the change of the Bank's core IT system to a state-of-the art Oracle platform (which was implemented on 1 January 2020) and (ii) an accelerated remediation plan.

(1) New Core Banking System

As announced in previous reports and communications, the Bank has announced a Core Banking Transformation programme to replace its information technology systems. It was the result of three years of commitment and hard work by its dedicated workforce to successfully conclude this ambitious transformation by 1 January 2020, as planned. Over the past year, BOV staff underwent intensive training and are now becoming more conversant with the new system. It is appropriate to keep in mind that such an extensive worldwide solution also needs an adaptation period both from a service perspective as well as ironing out functional issues. Throughout the changeover, the Bank also continued to deliver banking services to its customers, albeit reduced services by using cards through the ATM, ePOS and mobile locally and abroad during the changeover period.

With the implementation of the Core Banking Transformation programme, Bank of Valletta has achieved a critical cornerstone of the Group's strategy for 2020 and beyond. The new core banking system lays the foundation for a stronger bank and paves the way for the implementation of a comprehensive digitalisation strategy.

(2) Remediation Plan

This remediation plan envisages a full review and update of all customer files, the revamp of the Bank's risk appetite framework and its strategic planning process. The Bank has adopted industry best practice and chosen a risk based approach focusing efforts on potential risk.

The Bank registered a significant increase in administration expenses during the year relating primarily to the transformation programme and costs incurred ancillary with the change to the Bank's core IT system. The Bank is also working to instil a robust risk culture throughout the organisation, from the Board of Directors downwards.

The Parent Company

Bank of Valletta p.l.c. is licensed to carry out the business of banking and investment services in terms of the Banking Act,1994 (Chapter 371, Laws of Malta) and the Investment Services Act,1994 (Chapter 370, Laws of Malta). The Bank is an enrolled tied insurance intermediary of MAPFRE MSV Life p.l.c. under the Insurance Intermediaries Act, 2006 (Chapter 487, Laws of Malta).

The Bank offers the entire range of retail banking services as well as the sale of financial products such as units in collective investment schemes. The Bank also offers investment banking services, including underwriting and management of Initial Public Offerings (IPOs).

The Subsidiaries

BOV AM provides management services for collective investment schemes and portfolio management services for institutional

Directors' report as at 31 December 2019 (continued)

clients. BOV AM is a fully owned subsidiary of the Bank and has three regulatory functions: Asset Management, Risk Management and Compliance.

BOV FS is also a fully owned subsidiary of the Bank and is recognised as a fund administrator and licensed as a Company Services Provider by the Malta Financial Services Authority. BOV FS provides a comprehensive suite of services to fund managers and fund promoters, as well as a full suite of fund administration including fund accounting, shareholder registry services, regulatory reporting and corporate services.

Equity-Accounted Investees

MAPFRE MSV Life p.l.c. operates as a life assurance company licensed under the Insurance Business Act, 1998 (Chapter 403, Laws of Malta). MAPFRE Middlesea p.l.c. is engaged in the business of insurance, including group life assurance.

Strategic Initiatives of the Bank

During FY 2019, Bank of Valletta's strategy centred round the Vision 2020+, namely that of *"Making Bank of Valletta a safer and stronger bank for today and the future".*

This strategy was thus moulded into six strategic pillars:

1. Strong financial fundamentals to ensure long term stability and sustainability;
2. A Corporate Ethos based on integrity, fairness and transparency;
3. A business model based on prudence, sound governance and a secure and safe infrastructure;
4. A sustainable and equitable return to shareholders;
5. A superior customer experience based on customer centricity and on wider accessibility; and
6. Resourcing the organization for 2020 and beyond.

The Bank's strategy has been defined within the Risk Appetite Framework (RAF) approved by the Board during the year under review.

During the financial year under review, the Group has also continued with the restructuring of its business model, with the objective of lowering its risk profile through a de-risking programme aimed at turning Bank of Valletta into a lower risk and stronger Bank. The de-risking programme includes: (i) the winding down of certain business lines, namely the trusts and custody businesses; (ii) the re-dimensioning of other business lines notably the termination of thousands of customer relationships within the Bank's International Corporate Centre and International Personal Banking which no longer fit within the Bank's risk appetite; (iii) the revision of the Bank's risk appetite framework; (iv) the enhancement of risk policies such as the revision of the customer acceptance policy; and (v) comprehensive training programmes covering the entire organisation from the Board of Directors downwards.

Principal Risks and Uncertainties pursuant to Article 177 of the Companies Act, 1995 (Chapter 386, Laws of Malta)

The Directors are aware of the various risks faced by the Group as a result of its involvement in different business lines and operations. A number of measures are in place to ensure that such risks and uncertainties are maintained at acceptable levels and are in line with the Group's risk appetite and strategy of sustainable, long-term growth and profitability. In line with the Bank's Policy, the Risk Appetite Statement and Framework was reviewed and approved by the Board of Directors in December 2019. The document lays out the responsibilities of various stakeholders, including the Board of Directors and Senior Management, and establishes a number of qualitative and quantitative parameters for acceptable risk taking.

In line with the provisions of the Risk Appetite Statement and Framework, Senior Management is responsible for the day-to-day monitoring and control of risk taking, subject to the regular oversight of the Board of Directors through the Risk Management Committee. The overall structure is aimed at ensuring a sound risk culture supported by a performance management system that discourages excessive risk taking.

The key risks faced by the Group include credit risk, market risk, operational risk and liquidity risk. These, and other risks and uncertainties inherent in the business, require sound capital management to ensure adequacy against regulatory requirements and adverse events. With this in mind, the Group regularly sets out and reviews capital targets in line with actual and forecast business levels and monitors performance against such targets on a regular basis. A more detailed explanation of key risks and capital management is included within the Capital and Risk Management Report as well as Note 39 to the Financial Statements.

The Directors also recognize the fact that the Group may be subject to reputation and litigation risk as a result of its actions and operations. Conscious of the serious repercussions such risks may have on the Group's and the various stakeholders' wellbeing, both the Board of Directors and Senior Management exercise zero tolerance to conduct risk and aim to instil the highest levels of ethical behaviour through a number of appropriate policies, procedures and controls.

Operational Overview

A review of the business of the Group for the period ended 31 December 2019 and an indication of future developments are provided in the Chairman's Statement and the Chief Executive Officer's Commentary, which can be found in the front section of this Annual Report.

Directors' report as at 31 December 2019 (continued)

Dividends

The Directors propose a final gross dividend of €0.026 per share. The aggregate net dividend for the period is €0.017 per share, amounting to €10 million. The total dividend is analysed as follows:

	The Bank 2019 €
Gross	15,384,615
Tax at Source	5,384,615
Net	10,000,000

Board of Directors

The following Directors served on the Board during FY 2019:

Taddeo Scerri (Chairman)
Stephen Agius
Alan Attard (resigned on 1 January 2020)
Paul V Azzopardi (resigned 15 February 2020)
Miguel Borg
Diane Bugeja (appointed on 19 December 2019)
James Grech
Alfred Lupi
Mario Mallia (resigned on 27 December 2019)
Anita Mangion
Alfred Mifsud (appointed on 19 December 2019)
Antonio Piras
Joseph M Zrinzo (resigned on 1 September 2019)

Directors' Responsibilities

The Directors are required by the Companies Act, 1995 (Chapter 386, Laws of Malta) to prepare financial statements in accordance with International Financial Reporting Standards as adopted by the EU which give a true and fair view of the state of affairs of the Group and the Bank as at the end of the financial year and of the profit or loss of the Group and the Bank for the year then ended. In preparing the financial statements, the Directors should:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable; and
- prepare the financial statements on a going concern basis unless it is inappropriate to presume that the Group and the Bank will continue in business as a going concern.

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 the Bank, and which enable the Directors to ensure that the financial statements comply with the Banking Act, 1994 (Chapter 371, Laws of Malta) and the Companies Act, 1995 (Chapter 386, Laws of Malta) and with the requirements of Article 4 of the Regulation on the application of IFRS as adopted by the EU. This responsibility includes designing, implementing and maintaining such internal controls as the Directors determine necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error. The Directors are also responsible for safeguarding the assets of the Group and the Bank, and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

After reviewing the Group's plans for the coming financial years, the Directors are satisfied that at the time of approving these financial statements, it is appropriate to continue adopting the going concern basis in preparing these financial statements.

Auditors

A resolution to re-appoint KPMG Malta jointly with KPMG LLP (United Kingdom) as statutory auditors of the Bank will be proposed at the forthcoming Annual General Meeting (AGM). KPMG Malta and KPMG LLP (United Kingdom) have expressed their willingness to remain in office.

Going concern – Listing Rule 5.62

The financial statements are prepared on a going concern basis. The Directors regard that pursuant to Listing Rule 5.62, this is appropriate, after due consideration of the Bank's profitability, liquidity, the statement of financial position, capital adequacy and solvency. Specifically, the Directors have prepared financial and capital plans for the next five years which show that the Bank is in a position to continue operating as a going concern for the foreseeable future. These plans take into account risks facing the Bank, including but not limited to, the potential crystallisation of known contingent liabilities.

Directors' report as at 31 December 2019 (continued)

Information Pursuant to Listing Rule 5.64

Authorised Share Capital

The Bank has an authorised share capital of €1,000 million divided into 1,000 million ordinary shares with a nominal value of €1.00 each.

Issued Share Capital

The issued shares of the Bank consist of one class of ordinary shares with equal voting rights attached.

During the Annual General meeting held on 9 May 2019, the shareholders approved a bonus share issue of 53,077,206 fully paid ordinary shares of a nominal value of €1.00 per share, representing 1 bonus share for every 10 shares held, thereby increasing the Bank's issued share capital from the previous 530,772,064 shares to 583,849,270 shares of €1.00 each share fully paid up, resulting in a paid up capital of €583,849,270.

Shareholding Structure

Clause 4.3 of the Bank's Memorandum of Association provides that, with the exception of existing large shareholders, presently the Government of Malta and UniCredit S.p.A., no person may at any time, whether directly or indirectly and in any manner whatsoever, acquire such number of shares in the Bank, as would in aggregate be in excess of 5% of the issued share capital of the Bank.

As at 31 December 2019, Malta Government Investments Limited had a shareholding in the Bank of 0.48% and National Development and Social Fund (NDSF) had a shareholding in the Bank of 2.88%. Both entities are fully owned by the Government.

Any shareholder holding in excess of 50% of the issued share capital of the Bank or if no such shareholder exists, the shareholder holding the highest number of shares not being less than 25% of the issued share capital, may appoint the Chairman. Qualifying Shareholders with 10% or more of the shares in issue are entitled to recommend one Director for every 10% holding.

The Directors confirm that as at 31 December 2019, shareholding in excess of 5% of the issued share capital of the Bank was held directly by:

Government of Malta	25.0%
UniCredit S.p.A.	10.2%

Appointment of Directors

The rules governing the appointment and replacement of the Bank's Directors are contained in Articles 24 to 31 of the Bank's Articles of Association. More details on the appointment and rotation process of Directors is found under the Corporate Governance Statement of Compliance, under principle 3.

An extraordinary resolution approved by the shareholders in general meeting is required to amend the Memorandum and Articles of Association.

Powers of Directors

The Board of Directors has the power to transact all business of whatever nature, not expressly reserved by the Memorandum and Articles of Association of the Bank, to be exercised by the Bank in general meeting or by any provisions contained in any provision contained in any applicable laws.

The shareholders in general meeting authorised the Board to exercise during the Prescribed Period, all the powers of the Bank to issue and allot shares up to an aggregate nominal amount equal to the Prescribed Amount. The Prescribed Period refers to a term of five years approved during an Extraordinary General Meeting held on 27 July 2017 and which term expires on the 26 July 2022. This authority is renewable for further periods of five years each.

Directors' Service Contracts

The Directors have service contracts with the Bank. More information on the Directors' service contracts can be found under the Remuneration Report.

Collective Agreements

The relative Collective Agreements regulate the compensation payable to employees in case of resignation, redundancy or termination of employment for other reasons.

It is hereby declared that as at 31 December 2019, information required under Listing Rules 5.64.5, 5.64.7 and 5.64.10 was not applicable to the Bank.

Directors' report as at 31 December 2019 (continued)

Amendments to the Memorandum of Association

The Bank's Memorandum of Association was revised during the period under review and approved by the Shareholders during the Annual General Meeting held on 9 May 2019.

1. Amendments to clauses 4.5 and 4.6 of the Memorandum of Association:

Pursuant to this revision to the Memorandum of Association, a large shareholder (namely any person who currently holds more than 5% of the Bank's issued share capital) being a bank, credit institution, financial institution, insurance company or licensed collective investment scheme, or licenced retirement fund shall be able to sell its large shareholding, namely any holding of more than 5% of the Bank's issued share capital, to any of the following institutions:

- banks
- credit institutions
- financial institutions
- insurance companies
- licensed collective investment schemes or
- licensed retirement funds

Pursuant to this amendment "licensed retirement funds" were included in the list of eligible institutions which are now able to acquire and hold a large shareholding in the Bank. This provision therefore allowed large shareholders who wished to dispose of their large shareholding, a broader segment in the market to whom they could sell and dispose of their shares as one holding, whilst at the time ensuring that only institutions which are subject to regulation and licensing could be the holders of a large shareholding in the Bank.

2. Amendments to Article 7 of the Articles of Association:

A new Article 7.3 was introduced to clarify and regulate the current practical state of affairs when shares issued by the Bank were held subject to usufruct. The amendment did not result in any changes from a practical point of view, but it was merely intended to formalise the process currently in place.

3. The inclusion of a new Article 27A of the Articles of Association and further amendments to the Articles of Association in connection with the insertion of Article 27A:

The inclusion of the new Article 27A addressed situations where, notwithstanding the efforts that may be made by the Nominations and Governance Committee to ensure that the Board of Directors of the Company had the necessary mix of skills and experience, there could arise situations where those efforts may not yield the appropriate mix and combination of skills; or where the regulator may require certain skills which may not be present on the Board.

In such situations, the Board can now react to ensure that the composition of the Board fulfils its ultimate aim. Accordingly, this new Article 27A empowered the Board of Directors to co-opt up to a maximum additional two Non-Executive Directors to sit on the Board of Directors of the Company (only in those instances where the nine Non-Executive Director positions were already filled, but the then current Board complement still does not have the composition required by regulation or in the opinion of the Nominations and Governance Committee, the Board still does not have the appropriate mix of collective skills, knowledge and experience).

Such co-opted Non-Executive Directors would be appointed for a three (3) year term which shall not be subject to rotation but shall be eligible for re-appointment.

A new provision regulating retiring directors was also introduced, specifying that Non-Executive Directors who reached seventy-five (75) years of age will no longer remain eligible for re-appointment or re-election once their term of office has expired.

Information pursuant to Listing Rule 5.70.1

There were no material contracts to which the Bank, or any one of its subsidiaries, was a party and in which anyone of the Bank's Directors was directly or indirectly interested.

Declaration pursuant to Investment Services Rule R4-5.3.5

Pursuant to the Malta Financial Services Authority (MFSA) Investment Services Rule R4-5.3.5 for Investment Services Providers and Standard Licence Conditions (SLCs) SLC 2.30, it is hereby declared that during the reporting period, there were no breaches of the MFSA Investment Services Rules, Standard Licence Conditions or other regulatory requirements.

Whistleblowing

The Bank has in place a Whistleblowing Policy aimed to encourage reporting of improper practices and suspected wrongdoing in a controlled manner which safeguards the confidentiality of the whistleblower. The nature of the disclosures made through the Whistleblowing process are reported to the Audit Committee.

Directors' report as at 31 December 2019 (continued)

Information pursuant to the Sixth Schedule of the Companies Act, 1995 (Chapter 386, Laws of Malta)

Branches, Agencies and Centres

The Bank has the following Branches, Agencies and Centres around Malta and Gozo:

- 36 Branches offering both deposit taking and lending services
- 5 Business Centres
- 6 Investment Centres
- 4 Agencies offering deposit services only
- 1 Sub-Agency/Satellite Branch offering both deposit and lending services which reports to the "parent" branch

Besides the above local Branches, the Bank has four Representative Offices, one in Milan which was opened in 1996, one in Libya (temporarily closed) which was opened in 2002, one in Brussels, opened in 2012 and another one in London which was opened in 2018.

Research and Development

In light of the business sector in which it operates, the Bank does not consider research and development as a main area of activity.

Events occurring after the end of the accounting period

Appointment of new Chief Executive Officer (CEO) - With effect from 1 January 2020, the Bank has a new CEO, Mr Rick Hunkin, who replaced Mr Mario Mallia, the Bank's former Chief Executive Officer. More information on the new CEO is found under section (xvii).

Non-Financial Disclosures

The following disclosures are made pursuant to Directive 2014/95/EU:

1. <u>Business Model</u>

Bank of Valletta operates a business model driven retail funding strategy which has over the years provided a highly stable funding source to support the Bank's key business services to both personal and business customers.

The Bank's suite of products and services has been developed in a way to ensure that the Bank's customers are provided with a comprehensive range of solutions to meet their requirements as they progress through the different stages of their lifecycle. On the distribution side, the Bank's strong branch network plays an important role in this model and remains a critical touchpoint for the Bank's customers. In addition, the branch network has over the years been complemented with the introduction of a number of Investment Centres and a specialised Wealth Management Unit in order to provide our customers with convenient, professional and dedicated investment management and advisory services. On the other hand, through the Bank's Corporate Centre, as well as a number of Business Centres, the Bank attends to the bespoke financing requirements of its business customers.

Despite the importance of the Bank's physical customer touchpoints, the onset of technological developments has also driven the Bank to invest and deploy a number of key digital channels to strengthen the accessibility of its products and services to its customers. In fact, the introduction of internet banking, mobile banking and the newly launched BOV Pay portal, position the Bank at the very centre of its clients' financial wellbeing where these touchpoints have today become the preferred channels through which customers prefer to transact.

2. <u>Environmental Friendly Measures</u>

Notwithstanding that the Bank does not pursue a formal policy relating to environmental measures, various environmental related initiatives were taken by the Bank during the reporting year. These initiatives are part of the Bank's ongoing commitment to promote Green practices within the community and determination to decrease the carbon footprint led to various Green Initiatives and included installations of modern, energy efficient Heating Ventilation Air Conditioning (HVAC) systems, continuous disinfection and cleaning of ducting systems at various branches, replacement of lights to energy efficient Light Emitting Diodes (LED) light fittings, increased use of hybrid vehicles and installations of PV Cells which generated electrical energy and which resulted in lower electricity consumption costs. The Bank also participated in the annual global initiative Earth Hour by switching off the BOV Centre and Legal Office façade lights during the hour indicated, with the aim of reducing electricity consumption. The Bank also participated in the European Week for Waste Reduction. Waste Separation and Recycling of Electronic Waste was ongoing throughout the reporting period.

3. <u>Human Resources Matters</u>

The Bank is covered by a Collective Agreement which binds the relationship between the organisation and its employees. The prevailing Collective Agreement includes a number of Family Friendly measures ensuring employee matters are looked after, including but not limited to Flexible Work Arrangements, Adoption/Fostering Leave, Bereavement Leave, Community Work Leave, Employee Welfare and an Employee Wellness Allowance. Moreover, the Bank has in place a number of policies ensuring respect for human rights including

Directors' report as at 31 December 2019 (continued)

a Bullying Policy, a Sexual Harassment Policy, a Grievance Policy, Health and Safety Policy, a Code of Ethics and an Equality Policy. Related to the latter, the Bank has been awarded the Equality Mark, in recognition of the Bank's non-discriminatory approach to its workforce. Moreover, such policies ensure that employees have clear guidelines to follow if they feel they are not being fairly treated. No cases of discrimination were reported during 2019.

Employee Assistance Programme – This programme assists employees resolve personal or work related problems that hinder their ability to carry out responsibilities at work. The Bank, in conjunction with the Richmond Foundation, also offers its staff members free Mental Health Care related services. The Bank receives annual feedback from Richmond Foundation regarding the number of employees making use of these services, which information confirms that employees are well informed about these services and make use thereof when necessary.

4. Anti-Corruption and Bribery Matters

The Bank reiterates its zero tolerance stance towards financial crime, specifically including bribery and corruption. As part of its efforts to continuously increase controls in this area, thereby minimising risks to stakeholders, the economy and society in general, the Bank has during FY 2019 dedicated specific resources within its anti-financial crime function to control and mitigate bribery and corruption risk. Resources with experience in the area have also been recruited. The Bank has also approved a dedicated anti-bribery and corruption policy and has commenced work on procedures for its implementation, backed by a bank-wide training programme.

5. Identification and Management of Principle Risks

In conducting its day-to-day business activities, the Bank is exposed to different risk types. The sound management and control of such risks is important to ensure that the relative probability of risk event materialization is minimized to the greatest extent possible in the interest of institutional stakeholders.

Risk management and control is practised under the following configuration:

i) Top-level corporate governance: Board of Directors, various Board Committees such as the Risk Management Committee, Management Board, and other management committees such as the Asset and Liability Management Committee (ALCO);

ii) First line: revenue-generating business units – such ingrain frontline risk management internal control measures;

iii) Second line: this comprises various second-tier risk control and oversight functions such as Risk Management, Compliance, Anti-Financial Crime, Financial Control, and other backoffice support functions (e.g. quality control);

iv) Third line: independent assurance and constructive challenge by the Group Internal Audit;

The main risk types are outlined hereunder:

a) Credit risk: the risk of loss arising from default or credit quality deterioration of a customer or other counterparty to whom the Bank has either directly provided credit or in respect of whom it has assumed a contractual obligation.

   This risk is managed and controlled in various ways such as through the regular review of risk-averse credit policies, credit scoring systems, an internal risk rating system supplemented by an Early Warning System, a forward-looking expected loss model for quantifying provisions compliant with the IFRS 9 accounting regime, stress testing relating to credit risk, and various other measures. Examples of the latter include a four-eye approach in the sanctioning of credit facilities of significant magnitude, policies relating to forbearance and nonperforming loans, credit risk-related Key Risk Indicators in the Bank's Risk Appetite Framework, internal limits relating to single-name and sectoral concentration risk, and various other mitigants. Other developments are in the pipeline such as a risk-based pricing model.

b) Operational risk: The Group defines operational risk (OR), in line with the Basel framework, as the risk of losses arising from defects or failures in its internal processes, people, systems or external events, covering risk categories such as fraud, technological, cyber-risk, legal and conduct risk.

   Operational risk is inherent in all products, activities, processes and systems and is generated in all business and support areas. For this reason, all employees are responsible for managing and controlling the operational risks generated by their activities. The Group's goal in terms of operational risk management and control is focused on identifying, evaluating, and mitigating sources of risk, regardless of whether they have materialized or not. The analysis of exposure to operational risk helps determine the actions which should be taken to minimize the frequency and impact.

   In 2019, the Group's overall operational risk appetite was revised to low; this aims to protect the Bank's franchise, to support its strategic objectives, and ensure availability of services to support the local economy.

   As part of the strengthening of the Operational Risk Management Framework, the Bank has embarked, and is in advanced stage of deploying a dedicated Operational Risks IT solution which will enable the Group obtain a fuller and more precise view of risks in a timely manner, through the integration of risk and control assessment, risk event management, and metrics using a common set of risk taxonomy.

Directors' report as at 31 December 2019 (continued)

c) Market risk: in the main, the risk incurred as a result of changes in market factors that affect the value of positions mainly in the investment portfolio of securities. The Bank has its own Interest Rate Risk in the Banking Book (IRRBB) model to quantify risk arising under different shocks as prescribed by applicable regulatory dicta which is premised on two approaches: the Economic Value of Equity approach and the Earnings Based approach. A robust and prudent Treasury Management Policy ensures that responsible and well-informed risk-taking is practised by the Bank's Treasury function; such is complimented by independent arms-length analysis conducted by the Risk Management Department and submitted to ALCO and the Risk Management Committee from time to time. Inter alia, other important processes include the analysis of counterparty credit risk, credit valuation adjustment, and the development of a methodology to quantify equity risk on the part of the investment portfolio which is reported in the audited accounts at fair value (i.e. on a mark-to-market basis).

d) Liquidity risk: the risk that the BOV Group does not have the liquid financial resources to meet its obligations when they fall due, or can only obtain them at an unreasonably high cost.

Various liquidity risk management tools are used such maturity ladder gap analysis and the regular updating of key metrics. Inter alia, these include the Liquidity Coverage Ratio, the Net Stable Funding Ratio, the Loans-to-Deposit Ratio, the Maturity Transformation Metric and various others. Furthermore, over and above the Internal Liquidity Adequacy Assessment Process (ILAAP) which is thoroughly reviewed every year, the Bank conducts robust stress testing on liquidity at least on a semi-annual basis and which are supplemented by sensitivity analysis exercises from time to time. Other important elements with the liquidity risk management toolkit include the Contingency Funding Plan which is regularly updated and tested by means of simulation exercise and a prudent Liquidity Risk Policy which is also updated periodically.

e) Solvency risk: the risk of having insufficient capital to absorb unexpected losses and/or exceptional losses nascent from stress events. BOV has a regularly updated Capital Plan which is a key input in the institution's Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP is revised annually and ensures that there is enough capital not only to meet Pillar 1 risks – credit, operational, and market – but also other Pillar 2 risks such as IRRBB, concentration risk, equity risk, and others. Stress testing gauges the stressed capital position in terms of such key metrics as the stressed Common Equity Tier 1 capital and the stressed total Capital Adequacy Ratio; as a minimum this is done on a semi-annual basis. The Recovery Plan and the Resolution Plan respectively take even more adverse scenarios than the ICAAP as they are formulated under a gone concern perspective; such are also updated at least annually. Moreover, a proactive approach is practised relating to medium-term obligations nascent from the Minimum Requirement for own funds and Eligible Liabilities (MREL).

f) Regulatory compliance risk: the risk of non-compliance with legal and regulatory requirements as well as supervisory expectations which may result in administrative or disciplinary sanctions, or of material financial loss, due to failure to comply with the provisions governing the Group's activities. By ensuring that these rules are observed, the Group works to protect its customers, shareholders, counterparties and employees.

This is conducted in alignment with the Group strategy and Vision 2020+, which sets the Group's vision as operating a business model based on prudence and sound governance, and to continue strengthening the corporate ethos based on integrity, fairness and transparency.

(i) Financial Crime Compliance

The BOV group is committed to fight against financial crime and to set up and implement a programme to identify, understand and mitigate the financial crime risk. The financial crime risk encompasses:
a) money laundering and terrorist financing,
b) breaches of sanctions, and
c) bribery and corruption.

The Bank maintains a thorough AFC risk assessment in order to identify, understand, manage and mitigate inherent AFC risks. Risk mitigations measures are designed and implemented to control adequately and effectively those inherent risks. Inherent and residual risks are managed in line with the Bank's risk appetite.

BOV is always committed to be in compliance with all applicable laws and regulations regarding the fight against financial crime. The results of recommendations, provisions and sanctions by regulators for past shortcomings, together with the recommendations of in-house and external experts, form the basis for the current transformation programme aimed at leading BOV towards the highest industry standards of financial crime compliance.

(ii) Regulatory compliance

Complying with the regulatory obligations is not only the responsibility of the Compliance Department, but of all Group employees who must demonstrate compliance and integrity in their daily tasks. The management of compliance risks is based on a shared responsibility binding all business functions, the subsidiary companies and employees with in the internal control functions of the Group. All functions must integrate compliance with laws and regulations, the rules of good professional conduct and the Group's internal rules into their daily work. This consists of two main pillars - advisory and supervisory functions:

a) Advisory function – monitor regulatory developments, analyse the legislations that impact the Group, communicate the regulatory requirements to the impacted functions and provide guidance during implementation, and
b) Supervisory function - carry - out independent product and function oversight reviews on a risk-based compliance monitoring plan.

Directors' report as at 31 December 2019 (continued)

Group Compliance is an independent risk control function headed by the Group Chief Compliance Officer and constitutes the second line of defence for compliance risk. The Group Chief Compliance Officer is the designated Group Conflicts Officer. The Group Chief Compliance Officer reports to the Chief Executive Officer and has a direct escalation line to the Compliance and Crime Prevention Committee, which is a Board Committee.

Additionally, the Bank has a dedicated Money Laundering Reporting Officer and a Group Data Protection Officer.

g) Climate risk: The Bank is well aware of its environmental obligations as a responsible corporate citizen. Climate-change related risk drivers – whether physical or transition-led – are expected to act as factors that could aggravate the existing risks in the medium and long term. In a May 2019 European Central Bank publication it was stated that: "From a risk-management perspective, the lack of clear common definitions and data makes it difficult to measure the impact these risks have on individual banks, let alone compare them". Whilst it is still early days in this risk field, the Bank is not resting on its laurels. The publications of the Network for Greening the Financial System (NGFS) are on the institutional radar; so are those issued by the European Banking Authority (EBA) such as the press release issued in December 2019 entitled "EBA pushes for early action on sustainable finance". Taking a proactive approach, the Risk Management Department (RMD) reorganization which was in the pipeline as at reporting date, had already planned that a specific RMD unit will, with effect from 2020 be entrusted with proposing, formalizing, and developing the Bank's risk response to this emerging risk, one that is expected to gain importance in the coming years.

h) Key Performance Indicators (KPIs)

The Group has in place a set of key performance indicators (KPIs) that are quantifiable measures which ensure that material risks are kept within defined thresholds as formalized in the Risk Appetite Framework. A selection of key metrics is tabulated hereunder.

	CET 1	19.51%
Solvency	CAR	23.07%
	LCR	514.60%
Liquidity	NSFR	159.54%
Profitability	ROE*	6.2%

**Post Tax*

Various non-financial KPIs enable the Directors also to evaluate the risk profile exhibited on other risks such as reputational, compliance, anti-financial crime, operational, and risk culture.

The KPIs are reported on a regular basis in the Risk Dashboard which includes targets set to facilitate comparison between progress achieved towards attainment of strategic objectives and the actual risk profile exhibited viz.: 'within target', 'within tolerance', 'limit'.

Other than as disclosed in note 33 to the financial statements, there were no subsequent events which would have otherwise warranted an adjustment to or disclosure in these financial statements.

6. COVID-19 Outbreak

The events subsequent to the reporting date, notably the COVID-19 outbreak, will most likely have a substantial negative impact on both global and local economies. The existing capital buffers, together with measures made available by the regulatory authorities provide significant mitigation against the additional challenges of this unprecedented event. An adverse influence on 2020 performance is highly probable but a clear determination of the overall financial impact cannot be made at this early stage. There are uncertainties on both the duration of the crisis and the extent of the impact on the local economy as well as, the scale and effectiveness of mitigating measures provided by the local and EU authorities. The directors do not consider that any adjustments are required to the financial statements at this stage. The Bank has already taken steps and intends to launch further initiatives to continue to support the local economy as well as to help safeguard the well-being of its employees and its customers.

Statement by the Directors pursuant to Listing Rule 5.68

We, the undersigned, declare that to the best of our knowledge, the financial statements prepared in accordance with the applicable accounting standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Bank and its subsidiaries included in the consolidation taken as a whole, and that this report includes a fair review of the performance of the business and the position of the Bank and its subsidiaries included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Approved by the Board of Directors and authorised for issue on 18 March 2020 and signed on its behalf by:

Taddeo Scerri
Chairman

Mr Rick Hunkin
Director and Chief Executive Officer

Capital & risk management report 31 December 2019

Pillar 3 Disclosures

Basis for preparation

The Basel III capital adequacy framework consists of three complementary pillars: Pillar 1 provides a framework for measuring minimum capital requirements for the credit, market and operational risks faced by banks; Pillar 2 establishes a system of supervisory review, aimed at improving banks' internal risk management and capital adequacy assessment in line with their risk profile; Pillar 3 is intended to enhance market discipline and requires banks to publish a range of disclosures aimed at providing further insight on the capital structure, adequacy and risk management practices.

This Capital and Risk Management Report provides a comprehensive overview of the risk profile of the Bank of Valletta Group (hereinafter referred as 'BOV' or 'the Group') in accordance with disclosure requirements under Part Eight of EU Regulation No. 575/2013 Capital Requirements Regulation 'CRR'. During 2017, the EBA published guidelines on disclosure requirements which aim to improve the comparability and consistency of institution's Pillar 3 disclosures. The Basel Committee on Banking Supervision has published the updated Pillar 3 disclosures requirements in December 2018 which complete the Pillar 3 framework, aiming to promote market discipline through regulatory disclosure requirements.

The Bank publishes these disclosures on an annual basis as part of the Annual Report in accordance with Article 433 of the CRR. A reference has been added in cases where the information addressing Pillar 3 requirements is included in other parts of the Annual Report.

This Capital and Risk Management Report is not subject to external audit, except where a disclosure is equivalent to that made in the Financial Statements which adhere to International Financial Reporting Standards (IFRS) as adopted by the EU. Nonetheless, this Capital and Risk Management Report has been approved by the Bank's Audit Committee and the Board of Directors (BoD). The Bank is satisfied that internal verification procedures ensure that these Additional Regulatory Disclosures are presented fairly.

Section 1: BOV Risk Management

It is the core function of every bank to take risks consciously with the aim of managing them to achieve a return. The Group is consistently working towards achieving the required balance between profitability and growth against appropriate risk levels.

The Group's Risk Appetite Framework (RAF) articulates the types and level of risk, both quantitatively and qualitatively, that the Group is willing to take in pursuit of the strategic objectives. The RAF ensures that all material risks are kept within appropriate limits, both to safeguard the financial and non-financial sustainability of the Group, as well as to meet the needs of the stakeholders (including clients, shareholders and regulators). The risk appetite is embedded across the Group through a number of policies, ensuring that the risk profile remains within the Group's risk appetite and capacity to bear risk and outlines the acceptable levels of risk, as well as the controls and mitigants for achieving and maintaining the set levels. Any breaches or early warning signals are escalated to the CRO and/or CEO and further to the Risk Committee and/or the BoD as applicable, for immediate action. To maintain an environment where staff are comfortable raising concerns, the Bank also has a whistleblowing policy and the respective procedures in place. The Group's RAF was reviewed and approved by the BoD in December 2019.

Within this context, the Bank's organisational structure is built upon a framework that promotes a transparent and efficient, enterprise-wide risk management culture wherein the behaviour, attitude and decisions reflect risk awareness and mitigation across the Group. The Group strives to strengthen and build upon the existent risk values so as to minimise risk exposure to insignificant levels. This is supported by targeted training, specific internal policies, as well as the Group's stance on risk culture for all employees. One of the high priority objectives of the second line of defence is to instil a cultural awareness which helps to establish a robust risk management and control process. This is done through risk awareness and compliance training for all employees, various workshops and the continuous sharing of information between different departments and business lines.

The Bank adopts different layers of defence and segregates duties to reinforce the currently implemented risk control mechanisms. Such approach is embraced through the application of the three lines of defence model. The first line of defence is executed by the functions that own and manage risks, namely the business units, who are accountable to appropriately identify, measure, address and report the risks assumed. The second line is executed by the functions that oversee risks, namely Risk Management, Compliance, Anti-Financial Crime and Legal Departments. These are responsible for the effective control of risks and to ensure that they are managed in accordance with the Group's risk appetite. The third line of defence is executed by the Group Internal Audit, which is the function that provides independent assurance to the Board, relative to the effectiveness of the first and second line of defence functions. This means that responsibility for risk management resides at all levels within the Bank. The risk governance framework enhances the understanding of existing and emerging risks through cooperation between all three lines and ensures the effective execution of risk management controls. The collective effort across different lines of defence ensures that the Group's risk culture is recognised as an essential factor to achieve compliance and strategic objectives.

The Group's strategy ensures that the Group maintains its position as a strong stable institution, providing sustainable and equitable return to shareholders, whilst delivering a superior customer experience and developing BOV into the most accessible banks. The Bank, following the recruitment of a new CEO, will launch a new strategic plan during 2020.

The Board of Directors is responsible for the effectiveness of the risk governance framework and ensures that satisfactory risk policies and governance for controlling the Bank's risk exposure are implemented. The Board reviews on a regular basis the status of risk management issues to assess the management and monitoring of the Bank's risks.

Capital & risk management report 31 December 2019 (continued)

The Group's attitude towards risk is expressed through the risk appetite, which sets targets for the different types and levels of risk that the Group may expose itself to through its business activities. The Group's Risk Appetite is based on the guiding principles, high-level directional statements providing the overall structure of the RAF, reflected in the indicators, risk category and business line statements. The guiding principles are: i) proactively meeting all the regulatory standards, ii) adopt a low risk appetite for non-core business lines and pursue a sustainable growth strategy on core business lines, iii) safeguarding the Bank's reputation and brand, iv) ensuring quality and availability of services to support the Maltese economy and v) generate sustainable earnings to create long term shareholders value.

The Group's overall risk profile should be kept low, with the Group ensuring that it remains well capitalized at all times in relation to the risks it is exposed to, and holds liquid assets so that it can meet its payment commitments, including in situations of financial stress in the short and long term. As at the end of December 2019, the Management Board declares that the Group's risk profile remained well within the Group's risk appetite and tolerance limits established by the Board.

It is the Board's assessment that the Bank has in place adequate risk management arrangements in relation to the overall risk profile and business.

Risk Governance

The Group uses the three lines of defence approach to risk governance. The risk function is led by the Chief Risk Officer, who is a member of the Executive Committee and an Executive Director.

The Executive Committee and the Board of Directors approved changes to the organisation chart to make sure that the second line is adequate in both personnel and proficiency to support the assessment and monitoring of risk at all levels, while helping the front line (i.e. first line of defence) improve its capability to identify and control risk at the source. The risk function is made up of three distinct but complementary departments: Operational Risk Management, Credit Risk Management and Financial Risk Management. Moreover, the Bank established three different offices with a direct reporting line to the CRO: Enterprise Risk Management, Model Validation and Supervisory Affairs. Legal Office and Credit Risk Sanctioning Department report directly to the CRO in line with the previous organisation chart. It was decided that Anti-Financial Crime and MLRO shift to Compliance in order to increase synergies. Debt Management Department now also reports to the CRO.

The following give a brief description of the main functions of the second line of defence.

- *Operational Risk Management Department.* This department is responsible for the implementation of the Operational Risk Framework. The Framework compromises the following elements: Risk Appetite and Key Risk Indicators, Risk and Control Self-Assessments (RCSA), Events and Losses, Action Management and Scenario Analysis. In addition, the Department has an information security function which analyses and communicates information security risks and evaluates their potential impact on the business processes.

- *Credit Risk Management Department.* The objective is to safeguard the soundness of the loan portfolio, to ensure sustainable credit growth and to enable a diversified portfolio aligned with the Bank's risk appetite. The Department is responsible for the development and maintenance of the Credit Policy, which sets out the Bank's core principles governing the provision of credit. It is also responsible for measuring and managing asset quality in line with the prevailing banking rules.

- *Financial Risk Management Department.* The Department is responsible for the management of risk reporting, risk data governance and portfolio risk management. It is responsible for internal stress tests and is also actively involved in the compilation of the Internal Capital Adequacy Assessment Programme (ICAAP), Internal Liquidity Adequacy Assessment Programme (ILAAP) and the Recovery Plan.

- *Enterprise Risk Management.* The objective of this Office is to be the direct link between the first and the second line of defence by increasing the awareness of risk responsibilities and cultivating a risk culture so that risk can be owned and managed within each business unit. It is also responsible for maintaining the Risk Appetite Framework and ensuring that it is adequately communicated across the Group. It is also responsible for producing dashboard reporting to the Executive Committee and Board.

- *Model Validation Office.* The Office is responsible to validate all models used by the Group.

- *Supervisory Affairs Office.* The Office is responsible to maintain and sustain a strong relationship with the Joint Supervisory Team. It is responsible for the coordination, compilation and submission of regulatory documents and information. The Office liaise with senior management and other different departments to follow up on actions as required by the regulator.

The *Credit Risk Sanctioning Department* is responsible for conducting independent financial and risk analysis of lending and investment proposals that fall under the dual-voting system and to ensure that these are within the risk appetite communicated by the BoD.

The *Legal Services Department* ensures that the Bank's interests are duly safeguarded and that the Bank is kept duly updated with all legislative developments. This enables the Bank to map the way forward and be legally prepared even in terms of the Bank's processes.

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The *Debt Management Department* is responsible for the management of debt recovery.

The *Compliance Department* is responsible to ensure that the Group operates in line with regulatory requirements. The Compliance Department monitors regulatory developments and assesses the impact and applicability of rules and regulations. It also carries out specific and thematic reviews on various functions, while ensuring that the Group has effective policies for mitigating reputational and conduct risk. It provides regular training on regulatory obligations and requirements emanating from internal policies and procedures. It reports to the Chief Compliance Officer.

The *Anti-Financial Crime Department* is a second line of defence function and supports the frontline employees by providing guidance and assistance in the development and implementation of policies, procedures, systems and controls to counteract financial crime, money laundering, counter terrorism financing, bribery and corruption, and fraud. The Department is also responsible to ensure that the Bank is compliant with International Sanctions. The Money Laundering Reporting Officer is the Bank's liaison with the Financial Intelligence Analysis Unit. Both units report to the Chief Compliance Officer.

Key Risks

The Group has specific risk appetite statements for all of its material risks, which are reviewed on a regular basis and approved by the BoD. The main categories of risk to which the Group is exposed to in relation to its business model are shown in the following table. Further details on how these risks are identified and managed at different levels of the organisation can be found in the relevant sections as highlighted below.

Capital Adequacy Management	The ability to hold sufficient capital to meet both regulatory requirements and shareholder expectations. *[Notes to the Financial statements note 39.7; Pillar 3 disclosures Section 3, 4 and 5]*
Credit Risk	The risk of financial loss, which the Bank may incur, if a customer or counterparty fails to meet its obligations in accordance with agreed terms. *[Notes to the Financial statement note 39.2; Pillar 3 disclosures Section 6]*
Market Risk	The risk that the fair value or future cash flows will fluctuate because of changes in market prices. Given that the Group does not operate a Trading book, market risk is limited to interest rate risk, currency risk and other price risk. *[Notes to the Financial statements note 39.4; Pillar 3 disclosures Section 7]*
Non-Financial Risks	The risk of losses resulting from inadequate or failed processes, people and internal systems, or from external events. This includes risks related to compliance failures, misconduct, technology or operational losses and climate risk. *[Pillar 3 disclosures Section 8]*
Liquidity Risk	The risk of incurring losses due to the inability of meeting obligations as they become due and can be categorised into two types: • Funding liquidity risk which results when the Group cannot fulfil its obligations due to being unable to obtain new funding. • Market liquidity risk which occurs when the Group is unable to sell or transform its liquidity buffers into cash without incurring significant losses. *[Notes to the Financial statements note 39.3; Pillar 3 disclosures Section 10]*

The BoD, Management Board (MB), the Risk Management Committee and various other committees are presented with risk reports on a regular basis to ensure adequate risk management, enabling them to continuously monitor and manage risks. These reports provide insight on particular risks, highlighting the current position, compliance with set limits and sensitivity analysis. Key risk indicators included in the Risk Appetite Statement are monitored by the BoD on a regular basis to ensure adherence to risk appetite limits. The BoD receives risk reports, including the ICAAP and ILAAP documents which provide a holistic review of the Group's capital and liquidity adequacy.

Section 2: Scope of application of the regulatory framework

The accounting framework used in preparing the consolidation of the Group's financial statements is IFRS as adopted by the EU, whereas the prudential consolidation in the statement of capital is based on CRR 575/2013. Thus consolidation under prudential requirements may differ from consolidation under the accounting standards depending on the purpose for which they are being calculated.

The tables hereunder provide a breakdown of the relationship between the different categories of the financial statements and the risk categories in accordance with prudential requirements and highlight the main differences between the carrying amounts appearing on the financial statements and the exposures for prudential purposes.

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Template 1: EU LI1 – Differences between accounting and regulatory scopes of consolidation and the mapping of financial statement categories with regulatory risk categories

	a	b	c	d	e	f	g
			Carrying values of items				
€ millions	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	Subject to the credit risk framework	Subject to the CCR framework	Subject to the securitisation framework	Subject to the market risk framework	Not subject to capital requirements or subject to deduction from capital
ASSETS	**The Group**	**The Group**					
Balances with Central Bank of Malta, treasury bills and cash	3,669.6	3,669.6	3,669.6			3.5	
Financial assets at fair value through profit or loss	205.1	205.1	203.9	1.3			0.2
Investments	3,071.2	3,071.2	3,071.2			687.8	0.3
Loans and advances to banks	501.7	501.7	501.7			309.1	
Loans and advances to customers at amortised cost	4,445.8	4,445.8	4,445.8			47.3	
Investments in equity-accounted investees	101.5	101.5	101.5				0.1
Investments in subsidiary companies	-	-	-				
Intangible assets	60.5	60.5	0.0				60.5
Property and equipment	126.2	126.2	126.2				
Current tax	15.2	15.2	15.2				
Deferred tax	76.0	76.0	155.5				
Assets held for realisation	10.1	10.1	10.1				
Other assets	42.6	42.6	42.6			0.1	
Prepayments and accrued income	5.1	5.1	5.1				
Total Assets	12,330.6	12,330.6	12,348.3	1.3		1,047.7	61.0
LIABILITIES							
Financial liabilities at fair value through profit or loss	10.9	10.9				-	10.9
Amounts owed to banks	66.0	66.0				30.6	35.5
Amounts owed to customers	10,629.7	10,629.7				897.8	9,731.9
Debt securities in issue							
Current tax	15.2	15.2					15.2
Deferred tax	5.7	5.7					5.7
Other liabilities	189.1	189.1				7.4	181.7
Accruals and deferred income	0.5	0.5					0.5
Derivatives designated for hedge accounting	14.0	14.0					14.0
Subordinated liabilities	234.2	164.5					164.5
Total Liabilities	11,268.3	11,095.6				935.8	10,159.8
EQUITY							
Called up share capital	583.8	583.8					583.8
Share premium account	49.3	49.3					49.3
Revaluation reserves	54.9	54.9					54.9
Retained earnings	374.3	305.3					305.3
Total Equity	1,062.3	993.4					993.4
Total Liabilities and Equity	12,330.6	12,089.0	-	-		935.8	11,153.2

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Template 2: EU LI2 – Main sources of differences between regulatory exposure amounts and carrying values in financial statements

		a	b	c	d	e
			Items subject to			
€ millions		Total	Credit risk framework	CCR framework	Securitisation framework	Market risk framework
1	**Assets carrying value amount under the scope of regulatory consolidation**	**13,397.3**	**12,348.3**	**1.3**		**1,047.7**
2	Liabilities carrying value amount under the regulatory scope of consolidation	(935.8)	-			(935.8)
3	Total net amount under the regulatory scope of consolidation	12,461.5	12,348.3	1.3		111.9
4	Off-balance-sheet amounts	2,164.5	2,164.5			
5	Differences due to consideration of provisions	(15.2)	(15.2)			
6	Differences due to credit risk mitigation techniques	(451.4)	(451.4)			
7	Differences due to credit conversion factors	(1,900.1)	(1,900.1)			
8	Other differences	4.2		4.2		
9	**Exposure amounts considered for regulatory purposes**	**12,263.6**	**12,146.2**	**5.5**		**111.9**

The following table provides an overview of the accounting and regulatory consolidation methods for each entity within the Group. Any company or associate that cannot be consolidated based on their business activities are accounted for using the equity method. Further information on the Group's equity accounted investees and subsidiaries can be found in note 18 and 19 to the Financial Statements, respectively.

Template 3: EU LI3 – Outline of the differences in the scopes of consolidation (entity by entity)

Name of the entity	Method of accounting consolidation	Method of regulatory consolidation		Description of the entity
		Full consolidation	Deducted	
Bank of Valletta plc	Full consolidation	X		Credit institution
BOV Fund Services Ltd	Full consolidation	X		Fund Administration
BOV Asset Management Ltd	Full consolidation	X		Fund Management
MAPFRE MSV Life plc	Equity method of accounting		X	Life Assurance
MAPFRE Middlesea plc	Equity method of accounting		X	Insurance

Section 3: Own Funds

3.1 Capital Overview

The Group maintains its objective of actively managing capital in an integrated way, seeking to fulfil the regulatory requirements, guarantee solvency, and maximise profit. Through this holistic approach the Group is able to achieve long-term sustainability and identify growth opportunities that provide a sustainable risk-return performance. The Group's capital management approach aims to ensure a sufficient level of capitalisation to absorb unexpected losses from its risk.

Capital metrics and the successful implementation of the ICAAP process are continuously monitored by the BoD, the Assets and Liabilities Committee (ALCO), and the MB. The BoD regularly receives information and reports from the lines of defence and all other functions, and action is taken on emerging issues of concern. They also ensure that the three lines are operating uniformly and according to best practice. The MB meets on a weekly basis to oversee the overall management of the Bank. The MB formulates risk strategies and risk profiles, including policies that are conducive to the achievement of the organisation's goals. ALCO meets on a monthly basis to analyse financial information and to assess the impact that the various types of risks arising from changes in interest rates, exchange rates and the market, have on the profitability and capital of the Bank. Through this structured monitoring, it is ensured that the Group remains adequately capitalised to achieve the strategic objectives set by the BoD.

The Group is required to meet a total SREP capital requirement (TSCR) of 11.25%, consisting of 8.00% minimum own funds requirement in line with Article 92(1) of the CRR, and a 3.25% Pillar II Requirement (P2R), to be solely met by CET1 capital. As at

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end of 2019, the Group reported a comfortable solvency position which exceeds all minimum requirements of the European Central Bank (ECB) and other regulations with the CET1 ratio standing at 19.51%. This enabled the Bank to comply with increases in the regulatory capital requirements and to implement the Bank's strategic initiatives.

The Board decided that the provision for contingent liabilities will increase by an additional €25 million bringing the total provision to €100 million. Further details on the litigation provision is included in note 33 to the Financial Statements.

Following this year's results, and having taken note of extensive discussions with the regulators, the BoD resolved to distribute a total of €10 million net dividends to its shareholders, for the financial year ending December 2019.

BOV is closely monitoring the situation and constantly assessing the impact of the COVID-19 pandemic on the capital position of the Group.

On 12 March 2020, the European Central Bank announced a number of measures to ensure that banks have the necessary resources to support the real economy. Banks are allowed to operate temporarily below the level of capital defined by the Pillar 2 guidance, the capital conservation buffer and the countercyclical capital buffer (CCyB).

At this early stage of the pandemic, it is very difficult to estimate the potential impact of COVID-19 on the Bank's capital position. In recent years, the Bank built up a material capital buffer, prudently exceeding the regulatory capital requirements. This surplus buffer, coupled with the temporary usage of regulatory buffers, will serve as a strong cushion to weather stresses caused by the pandemic. Further details can be found in note 43 to the Financial Statements.

3.2 Capital Instruments

The Group's capital base is composed of CET1 and Tier 2 capital, as defined in Part Two of the CRR. In line with new regulations, the Group is continuously monitoring and focusing towards further strengthening its CET1 capital which is the highest form of quality capital, thus providing the greatest level of protection against losses. The Group's capital base is primarily composed of issued common shares and retained earnings, which form part of CET1 capital – the Group's core capital. In line with the CRR, the Group's capital is subject to relative deductions. The main deductions relate to intangible assets and the reserve held against the depositor compensation scheme which is an added requirement in national legislation. In accordance with Section 3, Chapter 2, Title I, Part Two of CRR there were no other items requiring deductions from Own Funds. As at the end of the financial year both the Group's significant investments and deferred taxation were below the 10% threshold as stipulated in Article 48(1) of the CRR.

The Group has four subordinated bonds in issue and these are included as part of Tier 2 Capital as they fully qualify for the provisions listed under CRR (575/2013) Part Two, Title 1, Chapter 4, and Article 63. Specifically, these instruments rank after the claim of all other creditors and are not to be repaid until all other debts outstanding at the time have been settled. The 4.80% Euro subordinated bond is redeemable at par within the coming months (15 March 2020) and thus only the amortised amount is eligible for inclusion in Own Funds.

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In accordance with Article 492 of the CRR, the Group is required to complete an own funds disclosure template set out below.

	Own funds	**Dec-19**
	CET1 CAPITAL	**€000s**
	Common Equity Tier 1 capital: instruments and reserves	
1	Capital instruments and the related share premium accounts	633,126
2	Retained earnings	310,401
3	Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under the applicable accounting standards)	54,898
3a	Funds for general banking risk	5,271
6	**Common Equity Tier 1 capital before regulatory adjustments**	**1,003,696**
	Common Equity Tier 1 (CET1) capital : regulatory adjustments	
7	Additional value adjustments (negative amount)	(596)
8	Intangible assets (net of related tax liability) (negative amount)	(60,463)
18	Direct and indirect holdings by an institution of CET1 instruments of financial sector entities where the institution has a significant investment in those entitites	-
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related liability where the conditions in 38 (3) are met, negative amount)	-
	Amount exceeding the 17.65% threshold (negative amount)	-
23	*of which: Significant direct and indirect holdings by the institution of the CET1 instruments of financial sector entities*	-
25	*of which : deferred tax assets arising from temporary differences*	-
	Amount to be deducted from or added to CET1 capital with regard to additional filters and deductions required pre CRR	(43,250)
28	**Total regulatory adjustments to Common equity Tier 1 (CET1)**	**(104,309)**
29	**Common Equity Tier 1 (CET1) Capital**	**899,388**
	TIER 2 CAPITAL	
46	Capital instruments and the related share premium accounts	164,472
51	**Tier 2 (T2) capital before regulatory adjustments**	164,472
56	Regulatory adjustments applied to Tier 2 in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out	-
57	**Total regulatory adjustments to Tier 2 (T2)**	**-**
58	**Tier 2 (T2) Capital**	**164,472**
59	**TOTAL CAPITAL**	**1,063,860**
	TOTAL Risk Weighted Assets	
59a	Risk weighted assets in respect of amounts subject to pre-CRR treatment and transitional treatments	
	of which deferred tax assets not deducted from CET1 capital	190,043
	of which direct holdings by the institution of the CET1 instruments of financial sector entities not included in CET1 capital	132,174
60	**TOTAL Risk Weighted Assets**	**4,610,703**
	Capital ratios and buffers	
62	Tier 1 capital	**19.51%**
63	Total capital	**23.07%**
64	Institution specific buffer requirement	9.01%
65	*of which: Capital conservation buffer requirement*	2.50%
66	*of which: Countercyclical buffer requirement*	0.01%
67	*of which: Other Systemically Important Institution (O-SII) buffer*	2.00%
68	Common Equity Tier 1 available to meet buffers	15.01%
	Amounts below the thresholds for deductions	
73	The part of the holdings of CET1 instruments of financial sector entities (as defined in Article 4(1)(27) of CRR) where the institution has a significant investment but which is below the 10 % threshold in Article 48(1) point (b) of CRR.	52,870
75	Deferred tax assets arising from temporary differences (amount below 10% threshold)	67,267

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In accordance with Part Eight Article 437 of the CRR the following table discloses the main features and the terms and conditions of Tier 1 and Tier 2 instruments.

Capital Instruments Main Features	BOV Ordinary Shares	4.8% BOV Subordinated Bonds 2020	3.5% BOV Subordinated Notes 2030 Series 1	3.5% BOV Subordinated Notes 2030 Series 2	3.75% BOV Subordinated Bonds 2026 - 2031
1 Issuer	Bank of Valletta plc	Bank of Valletta plc	Bank of Valletta plc	Bank of Valletta plc	Bank of Valletta plc
2 Unique identifier	MT0000020116	MT0000021270	MT0000021312	MT0000021320	MT0000021353
3 Governing Law(s) of the instrument	Maltese Law	Maltese Law	Maltese Law	Maltese Law	Maltese Law
Regulatory Treatment					
4 Transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2	Tier 2	Tier 2
5 Post-transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2	Tier 2	Tier 2
6 Eligible at solo/(sub)consolidated / solo & (sub)consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated
8 Amount recognised in regulatory capital	EUR 583.8 million	EUR 2.8 million	EUR 66.9 million	EUR 44.7 million	EUR 50.0 million
9 Nominal amount of instrument	EUR 583.8 million	EUR 70.0 million	EUR 66.9 million	EUR 44.7 million	EUR 50.0 million
9a Issue Price	N/A	At par (€100 per bond)	At par (€100 per bond)	At par (€100 per bond)	At par (€100 per bond)
9b Redemption Price	N/A	At €100	At €100	At €100	At €100
10 Accounting classification	Share Equity	Liability- amortised cost	Liability- amortised cost	Liability- amortised cost	Liability- amortised cost
11 Original date of issuance	26 August 1992	15 March 2010	22 December 2015 and 6 April 2016 *	22 December 2015 and 6 April 2016 **	9 July 2019
12 Perpetual or dated	N/A	Dated	Dated	Dated	Dated
13 Original maturity date	N/A	15 March 2020	8 August 2030	8 August 2030	15 June 2031
14 Issuer call subject to prior supervisory approval	No	No	No	No	Yes
Coupons/dividends					
17 Fixed or floating dividend coupon	Floating	Fixed	Fixed	Fixed	Fixed
18 Coupon rate and any related index	N/A	4.80%	3.50%	3.50%	3.75%
19 Existence of dividend stopper	No	No	No	No	No
20a Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary	Mandatory	Mandatory	Mandatory	Mandatory
20b Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Mandatory	Mandatory	Mandatory	Mandatory
21 Existence of step up or other incentive to redeem	N/A	No	No	No	No
22 Noncumulative or cumulative	Non-cumulative	Non-cumulative	Non-cumulative	Non-cumulative	Non-cumulative
23 Convertible or non-convertible	Non-convertible	Non-convertible	Non-convertible	Non-convertible	Non-convertible
30 Write-down features	No	No	No	No	No
35 Position in subordination hierarchy in liquidation	Subordinated to the Issuer's (BOV) subordinated bonds	Subordinated to other outstanding, unsubordinated and unsecured obligations of the Issuer (BOV), present and future.	"Subordinated to other outstanding, unsubordinated and unsecured obligations of the Issuer (BOV), present and future."	"Subordinated to other outstanding, unsubordinated and unsecured obligations of the Issuer (BOV), present and future."	Subordinated to other outstanding, unsubordinated and unsecured obligations of the Issuer (BOV), present and future.
36 Non-compliant transitional features	No	No	No	No	No

* €52,705,800 were issued on 22 December 2015 (Tranche 1 - MT0000021312) and €14,214,700 were issued on 6 April 2016 (Tranche II -MT 0000021338) These two tranches were subsequently merged on 8 August 2016 into ISIN MT0000021312
** €22,294,200 were issued on 22 December 2015(Tranche 1-MT0000021320) and €22,376,200 were issued on 6 April 2016 (Tranche II -MT 0000021346) These two tranches were subsequently merged on 8 August 2016 into ISIN MT0000021320

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3.3 Reconciliation of Own Funds to audited Financial Statements

The table below provides a full reconciliation of the Group's own funds to the statement of financial position within the audited financial statements for the period ended 31 December 2019.

Reconciliation between accounting and regulatory scope of consolidation

	Group 2019 €000
Common Equity Tier 1	
As per Statement of Financial Position	
Called up share capital	583,849
Share premium account	49,277
Retained earnings	374,281
Revaluation reserves	54,898
Less: Own Funds adjustments	
Investments in Associates	(48,610)
Depositor Compensation Scheme reserve	(43,250)
Intangible assets	(60,463)
Final dividend	(10,000)
Prudential Valuation on Fair-Valued Assets and Liabilities	(596)
	899,388
Tier 2	
As per Statement of Financial Position	
Subordinated liabilities	234,230
Less : Accrued Interest Payable	(2,639)
Less: Amortisation of subordinated loan capital	(67,118)
	164,472
Total Own Funds	**1,063,860**

Section 4: Capital Requirements (CRR Article 438)

4.1 Overview of Pillar 1 capital requirements

The Group uses the following approaches to calculate the own funds requirements for Pillar I risks.

- The *Standardised Approach for credit risk*. Risk weights for the Treasury Portfolio are determined by taking the worst credit rating from the best two credit ratings provided by eligible External Credit Assessment Institutions (ECAIs) – Fitch, Moody's and S&P. Regulatory risk weights are used for unrated exposures and the lending portfolio.
- The *Basic Indicator Approach for operational risk.* Under this approach the Group allocates capital by taking 15% of the average gross income of the preceding three years.
- The *Standardised Approach with respect to the Group's foreign exchange risk*. The capital charge for foreign exchange risk using the Basic Method is calculated at 8% of the higher of the sum of all the net short positions and the sum of all the net long positions in each foreign currency.
- A minimum capital requirement is also determined for non-credit obligation assets (i.e. 'other assets' on the balance sheet) in line with the CRD IV 575/2013.

In addition to the above, Banking Rule BR/15: Capital Buffers of Credit Institutions authorised under the Banking Act, 1994, requires additional buffers, namely the Capital Conservation Buffer (CCB), Countercyclical Capital Buffer (CCyB), Other-Systemically Important Institutions (O-SII) buffer, and Systemic Risk Buffer. These buffers are aimed at strengthening the resilience of the Group and have entered into force as from January 2016, with full application as from January 2019. Automatic restrictions on capital distributions apply if the Group's CET1 capital falls below the level of its CRD IV combined buffer.

The Group is also required to maintain an institution-specific CCyB based on the geographical location of the relevant credit exposure. Following Article 130(1) of Directive 2013/36/EU (CRD) the institution-specific countercyclical capital buffer is calculated by multiplying the total risk exposure amount (TREA) with the weighted average of the countercyclical buffer rates as calculated in line with Article 140 CRD. In line with Article 440 of the CRR the following table discloses the geographical distribution of the Group credit exposures relevant for the calculation of the institution-specific CCyB and the amount of the institution specific CCyB.

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Institution Specific Ccyb

€000					
Country	**Credit Exposure**	**RWA**	**Own Funds**	**CCyB Rate**	**CCyB Capital Charge**
BULGARIA	0.1	0.1	0.0	0.50%	0.0
DENMARK	181.4	63.6	5.1	1.00%	0.1
FRANCE	17,017.5	8,429.2	674.3	0.25%	1.7
HONG KONG	221.8	65.0	5.2	2.00%	0.1
IRELAND	5,374.4	2,677.1	214.2	1.00%	2.1
LITHUANIA	2.2	1.6	0.1	1.00%	0.0
NORWAY	908.5	318.6	25.5	2.50%	0.6
SLOVAKIA	2.2	0.3	0.0	1.50%	0.0
SWEDEN	15,499.2	7,765.2	621.2	2.50%	15.5
UNITED KINGDOM	18,921.0	9,001.2	720.1	1.00%	7.2
OTHERS	5,889,218.0	3,508,566.0	280,685.3	0.00%	-
	5,947,346.3	**3,536,887.9**	**282,951.0**	**0.00%**	**27.4**

Total Risk Exposure Amount	4,573,325.5
Institution Specific Countercyclical Buffer Rate	0.01%
Institution Specific Countercyclical Buffer Requirement	442.1

In accordance with Article 438(c) to (f) of the CRR, the following table provides an overview of the total RWA and the capital requirement for credit risk, split by the different exposure classes, as well as capital for operational risk, foreign exchange risk, and credit valuation adjustment risk. No capital is allocated for market risk as the Bank does not operate a trading book. The Bank has no exposure in items representing securitisation positions. Moreover, there is no capital allocated for settlement risk, commodities risk, position risk and large exposures. The exposure value is equal to the total on-balance sheet and off-balance sheet net of value adjustments and provisions and post Credit Conversion Factor (CCF).

	EU OV1 – Overview of RWAs	**31 December 2018**		**31 December 2019**	
	€ millions	**RWA amounts**	**Minimum capital requirements**	**RWA amounts**	**Minimum capital requirements**
1	**Credit risk (excluding CCR)**	**4,187.7**	**335.0**	**4,136.8**	**330.9**
2	of which the standardised approach	4,187.7	335.0	4,136.8	330.9
	Central government or central banks	2.1	0.2	2.1	0.2
	Regional government or local authorities	39.4	3.1	31.7	2.5
	Public sector entities	36.4	2.9	39.8	3.2
	Multilateral development banks	-	-	-	-
	International organisations	-	-	-	-
	Institutions	666.9	53.3	489.0	39.1
	Corporates	1,266.8	101.3	1,385.7	110.9
	Retail	539.1	43.1	585.6	46.8
	Secured by mortgages on immovable property	832.8	66.6	756.7	60.5
	Exposures in default	190.5	15.2	159.2	12.7
	Items associated with particular high risk	110.8	8.9	125.1	10.0
	Covered bonds	-	-	-	-
	Claims in the form of CIU	-	-	-	-
	Equity exposures	46.2	3.7	187.3	15.0
	Other items	456.6	36.5	374.5	30.0
6	**CCR**	**20.3**	**1.6**	**3.6**	**0.3**
7	Of which Mark to Market	6.4	0.5	2.5	0.2
12	Of which CVA	14.0	1.1	1.1	0.1
13	**Settlement risk**	**-**	**-**	**-**	**-**
19	**Market risk***	**1.9**	**0.2**	**2.9**	**0.2**
20	Of which the standardised approach	1.9	0.2	2.9	0.2
23	**Operational risk**	**463.6**	**37.1**	**467.5**	**37.4**
24	of which the basic indicator approach	463.6	37.1	467.5	37.4
27	**Amounts below the thresholds for deduction (subject to 250% risk weight)**	**311.6**	**24.9**	**322.2**	**25.8**
29	**TOTAL**	**4,673.5**	**373.9**	**4,610.7**	**368.9**

**Own Funds allocated for Commodities Risk is equal to zero*
**Own Funds allocated for Large Exposures and Position Risk is equal to zero*

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4.2 Internal Capital Adequacy Assessment Process (ICAAP) and stress testing

The ICAAP document is prepared on an annual basis with the aim of providing an overview of the Group's capital position and sustainability to ensure that the current and future capital requirements are met. The ICAAP document describes the Group's Strategy, Risk Appetite Framework (RAF) and budget forecasts to ultimately project the capital positions over five year horizon.

The main objective of the ICAAP is to ensure that the level of available capital exceeds the bank's minimum regulatory capital requirements, even under events of stress, which is sufficient to support the Bank's strategy and risk profile. For this reason the ICAAP also includes a number of stress tests which are applied to assess the resilience of the Bank's capital to severe but plausible events and identify any potential vulnerabilities. The Group's internal stress testing is based on various scenarios and sensitivity analysis on credit risk, interest rate risk and liquidity risk. Stress tests are an important means of analysing the risk profile since they give management a better understanding of how the Group's revenue streams and capital are impacted by macroeconomic changes. The Bank also participates in the Supervisory Review and Evaluation Process (SREP) EU-wide external stress test conducted by the ECB. The purpose of such an exercise is to assess the robustness of the Single Supervisory Mechanism (SSM) banks under stressed conditions and their ability to absorb losses in various economic scenarios.

Apart from encompassing the adequacy of capital requirements for Pillar 1 risks, the ICAAP includes the identification of other material residual risks, classified under Pillar 2 requirements, to which the Bank is or might be exposed to as a consequence of its activities and overall environment. These include concentration risk, interest rate risk in the banking book, reputational risks and other material risks. When these risks have been identified, the Group determines the means by which they will be mitigated and also which risks will be covered by capital.

The BoD and senior management strongly believe that the ICAAP document is an essential management tool which should be used at a strategic level and consider that promoting the knowledge and use of the ICAAP document across all relevant functions will contribute to a stronger capital position. Thus the ICAAP will continue to act as an important contribution to the strengthening of the risk management practices and capital adequacy of the Bank.

Section 5: Leverage Ratio (CRR Article 451)

The Leverage Ratio was introduced into the Basel III framework as a non-risk-based backstop limit, to supplement risk-based capital requirements. Its purpose is to limit the leverage effects in the balance sheet as it is a volume-based measure calculated as fully phased in Tier 1 capital divided by Total exposure in line with CRR Article 429. The latter is composed of on-balance sheet assets plus off-balance sheet exposures, such as undrawn commitments and derivatives potential future exposures, less amounts permitted to be deducted for Tier 1 capital.

As at December 2019, the actual leverage ratio increased by 29 basis points to 7.15% (Dec 2018: 6.86%) with a Tier 1 Capital of €899.4million and with total leverage exposure of €12,578 million. The increase in the ratio is mainly due to Tier 1 capital increasing by a largest percent then the leverage exposure. This lies well above the 3% minimum requirement and thus no additional capital is required. The leverage ratio is monitored and reported to the BoD on a frequent basis in line with the risk appetite framework to ensure that the risk of excessive leverage is managed.

	Leverage Ratio	**Dec-19 € millions**
1	On-balance sheet items (excluding derivatives and SFTs)	12,329.3
2	Asset amounts deducted in determining Tier 1 capital	(104.3)
3	**Total on-balance sheet exposures (excluding derivatives and SFTs)**	**12,225.0**
4	Replacement cost associated with all derivatives transactions	1.3
5	Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	4.2
11	**Total derivatives exposures**	**5.5**
17	Off-balance sheet exposures at gross nominal amount	2,137.1
18	Adjustments for conversion to credit equivalent amounts	(1,789.2)
19	**Total Other off-balance sheet exposures**	**347.9**
20	Tier 1 Capital	899.4
21	Leverage ratio total exposure measure	12,578.5
22	**Actual Leverage Ratio (transitional)**	**7.15%**
	Statutory Minimum	*3.00%*

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The following table provides a summarised reconciliation of accounting assets and leverage ratio exposures.

	Summary reconciliation of accounting assets and leverage ratio exposures	Dec-19 € millions
1	Total assets as per published financial statements	12,330.6
4	Adjustments for derivatives financial instruments	4.2
6	Adjustments for off-balance sheet items	347.9
7	Other adjustments	(104.3)
8	**Leverage ratio total exposure measure**	**12,578.5**

The following table provides a split-up of the on-balance sheet exposures, excluding derivatives.

	Table LRspl: Split-up of on balance sheet exposures (excludng derivatives, SFTs and exempted exposures)	Dec-19 € millions
EU-1	Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:	12,330.3
EU-2	Trading book exposures	0.0
EU-3	Banking book exposures, of which:	12,330.3
EU-4	Covered Bonds	0.0
EU-5	Exposures treated as sovereign	4,763.4
EU-6	Exposures to regional government, MDB, international organisations and PSE not treated as sovereigns	609.7
EU-7	Institutions	1,560.2
EU-8	Secured by mortgages of immovable properties	2,053.4
EU-9	Retail exposures	841.9
EU-10	Corporate	1,690.3
EU-11	Exposures in default	132.9
EU-12	Other exposures	678.3

Section 6: Credit Risk

6.1 Management of Credit Risk

Credit risk is the risk of suffering financial loss should any of the Bank's counterparties fail to fulfil their contractual payment obligations. The Group's exposure to credit risk arises mainly through its lending and investment activities and represents the Group's largest regulatory capital requirement. This is subject to rigorous monitoring and control.

Credit risk is on the Bank's primary risk factors and is managed in line with the credit risk appetite metrics. The Bank maintains a strong local presence and a close customer relationship, whilst ensuring that the credit quality is not neglected in favour of higher volumes or margins.

The credit risk management function is responsible for ensuring that the Bank's credit risk is properly managed. The main objectives of credit risk management are to: (i) maintain a framework of controls to ensure that credit risk-taking is based on sound credit risk management principles; (ii) identify, assess, and measure credit risk accurately, both on an individual level as well as on a portfolio basis, limiting undesirable concentrations of exposure by counterparty, sector and geography; and (iii) monitor credit risk whilst ensuring that risk-reward objectives are met.

The Bank has in place a number of policies tailored for each type of business, which articulate its appetite towards credit risk. These include (i) Business Lending; (ii) Home Loans; (iii) Personal Lending and Credit Cards; (iv) E-Commerce; (v) Trade Finance; (vi) Property Lending; (vii) Treasury management and (viii) policies related to the management of non-performing loans. These policies relate to (i) Forbearance; (ii) Collateral; (iii) Early Warning Indicators; (iv) Non-performing loans and Arrears Management; (v) Debt Recovery Management; and (vi) Write offs. Such policies are underpinned by core principles related to compliance with the Group's ethical standards, clear definition of responsibilities, the existence and implementation of procedures, limits that ensure a high degree of diversification, and thorough analysis of risk. Procedures for the consideration and monitoring of exceptions to each policy are included in the respective policy document.

Policies are reviewed periodically to keep them aligned with the ever-changing market conditions, new regulations and the Bank's risk appetite, and are approved by the BoD. During the financial year 2019, the Bank reviewed the Trade Finance Policy and updated the Business Lending Policy, the Treasury Management Policy and policies related to the non-performing loans. The Bank is also in the process of updating its Consumer Lending policies.

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6.2 Approval authorities

The Bank has in place a dual voting system with regards to business related transactions, governed mainly by the Business Credit Policy. New lending facilities are sanctioned through a vote by Business Sanctioning Officers and a vote by Risk Sanctioning Officers, in accordance with the relative limits. For proposals exceeding a defined limit, authorisation is sought from higher levels within the Bank or from the Credit Committee appointed by the BoD. Lending officers are each allocated a voting limit based on their individual capabilities and experience, and the nature and scale of lending in the business unit where they are posted. Voting limits are approved by the Chief Risk Officer and ratified by the Management Board.

Other areas such as Trade Finance, E-Commerce, Debt Management and Consumer Lending exposures exceeding an internally instituted threshold, are also subject to the dual voting system and governed by their respective policies.

The dual voting system does not govern other Consumer Lending for which a separate discretionary lending limits system applies, which in most cases is facilitated by the use of a credit scorecard. The latter analyses data and grades customers according to their creditworthiness. Borderline cases are referred and become subject to the normal approval process in line with the appropriate discretionary lending limits. The Bank has been using the credit scorecard for a number of years, and this has evolved from a generic to a bespoke application after an adequate history of defaults was accumulated.

The investment portfolio is managed by the Treasury Department and it is the Bank's strategy to buy and hold instruments until maturity rather than for trading purposes. Investment proposals are allocated limits according to the Treasury Management Policy (TMP) with a 'four-eye' approach applied when an investment proposal falls outside the criteria set out in the TMP. The Credit Risk Sanctioning Department undertakes an independent analysis of proposals which are then submitted to the Credit Committee for their consideration. The Credit Committee's approval is also required for exposures exceeding the relative TMP limit.

6.3 Quantitative information on credit risk exposures

Institutions are required to comply and publicly disclose information in accordance with Article 435(1) of Part Eight of the CRR at least on annual basis.

In accordance with the EBA guidelines on Pillar 3 disclosure requirements – EBA/GL/2016/11, version 2 – the following table shows the net exposure values, before accounting for the effects of credit risk mitigation, as at December 2019 and December 2018 by exposure classes and the average net exposure value of this financial period; such is based on the last four end-of-calendar quarter observations.

	EU CRB-B: Total and average net amount of exposures € millions	**Net value of exposures as at December 2019**	**Average net exposures over the period**	**Net value of exposures as at December 2018**
15	**Total IRB approach**	-	-	-
16	Central governments or central banks	4,775.1	4,745.1	4,336.9
17	Regional governments or local authorities	133.0	178.3	210.1
18	Public sector entities	79.5	79.6	72.9
19	Multilateral development banks	320.8	310.4	275.8
20	International organisations	81.0	73.0	35.5
21	Institutions	1,575.5	1,628.8	1,881.7
22	Corporates	3,040.4	3,215.1	3,146.1
23	Of which: SMEs	2,308.7	2,387.6	2,220.6
24	Retail	1,488.6	1,470.1	1,392.4
25	Of which: SMEs	150.2	144.1	108.2
26	Secured by mortgages on immovable property	2,053.4	2,007.5	2,178.8
27	Of which: SMEs	286.4	258.3	492.3
28	Exposures in default	186.2	187.2	199.0
29	Items associated with particularly high risk	153.1	111.1	86.0
30	Covered bonds	-	-	-
31	Claims on institutions and corporates with a short-term credit assessment	-	-	-
32	Collective investments undertakings	-	-	-
33	Equity exposures	156.6	76.9	46.2
34	Other exposures	421.8	419.9	445.9
35	**Total Standardised Approach**	**14,465.8**	**14,503.0**	**14,307.2**
36	**Total**	**14,465.8**	**14,503.0**	**14,307.2**

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6.3.1 Concentration Risk

Concentration risk is exhibited when there are significant exposures to one counterparty or to a group of connected counterparties, or to counterparties with similar characteristics within a given economic sector or to counterparty operating in the same geographical area. The Bank experiences concentration risk in its lending and investment activities due to the structure of the local economy and the size of the domestic financial sector.

As part of the Group's credit risk management approach and in order to avoid undue concentrations, the Bank has systems in place to identify, measure and monitor Single Name, Sectoral and Geographical concentrations. The systems and controls are designed to ensure adherence to prudential limits set by the BoD and/or by the regulatory authorities to a single counterparty or groups of related counterparties. The Board and senior management being informed on a regular basis on the level of concentration in the Bank's portfolio.

In terms of the Risk Appetite Framework (RAF), the Bank has defined and regularly monitors the following indicators related to concentration risk:

(a) Single-name exposure by Sovereign to CET1;
(b) Sectoral exposure by property lending to CET1;
(c) Non-performing loans ratio (NPL ratio as defined by EBA);
(d) Coverage ratio which gauges the degree of credit risk mitigation relating to NPLs.

Furthermore, the Bank is at all times compliant with CRR Article 395 relating to large exposures to single names including connected clients.

At the present time, credit default swaps (CDS) are not availed of; neither is netting of on- and off-balance sheet exposures as a credit risk mitigation technique. Information on the total exposure amount covered by financial guarantees is provided in EU CR3 in Section 6.1.5.

The Bank analyses its concentration risk in the advances and investment portfolios. The Herfindahl-Hirschman Index (HHI) calculated using risk-weighted assets to better reflect the degree of risk sensitivity is used to assign a capital add-on (%) to credit risk. This results in an amount of capital allocated against concentration risk under Pillar2.

The following tables show the distribution of the exposures (net values of on-balance sheet and off-balance balance) by geographical distribution, industry, and residual maturity broken down by exposure classes in line with CRR Article 442(d/e/f).

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	EU CRB-C: Geographical breakdown of exposures € millions	**Net value**								
		Malta	**Germany**	**France**	**Belgium**	**Netherlands**	**United Kingdom**	**Australia**	**Other Countries**	**Total**
6	**Total IRB approach**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
7	Central governments or central banks	4,120.8	212.4	74.6	76.4	26.2	-	-	264.7	4,775.1
8	Regional governments or local authorities	14.6	35.4	17.0	-	1.8	-	-	64.3	133.0
9	Public sector entities	79.5	-	-	-	-	-	-	-	79.5
10	Multilateral development banks	-	-	-	-	-	-	-	320.8	320.8
11	International organisations	-	-	-	-	-	-	-	81.0	81.0
12	Institutions	95.1	110.9	132.1	91.2	102.7	150.5	149.6	743.9	1,576.1
13	Corporates	2,795.6	38.7	16.0	17.0	47.6	12.3	-	113.2	3,040.4
14	Retail	1,482.8	0.0	0.1	0.0	0.1	0.9	0.2	4.4	1,488.6
15	Secured by mortgages on immovable property	2,036.4	0.4	0.9	0.3	0.2	5.4	0.6	9.3	2,053.4
16	Exposures in default	185.2	-	-	-	-	0.4	-	0.2	185.8
17	Items associated with particularly high risk	153.1	-	-	-	-	-	-	-	153.1
18	Covered bonds	-	-	-	-	-	-	-	-	-
19	Claims on institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-	-
20	Collective investments undertakings	-	-	-	-	-	-	-	-	-
21	Equity exposures	129.4	-	-	0.2	-	-	-	26.7	156.3
22	Other exposures	421.8	-	-	-	-	-	-	-	421.8
23	**Total standardised approach**	**11,514.5**	**397.9**	**240.7**	**185.1**	**178.6**	**169.5**	**150.4**	**1,628.5**	**14,465.8**
24	**Total**	**11,514.5**	**397.9**	**240.7**	**185.1**	**178.6**	**169.5**	**150.4**	**1,628.5**	**14,465.8**

Note to EU CRB-C Table: 'Other countries' account for circa 11% of the total net exposure value; this grouping comprises 64 different countries. The main ones are the USA, Austria, Sweden & Canada.

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	EU CRB-D: Concentration of exposures by industry or counterparty types € millions	Financial and Insurance Activities	Households and Individuals	Public administration and defence, compulsory social security	Wholesale and retail trade	Real estate activities	Construction	Others	Total
6	**Total IRB approach**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
7	Central governments or central banks	3,453.7	-	1,268.0	-	4.3	-	49.1	4,775.1
8	Regional governments or local authorities	3.1	-	126.0	0.1	12.2	-	-8.3	133.0
9	Public sector entities	-	-	-	-	-	-	79.5	79.5
10	Multilateral development banks	-	-	320.8	-	-	-	-0.0	320.8
11	International organisations	-	-	81.0	-	-	-	0.0	81.0
12	Institutions	1,575.5	-	-	-	-	-	-	1,575.5
13	Corporates	558.3	35.5	1.8	497.7	432.1	230.6	1,284.3	3,040.4
	of which: SMEs	215.7	0.0	1.1	322.4	395.1	206.1	1,168.4	2,308.7
14	Retail	10.4	1,189.3	0.0	98.5	29.8	23.8	136.9	1,488.6
	of which: SMEs	9.2	0.0	0.0	56.8	15.3	11.5	57.4	150.2
15	Secured by mortgages on immovable property	19.6	1,680.4	0.6	70.8	94.5	22.5	165.1	2,053.4
	of which: SMEs	17.5	-	0.3	52.8	82.2	20.4	113.2	286.4
16	Exposures in default	1.5	36.6	-	18.5	4.8	66.5	58.3	186.2
17	Items associated with particularly high risk	45.3	5.3	-	2.5	34.2	45.2	20.7	153.1
18	Covered bonds	-	-	-	-	-	-	-	-
19	Claims on institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-
20	Collective investments undertakings	-	-	-	-	-	-	-	-
21	Equity exposures	29.8	-	17.3	-	8.6	-	101.0	156.6
22	Other exposures	-	-	-	-	-	-	421.8	421.8
23	**Total standardised approach**	**5,697.1**	**2,947.2**	**1,815.5**	**688.6**	**620.4**	**388.5**	**2,309.1**	**14,465.8**
24	**Total**	**5,697.1**	**2,947.2**	**1,815.5**	**688.6**	**620.4**	**388.5**	**2,309.1**	**14,465.8**

Note to EU CRB-D Table: The industry being quoted in this table is by NACE Level 1 of the debtor.

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	EU CRB-E: Maturity of Exposures € millions	Net Exposure Value On demand	<= 1 year	> 1 year <= 5 years	> 5 years	No stated maturity	Total
6	**Total IRB approach**	-	-	-	-	-	-
7	Central governments or central banks	-	3,764.7	452.0	558.4	-	4,775.1
8	Regional governments or local authorities	1.5	28.5	28.9	69.5	4.6	133.0
9	Public sector entities	-	-	-	79.5	-	79.5
10	Multilateral development banks	-	43.6	168.7	108.4	-	320.8
11	International organisations	-	-	33.5	47.5	-	81.0
12	Institutions	343.4	515.4	691.6	24.7	1.0	1,576.1
13	Corporates	195.6	107.6	279.1	2,148.0	310.1	3,040.4
	of which: SMEs	173.5	25.4	96.7	1,351.8	661.4	2,308.7
14	Retail	70.3	243.3	94.1	1,043.0	37.9	1,488.6
	of which: SMEs	51.7	15.5	24.9	58.1	-	150.2
15	Secured by mortgages on immovable property	77.9	1.8	42.5	1,931.3	-	2,053.4
	of which: SMEs	66.7	0.6	26.3	192.9	-	286.4
16	Exposures in default	33.2	30.2	12.1	80.9	29.7	186.2
17	Items associated with particularly high risk	11.1	6.5	74.4	54.5	6.7	153.1
18	Covered bonds	-	-	-	-	-	-
19	Claims on institutions and corporates with a short-term credit assessment	-	-	-	-	-	-
20	Collective investments undertakings	-	-	-	-	-	-
21	Equity exposures	-	-	-	-	156.6	156.6
22	Other exposures	-	-	-	-	421.8	421.8
23	**Total standardised approach**	**732.9**	**4,741.8**	**1,877.0**	**6,145.7**	**969.3**	**14,465.8**
24	**Total**	**732.9**	**4,741.8**	**1,877.0**	**6,145.7**	**969.3**	**14,465.8**

6.4 Credit Risk Adjustments

6.4.1 Past due and Impaired

In accordance with CRR Article 178, non-performing exposures (NPL) are defined as exposures which satisfy either or both of the following criteria: (i) material exposures which are more than 90 days past due; and/or (ii) the debtor is assessed as unlikely to pay (UTP) its credit obligations in full without realisation of collateral, regardless of the existence of any past due amount or of the number of days past due.

As from 1st January 2018, the Bank adopted IFRS 9 and approved the new Provisioning Policy. The new framework outlines a 'three-stage' model for impairment based on changes in credit quality since initial recognition:

- Stage 1 – performing exposures which are not credit-impaired;
- Stage 2 – underperforming exposures where a significant increase in credit risk was determined; and
- Stage 3 – non-performing exposures which are credit-impaired.

Under IFRS 9, a financial asset is deemed to be credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset, have occurred. Evidence that a financial asset is credit-impaired include observable data about a number of events, namely significant financial difficulty on the part of the issuer or borrower, a breach of contract (such as a default or past due event), and when a concession has been granted to the borrower by the lender due to the borrower's financial difficulty. A specific allowance is set aside to cover the unsecured portion when cash flows from operations plus the estimated realisable value of any collateral held are considered insufficient to recover the full exposure.

The Bank has a comprehensive internal rating system designed to reflect the risk inherent in each lending relationship, identify problematic loans in a timely manner and thereby assist in the creation of a quality loan book. The loan portfolio is analysed in terms of the twelve grading levels within the internal credit rating system. The relative rating is primarily determined by the operating performance of the account and by other qualitative criteria. Exposures are analysed on a regular basis to determine whether there is impairment in the customer's business which merits a change in rating. For regulatory and high-level internal reporting, the twelve grading levels are mapped to the three IFRS 9 regime states as follows:

- Performing (exposures bearing a Regular rating);
- Underperforming (exposures rates Watch and Substandard); and
- Non-performing (those exposures classified as Doubtful on the internal rating system).

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The two tables below provide information on the changes of defaulted and impaired loans and debt securities during the financial year ending December 2019: first table provides information in respect to the changes in the stock of general and specific credit risk adjustments whereas the second table provides information on the changes in stock.

		Accumulated specific credit risk adjustment	Accumulated general credit risk adjustment
1	**Opening balance**	89.6	-
2	Increases due to amounts set aside for estimated loan losses during the period	23.4	-
3	Decreases due to amounts reversed for estimated loan losses during the period	(21.7)	-
4	Decreases due to amounts taken against accumulated credit risk adjustments	(1.0)	-
5	Transfers between credit risk adjustments	0.0	-
6	Impact of exchange rate differences	-	-
7	Business combinations, including acquisitions and disposals of subsidiaries	-	-
8	Other adjustments	(1.4)	-
9	**Closing balance**	88.9	-
10	Recoveries on credit risk adjustments recorded directly to the statement of profit or loss	-	-
11	Specific credit risk adjustments directly recorded to the statement of profit or loss	88.9	-

EU CR2-B - Changes in the stock of defaulted loans and debt securities € millions		Gross carrying value defaulted exposures
1	**Opening balance**	243.5
2	Loans and debt securities that have defaulted or impaired since the last reporting period	33.5
3	Returned to non-defaulted status	(15.2)
4	Amounts written off	(2.5)
5	Other changes	(41.5)
6	**Closing balance**	217.9

6.4.2 Impairment Allowances and Coverage

The Provisions Committee is responsible for developing and maintaining the Bank's provisioning methodology. It is composed of representatives from the following functions: Finance, Risk, Debt Management and Credit with the latter attending as observers.

IFRS 9 replaced the 'incurred loss' model ingrained in IAS 39 with a forward-looking 'expected credit loss' (ECL) model. Since a forward-looking approach is adopted, the occurrence of a credit event is not a prerequisite for the quantification of probable credit losses as at reporting date. The ECL is determined by multiplying the exposure at default (EAD) by the probabilities of default (PDs) and also includes an adjustment relating to the effective recovery rates post-default. The PDs are projected over a future time horizon on the basis of three alternative macroeconomic scenarios – base, downside, and upside – as required by the IFRS 9 accounting standard. Further detail relating to the calculation of the ECL is found in the Note 39.2.1.2 to the financial statements.

As defined in Commission Delegated Regulation (EU) 183/2014, the following shall be classified as specific credit adjustments:

a) losses recognized in the profit or loss account for instruments measured at fair value that represent credit risk impairment under the applicable accounting framework;
b) losses as a result of current or past events affecting certain exposures;
c) losses for which historical experience, adjusted on the basis of current observable data, indicating that the loss has occurred but the institution is not yet aware which individual exposure has suffered these losses.

Accordingly, the Group's impairment allowances calculated under IFRS 9 are classified as specific credit risk adjustments and in line with CRR Article 111 are deducted from the accounting values in order to determine the exposure value of an asset for risk weighted assets calculations. (Further details related to impairment allowances are found in the following notes to the Financial Statements – 17; 39.2) The Group does not account for any general credit risk adjustments.

6.4.3 External Credit Assessment Institutions (ECAIs)

The Standardized Approach (SA) requires banks to use the risk assessments prepared by ECAIs to be in a position to determine the risk weights to be applied. For treasury investments, three of the EBA-recognized ECAIs are resorted to – Fitch, Moody's and S&P – of which, the worst of the best two approach is used. Such approach is in line with the CRR for capital allocation purposes. Such external ratings are mapped to the credit quality steps in line with the relative EBA guidelines. Where no external rating is available, the standardized approach provides specific risk weights which need to be applied depending mainly on the counterparty type.

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

The above ECAIs are used for the following exposure classes, wherever such a credit assessment is available, in accordance with Part Three, Title II, Chapter 2 of the CRR:

- Central Governments or central banks
- Regional governments or local authorities
- Public sector entities
- Multilateral development banks
- International organizations
- Institutions
- Corporates

6.4.4 Credit quality of the Bank's exposures

In line with the EBA guidelines on disclosures, the tables below provide information on the credit quality of the Bank's assets by exposure class, industry and geography as at December 2019. Impaired exposures are equal to the defaulted exposures which are classified as IFRS 9 Stage 3 exposures.

EU CR1-A: Credit quality of exposures by exposure class and instrument € millions		Gross carrying values of		Specific credit risk adjustment	Accumulated write-offs*	Credit risk adjustment charges of the period**	Net values
		Defaulted exposures	Non-defaulted exposures				
15	**Total IRB approach**	-	-	-	-	-	-
16	Central governments or central banks	-	4,775.3	0.2	-	0.0	4,775.1
17	Regional governments or local authorities	-	133.1	0.0	-	0.0	133.0
18	Public sector entities	-	79.5	0.0	-	-	79.5
19	Multilateral development banks	-	320.8	0.0	-	-	320.8
20	International organisations	-	81.0	0.0	-	-	81.0
21	Institutions	-	1,576.2	0.1	-	-	1,576.1
22	Corporates	-	3,061.3	20.9	-	9.7	3,040.4
23	Of which: SMEs	-	2,326.7	18.0	-	8.6	2,308.7
24	Retail	-	1,500.4	11.7	-	4.3	1,488.6
25	Of which: SMEs	-	152.9	2.7	-	0.0	150.2
26	Secured by mortgages on immovable property	-	2,054.6	1.2	-	-	2,053.4
27	Of which: SMEs	-	286.7	0.2	-	-	286.4
28	Exposures in default	264.5	-	78.4	29.0	29.4	186.2
	Of which: past due	131.3	-	53.0	29.0	25.3	78.3
29	Items associated with particularly high risk	15.8	148.1	10.7	0.2	0.9	153.1
30	Covered bonds	-	-	-	-	-	-
31	Claims on institutions and corporates with a short-term credit assessment	-	-	-	-	-	-
32	Collective investments undertakings	-	-	-	-	-	-
33	Equity exposures	-	156.6	-	-	-	156.6
34	Other exposures	-	421.8	-	-	-	421.8
35	**Total standardised approach**	**280.3**	**14,308.8**	**123.3**	**29.2**	**44.4**	**14,465.8**
36	**Total**	**280.3**	**14,308.8**	**123.3**	**29.2**	**44.4**	**14,465.8**
37	Of which: Loans and advances	217.9	8,450.4	122.9	29.2	44.4	8,545.4
38	Of which: Debt securities	-	3,177.8	0.4	-	-	3,177.5
39	Of which: Off-balance-sheet exposures	62.4	2,102.1	-	-	-	2,164.5
	Of which: Other***	-	578.5	-	-	-	578.5

** Accumulated write-offs for the period October 2011 to December 2019*

*** Credit risk adjustment charges include additions (ECL movement) and new accounts.*

**** Other includes Equity and other exposures*

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EU CR1-B: Credit quality of exposures by industry or counterparty types € millions	Gross carrying values of							
	Defaulted exposures	*of which Past Due*	Non-defaulted exposures	Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs*	Credit risk adjustment charges**	Net values
Financial and Insurance Activities	2.1	1.9	5,698.8	3.2	-	0.9	0.9	5,697.6
Households and Individuals	51.6	36.3	2,919.8	24.2	-	3.9	8.8	2,947.2
Public administration and defence, compulsory social security	0.0	-	1,815.8	0.3	-	-	0.1	1,815.5
Wholesale and retail trade	29.5	20.9	674.2	15.3	-	1.5	4.6	688.5
Real estate activities	9.7	7.7	617.1	6.4	-	0.3	1.8	620.4
Construction	98.6	24.2	324.8	34.8	-	0.3	12.8	388.5
Others	88.4	40.2	2,258.3	38.6	-	22.3	15.4	2,309.1
Total	**280.3**	**131.3**	**14,308.8**	**122.7**	**-**	**29.2**	**44.4**	**14,465.8**

** Accumulated write-offs for the period October 2011 to December 2019*
** Credit risk adjustment charges include additions (ECL movement) and new accounts.

Note to EU CR1-B Table: The industry being quoted in this table is by NACE Level 1 of the debtor.

EU CR1-C - Credit quality of exposures by geography € millions	Gross carrying values of							
	Defaulted exposures	*of which Past Due*	Non-defaulted exposures	Specific credit risk adjustment	General credit risk adjustment	Accumulated write-offs*	Credit risk adjustment charges**	Net values
MALTA	279.5	130.6	11,358.5	122.7	-	29.2	44.1	11,514.5
GERMANY	-	-	397.9	0.0	-	-	0.0	397.9
FRANCE	-	-	240.7	0.0	-	-	0.0	240.7
BELGIUM	-	-	185.1	0.0	-	-	0.0	185.1
NETHERLANDS	-	-	178.6	0.0	-	-	0.0	178.6
UNITED KINGDOM	0.6	-	169.1	0.2	-	-	0.0	169.5
AUSTRALIA	-	-	150.4	0.0	-	0.0	0.0	150.4
OTHERS	0.3	0.3	1,628.4	0.3	-	0.0	0.2	1,628.5
Total	**280.3**	**130.9**	**14,308.8**	**123.3**	**-**	**29.2**	**44.4**	**14,465.8**

** Accumulated write-offs for the period October 2011 to December 2019*
*** Credit risk adjustment charges include additions (ECL movement) and new accounts.*

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The following table provides an ageing analysis of accounting on-balance sheet past due exposures regardless of their impairment status. None of the debt securities were past due as at end of the financial period 2019.

	EU CR1-D: Ageing of past-due exposures € millions	Gross carrying values					
		≤ 30 days	> 30 days ≤ 60 days	> 60 days ≤ 90 days	> 90 days ≤ 180 days	> 180 days ≤ 1 year	> 1 year
1	Loans	108.3	21.0	8.8	12.6	7.5	98.7
2	Debt securities	-	-	-	-	-	-
3	**Total exposures**	**108.3**	**21.0**	**8.8**	**12.6**	**7.5**	**98.7**

The Bank has instituted several units aimed at assisting obligors at an early stage and thereby helping to prevent deterioration into non-performing state. When the latter has already occurred or is deemed inevitable, other units focus on reducing, mitigating and/or recovering non-performing loans. Each unit, depending on the stage, exposure and severity of the relative Non-performing Loans (NPLs), has its internal procedures in order to strive towards achieving the desired results.

The Bank has in place policies and procedures regarding the management of NPLs. The NPL process warrants greater independence in the management of such exposures and to this effect, a specific department namely the Business Support Department discharges such responsibilities. The Non-performing Loans Committee monitors exposures displaying an increased likelihood of default.

During the financial year 2019, the Bank continued with its write-off exercise on non-performing loans wherein a number of exposures were transferred off-balance sheet. The Write-offs Committee is entrusted with the sanctioning of definite write-offs as per limits defined by the Board of Directors. The below tables provide a breakdown of the amount of exposures written-off during 2019 by number of days delinquent segregated by exposure class, economic sector and geography.

Exposures written off in 2019 (by exposure class) € thousands	Days Delinquent						Total	Specific credit risk adjustment	P&L Impact
	<= 30 days	> 30 days <= 60 days	> 60 days <= 90 days	> 90 days <= 180 days	> 180 days <= 1 year	> 1 year			
High Risk Areas	-	-	-	-	-	86.7	86.7	1.6	85.1
Past Due 90 Days+	489.0	0.2	0.7	0.2	16.5	1,861.6	2,368.3	999.6	1,368.8
Total	489.0	0.2	0.7	0.2	16.5	1,948.3	2,455.0	1,001.2	1,453.8

Exposures written off in 2019 (by economic sector) € thousands	Days Delinquent						Total	Specific credit risk adjustment	P&L Impact
	<= 30 days	> 30 days <= 60 days	> 60 days <= 90 days	> 90 days <= 180 days	> 180 days <= 1 year	> 1 year			
Accommodation and food service activities	0.5	0.1	0.7	-	0.8	19.7	21.8	4.3	17.5
Administrative and support service activities	1.8	-	-	0.1	-	171.7	173.6	116.5	57.2
Agriculture, forestry and fishing	2.9	-	-	-	-	60.8	63.6	1.6	62.1
Arts, entertainment and recreation	-	-	-	-	-	23.4	23.4	-	23.4
Construction	-	-	-	-	-	23.6	23.6	-	23.6
Electricity, gas, steam and air conditioning supply	-	-	-	-	-	0.1	0.1	-	0.1
Human health services and social work activities	-	-	-	-	0.1	-	0.1	-	0.1
Information and communication	-	-	-	-	-	7.4	7.4	-	7.4
Manufacturing	0.3	-	-	0.1	0.4	40.6	41.3	-	41.3
Other service activities	0.6	-	-	-	-	4.7	5.3	-	5.3
Households and Individuals	472.0	0.1	0.0	0.0	15.2	1,273.9	1,761.3	803.3	957.9
Professional, scientific and technical activities	-	-	-	-	-	19.8	19.8	-	19.8
Real estate activities	-	-	-	-	-	18.3	18.3	-	18.3
Wholesale and retail trade	10.9	-	-	-	0.1	284.3	295.3	75.5	219.8
Total	489.0	0.2	0.7	0.2	16.5	1,948.3	2,455.0	1,001.2	1,453.8

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Exposures written off in 2019 (by country) € thousands	**Days Delinquent**								
	<= 30 days	**> 30 days <= 60 days**	**> 60 days <= 90 days**	**> 90 days <= 180 days**	**> 180 days <= 1 year**	**> 1 year**	**Total**	**Specific credit risk adjustment**	**P&L Impact**
MALTA	489.0	0.2	0.7	0.2	16.5	1,948.2	2,455.0	1,001.2	1,453.8
RUSSIA	-	-	-	-	-	0.0	0.0	-	0.0
Total	489.0	0.2	0.7	0.2	16.5	1,948.3	2,455.0	1,001.2	1,453.8

Restructuring of facilities can occur under two scenarios. The first relates to a situation where the debtor has become problematic leading the Bank to grant concessions that it would otherwise not consider. In the other scenario, the customer does not have any financial difficulties but requests a restructuring in view of ongoing business model evolution.

Forbearance measures represent concessions granted by the Bank to borrowers when they are considered to be unable to meet the original terms and conditions of the contract due to financial difficulties. Through forbearance measures, the Bank may modify the terms and conditions of the contract to allow the borrower sufficient ability to service the debt or refinance the contract. Rigorous assessment is undertaken to ensure that restructuring is only allowed in those cases where the underlying fundamentals are sound and where the customer is expected to meet the revised obligations. When the concession is due to financial difficulty, the account is marked as forborne. As part of its asset quality measure, the Credit Risk Monitoring Unit (CRMU) reviews the financial difficulty tests and determines whether the facility is to be categorized as Forborne.

The table below provides an overview of non-performing and forborne exposures as at 31 December 2019.

EU CR1-E: Non-performing and forborne exposures € millions		**Gross carrying values of performing and non-performing exposures**						
			Of which performing but past due > 30 days and < = 90 days	**Of which performing forborne**	**Of which non-performing**			
						Of which defaulted	**Of which impaired**	**Of which forborne**
010	Debt securities	3,177.8	-	-	-	-	-	-
020	Loans and advances	8,639.4	25.2	22.3	217.9	-	217.9	92.7
030	Off-balance sheet exposures	2,164.5	NA	1.7	62.4	-	NA	0.9

€ millions		**Accumulated impairment and provisions and negative fair value adjustments due to credit risk**				**Collaterals and financial guarantees received**	
		On performing exposures		**On non-performing exposures**		**On non-performing exposures**	**Of which forborne exposures**
			Of which forborne		**Of which forborne**		
010	Debt securities	0.3	-	-	-	-	-
020	Loans and advances	28.6	2.0	79.8	34.9	138.1	0.4
030	Off-balance sheet exposures	6.6	-	9.2	-	-	-

In line with the Guidance to banks on non-performing loans (published in March 2017), information is being disclosed relating to forborne exposures as part of Annex 7 of the aforementioned guidance: Summary of supervisory reporting and disclosures related to NPLs - Table 5.

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Table 5a. Credit quality of forborne exposures € millions	All forborne exposures	of which: performing past due	of which: non-performing	*of which: impaired*	*of which: defaulted*	Impairment, provisions and value adjustments: Performing forborne exposures	of which: value adjustments	Non-performing forborne exposures	of which: value adjustments	Collateral and financial guarantees received on forborne exposures
Debt securities (including at amortised cost and fair value)	-	-	-	-	-	-	-	-	-	-
Central banks	-	-	-	-	-	-	-	-	-	-
General governments	-	-	-	-	-	-	-	-	-	-
Credit institutions	-	-	-	-	-	-	-	-	-	-
Other financial corporations	-	-	-	-	-	-	-	-	-	-
Non-financial corporations	-	-	-	-	-	-	-	-	-	-
Loans and advances (including at amortised cost and fair value)	115	22	39	-	53	2	-	35	-	0
Central banks	-	-	-	-	-	-	-	-	-	-
General governments	0	-	-	-	0	-	-	0	-	0
Credit institutions	-	-	-	-	-	-	-	-	-	-
Other financial corporations	1	0	0	-	0	0	-	0	-	0
Non-financial corporations	92	18	33	-	41	2	-	28	-	-
Households	23	4	6	-	12	0	-	7	-	-
DEBT INSTRUMENTS other than HFT	115	22	39	-	53	2	-	35	-	0
LOAN COMMITMENTS GIVEN	3	2	1	-	0	-	-	-	-	-
TOTAL EXPOSURES WITH FORBEARANCE MEASURES	118	46	80	-	106	4	-	69	-	1

Table 5c. Forborne exposures by credit category	<3 months	3-6 months	6-12 months	> 12 months
TOTAL EXPOSURES WITH FORBEARANCE MEASURES	3.4	1.5	11.7	98.4
of which: performing exposures	1.1	0.9	0.6	19.7
of which: non-performing exposures	2.3	0.6	11.1	78.7

6.5 Credit Risk Analysis and Mitigation

An assessment of the borrower's ability to service and repay the proposed debt is undertaken for each credit request and is a key element when considering an application for credit. In particular, before making any commitments, the Bank carries out an in-depth review of the borrower and ensures that it has a thorough knowledge of all the structural aspects of the borrower's operations and that adequate monitoring will be possible. Consideration is also given to the sector in which the borrower operates in terms of economic prospects and potential growth along with the Bank's sectoral default history.

The Bank has enhanced the identification of Early Warning Indicators by including a collection of variables leading to the early detection of potentially problematic borrowers or exposures and early identification of a significant increase in credit risk. The early detection of these higher risk debtors puts the Bank in a better position to manage the increased credit risk and avoid transition to default status.

Credit exposures are regularly reviewed for objective evidence of impairment, either individually or as part of a collective assessment, with a view to taking prompt recovery action. In addition, hindsight overviews are carried out on a sample basis by CRMU to strengthen the credit decision-making process wherein the judgement of the initial decision-makers is reviewed to determine the extent to which such decision-makers were in compliance with Bank policies and procedures in approving the credit application concerned. This ensures that the quality of the lending portfolio is properly and regularly monitored by an independent authority so that any necessary remedial action can be taken.

The granting of credit facilities is primarily based on the capacity, to repay rather than placing primary reliance on credit risk mitigants. The mitigation of credit risk is however a key aspect of effective risk management used to address the risk inherent in individual exposures. The nature and level of collateral required depends on a number of factors, including but not limited to: the amount of the exposure; the type of facility provided; the term of the facility; the amount of the counterparty's contribution; and an evaluation of the level of the credit risk or probability of default involved.

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Collateral is taken into account at a haircut which is applied to the market value and is only accepted as the main source of repayment in property development and other exceptional cases. The Collateral Policy includes details on the requirements of the appraisers and the valuation methodologies. Immovable properties held as collateral against material exposures are subject to regular revaluation in order to maintain a constant true picture of their values. The Bank also monitors the value of immovable properties regularly, mainly through the use of the Property Price Index. This ensures that the value being relied on as collateral adequately reflects the current value of the property. The Collateral Policy also includes details relating to the collateral valuations at recovery stage as well as those properties which are ready for disposal by the Bank.

In addition, the Collateral Policy also deals with other non-immovable collateral valuations and provides details on the processes, frequency of valuations of such collateral, and the different responsibilities of the relationship managers and relevant departments. The main types of collateral acceptable to the Bank are also articulated; in the main these are mortgages on properties (both residential and business), guarantees and financial instruments (such as debt securities and equities). The Policy refers to the categorization of collateral and classification of immovable property.

With reference to the information provided on Collateral in Note 39.2.1.5 of the financial statements, the main form of collateral held by the Bank in favour of both sanctioned and committed loan facilities is immovable property amounting to around 81.4% (53.5% Residential Property; 27.9%- Commercial Property). This is followed by guarantees and/or letters of comfort issued by the government (circa 10%). In line with the Collateral Policy, the creditworthiness of the guarantor is assessed prior to accepting guarantees as security, with different criteria taken into account when a value is extended on such guarantees, including the quality of the guarantor and the rating (if applicable).

At facility sanctioning stage, the Bank also mitigates credit risk through the adoption of terms and provisions known as covenants – both financial and non-financial – which allow the Bank to take action when a borrower's default risk increases. These may permit a reduction of the maximum amount of borrowing under the commitment, increases in collateral, repricing and, in a worst-case scenario, call-in of facilities.

Investment exposures and limits are regularly reviewed upon changes in credit ratings or outlook, so as to prompt any mitigating action that may be required. Credit risk in the investment portfolio is mitigated through limits set in the Treasury Management Policy (TMP). These limits are set on the level of credit risk undertaken in relation to any counterparty exposure in accordance with external ratings issued by major rating agencies. The TMP also sets limits in respect of settlements and derivatives.

Settlement risk is the risk of loss due to failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed. This risk is mitigated through settlement limits assigned to counterparties based on external credit ratings or by effecting payment on a delivery versus payment (DVP) basis.

6.5.1 Quantitative information on credit risk mitigation

The tables below provide information on the balance sheet exposure value (carrying amount net of provisions), that is covered by eligible collateral in line with CRR requirements. Tables below are segmented by exposure class, economic sector and country.

	EU CR3 - CRM techniques - Overview (by Exposure Class) € millions	**Exposures Total unsecured - Carrying amount**	**Exposures Total secured - Carrying amount**	**Exposures secured by Immovable Property collateral**	**Exposures secured by Financial Guarantees**	**Exposures secured by Credit Derivatives**	**Exposures secured by Other Eligible Collateral**
	Central governments or central banks	4,775.1	-	-	-	-	-
	Regional governments or local authorities	124.8	8.2	-	8.2	-	-
	Public sector entities	79.5	-	-	-	-	-
	Multilateral development banks	320.8	-	-	-	-	-
	International organisations	81.0	-	-	-	-	-
	Institutions	1,576.1	-	-	-	-	-
	Corporates	2,683.3	357.1	-	342.4	-	14.8
	Retail	1,413.7	74.9	-	0.5	-	74.3
	Secured by mortgages on immovable property	31.6	2,021.8	2,021.8	-	-	-
	Exposures in default	141.6	44.6	31.9	-	-	12.7
	Items associated with particularly high risk	132.7	20.4	14.4	-	-	6.1
	Covered bonds	-	-	-	-	-	-
	Claims on institutions and corporates with a short-term credit assessment	-	-	-	-	-	-
	Collective investments undertakings	-	-	-	-	-	-
	Equity exposures	156.6	-	-	-	-	-
	Other exposures	421.8	-	-	-	-	-
	Total	11,938.7	2,527.1	2,068.1	351.1	-	108.0
1	Total Loans and Advances	8,182.8	2,527.1	2,068.1	351.1	-	108.0
2	Total Debt Securities	3,177.5	-	-	-	-	-
	*of which: Other**	578.5	-	-	-	-	-
3	**Total exposures**	**11,938.7**	**2,527.1**	**2,068.1**	**351.1**	**-**	**108.0**
4	*of which Defaulted*	*141.6*	*44.6*	*31.9*	-	-	*12.7*

** Other includes Equity and other exposures*

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	EU CR3_SEC_CRM techniques - Overview (by Economic Sector) € millions	Exposures Total unsecured - Carrying amount	Exposures Total secured - Carrying amount	of which non-performing	Exposured secured by Immovable Property collateral	Exposured secured by Financial Guarantees	Exposured secured by Credit Derivatives	Exposures secured by Other Eligible Collateral
	Financial and Insurance Activities	5,415.4	282.2	1.4	20.7	254.4	-	7.1
	Households and Individuals	1,199.0	1,748.3	33.0	1,697.2	-	-	51.1
	Public administration and defence, compulsory social security	1,806.8	8.7	-	0.6	8.0	-	0.1
	Wholesale and retail trade	600.7	87.8	16.4	75.6	0.5	-	11.7
	Real estate activities	431.4	189.1	4.4	101.2	84.8	-	3.1
	Construction	352.1	36.5	40.8	30.4	-	-	6.0
	Others	2,134.0	174.6	90.2	142.4	3.4	-	28.8
	Total	11,939.4	2,527.1	186.2	2,068.1	351.1	-	**108.0**
1	of which: Total Loans and Advances	8,182.8	2,527.1	186.2	2,068.1	351.1	-	**108.0**
2	of which: Total Debt Securities	3,177.5	-	-	-	-	-	**-**
	*of which: Other**	578.5	-	-	-	-	-	**-**
3	**Total Exposures**	**11,938.7**	**2,527.1**	**186.2**	**2,068.1**	**351.1**	**-**	**108.0**
4	*of which Defaulted*	*141.6*	*44.6*	*186.2*	*31.9*	-	-	**12.7**

** Other includes Equity and other exposures*

	EU CR3_GEO - CRM techniques - Overview (by Country) € millions	Exposures Total unsecured - Carrying amount	Exposures Total secured - Carrying amount	of which non-performing	Exposured secured by Immovable Property collateral	Exposured secured by Financial Guarantees	Exposured secured by Credit Derivatives	Exposures secured by Other Eligible Collateral
	MALTA	9,005.7	2,508.8	185.6	2,050.8	351.1	-	106.9
	GERMANY	397.5	0.4	-	0.4	-	-	0.0
	FRANCE	239.8	0.9	-	0.9	-	-	0.0
	BELGIUM	184.8	0.3	-	0.3	-	-	-
	NETHERLANDS	178.4	0.2	-	0.2	-	-	0.0
	UNITED KINGDOM	163.8	5.7	0.4	5.5	-	-	0.1
	AUSTRALIA	149.8	0.6	-	0.6	-	-	0.0
	OTHERS	1,618.2	10.3	0.2	9.4	-	-	0.9
	Total	11,938.7	2,527.1	186.2	2,068.1	351.1	-	**108.0**
1	of which: Total Loans and Advances	8,182.8	2,527.1	186.2	2,068.1	351.1	-	**108.0**
2	of which: Total Debt Securities	3,177.5	-	-	-	-	-	**-**
	*of which: Other**	578.5	-	-	-	-	-	**-**
3	**Total Exposures**	**11,938.7**	**2,527.1**	**186.2**	**2,068.1**	**351.1**	**-**	**108.0**
4	*of which Defaulted*	*141.6*	*44.6*	*186.2*	*31.9*	-	-	**12.7**

** Other includes Equity and other exposures*

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	EU CR4 – Standardised approach – Credit risk exposure and CRM effects € millions	Exposures net of provisions before CCF and CRM		Exposures post CCF and CRM		RWA after SME factor and RWA density	
		On-Balance sheet amount	Off-Balance sheet amount	On-Balance sheet amount	Off-Balance sheet amount	RWAs	RWA density
1	Central governments or central banks	4,763.4	11.7	4,763.4	1.0	2.1	0.0%
2	Regional government or local authorities	128.4	4.6	128.4	0.9	31.7	24.5%
3	Public sector entities	79.5	-	79.5	-	39.8	50.0%
4	Multilateral development banks	320.8	-	320.8	-	-	0.0%
5	International organisations	81.0	-	81.0	-	-	0.0%
6	Institutions	1,559.5	15.8	1,560.2	1.7	489.0	31.3%
7	Corporates	1,690.3	1,350.1	1,333.0	174.0	1,387.1	92.0%
8	Retail	841.9	646.7	767.0	57.1	585.7	71.1%
9	Secured by mortgages on immovable property	2,053.4	-	2,053.1	-	756.7	36.9%
10	Exposures in default	132.9	53.2	120.3	12.3	159.3	120.1%
11	Exposures associated with particularly high risk	86.0	67.1	79.8	2.1	122.9	150.0%
12	Covered bonds	-	-	-	-	-	0.0%
13	Institutions and corporates with a short-term credit assessment	-	-	-	-	-	0.0%
14	Collective investment undertakings	-	-	-	-	-	0.0%
15	Equity	156.6	-	156.6	-	187.3	119.6%
16	Other items	421.8	-	421.8	-	337.9	80.1%
17	**Total**	**12,316.5**	**2,149.3**	**11,865.1**	**249.2**	**4,099.4**	**33.8%**

	EU CR5: Standardised approach Exposure Value € millions	EAD prior CRM	Risk Weight									
			0%	4%	20%	35%	50%	75%	100%	150%	250%	Total
1	Central governments or central banks	4,775.3	4,754.0	-	10.4	-	-	-	-	-	-	4,764.4
2	Regional government or local authorities	133.1	10.9	-	108.4	-	-	-	10.0	-	-	129.3
3	Public sector entities	79.5	-	-	-	-	79.5	-	-	-	-	79.5
4	Multilateral development banks	320.8	320.8	-	-	-	-	-	-	-	-	320.8
5	International organisations	81.0	81.0	-	-	-	-	-	-	-	-	81.0
6	Institutions	1,576.2	-	1.7	1,015.0	-	533.3	-	6.7	9.0	-	1,566.0
7	Corporates	3,061.3	-	-	87.5	-	83.4	-	1,337.5	-	-	1,508.5
8	Retail	1,500.4	-	-	-	-	-	824.2	-	-	-	824.2
9	Secured by mortgages on immovable property	2,054.6	-	-	-	1,718.5	334.6	-	-	-	-	2,053.1
10	Exposures in default	264.5	-	-	-	-	-	-	79.2	53.4	-	132.6
11	Exposures associated with particularly high risk	163.9	-	-	-	-	-	-	-	81.9	-	81.9
12	Covered bonds	-	-	-	-	-	-	-	-	-	-	-
13	Institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-	-	-	-
14	Collective investment undertakings	-	-	-	-	-	-	-	-	-	-	-
15	Equity	156.6	48.6	-	-	-	-	-	55.2	-	52.9	156.6
16	Other items	421.8	175.8	-	1.8	-	-	-	182.0	-	62.2	421.8
17	**Total**	**14,589.1**	**5,391.1**	**1.8**	**1,223.4**	**1,718.5**	**1,030.9**	**824.2**	**1,670.7**	**144.3**	**115.1**	**12,119.8**

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EU CR5.1_Credit Quality Step Exposure Value € millions		EAD prior CRM	Credit Quality Step 1	2	3	4	5	Not applicable	Total
1	Central governments or central banks	4,775.3	476.6	699.6	112.8	-	0.0	3,475.3	4,764.4
2	Regional government or local authorities	133.1	112.9	5.4	-	-	-	11.1	129.3
3	Public sector entities	79.5	-	79.5	-	-	-	-	79.5
4	Multilateral development banks	320.8	320.3	-	-	-	-	0.5	320.8
5	International organisations	81.0	81.0	-	-	-	-	-	81.0
6	Institutions	1,576.2	312.2	699.2	52.8	9.0	-	492.8	1,566.0
7	Corporates	3,061.3	47.9	122.9	44.1	-	-	1,293.5	1,508.5
8	Retail	1,500.4	-	-	-	-	-	824.2	824.2
9	Secured by mortgages on immovable property	2,054.6	-	-	-	-	-	2,053.1	2,053.1
10	Exposures in default	264.5	-	-	-	-	-	132.6	132.6
11	Exposures associated with particularly high risk	163.9	-	-	-	-	-	81.9	81.9
12	Covered bonds	-	-	-	-	-	-	-	-
13	Institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-
14	Collective investment undertakings	-	-	-	-	-	-	-	-
15	Equity	156.6	26.7	-	-	0.6	-	129.4	156.6
16	Other items	421.8	-	-	-	-	-	421.8	421.8
17	**Total**	**14,589.1**	**1,377.6**	**1,606.7**	**209.8**	**9.6**	**0.0**	**8,916.2**	**12,119.8**

6.6 Counterparty Credit Risk

The CRR defines 'counterparty credit risk' (CCR) as the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. The Group is exposed to CCR through over-the-counter (OTC) derivative exposures which are used to hedge against adverse interest rate and currency movements. To calculate the CCR, the Group follows the Mark-to-Market approach (as defined in CRR, Article 274) where a predefined add-on is summed up to the current positive fair value of the contract, taking into consideration the netting arrangements in place. This is prepared with the purpose of accounting for potential future changes (as per CRR, Article 298). By means of such netting arrangements, the positive and negative fair values of the collateral owed on derivatives contracts included under a master agreement can be offset against each other. This netting process reduces the credit risk and settlement risk to a single net claim on the party to the contract (close-out netting). The gross positive fair value of contracts is equivalent to the “Replacement cost” which amount is tabled in the following table.

EU CCR1 - Analysis of CCR exposure by approach € millions		Notional	Replacement cost/current market value	Potential future credit exposure	EEPE	Multiplier	EAD post CRM	RWAs
1	Mark to market		1.32	3.44			5.52	2.46

EU CCR3 – Standardised approach – CCR exposures by regulatory portfolio and risk
€ millions

	Exposure classes	EAD prior CRM	Risk Weight 0%	2%	4%	10%	20%	35%	50%	70%	75%	100%	150%	Others	Total	of which unrated
6	Institutions	4.06	-	-	0.07	-	0.15	-	0.78	-	-	-	-	-	1	
7	Corporates	0.34	-	-	-	-	-	-	-	-	-	0.34	-	-	0.34	0.34
10	Other items*	1.12	-	-	-	-	-	-	-	-	-	1.12	-	-	1.12	1.12
11	**Total**	**5.52**	**-**	**-**	**0.07**	**-**	**0.15**	**-**	**0.78**	**-**	**-**	**1.46**	**-**	**-**	**2.46**	**1.46**

**These include derivatives which serve as ‘back-to-back’ to derivatives created for Collective Investment Schemes.*

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EU CCR8 - Exposures to CCPs **€ millions**		**a**	**b**
		EAD post CRM	**RWAs**
1	Exposures to QCCPs (total)		0.07
2	Exposures for trades at QCCPs (excluding initial margin and default fund contributions); of which	1.76	0.07
4	(ii) Exchange-traded derivatives	1.76	0.07
12	Exposures for trades at non-QCCPs (excluding initial margin and default fund contributions); of which	3.76	2.39
13	(i) OTC derivatives	3.76	2.39

Internal limits and collateral management procedures are in place to address situations where the probability of default of a particular counterparty is positively correlated to the exposure with the same counterparty. This is referred to as wrong-way risk, whereby both the mark-to-market exposure and the riskiness of the counterparty, increase simultaneously. The TMP, which sets the limits on the maximum exposures held in derivatives, assumes that the business relationship with most counterparties is an ongoing one; therefore the limits are primarily based on the worst long-term credit rating of the counterparty. Requests falling outside the TMP are also reviewed by Credit Risk Sanctioning Department and approved by the Chief Risk Officer or the BoD according to the magnitude of exposure. Limits are reviewed annually or more frequently in the event of a downgrade of the counterparty. The Financial Control Department monitors on a monthly basis the hedge effectiveness of the Bank's derivatives.

The Bank ensures that an International Swaps and Derivatives Association (ISDA) agreement with the respective counterparties is in place prior to effecting a transaction and that the agreement covers the deal in question. Furthermore, in order to secure the collateral, the Bank enters into an agreement with the counterparties in accordance with the Credit Support Annex (CSA) under the ISDA agreement. The CSA is a schedule to the ISDA Master Agreement. By virtue of such CSAs, a party to a derivative who has exposure to its counterpart will post collateral to cover such exposure by way of an outright title transfer of such collateral. All CSAs held by the Bank are of a two-way nature. Variation margin is exchanged on a daily basis.

The Credit Rating Downgrade Threshold clause in some CSA agreements is designed to trigger a series of events which may include the termination of transactions by the non-affected party if the credit rating of the affected party falls below a specified level. Nevertheless, the amount of collateral posted will not change in the event the Bank suffers a credit rating downgrade. The Bank does not have any credit derivative hedges in place, neither relating to its own credit portfolio, nor in order to conduct intermediation activities. It does not hold any credit reserves with respect to counterparty credit risk since the collaterals and margins in place are deemed to suffice.

EU CCR5-B - Composition of collateral for exposures to CCR **€ millions**	**Collateral used in derivative transactions**			
	Fair value of collateral received		**Fair value of posted collateral**	
	Segregated	**Unsegregated**	**Segregated**	**Unsegregated**
Cash	0.13		37.34	
Total	**0.13**		**37.34**	

The collateral element listed in table EU CCR5-B is used purely for risk-mitigation; it is used to support (and not to reduce further) CCR exposures.

'Credit Valuation Adjustment' (CVA) is defined by the CRR as an adjustment to the mid-market valuation of the portfolio of transactions with a counterparty. This adjustment reflects potential mark-to-market losses due to counterparty migration risk on bilateral OTC derivative contracts. The CVA charge is computed in accordance with the Standardized Method as defined in Article 384 of the CRR.

EU CCR2 – CVA capital charge **€ millions**		**Exposure value**	**RWAs**
4	All portfolios subject to the standardised method	5.52	1.12
5	**Total subject to the CVA capital charge**	**5.52**	**1.12**

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Section 7: Market Risk

7.1 Nature of Market Risk

Market risk is the risk that the Bank's earnings or capital will be adversely affected by the volatility of market rates or prices such as interest rate, credit spread and foreign exchange rates. The Group's exposure to market risk is limited given that it does not operate a trading book. Accordingly, the Group's exposure to market risk comprises three types of risk: (i) interest rate risk in the banking book; (ii) currency risk; and (iii) equity price risk.

7.2 Interest Rate Risk in the Banking Book

Interest rate risk is defined as the financial losses incurred due to adverse movements in interest rates. The Bank is exposed to Interest Rate Risk in the Banking Book (IRRBB) from mismatches between interest rate sensitive assets and liabilities held in the banking book, both in terms of economic value and an earnings perspective.

The Interest Rate Risk Policy which is revised from time to time, clearly describes the approaches through which interest rate risk is identified, evaluated, monitored, managed, and reported to higher management. The Policy also outlines the structure, responsibilities and controls that manage and oversee the institution's interest rate positions.

The BoD is ultimately responsible for the interest rate risk assumed by the Bank and the manner in which this risk is managed to ensure that it is aligned with the interest rate risk strategy and risk appetite.

The Bank's exposure to interest rate risk is monitored and evaluated on a monthly basis by the Asset Liability Management Committee (ALCO). The role of ALCO is that of managing the balance sheet to attain an optimal balance between risk and return. ALCO assesses the interest rate risk with the objective of limiting potential adverse effects of interest rate movements on net interest income and on equity.

7.2.1 The Measurement of Interest Rate Risk

Risk management processes are in place to manage and control the interest rate risk exposure without negatively affecting organizational profitability. The Bank takes two different, yet complementary perspectives to the process of controlling and assessing IRRBB. These are the economic value of equity (EVE) and the earnings-based approach. The EVE approach measures the interest rate risk by observing the change in the theoretical value of the banking book. On the other hand, the earnings-based approach focuses on the impact on the net interest income following changes in the interest rates.

Impact on the Economic Value of Equity

As the interest rate increases/decreases, the monetary value of owning an instrument offering a fixed rate of interest decreases/increases. If this position is not perfectly offset by changes in the value of other instruments held by the Bank an economic loss materializes. Such open positions mostly result from differences in the nominal/principal values, varied residual terms to maturities, and different interest rate reset dates.

The economic loss (or gain) is estimated through the interest rate term structure – commonly referred to as the yield curve – which measures the relationship between the discount rates and the time to maturity. Changes to the yield curve are a reflection of the anticipated future interest rates, inflation, and economic growth. The discount rate provides the present value of the Bank's expected future cash flows. It is representative of a risk-free yield curve and this is generally a representation of either the secured interest rate swap curve or, in the absence of such, a high credit rating government yield curve.

In case of positions with no contractual maturity, the Bank regularly monitors the behaviour of non-maturity deposits (NMDs). Statistical evidence shows that even though NMDs do not have a specific contractual maturity, a significant share of the on-demand deposits is stable over time even when market rates change. The element of NMDs which is considered to be particularly stable – core deposits – is spread into different short-term and medium-term time buckets based on the customer.

For exposures with implicit optionality, where the customer has the legal right to repay early, the pattern exhibited over the preceding 12 months is used as the basis for forecasting the expected cash flows. This method implicitly assumes that the behavioural pattern is to a significant degree repeated from time to time, and is to remain substantially true under different market conditions.

Impact on the Net Interest Income

Changes in the interest rates affect the sensitivity of earnings in the short term by changing its net interest income and the level of other interest sensitive income and expenses. This approach provides information necessary to manage and optimize the risk-return position as well as the structure of the balance sheet from an earnings-based point of view.

ALCO monitors on a regular basis the current rates being paid on liabilities and the rates earned on assets. This method allows management to effectively monitor the interest earning potential of the present balance sheet as well as tracking its evolution over time.

In alignment with the risk-averse approach driven by the relative risk appetite framework (RAF) metrics, in selecting and updating the mix of investment portfolio assets held, the quality of the assets is prioritized over the return. Accordingly, the investment portfolio is prevalently composed of very high quality but relatively low yield assets.

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On a regular basis the sensitivity of the financial assets and liabilities to parallel shifts in the yield curve of 200 basis points over a time horizon of one year is also monitored. Interest rate risk arises from the different re-pricing characteristics of the Bank's interest-sensitive assets and liabilities and from the mismatch between interest rate-sensitive assets and liabilities.

Interest Rate Risk - Simulations and IRRBB capital charge	Sensitivity of reported equity to interest rate movements		Sensitivity of projected net interest income to interest rate movements	
€ millions	200bp Parallel increase	200bp Parallel decrease	200bp Parallel increase	200bp Parallel decrease
At 31 December 2019	**22.0**	**23.0**	**(29.3)**	**(63.0)**
Of which:				
EUR	30.0	24.0	(38.8)	(52.0)
USD	(13.0)	-	3.9	(4.0)
GBP	3.0	(1.0)	2.4	(2.0)
AUD	1.0	-	-	-
Other Currencies	1.0	-	4.0	(5.0)
At 31 December 2018	**26.0**	**5.0**	**5.0**	**(60.0)**
Of which:				
EUR	44.0	(14.0)	(15.0)	(42.0)
USD	(9.0)	11.0	11.0	(11.0)
GBP	(3.0)	-	5.0	(3.0)
AUD	(7.0)	7.0	(5.0)	(5.0)
Other Currencies	1.0	-	9.0	1.0

Simulations and IRRBB capital charge

In line with regulatory requirements – EBA/GL/2018/02 – the IRRBB EVE model, 6 prescribed interest rate shock scenarios are simulated for supervisory outlier test purposes. The table above depicts the sensitivity for a ±200bps parallel shift of reported equity and projected net interest income to the interest rate movements, split by currency. Moreover, the 6 prescribed shocks (EVE) and parallel shifts in net interest income (NII) are carried out for various magnitudes, for capital quantification purposes. These simulations are generated every quarter and subsequently reported to ALCO.

As at December 2019, the capital charge with respect to the IRRBB approximated €22.98 million. The ultimate capital charge is derived by reference to a twenty-year historic data series to determine the probability of occurrence of the net yearly interest rate shifts of different magnitudes, segmented into four buckets of: 25, 75, 125, 200 bps, respectively. The probability-weighted capital sensitivity is derived by multiplying the capital add-on at each one of the four magnitudes by the relative probability of occurrence. The probability-weighted sensitivities are then summed up; this is done under both EVE and NII approaches. The highest probability-weighted sensitivity arising out of the two approaches, is adopted as the ultimate capital allocation.

7.3 Currency Risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument would fluctuate because of changes in foreign exchange rates. The Treasury Management Policy sets limits on the level of net exposure by currency which are monitored on a daily basis. Further information related to currency risk is found in the notes to the financial statements Note 39.4.2.

7.4 Exposures to equities not included in the trading book (CRR Article 447)

The Group is exposed to equity price risks arising from the holding of equity instruments classified either as fair value through other comprehensive income (FVOCI) or at fair value through profit or loss (FVTPL). The overall strategy of the equity portfolio is to earn regular dividends and not invest in highly volatile equities. The investment portfolio has a relatively small allocation to equity investments which approximated €55 million as at end-December 2019.

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All equities are marked to market from time to time; however price changes are passed through the income statement for equities classified within the FVTPL portfolio, whereas for those classified within the FVOCI portfolio, price changes are accounted for in other comprehensive income. The fair value of all equities corresponds to their market value and there were no material deviations between the two. During financial year 2019:

- Fair value movement on FVTPL equity holdings amounted to: €5.0 million;
- Fair value movement through reserves – FVOCI Equities: €4.7million;
- Gain/Loss on FVOCI Equities transferred to Retained Profits during 2019: Nil;
- Latent revaluation gains / losses included in Common Equity Tier 1 Capital amount to €14.7 million.
- The total unrealized gains on equities for FY 2019 amounts to €9.7 million

The Bank also has exposures to private equities. These amounted to €0.36 million as at end-December 2019, split into €0.19 million in Venture Capital and €0.17 million in Non-Trading Equity.

The Bank's equity holdings are split between holdings in shares of locally exchange-traded companies which amount to €33.5 million. Approximately €23 million of equity investments are in corporate firms, whereas approximately €10 million of the aforementioned investments are in financial institutions / other financial corporations.

Section 8: Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, which can lead to adverse customer impact, reputational damage or financial loss. Operational risk is inherent to all business lines, support functions, products, activities, processes and systems. Failure to manage operational risk can result in direct or indirect financial loss, reputational impact, regulatory censure, or failure in the management of other risks such as credit or market risk.

The Risk Appetite Framework prescribes that the Group aims to minimise operational risk whilst ensuring that its operations are regulatory compliant, efficient and cost-effective. This is achieved through early identification, measurement monitoring and mitigation of risk by ensuring that adequate and effective controls are in place, supported by appropriate capital and/or insurance arrangements.

Operational risk arises from day-to-day operations and may impact any business line or function within the Group. Operational Risk can manifest itself in a number of ways and can take various forms including but not limited to fraud (internal/external), non-availability of latest technology, loss of data, staff absenteeism on large scale, natural disaster and system failures or process malfunction. Operational risks are mostly process, systems or people related albeit operational risk may arise equally from failure to embrace regulatory changes.

8.1 The Management of Operational Risk

In line with common industry practice, BOV applies the three lines of defence model for operational risk governance. Operational risk is managed across the Group through an operational risk framework and procedures. The operational risk framework which has been updated includes a risk control assessment process, risk impact likelihood analysis, key risk and control indicators, risk appetite, an event management and operational loss process. The Operational Risk Management Unit (ORMU) which is the second line of defence acts independently from risk generating business lines. It is primarily tasked with delivering and upholding a robust operational risk management framework and culture across the BOV Group. Although ownership and accountability for operational risk resides with business, the ORMU co-ordinates, supervises and provides direction for the consistent identification, assessment, monitoring and reporting on operational risks and controls. The unit is responsible for the design, development, delivery and continuous improvement of the operational risk management framework through the provisioning of the appropriate infrastructure, tools and methodology for rolling out operational risk management throughout the Group, ensuring that the overall risk portfolio is managed in line with the operational risk management policy. The identification and assessment of operational risk exposure across the various business lines is primarily upheld through risk and control assessments. Risk assessments involve the identification and evaluation of risks, including recommendations for managing and mitigating such risks. To support the risk identification process the Bank makes use of audit findings, internal loss data and scenario analysis. Operational risk exposures are mapped to the Group Risk Register which comprises key risks originating from forty-seven process areas. The process of cataloguing risks is designed to confirm that risks have been identified, assessed and are being managed effectively in accordance with the Bank's Operational Risk Management Policy.

ORMU maintains a repository of loss data which captures and records operational risk loss events and near misses. Loss data is used for regulatory and management reporting purposes. It is also relevant in capital modelling when calculating capital for Pillar II Operational risks. Events which are considered material are assessed and escalated to Senior Executive Management to ensure that remedial action is taken to avoid repeated incidents of similar nature.

ORMU is also responsible for ensuring that the Group is resilient and has contingencies in place in the event of business disruption.

The Group has in place a robust enterprise-wide Business Continuity Plan (BCP) which extends across all critical business lines and functions. BCPs for critical activities and IT systems are regularly tested, thus ensuring timely recovery from disruptions and expedite access to data.

ORMU is in the process of strengthening and modernising completely its management of operational risk through the acquisition of a dedicated Operational Risk Management system that consolidates information related to risks, loss events and controls. The implementation of this system will enhance the Group's risk culture and maturity of its operational risk framework. This would enable the Group adopt a more proactive, forward looking and effective approach in managing risks.

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The Group currently uses the Basic Indicator Approach to apportion capital for operational risk and accordingly allocates 15% of the average gross income over three years in line with Basel III guidelines.

The operational risk regulatory capital requirement for the Group as at December 2019 is €37.4 million (Notional Risk Weighted Assets €467.5 million).

8.2 Monitoring and Mitigation of Operational Risk

The Group continues to invest in strengthening its control environment leveraging on automation to optimise the efficiency and effectiveness of the control design. Material risks are reported and escalated to the Group's governance structures in order to give Executive Management and Board Committee member's visibility of these risks and a medium to ensure that corrective action, to lower risk exposure, has been taken. The treatment and mitigation of risk is key to ensure that the Group risk profile remains within the risk appetite. The Group employs a mix of risk mitigation strategies, including avoidance, mitigation, transfer (through insurance) and acceptance. Given the nature and magnitude of the threat the Group decides which strategy would be a best fit to lower the likelihood and financial impact arising from a risk event. High impact risk events are mitigated through comprehensive insurance coverage. The Group has different classes of Insurance covers to protect the Group's assets and core operations. A specialised team within Risk Management works in close liaison with the Group's Insurance Brokers and the Group's different business units to ensure that the insurance cover held aligns with the Group's risk profile.

The monitoring and reporting of operational risk is primarily undertaken by ORMU. The Group maintains a formal approach to operational risk event escalation, whereby material events are identified, captured and if required escalated to the Group's governance structure. Event root cause analysis is carried out to determine, where possible, any mitigation plans needed to ensure that the control framework remains effective and meet ongoing threats and any emerging risks.

8.3 Information Security Risk

Information security risk refers to the risk of loss caused by deliberate or accidental loss, alteration, falsification or leakage of information, or by destruction, disruption, errors or misuse of information systems. The Group adopts various international standards in its integrated approach to managing information security and privacy risks amidst threats that exploit increasing complexity and connectivity of systems. Such efforts have the fundamental objective of ensuring the confidentiality, integrity, availability and privacy of the Group's information assets.

In order to fulfil the proper processing of information assets and prevent loss or leakage of information, the Group has developed a number of qualitative measures to reduce such risks through its organisational structure. Such implementations include

- Effective governance through a security organisational structure, with resources having specific responsibilities for information security issues,
- The establishment of information security policies, procedures and standards,
- An information security awareness and training programme
- The implementation of a security infrastructure and systems to ensure a stable information security environment.

This approach to the management of information security risks seeks to align to global standards, in particular ISO/IEC 27001/2.

The Group has invested a significant amount of human capital towards its new Core Banking System which was implemented at the end of FY2019. This implementation ensures confidentiality, integrity and availability of information assets as well as providing a foundation for upcoming secure service offerings.

As part of the ongoing commitment towards ensuring the security of information systems, the Group will be focusing on the prevalent Information Security risks within the industry; which include logical access control management. Further to the significant cyber incident in February 2019, the Group has invested significantly in strengthening its security framework. This investment will continue so as to be proportionate with the Group's regulatory obligations and evolving cyber threat landscape.

8.3 Bank's Preparedness to Covid-19

The Bank has been monitoring the unfolding of events in relation to the outbreak of the new strain of corona virus since it was first reported in Wuhan, Hubei Province of China. A dedicated management response team, which is co-ordinated by Risk Management and which has representation from various key stakeholders across the Group, is screening and assessing the impact on banking operations, taking appropriate precautionary measures commensurate with the scale of the spreading of Covid-19.

The Bank is following closely the recommendations and directions issued by the superintendence of Public Health in Malta, including the frequent bulletin updates issued by the World Health Organisation.

The level of Bank's preparedness to a pandemic is resilient to a number of stress scenarios designed on varying degree of staff absenteeism. Once a level of overall staff absenteeism reaches pre-set thresholds or there is a concentration in any one function the Bank will initiate the corresponding Business Continuity Plan.

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Section 9: Remuneration Policy

The Bank has a Remuneration Policy aimed at aligning individual rewards with the Bank's performance, business strategy, risk appetite, values and long-term interests. It also encourages a prudent approach to risk taking. The Policy deals with the remuneration of all staff members including members of the MB, in accordance with regulation incorporated in the Capital Requirements Directive. Additional disclosures on the governance process related to remuneration have been made under the Remuneration Report section in this report.

The target population defined as Identified Staff for the purposes of this Disclosure represents 6.1% of total number of employees in the Group. Identified staff is determined in line with recommended EBA Regulatory Technical Standards[1] and includes:

- senior executives responsible for material business units/business lines or internal control functions including Risk, Compliance and Audit;
- executives of Support Functions;
- other employees who are members of committees with collective authority to commit to risk exposures per transaction beyond 0.5% of CET1 Capital; and
- employees who, individually or as part of a committee take, approve or veto decisions on new products, material processes or material systems.

For the purposes of remuneration, Identified Staff have been split into business areas according to EBA guidelines[2]. The table below includes the total fixed and variable remuneration and the number of beneficiaries for each business area. All fixed and variable remuneration were paid in cash.

Remuneration of Identified staff	Supervisory Function^	Management Function^	Investment Banking^	Independent Control Functions^	Retail Banking^	Asset Management^	Corporate Functions^	All Other^
Management Body	14	7						
Number of identified staff (IF)			4	28	42	2	16	2
IF in senior management positions			1	6	21	1	14	Nil
Total fixed remuneration	€ 400,000	€ 905,214	€ 268,237	€ 1,595,829	€ 2,871,635	€ 180,272	€ 1,152,234	€ 127,153
Total variable remuneration	Nil	€ 9,912	€ 8,836	€ 73,783	€ 128,841	€ 4,649	€ 42,830	€ 9,576
Variable to Fixed Remuneration Ratio	Nil	1.09%	3.29%	4.62%	4.49%	2.58%	3.72%	7.53%

^as defined in EBA guidelines EBA/GL/2014/8. None of the employees individually earn over €500,000. There are no amounts of outstanding deferred remuneration and no deferred remuneration was awarded during the financial year.

The figures in the table differ from the amounts shown in Section 3.3 as the methodology is different and not strictly comparable.

The above figures include the Bank's subsidiaries – BOVFS and BOVAM

Notes to the Table:

- the fixed remuneration of the management function and the retail banking function includes the amounts of €95,000 and €85,000 respectively, representing remuneration earned for additional roles performed within the supervisory function across the Group
- the variable remuneration of the management function includes also remuneration earned from a SICAV
- variable remuneration for identified staff includes performance related bonuses and other discretionary benefits.
- None of the employees individually earn over €500,000
- There are no amounts of outstanding deferred remuneration and no deferred remuneration was awarded during the financial year
- The Management Function of the Management Body was composed of 8 members on 31 December 2019, however one member is not reflected in the headcount due to the fact that he was appointed in November.

Link between Pay and Performance

The variable portion of remuneration is linked to the level of profit earned by the Bank during the relative financial period. The calculation of the bonus attributed to the staff in the clerical and managerial grades is determined in the Collective Agreement and is based on the profit achieved by the Bank. The bonus is distributed to employees in proportion to the performance achieved by the individual and in accordance with their respective grades. Employees in the executive grade are also eligible for an annual bonus determined by the Bank's performance and their individual performance. Annual bonus entitlements are also applicable to the CEO

[1] EBA Final Draft Regulatory Technical Standards EBA/RTS/2015/09 dated 16 July 2015
[2] EBA Guidelines on the remuneration benchmarking exercise EBA/GL/2014/08 dated 16 July 2014

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and members of the MB as highlighted under the Remuneration Report. The Bank does not pay variable remuneration in equity, equity-linked or other eligible instruments to any category of staff.

The application of the proportionality principle, according to instructions publishes by the Malta Financial Services Authority (MFSA) in 2015, prescribes that the provisions of CRR relating to variable pay in instruments and deferral rule are to be fully applied if an individual staff member is remunerated with a variable pay of more than €100,000, or for lower values where variable pay is more than 100% of the fixed pay of the individual concerned.

Performance Management System

Key Performance Indicators (KPIs), by which employees' performance is measured, provide individual, unit and organisation level targets aligned with the strategic objectives of the Group.

In order to avoid rewarding individuals for taking excessive risks, KPIs have been designed to account for the Group's long term interest and values, with quality and compliance measures receiving a strong weighting at target setting stage. Financial and non-financial performance indicators are based on a balanced scorecard approach and therefore, financial targets are counterbalanced by process, customer satisfaction and employee development measures. In line with principles set out in the Remuneration Policy, the Bank exercises focus on quality and compliance centric measures, so as to promote moderation and consideration of risk-taking within the Group's business areas. Performance targets are reviewed periodically to ensure that these are aligned to specific strategic and operational objectives set out by the Board of Directors, covering not only business generation, but also other areas of importance such as compliance with prevalent regulation and internal policies and procedures, on boarding and customer due diligence, non-performing borrowing, quality of service and others.

Section 10: Liquidity Risk

During 2017, the EBA issued guidelines – EBA/GL/2017/01 – which aim to harmonize the disclosures in line with CRR 575/2013 Article 435(1) in relation to liquidity risk. Additional disclosures relating to liquidity risk are provided in Note 39.3 to the financial statements.

Liquidity risk is the risk that a bank is unable to meet its current or future payment obligations as they fall due, and/or to replace at reasonable cost funds when they are withdrawn, even when this occurs unexpectedly. Funding liquidity risk arises when a bank is not able to efficiently meet various cash flow and collateral needs without affecting its daily operations and/or financial position. In contrast, market liquidity risk arises when a bank is not able to easily offset or eliminate positions at the market price because of inadequate market depth and/or market disruption. The Bank has always taken the management of liquidity risk very seriously; to this end, the objective of the Bank's liquidity risk management actions is to ensure that both foreseeable and unpredicted funding commitment can be met when due and at a reasonable cost.

Responsibility for the management of liquidity risk is delegated to the Asset and Liability Committee (ALCO), which is responsible to oversee the Group's balance sheet mix, to achieve an optimal balance between risk and return. The ALCO also gives guidance on risk and return to the business and exercises executive authority in the area of interest rate management by setting base rates and rates payable on retail deposit products. The Enterprise Risk Management Unit (ERMU), ensures that prudent parameters are established within which sound liquidity risk management and control activities are carried out by the respective risk and control owners. The unit selects, adopts, implements, and updates appropriate liquidity risk models, metrics, and other risk evaluation tools. Relevant liquidity risk-related information such as the results of the liquidity stress testing carried out periodically by ERMU, are deliberated upon by higher management including ALCO, which results are taken into consideration in determining the Group's funding needs from time to time. Treasury Department is entrusted to manage and monitor the Bank's liquidity, resulting from the liquidity surplus/deficit emanating from non-discretionary operations on a daily basis within the parameters set by ALCO, to ensure a constant state of readiness should an exceptionally high demand for liquidity arise at any time. Statutory Reporting Department (SRD) is responsible to compile and submit all the required regulatory reporting related to liquidity risk. The Board of Directors (BoD) is ultimately responsible for the liquidity risk assumed by the Bank and the manner it is managed and controlled.

In line with the Bank's risk appetite and in order to mitigate the aforementioned liquidity risks, adequate controls are established in a number of policies and procedures as highlighted below:

- The Liquidity Risk Management Policy sets out the overarching principles relating to the management of liquidity risk, and also articulates the control activities relating to the identification, quantification, reporting and monitoring of such risks. The ultimate objective is to maintain structurally sound liquidity profiles;
- The Treasury Management Policy (TMP) sets out the parameters for identifying and monitoring the Bank's treasury function activities. Control procedures involve formalized limits which are monitored on an ongoing basis to ensure that a highly diversified marketable investment portfolio in maintained, one that can be easily liquidated in times of need. The Bank maintains an ongoing presence in funding markets and ensures that standby unsecured credit lines are kept active, even if it does not have an immediate liquidity need to address. This is intended to sustain an enduring inter-bank relationship with fund providers. This is mostly done within the European market. A number of Global Master Repurchase Agreements with foreign banks are also in place to provide access to repurchase agreement (repo) borrowing;
- The Internal Liquidity Adequacy Assessment Process (ILAAP) contains detailed qualitative and quantitative information of

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the Bank's processes and methodology used to measure and manage funding liquidity risk and market liquidity risk. To better assist the liquidity management and to ensure the adequacy of the liquidity tolerance levels, the ILAAP document includes at least two liquidity stress testing scenarios;

- In the Stress Testing Policy, the use of scenario analysis and stress testing constitutes a forward-looking approach which helps to proactively identify and analyse the liquidity risks which might be latent under benign conditions but, if triggered, could have serious implications on a bank. The stress testing analysis results help the BoD and senior management to agree on a course of action designed to avoid or mitigate such risks. The said stress testing output provides a good indication of the level of capital and/or liquidity which might be needed to absorb losses should the modelled shocks materialize.
- The Contingency Funding Plan sets out the strategies that will be activated in case of excessive liquidity demand. It includes a well-defined process and action plan for responding to severe disruptions to the Bank's ability to fund some or all of its activities. This would ensure sufficient liquidity resources for meeting all liabilities when they fall due in a timely and cost-effective manner.

The BoD is satisfied with the Bank's liquidity adequacy and mitigants in place. In fact, in the last ILAAP report (reference date: December 2018), it was not deemed necessary to allocate Pillar II capital against liquidity risk. This was driven by the high degree of confidence that the Bank was in a position to address daily liquidity obligations and withstand a period of liquidity stress; this must also be viewed in the context of a situation of excess liquidity which has prevailed for several years.

ALCO continuously analyses the best way to utilize the excess liquidity and monitors the Bank's liquidity position by following key liquidity risk indicators set out in the Risk Appetite Framework.

The institution enjoys a favourable funding base with stable and diversified customer deposits, which provide the vast majority of the institution's total funding requirement. The highly liquid position was maintained during this financial period, with the loan portfolio fully funded by deposits. The Loan-to-Deposit (LtD) ratio (net of interest in suspense) has eased further throughout this period, standing at 44.16% for the BOV Group, and 44.14% for the Bank (December 2018: 44.20%), respectively as at December 2019. The relative decrease in the LtD ratio was driven by the fact that the rise in customer deposits somewhat outstripped the rate of increase exhibited over the loan portfolio reflecting the degree of confidence by external stakeholders in the institution.

The Liquidity Coverage Ratio (LCR) requires credit institutions to promote short-term resilience to potential liquidity disruptions thereby eliminating, or significantly reducing, structural mismatches between assets and liabilities. In terms of LCR requirements, credit institutions must hold sufficient unencumbered high quality liquid assets (HQLA) to withstand the excess of severe liquidity outflows over inflows that could be expected to accumulate over a 30-day stressed period. During such a period, a credit institution should be able to convert quickly its liquid assets into cash without recourse to central bank liquidity or public funds. The Bank calculates and monitors the LCR in line with the relative regulatory dictum – Commission Delegated Regulation (EU) 2015/61 – on a monthly basis. As at end of December 2019, the Bank was well positioned with an LCR of 514.6% (December 2018, 296.8%). Such level very comfortably exceeds the minimum threshold of 100% representing full ratio phase-in as from 2019.

The inter-year rise in LCR is a material one and approximated 217%. It is mainly attributable to a thorough review of the methodology involving improvements and fine-tuning in the reporting of inflows and liquid assets.

The following table provides quantitative LCR information which complements Article 435 (1) (f) of Regulation (EU) No 575/2013. The LCR components of the previous 23 months have also been restated in line with the above mentioned enhancements in inflows and liquid assets.

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EU LIQ 1 - LCR Disclosure table (consolidated)

€ millions		Total unweighted value (average)					Total weighted value (average)				
Quarter ending on		**Dec-18**	**Mar-19**	**Jun-19**	**Sep-19**	**Dec-19**	**Dec-18**	**Mar-19**	**Jun-19**	**Sep-19**	**Dec-19**
Number of data points used in the calculation of averages: 24		**12**	**12**	**12**	**12**	**12**	**12**	**12**	**12**	**12**	**12**
High - Quality Liquid Assets											
1.0	Total high-quality liquid assets (HQLA)						4,189.6	4,281.6	4,518.9	4,741.8	4,898.9
Cash - Outflows											
2.0	Retail deposits and deposits from small business customers, of which:	5,758.5	5,903.6	6,038.6	6,155.4	6,272.1	379.3	388.3	397.2	404.5	411.8
3.0	*Stable deposits*	4,071.6	4,179.7	4,267.9	4,350.7	4,430.4	203.6	209.0	213.4	217.5	221.5
4.0	*Less stable deposits*	1,686.9	1,724.0	1,770.6	1,804.7	1,841.7	175.7	179.4	183.8	186.9	190.3
5.0	Unsecured wholesale funding	3,037.8	2,997.9	2,995.9	2,954.1	2,903.7	1,352.8	1,329.5	1,329.3	1,301.6	1,284.1
6.0	*Operational deposits (all counterparties) and deposits in networks of cooperative banks*	-	-	-	-	-	-	-	-	-	-
7.0	*Non - operational deposits (all counterparties)*	3,037.8	2,997.9	2,995.9	2,954.1	2,903.7	1,352.8	1,329.5	1,329.3	1,301.6	1,284.1
8.0	*Unsecured debt*	-	-	-	-	-	-	-	-	-	-
9.0	Secured wholesale funding						-	-	-	-	-
10.0	Additional requirements	1,746.7	1,762.3	1,763.8	1,775.0	1,770.2	136.0	137.7	137.0	137.7	136.8
11.0	*Outflows related to derivative exposures and other collateral requirements*	1.6	1.8	1.2	1.4	1.2	1.6	1.8	1.2	1.4	1.2
12.0	*Outflows related to loss of funding on debt products*	-	-	-	-	-	-	-	-	-	-
13.0	*Credit and liquidity facilities*	1,745.1	1,760.5	1,762.6	1,773.6	1,769.0	134.4	135.9	135.9	136.2	135.6
14.0	Other conctractual funding obligations	4.7	2.5	1.8	1.9	2.0	-	-	-	-	-
15.0	Other contingent funding obligations	170.6	178.0	188.2	196.4	201.2	75.7	75.1	78.2	82.1	84.6
16.0	**Total Cash Outflows**						1,943.8	1,930.7	1,941.8	1,925.9	1,917.4
Cash - Inflows											
17.0	Secured lending (e.g. reverse repo)	-	-	-	-	-	-	-	-	-	-
18.0	Inflows from fully performing exposures	930.8	948.5	943.3	962.3	964.2	696.8	716.5	712.2	729.6	732.0
19.0	Other cash inflows	82.9	91.6	91.8	96.6	97.5	82.9	91.6	91.8	96.6	97.5
EU - 19a	(Difference between total weighted inflows and total weighted outflows arising from transactions in third countries where there are transfer restrictions or which are denominated in non-convertible currencies)						-	-	-	-	-
EU - 19b	(Excess inflows from a related specialised credit institution)						-	-	-	-	-
20.0	**Total Cash Inflows**						779.8	808.1	804.0	826.2	829.5
EU - 20a	**Fully exempt inflows**	-	-	-	-	-	-	-	-	-	-
EU - 20b	**Inflows subject to 90% cap**	-	-	-	-	-	-	-	-	-	-
EU - 20c	**Inflows subject to 75% cap**	1,013.7	1,040.1	1,035.1	1,058.9	1,061.7	779.8	808.1	804.0	826.2	829.5
							Total Adjusted Value				
21	**Liquidity Buffer**						4,189.6	4,281.6	4,518.9	4,741.8	4,898.9
22	**Total Net Cash Outflows**						1,164.0	1,122.6	1,137.8	1,099.7	1,087.9
23	**Liquidity Coverage Ratio (%)**						361.4%	387.3%	403.1%	435.4%	455.2%

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The Bank's liquidity buffer as at December 2019, quoted at post-haircut values, may be segmented into the following high quality liquid asset (HQLA) classes:

- Level 1 assets (96.9%), mainly composed of withdrawable central bank reserves (71.7%), and followed by central government assets (19.2%);
- Level 2A assets (2.6%), mainly composed of regional government or public sector entity assets with a 20% risk weight (49.7.0%); and
- Level 2B assets (0.5%), composed of corporate debt securities Credit Quality Step 2 or 3.

Level 1 securities increased by 13.9% from December 2018 whilst Level 2 instruments declined by 42.7% during the same period. Withdrawable Central Bank reserves rose by €220.3 million during 2019. This led to a total HQLA year-on-year increase of €474.8m (+10.5%) contributing to the increase of 26.55% in the LCR ratio. On the other hand, upon analysing the net liquidity outflow figure, taking into consideration the respective haircut rates, a decline of €141.3m (-12.69%) was registered during financial year ended December 2019. The main reason behind this decrease emanates from a reduction of 4.8% in outflows and an increase in inflows of 6.7%.

The top 10 Bank's deposit names (including groups of connected depositors) comprise 5.48% of total customer deposits whilst the top 20 depositors amount to 7.73% of total customer deposits. The large, diversified, and relatively stable customer deposit base avoids reliance on wholesale funding from financial customers. In fact, each of all the other customers, account for less than 0.18% of total customer deposits. An analysis of concentration by product type demonstrates that retail sight deposits account for 52.0% of total funding, followed by retail term deposits at 10.3% and unsecured wholesale funding at 26.5% (of which 20.4% are deposits from non-financial customers and 6.1% are deposits from financial customers). The weighted average residual maturity for retail term accounts not withdrawable within a 30-day time horizon, approximates 11 months.

Cash flows from derivatives are minimal and insignificant for LCR purpose. Initial Margin as at end of the reporting period read €5 million.

The LCR is also assessed by currency, if the currency is a material one. Since no other currency other than the domestic currency, exceeds the 5% aggregate amount of liabilities to total liabilities, only the euro-denominated LCR is calculated. In fact, 94.1% of total liabilities are euro-denominated. In principle, BOV does not finance its assets in a currency different from that in which the assets are denominated.

The Net Stable Funding Ratio (NSFR) is defined as the amount of available stable funding relative to the amount of required stable funding, used to monitor the structural long-term funding position of the Bank. The Bank quantifies the NSFR metric on a quarterly basis. Once more, the results are that the institution well exceeds the 100% minimum level prescribed by the Basel Committee for Banking Supervision of the Bank for International Settlements.

The LCR captures all significant cash flows of inflows and outflows over a 1-month time horizon. As at end December 2019 the LCR read 514.6%. Taking a longer term perspective, the NSFR captures liquidity over a 1-year time horizon and reads 159.26% as at reporting date. Such levels attest to a strong and robust institutional liquidity position.

BOV is closely monitoring the liquidity position in light of possible pressures caused by the COVID-19 pandemic. At this early stage of the pandemic, it is very difficult to estimate the potential impact of COVID-19. The Bank has excess liquidity that can be utilised to weather stresses caused by the pandemic.

Section 11: Risk Management in Subsidiary Companies

The Group has two fully owned subsidiaries: BOV Asset Management Limited ("BOVAM") and BOV Fund Services Limited ("BOVFS"). BOVAM, formerly known as Valletta Fund Management Limited, was registered as a limited liability company under the laws of Malta on the 6 June 1995. BOVAM is licensed by the Malta Financial Services Authority (MFSA), to provide investment management services to collective investment schemes and qualifies as a 'Maltese Management Company' in terms of the Investment Services Act (Marketing of UCITS) Regulations (Subsidiary Legislation 370.18), by virtue of a licence issued on 22 September 1995. On 17 March 2017, BOVAM extended its licence to offer services beyond collective investment schemes. Upon extension of the licence, BOVAM started offering portfolio management service to institutional clients. Furthermore, BOVAM has had its licence extended to offer portfolio management service to retirement schemes and retirement funds.

BOVAM is the appointed manager of Vilhena Funds SICAV plc which is a company organised as a multi-fund investment company with variable share capital pursuant to the Companies Act, Cap 386 of the Laws of Malta, registered on 10 October 1997, bearing registration Number SV4 and licensed by the MFSA as a collective investment scheme pursuant to the Investment Services Act, Cap 370 of the Laws of Malta and the UCITS Directive. BOVAM is responsible to ensure that the investment limits and risk parameters of the Vilhena Funds SICAV plc and its sub-funds are adhered to. A risk management policy is in place.

BOVAM is also the appointed manager of the BOV Investment Funds which is a common contractual fund licenced by the MFSA as a collective investment scheme pursuant to the Investment Services Act and the UCITS Directive. BOVAM is responsible to ensure that the investment limits and risk parameters of the BOV Investment Funds and its sub-funds are adhered to. A risk management policy is in place.

Collectively, the sub-funds of the Vilhena Funds SICAV plc and of the BOV Investment Funds as well as the institutional clients will be referred to as 'portfolios'.

BOVAM has three regulatory functions, Asset Management, Risk Management and Compliance Monitoring. Risk Management and Compliance Monitoring are core functions of the company's culture and operations. Both functions are interlinked and work together to:

a) Ensure compliance with limits laid out in the UCITS directive, MFSA rules, Vilhena Funds SICAV plc and BOV Investment Funds Prospectus and respective Fund Supplements;
b) Ensure that risk measurement arrangements, processes and techniques on the portfolios' positions are in place, and that their contribution to the overall risk profile of the portfolios are accurately measured and documented;
c) Conduct periodic stress tests and scenario analyses to address risks arising from potential changes in market conditions that might adversely impact the portfolios;

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d) Establish, implement and maintain a documented system of internal limits concerning the measures used to manage and control the relevant risks of the portfolios;
e) Ensure that the current level of risk complies with the risk limits set; and
f) Establish, implement and maintain adequate procedures that, in the event of actual or anticipated breaches to the risk limits of the portfolios, result in timely remedial actions.

The risk management techniques applied are appropriate and proportionate to the nature, scale and complexity of the BOVAM's activities and of the UCITS it manages. From time to time, BOVAM reviews its measurement techniques to ensure that these remain appropriate and effective, depending on the investment strategies of the portfolios it manages.

BOVAM has a robust governance structure. It has documented policies and procedures in place and a comprehensive risk register identifying primary and consequential risks. For all the risks outlined in the risk register, BOVAM has internal control principles that enable it to operate in an efficient and diligent way.

Moreover, the BoD of BOVAM has established a Risk and Regulatory Committee ("RRC"), whose terms of reference are laid out in an appropriate document. This Committee is, amongst others, responsible to ensure that BOVAM has an appropriate risk management process in place. The RRC is also responsible to monitor, on a regular basis, the effective implementation of the risk management process, such that BOVAM is able to monitor, measure and manage at any time the various risks of the positions and their contribution to the overall risk-profile of the portfolios.

BOV Fund Services (formerly Valletta Fund Services) was set up in 2006 as a fully owned subsidiary of the Bank to provide asset managers with a comprehensive suite of administration services to investment funds. BOV Fund Services is recognised to provide fund administration services by the MFSA, and is also licensed as a Corporate Service Provider in terms of the Company Service Providers Act, 2013. In providing its services, BOV Fund Services is exposed to both operational and reputation risks, and to a lesser extent also market risks. To mitigate these risks, BOV Fund Services has in place compliance and risk monitoring internal audit programs through the Company's Compliance and Risk Management Division, aimed at reviewing the processes and the corresponding control procedures. In addition, audits of the Company's various operations are undertaken by the Group's Internal Audit department. BOV Fund Services has also engaged an independent audit firm to perform a biennial ISAE 3402 examination of its processes and controls, which consists of an evaluation of the design and operating effectiveness of the controls of the Company. In relation to managing reputation risks, BOV Fund Services carries out an extensive due diligence process on its potential clients and has in place the necessary procedures to ensure that the business is compliant with prevention of money laundering regulations.

In view of the dependency of the Company on its various IT systems, BOV Fund Services has in place a detailed business continuity plan in order to appropriately manage the incidence of business interruptions and disaster recovery.

Moreover, the BOV FS Risk and Compliance Committee was set up by the Board of Directors of BOV Fund Services Limited (BOV FS) during Financial Year 2019, to assist the Board in fulfilling its oversight responsibilities in relation to the risk management and compliance framework and the governance structure that supports it. Amongst other tasks, the Committee reviews relevant policies and report to the Board on the adequacy or otherwise thereof, and also provides advice and guidance to the BOV FS Board on the Risk Appetite and related tolerances, ensuring that such tolerances are within the Group's Risk Appetite. The Committee also oversees the procedures, practices and activities of BOV FS and of any person employed with or acting for or on behalf of BOV FS for the purpose of ensuring that the compliance obligations of BOV FS are being discharged according to law and that the internal rules, procedures and guidelines are complied with. The Committee meets at least on a quarterly basis unless further required, and the Chief Officer Fund Business attend the Meeting by way of invitation.

CRR Articles	Description	Reference
Article 435	Risk Management objectives and policies	Section 1,6,7,8,10,11
Article 436	Scope of application	Section 2
Article 437	Own funds	Section 3
Article 438	Capital requirements	Section 4
Article 439	Exposure to counterparty credit risk	Section 6.6
Article 440	Capital buffers	Section 4
Article 441	Indicators of global systemic importance	Not applicable
Article 442	Credit risk adjustments	Section 6.4
Article 443	Unencumbered assets	Note to the Financial Statements 39.9
Article 444	Use of ECAIs	Section 6.4.3
Article 445	Exposure to market risk	Section 7
Article 446	Operational risk	Section 8
Article 447	Exposures to equities not included in the trading book	Section 7.4
Article 448	Exposure to interest rate risk on positions not included in the trading book	Section 7.2
Article 449	Exposure to securitisation positions	Not applicable
Article 450	Remuneration policy	Section 9 and Remuneration Report
Article 451	Leverage	Section 5
Article 452	Use of IRB Approach to credit risk	Not applicable
Article 453	Use of credit risk mitigation techniques	Section 6.5
Article 454	Use of advances measurements approaches to operational risk	Not applicable
Article 455	Use of Internal Market Risk models	Not applicable

Corporate governance statement of compliance

A. INTRODUCTION

Pursuant to the Listing Authority Listing Rules, Bank of Valletta p.l.c. (the Bank) as a company whose equity securities are listed on a regulated market, should endeavour to adopt the Code of Principles of Good Corporate Governance (the Code) contained in Appendix 5.1 to Chapter 5 of the Listing Rules. In terms of Listing Rule 5.94, the Bank is obliged to prepare a report explaining how it has complied with the Code. For the purposes of the Listing Rules, the Bank is hereby reporting on the extent of its adoption of the Code.

The Board of Directors (the Board) is committed to the values of truth, transparency, honesty and integrity in all its actions. The Board strongly believes that the Bank benefits from having in place more transparent governance structures and from improved relations with the market which enhance market integrity and confidence. The Board acknowledges that the Code recommends principles for the Board and the Bank's management to pursue objectives that are in the interest of the Bank and its shareholders.

Good Corporate Governance is the responsibility of the Board, and in this regard the Board has adopted a corporate decision-making and supervisory structure that is tailored to suit the requirements of the Bank's constitutional documents as well as its size, nature and operational needs. In addition, while the structure provides flexibility and an efficient decentralisation of selective decision-making, it concurrently provides a system of checks and balances. The Board believes that any structure which is adopted must be geared to meet the necessary standards of accountability and probity, and considers that the structure which it has adopted does so.

As demonstrated by the information set out in this Statement, together with the information contained in the Remuneration Report and in the Nominations Report, the Bank believes that it has, save as indicated herein, in the section entitled Non-Compliance with the Code, throughout the accounting period under review, applied the principles and complied with the provisions of the Code. In the Non-Compliance section, the Board indicates and explains the instances where it has departed from or where it has not applied the Code.

B. COMPLIANCE WITH THE CODE

Principle 1: The Board

The Board's role and responsibility is to provide the necessary leadership, to set strategy and to exercise good oversight and stewardship. The Board is composed of a Chairman, two Executive Directors and eight Non-Executive Directors. This mix of Executive and Non-Executive Directors on the Board enables the Non-Executive Directors to exercise their monitoring function over the management and the executive arm of the Board at the level of the Board. Moreover, the fact that the Chief Executive Officer (CEO) is also an Executive Director on the Board, enables the Board to be in receipt of timely and appropriate information in relation to the business of the Bank and Management's performance. As a result, the Board can contribute effectively to the decision-making process, whilst at the same time exercising prudent and effective controls.

The Board delegates specific responsibilities to a number of Committees, notably the Credit Committee, the Audit Committee, the Risk Management Committee, the Compliance and Crime Prevention Committee, the Ethics Committee, the Remuneration Committee and the Nominations and Governance Committee, each of which operates under formal Terms of Reference approved by the Board.

Further details in relation to the Committees and the responsibilities of the Board is found under Principles 4 and 5 of this Statement.

Principle 2: Chairman and Chief Executive Officer (CEO)

The Bank's current organisational structure incorporates the position of a CEO. The position of the Chairman and that of the CEO are occupied by different individuals. Their respective positions have been defined with specific roles rendering these positions completely separate from one another. These specific roles are identified within the Board Terms of Reference and in their contract of engagement. This separation of roles of the Chairman and the CEO avoids concentration of authority and power in one individual.

The Chairman is responsible to lead the Board and to set its agenda. The Chairman ensures that the Board's discussions on any issue put before it go into adequate depth, that the opinions of all the Directors are taken into account and that all the Board's decisions are supported by adequate and timely information. The Chairman ensures that the CEO develops a strategy which is agreed to by the Board.

On the other hand, the CEO, besides being an Executive Director, leads the Bank's Management Board, which is the highest executive decision-making body within the Bank.

More information on the Bank's Management Board can be found under the section entitled Management Committees, within this Statement.

Corporate governance statement of compliance (continued)

Principle 3: Composition of the Board

The Board considers that during the year under review the size of the Board, whilst not being too large as to be unwieldy, was appropriate, taking into account the size of the Bank and its operations. The combined and varied knowledge, experience and skills of the Board members provided a balance of competences that are required and add value to the proper functioning of the Board.

Independence of Directors

During the year under review, the Board consisted of seven Independent Non-Executive Directors (including the Chairman), two Non-Independent Non-Executive Directors (as indicated on pages (ii) and (iii) of the Annual Report) and two Executive Directors. In determining the independence or otherwise of its Directors, the Board has considered, amongst others, the notion of independence as contained in the Code, the Bank's own practice as well as general good practice principles. Moreover, the Non-Executive Directors have to prepare a written annual declaration of their independence to the Board. The Board believes that, by definition, employment with the Bank rendered Directors Alan Attard and James Grech as Non-Independent from the Institution. However, this should not, in any manner, detract from the said Non-Independent Directors' ability to maintain independence of analysis, decision and action at all times. Moreover, having considered their roles and duties as Bank employees, the Bank deemed Mr Attard and Mr Grech to be Non-Executive Directors.

Appointment of Executive Directors

The appointment of Executive Directors is regulated by article 24 of the Articles of Association. In accordance with the said article, the CEO of the Bank shall ex officio become an Executive Director by virtue of his office and shall remain in office until the tenure of office as CEO.

The Non-Executive Directors shall appoint at least one other Executive Director on the Board from amongst the Senior Management and may also appoint a third Executive Director if the Non-Executive Directors consider it in the best interest of the collective knowledge and competence of the Board to do so. To date one additional Executive Director has been appointed and that position is held by the Chief Risk Officer, which is in line with the Bank's strategic initiatives to highlight risk management even at Board level.

Appointment of Non-Executive Directors

Article 23.3 of the Bank's Articles of Association specifies that the Board of Directors shall consist of a maximum of three (3) Executive Directors and a maximum of nine (9) Non-Executive Directors. In the event of the co-option to the Board, pursuant to article 27A, of a maximum 2 additional Non-Executive Directors, the maximum number of Non-Executive Directors shall be eleven (11).

The appointment of the Non-Executive Directors is governed by articles 25 and 27A of the Articles of Association and appointments may be made as follows:

(a) By Qualifying Shareholders – namely members holding at least 10% of the issued share capital of the Bank having voting rights, that are entitled to nominate, for the approval of the Nominations and Governance Committee, one person for each 10% voting shares held; and

(b) By Non-Qualifying Shareholders not having a Qualifying Shareholding, but who individually or in aggregate hold not less than €50,000 in nominal value of shares having voting rights in the Bank and who are entitled to make recommendations for the approval of the Nominations and Governance Committee; or

(c) By the Nominations and Governance Committee itself seeking the recruitment of fit and proper persons having the right attributes that can add value to the Board of Directors.

(d) By the Non-Executive Directors pursuant to Article 27A of the Articles of Association as explained in further detail below.

Save for the provisions in para (d) above, all Non-Executive Directors are appointed by the Bank's shareholders during the Annual General Meeting.

Appointment of Additional Non-Executive Directors by Co-Option

Article 27A of the Bank's Articles of Association provides for the additional appointment of Non-Executive Directors by Co-Option. This article was recently introduced in the Articles of Association and approved during the Annual General Meeting held on 9 May 2019.

The objective of this article was to address situations where, notwithstanding the efforts that may be made by the Nominations and Governance Committee to ensure that the Board of Directors of the Bank had the necessary mix of skills and experience, there could arise situations where those efforts could not yield the appropriate mix and combination of skills, or where the regulator could require certain skills which may not be present on the Board. In these situations, the Board would need to react in a relatively short time to ensure that the composition of the Board fulfils its ultimate aim. Accordingly, this Article empowers the Board of Directors (specifically, the Non-Executive Directors) to co-opt up to a maximum of additional two Non-Executive Directors to sit on the Board of Directors of the Bank, only in those instances where the nine Non-Executive Director positions were already filled, but the then current Board complement did not have the composition required by regulation or in the opinion of the Nominations and Governance

Corporate governance statement of compliance (continued)

Committee, the Board still did not have the appropriate mix of collective skills, knowledge and experience. Such co-opted Non-Executive Directors would be appointed for a three (3) year term with eligibility for re-appointment.

By virtue of this Article, during the period under review, two Non-Executive Directors, namely Mr Alfred Mifsud and Dr Diane Bugeja were, with effect from 19 December 2019, appointed to the Board by co-option. More details on these Directors was found on pages (ii) to (iv) of this Report.

Nominations and Governance Committee

All Directors, irrespective of the manner in which they are proposed, can only take office following the approval of their nomination by the Nominations and Governance Committee. In this context, the Nominations and Governance Committee is the organ that, after having scrutinised the list of candidates to ensure that the Board will have the appropriate collective knowledge, experience and competence, will then place the list of approved candidates for election at the Annual General Meeting. More information on the Nominations and Governance Committee is found under the Nominations Report.

The appointment of all Directors is subject to regulatory approval.

Rotation of Directors

The Bank has a system of rotation of Directors aimed at ensuring a certain level of continuity within the Board of Directors. The system of rotation of Directors contemplates the retirement of one-third of the Non-Executive Directors in each year, with the remaining two-thirds of the Board retaining office. This is aimed at providing stability of policy-making and implementation by retaining a majority of the Board in place for a period of at least three years at any time. Those Directors whose turn it is to retire from office, pursuant to the rotation system, will be eligible for reappointment, subject to approval by the Nominations and Governance Committee. The Directors to retire first shall be determined as follows:

a) Those Non-Executive Directors who wish to retire and who do not seek reappointment prior to the full term of their appointment; otherwise,

b) To the extent that there are no Non-Executive Directors who wish to retire and who do not seek reappointment prior to the full term of their appointment, those who retire first shall be the Non-Executive Directors who have been longest in office, including by virtue of re-election, since their first election, but as between persons who became Directors on the same day or in the event that the duration in office cannot be properly determined those to retire shall (unless they otherwise agree among themselves) be determined by lot.

A retiring Director shall only be eligible for re-election provided that such person did not occupy the office of Non-Executive Director for an aggregate period of more than 12 years in any period of 15 years.

Pursuant to Article 28.2 of the Bank's Articles of Association, one-third of the Bank’s Non-Executive Directors will retire at the Annual General Meeting (AGM). During 2019 the three most senior directors due to retire during the 2019 AGM were Mr Taddeo Scerri, Mr James Grech and Mr Joseph M Zrinzo. Mr Taddeo Scerri was appointed on the Bank’s Board as Director in April 2013. Mr Joseph M Zrinzo and Mr James Grech were elected as Directors in December 2013 and December 2014 respectively. Thus, three vacancies for Non-Executive Directors arose. Out of the three vacancies, one was appointed by a Qualifying Shareholder of the Bank. Insofar as the two (2) other vacancies were concerned, there were as many nominations by the Non-Qualifying Shareholders as there were vacancies. Since all three (3) nominees were deemed by the Nominations and Governance Committee to be fit and proper to act as directors, no election took place during the 2019 AGM.Therefore, the three vacancies were filled by the re-appointment of the three directors mentioned above.

Mr Joseph M Zrinzo, who was a Non-Executive Director of the Bank, has resigned during FY 2019. Two other Non-Executive Directors, namely Mr Alan Attard and Mr Paul V Azzopardi have resigned during the first quarter of FY 2020. Thus, three vacancies for Non-Executive Directors will arise during the forthcoming Annual General Meeting. Since there were three (3) resignations of Non-Executive Directors, no rotation of directors was necessary. Pursuant to Article 25 of its Articles of Association, on the 23 January 2020, the Bank issued a call for interested persons who would like to submit their nomination for appointment as Non-Executive Directors on the Board. The Bank received nominations from 4 individuals. An assessment of each nomination will be carried out by the Nominations and Governance Committee.

Corporate governance statement of compliance (continued)

Number of directorships held by members of the Board of Directors, including the appointment on the Board of Bank of Valletta p.l.c.

Name	Number of Directorships held – Executive Director (ED) and Non-Executive Director (NED)
Stephen Agius	1 NED
Alan Attard (resigned 1 January 2020)	1 NED
Paul V Azzopardi (resigned 15 February 2020)	2 NED + 1 ED
Miguel Borg	3 NED +1 ED
Diane Bugeja (appointed 19 December 2019)	1 NED
James Grech	4 NED
Alfred Lupi	3 NED
Mario Mallia (resigned 27 December 2019)	2 NED + 1 ED
Alfred Mifsud (appointed 19 December 2019)	1 NED
Antonio Piras	1 NED
Joseph M Zrinzo (resigned 1 September 2019)	2 NED

Taddeo Scerri and Anita Mangion are not subject to the provisions of Article 91 of the CRD IV and Article 14 (3) (a) of the Banking Act, 1994 (Chapter 371, Laws of Malta) as regards the number of directorships held by them in view of their appointment in a national representative capacity.

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

The Board meets approximately twice a month, unless further meetings are required for the Board to discharge its duties effectively. The Board discusses and decides upon matters relating to the Bank's business. During the financial year under review, the Board met twenty nine (29) times. As from FY 2020, the Board meetings will be held on a monthly basis. Additional ad hoc Board meetings may be convened as necessary and according to exigencies. Credit proposals are not discussed at Board level but are considered by the Credit Committee. More information on the Credit Committee can be found under the section entitled Board Committees.

The Board regularly reviews and evaluates corporate strategy, major operational and financial plans, risk policies, performance objectives which are benchmarked against industry norms and business alternatives. The strategy, processes and policies adopted for implementation are regularly reviewed by the Board so that corrective measures can be taken to address any deficiencies and ensure the future sustainability of the enterprise. The Board also monitors implementation and corporate performance within the parameters of all relevant laws, regulations and codes of best business practice. The Board has a formal schedule of matters reserved for its decision and also delegates specific responsibilities to Board Committees.

The Board ensures that it has the appropriate policies and procedures in place which guarantee that the Bank and its employees maintain the highest standards of corporate conduct, including compliance with applicable laws, regulations, business and ethical standards.

Notice of the dates of upcoming meetings, together with supporting material, are circulated well in advance to Directors to allow ample time to appropriately consider the information prior to the next board meeting. Furthermore, advance notice is also provided of ad hoc meetings to allow sufficient time to re-arrange commitments.

After each Board meeting, minutes that faithfully record attendance, matters discussed and decisions taken, are prepared and circulated to all Directors as soon as practicable after the meeting.

Members of Senior Management attend Board Meetings by invitation on a regular basis.

Corporate governance statement of compliance (continued)

Members	Independent & Non Independent / Executive & Non-Executive Directors	Meetings Held: 29 Meetings attended by member	
Taddeo Scerri (Chairman)	Independent NED	29	
Stephen Agius	Independent NED	25	
Alan Attard (resigned 1 January 2020)	Non-Independent NED	26	
Paul V Azzopardi* (resigned 15 February 2020)	Independent NED	29	
Miguel Borg	ED	28	
Diane Bugeja (appointed 19 December 2019)	Independent NED	1	(out of 1)
James Grech	Non-Independent NED	25	
Alfred Lupi	NED	28	
Mario Mallia (resigned 27 December 2019)	ED	26	(out of 28)
Anita Mangion**	Independent NED	28	
Alfred Mifsud (appointed 19 December 2019)	Independent NED	1	(out of 1)
Antonio Piras***	Independent NED	29	
Joseph M Zrinzo (resigned 1 September 2019)	Independent NED	19	(out of 19)

*19 by video/tele conferencing
** 1 by video/tele conferencing
***19 by video/tele conferencing

Board Committees

The Board also delegates specific responsibilities to Committees, which operate under their respective formal Terms of Reference. In this respect, the Board has established the following Committees:

Credit Committee

The Credit Committee was set up by the Board to discuss and decide upon credit proposals. The Committee also considers and decides upon investment limits which require a level of authority higher than that of the Bank's Executives. The Committee further considers credit related issues which the Bank's Executives may wish to escalate.

Members	Meetings Held: 19 Meetings attended by member
Taddeo Scerri (Chairman)	17
James Grech	14
Alfred Lupi	18
Mario Mallia (resigned 27 December 2019)	17

The Executive Chairman's Office, the Chief Risk Officer, the Executive Credit Risk Sanctioning, the Chief Credit Officer and the Chief Officer Corporate Finance attend the Credit Committee by invitation.

The Audit Committee

The Audit Committee's Terms of Reference include the monitoring of the financial reporting process, the effectiveness of the Bank's internal control, internal audit and risk management systems and the audit of the Bank's annual and consolidated accounts. The Audit Committee is also responsible to oversee the establishment of accounting policies by the Bank. The primary purpose of the Audit Committee is to protect the interests of the Bank's shareholders and assist the Directors in conducting their role effectively so that the Bank's decision-making capability and the accuracy of its reporting and financial results are maintained at high level at all times. The Audit Committee has established internal procedures and monitors these on a regular basis. The Audit Committee also scrutinizes and approves related party transactions in line with the Related Party Transaction Policy. The Audit Committee considers the materiality and the nature of the related party transactions carried out by the Bank to ensure that the arms' length principle is adhered to at all times. The Audit Committee is also responsible for managing the Board's relationships with internal and external

Corporate governance statement of compliance (continued)

auditors. The Audit Committee also recommends the appointment of the External Auditors in accordance with Article 16 of the Statutory Audit Regulations.

In terms of Listing Rules 5.117, 5.118 and 5.118A, the Audit Committee is composed of three Non-Executive Directors, all of whom are considered as independent of the Bank, since they are free from any business, family or other relationship with the Bank or its management that may create a conflict of interest such as to impair their judgement.

Alfred Lupi FCCA, FIA, BSc Econ is a Non-Executive Director. He is a professional accountant with an economics degree and is currently engaged in consultancy services. He is appointed Chairman of the Audit Committee by the Board and is the Director whom the Bank considers as competent in accounting. Alfred Lupi is independent of the Bank.

Stephen Agius is a Non-Executive Director. During his career he occupied various positions where he was responsible for large scale projects both local and abroad. Mr Agius is also a visiting lecturer at the University of Malta. More detail on his brief resume is found on pages (ii) to (iv) of this Report. He is independent of the Bank and is considered as competent to be a member of the Audit Committee.

Paul V Azzopardi is a Non-Executive Director. His area of expertise is financial services and investments. During his career he occupied various Directorship positions and has lectured in a number of Universities both local and abroad. More detail on his brief resume is found on pages (ii) to (iv) of this Report.

During January to August 2019, Joseph M Zrinzo was member of the Audit Committee.

Joseph M Zrinzo was a Non-Executive Director of the Bank. Mr Zrinzo has various Board directorship experiences on a number of companies. He also served as a member of various committees. He was independent of the Bank and was considered as competent to be a member of the Audit Committee.

Mr Zrinzo was substituted on the Audit Committee by Paul V Azzopardi, following the former's resignation from the Bank's Board of Directors on the 1 September 2019.

Antonio Piras is a Non-Executive Director appointed on the Bank's Board of Directors in 2016. During his career he held various senior positions as was further detailed in his brief resume on pages (ii) to (iv) of this Report. He is independent of the Bank, and was considered as competent to be a member of the Audit Committee.

In view of the diverse skills and professional experience of each of the Audit Committee Members, the Bank considers the Audit Committee as a whole to have the adequate competence and meet the independence criteria as required by Listing Rule 5.118.

Members	**Meetings Held: 12** **Meetings attended by member**
Alfred Lupi (Chairman)	12
Stephen Agius	6
Paul V Azzopardi* (resigned 15 February 2020)	4 (out of 4)
Antonio Piras**	6 (out of 6)
Joseph M Zrinzo (resigned 1 September 2019)	8 (out of 8)

* 1 by video/tele conferencing
** 3 by video/tele conferencing

The CEO, the Chief Risk Officer and the Chief Group Internal Auditor attend Audit Committee meetings. The Chief Financial Officer, the Executive Risk Management and a representative of the External Auditors attend the Audit Committee meetings by invitation. KPMG Malta are the Group's statutory auditors. A designated person from the Office of the Company Secretary acts as Secretary to the Audit Committee.

The Remuneration Committee – This is considered under the Report of the Remuneration Committee.

The Nominations and Governance Committee – This is considered under the Nominations Report.

The Risk Management Committee

The Risk Management Committee assists the Board in assessing the different types of risks to which the organisation is exposed. This Committee is responsible for the proper implementation and review of the Group's risk policies related mainly, but not restricted to, Credit, Market and Operational Risks. It reports to the Board on the adequacy, or otherwise, of such policies. The Committee is also responsible to review delegated limits, together with an oversight of the Group's monitoring and reporting systems, to ensure regular and appropriate monitoring and reporting on the Group's risk positions.

Corporate governance statement of compliance (continued)

Members	Meetings Held: 13 Meetings attended by member
Joseph M Zrinzo (Chairman) (resigned on 1 September 2019)	9 (out of 9)
Alan Attard (resigned on 1 January 2020)	11
Paul V Azzopardi (Deputy Chairman) (resigned 15 February 2020)	13
James Grech	9

The CEO, the Chief Risk Officer and the Risk Committee Consultant attend Risk Management Committee meetings. The Chief Financial Officer, the Chief Officer Group Internal Audit, the Executive Risk Management and the Head Supervisory Coordination Unit attend the Risk Management Committee meetings by invitation. A designated person from the Office of the Company Secretary acts as Secretary to the Risk Management Committee.

As at date of publication of this Annual Report, the Risk Management Committee is composed of the following members: Alfred Mifsud (Chairman), Alfred Lupi and Dr Diane Bugeja.

The above information on the Risk Management Committee, together with the information contained in Section 1 of the Capital and Risk Management Report included in this Annual Report, is also to be considered as a disclosure for the purposes of Regulation 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms.

The Compliance and Crime Prevention Committee

The primary objective of the Compliance and Crime Prevention Committee is to assist and guide the Board of Directors in the discharge of their obligations imposed from time to time by regulation in the area of financial services and in light of the Bank acting as a credit and financial institution licensed to provide services under different laws and within the framework of the Compliance Function as defined in the Compliance Charter and as approved by the Board of Directors. The Committee is also responsible to assist the Bank in combatting financial crime and money laundering activities.

Members	Meetings Held: 6 Meetings attended by member
Paul V Azzopardi* (resigned on 15 February 2020)	6
Anita Mangion	6
Alan Attard	6
Alfred Lupi	6

*2 by video/tele conferencing

The CEO and the Chief Risk Officer attend the Compliance and Crime Prevention Committee meetings. The Chief Business Development Officer, the Chief Officer Group Compliance, the Executive Anti-Financial Crime and the Money Laundering Reporting Officer attend the Compliance and Crime Prevention Committee meetings by invitation. A designated person from the Office of the Company Secretary acts as Secretary to the Compliance and Crime Prevention Committee.

Ethics Committee

The Ethics Committee is a Board appointed Committee and its Terms of Reference have likewise been approved by the Board. The aim of the Committee is to develop a BOV Group Ethics Policy, regularly review such policy in line with best practice and oversee the investigation of any breaches to the Ethics Policy. The Committee is chaired by one of the Non-Executive Directors of the Bank and is composed of the Chief Executive Officer and the Chief Risk Officer. The Chief Officer Human Resources and Ethics and the Chief Officer Group Internal Audit attend the Committee by invitation. A designated person from the Office of the Company Secretary acts as Secretary to the Ethics Committee. The Committee meets on a bi-annual basis.

Business Restructuring Action Committee (BRAC)

The BRAC assists the Board in ensuring that the implementation process of the business restructuring plan is in line with the Bank's strategy. The Committee is responsible to oversee and monitor the implementation plan and to take executive decisions with respect to the plan as are necessary or desirable for the efficient and effective implementation of the plan. The BRAC reports to the Board on work undertaken by the Committee on a regular basis. The Committee meets on a monthly basis and is composed of the Chairman, the Chief Executive Officer, the Chief Risk Officer, the Chief Business Development Officer and the Chief Business Restructuring Officer. A designated person from the Risk Management Department acts as Secretary to the Business Restructuring Action Committee. The BRAC is a temporary Committee and will be dissolved once the Business Restructuring exercise is completed.

Corporate governance statement of compliance (continued)

IT Oversight Committee

The IT Oversight Committee is a temporary Board Committee that was set up in 2019 to assist the Board of Directors in fulfilling its oversight responsibilities in relation to the digital ecosystem including cyber security, the Core Banking Transformation (CBT) programme, and innovative technologies. The Committee is chaired by one of the Non-Executive Directors of the Bank and is composed of members of Senior Management and an External Consultant. The Committee meets according to business exigencies.

Post-CBT implementation, the IT Oversight Committee was tasked to conclude a post-implementation review of the CBT implementation exercise and will be wound up during the course of 2020.

Transformation Committee

The Transformation Committee is a temporary Board Committee, set up in 2019 to address the Bank's remediation programme, with responsibilities for the oversight and coordination of risk, compliance and anti-financial crime projects and initiatives across the Group. The Committee is chaired by the Chairman of the Bank and is composed of Non-Executive Directors, members of Senior Management and External Consultants. The Committee meets according to business exigencies.

Suitability Policy

During the period under review, the Bank has adopted and implemented a Suitability Policy, applicable to all Directors, Management Board Members and Key Function Holders within the BOV Group (collectively termed as "Subject Persons"). The aim of the Suitability Policy is to ensure the suitability of the members of the Management Body and Key Function Holders, not just at the inception of their appointment but also throughout the duration of their appointment. In this context, suitability refers to the ability of all Subject Persons to ensure, at all times, a sound and prudent management of the financial institution, viewing, in particular, the safeguarding of the financial system and the interests of respective clients, depositors, investors and other creditors. Subject Persons must comply with requirements of fitness and appropriateness, professional qualification, independence and time-commitment (availability).

The Bank's **Diversity Policy** is embedded within the Suitability Policy, and aims to ensure diversity amongst the members of the Management Board and Board of Directors (the "Management Body"). When approving members for the Management Body, the Nominations and Governance Committee is to engage a broad set of qualities and competences. The diversity in educational and professional background, gender and age provide for divergent views and experiences thus facilitating independent opinions and sound decision-making within the Management Body. With respect to the composition of the BOV Group, the Nominations and Governance Committee will strive to increase diversity in the Board composition of the subsidiary companies. The Nominations and Governance Committee will also undertake an assessment to determine ways by which diversity within the Board of Directors of the Bank is also increased, whilst remaining cognisant that their election is subject to shareholders vote.

Whilst recognising that in the Maltese environment, it is difficult to ensure gender diversity, the Bank is committed to reasonably dedicate best efforts to increase gender representation in the coming years. In terms of equal treatment, the Bank aims to provide an inclusive environment which promotes equality, values diversity and maintains a working environment where the rights and dignity of all employees are respected.

The Suitability Policy also provides for a **Training Policy** through which the Bank commits the necessary resources and time to ensure continuous training to broaden the knowledge and skills required for a suitable performance of the functions assigned to subject persons. Prior to assuming their role, Subject Persons will be provided with key information including a description of the role and responsibilities of the particular appointment. This also applies to Directors being appointed as Chair or Members of Board Committees. The Bank is committed to provide newly appointed Subject Persons with an induction course within the first few months of their taking up the position, taking into account the strategy of the Bank, the risk and compliance framework and other key matters on the Bank and in the banking and financial area. The Training Policy also provides for the continuous training of subject persons, wherein the latter are expected to possess the experience and professional qualifications necessary to perform their function, taking into account the responsibilities conferred to them, the complexity of the activity and the need to ensure sound and prudent management.

The Suitability Policy was approved by the Board of Directors during the last quarter of the period under review.

Management Board Suitability

The Nominations and Governance Committee undertakes a suitability assessment of members proposed to the Management Board, which assessment is based on such individual's knowledge, skills and expertise. Following such suitability assessment, the Nominations and Governance Committee then nominates and recommends for Board Approval, members of the Management Board. Members of the Management Board also require regulatory approval before being appointed on the Management Board.

In 2019, the Bank appointed an independent external consultant firm to carry out an assessment of the fitness and properness of members of the Management Board. Following this assessment, a training plan is being devised to address any gaps in the individual and collective skills which members of the Management Board should possess in order to perform their role effectively.

Corporate governance statement of compliance (continued)

More detail on the Management Board members and their experience is found in their brief CV on page xvi of this Annual Report. With expertise in accountancy, risk, economics, business and IT, the Members of the Management Board are deemed to have the necessary collective knowledge, skills and competence to manage the business of the Group, exert oversight of the Group's operations, recommend and follow a strategic plan for the Bank, oversee the Group's financial, business and operational performance, establish and maintain a risk appetite framework, organised the allocation and adequacy of the Group's human resources and ensure that the Bank has a reliable and sustainable IT infrastructure, amongst other functions.

Management Committees – FY 2019

The Management Board is responsible for recommending strategy to the Board of Directors. Upon Board approval of such strategy, the Management Board becomes responsible for its execution. Execution includes, inter alia, ensuring adequate resourcing, proper internal controls, evaluating performance, and ensuring the timely implementation of the strategic initiatives within budget.

The Bank's Management Board meets on a regular basis. It is chaired by the CEO and is composed of the following members:

- The Chief Operations Officer
- The Chief Risk Officer
- The Chief Finance Officer
- The Chief Business Development Officer
- The Chief Credit Officer
- The Chief Technology Officer
- The Chief Officer Human Resources and Ethics

The Group Chief Compliance Officer attends Management Board meetings as an observer. Other Chief Officers and Bank Executives attend Management Board meetings by invitation.

The **Asset Liability Management Committee (ALCO)** is an integral part of the Bank. The Committee takes an integrated view in managing the Group's assets and liabilities to achieve an optimal balance between risk and return. ALCO evaluates the asset and liability cash flows, and the management of integrated exposures at a consolidated level, to enable it to give strategic direction to the business. Consideration is given, inter alia, to solvency, liquidity and interest rate risks. It also monitors the capital adequacy of the Group on a continuous basis, making use of capital forecasts to ensure that enough capital is readily available at all times to meet the demand arising from business growth and regulation. Additionally, the Committee ensures that the investment of the Bank's funds is conducted in accordance with the approved investment strategy and exercises executive authority in the area of interest rate management by setting the interest rates payable on deposit products. ALCO meets at least once a month to review the balance sheet risks and ensures its prudent management. The Committee is chaired by the CEO and is composed of members of Senior Management.

The **Provisions Committee** is responsible to ensure that Expected Credit Loss (ECL) is in line with IFRS 9 requirements. It will challenge, amend or approve key management judgements applied to ECL. The Committee is also responsible to assess significant credit risk assessments performed by the first lines of defence (Credit and Treasury departments) in relation to the determination of the application of the staging criteria together with the appropriateness of the impairment allowances measured by the Finance Department in accordance with the expected loss model prescribed by IFRS 9. The Committee, which meets on a regular basis, is chaired by the Chief Finance Officer and is composed of members of Senior Management from Credit, Debt Management, Finance and Risk Management.

The **IT Steering Committee** is responsible for the effective and cost-efficient application of information technologies, related personnel resources and funding in support of the objectives and needs of the Bank. The Committee meets at least every two months unless further meetings are required. The IT Steering Committee is chaired by the Chief Technology Officer and is composed of members of Senior Management.

The **Procurement Committee** is responsible for the approval of procurement of goods and services that exceed limits afforded to management and to make recommendations to the Management Board and to the Board of Directors on the award of contracts that exceed a defined value. The Committee meets at least once a month unless further meetings are required. The Committee is chaired by the Chief Operations Officer and is composed of members of Senior Management.

The **Core Banking Transformation Steering Committee** is responsible for overseeing the implementation of the new selected core banking solution, together with overseeing the transformation required in line with the Bank's operations. The Committee takes into consideration current banking practices that need to be transformed in order to adopt the solution selected. The Committee meets on a monthly basis, is chaired by the CEO and is composed of members of Senior Management. This Committee was wound up during the first quarter of FY 2020.

The **Anti-Money Laundering Committee (AMLC),** is responsible to provide effective management oversight over the Bank's AML initiatives. The AMLC is also responsible to review and approve recommendations of the two Working Groups established to assist the AMLC in fulfilling its function, namely the Client Onboarding and Monitoring Working Group and the AFC Implementation Working Group. AML policies approved by the AMLC are then presented for approval to the Compliance and Crime Prevention Committee, which is a Board Committee. The AMLC is chaired by the Chief Risk Officer and is composed of members of the Senior Management and the Group Chief Compliance Officer, the Chair of the Working Group on Client Onboarding and Monitoring and the Chair of the AFC Implementation Working Group.

Corporate governance statement of compliance (continued)

The **New Product Approval Committee (NPAC)** ensures the enhancement of long term value creation for the benefit of all stakeholders. The aim is to ensure adequate due diligence before a new product or service is launched by understanding and vetting its features. The Committee aims to identify and mitigate potential risks which impact both the product or service and the Group. The NPAC makes the final decision to either approve, decline or recommend changes to the proposed product or service.

The Committee also provides guidance and recommendations to the Board of Directors in case of a new business line. The NPAC is appointed by the Management Board and is chaired by the Chief Risk Officer to ensure a risk adequate approach and the necessary degree of intervention in relation to product development, hence also ensuring that the new proposed product or service falls within the Group's risk appetite.

The **Property Committee** ensures that the BOV Group's property management and capital projects related to property, are carried out in accordance with adopted policies, principles, strategies and the applicable legal framework. The Committee is chaired by the Chief Operations Officer and is composed of representatives from the Office of the Company Secretary, Architect Services Unit, the Administration and Risk functions.

The **Trustee Services Steering Committee (TSSC)** was set up to oversee that the winding down of the Trusts business is aligned with stated strategy and to monitor the interim management of the Trusts business during the winding down period. It is responsible to inter alia advise on and recommend processes to mitigate and manage potential costs and risks related to the winding down process, take decisions in line with Board approved policies and strategies, review changes in regulations that may have an impact on the business, and keep under review any litigation involving trustee services.

The main purpose of the **Custody Committee** was to approve, extend or decline business proposals from Fund clients under the remit of the Custody Unit. The de-risking strategy undertaken by the Bank equated to an immediate commencement of a gradual winding down of the entire Fund Custody book. As a result of this exercise, the remit of the Custody Committee for approval of new mandates/additional business was restricted. The Custody Committee's additional functionalities, which include the provision of data assessment /analysis by the Custodian vis-a-vis compliance with oversight obligations and related client follow-ups remained operative during the course of business.

The **Human Resources Steering Committee (HRSC**) is responsible to oversee the Human Resources (HR) Strategy, HR Policy development and implementation, direct the Group's HR Department towards effective HR management. The Committee, composed of Senior Management and external HR consultant provides advice, input and direction to the Group's HR Department regarding matters impacting HR Strategy and its respective implementation. During FY 2019, the HRSC held several meetings, the main focus being on the review and creation of structures within the Organisation in line with the Bank's strategy to ensure that the Group is in a position to meet the short and medium term challenges. Moreover, relative position descriptions are assessed to ensure alignment of roles throughout the Group.

The **Write-Offs Committee** has been entrusted with the sanctioning of definite write-offs as per limits defined by the Board of Directors and in line with the Write-Offs Policy. The Write-Offs Committee meets on an ad hoc basis. The committee is chaired by the CEO and is composed of members of Senior Management. The presence of the Risk function is required in all cases.

Management Board and Management Committees Restructuring – FY 2020

As part of the strengthening of the Bank's governance framework to improve efficiency and effectiveness of committees, during the first quarter of FY 2020, the Bank effected a number of changes at Management Board level and at Management Sub-Committees level. The Management Board is now known as Executive Committee and is composed of the following Chief Officers;

- Chief Executive Officer – Chair
- Chief Risk Officer
- Chief Finance Officer
- Chief Operations Officer
- Chief Business Development Officer (previously known as Chief Business Development Officer – Investments)
- Chief Credit Officer (previously known as Chief Business Development Officer – Credit)
- Chief Technology Officer
- Chief Officer Human Resources & Ethics (previously known as Chief Officer Ethics and Employee Development)

The Group Chief Compliance Officer attends Management Board meetings as an observer. Other Chief Officers and Bank Executives attend Management Board meetings by invitation.

Besides the Executive Committee, as from FY 2020 the Management Committees are as follows:

- Asset and Liability Management Committee (ALCO)
- Internal Control and Risk Management Committee
- Credit Committee (previously a Board Committee)
- Product Governance and Pricing Committee
- Change Management Committee

During the first quarter of FY 2020 a number of Management Committees were wound up or integrated into other Sub-Committees.

Corporate governance statement of compliance (continued)

Principle 6: Information and Professional Development

The CEO is appointed by the Board and is inter alia responsible for the recruitment and selection of Senior Management and consults with the Nominations and Governance Committee and with the Board on the appointment of Senior Management. Training of management and employees is a priority and internal and external training is provided by the Bank's Training Centre specifically set up for this purpose. The Bank also has a system in place which monitors management and staff morale.

On joining the Board, a Non-Executive Director is provided with briefings by the CEO and Chief Officers on the activities of the Bank. All Directors are provided with appropriate induction training and a dossier that, apart from incorporating relevant information on the Bank, also includes the Bank's Policy documents.

Directors may, where they judge it necessary to discharge their duties as Directors, take independent professional advice on any matter at the Bank's expense. Directors have access to the advice and services of the Company Secretary, who is responsible for ensuring adherence to Board procedures as well as good information flows within the Board and its Committees.

Informative sessions on blockchain, money laundering, market abuse, cyber and credit facilities, and training sessions on the capital regime were organised during the period under review for the Board and for the members of the Management Board. In addition, the Company Secretary directs members of the Board to seminars or conferences which serve as professional development for Directors in the discharge of their functions on the Board and on the Committees.

Principle 7: Evaluation of the Board's Performance

During the period under review, the Bank engaged an independent external consultant to undertake a suitability assessment on the Bank's Board of Directors, Management Board and Key Function Holders. The assessment was carried out both on an individual basis as well as on a collective basis.

The external consultant recommended that the Bank develops a comprehensive and ongoing training programme for its Directors. In order to address any gaps in the skills and knowledge of Directors, a training plan for Directors, Management Board members and Key Function Holders is in the process of being drawn up and will be implemented over the coming months.

Principle 8: Committees

The **Remuneration Committee** is dealt with under the Report of the Remuneration Committee, which also includes the Remuneration Statement of Compliance in terms of Code Provisions 8.A.3 and 8.A.4.

The **Nominations and Governance Committee** is dealt with under the Nominations Report as per Listing Rule 8.B.7.

Principles 9 and 10: Relations with Shareholders and with the Market and Institutional Shareholders

The Bank recognizes the importance of maintaining a dialogue with its shareholders and of keeping the market informed to ensure that its strategies and performance are well understood.

The Board is of the view that during the year under review the Bank has communicated effectively with the market through a number of company announcements and press releases.

The Bank also communicates with its shareholders through the Bank's Annual General Meeting (AGM) (further detail is provided under the section entitled General Meetings). All Directors attend the AGM and are available to answer questions, if necessary.

The Chairman and the CEO also ensure that sufficient contact is maintained with major shareholders to understand issues and concerns. The Chairman also ensures that arrangements are made for all Directors to attend the AGM and for the Chairmen of the Audit Committee, Remuneration Committee and the Nomination and Governance Committee to be available to answer questions at the AGM.

Apart from the AGM, the Bank communicates with its shareholders by way of the Annual Report and Financial Statements, by publishing its results on a six-monthly basis and through a bi-annual newsletter to shareholders. The Bank also issues the Interim Directors' Statement for Quarter 1 and Quarter 3 of its financial year. In addition, the Bank's website (www.bov.com) contains information about the Bank and its business, including an Investor Relations Section.

Furthermore, the Bank holds a meeting for stockbrokers and financial intermediaries, usually twice a year, to coincide with the publication of its Financial Statements. Other meetings with stockbrokers and financial intermediaries are held as necessary. From time to time, the Bank also holds meetings with the Malta Association of Small Shareholders.

The Office of the Company Secretary maintains two-way communication between the Bank and its investors. Individual shareholders can raise matters relating to their shareholdings and the business of the Group at any time throughout the financial year and are given the opportunity to ask questions at the AGM or submit written questions in advance. In terms of Article 18.3 of the Articles of Association of the Bank and Article 129 of the Companies Act,1995 (Chapter 386, Laws of Malta), the Directors may call an Extraordinary General Meeting on the requisition of shareholders holding not less than one-tenth of the paid up share capital of the Company.

Principle 11: Conflicts of Interest

Should an actual or potential conflict arise during the tenure of a directorship, a director must disclose and record the conflict in full and in time to the Board. A director shall not participate in a discussion concerning matters in which he has a conflict of interest unless the Board finds no objection to the presence of such director. In any event, the director shall refrain from voting on the matter.

Corporate governance statement of compliance (continued)

A director having a continuing material interest that conflicts with the interests of the Group, should take effective steps to eliminate the grounds of conflict. Each director should declare to the Group his or her interest in the share capital of the Group and should only deal in such shares as allowed by law and in accordance with internal policies.

Directors' interest in the share capital of the Bank as at 31 December 2019 was as follows:

	Beneficial Interest*
Alan Attard (resigned on 1 January 2020)	16,260 shares
Paul V Azzopardi (resigned on 15 February 2020)	10,068 shares
Miguel Borg	7,635 shares
Diane Bugeja (appointed on 19 December 2019)	29,310 shares
Alfred Lupi	34,204 shares
Joseph Zrinzo (resigned on 1 September 2019)	657,675 shares

**Includes any shares held by spouses or partners*

Alan Attard held 17,324,940 shares by way of non-beneficial interest in his capacity as one of the five trustees of the BOV Employees' Foundation.

No Director has any other benefit or non-beneficial interest in the share capital of the Bank.

As at 31 December 2019, the Directors below also held the following:

	Beneficial Interest**	
Joseph M Zrinzo (resigned on 1 September 2019)	35,000	3.5% BOV Subordinated Notes 2030 Series 2 tranche 1
	31,500	4.8% BOV Subordinated Bonds 2020

***Includes any holdings by spouses or partners*

Principle 12: Corporate Social Responsibility

"We are committed to play a leading and effective role in the Country's sustainable development, whilst tangibly proving ourselves to be responsible and caring citizens of the community in which we operate."

Bank of Valletta prides itself in being Malta's Community Bank, with a strong presence in almost every town and village in Malta and Gozo. Just as we are committed to serve our customers by providing high-quality personalized service, backed by superior financial knowledge, we are also continuously looking for ways to make a difference to the communities within which we serve.

This is achieved through BOV's extensive Community Programme and through continuous investment in staff at all levels. There is no doubt that staff is a key intangible asset for the BOV Group. In today's dynamic and continuously changing business world, human assets, as opposed to fixed or tangible assets, differentiate us from competition.

While working hard to update legacy systems and turning to technology to enhance operating effectiveness and improve the customer experience, we continually strive to offer dynamic and different career paths to match employee interests, skills and experience, all the while recruiting talented people and providing appropriate training and development.

Besides the Equality Mark Certification, which recognized BOV as having a non-discriminative workplace, the Bank was this year presented with the 'Premju Socjeta Ġusta' award in recognition of its work in strengthening the rights of persons with disability. Regular 'dress-down days' in aid of charitable organisations, blood donation drives, as well as other philanthropic initiatives, further support staff engagement within the community.

Through the Community Programme we work very closely with several of our stakeholders, including Government, non-governmental and non-profit organisations, charities and other local businesses to support projects and initiatives that add value to the community. The highlights for financial year 2019 are the following:

Arts and Culture – BOV has always been synonymous with local art and culture. Malta's participation in 'The Venice Art Biennale', one of the largest exhibitions of contemporary art in the world, received BOV's support this year, as did the Venice Art Biennale Malta Pavilion Outreach Programme for Youths organised by the Arts Council Malta. The Manoel Theatre annual opera, as well as opera month in Gozo, featuring two major operas at Teatru Astra and Teatru Aurora, once again garnered BOV's support.

The Bank also supported Maltese Tenor Joseph Calleja and the BOV Joseph Calleja Foundation, which supports underprivileged children as well as children with distinctive or unique artistic talents who are in some way unable to develop their talents independently.

Heritage – In the area of local heritage, BOV supported the restoration of the 17th Century Crucifix at the Franciscan Church of Jesus (Ta' Ġieżu) in Valletta, deemed both miraculous and a national monument. BOV also supported conservation of the 16th Century baroque 'Grand Salon' at the Auberge de Provence in Valletta. The unique 'Return of the Holy Family from Egypt', an anonymous, early 18th century painting, and the only work of art found in the Comino Church, is also receiving much needed conservation through our assistance. Another unique project we supported is the restoration of a late 1800s Gilt Monstrance Throne (Gelandra) found at the St Dominic Church of the Annunciation in Birgu.

Corporate governance statement of compliance (continued)

Bank of Valletta is proud of the healthy collaborative relationship it has with Malta's premiere organisations active in the field of heritage preservation, mainly Heritage Malta, Fondazzjoni Wirt Artna, Fondazzjoni Patrimonju Malti and Din l-Art Ħelwa.

Natural Environment – BOV is also making crucial contributions to the local environment. Saving Malta's national fish, the endemic Bużaqq (killifish) featured high on this year's agenda. This multi-year project driven by Nature Trust reached a major milestone this year when the first fish were introduced at 'il-Magħluq' in Marsaskala, a site that received major upgrading specifically for this project.

The Bank continues its support to 'Dinja Waħda', a nationwide education and awareness program by the NGO BirdLife Malta. This year focus was made on protecting wildlife and habitats through outdoor activities for school children, held both on school grounds and through educational visits to Malta's nature reserves.

Philanthropy – Staff engagement ranked high on BOV's social agenda. Staff members came to work in colourful attire in May to support Caritas, in Pink to support the 'Pink October' cause, while others sported a moustache during the Movember campaign.

The l-Istrina BOV Piggy Bank Campaign 2019 raised €54,000, which the Bank topped up by another €200,000, in its efforts to assist the Malta Community Chest Fund Foundation and its cause. The Marigold Foundation – BOV in the Community, the trust that manages requests by NGOs and individuals with philanthropic objectives, continued its journey towards the creation of a better community.

Sport – The BOV logo is a staple fixture in most local sporting venues, with the bank maintaining its strong position as the main sponsor of the Malta Football Association, the Malta Basketball Association and the Aquatic Sports Association of Malta. Besides the entertainment and health elements associated with sport, BOV encourages individual excellence through the 'Player of the Month' awards for football, basketball and waterpolo. The Bank also supports other disciplines such as sailing, horse-racing, tennis and ten-pin bowling.

Support at grassroots level is tackled through the Youth Development Scheme in collaboration with SportMalta, a scheme for athletes below the age of 18. The Bank also encourages its own staff to participate in sporting events through the BOV Sports and Social Club.

Education – Education was given a broader dimension this year through BOV's financial-education campaign. Throughout 2019, over 100 articles about banking, investments, financial safety and security were issued. Informative sessions and symposia were also organised about projects supported by the bank, with the aim of creating more awareness about Malta's Cultural heritage and divulging information that would otherwise get 'lost' and would never reach the local community.

The 'Read with Me' project, held in collaboration with the Malta Literacy Agency, continued to focus on early literacy and parental education, this year reaching over 2,500 children and their parents through shared reading experiences.

Strategic Alliances – The Bank exploited its close relationships with the main local representative bodies and business associations. These included the Malta Chamber of Commerce, Enterprise and Industry, the Malta Hotels and Restaurants Association, the Gozo Business Chamber and the Chamber of Engineers. Various information sessions were held for their members and the general public, facilitating open discussion about topical issues of interest.

The success of a community goes beyond sustaining a prosperous economy. A successful community finds ways to retain its values, its historic character, its scenic beauty and its sense of belonging. The Corporate Social Responsibility initiatives highlighted above are just a small representation of the effort undertaken by the bank as a responsible, corporate citizen.

C. NON-COMPLIANCE WITH THE CODE

Principle 4 (Code Provision 4.2.7)

The Code recommends "the development of a succession policy for the future composition of the Board of Directors and particularly the executive component thereof, for which the Chairman should hold key responsibility". Although the Bank does not have a Succession Policy per se, the concept of Rotation of Directors (as further explained under Principle 3 above) was introduced to ensure continuity at Board level and is embedded within the Bank's Memorandum and Articles of Association.

Principle 6 (Code Provision 6.4.4)

During the financial year under review the Bank did not have a system in place to establish a succession plan for Senior Management. This notwithstanding, the Bank has always been successful in appointing suitable individuals internally and externally. Moreover, the Bank is currently working on a succession planning policy.

Principle 7 (Code Provision 7.1)

The Code recommends that the Board should appoint a committee chaired by a Non-Executive Director in order to carry out a performance evaluation of its role. During the financial year under review the Nominations and Governance Committee did not undertake a performance evaluation of the Board and of its Committees. Instead, and as highlighted earlier in the report, the Bank engaged an external consultant to undertake a comprehensive suitability assessment on the Bank's Board of Directors, both individually and collectively.

Principle 9 (Code Provision 9.3 and 9.4)

Code Provision 9.3 requires the Bank to have in place a mechanism to resolve conflicts between minority shareholders and controlling shareholders. Code Provision 9.4 requires that minority shareholders should be allowed to formally present an issue to the Board of Directors. Both Code Provisions were not necessary to the Bank during the financial year.

Corporate governance statement of compliance (continued)

D. INTERNAL CONTROL

Authority to manage the activities of the Bank is delegated to the CEO within the limits set by the Board.

The Board is ultimately responsible for the Bank's systems of internal control and for reviewing their effectiveness. Such systems are designed to manage, rather than eliminate, the risk of failure to achieve business objectives, and can only provide reasonable as opposed to absolute assurance against material misstatement or loss. Through the Audit Committee, the Risk Management Committee and the Compliance and Crime Prevention Committee, the Board reviews the process and procedures to ensure the effectiveness of the Group's systems of internal control, which are monitored by the Group Internal Audit Department.

The key features of the Group's systems of internal control are as follows:

Organisation

The Group operates through the Board of Directors of subsidiary companies and equity-accounted investee companies with clear reporting lines and delegation of powers.

Control Environment

The Group is committed to the highest standards of business conduct and seeks to maintain these standards across all of its operations. Group policies and employee procedures are in place for the reporting and resolution of fraudulent activities. The Group has an appropriate organisational structure for planning, executing, controlling and monitoring business operations in order to achieve Group objectives.

Risk Identification

The Management of each of the Group members is responsible for the identification and evaluation of key risks applicable to their areas of business. The risk management model adopted by BOV is the classic "three lines of defence model" wherein the first line of defence is constituted by the functions that own and manage risks, namely the business units; the second line is constituted by the functions that oversee risks, namely Risk Management, Compliance and Anti-Financial Crime; and the third line is constituted by Internal Audit, which is the function that provides independent assurance. The Risk Management function, within the second line of defence, falls under the responsibility of the Chief Risk Officer, and operates within a wider Bank structure that reflects the risk appetite and risk management philosophy articulated by the Board of Directors.

Reporting

Functional, operating and financial reporting standards are applicable to all entities of the Group. These are supplemented by operating standards set, as required, by the Bank's Board and the Management Board. Systems and procedures are in place to identify, control and to report on the major risks including credit risk, changes in the market prices of financial instruments, liquidity, operational error and fraud. Exposure to these risks is monitored by ALCO and by the Risk Management Committee. The Board receives periodic management information giving comprehensive analysis of financial and business performance including variances against budgets.

E. LISTING RULE 5.97.5

Whilst Listing Rule 5.97.5 is not applicable, the information relating to the shareholder register required by this Listing Rule is found in the Directors' Report.

F. GENERAL MEETINGS

The general meeting is the highest decision making body of the Bank. A general meeting is called by twenty-one days' notice and it is conducted in accordance with the Articles of Association of the Bank.

The Annual General Meeting (AGM) deals with what is termed as "ordinary business", namely, the receiving or adoption of the annual financial statements, the declaration of a dividend, if any, the appointment of the auditors, Board authorisation to fix the auditors' emoluments and the Election of Directors. Other business which may be transacted at a general meeting (including at the AGM) will be dealt with as Special Business.

All shareholders registered in the Shareholders' Register on the Record Date as defined in the Listing Rules, have the right to attend, participate and vote in the general meeting. A shareholder or shareholders holding not less than 5% in nominal value of all the shares entitled to vote at the general meeting may request the Bank to include items on the agenda of a general meeting and/or table draft resolutions for items included in the agenda of a general meeting. Such requests are to be received by the Bank at least forty six days before the date set for the relative general meeting.

A shareholder who cannot participate in the general meeting can appoint a proxy by written or electronic notification to the Bank. Every shareholder represented in person or by proxy is entitled to ask questions which are pertinent and related to items on the agenda of the general meeting and to have such questions answered by the Directors or by such persons as the Directors may delegate for that purpose.

Remuneration report as at 31 December 2019

1. Terms of Reference and Membership of the Remuneration Committee

The Remuneration Committee (the Committee) is charged with overseeing the development and implementation of the remuneration and related policies of the Group. Its primary purpose is to make recommendations to the Board of Directors on the remuneration policy of the Group, support the Board of Directors in overseeing the remuneration system's design and operation and ensure that remuneration is appropriate and consistent with the Bank's culture, long term business and risk appetite, performance and control environment as well as with any legal or regulatory requirements. The role of the Committee is to devise the appropriate remuneration packages needed to attract, retain and motivate Directors, as well as key function holders required for the proper governance of the Group.

During FY 2019 the Committee was composed of Taddeo Scerri (Chairman), Anita Mangion and Antonio Piras as members, all of whom are Independent Non-Executive Directors. The Chief Executive Officer, the Chief Risk Officer and the Chief Officer Human Resources and Ethics attend meetings of the Committee. None of the Executives participated in the discussion regarding their remuneration. The Company Secretary acts as secretary to the Committee.

2. Meetings

The Committee held five meetings during the period under review, which were attended by all members.

3. Remuneration Statement

3.1 Remuneration Policy – Executive Management

The Board of Directors determines the framework of the overall remuneration policy for Executive Management based on recommendations from the Committee. The Committee, on the recommendations of the Chief Executive Officer, then establishes the individual remuneration arrangements of the Group's Executive Management, namely the members of the Management Board and Heads of Departments.

The Remuneration Policy applies consistently to all employees within the Group. Its objective is to align employees' remuneration with the Group's performance, business strategy and business models, risk appetite framework, values and long term goals. The overriding principle of the Remuneration Policy is that individual performance is evaluated according to both quantitative/financial and qualitative/behavioural measures. Further details about the Bank's Remuneration Policy are found in the Capital and Risk Management Report.

The Committee considers that the current Executive Management remuneration packages are based upon the appropriate local market equivalents and are adequate for the responsibilities involved. The Committee is of the opinion that the remuneration packages are such, as to enable the Bank to attract, retain and motivate executives having the appropriate skills and qualities, in order to ensure the proper management of the organisation. Such packages should therefore be kept under constant review.

Hereinafter, for the purposes of this Remuneration Statement, references to "Senior Executives" shall mean the Chief Executive Officer and the other seven members of the Management Board.

Senior Executives are in full employment with the Bank on an indefinite contract but their appointment on the Management Board is on a definite contract. They enjoy the health insurance arrangements and death in service benefits as all Bank employees. Senior Executives are also entitled to the use of a company car. Certain members of the Management Board have a clause in their contract, wherein should their contract be terminated without due reason, they may be eligible for monetary compensation. Share options and profit sharing are not part of the Group's Remuneration Policy. Subject to the foregoing, the terms and conditions of the Management Board members' contracts are considered as commercially sensitive information.

The Chief Executive Officer's remuneration is reviewed and approved by the Committee. The Chief Executive Officer is eligible for an annual bonus entitlement by reference to the attainment of pre-established objectives and targets as approved by the Committee. The Members of the Management Board are also eligible for an annual bonus entitlement.

The Members of the Management Board are eligible for an annual salary increase within a maximum salary range approved by the Committee.

No supplementary pension or other pension benefits are payable to the Senior Executives. Insofar as early retirement schemes are concerned, the Senior Executives are subject to the schemes which are set out and defined in the Collective Agreement (for Managerial and Clerical Grades) as may be applicable to employees from time to time.

The Committee is of the view that the amount of performance bonus paid out at all staff levels is not significant.

Total emoluments received by Senior Executives during FY 2019 are reported on page 64 in terms of Code Provisions 8.A.5.

Remuneration report as at 31 December 2019 (continued)

Variable Remuneration of Senior Executives (Management Board)

The Variable Remuneration of Senior Executives is determined by the Remuneration Committee. During Financial Year 2019 Management Board members qualified for a collective performance-related pay system. The payment of bonuses payable to the Management Board members was linked to the performance and achievement of the objectives of the Management Board. The objectives of the Management Board were based partly on financial targets (financial ratios) and partly on qualitative targets (qualitative ratios).

3.2 Remuneration Policy – Directors

The Board of Directors is composed of Executive and Non-Executive Directors. Directors' remuneration is determined and regulated by service contracts as detailed below. The maximum annual aggregate emoluments that may be paid to the Directors is approved by the shareholders at the General Meeting in terms of Article 33.1 of the Bank's Articles of Association. The aggregate emoluments of all directors of €450,000 per annum, was fixed at an Extraordinary General Meeting held on 27 July 2017. This amount excludes the salaries of Directors in the Bank's employment.

Remuneration Policy of Directors for Shareholders' Approval

In terms Listing Rule 12.26A which was introduced in 2019, the Bank is required to establish a remuneration policy as regards directors. Shareholders are to be granted the right to vote on the remuneration policy at the general meeting. The Bank shall be placing for shareholders' approval during the forthcoming Annual General Meeting, a remuneration policy for directors.

Service Contracts for Directors

The Directors have service contracts with the Bank, none of which provide for severance payments upon termination of their respective directorship. In terms of the said service contracts, the Directors are entitled to certain benefits after the termination of their directorship, including discounts on products and services offered by the Group. Service contracts regulate the term of office of Non-Executive Directors, referring specifically to the concept of Rotation of Directors provided within the Memorandum and Articles of Association (as further explained under Principle 3 of the Corporate Governance Statement of Compliance).

The Chief Executive Officer is appointed as Executive Director, on an ex officio basis, by virtue of his role of Chief Executive Officer. Moreover, the second Executive Director on the Board has a term of office of three (3) years and shall thereafter be eligible for re-appointment.

Vacation of office of Directors shall be served in writing. Service contracts also provide for the Directors' powers and duties vis à-vis the Bank and their obligation to dedicate sufficient time to carry out their responsibilities. Directors are obliged to avoid conflicts of interest and shall take reasonable steps to keep the Bank's matters confidential. Directors' emoluments are designed to reflect the time committed by Directors to the Bank's affairs, including the different Board Committees of which Directors are members, and their responsibilities on such Committees. None of the Directors, in the capacity as a Director of the Bank, is entitled to profit sharing, share options or pension benefits. In terms of non-cash benefits, Directors are entitled to health insurance and to a refund of out-of-pocket expenses.

The Directors' fees as approved by the Board of Directors are as follows:

Directors' Fees	**€**
Chairman	80,000
All other Directors (both Executive and Non-Executive)	20,500
Board Committees Fees	
Chairman	5,000
Members	3,000

Two of the Non-Executive Directors, as well as both the Executive Directors, are employees of the Bank and therefore also receive remuneration by virtue of their employment.

Total fees received by Directors during FY 2019 are reported on page 64 in terms of Code Provisions 8.A.5.

Review of Remuneration Policy for Senior Management and Employees

The Bank is in the process of revising its Remuneration Policy for Senior Management and Employees so that the assignment of variable remuneration shall become subject to:
i) risk-adjusted performance
ii) the individual and collective progress made to enhance the institution's risk culture, as well as,
iii) the contribution to remediate findings of the Internal Audit Function in the respective business area.
The Remuneration Policy shall be further revised to include malus and clawback clauses. Risk-adjusted performance indicators for Senior Management and all employees, as well as a variable remuneration structure shall also be developed. It is envisaged that the amendments to the Remuneration Policy will be concluded in 2020.

Remuneration report as at 31 December 2019 (continued)

3.3 Code Provision 8.A.5

Senior Executives' Emoluments (Management Board)

Fixed Remuneration	Group Directors Fees	Variable Remuneration	Share Options	Others
€1,094,175*	€30,000**	€72,000	None	Non-cash benefits: health insurance and refund of out-of-pocket expenses

*This amount includes compensation paid to a former senior executive in connection with the termination of his activities during FY 2019.

**This amount represents emoluments received by senior executives in relation to their directorships on the Bank's subsidiary companies.

Directors' Fees

Fixed Remuneration	Variable Remuneration	Share Options	Others
€362,249	None	None	Non-cash benefits: health insurance and refund of out-of-pocket expenses: €14,131

Directors' fees including benefits – FY 2019	**€**
Taddeo Scerri (Chairman)	97,715
Stephen Agius	27,961
Alan Attard	27,961
Paul V Azzopardi	30,094
Miguel Borg	20,921
Diane Bugeja (appointed 19 December 2019)	730
James Grech	30,763
Alfred Lupi	33,382
Alfred Mifsud (appointed 19 December 2019)	730
Mario Mallia	24,688
Anita Mangion	27,763
Antonio Piras	25,789
Joseph M Zrinzo (resigned 1 September 2019)	27,882
Total	376,380

Nominations report as at 31 December 2019

The Nominations and Governance Committee

The Nominations and Governance Committee (the Committee) was set up by the Board of Directors and is enshrined within the Bank's Memorandum and Articles of Association. The Committee works under the guidance of its Terms of Reference as approved by the Board of Directors.

The role of the Committee is twofold, namely (i) to ensure that the composition of the Bank's Board of Directors has the appropriate level and mix of experience, skills and competence that are required for the operation of a credit institution and (ii) to ensure that persons occupying the post of Directors meet the requirements of prevailing legislation and regulation.

From time to time, the Board of Directors reviews the Terms of Reference of the Committee. However, certain fundamentals are entrenched in the Memorandum and Articles of Association, which set out both the basic role of the Committee as well as its functions, namely:

i) To recommend to the Board of Directors, candidates having the right attributes, including integrity, skill, competence and experience individually; and who can contribute to the collective skills, experience and competence required at Board level;
ii) To make recommendations to the Board of Directors on persons considered as independent to occupy positions on the Board;
iii) To make recommendations on matters such as succession planning, establishment of policies and procedures related to the selection of Senior Management and the optimal size of the Board of Directors and the Management Board;
iv) To ensure that nominations to the Board of Directors are made on merit and in line with the overall requirements of the skills and competence required;
v) To ensure that persons whose nomination is approved and recommended to shareholders or the Board of Directors as the case may be, are in a position to dedicate sufficient time and resources to the office of Director;
vi) To monitor on an ongoing basis any significant additional time commitments of the Board Members;
vii) To evaluate and test each candidate to the Board against guidelines issued from time to time by the Regulators; and
viii) Periodically assess the skills, knowledge and experience that may be required within the Board and make recommendations to the Board.

With a view to avoid possible perceptions of conflicts of interest in the scrutiny and approval of candidates for appointment as Non-Executive Directors, the Articles of Association provide that no member of the Committee shall be present when his nomination as a director or a matter which concerns that member in question, is being evaluated by the Committee. In these instances such member shall be substituted by another director. In this same context, the proposals include a system of rotation that would, as far as practicably possible, ensure that members on the Committee will not have an interest in the scrutiny of other candidates for the same position.

The Committee is Chaired by the Chairman of the Bank and composed of two other Independent Non-Executive Directors.

The Committee held eleven meetings during the period under review.

Members	Meetings Held: 11 Meetings attended by member	
Taddeo Scerri (Chairman)	10	(out of 11)
Joseph M Zrinzo (resigned on 1 September 2019)	8	(out of 8)
Stephen Agius	11	
Alan Attard*	1	(out of 1)
Alfred Lupi**	1	(out of 1)
Antonio Piras (appointed on 27 September 2019)	1	(out of 1)

** in lieu of Mr Joseph M Zrinzo*
*** in lieu of the Chairman (Taddeo Scerri)*

During FY 2019, the Committee considered the amendments to the Articles of Association in particular for the inclusion of a new Clause 27A whereby the Non-Executive Directors of the Board were granted the right to co-opt up to a maximum of 2 additional Non-Executive Directors on the Board. The Committee focused on the nomination process for the appointment of Non-Executive Directors on the Board including also the 2 additional Non-Executive Directors who were co-opted to the Board. The Committee conducted a suitability assessment on candidates seeking appointment on the Board. During the year, the Committee ensured that persons whose nomination is approved and recommended to shareholders or the Board of Directors for the post of Non-Executive Directors are in a position to dedicate sufficient time commitment to their position as Non-Executive Directors on the Bank's Board. The Committee was also responsible to monitor any additional time commitments by Board members. In addition the Committee considered appointments of executives in various roles within the Bank and was also actively involved in the engagement of the new Chief Executive Officer.

Disclosures for the purposes of Regulation 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms:

While information about every member of the Board is found on pages (ii) to (iv) of the Annual Report, a detailed curriculum vitae of every member of the Board and of the nominees is available at the Office of the Company Secretary.

Independent Assurance Report to the Shareholders of Bank of Valletta p.l.c.

Report required by Listing Rule 5.98 issued by the Listing Authority in Malta

We were engaged by the Directors to report on specific disclosures in the Corporate Governance Statement (the "Disclosures") of Bank of Valletta p.l.c. (the "Company") as at 31st December 2019 as to whether these are in compliance with corporate governance regulations set out in the Listing Rules issued by the Listing Authority, the Malta Financial Services Authority (the "Listing Rules"). We are required to report in the form of an independent reasonable assurance conclusion as to whether:

(a) in light of our knowledge and understanding of the Company and its environment obtained during the course of the statutory audit, we have identified material misstatements with respect to the information requirements referred to in Listing Rule 5.97.4 and, and, for issuers of securities that carry voting rights that are subject to the requirements of Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids, Listing Rule 5.97.5. Where material misstatements are identified in relation to the requirements of Listing Rules 5.97.4 and 5.97.5, as applicable, we shall, in addition to our opinion, provide an indication of the nature of such misstatements; and,

(b) the Disclosures include the other information required by Listing Rule 5.97, in so far as it is applicable to the Company.

Responsibilities of the Directors

The directors are responsible for preparing and presenting the Disclosures that are free from material misstatement and for the information contained therein.

This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and presentation of the Disclosures that is free from material misstatement whether due to fraud or error. It also includes ensuring that the Company complies with the Listing Rules, selecting and applying policies and procedures in relation to both financial and non-financial information, making estimates and judgement that are reasonable in the circumstances and for maintaining adequate records in relation to the Disclosures.

The Directors are also responsible for preventing and detecting fraud and for identifying and ensuring that the Company complies with laws and regulations applicable to its activities.

The Directors are also responsible for ensuring that staff involved with the preparation and presentation of the Disclosures are properly trained, information systems are properly updated and that any changes in reporting encompass all significant reporting units.

Auditors' Responsibilities

Our responsibility is to examine the Disclosures and to report thereon in the form of a reasonable assurance conclusion based on the evidence obtained. We conducted our engagement in accordance with International Standard on Assurance Engagements 3000, *Assurance Engagements Other Than Audits or Reviews of Historical Financial Information* issued by the International Auditing and Assurance Standards Board.

That standard requires that we plan and perform our procedures to obtain reasonable assurance about whether the Disclosures are properly prepared and presented, in all material respects, in accordance with the requirements set out in the relevant Listing Rules.

The firm applies International Standard on Quality Control 1 *Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements* and, accordingly, maintains a comprehensive system of quality control including documented policies and procedures regarding compliance with ethical requirements, professional standards and applicable legal and regulatory requirements.

We have complied with the independence and other ethical requirements of the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants*, together with the ethical requirements that are relevant to our assurance engagement in accordance with the *Accountancy Profession (Code of Ethics for Warrant Holders) Directive* issued in terms of the Accountancy Profession Act (Chapter 281, Laws of Malta).

The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the Disclosures whether due to fraud or error.

In making those risk assessments, we have considered internal control relevant to the preparation and presentation of the Disclosures in order to design assurance procedures that are appropriate in the circumstances, but not for the purposes of expressing a conclusion as to the effectiveness of Company's internal control over the preparation and presentation of the Disclosures. Our engagement also included assessing the appropriateness of the Disclosures, the suitability of the criteria, being the relevant Listing Rules, in preparing and presenting the Disclosures in the circumstances of the engagement and evaluating the appropriateness of the method used in the preparation and the overall presentation of the Disclosures. Reasonable assurance is less than absolute assurance.

KPMG, a Maltese civil partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.
Document classification: KPMG Confidential

The firm is registered as a partnership of Certified Public Accountants in terms of the Accountancy Profession Act.

A list of partners and directors of the firm is available at 92, Marina Street, Pietà, PTA9044, Malta.

Independent Assurance Report to the Shareholders of Bank of Valletta p.l.c. (continued)

We are not required to, and we do not, consider whether the directors' statements on internal control and risk management systems cover all the risks and controls in relation to the financial reporting process or form an opinion on the effectiveness of the Company's corporate governance procedures or its risks and control procedures, nor on the ability of the Company to continue in operational existence. Our opinion in relation to the disclosures pursuant to Listing Rule 5.97.4 and Listing Rule 5.97.5 is based solely on our knowledge and understanding of the Company and its environment obtained in forming our opinion on the audit of the financial statements. We have not performed any procedures by way of audit, verification or review on the underlying information from which the other disclosures required by Listing Rule 5.97 is derived.

We also read the other information included in the Annual Report in order to identify any material inconsistencies with the Disclosures.

Conclusion

Our conclusion has been formed on the basis of, and is subject to, the matters outlined in this report.

We believe that the evidence we have obtained is sufficient and appropriate to provide a basis for our conclusion.

In our opinion:

(a) in light of the knowledge and understanding of the Company and its environment obtained during the course of our statutory audit, we have not identified material misstatements with respect to the following disclosures:

   (i) the information referred to in Listing Rule 5.97.4, included in the directors' Corporate Governance Statement, as this relates to the Company's internal control and risk management systems in relation to the financial reporting process; and,

   (ii) the information referred to in Listing Rule 5.97.5, included in the Directors' Report, insofar as it is applicable to the Company;

(b) the other disclosures required by Listing Rule 5.97 have been included in the directors' Corporate Governance Statement, as these apply to the Company.

The Principal authorised to sign on behalf of KPMG on the work resulting in this assurance report is Noel Mizzi.

KPMG
Registered Auditors,

18 March 2020

Statements of profit or loss

For the year ended 31 December 2019

	Note	The Group		The Bank	
		2019	2018	2019	2018
		€000	€000	€000	€000
Interest and similar income					
- on loans and advances	2	169,825	165,177	169,825	165,177
- on debt and other fixed income instruments	2	37,138	48,719	37,138	48,719
Interest expense	3	(54,113)	(57,350)	(54,113)	(57,350)
Net interest income		**152,850**	**156,546**	**152,850**	**156,546**
Fee and commission income		86,410	92,368	77,403	83,346
Fee and commission expense		(12,582)	(11,231)	(12,582)	(11,231)
Net fee and commission income	4	**73,828**	**81,137**	**64,821**	**72,115**
Dividend income		757	1,075	30,078	12,828
Trading profits	5	22,241	18,019	22,243	18,007
Net gain on investment securities and hedging instruments	6	88	989	88	989
Operating income		**249,764**	**257,766**	**270,080**	**260,485**
Employee compensation and benefits	7	(71,240)	(65,696)	(68,593)	(63,043)
General administrative expenses		(78,306)	(54,596)	(76,842)	(53,093)
Amortisation of intangible assets	20	(6,317)	(4,607)	(6,317)	(4,607)
Depreciation of property and equipment	21	(7,155)	(5,699)	(7,096)	(5,636)
Net impairment reversals	8	11,562	10,816	11,562	10,816
Operating profit before litigation provision		**98,308**	**137,984**	**122,794**	**144,922**
Litigation provision	33	(25,000)	(75,000)	(25,000)	(75,000)
Operating profit		**73,308**	**62,984**	**97,794**	**69,922**
Share of results of equity-accounted investees, net of tax	18	15,897	8,214	-	-
Profit before tax	9	**89,205**	**71,198**	**97,794**	**69,922**
Income tax expense	10	(25,713)	(19,788)	(26,569)	(19,357)
Profit for the year		**63,492**	**51,410**	**71,225**	**50,565**
Earnings per share	11	**10.9c**	**8.8c**	**12.2c**	**8.7c**

Statements of profit or loss and other comprehensive income

For the year ended 31 December 2019

	Note	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Profit for the year		63,492	51,410	71,225	50,565
Other comprehensive income					
Items that may be reclassified subsequently to profit or loss:					
Debt investments at FVOCI					
- change in fair value		2,867	(1,958)	2,867	(1,958)
tax thereon		(1,003)	685	(1,003)	685
Items that will not be reclassified to profit or loss:					
Equity investments at FVOCI					
- change in fair value		4,711	(1,904)	4,711	(1,904)
tax thereon		(1,649)	666	(1,649)	666
Property revaluation	21	22	12,762	22	12,762
tax thereon		(2)	(1,276)	(2)	(1,276)
Remeasurement of actuarial losses on defined benefit plans	35	(409)	(3,777)	(409)	(3,777)
tax thereon		143	1,322	143	1,322
Other comprehensive income for the year, net of tax		4,680	6,520	4,680	6,520
Total comprehensive income		68,172	57,930	75,905	57,085

The notes are an integral part of these financial statements.

Statements of financial position

As at 31 December 2019

	Note	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	13	3,669,580	3,400,588	3,669,580	3,400,588
Financial assets at fair value through profit or loss	14	205,139	206,206	204,979	205,227
Investments	15	3,071,160	3,314,955	3,071,160	3,314,955
Loans and advances to banks	16	501,686	490,644	501,686	490,644
Loans and advances to customers at amortised cost	17	4,445,812	4,362,983	4,445,812	4,362,983
Investments in equity-accounted investees	18	101,479	108,510	52,870	52,870
Investments in subsidiary companies	19	-	-	6,230	6,230
Intangible assets	20	60,463	42,043	60,463	42,043
Property and equipment	21	126,196	119,155	126,031	118,978
Current tax		15,185	7,606	14,678	7,086
Deferred tax	22	76,017	71,749	76,017	71,749
Assets held for realisation	40	10,123	4,335	10,123	4,335
Other assets	23	42,627	7,900	42,627	7,900
Prepayments		5,142	10,314	3,031	8,851
Total Assets		**12,330,609**	**12,146,988**	**12,285,287**	**12,094,439**
LIABILITIES					
Financial liabilities at fair value through profit or loss	14	10,907	8,812	10,907	8,812
Amounts owed to banks	24	66,047	146,021	66,047	146,021
Amounts owed to customers	25	10,629,719	10,414,908	10,632,260	10,417,999
Debt securities in issue	26	-	40,197	-	40,197
Deferred tax	22	5,736	5,743	5,736	5,743
Other liabilities	27	189,109	196,421	188,881	196,204
Provisions	33	118,109	95,767	118,109	95,767
Accruals and deferred income	28	484	539	-	-
Derivatives designated for hedge accounting	29	13,963	10,206	13,963	10,206
Subordinated liabilities	30	234,230	234,241	234,230	234,241
Total Liabilities		**11,268,304**	**11,152,855**	**11,270,133**	**11,155,190**
EQUITY					
Called up share capital	31	583,849	530,772	583,849	530,772
Share premium account	31	49,277	49,277	49,277	49,277
Revaluation reserves	32	54,898	50,034	54,786	49,922
Retained earnings	32	374,281	364,050	327,242	309,278
Total Equity		**1,062,305**	**994,133**	**1,015,154**	**939,249**
Total Liabilities and Equity		**12,330,609**	**12,146,988**	**12,285,287**	**12,094,439**
MEMORANDUM ITEMS					
Contingent liabilities	33	341,618	335,405	341,618	335,405
Commitments	34	1,828,756	1,881,392	1,828,756	1,881,392

The notes are an integral part of these financial statements. These financial statements were approved by the Board of Directors and authorised for issue on 18 March 2020 and signed on its behalf by:

Taddeo Scerri
Chairman

Alfred Lupi
Director

Rick Hunkin
Director and Chief Executive Officer

Statements of changes in equity

For the year ended 31 December 2019

The Group	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000
At 31 December 2017	**525,000**	**45,427**	**33,194**	**358,466**	**962,087**
Adjustments on initial application of IFRS 9	-	-	9,573	(17,779)	**(8,206)**
At 1 January 2018	**525,000**	**45,427**	**42,767**	**340,687**	**953,881**
Profit for the year	-	-	-	51,410	**51,410**
Other comprehensive income					
Debt investments at FVOCI					
- change in fair value, net of tax	-	-	(1,273)	-	**(1,273)**
Equity investments at FVOCI					
- change in fair value, net of tax	-	-	(1,238)	-	**(1,238)**
- change in fair value transferred to retained earnings, net of tax	-	-	(1,246)	1,246	**-**
Property revaluation, net of tax	-	-	11,486	-	**11,486**
Release of surplus on sale of property, net of tax	-	-	(462)	462	**-**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(2,455)	**(2,455)**
Total other comprehensive income	-	-	7,267	(747)	**6,520**
Total comprehensive income for the year	-	-	7,267	50,663	**57,930**
Transactions with owners, recorded directly in equity:					
Scrip Dividend	5,772	3,850	-	(9,622)	**-**
Dividends to equity holders	-	-	-	(17,678)	**(17,678)**
	5,772	3,850	-	(27,300)	**(17,678)**
At 1 January 2019	**530,772**	**49,277**	**50,034**	**364,050**	**994,133**
Profit for the year	-	-	-	63,492	**63,492**
Other comprehensive income					
Debt investments at FVOCI					
- change in fair value, net of tax	-	-	1,864	-	**1,864**
Equity investments at FVOCI					
- change in fair value, net of tax	-	-	3,062	-	**3,062**
Property revaluation, net of tax	-	-	20	-	**20**
Release of surplus on sale of property, net of tax	-	-	(82)	82	**-**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(266)	**(266)**
Total other comprehensive income	-	-	4,864	(184)	**4,680**
Total comprehensive income for the year	-	-	4,864	63,308	**68,172**
Transactions with owners, recorded directly in equity:					
Bonus issue	53,077	-	-	(53,077)	**-**
At 31 December 2019	**583,849**	**49,277**	**54,898**	**374,281**	**1,062,305**

The notes are an integral part of these financial statements.

Statements of changes in equity

For the year ended 31 December 2019 (continued)

	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000
The Bank					
At 31 December 2017	**525,000**	**45,427**	**33,082**	**304,539**	**908,048**
Adjustments on initial application of IFRS 9	-	-	9,573	(17,779)	**(8,206)**
At 1 January 2018	**525,000**	**45,427**	**42,655**	**286,760**	**899,842**
Profit for the year	-	-	-	50,565	**50,565**
Other comprehensive income					
Debt investments at FVOCI					
- change in fair value, net of tax	-	-	(1,273)	-	**(1,273)**
Equity investments at FVOCI					
- change in fair value, net of tax	-	-	(1,238)	-	**(1,238)**
- change in fair value transferred to retained earnings, net of tax	-	-	(1,246)	1,246	**-**
Property revaluation, net of tax	-	-	11,486	-	**11,486**
Release of surplus on sale of property, net of tax	-	-	(462)	462	**-**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(2,455)	**(2,455)**
Total other comprehensive income	-	-	7,267	(747)	**6,520**
Total comprehensive income for the year	-	-	7,267	49,818	**57,085**
Transactions with owners, recorded directly in equity:					
Scrip Dividend	5,772	3,850	-	(9,622)	**-**
Dividends to equity holders	-	-	-	(17,678)	**(17,678)**
	5,772	3,850	-	(27,300)	**(17,678)**
At 1 January 2019	**530,772**	**49,277**	**49,922**	**309,278**	**939,249**
Profit for the year	-	-	-	71,225	**71,225**
Other comprehensive income					
Debt investments at FVOCI					
- change in fair value, net of tax	-	-	1,864	-	**1,864**
Equity investments at FVOCI					
- change in fair value, net of tax	-	-	3,062	-	**3,062**
Property revaluation, net of tax	-	-	20	-	**20**
Release of surplus on sale of property, net of tax	-	-	(82)	82	**-**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(266)	**(266)**
Total other comprehensive income	-	-	4,864	(184)	**4,680**
Total comprehensive income for the year	-	-	4,864	71,041	**75,905**
Transactions with owners, recorded directly in equity:					
Bonus issue	53,077	-	-	(53,077)	**-**
At 31 December 2019	**583,849**	**49,277**	**54,786**	**327,242**	**1,015,154**

The notes are an integral part of these financial statements.

Statements of cash flows

For the year ended 31 December 2019

	Note	The Group		The Bank	
		2019	2018	2019	2018
		€000	€000	€000	€000
Cash flows from operating activities					
Interest and commission receipts		274,907	280,296	265,902	271,267
Interest, commission and compensation payments		(56,017)	(54,040)	(55,962)	(54,086)
Payments to employees and suppliers		(139,946)	(125,250)	(135,187)	(118,700)
Operating profit before changes in operating assets and liabilities		78,944	101,006	74,753	98,481
(Increase)/decrease in operating assets:					
Loans and advances		(68,083)	(157,854)	(68,083)	(157,854)
Reserve deposit with Central Bank of Malta		(1,521)	(749)	(1,521)	(749)
Fair value through profit or loss financial assets		8,528	26,063	8,528	26,063
Fair value through profit or loss equity instruments		755	11,671	(64)	11,675
Treasury bills with original maturity of more than 3 months		(23,855)	(7,662)	(23,855)	(7,662)
Other assets		(30,433)	(288)	(30,433)	(372)
Increase/(decrease) in operating liabilities:					
Amounts owed to banks and to customers		185,260	301,801	184,710	303,353
Other liabilities		(19,958)	(1,331)	(18,879)	(1,677)
Net cash from operating activities before tax		129,637	272,657	125,156	271,258
Tax paid		(39,480)	(20,881)	(40,938)	(21,602)
Net cash from operating activities		90,157	251,776	84,218	249,656
Cash flows from investing activities					
Dividends received		24,186	10,774	30,078	12,828
Interest received from amortised and other fixed income instruments		50,840	54,953	50,840	54,953
Purchase of debt instruments		(569,278)	(892,021)	(569,278)	(892,021)
Proceeds from sale or maturity of debt instruments		832,503	1,021,261	832,503	1,021,261
Proceeds from sale of equity instruments		-	12,296	-	12,296
Purchase of property and equipment and intangible assets		(34,996)	(26,295)	(34,949)	(26,229)
Proceeds from disposal of property and equipment		330	2,000	330	2,000
Net cash from investing activities		303,585	182,968	309,524	185,088
Cash flows from financing activities					
Interest paid on debt securities and subordinated liabilities		(10,050)	(13,414)	(10,050)	(13,414)
Repayment of debt securities		(40,208)	(55,400)	(40,208)	(55,400)
Payment of lease liabilities		(1,475)	-	(1,475)	-
Dividends paid to equity holders		-	(17,678)	-	(17,678)
Net cash used in financing activities		(51,733)	(86,492)	(51,733)	(86,492)
Net change in cash and cash equivalents		342,009	348,252	342,009	348,252
Effect of exchange rate changes on cash and cash equivalents		2,011	1,252	2,011	1,252
Net change in cash and cash equivalents after effect of exchange rate changes		339,998	347,000	339,998	347,000
Net change in cash and cash equivalents		342,009	348,252	342,009	348,252
Cash and cash equivalents at 1 January		3,626,859	3,278,607	3,626,859	3,278,607
Cash and cash equivalents at 31 December	36	**3,968,868**	**3,626,859**	**3,968,868**	**3,626,859**

The notes are an integral part of these financial statements.

Notes to the financial statements 31 December 2019

1. SIGNIFICANT ACCOUNTING POLICIES

1.1 Basis of preparation

Legal Notice 19 of 2009 as amended by Legal Notice 233 of 2016, Accountancy Profession (Accounting and Auditing Standards) (Amendments) Regulations, 2016, defines compliance with generally accepted accounting principles and practice as adherence to International Financial Reporting Standards (IFRS) as adopted by the EU for financial periods starting on or after 1 January 2008. These Regulations have come into force on 17 June 2016.

Article 4 of Regulation 1606/2002/EC requires that, for each financial period starting on or after 1 January 2005, companies governed by the law of an EU Member State shall prepare their consolidated financial statements in conformity with IFRS as adopted by the EU if, at their reporting date, their securities are admitted to trading on a regulated market of any EU Member State. This Regulation prevails over the provisions of the Companies Act, 1995, (Chapter 386, Laws of Malta) to the extent that the said provisions of the Companies Act, 1995, (Chapter 386, Laws of Malta) are incompatible with the provisions of the Regulation.

Consequently, the separate and the consolidated financial statements are prepared in conformity with IFRS as adopted by the EU.

These financial statements have also been prepared in accordance with the provisions of the Banking Act, 1994 (Chapter 371, Laws of Malta) and the Companies Act, 1995 (Chapter 386, Laws of Malta).

The financial statements have been prepared on the historical cost basis. Assets and liabilities are measured at historical cost except for the following that are measured at fair value: financial assets measured at fair value through other comprehensive income (FVOCI), financial instruments classified at fair value through profit or loss (FVTPL), derivatives and land and buildings. Additionally, assets held for realisation are measured at fair value less costs to sell, if it is lower than their cost.

Going concern

The time period that the Directors have considered in evaluating the appropriateness of the going concern basis in preparing the financial statements for 2019 is a period of twelve months from the date of approval of these financial statements (the 'period of assessment').

In making this assessment, the Directors considered the Group's business, profitability projections, funding and capital plans, together with a range of other factors such as the outlook for the Maltese economy, along with ongoing developments in EU.

The matters of primary consideration by the Directors are set out below:

Capital: The Group has developed capital plans under base and stress scenarios and the Directors believe that the Group has sufficient capital to meet its regulatory capital requirements throughout the period of assessment.

Funding and liquidity: The Directors have considered the Group's funding and liquidity position and are satisfied that the Group has sufficient funding and liquidity throughout the period of assessment.

On the basis of the above, the Directors consider it appropriate to prepare the financial statements on a going concern basis having concluded that there are no material uncertainties related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern over the period of assessment.

Changes in accounting policies arising from the adoption of new standards during the year ended 31 December 2019:

A. IFRS 16 Leases

The Group has adopted IFRS 16 with effect from 1 January 2019. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

IFRS 16 introduced a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make future lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the accounting requirements under IAS 17 Leases – i.e. lessors continue to classify leases as finance or operating leases.

IFRS 16 replaces existing leases guidance, including IAS 17 Leases, IFRIC 4 *Determining whether an Arrangement contains a Lease,* SIC-15 *Operating Leases – Incentives* and SIC-27 *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.1 Basis of preparation (continued)

A. IFRS 16 Leases (continued)

Leases in which the Group is a lessee

The Group's lease arrangements comprise long-term leasehold properties, other immovable property leaseholds, equipment leases and property space for ATMs which were classified as operating leases under IAS 17. Under IFRS 16, the Group has recognised new assets (right-of-use assets) and liabilities (lease liabilities) for all its lease arrangements which were previously classified as operating leases under IAS 17, with the exceptions of some arrangements of low value items or short-term arrangements of one year or less. The Group has applied IFRS 16 on its mandatory adoption date of 1 January 2019 using a modified retrospective approach with no restatement of comparative information. Under this approach, the lease liability is measured at the present value of the remaining lease payments as at 1 January 2019. With regards to the right-of-use the Group chose the option given by the standard of measuring the right-of-use asset at an amount equal to the lease liability, adjusted by the amount of any prepayment relating to that lease as recognised in the statement of financial position at 31 December 2018. As a result, there was no impact on equity.

Up until 31 December 2018, the Group recognised an operating lease expense on a straight-line basis over the term of the lease, and recognised assets and liabilities only to the extent that there was a timing difference between actual lease payments and the expense recognised. The nature of expenses related to these leases has changed with effect from 1 January 2019 because IFRS 16 replaced the operating lease expense with an amortisation charge for right-of-use assets and interest expense on lease liabilities.

In the Group's statement of cash flows, rental payments had been included as operating cash flows under IAS 17 up until 31 December 2018. Under IFRS 16, these payments are now split between interest payments and reductions in the lease liability. Whilst the interest payments will continue to be presented under operating cash flows in accordance with the Group's existing policy for interest payments, the portion of the payments relating to reduction in the lease liability will be presented under financing cash flows under IFRS 16. The Group presents right-of-use assets in 'Property and equipment' and lease liabilities in 'Other liabilities' in the statement of financial position.

The Group has elected not to recognise right-of-use assets and lease liabilities for short term leases. The Group recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term. Furthermore, the Group has elected to exclude initial direct costs from the measurement of the right of use asset at the date of initial application.

The Group recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, and subsequently at cost less any accumulated depreciation and impairment losses, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate.

The lease liability is subsequently increased by the interest cost on the lease liablity and decreased by lease payments made. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, a change in the estimate of the amount expected to be payable under a residual value guarantee, or as appropriate, changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised.

The Group has applied judgement to determine the lease term for some lease contracts in which it is a lessee that include renewal options. The assessment of whether the Group is reasonably certain to exercise such options impact the lease term, which significantly affects the amount of lease liabilities and right-of-use assets recognised.

Impact on transition

On transition to IFRS16, the Group recognised additional right-of-use assets and additional lease liabilities with no impact on retained earnings. The impact on transition is summarised below:

	Land and buildings €000	Other €000	Total €000
Balance at 1 January 2019:			
Right-of-use assets presented in property and equipment	7,419	1,184	8,603
Lease liabilities	7,419	1,184	8,603

When measuring lease liabilities for leases that were classified as operating leases, the Group discounted lease payments using its incremental borrowing rate at 1 January 2019. This rate was based on the swap rate curves as proxies for the risk free rate, the MGS yield to include the local context and applying a risk margin. The weighted-average rate applied is 2.44%.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.1 Basis of preparation (continued)

B. Interest rate benchmark reform

The Group considered the application of the interest rate benchmark reform amandments retrospectively to hedging relationships that existed at 1 January 2019 or were designated thereafter and the extent to which those are directly affected by interest rate benchmark reform. More information about the impact is disclosed in note 39.4.

Standards issued but not yet effective

A number of new standards and amendments were endorsed by the EU but effective for periods starting after 1 January 2020 as disclosed hereunder. The impact that the adoption of other International Financial Reporting Standards and amendments will have on the financial statements of the Group and the Bank in the period of initial application is currently being assessed by the directors but is not expected to have a significant impact on the Group's financial statements. These standards and amendments include the following:

Amendments:
- Amendments to References to Conceptual Framework in IFRS Standards (issued on 29 March 2018) - effective 01/01/2020
- Amendments to IAS1 and IAS8: Definition of material (issued on 31 October 2018) - effective 01/01/2020

In addition, the following new standards and amendments have not yet been endorsed by the EU:
- Amendments to IFRS 3 Business Combinations (issued on 22 October 2018) - effective 01/01/2020
- IFRS 17 Insurance Contracts (issued on 18 May 2017) - effective 01/01/2021
- Amendments to IAS1 Presentation of Financial Statements: Classification of Liabilities as Current or Non-current (issued on 23 January 2020) - effective date still to be announced.

1.2 Basis of consolidation

The Group financial statements comprise the financial statements of Bank of Valletta p.l.c., (the Bank), a limited liability company domiciled and incorporated in Malta, and its subsidiaries. Subsidiaries are entities controlled by the Group. The Group 'controls' an entity if it is exposed to, or has rights to, variable returns from its involvement with the entity. The Group reassesses whether it has control if there are changes to one or more of the elements of control. This includes circumstances in which protective rights held (e.g. those resulting from a lending relationship) become substantive and lead to the Group having power over an investee. The results of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Intragroup balances, transactions, income and expenses are eliminated on consolidation. Non-controlling interests that represent ownership interests and entitle their holders to a proportionate share of the entity's net assets in the event of liquidation may be initially measured either at their present ownership interests' proportionate share in the recognised amounts of the acquiree's identifiable net assets or at fair value. The choice of measurement basis is made on an acquisition-by-acquisition basis. After initial recognition, non-controlling interests in the net assets consist of the amount of those interests at the date of the original business combination and the non-controlling interests' share of changes in equity since the date of the combination.

The excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets and liabilities is recognised as goodwill and is included within the carrying amount of the investment and assessed for impairment as part of the investment. If the cost of acquisition is less than the Group's share of the net fair value of the identifiable assets and liabilities, the difference is included as income in the determination of the Group's share of the profit or loss in the period in which the investment is acquired. Equity-accounted investees comprise interests in associates. The results and assets and liabilities of equity-accounted investees are incorporated in the consolidated financial statements using the equity method of accounting from the date that significant influence or joint control commences until the date that significant influence or joint control ceases. Equity-accounted investees are those entities in which the Group has significant influence, but not control or joint control over the financial and operating policies. A joint venture is an arrangement in which the Group has joint control, whereby the Group has rights to the net assets of the arrangement rather than rights to its assets and obligations for its liabilities.

The significant accounting policies adopted are set out in the following page.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.3 Financial instruments

1.3.1 Amortised cost and effective interest rate

Interest income and expense is recognised using the effective interest method, by reference to the principal outstanding and the effective interest rate applicable, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the instrument or, when appropriate, a shorter period to that instrument's gross carrying amount. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the instrument but not future credit losses. The calculation includes payments and receipts that are an integral part of the effective interest rate, transaction costs and all other discounts or premiums upon initial recognition.

Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

The 'amortised cost' of a financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets adjusted for any expected credit loss allowance.

1.3.2 Interest income and expense

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for:

- Financial assets that are not purchased or originated credit-impaired ('POCI') but have subsequently become credit-impaired (or 'stage 3'), for which interest revenue is calculated by applying the effective interest rate to their amortised cost (i.e. net of the expected credit loss provision).
- POCI financial assets, for which the original credit-adjusted effective interest rate is applied to the amortised cost of the financial asset.

1.3.3 Initial recognition

Financial assets and financial liabilities are recognised when a Group entity becomes a party to the contractual provisions of the instrument.

All loans and advances to customers and to banks are recognised when cash is advanced to borrowers.

All purchases and sales of securities are recognised and derecognised on settlement date, which is the date that an asset is delivered to or by the Group.

1.3.4 Measurement at initial recognition

At initial recognition, the Group measures a financial asset or financial liability at its fair value plus or minus, in the case of financial asset or financial liability not at fair value through profit or loss, 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 fair value through profit or loss are expensed in profit or loss.

An expected credit loss allowance (ECL) is also recognised immediately after initial recognition for financial assets measured at amortised cost and investments in debt instruments measured at FVOCI, as described in note 39.2.1.2, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

1.4 Financial Assets

1.4.1 Classification and measurement of financial assets

The Group classifies its financial assets in the following measurement categories:

- Fair value through profit or loss (FVTPL);
- Fair value through other comprehensive income (FVOCI); or
- Amortised cost.

Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds.

Classification and subsequent measurement of debt instruments depend on:
(i) the Group's business model for managing the asset; and
(ii) the cash flow characteristics of the asset.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.4 Financial Assets (continued)

1.4.1 Classification and measurement of financial assets (continued)

Based on these factors, the Group classifies its debt instruments into one of the following three measurement categories:

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI') on specified dates, and that are not designated at FVTPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any expected credit loss allowance recognised and measured as described in note 39.2.1.1. Interest income from these financial assets is included in 'Interest and similar income' using the effective interest rate method.

- Fair value through other comprehensive income (FVOCI): Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVTPL, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses on specified dates, 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 gain on investment securities and hedging instruments'. Interest income from these financial assets is included in 'Interest and similar income' using the effective interest rate method.

- Fair value through profit or loss (FVTPL): Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVTPL. A gain or loss on a debt investment that is subsequently measured at FVTPL and is not part of a hedging relationship is recognised in profit or loss and presented in the statement of profit or loss within 'Trading profits' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Net investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

Financial assets and liabilities are designated at fair value through profit or loss on initial recognition where such designation results in more relevant information because it eliminates or significantly reduces a measurement or recognition inconsistency (sometimes referred to as an ‘accounting mismatch’) that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Business Model Assessment

The Group makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, 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 the 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;
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its 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.

Financial assets that are held for trading and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Cash flows that represent solely payments of principal and interest

'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 and 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 profit margin.

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 considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Group's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.4 Financial Assets (continued)

1.4.1 Classification and measurement of financial assets (continued)

Embedded derivatives

Derivatives may be embedded in another contractual arrangement (a host contract). The Group accounts for an embedded derivative separately from the host contract when:
- the host contract is not an asset in the scope of IFRS 9;
- the host contract is not itself carried at FVTPL;
- the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract; and
- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract.

Separated embedded derivatives are measured at fair value, with all changes in fair value recognised in profit or loss unless they form part of a qualifying cash flow or net investment hedging relationship. Separated embedded derivatives are presented in the statement of financial position together with the host contract.

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis and is irrevocable. Other equity instruments are classified as measured at FVTPL.

Gains and losses on such equity instruments are never reclassified to profit or loss and no impairment is recognised. Dividends are recognised in profit or loss (see note 1.22) unless they clearly represent a recovery of part of the cost of the investment, in which case they are recognised in OCI. Cumulative gains and losses recognised in OCI are transferred to retained earnings on disposal of an investment.

Gains and losses on equity investments at FVTPL are included in the 'Trading profits' line in the statement of profit or loss.

1.4.2 Modification of terms

When modification of a loan agreement occurs as a result of commercial restructuring activity rather than due to the credit risk of the borrower, the Group evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised (see 1.4.4) and a new financial asset is recognised at fair value. If the cash flows of the modified asset carried at amortised cost are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, the Group recalculates the gross carrying amount of the financial asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss.

Additionally, in the case of loans and advances which encountered actual or apparent financial difficulties, the Group may grant a concession where a customer's financial difficulty indicates that with the original terms and conditions of the contract satisfactory repayment may not be possible. Such concession are recognised as revisions to the expected credit loss on the associated loan.

A concession refers to either of the following:
- a change in the previous terms and conditions of a contract the customer is considered unable to comply with due to its financial difficulties to allow for sufficient debt service ability, that would not have been granted had the customer not been in financial difficulties;
- a total or partial refinancing of a troubled debt contract, that would not have been granted had the customer not been in financial difficulties.

1.4.3 Impairment

The Group assesses on a forward-looking basis the expected credit losses ('ECL') associated with its debt instrument assets carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. 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.

Note 39.2.1.2 provides more detail of how the expected credit loss allowance is measured.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.4 Financial Assets (continued)

1.4.3 Impairment (continued)

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position 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: as a provision;
- Where a financial instrument includes both a drawn and 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. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- Debt instruments measured at FVOCI: 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 disclosed and is recognised in the fair value reserve.

Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- Financial assets that are not credit-impaired at the reporting date: at 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: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- Undrawn loan commitments: as 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.

Modification of financial assets

When there is a modification of financial assets' terms (note 1.4.2), the date of renegotiation is 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.

1.4.4 Derecognition of financial assets

A financial asset is derecognised when the contractual rights to the cash flows from the financial asset expire, or when the Group transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset and the transfer qualifies for derecognition.

1.4.5 Fair valuation of financial assets

Where possible, fair value is based on quoted bid prices in an active market. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. If the market for a financial asset is not active, the Group establishes fair value by using valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

1.5 Financial liabilities

1.5.1 Classification and measurement of financial liabilities

Financial liabilities are classified according to the substance of the contractual arrangements entered into.

Financial liabilities are initially measured at fair value less, in the case of financial liabilities not at fair value through profit or loss, transaction costs that are directly attributable to their issue. Financial liabilities are subsequently measured at amortised cost using the effective interest method, except for financial liabilities at fair value through profit or loss, which are measured at fair value.

Financial liabilities at fair value through profit or loss include financial liabilities classified as held for trading and those designated at fair value through profit or loss upon initial recognition. During the current and the previous year, the Group did not designate any financial liabilities as at fair value through profit or loss upon initial recognition. Derivatives are categorised as held for trading, unless they are designated and effective hedging instruments.

Financial liabilities that are measured at amortised cost using the effective interest method include amounts owed to banks, amounts owed to customers, debt securities in issue and subordinated liabilities.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.5 Financial liabilities (continued)

1.5.1 Classification and measurement of financial liabilities (continued)

The gain or loss on financial liabilities at fair value through profit or loss is recognised in profit or loss. For financial liabilities carried at amortised cost, the gain or loss is recognised in profit or loss when the financial liability is derecognised and through the amortisation process whereby any difference between the proceeds net of transaction costs, and the settlement or redemption is recognised over the term of the financial liability.

1.5.2 Derecognition of financial liabilities

A financial liability is derecognised when it is extinguished. This occurs when the obligation specified in the contract is discharged, cancelled or expires.

1.6 Financial guarantee contracts and loan commitments

'Financial guarantees' are contracts that require the Group to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value. Subsequently, they are measured at the higher of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15.

For financial guarantees issued or commitments the Group recognises a loss allowance.

Impairment allowances and provisions on loan commitments that comprise both a drawn and undrawn commitment are presented in accordance with the policy set out in the note 1.4.3 Impairment.

1.7 Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when the Group currently has a legally enforceable right to set off the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

1.8 Derivatives held for risk management purposes and hedge accounting

Derivatives held for risk management purposes include all derivative assets and liabilities that are not classified as trading assets or liabilities. Derivatives held for risk management purposes are measured at fair value in the statement of financial position.

The Group designates certain derivatives held for risk management as well as certain non-derivative financial instruments as hedging instruments in qualifying hedging relationships. On intial desigation of the hedge, the Group formally documents the relationship between the hedging instrument(s) and hedged item(s), including the risk management objective and strategy in undertaking the hedge, together with the method that will be used to assess the effectiveness of the hedging relationship. The Group makes an assessment, both on inception of the hedging relationship and on an ongoing basis, of whether the hedging instrument(s) is (are) expected to be highly effective in offsetting the changes in the fair value or cash flows of the respective hedged item(s) during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80-125%. For a cash flow hedge of a forecast transaction, the Group makes an assessment of whether the forecast transaction is highly probable to occur and presents an exposure to variations in cash flows that could ultimately affect profit or loss.

These hedging relationships are discussed below.

Fair value hedges

When a derivative is designated as the hedging instrument in a hedge of the change in fair value of a recognised asset or liability or a firm commitment that could affect profit or loss, changes in the fair value of the derivative are recognised immediately in profit or loss. The change in fair value of the hedged item attributable to the hedged risk is recognised in profit or loss. If the hedged item would otherwise be measured at cost or amortised cost, then its carrying amount is adjusted accordingly.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.8 Derivatives held for risk management purposes and hedge accounting (continued)

Fair value hedges (continued)

If the hedging derivative expires or is sold, terminated or exercised, or the hedge no longer meets the criteria for fair value hedge accounting, or the hedge designation is revoked, then hedge accounting is discontinued prospectively. However, if the derivative is novated to a Central Counterparty Clearing (CCP) by both parties as a consequence of laws or regulations without changes in its terms except for those that are necessary for the novation, then the derivative is not considered expired or terminated.

Any adjustment up to the point of discontinuation to a hedged item for which the effective interest method is used is amortised to profit or loss as an adjustment to the recalculated effective interest rate of the item over its remaining life.

On hedge discontinuation, any hedging adjustment made previously to a hedged financial instrument for which the effective interest method is used is amortised to profit or loss by adjusting the effective interest rate of the hedged item from the date on which amortisation begins. If the hedged item is derecognised, then the adjustment is recognised immediately in profit or loss when the item is derecognised.

Other non-trading derivatives

Other non-trading derivatives are recognised on balance sheet at fair value on initial recognition. If a derivative is not held for trading, and is not designated in a qualifying hedge relationship, then all changes in its fair value are recognised immediately in profit or loss as a component of net income from other financial instruments at FVTPL.

1.9 Sale and repurchase agreements

Securities sold subject to a linked repurchase agreement ('repos') are retained in the financial statements as financial assets at fair value through profit or loss or as investment securities as appropriate, and the counterparty liability is included in amounts owed to banks. Securities purchased under agreements to resell ('reverse repos') are not recognised but the amounts paid are recorded as loans and advances to banks. The difference between sale and repurchase price or purchase and subsequent sale price is recognised over the life of the repo/reverse repo agreements using the effective interest method and is treated as interest.

1.10 Investments in subsidiaries and equity-accounted investees

Investments in subsidiaries and equity-accounted investees are initially included in the Bank's statement of financial position at cost and subsequently at cost less any impairment loss which may have arisen. Interest in equity-accounted investees are accounted for using the equity method at Group level. They are initially recognised at cost, which includes transaction costs. Subsequently, the consolidated financial statements include the Group's share of profit or loss and other comprehensive income of equity-accounted investees, until the date on which significant influence ceases. Dividends from the investments are recognised in the Bank's profit or loss when its right to receive dividend is established.

Impairment
At the end of each reporting period, the Bank reviews the carrying amount of its investments in subsidiaries and equity-accounted investees to determine whether there is any indication of impairment and if any such indication exists, the recoverable amount of the asset is estimated.

An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount. The recoverable amount is the higher of fair value less costs of disposal and value in use. An impairment loss recognised in a prior year is reversed if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, provided that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. Impairment losses and reversals are recognised immediately in profit or loss.

1.11 Property and equipment

Property and equipment are classified into the following classes – land and buildings, IT infrastructure and equipment and other (primarily furniture and fittings).

Property and equipment are initially measured at cost. Subsequent costs are included in the asset's carrying amount when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. Expenditure on repairs and maintenance of property and equipment is recognised as an expense when incurred.

Subsequent to initial recognition, freehold and long-term leasehold properties are stated in the statement of financial position at revalued amounts, being the fair value at the date of revaluation, less any subsequent accumulated depreciation and subsequent accumulated impairment losses.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.11 Property and equipment (continued)

Revaluations are performed by a professionally qualified architect on a regular basis such that the carrying amount does not differ materially from that which would be determined using fair values at the end of the reporting period. Any surpluses arising on such revaluation are recognised in other comprehensive income and accumulated in equity as a revaluation reserve unless they reverse a revaluation decrease for the same asset previously recognised in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously charged. Any deficiencies resulting from decreases in value are deducted from this revaluation reserve to the extent that the balance held in this reserve relating to a previous revaluation of that asset is sufficient to absorb these, and charged to profit or loss thereafter.

Other tangible assets are stated at cost less accumulated depreciation and any accumulated impairment losses.

Property and equipment are derecognised on disposal or when no future economic benefits are expected from their use or disposal. Gains or losses arising from derecognition represent the difference between the net disposal proceeds, if any, and the carrying amount, and are included in profit or loss in the period of derecognition.

1.12 Intangible assets

Intangible assets comprise computer software. In determining the classification of an asset that incorporates both intangible and tangible elements, judgement is used in assessing which element is more significant. Computer software which is an integral part of the related hardware is classified as property and equipment and accounted for in accordance with the Group's accounting policy on property and equipment. Where the software is not an integral part of the related hardware, this is classified as an intangible asset. Computer software is externally generated.

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates.

Computer software is initially measured at cost. It is subsequently carried at cost less accumulated amortisation and any accumulated impairment losses.

Computer software is derecognised on disposal or when no future economic benefits are expected from its use or disposal. Gains or losses arising from derecognition represent the difference between the net disposal proceeds, if any, and the carrying amount, and are included in profit or loss in the period of derecognition.

1.13 Depreciation and amortisation

Depreciation on property and equipment and amortisation on intangible assets commence when these assets are available for use and are charged to profit or loss so as to write off the cost or revalued amount of assets, other than land, less any estimated residual value, over their estimated useful life, using the straight line method, on the following bases:

Property and equipment		
Freehold and long-term leasehold buildings	2%	per annum
IT infrastructure and equipment	10% - 25%	per annum
Other (primarily furniture and fittings)	5% - 33%	per annum
Intangible assets		
Computer software	10% - 20%	per annum

The depreciation or amortisation method applied, the residual value and the useful life are reviewed at the end of each reporting period and adjusted if appropriate.

1.14 Impairment of property and equipment and intangible assets

At the end of each reporting period the Group reviews the carrying amount of its property and equipment and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If such indication exists the recoverable amount is estimated in order to determine the extent of the impairment loss and the carrying amount of the asset is reduced to its recoverable amount. The recoverable amount is the higher of fair value less costs of disposal and value in use.

An impairment loss is recognised immediately in profit or loss, unless the asset is carried at a revalued amount, in which case the loss is recognised in other comprehensive income to the extent that it does not exceed the amount in the revaluation surplus for that asset.

An impairment loss recognised in a prior year is reversed if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognised. When an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, to the extent that it does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. Impairment reversals are recognised immediately in profit or loss, unless the asset is carried at a revalued amount, in which case the impairment reversal is recognised in other comprehensive income, unless an impairment loss on the same asset was previously recognised in profit or loss.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.15 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. In such case, the unwinding of the discount is recognised as finance cost.

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 but 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.

1.16 Non-current assets and disposal groups held for sale

Non-current assets and disposal groups are classified as held for sale if it is highly probable that they will be recovered primarily through a sale transaction rather than through continuing use. Such assets, or disposal groups, are generally measured at the lower of their carrying amount and fair value less costs to sell and the asset or disposal group is available for immediate sale in its present condition. Management must be committed to the sale, which should be expected to qualify for recognition as a completed sale within a reasonable period from the date of classification. Non-current assets are not depreciated (or amortised) while they are classified as held for sale or while they are part of a disposal group classified as held for sale.

1.17 Cash and cash equivalents

Cash and cash equivalents comprise cash in hand and deposits repayable on demand or with a contractual period to maturity of less than 3 months; advances to banks repayable within 3 months from the date of the advance; balances with the Central Bank of Malta, excluding reserve deposit requirements, and treasury bills with an original maturity of less than 3 months. Amounts owed to banks that are repayable on demand or with a contractual period to maturity of less than 3 months and which form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statements of cash flow.

1.18 Dividends payable

Interim dividends approved by the directors are recognised when paid. Final dividends are recognised as liability upon approval by the shareholders at the Annual General Meeting.

1.19 Operating segments

An operating segment is a component of an entity (a) that engages in business activities from which it may earn revenues and incur expenses, (b) whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and (c) for which discrete financial information is available. Unallocated items comprise mainly head office expenses and tax assets and liabilities.

1.20 Fair value

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 in the principal or, its absence, the most advantageous market to which the Group has access at the date. The fair value of a liability reflects its non-performance risk.

Fair value reflects conditions, including but not limited to liquidity in the market, at a specific date and may therefore differ significantly from the amounts which will actually be received on the maturity or settlement date. The Bank's portfolio remains deployed across a wide spread of holdings of moderate duration debt securities issued by quality, credit rated, sovereign, supranational, corporate and financial institutions, as further disclosed in notes 14 and 15 to the financial statements.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.20 Fair value (continued)

The best evidence of fair value of an instrument is a quoted price in an actively traded market for that instrument. The determination of what constitutes an active market is subjective and requires the collation of data and the exercise of judgement. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The Bank determines whether active market conditions exist by taking into consideration various characteristics, including:

- a significant decline in volume and level of trading activity;
- significant variations in available prices either over time or among market participants;
- the absence of or stale prices;
- unusually wide bid/offer spreads; and
- exceptionally minimal transactions when compared with the quantum of the issue in question.

Where it is concluded that an active market does not exist a valuation technique is used. The latter gives consideration to transaction prices in inactive markets, however it makes use of other observable market data which include a combination of the following:

- the risk premium of more active instruments of the same issuer, the same type of debt, the same currency and with the same or similar maturity;
- the spreads payable on Credit Default Swaps of the issuer;
- the risk premium over and above the risk free bonds for similarly rated issuers in the same industry sector;
- yield curve or Discounted Cash Flow (DCF) calculations to maturity using appropriate interest rate/discount factors;
- liquidity adjustments to reflect ability to sell asset over a reasonable timeframe; and
- other overall reasonableness tests.

The main assumptions and estimates which management considers when using valuation techniques are the likelihood and expected timing of future cash flows on the instrument, selecting an appropriate discount rate for the instrument and a risk premium. The valuation techniques used by the Group incorporate all factors that market participants would consider in setting a price and are consistent with accepted economic methodologies for pricing financial instruments.

1.21 Taxation

Income tax expense comprises current and deferred tax and is recognised in profit or loss, except when it relates to items recognised in other comprehensive income or directly in equity, in which case it is dealt with in other comprehensive income or in equity, as appropriate.

Current tax
Current tax is based on the taxable result for the period. The taxable result for the period differs from the result as reported in profit or loss because it excludes items which are non-assessable or disallowed and it further excludes items that are taxable or deductible in other periods. Current tax also includes any tax arising from dividends. It is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period, and any adjustments in relation to the prior periods.

Deferred tax
Deferred tax is determined under the liability method in respect of all temporary differences between the carrying amount of an asset or liability in the financial statements and its tax base. Deferred tax liabilities are generally recognised for all taxable temporary differences subject to certain exceptions and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax is calculated at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled based on tax rates that have been enacted or substantively enacted by the end of the reporting period. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Deferred tax is not recognised for temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the forseeable future.

1.22 Revenue recognition

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

Dividend income from investments is recognised when the right to receive payment has been established.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.22 Revenue recognition (continued)

Interest income and expense is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the instrument or, when appropriate, a shorter period to that instrument’s net carrying amount. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the instrument but not future credit losses. The calculation includes payments and receipts that are an integral part of the effective interest rate, transaction costs and all other discounts or premiums.

Generally fee and commission income, is recognised as the related services are performed.

A contract with a customer that results in a recognised financial instrument in the Group's financial statements may be partially in the scope of IFRS 9 and partially in the scope of IFRS 15. If this is the case then the Group first applies IFRS 9 to separate and measure the part of the contract that is in the scope of IFRS 9 and then applies IFRS 15 to the residual.

Other fee and commission expenses are expensed as the services are received.

1.23 Foreign currency translation

For the purpose of the consolidated and separate financial statements, the presentation currency is the Euro. The functional currency of the Bank and of all its subsidiaries is the Euro.

In preparing the financial statements of the individual group entities, transactions denominated in currencies other than the functional currency are translated at the exchange rates ruling on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated to Euro at the rates of exchange ruling at the end of the reporting period. Gains and losses arising from such translation are dealt with in profit or loss and presented with trading income. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Euro at the exchange rate ruling on the date the fair value was measured. Non-monetary assets and liabilities denominated in foreign currencies that are measured in terms of historical cost are not retranslated.

1.24 Employee benefits

The Group and the Bank contribute towards the state pension in accordance with local legislation. The only obligation of the Group and the Bank is to make the required contribution. Costs are expensed in the period in which they are incurred in profit or loss.

For the Group’s and the Bank’s defined benefit plans, the cost of providing benefits is determined using the projected unit credit method, with estimations being carried out at each reporting date. Past service cost is recognised as an expense at the earlier of the following dates (a) when the plan amendment or curtailment occurs and (b) when the entity recognises related restructuring costs or termination benefits. The amount recognised in the Statement of Financial Position represents the present value of the expected future payments required to settle the obligation resulting from employee service in the current and prior periods. The service cost and the net interest on the net defined benefit liability are recognised in profit or loss. Remeasurements of the net defined benefit liability, comprising actuarial gains and losses are recognised in other comprehensive income and are not reclassified to profit or loss in a subsequent period. Such remeasurements are recognised immediately in retained earnings. Actuarial gains and losses are changes in the present value of the defined benefit obligation resulting from experience adjustments and the effects of changes in actuarial assumptions. Actuarial assumptions are an entity’s best estimates of the variables that will determine the ultimate cost of providing post-employment benefits. Due to the nature of the actuarial assumptions, in accordance with the provisions of IAS 19, Employee Benefits, the Group and the Bank did not involve a qualified actuary in the measurement of their post-employment benefit obligations.

1.25 Judgements in applying accounting policies and key sources of estimation uncertainty

The amounts recognised in the financial statements are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of financial statements. The judgements made by management in applying the Group’s and the Bank's accounting policies that have the most significant effect on the amounts recognised in the financial statements, together with information about the key assumptions concerning the future, and other key sources of estimation uncertainty at the end of the reporting period, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year, are either disclosed below or in note 39.2.1.2.5. This note discloses the determination of inputs in the IFRS 9 ECL measurement model; including key assumptions used in incorporation of forward-looking information.

1.25.1 Portfolio valuation

The Group measures portfolios of financial assets and financial liabilities on the basis of net exposures to market risks, then it applies judgement in determining appropriate portfolio-level adjustments such as bid-ask spreads. Such adjustments are derived from observable bid-ask spreads for similar instruments and adjusted for factors specific to the portfolio. Similarly, when the Group measures portfolios of financial assets and financial liabilities on the basis of net exposure to the credit risk of a particular counterparty, then it takes into account any existing arrangements that mitigate the credit risk exposure - e.g. master netting agreements with the counterparty.

Notes to the financial statements 31 December 2019 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.25 Judgements in applying accounting policies and key sources of estimation uncertainty (continued)

1.25.2 Fair value of financial instruments not quoted in active markets

The fair value of financial instruments that are not quoted in active markets is determined by using valuation techniques. Periodically, the Group calibrates these valuation techniques and tests them for validity. Where possible the valuation techniques used by the Group make use of observable data and incorporate all factors that market participants would consider in setting a price and are consistent with accepted economic methodologies for pricing financial instruments. Management is required to make certain assumptions and estimates in arriving at an appropriate fair value, based on available observable market data. A change in assumptions could affect the reported fair value of these financial instruments. Further disclosures are provided in note 39.

1.25.3 Fair value of land and buildings

The fair value of the Group's and the Bank's land and buildings is determined by using valuation techniques as further disclosed in note 21. In arriving at an estimate of fair value at the end of the reporting period, the Group and the Bank make use of significant unobservable inputs. A change in such inputs could affect the reported fair value of these land and buildings.

1.25.4 Classification of facilities as forborne

Management follows the European Banking Authority technical standard in identifying performing/non-performing exposures and in determining forborne exposures. Judgement is exercised in determining whether the modification of the original terms of a facility are granted, because of financial difficulties, which would result in the exposure being classified as forborne.

1.25.5 Provisions and contingent liabilities

In the ordinary course of operations, the Group faces loss contingencies that may result in the recognition of a liability. Management periodically assesses these issues based on information available and assessments from internal and/or external legal counsel.

The Group is currently involved in various claims and legal proceedings arising out of it normal business operations. Periodically, the status of each significant loss contingency is reviewed to assess the potential financial exposure. If the potential loss from any claim or legal proceeding is considered probable and the amount can be reasonably estimated, a liability for the estimated loss is provided for. Due to the uncertainties inherent in such matters, provisions are based on the best information available at the reporting date. As additional information becomes available, the potential liability related to pending claims and litigation is reassessed and, if required, estimates are revised. Such revisions in the estimates of the potential liabilities could have a material impact on results of operations and the financial position of the Group. Where an individual provision is material, the fact that a provision has been quantified would not constitute any admission of wrongdoing or legal liability.

Notes to the financial statements 31 December 2019 (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
2. INTEREST AND SIMILAR INCOME				
On loans and advances to banks	3,683	3,235	3,683	3,235
On loans and advances to customers	166,142	161,942	166,142	161,942
	169,825	165,177	169,825	165,177
On debt and other fixed income instruments				
- fair value through other comprehensive income	6,427	6,359	6,427	6,359
- amortised cost	44,414	50,268	44,414	50,268
- fair value through profit or loss	1,334	1,993	1,334	1,993
	52,175	58,620	52,175	58,620
Amortisation of discounts and premiums				
- fair value through other comprehensive income	(2,331)	(1,425)	(2,331)	(1,425)
- amortised cost	(12,706)	(8,476)	(12,706)	(8,476)
	(15,037)	(9,901)	(15,037)	(9,901)
Net interest income on debt and other fixed income instruments	37,138	48,719	37,138	48,719
	206,963	213,896	206,963	213,896

3. INTEREST EXPENSE

On amounts owed to banks	2,787	6,970	2,787	6,970
On interest rate swaps	4,006	4,023	4,006	4,023
On amounts owed to customers	21,992	19,964	21,992	19,964
On debt securities in issue	641	3,473	641	3,473
On subordinated liabilities	9,409	9,941	9,409	9,941
Negative interest on loans to banks, treasury bills and balances with Central Bank of Malta	15,278	12,979	15,278	12,979
	54,113	57,350	54,113	57,350

4. NET FEE AND COMMISSION INCOME

On loans and advances, similar activities and local business	38,131	42,188	38,131	42,188
On life assurance, fund management and similar activities	19,582	20,425	10,575	11,403
On other activities	16,115	18,524	16,115	18,524
	73,828	81,137	64,821	72,115

The fees and commission presented in this note include income of €26.2 million (2018: €28.9 million) relating to financial assets and financial liabilities not measured at FVTPL.

A significant portion of the fees and commissions earned by the Group are of a one time nature and are recognised at the point in time when the transaction takes place.

The other fee and commission income earned from contracts with customers is measured based on the consideration specified in the contract with a customer. The Group recognises revenue when it transfers control over a service to a customer.

Notes to the financial statements 31 December 2019 (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
5. TRADING PROFITS				
Net income on foreign exchange activities	17,341	16,963	17,343	16,956
Fair value movements and net gains on sale of financial instruments designated at fair value through profit or loss	4,927	881	4,927	876
Fair value movements and net (losses)/gains on sale of financial instruments mandatorily measured at fair value through profit or loss	(27)	175	(27)	175
	22,241	18,019	22,243	18,007
6. NET GAIN ON INVESTMENTS AND HEDGING INSTRUMENTS				
Amortised cost instruments				
- net (loss)/gain on disposal	(1)	818	(1)	818
Financial assets at FVOCI - debt instruments				
- net revaluation gain/(loss) attributable to hedged risk	3,488	(2,571)	3,488	(2,571)
Derivative financial instruments				
- net (loss)/gain on derivative financial instruments held for hedging	(3,399)	2,742	(3,399)	2,742
	88	989	88	989
7. EMPLOYEE COMPENSATION AND BENEFITS				
Employee compensation and benefits				
- wages and salaries	60,871	55,779	58,324	53,225
- social security costs	3,974	3,726	3,875	3,627
- retirement benefits	683	556	682	556
- other staff costs	5,712	5,635	5,712	5,635
	71,240	65,696	68,593	63,043
	No. of persons	**No. of persons**	**No. of persons**	**No. of persons**
The average number of employees are analysed as follows:				
Managerial	633	578	607	556
Supervisory and clerical	1,127	1,054	1,090	1,013
Others	63	70	54	59
	1,823	1,702	1,751	1,628

Notes to the financial statements 31 December 2019 (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
8. NET IMPAIRMENT REVERSAL				
Loans and advances to customers				
- increase in expected credit losses	(27,815)	(30,988)	(27,815)	(30,988)
- bad debts written off	(2,455)	(46,869)	(2,455)	(46,869)
	(30,270)	(77,857)	(30,270)	(77,857)
Loans and advances to customers				
- decrease in expected credit losses	33,939	83,310	33,939	83,310
- recoveries of amounts previously written off	8,040	4,717	8,040	4,717
	41,979	88,027	41,979	88,027
Investments				
- (increase)/decrease in expected credit losses	(147)	646	(147)	646
Net impairment reversals	11,562	10,816	11,562	10,816

9. PROFIT BEFORE TAX

Profit before tax is stated after charging:

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Total remuneration payable to the external auditors of the parent company				
- the audit of financial statements	650	386	620	356
- other assurance services	51	59	46	54
- tax advisory services	50	25	45	22
- other non-audit services	55	35	47	35
	806	505	758	467
Directors' emoluments:				
- fees	396	408	376	382
- directors' salaries as full-time bank employees	434	426	434	426
	830	834	810	808
Compensation to other key management personnel is analysed as follows:				
- other fees	160	154	-	-
- short term employee benefits	582	513	582	513
	742	667	582	513
Total remuneration of directors and other key management personnel	1,572	1,501	1,392	1,321

Notes to the financial statements 31 December 2019 (continued)

10. INCOME TAX EXPENSE

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Through profit and loss				
Current				
- for the period	29,838	27,808	30,694	27,377
- over provision in prior years	-	(2,500)	-	(2,500)
Deferred	(4,125)	(5,520)	(4,125)	(5,520)
	25,713	19,788	26,569	19,357

The charge for income tax is based on the taxable profit for the period at a rate of 35%. The income tax expense and the product of accounting profit multiplied by the statutory domestic income tax rate are reconciled as follows:

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Profit before tax	89,205	71,198	97,794	69,922
Tax at the applicable rate of 35%	31,222	24,919	34,228	24,473
Tax effect of:				
Exempt and untaxed dividends	(109)	(47)	(7,809)	(2,907)
Share of results of equity-accounted investees	(5,564)	(2,875)	-	-
Withholding tax on property sales	(146)	(98)	(146)	(98)
Depreciation on premises	775	170	775	170
Non-deductible expenses	1	45	2	45
Over provision in prior years	-	(2,500)	-	(2,500)
Other differences	(466)	174	(481)	174
Income tax expense	25,713	19,788	26,569	19,357

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Through equity				
On opening retained earnings on adoption of IFRS 9				
- current	-	369	-	369
- deferred	-	(4,742)	-	(4,742)
	-	(4,373)	-	(4,373)
Other comprehensive income				
- current	2,652	(1,352)	2,652	(1,352)
- deferred	(142)	(66)	(142)	(66)
	2,510	(1,418)	2,510	(1,418)

Notes to the financial statements 31 December 2019 (continued)

11. EARNINGS PER SHARE

	The Group		The Bank	
	2019	2018	2019	2018
	cents per share	cents per share	cents per share	cents per share
Earnings per share	10.9c	8.8c	12.2c	8.7c

The earnings per share for the Group and Bank have been calculated on the profits of the Group and the Bank, as shown in the statements of profit or loss, divided by number of shares in issue. The calculation of the earnings per share for all periods presented was adjusted retrospectively in view of the increase in the number of ordinary shares outstanding as a result of the bonus issue of shares, as described in note 31.

Earnings per share was calculated on profit attributable to shareholders of the Group €63,492,000 (2018: €51,410,000) and the Bank €71,225,000 (2018: €50,565,000) divided by 583,849,270 shares outstanding as at 31 December 2019.

12. DIVIDENDS

The amounts of dividends recognised as distributions to equity holders during the period, and the related amount per qualifying share, are as follows:

	The Bank			
	2019	2018	2019	2018
	cents per share	cents per share	€000	€000
Gross of income tax				
- prior year's final paid	-	8.0	-	42,000
- interim paid	-	-	-	-
	-	8.0	-	42,000
Net of income tax				
- prior year's final paid	-	5.2	-	27,300
- interim paid	-	-	-	-
	-	5.2	-	27,300

In respect of the current period, the directors propose that a final gross ordinary dividend of €0.026 per share amounting to €15.4 million (net ordinary dividend of €0.017 per share - €10.0 million) be paid to shareholders. This dividend is subject to regulatory approval and to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. The proposed dividend is payable to all shareholders on the register of members as at the "record date". The record date for the purposes of Article 2.1 of the Bank's Articles of Association is 30 days immediately proceeding the date set for the Annual General Meeting.

Dividend was paid out of profits taxed at 35%.

Notes to the financial statements 31 December 2019 (continued)

	Note	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
13. BALANCES WITH CENTRAL BANK OF MALTA, TREASURY BILLS AND CASH					
Balances with Central Bank of Malta		3,474,400	3,254,070	3,474,400	3,254,070
Malta Government Treasury Bills		97,053	86,231	97,053	86,231
Cash	36	98,127	60,287	98,127	60,287
		3,669,580	3,400,588	3,669,580	3,400,588

Balances with the Central Bank of Malta include Reserve Deposit, in terms of Regulation (EC) No.1745/2003 of the European Central Bank amounting to €101.3 million (2018: €99.8 million) in respect of both the Group and the Bank. Balances with Central Bank of Malta and Malta Government Treasury Bills are subject to negative interest rates.

During the current financial year, 'Term placements with Central Bank of Malta' of €3.1 million have been reclassified from Loans and Advances to Banks to Balances with Central Bank of Malta, Treasury Bills and Cash. Prior year figures have been restated.

Balances held with Central Bank of Malta are subject to negative interest rates.

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
14. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS				
Financial assets at fair value through profit or loss				
Financial assets mandatorily measured at FVTPL:				
Debt and other fixed income instruments (note 14.1)	7,723	7,778	7,723	7,778
Derivative financial instruments (note 14.3)	1,275	4,391	1,275	4,391
	8,998	12,169	8,998	12,169
Financial assets designated at FVTPL:				
Debt and other fixed income instruments (note 14.1)	25,338	31,855	25,338	31,855
Equity and other non-fixed income instruments (note 14.2)	31,381	27,072	31,221	26,093
Loans and advances to customers (note 17)	139,422	135,110	139,422	135,110
	196,141	194,037	195,981	193,058
	205,139	206,206	204,979	205,227

As at 31 December 2019, debt instruments with a nominal value of €12.5 million (2018: €12.5 million) were pledged in favour of the Italian Bank Intesa San Paolo against the precautionary warrant of seizure in respect of Deiulemar Trust (note 15 and note 33).

Financial liabilities at fair value through profit or loss

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Financial liabilities classified as held for trading:				
Derivative financial instruments (note 14.3)	10,907	8,812	10,907	8,812

Notes to the financial statements 31 December 2019 (continued)

14. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
14.1 Debt and other fixed income instruments				
Issued by public bodies				
- local general government	20,081	21,989	20,081	21,989
- foreign general government	12,898	13,184	12,898	13,184
	32,979	35,173	32,979	35,173
Issued by other issuers				
- foreign banks	82	4,460	82	4,460
	33,061	39,633	33,061	39,633
Listing status				
- listed on Malta Stock Exchange	20,081	21,989	20,081	21,989
- listed elsewhere	12,980	13,262	12,980	13,262
- foreign unlisted	-	4,382	-	4,382
	33,061	39,633	33,061	39,633
Summary of movements during the year:				
At the beginning of the year	39,633	111,417	39,633	111,417
Reclassification on adoption of IFRS 9	-	(48,622)	-	(48,622)
Remeasurement on adoption of IFRS 9	-	324	-	324
Reclassification of accrued interest receivable	-	526	-	526
Movement in accrued interest receivable	(36)	-	(36)	-
Acquisitions	-	1	-	1
Disposals at carrying amount	-	(1,351)	-	(1,351)
Redemptions	(5,412)	(21,614)	(5,412)	(21,614)
Movement in fair value	(1,170)	(1,516)	(1,170)	(1,516)
Exchange adjustment	46	468	46	468
At the end of the year	33,061	39,633	33,061	39,633

14.2 Equity and other non-fixed income instruments

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Issued by other issuers				
- local banks	584	688	584	688
- foreign other	26,894	22,016	26,894	22,016
- local other	3,903	4,368	3,743	3,389
	31,381	27,072	31,221	26,093
Listing status				
- listed on Malta Stock Exchange	4,487	5,056	4,327	4,077
- listed elsewhere	-	1,245	-	1,245
- foreign unlisted	26,894	20,771	26,894	20,771
	31,381	27,072	31,221	26,093
Summary of movements during the year:				
At the beginning of the year	27,072	64,811	26,093	63,836
Reclassification on adoption of IFRS 9	-	(27,851)	-	(27,851)
Acquisitions	332	4	332	-
Redemption	-	(215)	-	(215)
Disposals at carrying amount	(1,087)	(11,460)	(268)	(11,460)
Movement in fair value	4,819	1,756	4,819	1,756
Exchange adjustment	245	27	245	27
At the end of the year	31,381	27,072	31,221	26,093

Notes to the financial statements 31 December 2019 (continued)

14. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
14.3 Derivative financial instruments				
Fair value of assets	1,275	4,391	1,275	4,391
Fair value of liabilities	10,907	8,812	10,907	8,812
The above comprise over-the-counter forward exchange contracts and interest rate swaps that have not been designated as hedging instruments stated at fair value, with notional amounts analysed with remaining life as follows :				
- less than 3 months	392,559	397,454	392,559	397,454
- between 3 months and 1 year	17,489	7,496	17,489	7,496
- more than 1 year	125,102	147,112	125,102	147,112
	535,150	552,062	535,150	552,062

15. INVESTMENTS

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Debt and other fixed income instruments				
- measured at FVOCI (note 15.1)	144,011	142,907	144,011	142,907
- measured at amortised cost (note 15.2)	2,903,359	3,152,919	2,903,359	3,152,919
Equity and other non-fixed income instruments (note 15.3)				
- measured at FVOCI	23,790	19,129	23,790	19,129
	3,071,160	3,314,955	3,071,160	3,314,955

Investments with a nominal value of €66.3 million (2018: €122.2 million) have been pledged against the provision of credit lines by the Central Bank of Malta.

Investments with a nominal value of €39.7 million (2018: €39.7 million) have been pledged in favour of Depositor Compensation Scheme as at 31 December 2019.

As at 31 December 2019, Investments with a nominal value of €344 million (2018: €351 million) were pledged in favour of the Italian Bank Intesa San Paolo against the precautionary warrant of seizure in respect of Deiulemar Trust. A nominal value of €7 million has during the year been redeemed and funds kept with the Italian Bank Intesa San Paolo (notes 14, 16 and 33).

Notes to the financial statements 31 December 2019 (continued)

15. INVESTMENTS (continued)

15.1 Debt and other fixed income instruments measured at FVOCI

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Issued by public bodies				
- local general government	64,473	64,930	64,473	64,930
- local public sector	79,538	72,904	79,538	72,904
Issued by other issuers				
- foreign banks	-	5,073	-	5,073
	144,011	142,907	144,011	142,907
Listing status				
- listed on Malta Stock Exchange	144,011	137,834	144,011	137,834
- listed elsewhere	-	5,073	-	5,073
	144,011	142,907	144,011	142,907
Summary of movements during the year:				
At the beginning of the year	142,907	139,328	142,907	139,328
Reclassification on adoption of IFRS 9	-	5,181	-	5,181
Remeasurement on adoption of IFRS 9	-	(2)	-	(2)
Reclassification of interest receivable accrued	-	1,426	-	1,426
Movement in interest receivable accrued	(68)	-	(68)	-
Redemptions	(5,000)	-	(5,000)	-
Amortisation	(2,331)	(1,425)	(2,331)	(1,425)
Movement in fair value	6,535	(4,525)	6,535	(4,525)
Exchange adjustment	1,968	2,924	1,968	2,924
At the end of the year	144,011	142,907	144,011	142,907

As at 31 December 2019 the loss allowance on Debt Instruments at FVOCI amounts to €25,879 (2018: €22,867).

15.2 Debt and other fixed income instruments measured at amortised cost

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Issued by public bodies				
- local general government	453,129	418,696	453,129	418,696
- foreign general government	1,161,607	934,143	1,161,607	934,143
	1,614,736	1,352,839	1,614,736	1,352,839
Issued by other issuers				
- foreign banks	1,060,246	1,395,571	1,060,246	1,395,571
- foreign other	225,123	401,257	225,123	401,257
- other local	3,254	3,252	3,254	3,252
	1,288,623	1,800,080	1,288,623	1,800,080
	2,903,359	3,152,919	2,903,359	3,152,919
Listing status				
- listed on Malta Stock Exchange	456,383	421,947	456,383	421,947
- listed elsewhere	1,980,976	2,203,799	1,980,976	2,203,799
- foreign unlisted	466,000	527,173	466,000	527,173
	2,903,359	3,152,919	2,903,359	3,152,919

At 31 December 2019, the fair value of debt and other fixed income instruments measured at amortised cost, without deducting transaction costs, amounted to €2,948.5 million (2018: €3,176.5 million).

Notes to the financial statements 31 December 2019 (continued)

15. INVESTMENTS (continued)

15.2 Debt and other fixed income instruments measured at amortised cost (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Summary of movements during the year:				
At the beginning of the year	3,152,919	3,229,915	3,152,919	3,229,915
Reclassification on adoption of IFRS 9	-	43,441	-	43,441
Remeasurement on adoption of IFRS 9	-	(5,192)	-	(5,192)
Reclassification of interest receivable accrued	-	13,127	-	13,127
Movement in interest receivable accrued	(1,192)	-	(1,192)	-
Acquisitions	569,278	892,021	569,278	892,021
Disposals at carrying amount	-	(223,520)	-	(223,520)
Redemptions	(827,504)	(796,923)	(827,504)	(796,923)
Amortisation	(12,706)	(8,476)	(12,706)	(8,476)
Realised profit on disposals	-	818	-	818
Impairment reversal/(loss)	162	(508)	162	(508)
Exchange adjustment	22,402	8,216	22,402	8,216
At the end of the year	2,903,359	3,152,919	2,903,359	3,152,919

15.3 Equity and other non-fixed income instruments measured at FVOCI

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Issued by other issuers				
- local other	22,073	17,411	22,073	17,411
- local Banks	130	166	130	166
- local Public	1,587	1,552	1,587	1,552
	23,790	19,129	23,790	19,129
Listing status				
- listed on Malta Stock Exchange	23,790	19,129	23,790	19,129
	23,790	19,129	23,790	19,129
Summary of movements during the year:				
At the beginning of the year	19,129	5,298	19,129	5,298
Reclassification on adoption of IFRS 9	-	27,851	-	27,851
Disposals at carrying amount	-	(12,296)	-	(12,296)
Movement in fair value	4,661	(1,904)	4,661	(1,904)
Exchange adjustment	-	180	-	180
At the end of the year	23,790	19,129	23,790	19,129

Notes to the financial statements 31 December 2019 (continued)

16. LOANS AND ADVANCES TO BANKS

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Repayable on call and at short notice	342,702	262,013	342,702	262,013
Term placements with other banks	157,213	214,590	157,213	214,590
Cheques in course of collection	1,771	14,041	1,771	14,041
	501,686	490,644	501,686	490,644

Following amendments to the Depositor Compensation Scheme (DCS) Regulations (Regulation (27)(2) of the DCS Regulations, 2015), Banks can opt to pledge securities instead of deposits with Central Bank of Malta. In this respect, no balances with Central Bank of Malta have been pledged in favour of the Depositor Compensation Scheme as at 31 December 2019 (2018: nil).

Balances with a carrying amount of €29.8 million (2018: €22.9 million) were held as collateral against derivative contracts.

During the current financial year, 'Term placements with Central Bank of Malta' of €3.1 million have been reclassified from Loans and Advances to Banks to Balances with Central Bank of Malta, Treasury Bills and Cash. Prior year figures have been restated.

Balances held with certain banks are subject to negative interest rates.

An amount of €7 million (2018: nil) have been pledged in favour of the Italian Bank Intesa San Paolo against the precautionary warrant of seizure in respect of Deiulemar Trust (notes 15 and 33).

17. LOANS AND ADVANCES TO CUSTOMERS

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
Repayable on call and at short notice	477,853	492,017	477,853	492,017
Term loans and advances	4,076,280	3,978,029	4,076,280	3,978,029
	4,554,133	4,470,046	4,554,133	4,470,046
Less impairment losses	(108,321)	(107,063)	(108,321)	(107,063)
Net loans and advances at amortised cost	4,445,812	4,362,983	4,445,812	4,362,983
Loans and advances designated at fair value through profit or loss (note 14)	139,422	135,110	139,422	135,110
Total loans and advances	4,585,234	4,498,093	4,585,234	4,498,093

Notes to the financial statements 31 December 2019 (continued)

18. INVESTMENTS IN EQUITY-ACCOUNTED INVESTEES

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
At the beginning of the year	108,510	109,461	52,870	52,870
Share of results, net of tax	15,897	8,214	-	-
Dividend received	(22,928)	(9,165)	-	-
At the end of the year	101,479	108,510	52,870	52,870
Amounts include:				
Local listed	27,794	28,489	22,304	22,304
Local unlisted	73,685	80,021	30,566	30,566
	101,479	108,510	52,870	52,870

On the historical cost basis, shares in equity-accounted investees of the Group, would have been included at a cost of €52.9 million (2018: €52.9 million).

The fair value of the equity-accounted investees that is publicly quoted amounted to €61.8 million (2018: €56.9 million) at 31 December 2019. The cost of this investment is €22.3 million (2018: €22.3 million).

The fair value of the publicly quoted investee is calculated using observable inputs and are regarded as being Level 1 under IFRS 13.

Details of the associates held by the Group and the Bank are as follows:

Name of company	Equity Interest 2019 %	Equity Interest 2018 %	Class	Incorporated in	Nature of Business
MAPFRE Middlesea p.l.c.	31.08	31.08	Ordinary Shares	Malta	Insurance
MAPFRE MSV Life p.l.c.*	50.00	50.00	Ordinary Shares	Malta	Life Assurance

Name of company	Group's share of results 2019 €000	Group's share of results 2018 €000
MAPFRE Middlesea p.l.c.	4,588	2,647
MAPFRE MSV Life p.l.c.	11,309	5,567
	15,897	8,214

*A further 15.54% (2018:15.54%) is held indirectly via another equity accounted investee. Although the Bank has an effective participating interest of 65.54% (2018: 65.54%), it does not exercise control over the financial and operating decisions of the associate as it only has the right for equal representation on the Board of Directors of the associate together with the other shareholders. Furthermore, as from 1 October 2011 the Bank is deemed to exercise significant influence on MAPFRE MSV Life p.l.c. as opposed to joint control as a result of a shareholders' agreement which gives the other shareholder control and as from the financial year 30 September 2012 it is being treated as an equity-accounted investee.

The financial statements of the equity-accounted investees are prepared to 31 December.

The registered addresses of the associates are as follows:

MAPFRE Middlesea p.l.c.	Middlesea House, Floriana FRN 1442, Malta
MAPFRE MSV Life p.l.c.	The Mall, Mall Street, Floriana FRN 1470, Malta

Notes to the financial statements 31 December 2019 (continued)

18. INVESTMENTS IN EQUITY-ACCOUNTED INVESTEES (continued)

Summarised financial information extracted from the published preliminary statement of annual results of the associates as at 31 December 2019 in respect of the equity-accounted investees:

	2019	2018
	€000	€000
Total assets	2,616,125	2,318,779
Total liabilities	2,452,936	2,147,085
Revenues	545,421	370,221
Results for the period	15,505	14,035

	The Group	
	2019	2018
	€000	€000
Share of net assets of equity-accounted investees	101,479	108,510
Share of results of equity-accounted investees	15,897	8,214

The judgements made by the equity-accounted investees and the key sources of estimation uncertainties are disclosed below:

Estimate of in-force business

Assumptions
The value of in-force business is determined by the directors of the equity-accounted investee based on the advice of the entity's consulting actuaries. The valuation represents the discounted value of projected future transfers to shareholders from policies in force at the year end, after making provision for taxation. In determining this valuation, assumptions relating to future mortality, persistence and levels of expenses are based on experience of the type of business concerned. Gross investment returns assumed vary depending upon the mix of investments held by the associates and expected market conditions. The value depends on assumptions made regarding future economic and demographic experience. The impact of the change of the present value of in-force (PVIF) accounts was 23% of the result for the year. The PVIF represents 35% of the carrying value of the investments in equity-accounted investees.

This valuation assumes a spread of 2% (2018: 2%) between the weighted average projected investment return and the risk adjusted discount factor applied of 6.5% (2018: 6.5%). The calculation also assumes lapse rates varying from 0.5% to 8% per annum (2018: 0.5% to 8% per annum) and an expense inflation rate 3.5% (2018: 3.5%).

Changes in assumptions
Assumptions are reviewed on an annual basis to reflect the development of experience and to improve on the reliability of the estimation process.

Ultimate liability arising from claims made under insurance contracts
There are several sources of uncertainty that need to be considered in the estimate of the liability that the equity-accounted investees will ultimately pay for such claims. In particular insurance risks including exposure to liability can span over more than one accounting year, and this increases the uncertainty surrounding the estimate for final settlement.

In calculating the estimated cost of unpaid claims, the equity-accounted investees uses a combination of estimation techniques, based partly on known information at year end, partly on statistical analysis of historical experience and on actuarial valuations carried out by an independant external actuary.

Notes to the financial statements 31 December 2019 (continued)

19. INVESTMENTS IN SUBSIDIARY COMPANIES

Name of company	Equity interest 2019 %	Equity interest 2018 %	Class	Incorporated in	Nature of Business
BOV Asset Management Limited	100	100	Ordinary	Malta	Fund Management
BOV Fund Services Limited	100	100	Ordinary	Malta	Fund Administration

Name of company Cost/Carrying amount	The Bank 2019 €000	The Bank 2018 €000
BOV Asset Management Limited	5,481	5,481
BOV Fund Services Limited	749	749
	6,230	6,230

The registered address of the above unlisted undertakings is as follows:

BOV Asset Management Limited	58, Triq San Żakkarija, Il-Belt Valletta VLT 1130
BOV Fund Services Limited	58, Triq San Żakkarija, Il-Belt Valletta VLT 1130

All subsidiaries prepared their financial statements to the same date, 31 December.

20. INTANGIBLE ASSETS

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Software				
Cost				
1 January	66,813	49,764	66,813	49,764
Additions	24,737	18,197	24,737	18,197
Assets retired from active use	(345)	(1,148)	(345)	(1,148)
31 December	91,205	66,813	91,205	66,813
Accumulated amortisation				
1 January	24,770	21,311	24,770	21,311
Charge for the year	6,317	4,607	6,317	4,607
Accumulated amortisation on assets retired from active use	(345)	(1,148)	(345)	(1,148)
31 December	30,742	24,770	30,742	24,770
Carrying amount at 31 December	60,463	42,043	60,463	42,043
Future capital expenditure:				
- contracted but not provided for in the financial statements	4,386	14,201	4,386	14,201
- authorised by the directors but not contracted	26,797	16,970	26,797	16,970

No amortisation has been recognised on accumulated software costs amounting to €38.3 million as at 31 December 2019 relating to the core banking transformation project as these were not yet available for use by the end of financial year.

Notes to the financial statements 31 December 2019 (continued)

21. PROPERTY AND EQUIPMENT

See Accounting policies in Note 1.1 Basis of preparation - Changes in accounting policies arising from the adoption of new standards during the year ended 31 December 2019:

21.1 Reconciliation of Carrying Amount

	Land and buildings €000	IT infrastructure and equipment €000	Other €000	Total €000
The Group				
Cost or valuation				
Balance at 1 January 2018	101,705	31,882	31,017	164,604
Additions	3,006	3,501	1,591	8,098
Assets retired from active use	(429)	(5,593)	(5,500)	(11,522)
Disposals	(1,726)	-	-	(1,726)
Revaluation	12,762	-	-	12,762
Balance at 31 December 2018	115,318	29,790	27,108	172,216
Balance at 1 January 2019	115,318	29,790	27,108	172,216
Recognition of right-of-use asset on initial application of IFRS 16	7,420	-	1,185	8,605
Adjusted balance at 1 January 2019	122,738	29,790	28,293	180,821
Additions	4,864	5,980	1,699	12,543
Assets retired from active use	(3)	(133)	(1,144)	(1,280)
Disposals	(479)	-	(9)	(488)
Revaluation	22	-	-	22
Reclassification to Assets held for realisation	(6,638)	-	-	(6,638)
Balance at 31 December 2019	120,504	35,637	28,839	184,980
Accumulated depreciation				
Balance at 1 January 2018	15,663	19,926	23,793	59,382
Depreciation for the year	948	3,308	1,443	5,699
Accumulated depreciation on assets retired from active use	(424)	(5,617)	(5,516)	(11,557)
Disposals	(463)	-	-	(463)
Balance at 31 December 2018	15,724	17,617	19,720	53,061
Balance at 1 January 2019	15,724	17,617	19,720	53,061
Depreciation for the year	2,117	3,322	1,716	7,155
Accumulated depreciation on assets retired from active use	(3)	(133)	(1,144)	(1,280)
Disposals	(152)	-	-	(152)
31 December 2019	17,686	20,806	20,292	58,784
Carrying amount at:				
Balance at 31 December 2018	**99,594**	**12,173**	**7,388**	**119,155**
Balance at 31 December 2019	**102,818**	**14,831**	**8,547**	**126,196**

Notes to the financial statements 31 December 2019 (continued)

21. PROPERTY AND EQUIPMENT (continued)

21.1 Reconciliation of Carrying Amount (continued)

	Land and buildings €000	IT infrastructure and equipment €000	Other €000	Total €000
The Bank				
Cost or valuation				
Balance at 1 January 2018	101,666	31,238	29,336	162,240
Additions	3,006	3,501	1,525	8,032
Assets retired from active use	(429)	(5,593)	(5,500)	(11,522)
Disposals	(1,726)	-	-	(1,726)
Revaluation	12,762	-	-	12,762
Balance at 31 December 2018	115,279	29,146	25,361	169,786
Balance at 1 January 2019	115,279	29,146	25,361	169,786
Recognition of right-of-use asset on initial application of IFRS 16	7,420	-	1,185	8,605
Adjusted balance at 1 January 2019	122,699	29,146	26,546	178,391
Additions	4,864	5,980	1,652	12,496
Assets retired from active use	(3)	(133)	(1,144)	(1,280)
Disposals	(479)	-	(9)	(488)
Revaluation	22	-	-	22
Reclassification to Assets held for realisation	(6,638)	-	-	(6,638)
Balance at 31 December 2019	120,465	34,993	27,045	182,503
Accumulated depreciation				
Balance at 1 January 2018	15,570	19,103	22,519	57,192
Depreciation for the year	948	3,308	1,380	5,636
Accumulated depreciation on assets retired from active use	(424)	(5,617)	(5,516)	(11,557)
Disposals	(463)	-	-	(463)
Balance at 31 December 2018	15,631	16,794	18,383	50,808
Balance at 1 January 2019	15,631	16,794	18,383	50,808
Depreciation for the year	2,117	3,322	1,657	7,096
Accumulated depreciation on assets retired from active use	(3)	(133)	(1,144)	(1,280)
Disposals	(152)	-	-	(152)
Balance at 31 December 2019	17,593	19,983	18,896	56,472
Carrying amount at:				
31 December 2018	**99,648**	**12,352**	**6,978**	**118,978**
31 December 2019	**102,872**	**15,010**	**8,149**	**126,031**

As at 31 December 2019, Property and Equipment includes right-of-use assets of €9.6million related to office premises and motor vehicles (see note 21.1).

	The Group		The Bank	
	2019 €000	2018 €000	2019 €000	2018 €000
Carrying amount of land and buildings occupied for own use	102,818	94,398	102,872	94,452
Future capital expenditure:				
- contracted but not provided for in the financial statements	5,109	4,617	5,109	4,617
- authorised by the directors but not contracted for	20,119	21,600	20,119	21,600

Notes to the financial statements 31 December 2019 (continued)

21. PROPERTY AND EQUIPMENT (continued)

21.1 Reconciliation of Carrying Amount (continued)

Land and buildings are revalued by professionally qualified architects in accordance with the policy documented in Note 1. The carrying amounts of land and buildings that would have been included in the financial statements had these assets been carried at cost less accumulated depreciation are:
2019: Group and Bank €48.3 million (2018: Group and Bank €53.6 million).

Property valuations are mainly valued using the 'comparative investment approach' whereby market value is arrived at by capitalising at an appropriate yield rate, the annual income produced, should the property be leased out to third parties. The income is arrived at by analysing a number of estate agent listings for comparative properties and determining a mean rental value rate. The valuation techniques were consistent with those applied for the year ended 31 December 2018. Revaluations are carried out on a regular basis in accordance with the Group's accounting policies.

Property fair value measurement is classified as Level 3. Significant unobservable inputs used in the valuation of these properties is the rental income for office space and the percentage capitalisation rate which indicates the multiplier relationship between Net Rental Income and Property Value. Further details about these significant inputs are summarised in the table below:

	Significant unobservable input	**Narrative sensitivity**
Buildings in Commercial Area	Price per square metre, ranging from €110/sqm to €995/sqm	The higher the price per square metre the higher the fair value
	Capitalisation rate, ranging from 5.5% to 8.10%	The higher the capitalisation rate the lower the fair value
Buildings in Residential Area	Price per square metre, ranging from €100/sqm to €293/sqm	The higher the price per square metre the higher the fair value
	Capitalisation rate, ranging from 5.25% to 6.00%	The higher the capitalisation rate the lower the fair value

Notes to the financial statements 31 December 2019 (continued)

21. PROPERTY AND EQUIPMENT (continued)

21.2 Leases

See Accounting policies in Note 1.1 Basis of preparation - Changes in accounting policies arising from the adoption of new standards during the year ended 31 December 2019:

The Group's lease arrangements comprise long-term leasehold properties, other immovable property leaseholds, equipment leases and property space for ATMs which were classified as operating leases under IAS 17. Under IFRS 16, the Group has recognised new assets (right-of-use assets) and liabilities (lease liabilities) for all of its lease arrangements which were previously classified as operating leases under IAS 17, with the exceptions of some arrangements of low value items or short-term arrangements of one year or less.

Information about leases for which the Group is a lessee is presented below.

i. Right-of-use assets

Right-of-use assets relate to office premises and motor vehicles that are presented within property and equipment (see note 21.1).

	Land and buildings €000	Other €000	Total €000
Balance at 1 January	7,421	1,184	8,605
Depreciation charge for the year	(1,029)	(253)	(1,282)
Additions	2,167	118	2,285
Disposals	-	(9)	(9)
Balance at 31 December	8,559	1,040	9,599

See Note 27 for maturity analysis of lease liabilities as at 31 December 2019.

ii. Amounts recognised in profit or loss

	Land and buildings €000	Other €000	Total €000
Interest on lease liabilities	191	21	212
Expenses relating to short-term leases	310	5	315
Expenses relating to low value items	-	8	8
	501	34	535

iii. Amounts recognised in statement of cash flows

	Land and buildings €000	Other €000	Total €000
Total cash outflow for leases	1,212	263	1,475

iv. Extension options

Some property leases contain extension options exercisable by the Group and not by the lessors. The Group assesses at lease commencement date whether it is reasonably certain to exercise the extension options, and if it is reasonably certain to exercise the extension option, the Group includes this period in the lease term and the potential future lease payments in the lease liability.

Notes to the financial statements 31 December 2019 (continued)

22. DEFERRED TAX

Deferred taxation is analysed as follows:

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
Net deferred tax asset arising on:				
Fair value movement of financial instruments	281	281	281	281
Impairment allowances	43,802	44,375	43,802	44,375
Allowance for employee benefits	4,785	5,814	4,785	5,814
Excess of capital allowances over depreciation	(11,354)	(8,330)	(11,354)	(8,330)
Defined benefit plans	3,503	3,359	3,503	3,359
Provisions and other temporary differences	35,000	26,250	35,000	26,250
	76,017	71,749	76,017	71,749
Deferred tax liability arising on:				
Property revaluation	5,736	5,743	5,736	5,743

The Group and the Bank

	At 31 December 2018 €000	Recognised in profit or loss €000	Recognised in OCI €000	Recognised in other equity €000	IFRS 9 adoption €000	At 31 December 2019 €000
Movement in temporary differences relating to:						
Fair value movement of financial instruments	281	-	-	-	-	281
Impairment allowances	44,375	(573)	-	-	-	43,802
Allowance for employee benefits	5,814	(1,029)	-	-	-	4,785
Excess of capital allowances over depreciation	(8,330)	(3,023)	-	-	-	(11,354)
Defined benefit plans	3,359	-	144	-	-	3,503
Property revaluation	(5,743)	-	(2)	9	-	(5,736)
Provisions and other temporary differences	26,250	8,750	-	-	-	35,000
	66,006	4,125	142	9	-	70,281

The Group and the Bank

	At 31 December 2017 €000	Recognised in profit or loss €000	Recognised in OCI €000	Recognised in other equity €000	IFRS 9 adoption €000	At 31 December 2018 €000
Movement in temporary differences relating to:						
Fair value movement of financial instruments	(1,793)	-	-	-	2,074	281
Impairment allowances	58,317	(16,610)	-	-	2,668	44,375
Allowance for employee benefits	7,111	(1,297)	-	-	-	5,814
Excess of capital allowances over depreciation	(5,507)	(2,823)	-	-	-	(8,330)
Defined benefit plans	2,069	-	1,290	-	-	3,359
Property revaluation	(4,519)	-	(1,224)	-	-	(5,743)
Provisions and other temporary differences	-	26,250	-	-	-	26,250
	55,678	5,520	66	-	4,742	66,006

The Group's deferred tax assets and liabilities on the statement of financial position have not been off-set to the extent that there is no legally enforceable right of set-off with the tax authorities.

Notes to the financial statements 31 December 2019 (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
23. OTHER ASSETS				
Settlement account	38,204	5,027	38,204	5,027
Deferred expenditure	3,816	2,211	3,816	2,211
Other	607	662	607	662
	42,627	7,900	42,627	7,900
24. AMOUNTS OWED TO BANKS				
Term deposits	30,445	73,380	30,445	73,380
Repayable on demand	35,602	72,641	35,602	72,641
	66,047	146,021	66,047	146,021
25. AMOUNTS OWED TO CUSTOMERS				
Term deposits	1,726,294	1,791,042	1,726,294	1,791,042
Repayable on demand	8,903,425	8,623,866	8,905,966	8,626,957
	10,629,719	10,414,908	10,632,260	10,417,999
26. DEBT SECURITIES IN ISSUE				
4.25% Euro debt securities	-	40,197	-	40,197
	-	40,197	-	40,197

The 4.25% Euro unsubordinated bonds matured on 17 May 2019.

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
27. OTHER LIABILITIES				
Post employment and termination liabilities (see note 35)	23,772	26,302	23,772	26,302
Cash collateral for commitments	56,096	55,574	56,096	55,574
Deposits from companies in formation	3,454	4,941	3,454	4,941
Bills payable	41,625	36,024	41,625	36,024
Accruals and deferred income	29,699	25,272	29,699	25,272
Payment orders outwards	257	23,572	257	23,572
Lease Liability (analysed in the following table)	9,617	-	9,617	-
Other	24,589	24,736	24,361	24,519
	189,109	196,421	188,881	196,204

Notes to the financial statements 31 December 2019 (continued)

27. OTHER LIABILITIES (continued)

Lease Liability

At 31 December 2019, the future minimum lease payments under non-cancellable operating leases were payable as follows:

	The Group and the Bank		
	Land and buildings	Other	Total
	€000	€000	€000
Maturity analysis - Contractual undiscounted cash flows			
Less than one year	1,128	261	1,389
Between one and five years	4,531	831	5,362
More than five years	5,209	5	5,214
Total undiscounted lease liabilities at 31 December	10,868	1,097	11,965
Lease liabilities included in statement of financial position at 31 December:			
Current	920	244	1,164
Non-current	7,648	805	8,453
	8,568	1,049	9,617

Operating lease commitments as at 31 December 2018 under IAS 17 were equivalent to the opening lease liability as at 1 January 2019.

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
28. ACCRUALS AND DEFERRED INCOME				
Accruals	484	539	-	-
	484	539	-	-

The above amounts include amounts owed to suppliers in respect of services rendered in the current financial year which were not yet invoiced.

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
29. DERIVATIVES DESIGNATED FOR HEDGE ACCOUNTING				
Derivative financial instruments designated as fair value hedges	13,963	10,206	13,963	10,206

Refer to Note 6. Net gain on Investments and hedging instruments for the net gain/loss on the bond and hedging instrument.

The above comprise over-the-counter interest rate swaps, stated at fair value with notional amounts analysed by the remaining life as follow:

-less than 3 months	5,000	-	5,000	-
-more than 1 year	58,280	61,754	58,280	61,754
	63,280	61,754	63,280	61,754

Notes to the financial statements 31 December 2019 (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
30. SUBORDINATED LIABILITIES				
5.35% Euro subordinated unsecured bonds	-	50,118	-	50,118
4.80% Euro subordinated unsecured bonds	70,993	70,993	70,993	70,993
3.50% Euro subordinated unsecured bonds	113,130	113,130	113,130	113,130
3.75% Euro subordinated unsecured bonds	50,107	-	50,107	-
	234,230	234,241	234,230	234,241

The 5.35% Euro subordinated bonds matured on 15 June 2019.

The 4.8% Euro subordinated bonds are redeemable at par on 15 March 2020 and are listed on the Malta Stock Exchange. The fair value of these unsecured bonds as at 31 December 2019 is €70.0 million (2018: €70.6 million).

The 3.5% Euro subordinated bonds are redeemable at par on 8 August 2030 and are listed on the Malta Stock Exchange. The fair value of these unsecured bonds as at 31 December 2019 is €111.1 million (2018: €111.5 million).

The 3.75% Euro subordinated bonds which were issued during this financial year, are redeemable at par on 15 June 2031 and are listed on the Malta Stock Exchange. The fair value of these unsecured bonds as at 31 December 2019 is €50.4 million (2018: nil).

	The Bank	
	2019	2018
31. SHARE CAPITAL AND SHARE PREMIUM	€000	€000
Share capital		
Authorised:		
1,000,000,000 Ordinary shares of €1.00 each	1,000,000	1,000,000
(2018: 1,000,000,000 Ordinary shares of €1.00 each)		
Issued and paid up:		
583,849,000 Ordinary shares of €1.00 each fully paid	583,849	530,772
(2018: 530,772,000 Ordinary shares of €1.00 each fully paid)		

During the financial year ended 31 December 2018 ordinary share capital increased by €5,772,000 (57,772,000 shares at €1.00) as a result of the scrip dividend programme. On 11 June 2019, the Bank made a bonus issue of 53,077,200 fully paid ordinary shares of a nominal value of €1.00 per share, representing 1 bonus share for every 10 shares held, thereby increasing the issued share capital from 531 million shares to 584 million shares, resulting in a paid up capital of €584 million.

	The Bank	
	2019	2018
Share Premium	€000	€000
Share Premium	49,277	49,277

32. OTHER RESERVES

Retained Earnings
Retained earnings represent the profits retained over the years and primarily comprise the profit attributable to equity holders and transfers to share capital in respect of the bonus issue. This reserve includes the amount held in respect of General Banking Reserves.

General Banking Reserves
The revised Banking Rule 09 requires banks in Malta to hold additional reserves for general banking risks against non-performing loans. This reserve is required to be funded from planned dividend. As at the reporting date this reserve amounts to €5.3 million (2018: €6.3 million).

Revaluation Reserves
Revaluation reserves represent fair value movements on land and buildings and financial assets at FVOCI net of tax, which are recognised in Other Comprehensive Income.

Notes to the financial statements 31 December 2019 (continued)

32. OTHER RESERVES (continued)

	The Group	The Bank
	€000	€000
On land and buildings:		
31 December 2017	29,232	29,232
Property revaluation	12,762	12,762
Deferred tax and effect of changes in property tax rates	(1,276)	(1,276)
Release of surplus on sale of property, net of tax	(462)	(462)
31 December 2018	40,256	40,256
Property revaluation	22	22
Deferred tax and effect of changes in property tax rates	(2)	(2)
Release of surplus on sale of property, net of tax	(82)	(82)
31 December 2019	**40,194**	**40,194**
On fair value through other comprehensive income:		
31 December 2017	3,962	3,850
Adjustments on initial application of IFRS 9	14,728	14,728
Tax thereon	(5,155)	(5,155)
Adjusted balance at 1 January 2018	13,535	13,423
Fair value adjustments	(3,863)	(3,863)
Transfer to retained earnings on disposal	(1,917)	(1,917)
Tax thereon	2,023	2,023
31 December 2018	**9,778**	**9,666**
Fair value adjustments	7,578	7,578
Tax thereon	(2,652)	(2,652)
31 December 2019	**14,704**	**14,592**
Total	**54,898**	**54,786**

33. PROVISIONS AND CONTINGENCIES

Provisions	Financial guarantees and loan commitments provisions €000	Custody and trust litigation provision €000	Other litigation provision €000	Total €000
Carrying amount at 1 January 2019	18,767	75,000	2,000	95,767
Movement	(2,658)	25,000	-	22,342
Carrying amount at 31 December 2019	**16,109**	**100,000**	**2,000**	**118,109**

	The Group		The Bank	
	2019	2018	2019	2018
Contingencies	€000	€000	€000	€000
Acceptances and endorsements	2,800	2,862	2,800	2,862
Guarantees	313,651	304,310	313,651	304,310
Provision for default on forward contracts	2,815	5,815	2,815	5,815
Other contingent liabilities	22,352	22,418	22,352	22,418
	341,618	**335,405**	**341,618**	**335,405**

Notes to the financial statements 31 December 2019 (continued)

33. PROVISIONS AND CONTINGENCIES (continued)

Financial guarantee contracts and loan commitments provision
The amount in respect of financial guarantee contracts and loan commitments issued represent the expected credit loss as at 31 December 2019.

Contingent liabilities
Contingent liabilities are backed by corresponding obligations from third parties.

Bank of Valletta is a party to legal proceedings arising out of its normal business operations. Matters arising from a set of similar circumstances can give rise to either a provision or a contingent liability, depending on the relevant facts and circumstances. The recognition of provisions and the disclosure of contingent liabilities in relation to such matters involves critical accounting estimates and judgements and is determined in accordance with the relevant accounting policies described in Note 1 (1.25.5). Except as disclosed hereunder, it is not practicable to provide an aggregate estimate of potential liability for the Bank's other legal proceedings as a class of contingent liabilities.

The Bank considers the provisions recognised to date to be sufficient to cover any likely requirements of the Bank to settle its claims.

Litigation and claims provisions
The significant developments in the principal legal outstanding cases in relation to custody and trusts are disclosed below:

Deiulemar Trust
In November 2014, court action was instituted against the Bank by the curator of a failed group while under the trust of the Bank, by virtue of which a claim of €363 million was made. In March 2018, the Italian Tribunal of Torre Annunziata upheld the issue of the precautionary warrant against the Bank for the sum of €363 million. Although the amount of the warrant does not necessarily reflect Bank of Valletta's potential financial exposure, the Bank pledged financial instruments in favour of the Italian Bank Intesa San Paolo. The Italian Tribunal declined the Bank's request for suspension of the garnishee and in 2018 the Bank's appeal was also rejected. The Bank's request for the judge to recuse herself was not accepted. Following these events the Bank sought to protect its "right to a fair hearing" before an independent and impartial judiciary and invoked Art. 51 of the Italian Code of Procedure regarding constitutional legitimacy but the Court of Torre Annunziata rejected this attempt. During this financial year the Bank filed an application before the European Court of Human Rights (ECHR) to defend its right for a fair hearing and also presented its submissions to the Court of Torre Anunziata to reconsider the Bank's request to appoint a valuation expert and to stay proceedings pending the ECHR application. Proceedings continue and final judgement may technically be delivered by the Judge at Torre Annunziata as early as May/June 2020. There remain significant uncertainties on the eventual outcome. The Bank has further sought additional, completely independent, specialist legal advice in February 2020, which clearly substantiates the basis up on which the Bank's legal arguments are formed. The Bank considers the claim against it to be without merit and considers that a fair hearing would confirm this.

Falcon Fund SICAV
The Bank has received a claim from Hammaeskiold & Co as legal representatives of the Swedish Pension Agency (SPA), being the sole investor in the Falcon Fund SICAV (FFS). The damages claimed to have been suffered by SPA amount to at least SEK 740 million (€71 million). No court proceedings have yet been initiated, SPA had indicated their intention to do so. The amount of the claim does not necessarily reflect Bank of Valletta's potential financial exposure on this matter. Discussion between parties to resolve the matter are ongoing, and both parties have agreed to independent mediator. The Bank expects to resolve the matter in the middle of 2020.

La Vallette Multi Manager Property Fund (LVMMPF)
Proceedings in front of the Office of the Arbiter for Financial Services (OAFS) were instituted by a number of investors in the defunct La Vallette Multi Manager Property Fund against Financial Service Providers (FSPs), namely the Bank, the fund manager (a subsidiary of the BOV Group) and the SICAV. On 23 February 2018, the arbiter found in favour of the claimants and ordered the FSPs, in solidum between them, to pay the claimants the sum of €3.4 million, together with legal interest from the date when each complainant filed his claim before OAFS up to date of effective payment and also together with legal costs. On 14 March 2018, the Group filed an appeal before the Court of Appeal (Inferior Jurisdiction) from the before mentioned decision. Judgement on the appeal was delivered on 16 December 2019 and the Bank won the appeal from the decision given by the Arbiter of Financial Services.

Due to the uncertainties inherent in such matters, provisions on the above principal cases are based on the best information and legal advice available at the reporting date and the ultimate settlement could be higher or lower depending on the outcome whilst the timing of the outflow of economic resources is uncertain. During the year ended 31 December 2019 the initial estimate of €75 million litigation provision recognised in 2018 was re-estimated to €100m which is deemed to better reflect any resulting outflows, including potentially protracted legal costs and any negotiated settlements. No amount was utilised during the year.

Notes to the financial statements 31 December 2019 (continued)

	The Group		The Bank	
	2019	2018	2019	2018
	€000	€000	€000	€000
34. COMMITMENTS				
Documentary credits	44,816	60,212	44,816	60,212
Undrawn formal standby facilities, credit facilities and other commitments to lend	1,768,695	1,796,548	1,768,695	1,796,548
Capital expenditure contracted but not provided for in the financial statements	9,495	18,818	9,495	18,818
Commitments to financial institutions	5,750	5,814	5,750	5,814
	1,828,756	**1,881,392**	**1,828,756**	**1,881,392**

35. POST EMPLOYMENT AND TERMINATION LIABILITIES

The Group's and the Bank's major post-employment benefit plan (the "plan") applies to eligible individuals. The benefits provided to the individuals in terms of the plan are computed on a specified formula which takes into consideration, amongst other things, the employees' salary on retirement and the pension entitlement in terms of Maltese law.

The provision is computed in accordance with the accounting policy for post-employment benefit plans.

This provision represents the Group's and the Bank's obligation:

(i) discounted to the net present value at the rate which has been determined by reference to market yields at the end of the reporting period on Malta government bonds (the Directors consider this to be an appropriate proxy to a high quality corporate bond);
(ii) after considering the life expectancy of such employees based on the latest publicly available mortality tables;
(iii) the expected terminal salaries; and
(iv) the Bank's expectations of the employees' retirement date.

The Group and the Bank have during financial year 2019 launched three Voluntary Retirement Schemes and a Gradual Retirement Scheme. Accepted applicants under the respective schemes shall be given:

(i) a lump sum payment of three times their terminal salary; or
(ii) a lump sum payment of one time their terminal salary and a proportion of the terminal annual salary depending on the aggregate years of services; or
(iii) a sum equivalent to 1 year's terminal salary paid by way of a Retirement Gratuity, reduced pro-rata, up to the age of 61.

Applicants shall be eligible to the different schemes according to the schemes' individual criteria.

Furthermore, the Group and the Bank make payments to certain eligible employees in consideration of the liquidation of a defunct pension scheme.

The movement in the plans is analysed as follows:

	The Group and the Bank	
	2019	2018
	€000	€000
Present value at 1 January	26,302	26,229
Payments effected	(3,622)	(4,259)
Recognised in profit or loss:		
- Interest expense	131	(249)
- Terminal benefits	552	804
Remeasurement of actuarial gains/(losses) recognised in other comprehensive income resulting from:		
- Experience adjustments	(230)	(309)
- Changes in financial assumptions	639	-
- Changes in demographic assumptions	-	4,086
Present value at 31 December	23,772	26,302

Notes to the financial statements 31 December 2019 (continued)

35. POST EMPLOYMENT AND TERMINATION LIABILITIES (continued)

The year-end obligation in relation to the plan is mainly in relation to retired employees.

The plan exposes the Group and the Bank to the following main risks:
(i) interest risk, since a decrease in market yields will increase the plan liability;
(ii) longevity risk, since an increase in the life expectancy of the plan participants will increase the plan liability.

The significant actuarial assumptions applied by the Group and the Bank in respect of the plan were as follows:

	The Group and the Bank	
	2019	**2018**
Discount rates	0.0%	0.5%
Life expectancy (years):		
Males	81	81
Females	85	85

The Group and the Bank are providing sensitivity analysis in connection with each significant actuarial assumption applied in respect of the plan. These analyses are prepared as of the end of the reporting period, showing how the liability would have been affected by hypothetical changes in the relevant actuarial assumptions that were reasonably possible at that date, while holding all other assumptions constant. The analysis presented below are for illustrative purposes only and may not be representative of the actual change in the defined benefit obligation as it is unlikely that the change in assumptions would occur in isolation of one another. In presenting the sensitivity analysis, the present value of the obligation has been calculated using the projected unit credit method at the end of the reporting period. The amounts generated from the analysis represent forward-looking estimates and hence, actual results in the future may differ materially from those projected results. In accordance with the transitional provisions in the revised IAS 19, the Group and the Bank have not disclosed comparative information in this respect.

- If the discount rate is 100 basis points higher (lower) with all other assumptions held constant, the defined benefit obligation decreases by €1.4 million (increases by €1.5 million)
- If the life expectancy increases (decreases) by two years for both men and women with all other assumptions held constant, the defined benefit obligation increases by €3.4 million (decreases by €3.4 million).

The weighted average duration of the liability in respect of the plan at 31 December 2019 is 9 years (2018: 10 years).

The Bank does not fund these pensions by assigning specific assets as there is sufficient liquidity to meet the required payments as these arise.

36. NOTES TO THE STATEMENTS OF CASH FLOWS

		The Group		The Bank	
	Note	**2019**	**2018**	**2019**	**2018**
		€000	**€000**	**€000**	**€000**
Cash	13	98,127	60,287	98,127	60,287
Balances with Central Bank of Malta (excluding Reserve Deposit)		3,373,098	3,154,289	3,373,098	3,154,289
Treasury bills (with original maturity of less than 3 months)		61,033	74,066	61,033	74,066
Money at call and short notice		499,921	476,610	499,921	476,610
Amounts owed to banks		(63,311)	(138,393)	(63,311)	(138,393)
Cash and cash equivalents included in the statements of cash flows		**3,968,868**	**3,626,859**	**3,968,868**	**3,626,859**
Balances with contractual maturity of more than 3 months		35,049	18,571	35,049	18,571
		4,003,917	3,645,430	4,003,917	3,645,430
Equivalent items reported in the statement of financial position:					
Balances with Central Bank of Malta, Treasury bills and cash (excluding Reserve Deposit)		3,568,278	3,300,807	3,568,278	3,300,807
Loans and advances to banks		501,686	490,644	501,686	490,644
Amounts owed to banks		(66,047)	(146,021)	(66,047)	(146,021)
		4,003,917	3,645,430	4,003,917	3,645,430

Notes to the financial statements 31 December 2019 (continued)

37. RELATED PARTY TRANSACTIONS

During the current and prior year, the Group and the Bank entered into transactions during the course of their normal business, with equity-accounted investees, subsidiaries, the Government of Malta ("The Government") (which has a 25% holding in the Bank), Government related entities, key management personnel, and other related parties. Government related entities are those where, in the opinion of the Bank, the Government is either deemed to exercise control, that is, it has the power to govern the financial and operating policies of the entity or linked to the Government but not controlled by the Government.

Key management personnel includes the Chairman, Directors, the members of the Management Board and their respective spouses, spousal equivalent and dependants. Other related parties are those companies over which the key management personnel hold control or significant influence (directorship).

Transactions with related parties are made on an arm's length basis.

The Bank also entered into related party transactions on an arm's length basis with its subsidiaries and equity-accounted investees. Transactions between the Bank and its subsidiaries have been eliminated on consolidation.

The amounts due to or from related parties are settled in cash and the amount of related party transactions and outstanding balances at the reporting date are disclosed below:

The Group	2019 Related party balances €000	Total activity/ balance €000	% of total	2018 Related party balances €000	Total activity/ balance €000	% of total
Interest and similar income:						
- on loans and advances						
The Government	1,516			1,990		
Government related entities	14,123			13,766		
Key management personnel	37			37		
Other related parties	87			94		
	15,763	169,825	9%	15,887	165,177	10%
Interest and similar income:						
- on debt and other fixed income instruments						
The Government	10,452	37,138	28%	10,548	48,719	22%
Interest expense						
Equity-accounted investees	1,766			575		
The Government	14,743			12,242		
Government related entities	1,283			904		
Key management personnel	20			22		
Other related parties	1			1		
	17,813	54,113	33%	13,744	57,350	24%
Fee and commission income						
Equity-accounted investees	4,751			5,772		
The Government	210			168		
Government related entities	399			399		
Key management personnel	4			4		
Other related parties	23			23		
	5,387	86,410	6%	6,366	92,368	7%

Notes to the financial statements 31 December 2019 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Group	2019 Related party balances €000	2019 Total activity/ balance €000	2019 % of total	2018 Related party balances €000	2018 Total activity/ balance €000	2018 % of total
Employee compensation and benefits						
Key management personnel	1,570	71,240	2%	1,501	65,696	2%
General administrative expenses						
Equity-accounted investees	77			74		
Key management personnel	49			44		
Other related parties	66			71		
	192	78,306	0%	189	54,596	0%
Movement in impairment allowances						
The Government	(66)			(28)		
Government related entities	33			(9,549)		
Key management personnel	3			7		
Other related parties	18			(12)		
	(12)	11,562	0%	(9,582)	(10,816)	89%
Balances with Central Bank of Malta, treasury bills and cash						
The Government	3,571,453	3,669,580	97%	3,340,301	3,400,588	98%
Financial assets at fair value through profit or loss						
The Government	20,081	205,139	10%	21,989	206,206	11%
Investments						
The Government	517,602	3,071,160	17%	483,626	3,314,955	15%
Loans and advances to customers (net)						
Equity-accounted investeess	-			-		
The Government	31,986			53,494		
Government related entities	424,966			429,532		
Key management personnel	3,338			2,992		
Other related parties	888			1,159		
	461,178	4,445,812	10%	487,177	4,362,983	11%
Impairment allowances						
The Government	(41)			(107)		
Government related entities	(1,562)			(1,529)		
Key management personnel	(10)			(7)		
Other related parties	(21)			(3)		
	(1,634)	(108,321)	2%	(1,646)	(107,063)	2%

Notes to the financial statements 31 December 2019 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Group

	2019 Related party balances €000	2019 Total activity/ balance €000	2019 % of total	2018 Related party balances €000	2018 Total activity/ balance €000	2018 % of total
Amounts owed to customers						
Equity-accounted investees	220,877			193,624		
The Government	253,237			221,198		
Government related entities	161,019			153,534		
Key management personnel	6,203			5,716		
Other related parties	11,571			9,338		
	652,907	10,629,719	6%	583,410	10,414,908	6%
Total Assets less Liabilities						
Equity-accounted investees	(220,877)			(193,624)		
The Government	3,887,844			3,678,105		
Government related entities	262,385			274,469		
Key management personnel	(2,875)			(2,731)		
Other related parties	(10,704)			(8,182)		
	3,915,773			3,748,037		
Commitments						
Equity-accounted investees	303			301		
The Government	19,714			20,250		
Government related entities	103,802			120,388		
Key management personnel	431			339		
Other related parties	3,852			6,124		
	128,102	1,828,756	7%	147,402	1,881,392	8%

The Bank

	2019 Related party balances €000	2019 Total activity/ balance €000	2019 % of total	2018 Related party balances €000	2018 Total activity/ balance €000	2018 % of total
Interest and similar income: - on loans and advance						
The Government	1,516			1,990		
Government related entities	14,123			13,766		
Key management personnel	19			13		
Other related parties	14			26		
	15,672	169,825	9%	15,795	165,177	10%
Interest and similar income: - on debt and other fixed income instruments						
The Government	10,452	37,138	28%	10,548	48,719	22%
Interest expense						
Equity-accounted investees	1,766			575		
Subsidiaries	1			2		
The Government	14,743			12,242		
Government related entities	1,283			904		
Key management personnel	19			21		
Other related parties	-			-		
	17,812	54,113	33%	13,744	57,350	24%

Notes to the financial statements 31 December 2019 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Bank	2019 Related party balances €000	2019 Total activity/ balance €000	2019 % of total	2018 Related party balances €000	2018 Total activity/ balance €000	2018 % of total
Fee and commission income						
Equity-accounted investees	4,751			5,772		
Subsidiaries	2,087			2,120		
The Government	210			168		
Government related entities	399			399		
Key management personnel	3			3		
Other related parties	2			2		
	7,452	77,403	10%	8,464	83,346	10%
Dividend income						
Equity-accounted investees	23,428			9,699		
Subsidiaries	5,892			2,054		
	29,320	30,078	97%	11,753	12,828	92%
Employee compensation and benefits						
Key management personnel	1,390	68,593	2%	1,321	63,043	2%
General administrative expenses						
Equity-accounted investees	77			74		
Key management personnel	45			57		
Other related parties	21			25		
	143	76,842	0%	156	53,093	0%
Movement in impairment allowances						
The Government	(66)			(28)		
Government related entities	33			(9,549)		
Key management personnel	3			7		
Other related parties	-			(12)		
	(30)	11,562	0%	(9,582)	(10,816)	89%
Balances with Central Bank of Malta, treasury bills and cash						
The Government	3,571,453	3,669,580	97%	3,340,301	3,400,588	98%
Financial assets at fair value through profit or loss						
The Government	20,081	204,979	10%	21,988	205,227	11%
Investments						
The Government	517,602	3,071,160	17%	483,626	3,314,955	15%
Loans and advances to customers (net)						
The Government	31,986			53,494		
Government related entities	424,966			429,532		
Key management personnel	2,725			2,392		
Other related parties	324			328		
	460,001	4,445,812	10%	485,746	4,362,983	11%

Notes to the financial statements 31 December 2019 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Bank	2019 Related party balances €000	2019 Total activity/ balance €000	2019 % of total	2018 Related party balances €000	2018 Total activity/ balance €000	2018 % of total
Impairment allowances						
The Government	(41)			(107)		
Government related entities	(1,562)			(1,529)		
Key management personnel	(10)			(7)		
Other related parties	-			-		
	(1,613)	(108,321)	1%	(1,643)	(107,063)	2%
Other assets						
Subsidiaries	2,617	136,353	2%	1,983	95,586	2%
Amounts owed to customers						
Equity-accounted investees	220,877			193,624		
Subsidiaries	2,541			3,091		
The Government	253,237			221,198		
Government related entities	161,019			153,534		
Key management personnel	4,452			4,521		
Other related parties	3,228			2,801		
	645,354	10,632,260	6%	578,769	10,417,999	6%
Total Assets less Liabilities						
Equity-accounted investees	(220,877)			(193,624)		
Subsidiaries	76			(1,108)		
The Government	3,887,844			3,678,104		
Government related entities	262,385			274,469		
Key management personnel	(1,737)			(2,136)		
Other related parties	(2,904)			(2,473)		
	3,924,787			3,753,232		
Commitments						
Equity-accounted investees	303			301		
The Government	19,714			20,250		
Government related entities	103,802			120,388		
Key management personnel	419			306		
Other related parties	1,556			1,623		
	125,794	1,828,756	7%	142,868	1,881,392	8%

	The Group 2019 €000	The Group 2018 €000	The Bank 2019 €000	The Bank 2018 €000
All outstanding balances are secured except for the following:				
Loans and advances to customers:				
- Key management personnel	231	118	197	106
- Other related parties	190	243	-	-
	421	361	197	106
Details of guarantees received are disclosed below:				
Loans and advances to customers:				
- Amounts guaranteed by The Government	378,436	471,540	378,436	471,540

Notes to the financial statements 31 December 2019 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

Loans to and commitments on behalf of directors and other key management personnel (including connected persons):

	The Group		The Bank	
	Loans and advances	Commitments	Loans and advances	Commitments
	€000	€000	€000	€000
Directors				
At 31 December 2017	1,969	333	760	170
Additions	64	68	9	33
	2,033	401	769	203
Less reductions/repayments	(735)	(301)	(71)	(136)
At 31 December 2018	1,298	100	698	67
Additions	104	11	57	11
	1,402	111	755	78
Less reductions/repayments	(120)	(50)	(86)	(29)
At 31 December 2019	1,282	61	669	49
Other key management personnel				
At 31 December 2017	1,561	351	1,561	351
Additions	257	236	257	220
	1,818	587	1,818	571
Less reductions/repayments	(125)	(348)	(124)	(332)
At 31 December 2018	1,693	239	1,694	239
Additions	515	147	515	147
	2,208	386	2,209	386
Less reductions/repayments	(152)	(16)	(153)	(16)
At 31 December 2019	2,056	370	2,056	370

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.

Notes to the financial statements 31 December 2019 (continued)

38. SEGMENTAL INFORMATION BY CLASSES OF BUSINESS (continued)

The Group's reportable segments are shown in the table below.

Reportable segments	Operations
Personal Banking & Wealth Management	Loans and other transactions and balances with retail customers, including wealth and asset management related activities
Corporate Banking	Loans and other transactions and balances with corporate customers
Proprietary Investments	Funding and centralised risk management activities through borrowings and issues of debt securities
Liquidity Management	Investments in liquid assets such as short-term placements and corporate and government debt securities

Interest income is the main revenue generating activity for all segments. The customer-oriented segments also have income derived from fees and commissions and earnings arising on foreign exchange transactions.

	Personal Banking & Wealth Management		Corporate Banking		Proprietary Investments		Liquidity Management		Total Reportable Segments	
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
	€000	€000	€000	€000	€000	€000	€000	€000	€000	€000
Interest income	77,306	73,978	90,396	89,733	36,837	48,533	2,424	1,652	206,963	213,896
Interest expense	(5,386)	(5,305)	(5,793)	(5,987)	(6,554)	(7,363)	(36,380)	(38,695)	(54,113)	(57,350)
Fee and commission income	56,980	56,676	20,233	21,456	464	1,194	8,733	13,042	86,410	92,368
Fee and commission expense	(12,090)	(10,612)	(91)	(139)	-	-	(401)	(480)	(12,582)	(11,231)
Trading income	287	287	10,945	11,022	-	-	6,108	5,654	17,340	16,963
Gains from financial assets	-	-	-	-	4,989	2,045	-	-	4,989	2,045
Other income	-	-	-	-	757	1,075	-	-	757	1,075
Depreciation/ amortisation	(7,916)	(5,515)	(2,353)	(1,644)	(469)	(431)	(2,734)	(2,716)	(13,472)	(10,306)
Other costs	(67,754)	(57,183)	(25,846)	(18,747)	(4,865)	(4,004)	(51,081)	(40,358)	(149,546)	(120,292)
Impairment (loss)/ reversal	(1,872)	2,135	13,274	8,034	160	647	-	-	11,562	10,816
Operating profit/ (loss) before litigation provision	39,555	54,461	100,765	103,728	31,319	41,696	(73,331)	(61,901)	98,308	137,984
Litigation provision	(25,000)	(75,000)	-	-	-	-	-	-	(25,000)	(75,000)
Operating (loss)/ profit before share of results of equity-accounted investees	14,555	(20,539)	100,765	103,728	31,319	41,696	(73,331)	(61,901)	73,308	62,984
Group share of results after tax of equity-accounted investees	-	-	-	-	15,897	8,214	-	-	15,897	8,214
Group profit before taxation for the year									89,205	71,198

Notes to the financial statements 31 December 2019 (continued)

38. SEGMENTAL INFORMATION BY CLASSES OF BUSINESS (continued)

	Personal Banking & Wealth Management		Corporate Banking		Proprietary Investments		Liquidity Management		Total Reportable Segments	
	2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
	€000	€000	€000	€000	€000	€000	€000	€000	€000	€000
ASSETS	2,425,661	2,251,668	2,274,103	2,325,771	3,171,441	3,408,610	4,171,266	3,891,231	12,042,471	11,877,280
Property and equipment and Intangible assets	-	-	-	-	149,379	134,903	-	-	149,379	134,903
Additions to property and equipment and intangible assets	-	-	-	-	37,280	26,295	-	-	37,280	26,295
Carrying value of equity-accounted investees	-	-	-	-	101,479	108,510	-	-	101,479	108,510
Total Assets	2,425,661	2,251,668	2,274,103	2,325,771	3,459,579	3,678,318	4,171,266	3,891,231	12,330,609	12,146,988
LIABILITIES										
Total Liabilities	2,628,735	2,453,189	2,640,842	2,726,077	3,321,384	3,561,412	2,677,343	2,412,177	11,268,304	11,152,855

The revenue which is reported above represents revenue generated from external customers. There were no inter-segment revenue during the year (2018: nil).

The accounting policies of the reportable segments are the same as the Group's accounting policies described in note 1. Segment's operating profit represents the profit earned by each segment.

There are no material activities which are carried out outside Malta.

39. FINANCIAL RISK MANAGEMENT

39.1 Use of financial instruments

By their nature, the Group's activities are principally related to the use of financial instruments including derivatives. The Group accepts deposits from customers at both fixed and floating rates and for various periods, and seeks to earn interest margins by investing these funds in high-quality assets. The Group seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due.

The Group also seeks to increase its interest margins through lending to commercial and retail borrowers with a range of credit standings. Such exposures involve both on-balance sheet loans and advances, as well as guarantees and other commitments such as performance and other bonds and letters of credit.

The Board places trading limits on the level of exposure that can be taken in relation to both overnight and intra-day market positions. Foreign exchange and interest rate exposures are normally offset by entering into counterbalancing positions, thereby controlling the variability in the net cash amounts required to liquidate market positions.

Given that the difference between the Group and the Bank balances in respect of financial instruments, and the corresponding effect on the statement of profit or loss and other comprehensive income and reserves in respect thereof, are not material, references in this note to the Group are to be construed as references to the Bank, unless otherwise stated.

The principal areas of financial risk are detailed below:

39.2 Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss to the other party by failing to discharge an obligation.

Financial assets which could potentially expose the Group to credit risk, mainly include balances with Central Bank of Malta, treasury bills and cash, derivative financial assets, debt and other fixed income instruments, and loans and advances to banks and customers.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure

(i) Loans and advances

The purpose of credit risk management is to keep credit risk exposure to a permissible level relative to capital, to maintain the soundness of assets, and to ensure returns commensurate with risk. This leads to a loan portfolio that achieves high returns on capital and assets.

Credit risk is managed and controlled throughout the Bank on the basis of established credit processes, and within a framework of credit policy and delegated authorities based on responsibility, skill and experience.

Credit grading and monitoring systems are in place to accommodate the early identification and management of deterioration in loan quality. In addition, the credit management process is underpinned by an independent system of credit review.

Credit risk analysis is carried out on two levels: the single name; and the bank's lending portfolio review. The Bank uses a number of tools to limit its exposure to undue credit risk. These include the application of:

- High-level credit policies designed to ensure a balanced and managed approach to the identification and mitigation of credit risk;
- Lending guidelines defining the responsibilities of lending officers that seek to provide a disciplined and focused benchmark for credit decisions;
- Independent reviews of credit exposures;
- Sector caps, encompassing both industry and specific product types, to communicate the Board's risk appetite for specific types of business;
- Establishment and maintenance of large exposures and provisioning policies in accordance with regulatory reporting requirements; and
- Communication and provision of general guidance on all credit-related risk issues, including regulatory changes to promote consistent and best practice throughout the Bank.

Where possible the Bank aims to reduce and control risk concentrations. Broadly stated, concentration results when the Bank has a high level of exposure to a single or related group of borrowers, credit exposures secured by a single security, or credit exposures with common characteristics within an industry, such that adverse developments in this exposure would be damaging to the Bank.

Given the size and nature of the domestic financial sector and the local economy, the Bank is exposed to concentration risk in its credit business. The Bank has systems in place to identify material concentrations in the loan portfolio, and to ensure adherence to prudential limits set by the Board of Directors and/or the regulators to single borrowers or groups of related borrowers and other significant risk concentrations. The CEO and the Board of Directors are regularly informed on the concentration of the Bank's portfolio.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

The following industry concentrations in connection with loans and advances to banks and customers are considered significant:

	The Group	
	2019	2018
	€000	€000
Agriculture	4,428	5,338
Fishing	1,419	14,216
Mining and quarrying	427	502
Manufacturing	125,746	191,944
Electricity, gas, steam and air conditioning supply	113,561	113,219
Water supply, sewerage waste management and remediation activities	2,114	2,071
Construction	184,303	203,666
Wholesale and retail trade	349,885	354,329
Transportation and storage	130,101	158,425
Accommodation and food service activities	185,715	175,503
Information and communication	24,163	32,102
Financial and insurance activities	412,591	411,068
Real estate activities	442,523	398,023
Professional, scientific and technical activities	93,497	98,502
Administrative and support service activities	110,809	49,592
Public administration and defence, compulsory social security	10,336	35,057
Education	18,128	16,121
Human health and social work activities	48,185	48,698
Arts, entertainment and recreation	25,304	27,490
Other services activities	18,431	13,497
Households and individuals	2,391,889	2,255,793
Loans and advances to customers	4,693,555	4,605,156
Loans and advances to banks	501,686	490,644
	5,195,241	**5,095,800**

(ii) Other financial assets

The credit risk in respect of other financial assets is mitigated through limits set in the Treasury Management Policy. The Bank assigns limits on the level of credit risk undertaken in relation to any single counterparty or sovereign exposure in accordance with external ratings based on Fitch's ratings or on those of other major rating agencies.

Changes in credit ratings are monitored on a daily basis and are subject to frequent review, when considered necessary. The limits on the level of credit risk are reviewed consistently and approved by the Board of Directors at regular intervals. Actual exposures are monitored against limits on an on going basis. The Bank enters into security transactions only with such authorised counterparties and it invests only in securities or paper with credit quality within specific parameters stated in the Treasury Management Policy.

The level of concentration in respect of other significant financial assets is disclosed in the remaining notes to the financial statements.

Collateral and other credit enhancements

Credit risk mitigation is one of the key elements of the Group's credit policy. This includes the requirement to obtain collateral, depending on the nature of the proposal, as set out in the Bank's policies and procedures. The nature and level of collateral required depends on a number of factors, including, but not limited to the amount of the exposure, the type of facility provided, the term of the facility, the amount of the counterparty's contribution and an evaluation of the level of the credit risk or probability of default involved (see note 39.2.1.5).

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

Settlement Risk

The Group's activity may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed. Settlement risk in respect of security transactions is mitigated through settlement limits assigned to counterparties based on external credit ratings or by effecting payment on a delivery versus payment (DVP) basis.

Sovereign Debt

Sovereign risk refers to the risk that a government may default on its obligations, and includes refinancing risk related to the inability to raise capital to repay maturing bonds. The Group monitors sovereign risks through sovereign credit ratings issued by credit rating agencies which include Fitch, Moody's, and S&P. The Treasury Management Policy seeks to mitigate sovereign risk, whether directly or indirectly through exposures to corporate and financial institutions domiciled therein, through investment limits assigned on the basis of the long-term credit rating of such sovereigns. This is further supplemented by in depth economic reviews undertaken periodically and assessments of the fiscal, economic and socio-political aspects upon which such limits are accordingly aligned.

39.2.1.1 Credit Quality

(i) Financial Assets by rating agency (Fitch) designation

The Group	Balances with CBM and Treasury Bills €000	Debt Securities €000	Loans and Advances to Banks €000	Derivatives €000	Total €000
As at 31 December 2019					
AAA	3,474,400	610,809	-	-	4,085,209
AA- to AA+	-	783,000	133,264	511	916,775
A- to A+	97,053	1,463,547	247,258	336	1,808,194
BBB- to BBB+	-	211,662	88,121	-	299,783
Lower than BBB-	-	11,395	10,503	-	21,898
Unrated	-	18	22,540	428	22,986
	3,571,453	**3,080,431**	**501,686**	**1,275**	**7,154,845**
As at 31 December 2018					
AAA	3,154,289	554,918	24,805	-	3,734,012
AA- to AA+	-	777,283	102,776	678	880,737
A- to A+	186,012	1,705,710	262,775	3,273	2,157,770
BBB- to BBB+	-	280,981	30,252	-	311,233
Lower than BBB-	-	11,464	13,966	-	25,430
Unrated	-	5,103	56,070	440	61,613
	3,340,301	**3,335,459**	**490,644**	**4,391**	**7,170,795**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.1 Credit Quality (continued)

The tables below analyse debt securities by sector, classification and residency.

Sector

	The Group		
	Amortised cost	FVOCI	FVTPL
2019	€000	€000	€000
Banks	1,060,246	-	82
Government	1,614,736	64,473	32,979
Public	-	79,538	-
Others	228,377	-	-
	2,903,359	144,011	33,061

	The Group		
	Amortised cost	FVOCI	FVTPL
2018	€000	€000	€000
Banks	1,395,572	5,073	4,460
Government	1,352,838	64,930	35,173
Public	-	72,904	-
Others	404,509	-	-
	3,152,919	142,907	39,633

Residency

	The Group		
	Amortised cost	FVOCI	FVTPL
2019	€000	€000	€000
Malta	456,383	144,011	20,081
Monetary Union member states	1,194,403	-	12,898
Rest of the world	1,252,573	-	82
	2,903,359	144,011	33,061

	The Group		
	Amortised cost	FVOCI	FVTPL
2018	€000	€000	€000
Malta	421,947	137,834	21,989
Monetary Union member states	1,205,379	-	13,184
Rest of the world	1,525,593	5,073	4,460
	3,152,919	142,907	39,633

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.1 Credit Quality (continued)

(ii) Loans and advances to customers analysed into performing and non-performing exposures

	The Group		The Group	
Total Gross/Forborne Exposures	**Total**	**of which Forborne**	**Total**	**of which Forborne**
	2019	**2019**	**2018**	**2018**
	€000	**€000**	**€000**	**€000**
Performing				
Stage 1	4,127,997	-	4,063,331	-
Stage 2	347,610	22,280	298,277	16,263
	4,475,607	22,280	4,361,608	16,263
Non-performing				
Stage 3	217,948	92,680	243,548	101,761
Total Gross/Forborne Exposures	4,693,555	114,960	4,605,156	118,024

Gross Forborne Exposures are analysed as follows:

	Modification in Terms	**Refinancing**	**Modification in Terms**	**Refinancing**
	2019	**2019**	**2018**	**2018**
Performing	**€000**	**€000**	**€000**	**€000**
Personal	3,397	1,085	2,898	181
Business	16,001	1,797	10,877	2,307
	19,398	2,882	13,775	2,488
Non-performing				
Personal	15,259	2,205	20,371	242
Business	73,009	2,207	77,049	4,099
	88,268	4,412	97,420	4,341

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2 Expected credit loss measurement (continued)

The movement in forebearance activity during the period is as follows:

	Loans & Advances	
	2019	**2018**
	€000	**€000**
1 January	118,024	167,870
Additions	17,695	21,763
Retired from forborne	(20,759)	(71,609)
31 December	114,960	118,024

(iii) Analysis of past due balances

Past due up to 29 days	100,077	104,598
Past due 30 - 59 days	24,782	21,681
Past due 60 - 89 days	7,340	2,824
	132,199	129,103

Analysis of past due balances comprise all loan exposures (including forborne exposures).

A financial asset is past due when a counterparty has failed to make a payment when contractually due.

Defaulted gross loans by segment:

Business	170,111	193,524
Personal	47,837	50,024
	217,948	**243,548**

Defaulted facilities are those credit facilities with payments of interest and/or capital overdue by 90 days or more or where the Group has reasons to doubt the eventual recoverability of funds. A variety of types of collateral are accepted including property, securities, cash, guarantees and insurance, as disclosed in note 39.2.1.5.

Information about impairment allowances is disclosed in note 39.2.1.2 in respect of the Group's exposures as at 31 December 2019 and 31 December 2018.

39.2.1.2 Expected credit loss 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. Refer to note 39.2.1.2.1 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. Refer to note 39.2.1.2.2 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 and 3 have their ECL measured based on expected losses on a lifetime bases. Refer to note 39.2.1.2.4 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 39.2.1.2.5 includes an explanation of how the Group has incorporated this in its ECL models.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2.1 Significant increase in credit risk (continued)

Further explanation is also provided of how the Group determines appropriate groupings when ECL is measured on a collective basis (refer to note 39.2.1.2.8).

The following diagram summarises the impairment requirements under IFRS 9 (other than purchased or originated credit-impaired financial assets):

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 losses	Lifetime expected credit losses	Lifetime expected credit losses

39.2.1.2.1 Significant increase in credit risk

With the exception of instruments measured at FVTPL, exposures with low credit risk at the reporting date and any originated credit-impaired financial assets (note 39.2.1.2.2), the Group assesses whether financial instruments have experienced a significant increase in credit risk since initial recognition.

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and expert credit assessment and including forward-looking information.

In the case of the Group's advances portfolio, the objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure (adjusted where relevant for changes in prepayment expectations).

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. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 2 and 3.

Stage	Internal rating
1	1 - 3
2	4 - 5
3	6 - 11

Each exposure is allocated to a credit risk grade at initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. The monitoring typically involves use of the following data.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2.1 Significant increase in credit risk (continued)

Commercial exposures	Personal exposures	All exposures
• Information obtained during periodic review of customer files - e.g. audited financial statements, management accounts, budgets and projections. Examples of areas of particular focus are: gross profit margins, financial leverage ratios, debt service coverage, compliance with covenants, quality of management, senior management changes • Actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities	• Internally collected data on customer behaviour -e.g. utilisation of credit card facilities • Affordability metrics	• Payment record - this includes overdue status as well as a range of variables about payment ratios • Utilisation of the granted limit • Requests for and granting of forbearance • Existing and forecast changes in business • Financial and economic conditions

The Group applies the low credit risk simplification for all investments which are of an investment grade, which comprises the vast majority of its treasury portfolio. The Group accordingly only assesses SICR for investments in those debt securities which are rated as sub-investment grade. For sub-investment grade securities, the Group considers a security to have experienced a significant increase in credit risk if the security has been the subject to a credit rating downgrade since initial recognition.

39.2.1.2.2 Definition of default and credit impaired

The Group considers financial assets in the advances portfolio 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); or
- the borrower is past due more than 90 days on any material credit obligation to the Group.

Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit lower than the current amount outstanding.

In assessing whether a borrower is in default, the Group considers indicators that are:

- qualitative – e.g. breaches of covenant;
- quantitative – e.g. overdue status and non-payment on 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.

The definition of default aligns with that applied by the Group for regulatory capital purposes.

At each reporting date, the Group assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI 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. In addition, a retail loan that is overdue for 90 days or more is considered impaired.

In the case of the treasury portfolio, the Group considers investments in debt instruments to be in default when a payment, including a coupon payment, is missed.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2.3 Cure rate

An instrument in the Group's advances portfolio is considered to be no longer 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.

A foreborne instrument is considered to no longer be in default when it no longer meets any of the criiteria for a consecutive period of twelve months.

The Group's experience is that defaulted debt investments within the treasury portfolio do not cure given that a security's default mechanism is triggered when a security's issuer misses a coupon payment. Any new instruments which the Group receives as part of an eventual debt restructuring exercise is considered to be a new instrument altogether.

39.2.1.2.4 Measuring ECL

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:

- The PD represents the likelihood of a borrower defaulting on its financial obligation (as per "Definition of default and credit-impaired" above), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation.
- EAD is based on the amounts the Group expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For example, for a revolving overdraft, the Group includes the current drawn balance plus any further amount that is expected to be drawn up to the current contractual limit by the time of default, should it occur.
- LGD represents the Group's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counter party, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). LGD is calculated on a 12 month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and Lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described in note 39.2.1.2.5.

PD estimates are estimates at a certain date, which 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. Where it is available, market data may also be used to derive the PD for large corporate counterparties. If a counterparty or exposure migrates between rating classes, then this will lead to a change in the estimate of the associated PD. PDs are estimated considering the contractual maturities of exposures and estimated prepayment rates.

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. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount drawn, as well as potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts. For some financial assets, EAD is determined by modelling the range of possible exposure outcomes at various points in time using scenario and statistical techniques.

The Group estimates LGD parameters on its advances portfolio based on the history of recovery rates of claims 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. For loans secured by retail property, LTV ratios are a key parameter in determining LGD. In the case of the Group's treasury portfolio, the Group lacks historical experience of defaults, and accordingly makes use of the LGD parameters set out by the Bank for International Settlements.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2.4 Measuring ECL (continued)

As described above, and subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Group measures ECL 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.

However, for retail overdrafts and credit card facilities that include both a loan and an undrawn commitment component, the Group measures ECL 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 managed on a collective basis. The Group can cancel them with immediate effect but this contractual right is not enforced in the normal day-to-day management, but only when the Group becomes aware of an increase in credit risk at the facility level. This longer period is estimated taking into account the credit risk management actions that the Group expects to take and that serve to mitigate ECL. These include a reduction in limits, cancellation of the facility and/or turning the outstanding balance into a loan with fixed repayment terms.

39.2.1.2.5 Forward-looking information

The assessment of SICR and the calculation of ECL both incorporate forward-looking information. The Group has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio.

These economic variables and their associated impact on the PD, EAD and LGD vary by financial instrument. Forecasts of these economic variables (the "base economic scenario") are calculated using statistical models and forecasts are obtained for all maturities to which the Bank has exposure. Macro factors that are found to be statistically significant for all portfolios are forecasted using a vector autoregressive model (VAR). On an annual basis, as part of the model recalibration exercise an assessment is carried out to ensure that these economic variables are still statistically significant.

The impact of these economic variables on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent 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.

39.2.1.2.6 Critical estimates

The most significant key macroeconomic variables used for the ECL estimate as at 31 December 2019 are set out below. The scenarios "base", "upside" and "downside" were used for all loan portfolios.

Macro economic forecasts (2020-2024)	Downside	Base	Upside
	%	%	%
GDP Growth rate	1.4	4.7	8.1
Housing index	-6.9	3.6	15.3
Inflation rate	2.6	1.8	1.0
Interest rate	1.2	-0.1	0.0
Money supply	26.1	15.0	5.0
Trade ratio	-191.6	64.3	315.6
Unemployment rate	5.1	2.6	1.1
Probability (%)	25.0	50.0	25.0

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political changes, have also been considered, but are not deemed to have a material impact. This is reviewed and monitored for appropriateness on a quarterly basis.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2.7 Sensitivity of ECL to future economic conditions

ECL is sensitive to judgements and assumptions made regarding formulation of forward-looking scenarios and how such scenarios are incorporated into the calculations. A sensitivity analysis is performed on ECL recognised on the credit portfolio, assuming the upside and downside foward-looking scenarios are weighted at 100% instead of applying an unbiased set of probability weights.

Applying a baseline scenario would approximate the probability weighted scenario.

	2019
	€000
Gross performing exposures	4,475,606
ECL variance	
- Upside	(10,262)
- Downside	12,208

The Group performed additional ECL runs to sensitise expected credit loss allowances to changes in the impact of macrovariable inputs and their impact on projected PD curves.

The most significant changes in ECL resulting from shifts in macro variable inputs are inflation and unemployment. Both variables result in significant impact on the purchasing power and hence on the borrowers' ability to meet its contractual obligations.

Set out below are the changes to ECL as at 31 December 2019 that would result from changes in parameters from the actual observations. The most significant sensitivity tests affecting the ECL allowance are as follows:

Macrovariable	Shift in basis points	Variance in ECL
		€000
Inflation rate	+150	6,925
Unemployment	+100	1,350

In a scenario of economic downturn assuming a 1% shift of exposures from Stage 1 to Stage 2 and applying the difference in Stage 2 and Stage 1 average impairment coverage ratios to the movement in gross exposure, is estimated to increase ECL by €2.4 million, mostly arising on loans and advances to customers.

39.2.1.2.8 Grouping by shared risk characteristics

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics that include:

- instrument type;
- credit risk gradings;
- collateral type;
- LTV ratio for retail mortgages;
- date of initial recognition;
- remaining term to maturity;
- industry; and
- geographic location of the borrower.

The groupings are subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.2.8 Grouping by shared risk characteristics (continued)

For portfolios in respect of which the Group has limited historical data, external benchmark information is used to supplement the internally available data. The portfolios for which external benchmark information represents a significant input into measurement of ECL are as follows.

As at December 2019	Exposure	External benchmarks used LGD
Investments in debt securities within the treasury portfolio	€ 3,047,716	8% - 55% Bank for International Settlements parameters

As at December 2018	Exposure	External benchmarks used LGD
Investments in debt securities within the treasury portfolio	€ 3,296,334	11% - 61% Bank for International Settlements parameters

39.2.1.3 Gross carrying amount and exposure to credit risk

The following table sets out information about the credit quality of financial assets measured at amortised cost, FVOCI debt investments. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

Explanation of the terms: 12-month ECL, lifetime ECL and credit-impaired are included in Note 39.2.1.1.

	Stage 1 12-month ECL	Stage 2 Lifetime ECL not credit-Impaired	Stage 3 Lifetime ECL credit-Impaired	Total
	€000	€000	€000	€000
Loans and advances to banks at amortised cost				
As at 31 December 2019				
AAA	3,474,270	-	-	3,474,270
AA- to AA+	29,935	-	-	29,935
A- to A+	215,501	-	-	215,501
BBB- to BBB+	-	-	-	-
Lower than BBB-	-	8,972	-	8,972
	3,719,706	8,972	-	3,728,678
Loss allowance	(9)	(3)	-	(12)
Carrying amount	3,719,697	8,969	-	3,728,666
Loans and advances to banks at amortised cost				
As at 31 December 2018				
AAA	3,154,289	-	-	3,154,289
AA- to AA+	32,228	-	-	32,228
A- to A+	165,710	-	-	165,710
BBB- to BBB+	490	-	-	490
Lower than BBB-	-	13,970	-	13,970
	3,352,717	13,970	-	3,366,687
Loss allowance	(3)	(3)	-	(6)
Carrying amount	3,352,714	13,967	-	3,366,681

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.3 Gross carrying amount and exposure to credit risk (continued)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL not credit-Impaired	Stage 3 Lifetime ECL credit-Impaired	Total
	€000	€000	€000	€000
Loans and advances to customers at amortised cost				
As at 31 December 2019				
Grades 1-3	3,988,575	81,474	1,155	4,071,204
Grades 4-5	-	266,136	4,103	270,239
Grades 6-11	-	-	212,690	212,690
	3,988,575	347,610	217,948	4,554,133
Loss allowance	(9,145)	(19,405)	(79,771)	(108,321)
Carrying amount	3,979,430	328,205	138,177	4,445,812
Loans and advances to customers at amortised cost				
As at 31 December 2018				
Grades 1-3	3,928,221	45,687	1,705	3,975,613
Grades 4-5	-	252,591	3,188	255,779
Grades 6-11	-	-	238,654	238,654
	3,928,221	298,278	243,547	4,470,046
Loss allowance	(9,210)	(18,345)	(79,508)	(107,063)
Carrying amount	3,919,011	279,933	164,039	4,362,983

Facilities under probation result in an ECL stage which is worse from the stage related with their internal grading.

	Stage 1 12-month ECL	Stage 2 Lifetime ECL not credit-Impaired	Stage 3 Lifetime ECL credit- Impaired	Total
	€000	€000	€000	€000
Investments in debt securities				
As at 31 December 2019				
AAA	610,817	-	-	610,817
AA- to AA+	783,009	-	-	783,009
A- to A+	1,435,322	3,101	-	1,438,423
BBB- to BBB+	204,020	-	-	204,020
Lower than BBB-	-	11,447	-	11,447
Unrated	-	-	-	-
	3,033,168	14,548	-	3,047,716
Loss allowance	(289)	(57)	-	(346)
Carrying amount	3,032,879	14,491	-	3,047,370

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.3 Gross carrying amount and exposure to credit risk (continued)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL not credit-Impaired	Stage 3 Lifetime ECL credit- Impaired	Total
	€000	€000	€000	€000
Investments in debt securities				
As at 31 December 2018				
AAA	554,918	-	-	554,918
AA- to AA+	772,914	-	-	772,914
A- to A+	1,675,570	3,116	-	1,678,686
BBB- to BBB+	273,283	-	-	273,283
Lower than BBB-	-	11,464	-	11,464
Unrated	-	5,069	-	5,069
	3,276,685	19,649	-	3,296,334
Loss allowance	(382)	(126)	-	(508)
Carrying amount	3,276,303	19,523	-	3,295,826

39.2.1.4 Maximum exposure to credit risk on FVTPL securities, financial guarantees and loan commitments

Maximum exposure
The carrying amount of financial assets recorded in the financial statements, which is net of impairment losses, represents the maximum exposure to credit risk without taking account of the value of any collateral obtained, except as disclosed below:

Financial guarantees
The maximum exposure to credit risk is the full amount that the Group would have to pay if the guarantees are called upon (note 33).

Loan commitments
The maximum exposure to credit risk arising on loan commitments and other credit related commitments that are irrecoverable over the life of the respective facilities is the full amount of the committed facilities (note 34).

The following table contains an analysis of the maximum credit risk exposure from financial assets not subject to impairment (i.e. FVTPL):

	Maximum exposure to credit risk	
	2019	2018
	€000	€000
Financial assets mandatorily measured at FVTPL:		
- Debt securities	7,723	7,778
	7,723	**7,778**
Financial assets designated at fair value:		
- Debt securities	25,338	31,855
- Loans and advances to customers	139,422	135,110
	164,760	**166,965**
	172,483	**174,743**
Derivatives financial instruments	1,275	4,391

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.5 Collateral

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. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities; and
- Margin agreement for derivatives, for which the Group has master netting agreements imposed by way of law.

Longer-term finance and lending to corporate entities are generally secured; revolving individual 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, treasury and other eligible bills are generally unsecured, with the exception of asset-backed securities and similar instruments, which are secured by portfolios of financial instruments. Derivatives are also collateralised.

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.

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 €581.2 million as at 31 December 2019.

Security values are reviewed on a regular basis and are also re-assessed at time of default if it is found that the carrying value of the collateral item could have materially changed since last valuation. The Bank calculates the value of collateral as the market value less a haircut, with the latter representing a conservative estimate of the costs to sell and the potential loss of value in a forced sale scenario. For financial instruments, haircuts are calculated according to the risk profile of each individual security and depend on a number of variables including price volatility and liquidity/marketability of the instrument.

The table below shows the financial effect and main types of collateral held against the Group's customer loan exposures:

The Group

As at 31 December 2019	Loans and advances to customers	Undrawn credit facilities and other commitments to lend
	€000	€000
Loans collateralised by:		
Prime bank guarantees	83	31
Cash or quasi cash	108,289	40,807
Guarantees and/or letters of comfort issued by the Malta Government, the Central Bank of Malta or Public agencies	381,946	143,929
Residential property	2,111,861	795,823
Commercial property	1,099,471	414,319
Personal guarantees and others	243,269	91,672
	3,944,919	**1,486,581**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.5 Collateral (continued)

The Group

As at 31 December 2018	**Loans and advances to customers**	**Undrawn credit facilities and other commitments to lend**
	€000	**€000**
Loans collateralised by:		
Prime bank guarantees	1,004	392
Cash or quasi cash	109,593	42,754
Guarantees and/or letters of comfort issued by the Malta Government, the Central Bank of Malta or Public agencies	471,762	184,041
Residential property	1,946,718	759,447
Commercial property	1,118,414	436,312
Personal guarantees and others	220,272	85,932
	3,867,763	**1,508,878**

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

As at 31 December 2019	**Gross carrying amount**	**Impairment allowance**	**Net carrying amount**	**Fair value of collateral held post haircut**
	€000	**€000**	**€000**	**€000**
Credit-impaired assets				
Loans to individuals:				
- Personal Loans	4,956	(2,885)	2,071	2,882
- Home Loans	40,665	(8,871)	31,794	30,438
- Personal Overdrafts	942	(534)	408	680
- Credit Cards	1,361	(1,269)	92	-
Loans to corporate entities:				
- Business Loans	115,922	(44,520)	71,402	78,658
- Business Overdrafts	52,578	(20,420)	32,158	44,176
- Encroachments	1,524	(1,272)	252	-
Total credit-impaired assets	217,948	(79,771)	138,177	156,834

The Group

As at 31 December 2018	**Gross carrying amount**	**Impairment allowance**	**Net carrying amount**	**Fair value of collateral held post haircut**
	€000	**€000**	**€000**	**€000**
Credit-impaired assets				
Loans to individuals:				
- Personal Loans	4,570	(2,645)	1,925	2,064
- Home Loans	43,740	(7,796)	35,944	34,726
- Personal Overdrafts	999	(531)	468	963
- Credit Cards	715	(712)	3	-
Loans to corporate entities:				
- Business Loans	128,690	(45,693)	82,997	99,408
- Business Overdrafts	63,674	(20,980)	42,694	54,595
- Encroachments	1,159	(1,151)	8	-
Total credit-impaired assets	243,547	(79,508)	164,039	191,756

Fair value of collateral refers to architect's valuation less applicable haircuts.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

39.2.1.5 Collateral (continued)

Lending covered by Residential Property

The table below stratifies credit exposures, covered by residential property, to customers by ranges of loan-to-value ('LTV'). LTV is calculated as the ratio of the gross amount of loan or the amount committed for loan commitments to the value of the collateral. The gross amounts exclude any impairment allowances. The valuation of the collateral excludes any adjustments for obtaining and selling the collateral. The value of the collateral for these loans is based on the collateral value at origination updated based on changes in house price indices.

Lending and commitments covered by residential lending	**2019**	**2018**
	€000	**€000**
Less than 25%	151,964	146,309
25% to 50%	477,560	456,424
51% to 75%	905,468	856,469
76% to 90%	1,018,472	918,239
	2,553,464	2,377,441

The following table shows the distribution of LTV ratios for the Group's mortgage credit-impaired portfolio

Mortgage portfolio - LTV distribution	**Credit Impaired (Gross carrying amount)**	**Credit Impaired (Gross carrying amount)**
	2019	**2018**
	€000	**€000**
Lower than 25%	1,580	3,230
25% to 50%	8,399	9,013
51% to 75%	24,886	11,833
76% to 90%	2,432	20,866
Total	37,297	44,942

39.2.2 The expected credit loss provision and write-offs of exposures

39.2.2.1 Reconciliation of ECL

The following tables explain the changes in the loss allowance between the beginning and the end of the annual period due to the following factors:

- Transfers between Stage 1 and Stages 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. Changes in the staging allocation of balances existing at 1 January 2019 (and associated ECL changes) are presented in "transfers to/(from)", whereas subsequent changes in the staging allocation of new assets originated during the year are presented in "new financial assets originated";
- Additional allowances 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 measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period (see note 39.2.2.4)

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.1 Reconciliation of ECL (continued)

Allowances on On-Balance Sheet Exposures	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL €000	Total €000
Total allowances at 1 January 2019	**9,210**	**18,345**	**79,508**	**107,063**
Home Loans				
Allowances at 1 January 2019	1,458	1,158	7,796	**10,412**
Transfer to/(from):				
Stage 1	(9)	428	455	**874**
Stage 2	2	(109)	93	**(14)**
Stage 3	-	117	(546)	**(429)**
New financial assets originated*	840	427	4	**1,271**
Financial assets that have been derecognised	(165)	(156)	(490)	**(811)**
Write-offs	-	-	(47)	**(47)**
Changes to model assumptions and methodologies	(260)	(12)	-	**(272)**
Other movements	(93)	(29)	1,606	**1,484**
Allowances on home loans at 31 December 2019	1,773	1,824	8,871	**12,468**
Personal				
Allowances at 1 January 2019	835	451	3,175	**4,461**
Transfer to/(from):				
Stage 1	(7)	85	165	**243**
Stage 2	1	(42)	45	**4**
Stage 3	-	9	(69)	**(60)**
New financial assets originated*	325	79	408	**812**
Financial assets that have been derecognised	(101)	(117)	(180)	**(398)**
Write-offs	-	-	(191)	**(191)**
Changes to model assumptions and methodologies	(133)	(15)	-	**(148)**
Other movements	(24)	1	66	**43**
Allowances on personal at 31 December 2019	896	451	3,419	**4,766**
Credit Cards				
Allowances at 1 January 2019	1,676	1,106	721	**3,503**
Transfer to/(from):				
Stage 1	(155)	466	242	**553**
Stage 2	117	(364)	350	**103**
Stage 3	1	11	(85)	**(73)**
New financial assets originated*	73	20	13	**106**
Financial assets that have been derecognised	(62)	(57)	(101)	**(220)**
Write-offs	-	-	-	**-**
Changes to model assumptions and methodologies	(275)	(132)	-	**(407)**
Other movements	304	106	128	**538**
Allowances on credit cards at 31 December 2019	1,679	1,156	1,268	**4,103**
Business				
Allowances at 1 January 2019	5,241	15,630	67,816	**88,687**
Transfer to/(from):				
Stage 1	(532)	2,215	1,162	**2,845**
Stage 2	41	(1,733)	1,930	**238**
Stage 3	2	431	(3,485)	**(3,052)**
New financial assets originated*	937	3,222	5,276	**9,435**
Financial assets that have been derecognised	(283)	(1,516)	(7,670)	**(9,469)**
Write-offs	-	-	(747)	**(747)**
Changes to model assumptions and methodologies	(676)	(584)		**(1,260)**
Other movements	67	(1,691)	1,931	**307**
Allowances on business at 31 December 2019	4,797	15,974	66,213	**86,984**
Total allowances at 31 December 2019	**9,145**	**19,405**	**79,771**	**108,321**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.1 Reconciliation of ECL (continued)

	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL €000	Total €000
Total Allowances at 1 January 2018	**11,252**	**26,813**	**115,556**	**149,621**
Home Loans				
Allowances at 1 January 2018	2,149	1,682	8,627	**12,458**
Transfer to/(from):				
Stage 1	(8)	176	600	**768**
Stage 2	5	(488)	231	**(252)**
Stage 3	1	60	(137)	**(76)**
New financial assets originated*	404	174	229	**807**
Financial assets that have been derecognised	(242)	(208)	(237)	**(687)**
Write-offs	-	-	(797)	**(797)**
Changes to model assumptions and methodologies	(608)	(155)	(2)	**(765)**
Other movements	(243)	(83)	(718)	**(1,044)**
Allowances on home loans at 31 December 2018	1,458	1,158	7,796	**10,412**
Personal				
Allowances at 1 January 2018	1,084	757	2,432	**4,273**
Transfer to/(from):				
Stage 1	(8)	127	586	**705**
Stage 2	2	(77)	99	**24**
Stage 3	-	20	(71)	**(51)**
New financial assets originated*	344	77	520	**941**
Financial assets that have been derecognised	(160)	(36)	(296)	**(492)**
Write-offs	-	-	(14)	**(14)**
Changes to model assumptions and methodologies	(198)	(42)	-	**(240)**
Other movements	(229)	(375)	(81)	**(685)**
Allowances on personal at 31 December 2018	835	451	3,175	**4,461**
Credit Cards				
Allowances at 1 January 2018	1,785	2,815	812	**5,412**
Transfer to/(from):				
Stage 1	(153)	394	87	**328**
Stage 2	112	(567)	125	**(330)**
Stage 3	3	17	(140)	**(120)**
New financial assets originated*	89	24	4	**117**
Financial assets that have been derecognised	(59)	(110)	(165)	**(334)**
Write-offs	-	-	-	**-**
Changes to model assumptions and methodologies	(477)	(143)	(2)	**(622)**
Other movements	376	(1,324)	-	**(948)**
Allowances on credit cards at 31 December 2018	1,676	1,106	721	**3,503**
Business				
Allowances at 1 January 2018	6,234	21,559	99,685	**127,478**
Transfer to/(from):				
Stage 1	(273)	1,449	5,097	**6,273**
Stage 2	50	(6,848)	2,386	**(4,412)**
Stage 3	6	228	(1,588)	**(1,354)**
New financial assets originated*	2,909	5,828	883	**9,620**
Financial assets that have been derecognised	(779)	(4,894)	(7,498)	**(13,171)**
Write-offs	-	-	(33,356)	**(33,356)**
Changes to model assumptions and methodologies	(991)	(643)	(851)	**(2,485)**
Other movements	(1,915)	(1,049)	3,058	**94**
Allowances on business at 31 December 2018	5,241	15,630	67,816	**88,687**
Total allowances at 31 December 2018	9,210	18,345	79,508	**107,063**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.1 Reconciliation of ECL (continued)

	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL €000	Total €000
Provisions on Off-Balance Sheet Exposures				
Total Provisions at 1 January 2019	**3,918**	**4,743**	**10,106**	**18,767**
Home Loans				
Provisions at 1 January 2019	363	360	390	**1,113**
Transfer to/(from):				
Stage 1	(1)	27	67	**93**
Stage 2	-	(2)	-	**(2)**
Stage 3	-	-	(10)	**(10)**
New financial assets originated*	400	199	-	**599**
Financial assets that have been derecognised	(63)	(7)	(87)	**(157)**
Write-offs	-	-	(2)	**(2)**
Changes to model assumptions and methodologies	(71)	10	-	**(61)**
Other movements	(145)	(122)	(109)	**(376)**
Provisions on home loans at 31 December 2019	483	465	249	**1,197**
Personal				
Provisions at 1 January 2019	62	61	104	**227**
Transfer to/(from):				
Stage 1	(3)	1	7	**5**
Stage 2	-	(18)	-	**(18)**
Stage 3	-	-	(14)	**(14)**
New financial assets originated*	45	45	43	**133**
Financial assets that have been derecognised	(9)	(5)	(9)	**(23)**
Write-offs	-	-	(10)	**(10)**
Changes to model assumptions and methodologies	(9)	(1)	-	**(10)**
Other movements	(26)	(35)	(4)	**(65)**
Provisions on personal at 31 December 2019	60	48	117	**225**
Credit Cards				
Provisions at 1 January 2019	388	22	15	**425**
Transfer to/(from):				
Stage 1	(16)	14	14	**12**
Stage 2	15	(13)	10	**12**
Stage 3	1	-	(6)	**(5)**
New financial assets originated*	29	1	-	**30**
Financial assets that have been derecognised	(26)	(1)	(4)	**(31)**
Write-offs	-	-	-	**-**
Changes to model assumptions and methodologies	(72)	(5)	-	**(77)**
Other movements	121	18	15	**154**
Provisions on credit cards at 31 December 2019	440	36	44	**520**
Business				
Provisions at 1 January 2019	3,105	4,300	9,597	**17,002**
Transfer to/(from):				
Stage 1	(49)	152	207	**310**
Stage 2	3	(350)	62	**(285)**
Stage 3	3	43	(548)	**(502)**
New financial assets originated*	1,212	1,137	1,836	**4,185**
Financial assets that have been derecognised	(347)	(1,469)	(768)	**(2,584)**
Write-offs	-	-	(2)	**(2)**
Changes to model assumptions and methodologies	(349)	(116)	-	**(465)**
Other movements	(1,025)	(1,151)	(1,623)	**(3,799)**
Provisions on business at 31 December 2019	2,553	2,546	8,761	**13,860**
Total Provisions at 31 December 2019	**3,536**	**3,095**	**9,171**	**15,802**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.1 Reconciliation of ECL (continued)

	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL €000	Total €000
Total Provisions at 1 January 2018	**3,995**	**4,791**	**14,230**	**23,016**
Home Loans				
Provisions at 1 January 2018	421	259	612	**1,292**
Transfer to/(from):				
Stage 1	(2)	-	5	**3**
Stage 2	-	(17)	11	**(6)**
Stage 3	-	-	(70)	**(70)**
New financial assets originated*	35	144	-	**179**
Financial assets that have been derecognised	(73)	(33)	(215)	**(321)**
Write-offs	-	-	(36)	**(36)**
Changes to model assumptions and methodologies	(151)	(51)	(8)	**(210)**
Other movements	133	58	91	**282**
Provisions on home loans at 31 December 2018	363	360	390	**1,113**
Personal				
Provisions at 1 January 2018	60	12	167	**239**
Transfer to/(from):				
Stage 1	(2)	14	6	**18**
Stage 2	-	(1)	-	**(1)**
Stage 3	-	-	(11)	**(11)**
New financial assets originated*	50	47	21	**118**
Financial assets that have been derecognised	(17)	(1)	(69)	**(87)**
Write-offs	-	-	-	**-**
Changes to model assumptions and methodologies	(15)	(7)	(2)	**(24)**
Other movements	(14)	(3)	(8)	**(25)**
Provisions on personal at 31 December 2018	62	61	104	**227**
Credit Cards				
Provisions at 1 January 2018	390	29	14	**433**
Transfer to/(from):				
Stage 1	(15)	14	6	**5**
Stage 2	12	(17)	3	**(2)**
Stage 3	1	-	(4)	**(3)**
New financial assets originated*	28	1	-	**29**
Financial assets that have been derecognised	(21)	(4)	(4)	**(29)**
Write-offs	-	-	-	**-**
Changes to model assumptions and methodologies	(115)	(6)	-	**(121)**
Other movements	108	5	-	**113**
Provisions on credit cards at 31 December 2018	388	22	15	**425**
Business				
Provisions at 1 January 2018	3,124	4,491	13,437	**21,052**
Transfer to/(from):				
Stage 1	(23)	16	482	**475**
Stage 2	11	(834)	15	**(808)**
Stage 3	-	-	(31)	**(31)**
New financial assets originated*	1,665	5,736	-	**7,401**
Financial assets that have been derecognised	(770)	(600)	(816)	**(2,186)**
Write-offs	-	-	(17)	**(17)**
Changes to model assumptions and methodologies	(660)	(362)	(420)	**(1,442)**
Other movements	(242)	(4,147)	(3,053)	**(7,442)**
Provisions on business at 31 December 2018	3,105	4,300	9,597	**17,002**
Total Provisions at 31 December 2018	**3,918**	**4,743**	**10,106**	**18,767**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.2 Contributors to changes in provision

Significant changes in the gross carrying amount of financial assets that contributed to changes in the loss allowance were as follows:

- Gross loans and advances increased by 2% during the year (2018: 3%). The high volume of new loans originated during the period, aligned with the Group's organic growth objective, increased the gross carrying amount of the loan book by 15% (2018: 15%), with a corresponding €10.8 million increase in loss allowance (2018: €11.5 million).
- There were no significant changes to the modification of facility contracts following renegotiation with customers facing financial difficulties.
- The write-off of loans with a total gross carrying amount of €2.5 million (2018: €46.9 million) resulted in the reduction of the Stage 3 expected credit losses by €1.0 million (2018: €34.2 million).

The following tables further explains changes in the gross carrying amount of the loan portfolio to help explain their significance to the changes in the loss allowance for the same portfolio as discussed above:

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€000	€000	€000	€000
Total Gross Carrying Amount at 1 January 2019	**4,063,331**	**298,278**	**243,547**	**4,605,156**
Home Loans				
Gross carrying amount as at 1 January 2019	1,964,414	38,043	43,739	**2,046,196**
Transfer to/(from):				
Stage 1	(12,997)	11,236	1,631	**(130)**
Stage 2	3,337	(4,198)	883	**22**
Stage 3	274	1,182	(1,577)	**(121)**
New financial assets originated*	367,436	2,252	-	**369,688**
Financial assets that have been derecognised	(146,075)	(2,928)	(3,965)	**(152,968)**
Write-offs	-	-	(46)	**(46)**
Other changes in carrying amount	(86,420)	(1,862)	-	**(88,282)**
Home loans gross carrying amount as at 31 December 2019	**2,089,969**	**43,725**	**40,665**	**2,174,359**
Personal				
Gross carrying amount as at 1 January 2019	147,946	5,554	5,562	**159,062**
Transfer to/(from):				
Stage 1	(1,492)	990	295	**(207)**
Stage 2	125	(314)	109	**(80)**
Stage 3	73	200	(301)	**(28)**
New financial assets originated*	46,924	605	1,012	**48,541**
Financial assets that have been derecognised	(20,333)	(643)	(655)	**(21,631)**
Write-offs	-	-	(12)	**(12)**
Other changes in carrying amount	(14,688)	(348)	(112)	**(15,148)**
Personal gross carrying amount as at 31 December 2019	**158,555**	**6,044**	**5,898**	**170,497**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.2 Contributors to changes in provision (continued)

	Stage 1 12-month ECL €000	Stage 2 Lifetime ECL €000	Stage 3 Lifetime ECL €000	Total €000
Credit cards				
Gross carrying amount as at 1 January 2019	43,553	8,806	721	**53,080**
Transfer to/(from):				
Stage 1	(4,569)	5,136	352	**919**
Stage 2	3,211	(4,444)	463	**(770)**
Stage 3	41	94	(160)	**(25)**
New financial assets originated*	1,616	224	17	**1,857**
Financial assets that have been derecognised	(1,612)	(519)	(110)	**(2,241)**
Write-offs	-	-	-	**-**
Other changes in carrying amount	1,282	525	78	**1,885**
Credit cards gross carrying amount as at 31 December 2019	**43,522**	**9,822**	**1,361**	**54,705**
Business				
Gross carrying amount as at 1 January 2019	1,907,418	245,875	193,525	**2,346,818**
Transfer to/(from):				
Stage 1	(71,812)	64,096	6,218	**(1,498)**
Stage 2	29,062	(38,301)	5,624	**(3,615)**
Stage 3	262	9,322	(13,118)	**(3,534)**
New financial assets originated*	183,821	50,777	16,843	**251,441**
Financial assets that have been derecognised	(242,422)	(23,944)	(17,301)	**(283,667)**
Write-offs	-	-	(2,397)	**(2,397)**
Other changes in carrying amount	29,622	(19,806)	(19,370)	**(9,554)**
Business gross carrying amount as at 31 December 2019	**1,835,951**	**288,019**	**170,024**	**2,293,994**
Total Gross carrying amount as at 31 December 2019	**4,127,997**	**347,610**	**217,948**	**4,693,555**
Less Allowances	(9,145)	(19,405)	(79,771)	(108,321)
Net Loans and Advances to customers	**4,118,852**	**328,205**	**138,177**	**4,585,234**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.2 Contributors to changes in provision (continued)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€000	€000	€000	€000
Total Gross Carrying Amount at 1 January 2018	**3,940,225**	**249,576**	**281,004**	**4,470,805**
Home Loans				
Gross carrying amount as at 1 January 2018	1,834,094	42,461	45,622	**1,922,177**
Transfer to/(from):				
Stage 1	(10,644)	7,281	3,349	**(14)**
Stage 2	7,820	(9,788)	1,573	**(395)**
Stage 3	376	1,828	(2,177)	**27**
New financial assets originated*	366,156	2,906	1,411	**370,473**
Financial assets that have been derecognised	(159,387)	(5,195)	(3,639)	**(168,221)**
Write-offs	-	-	(2,330)	**(2,330)**
Other changes in carrying amount	(74,001)	(1,450)	(70)	**(75,521)**
Home loans gross carrying amount as at 31 December 2018	**1,964,414**	**38,043**	**43,739**	**2,046,196**
Personal				
Gross carrying amount as at 1 January 2018	150,304	6,947	4,673	**161,924**
Transfer to/(from):				
Stage 1	(1,541)	829	718	**6**
Stage 2	758	(1,234)	242	**(234)**
Stage 3	20	68	(127)	**(39)**
New financial assets originated*	50,029	1,310	769	**52,108**
Financial assets that have been derecognised	(27,230)	(899)	(490)	**(28,619)**
Write-offs	-	-	(830)	**(830)**
Other changes in carrying amount	(24,394)	(1,467)	607	**(25,254)**
Personal gross carrying amount as at 31 December 2018	**147,946**	**5,554**	**5,562**	**159,062**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.2 Contributors to changes in provision (continued)

	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€000	€000	€000	€000
Credit cards				
Gross carrying amount as at 1 January 2018	42,579	8,264	787	**51,630**
Transfer to/(from):				
Stage 1	(4,035)	4,697	133	**795**
Stage 2	3,356	(4,073)	173	**(544)**
Stage 3	82	109	(215)	**(24)**
New financial assets originated*	2,110	273	4	**2,387**
Financial assets that have been derecognised	(1,478)	(513)	(186)	**(2,177)**
Write-offs	-	-	-	**-**
Other changes in carrying amount	939	49	25	**1,013**
Credit cards gross carrying amount as at 31 December 2018	43,553	8,806	721	**53,080**
Business				
Gross carrying amount as at 1 January 2018	1,913,248	191,905	229,921	**2,335,074**
Transfer to/(from):				
Stage 1	(65,771)	55,556	9,020	**(1,195)**
Stage 2	15,969	(25,771)	7,004	**(2,798)**
Stage 3	1,187	2,938	(6,897)	**(2,772)**
New financial assets originated*	213,880	49,019	2,917	**265,816**
Financial assets that have been derecognised	(138,131)	(49,196)	(19,993)	**(207,320)**
Write-offs	-	-	(43,708)	**(43,708)**
Other changes in carrying amount	(32,964)	21,424	15,261	**3,721**
Business gross carrying amount as at 31 December 2018	1,907,418	245,875	193,525	**2,346,818**
Total Gross carrying amount as at 31 December 2018	4,063,331	298,278	243,547	4,605,156
Less Allowances	(9,210)	(18,345)	(79,508)	(107,063)
Net Loans and Advances to customers	**4,054,121**	**279,933**	**164,039**	**4,498,093**

Gross carrying amount comprises of loans and advances to customers at amortised cost and loans and advances to customers designated as fair value through profit or loss.

*- Originated loans during the period include €15.8 million of originated credit impaired assets which relate to new facilities granted to counterparties in default as part of existing commitments
- Assets that have been originated to counterparties in stage two that are still subject to the Bank's cure/probation criteria

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.3 Impairment Allowances on Total/Forborne Exposures

	The Group		The Group	
	Total	of which Forborne	Total	of which Forborne
	2019	2019	2018	2018
	€000	€000	€000	€000
Performing				
Stage 1	9,145	-	9,210	-
Stage 2	19,405	1,962	18,345	1,816
	28,550	1,962	27,555	1,816
Non-performing				
Stage 3	79,771	34,963	79,508	33,330
Total Impairment Allowances	108,321	36,925	107,063	35,146

The movement in allowance accounts for loans and advances to customers are as follows:

	The Group	
	Allowances	Allowances
	2019	2018
	€000	€000
Change in allowances for uncollectability:		
At 1 January	107,063	166,200
Impact on adoption of IFRS 9	-	(16,579)
Additions	44,356	37,616
Reversals	(43,098)	(80,174)
At 31 December	108,321	107,063

Interest income recognised during the year ended 31 December 2019 in respect of forborne assets amounted to €6.3 million (2018: €6.5 million).

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 The expected credit loss provision and write-offs of exposures (continued)

39.2.2.4 Write-off policy

Loans and debt securities are written off in full when there is no realistic prospect of recovery. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts. However, financial assets that are written off could be subject to enforcement activities on order to comply with the Group's procedures for recovery of amounts due.

39.2.2.5 Contractual amounts outstanding on assets that were written off

The contractual amount outstanding on financial assets that were written off during the year ended 31 December 2019 and that are still subject to enforcement activity is €2.5 million (2018: €46.9 million).

39.2.3 Modification of financial assets' terms

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 in accordance with the accounting policy set out in Note 1.4.2.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting data based on the modified terms; with
- the remaining lifetime PD estimated based on data at initial recognition and the original contractual terms.

For financial assets modified as part of the Group's policy, the estimate of PD reflects 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 evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired (see Note 39.2.1.1.2). A customer needs to demonstrate consistently good payment behaviour over a period of 12 months before the exposure is no longer considered to be credit-impaired in default or a period of 3 months before the exposure's PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to 12-month ECL.

During the current financial year there were no significant modification of financial assets.

39.2.4 Equity instruments designated as at FVOCI

The fair value of equity instruments designated at FVOCI and the dividend income recognised is detailed below.

	Fair value	Dividend income recognised	Fair value	Dividend income recognised
	2019	2019	2018	2018
	€000	€000	€000	€000
Local Other	22,073	515	17,411	240
Local Banks	130	3	166	11
Local Public	1,587	62	1,552	62
	23,790	580	19,129	313

During financial year ending 2018 a number of equity instruments were sold in line with the Bank's risk appetite strategy. The fair value of these equity instruments upon disposal was €12.3 million. Transfers of cumulative gains within equity amounted to €1.9 million.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from an inability to sell a financial asset quickly at close to its fair value. The Group monitors and manages this risk by maintaining sufficient cash and, where possible, financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs. The Group is exposed to daily calls on its available cash resources from overnight deposits, current and call deposits, maturing term deposits, loan drawdowns, guarantees and from margin and other calls on cash-settled derivatives. In order to ensure that maturing funds are always available to meet expected demand for cash, the Board sets parameters within which maturities of assets and liabilities may be mismatched. Unmatched positions potentially enhance profitability, but also increase the risk of losses. In addition, the Group manages its risk to a shortage of funds by monitoring forecast and actual cashflows, by monitoring the availability of raising funds to meet commitments associated with financial instruments and by holding financial assets which are expected to generate cash inflows that will be available to meet cash outflows on liabilities.

The table below analyses Group financial liabilities into relevant maturity groupings, based on the remaining period at the reporting date to the contractual maturity date. The balances in this table will not agree directly to the balances in the statement of financial position as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments. Furthermore, loan commitments do not meet the criteria for recognition in the statement of financial position.

Financial liabilities at fair value through profit or loss and derivatives designated for hedge accounting, disclosed below, represent amounts for which net cash flows are exchanged.

The Group	**Due within 3 months**	**Due between 3 & 12 months**	**Due between 1 & 5 years**	**Due after 5 years**	**Gross nominal outflow**	**Carrying amount**
At 31 December 2019	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Financial liabilities at fair value through profit or loss	633	2,841	9,823	5,565	18,862	10,907
Amounts owed to banks	66,209	-	-	-	66,209	66,047
Amounts owed to customers	9,331,012	869,378	447,024	4,574	10,651,988	10,629,719
Debt securities in issue	-	-	-	-	-	-
Subordinated liabilities	73,633	3,828	22,623	197,275	297,359	234,230
Derivatives designated for hedge accounting	288	1,666	8,934	3,997	14,885	13,963
Other financial liabilities	180,889	102,099	13,751	15,817	312,556	313,438
	9,652,664	**979,812**	**502,155**	**227,228**	**11,361,859**	**11,268,304**
Loan commitments	1,768,695					
At 31 December 2018						
Financial liabilities at fair value through profit or loss	1,394	2,704	7,073	2,413	13,584	8,812
Amounts owed to banks	146,560	8	-	-	146,568	146,021
Amounts owed to customers	9,096,232	924,826	404,546	3,857	10,429,461	10,414,908
Debt securities in issue	-	1,700	40,850	-	42,550	40,197
Subordinated liabilities	3,633	54,970	87,303	138,931	284,837	234,241
Derivatives designated for hedge accounting	433	1,086	5,162	5,162	11,843	10,206
Other financial liabilities	190,748	76,202	9,397	13,784	290,131	298,470
	9,439,000	**1,061,496**	**554,331**	**164,147**	**11,218,974**	**11,152,855**
Loan commitments	1,796,548					

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

Assets available to meet these liabilities, and to cover outstanding commitments, include balances with Central Bank of Malta, treasury bills and cash, cheques in course of collection, loans to banks and to customers and marketable securities and undrawn credit lines.

The table below analyses the assets and liabilities that are recognised in the statement of financial position into relevant maturity groupings, based on the remaining period at the reporting date to their contractual maturity date.

The Group	Less than 3 months	Between 3 months and 1 year	Between 1 and 5 years	More than 5 years	Other	Carrying amount
	€000	€000	€000	€000	€000	€000
At 31 December 2019						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,539,435	32,018	-	-	98,127	**3,669,580**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	-	23,118	9,845	98	-	**33,061**
- Equity and other non-fixed income instruments	-	-	-	-	31,381	**31,381**
- Loans and advances	-	385	7,048	131,989	-	**139,422**
- Derivative financial instruments	1,252	23	-	-	-	**1,275**
Investments						
- Debt and other fixed income financial instruments						
- FVOCI	-	5,712	44,003	94,296	-	**144,011**
- Amortised cost	202,294	478,460	1,466,196	756,409	-	**2,903,359**
- Equity and other non-fixed income instruments						
- FVOCI	-	-	-	-	23,790	**23,790**
Loans and advances to banks	501,686	-	-	-	-	**501,686**
Loans and advances to customers	504,181	25,375	344,431	3,571,825	-	**4,445,812**
Investments in equity-accounted investees	-	-	-	-	101,479	**101,479**
Other assets	-	-	-	-	335,753	**335,753**
	4,748,848	**565,091**	**1,871,523**	**4,554,617**	**590,530**	**12,330,609**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	3,045	154	1,274	6,434	-	**10,907**
Amounts owed to banks	66,047	-	-	-	-	**66,047**
Amounts owed to customers	9,328,539	860,065	436,806	4,309	-	**10,629,719**
Debt securities in issue	-	-	-	-	-	**-**
Other liabilities	-	-	-	-	313,438	**313,438**
Derivatives held for hedging accounting	180	-	-	13,783	-	**13,963**
Subordinated liabilities	70,993	-	-	163,237	-	**234,230**
Equity holders of the Bank	-	-	-	-	1,062,305	**1,062,305**
	9,468,804	**860,219**	**438,080**	**187,763**	**1,375,743**	**12,330,609**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Group	Less than 3 months	Between 3 months and 1 year	Between 1 and 5 years	More than 5 years	Other	Carrying amount
	€000	€000	€000	€000	€000	€000
At 31 December 2018						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,230,310	10,210	-	-	160,068	**3,400,588**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	4,383	1,067	34,092	91	-	**39,633**
- Equity and other non-fixed income instruments	-	-	-	-	27,072	**27,072**
- Loans and advances	-	-	-	135,110	-	**135,110**
- Derivative financial instruments	4,186	60	145	-	-	**4,391**
Investments						
- Debt and other fixed income financial instruments						
- FVOCI	-	5,073	51,243	86,591	-	**142,907**
- Amortised cost	211,526	614,046	1,898,086	429,261	-	**3,152,919**
- Equity and other non-fixed income instruments						
- FVOCI	-	-	-	-	19,129	**19,129**
Loans and advances to banks	474,430	-	-	-	16,214	**490,644**
Loans and advances to customers	510,465	36,694	153,070	3,662,754	-	**4,362,983**
Investments in equity-accounted investees	-	-	-	-	108,510	**108,510**
Other assets	-	-	-	-	263,102	**263,102**
	4,435,300	**667,150**	**2,136,636**	**4,313,807**	**594,095**	**12,146,988**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	2,161	109	2,765	3,777	-	**8,812**
Amounts owed to banks	110,008	36,013	-	-	-	**146,021**
Amounts owed to customers	9,100,245	915,990	395,050	3,623	-	**10,414,908**
Debt securities in issue	-	40,197	-	-	-	**40,197**
Other liabilities	-	-	-	-	298,470	**298,470**
Derivatives held for hedging accounting	-	-	368	9,838	-	**10,206**
Subordinated liabilities	-	50,118	70,993	113,130	-	**234,241**
Equity holders of the Bank	-	-	-	-	994,133	**994,133**
	9,212,414	**1,042,427**	**469,176**	**130,368**	**1,292,603**	**12,146,988**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Bank

At 31 December 2019	Less than 3 months €000	Between 3 months and 1 year €000	Between 1 and 5 years €000	More than 5 years €000	Other €000	Carrying Amount €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,539,435	32,018	-	-	98,127	**3,669,580**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	-	23,118	9,845	98	-	**33,061**
- Equity and other non-fixed income instruments	-	-	-	-	31,221	**31,221**
- Loans and advances	-	385	7,048	131,989	-	**139,422**
- Derivative financial instruments	1,252	23	-	-	-	**1,275**
Investments						
- Debt and other fixed income financial instruments						
- FVOCI	-	5,712	44,003	94,296	-	**144,011**
- Amortised cost	202,294	478,460	1,466,196	756,409	-	**2,903,359**
- Equity and other non-fixed income instruments						
- FVOCI	-	-	-	-	23,790	**23,790**
Loans and advances to banks	501,686	-	-	-	-	**501,686**
Loans and advances to customers	504,181	25,375	344,431	3,571,825	-	**4,445,812**
Investments in equity-accounted investees and subsidiaries	-	-	-	-	59,100	**59,100**
Other assets	-	-	-	-	332,970	**332,970**
	4,748,848	**565,091**	**1,871,523**	**4,554,617**	**545,208**	**12,285,287**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	3,045	154	1,274	6,434	-	**10,907**
Amounts owed to banks	66,047	-	-	-	-	**66,047**
Amounts owed to customers	9,331,080	860,065	436,806	4,309	-	**10,632,260**
Debt securities in issue	-	-	-	-	-	**-**
Other liabilities	-	-	-	-	312,726	**312,726**
Derivatives designated for hedge accounting	180	-	-	13,783	-	**13,963**
Subordinated liabilities	70,993	-	-	163,237	-	**234,230**
Equity holders of the Bank	-	-	-	-	1,015,154	**1,015,154**
	9,471,345	**860,219**	**438,080**	**187,763**	**1,327,880**	**12,285,287**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Bank

At 31 December 2018	Less than 3 months €000	Between 3 months and 1 year €000	Between 1 and 5 years €000	More than 5 years €000	Other €000	Carrying Amount €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,230,310	10,210	-	-	160,068	**3,400,588**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	4,383	1,067	34,092	91	-	**39,633**
- Equity and other non-fixed income instruments	-	-	-	-	26,093	**26,093**
- Loans and advances	-	-	-	135,110	-	**135,110**
- Derivative financial instruments	4,186	60	145	-	-	**4,391**
Investments						
- Debt and other fixed income financial instruments						
- FVOCI	-	5,073	51,243	86,591	-	**142,907**
- Amortised cost	211,526	614,046	1,898,087	429,260	-	**3,152,919**
- Equity and other non-fixed income instruments						
- FVOCI	-	-	-	-	19,129	**19,129**
Loans and advances to banks	474,430	-	-	-	16,214	**490,644**
Loans and advances to customers	510,465	36,694	153,070	3,662,754	-	**4,362,983**
Investments in equity-accounted investees and subsidiaries	-	-	-	-	59,100	**59,100**
Other assets	-	-	-	-	260,942	**260,942**
	4,435,300	**667,150**	**2,136,637**	**4,313,806**	**541,546**	**12,094,439**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	2,161	109	2,765	3,777	-	**8,812**
Amounts owed to banks	110,008	36,013	-	-	-	**146,021**
Amounts owed to customers	9,103,336	915,990	395,050	3,623	-	**10,417,999**
Debt securities in issue	-	40,197	-	-	-	**40,197**
Other liabilities	-	-	-	-	297,714	**297,714**
Derivatives designated for hedge accounting	-	-	368	9,838	-	**10,206**
Subordinated liabilities	-	50,118	70,993	113,130	-	**234,241**
Equity holders of the Bank	-	-	-	-	939,249	**939,249**
	9,215,505	**1,042,427**	**469,176**	**130,368**	**1,236,963**	**12,094,439**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

Banking Rule 07 transposing the provisions of the EBA Guidelines on Disclosures of Encumbered and Unencumbered Assets (EBA/GL/2014/03) requires disclosure on asset encumbrance. The Group is in compliance with the contents thereof.

This disclosure provides details of available and unrestricted assets that could be used to support potential future funding and collateral needs. An asset is considered as encumbered when it has been pledged as collateral against an existing liability, and as a result is no longer available to the Group to secure funding, satisfy collateral needs or be sold to reduce the funding requirement.

This disclosure is limited to assets available for central bank refinancing and securities that are transferable and is not designed to identify assets which would be available to meet the claims of creditors or to predict assets that would be available to creditors in the event of a resolution or bankruptcy.

Asset Encumbrance

	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
	€000	€000	€000	€000
The Group				
As at 31 December 2019				
Equity instruments	-	-	55,171	55,171
Debt securities	448,038	460,967	2,729,446	2,761,712
Loans and advances	7,517	-	8,553,802	-
Other assets	-	-	536,635	-
	455,555	**460,967**	**11,875,054**	**2,816,883**
The Group				
As at 31 December 2018				
Equity instruments	-	-	46,201	46,201
Debt securities	485,349	493,951	2,850,110	2,951,820
Loans and advances	-	-	8,242,807	-
Other assets	-	-	522,521	-
	485,349	**493,951**	**11,661,639**	**2,998,021**
The Bank				
As at 31 December 2019				
Equity instruments	-	-	55,011	55,011
Debt securities	448,038	460,967	2,729,446	2,761,712
Loans and advances	7,517	-	8,553,802	-
Other assets	-	-	491,473	-
	455,555	**460,967**	**11,829,732**	**2,816,723**
The Bank				
As at 31 December 2018				
Equity instruments	-	-	45,222	45,222
Debt securities	485,349	493,951	2,850,110	2,951,820
Loans and advances	-	-	8,242,807	-
Other assets	-	-	470,951	-
	485,349	**493,951**	**11,609,090**	**2,997,042**

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

Asset Encumbrance (continued)

The Group does not encumber any of the collateral received or any of its debt securities issued.

For the financial years ended 31 December 2019 and 31 December 2018, the Bank has an outstanding liability with regards to significant claims associated with encumbered assets.

The Group and the Bank undertake the following:
(i) Pledging of debt securities against the provision of credit lines by the Central Bank of Malta;
(ii) Pledging of debt securities in favour of the Depositor Compensation Scheme.
(iii) Pledging of assets in favour of the Italian bank Intesa San Paolo against the precautionary warrant of seizure in respect of Deilumar Trust. This amount does not necessarily reflect BOV's potential financial exposure.

39.4 Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: interest rate risk, currency risk and other price risk. It arises in all areas of the Group's activities and is managed by a variety of different techniques as detailed below.

The objective of the Group is to manage and control market risk exposures in order to optimise return on risk while maintaining a market profile consistent with the Bank's status as a leading Bank in providing financial products and services.

The market risk appetite is articulated in the Treasury Management Policy. It is defined as the quantum and composition of market risk that the Bank is currently exposed to and the direction in which the Bank desires to manage this risk. Market risk is managed through limits set in the Treasury Management Policy. The Policy is reviewed by Treasury department in co-ordination with Risk Management department and is approved by the Asset and Liability Management Committee (ALCO) and the Board of Directors.

39.4.1 Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument would fluctuate because of changes in market interest rates.

The Group is exposed to fair value interest rate risk arising from financial assets and liabilities with fixed interest rates and to cash flow interest rate risk arising from financial assets and liabilities with floating interest rates. The Group is not directly exposed to interest rate risk on investment in equity instruments. The Group uses interest rate swaps to hedge the interest rate risk of certain financial instruments.

The analysis of interest rate risk has evolved from assessing the sensitivity of the treasury portfolio, using a modified duration method, to a more comprehensive methodology. The latter approach covers all interest sensitive assets and liabilities, as well as off-balance sheet items; this effectively widens the analysis and enables the stressing of various movements in the yield curve. The tables below depict the movement of stressed yield curves and the changes in the Report Equity and Net Interest Income to such movement. For further information related to the measurement of interest rate risk can be found in the Capital & Risk Management Report section 7.2.1.

	Basis points	Direction
Parallel Shock Up	200	Up
Parallel Shock Down	200	Down
Short Rates Up	250	Up
Short Rates Down	250	Down
Steepener	250	Short Rates Down
	100	Long Rates Up
Flattener	250	Short Rates Up
	100	Long Rates Down

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.4 Market risk (continued)

39.4.1 Interest rate risk (continued)

	Parallel Shock Up	Parallel Shock Down	Short Rates up	Short Rates Down	Steepener	Flattener
	€ millions	€ millions	€ millions	€ millions	€ millions	€ millions
Sensitivity of reported equity to interest rate movements						
2019						
At 31 December	22	23	37	-	(36)	33
Average for the period	50	2	42	(9)	(27)	28
Maximum for the period	83	23	54	-	(13)	35
Minimum for the period	22	(11)	37	(17)	(36)	14
2018						
At 31 December	26	5	11	(13)	(14)	1
Average for the period	26	20	30	10	-	25
Maximum for the period	56	40	57	34	28	52
Minimum for the period	(1)	-	11	(13)	(14)	1

	Parallel Shock Up	Parallel Shock Down
	€ millions	€ millions
Sensitivity of projected net interest income to interest rate movements		
2019		
At 31 December	(29)	(63)
Average for the period	(17)	(64)
Maximum for the period	(4)	(63)
Minimum for the period	(29)	(66)
2018		
At 31 December	6	(60)
Average for the period	3	(79)
Maximum for the period	9	(60)
Minimum for the period	(3)	(98)

Interest rate benchmark reform

A fundamental reform of major interest rate benchmarks is being undertaken globally to replace or reform IBOR with alternative nearly risk-free rates (referred to as 'IBOR reform'). The Group does not have significant exposure to interbank offered rates ('IBOR') on its financial instruments that will be replaced or reformed as part of this market-wide initiative. In any case, there is significant uncertainty over the timing and the methods of transition. The Group does not anticipate that the IBOR reform will have significant operational, risk management and accounting impacts across its business lines.

The Bank has entrusted its Treasury function to manage its transition to alternative rates. Its objective include evaluating the extent to which loans granted and the Group's financial liabilities are based on IBOR cash flows, whether such contracts need to be amended as a result of IBOR reform and how to manage communication about IBOR reform with counterparties.

The majority of the Bank's loan portfolio is priced against the Bank's base rate and only very few loans are floating rate loans. Presently, no fallback provisions have been contracted for when IBOR ceases to exist.

The Bank has no floating-rate financial liabilities. All deposit products are linked to fixed rates of interest that do not depend on IBOR.

With respect to derivative instruments, the Bank holds such positions for risk management purposes only. The interest rate derivatives instruments all have receive-floating legs that are IBOR indexed and are entered into as economic fair value hedges. The Bank did not designate any derivatives as hedging instruments in cash flow hedges.

The calculation methodology of Euribor changed during 2019. In July 2019, the Belgian Financial Services and Markets Authority granted authorization with respect to Euribor under the European Union Benchmark Regulation. This allows market participants to continue to use Euribor after 1 January 2020 for both existing and new contracts. The Bank expects that Euribor will continue to exist as a benchmark rate for the foreseeable future and does not anticipate changing the hedged risk to a different benchmark. For these reasons, the Bank does not consider its fair value hedges of the Euribor benchmark interest rate to be directly affected by interest rate benchmark reform at 31 December 2019.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.4 Market risk (continued)

39.4.1 Interest rate risk (continued)

(iv) Interest rate repricing gap

The table below summarises the Group's exposure to interest rate risk. Included in the table are Group assets and liabilities, including derivative financial instruments which are principally used to reduce exposure to interest rate risk, categorised by repricing date.

The Group's assets and liabilities are set to reprice as follows:

	Up to 1 Month €000	3 months or less but over 1 month €000	1 year or less but over 3 months €000	Over 1 year €000	Others €000	Total €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,474,400	65,035	32,018	-	98,127	**3,669,580**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	-	-	23,118	9,845	98	**33,061**
- Equity and other non-fixed income instruments	-	-	-	-	31,381	**31,381**
- Loans and advances	139,422	-	-	-	-	**139,422**
- Derivative financial instruments	-	-	-	-	1,275	**1,275**
Investments						
- FVOCI	-	-	5,712	138,299	-	**144,011**
- Amortised cost	356,479	673,211	287,506	1,586,163	-	**2,903,359**
- Equity and other non-fixed income instruments - FVOCI	-	-	-	-	23,790	**23,790**
Loans and advances to banks	148,213	9,000	-	-	344,473	**501,686**
Loans and advances to customers	3,610,198	-	-	835,614	-	**4,445,812**
Investments in equity-accounted investees	-	-	-	-	101,479	**101,479**
Other assets	-	-	-	-	335,753	**335,753**
Total 2019	**7,728,712**	**747,246**	**348,354**	**2,569,921**	**936,376**	**12,330,609**
Total 2018	8,190,966	1,165,655	289,756	1,741,973	758,638	12,146,988
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	1,198	2,403	4,431	-	2,875	**10,907**
Amounts owed to banks	18,807	8,903	-	-	38,337	**66,047**
Amounts owed to customers	9,112,716	210,292	850,757	419,019	36,935	**10,629,719**
Other liabilities	-	-	-	-	313,438	**313,438**
Derivatives designated for hedge accounting	-	180	13,783	-	-	**13,963**
Subordinated liabilities	-	71,013	-	163,217	-	**234,230**
Equity holders of the Bank	-	-	-	-	1,062,305	**1,062,305**
Total 2019	**9,132,721**	**292,791**	**868,971**	**582,236**	**1,453,890**	**12,330,609**
Total 2018	6,084,138	300,630	1,008,320	562,874	4,191,026	12,146,988
Interest rate swaps - 2019	**29,786**	**62,874**	**90,723**	**(183,383)**	-	
Interest rate swaps - 2018	47,084	56,445	94,564	(198,093)	-	
Gap - 2019	**(1,374,223)**	**517,329**	**(429,894)**	**1,804,303**	**-**	
Gap - 2018	2,153,912	921,470	(624,000)	981,005	-	
Cumulative Gap - 2019	**(1,374,223)**	**(856,894)**	**(1,286,788)**	**517,515**	**-**	
Cumulative Gap - 2018	2,153,912	3,075,382	2,451,382	3,432,387	-	

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.4 Market risk (continued)

39.4.2 Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Board of Directors sets limits on the level of exposure by currency and in total, which levels are monitored daily.

The following table summarises the Group's exposure to foreign currency exchange rate risk at the reporting date. Included in the table are the Group's assets and liabilities at carrying amounts, analysed into relevant currency groupings.

The Group 31 December 2019	EUR €000	USD €000	GBP €000	AUD €000	Other Currencies €000	Total €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,666,110	1,065	1,770	74	561	**3,669,580**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	32,999	50	12	-	-	**33,061**
- Equity and other non-fixed income instruments	21,431	9,950	-	-	-	**31,381**
- Loans and advances	139,422	-	-	-	-	**139,422**
- Derivative financial instruments	751	374	150	-	-	**1,275**
Investments						
- FVOCI	64,473	79,539	-	-	-	**144,012**
- Amortised cost	2,300,934	302,034	142,152	145,299	12,939	**2,903,358**
- Equity and other non-fixed income instruments						
- measured at FVOCI	23,790	-	-	-	-	**23,790**
Loans and advances to banks	194,550	121,361	82,556	7,188	96,031	**501,686**
Loans and advances to customers	4,401,082	26,329	17,415	-	986	**4,445,812**
Other assets	437,706	(733)	250	-	9	**437,232**
	11,283,248	**539,969**	**244,305**	**152,561**	**110,526**	**12,330,609**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	10,266	214	362	23	42	**10,907**
Amounts owed to banks	31,496	29,572	2,994	115	1,870	**66,047**
Amounts owed to customers	9,725,248	508,160	238,921	53,802	103,588	**10,629,719**
Other liabilities	194,814	(2,733)	1,880	166	1,202	**195,329**
Provision	118,109	-	-	-	-	**118,109**
Derivatives designated for hedge accounting	181	13,782	-	-	-	**13,963**
Subordinated liabilities	234,230	-	-	-	-	**234,230**
Equity	1,060,993	27,186	14	-	(25,888)	**1,062,305**
	11,375,337	**576,181**	**244,171**	**54,106**	**80,814**	**12,330,609**

	USD	GBP	AUD	Other Currencies
Net on balance sheet financial position	(36,212)	134	98,455	29,712
Notional amount of derivative instruments	7,562	(1,336)	(99,003)	(3,473)
Net open position	(28,650)	(1,202)	(548)	26,239

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.4 Market risk (continued)

39.4.2 Currency risk (continued)

The Group 31 December 2018	EUR €000	USD €000	GBP €000	AUD €000	Other Currencies €000	Total €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	3,396,334	1,489	1,986	86	693	**3,400,588**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	35,191	4,193	44	203	2	**39,633**
- Equity and other non-fixed income instruments	19,585	7,090	397	-	-	**27,072**
- Loans and advances	135,110	-	-	-	-	**135,110**
- Derivative financial instruments	3,200	868	174	-	149	**4,391**
Investments						
- Debt and other fixed income financial instruments						
- FVOCI	70,003	72,904	-	-	-	**142,907**
- Amortised cost	2,230,724	490,031	212,223	179,123	40,818	**3,152,919**
- Equity and other non-fixed income instruments						
- FVOCI	19,129	-	-	-	-	**19,129**
Loans and advances to banks	146,529	122,756	101,996	14,427	104,936	**490,644**
Loans and advances to customers	4,317,432	29,763	14,838	-	950	**4,362,983**
Other assets	372,236	(750)	104	-	22	**371,612**
	10,745,473	**728,344**	**331,762**	**193,839**	**147,570**	**12,146,988**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	7,288	1,320	153	-	51	**8,812**
Amounts owed to banks	43,721	59,008	9,509	27,696	6,087	**146,021**
Amounts owed to customers	9,251,190	668,990	296,182	58,493	140,053	**10,414,908**
Debt securities in issue	40,197	-	-	-	-	**40,197**
Other liabilities	195,879	(924)	(1,175)	266	8,657	**202,703**
Provision	95,767	-	-	-	-	**95,767**
Derivatives designated for hedge accounting	368	9,838	-	-	-	**10,206**
Subordinated liabilities	234,241	-	-	-	-	**234,241**
Equity	988,989	31,352	(84)	(39)	(26,085)	**994,133**
	10,857,640	**769,584**	**304,585**	**86,416**	**128,763**	**12,146,988**
Net on balance sheet financial position		(41,240)	27,177	107,423	(76,960)	
Notional amount of derivative instruments		10,035	(29,585)	(108,070)	6,766	
Net open position		(31,205)	(2,408)	(647)	(70,194)	

39.4.3 Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

The Group is exposed to equity price risks arising from the holding of equity instruments classified either as FVOCI or at fair value through profit or loss.

The carrying amounts of financial instruments at the reporting date which could potentially subject the Group to equity price risk are disclosed in the notes to the financial statements.

This risk is monitored and managed by the Risk management function of the Bank, as disclosed in more detail above.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.5 Transferred financial assets that are not derecognised in their entirety

	The Group and the Bank	
	2019	2018
	€000	€000
Debt securities classified as		
- amortised cost	27,707	52,135
Amounts owed to banks	27,707	52,135

These transactions are covered by the TBMA/ISMA Global Repurchase Master Agreement ("the Agreement") and involve the sale of financial assets with a simultaneous agreement to repurchase them at a pre-determined price at a future date. The securities sold comprise investment securities. The counterparty's liability is included in amounts owed to banks. The Group and the Bank continue to recognise the transferred assets since all the risks and rewards of the assets will be substantially retained in a manner that does not result in the transferred assets being derecognised for accounting purposes.

Each party to a transaction is subject to the events of default listed in the Agreement. In the event that any of the events of default is/are triggered, transactions are immediately terminated. Consequently, performance of the respective obligations of the parties with respect to the delivery of securities, the payment of the repurchase prices for any equivalent securities and the repayment of any cash margin shall become due and payable.

39.6 Fair value of financial instruments

The Group's accounting policy for determining the fair value of financial instruments is described in notes 1.3, 1.20 and 1.25 to these Financial Statements.

For financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly. This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3 inputs are unobservable inputs for the asset or liability. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instruments' valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis, the Group and the Bank determine when transfers are deemed to have occurred between Levels in the hierarchy at the end of each reporting period.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.6 Fair value of financial instruments (continued)

Bases of valuing financial assets and liabilities measured at fair value

	Fair value measurement			
	Level 1 €000	Level 2 €000	Level 3 €000	Total €000
The Group				
At 31 December 2019				
Assets				
Financial assets at fair value through profit or loss				
- debt and other fixed income instruments	33,061	-	-	33,061
- equity and other non-fixed income instruments	4,487	10,758	16,136	31,381
- loans and advances	-	139,422	-	139,422
- derivative financial instruments	-	1,275	-	1,275
Investments				
Debt and other fixed income instruments				
- FVOCI	64,472	79,539	-	144,011
Equity and other non-fixed income instruments				
- FVOCI	15,306	8,484	-	23,790
	117,326	**239,478**	**16,136**	**372,940**
Liabilities				
Financial liabilities at fair value through profit or loss	-	10,907	-	10,907
Derivatives designated for hedge accounting	-	13,963	-	13,963
	-	**24,870**	**-**	**24,870**
The Group				
At 31 December 2018				
Assets				
Financial assets at fair value through profit or loss				
- debt and other fixed income instruments	35,264	4,369	-	39,633
- equity and other non-fixed income instruments	5,056	12,042	9,974	27,072
- loans and advances	-	135,110	-	135,110
- derivative financial instruments	-	4,391	-	4,391
Investments				
Debt and other fixed income instruments				
- FVOCI	70,003	72,904	-	142,907
Equity and other non-fixed income instruments				
- FVOCI	9,982	9,147	-	19,129
	120,305	**237,963**	**9,974**	**368,242**
Liabilities				
Financial liabilities at fair value through profit or loss	-	8,812	-	8,812
Derivatives designated for hedge accounting	-	10,206	-	10,206
	-	**19,018**	**-**	**19,018**

During the period under review there were no transfers in levels in financial assets at fair value through profit or loss (2018: Level 2 to Level 3 €0.4 million). No change in levels was made in financial assets classified as investments in both financial years.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.6 Fair value of financial instruments (continued)

Control Framework

Fair values are subject to a control framework designed to ensure that they are either determined or validated by a function independent of the risk taker and that they are appropriately performed and reviewed by competent personnel. To this end, the determination of fair values is a process which is performed by Financial Markets and Investments and reviewed by Finance. Finance establishes the accounting policies and, in conjunction with Financial Markets and Investments, it establishes the procedures governing valuation, and is responsible for ensuring that they comply with all relevant accounting standards. The valuation techniques and procedures applied are subject to a process of due diligence, which process was duly approved by the Board and the Audit Committee and documented accordingly.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to valuation techniques, independent price determination or validation is utilised, to the extent practicable. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Bank sources alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable. The factors which are mainly considered are the following:

- the extent to which prices may be expected to represent genuine traded or tradable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the end of the reporting period; and
- the manner in which the data was sourced.

In determining the fair values for financial instruments measured at fair value the credit risk adjustment for the counterparty, the Bank or both, as the case may be, is deemed to be immaterial and hence no adjustment to the fair value of financial instruments at fair value through profit or loss was effected.

The Group calculates the credit risk adjustment by applying the probability of default of the counterparty to the expected positive exposure to the counterparty, and multiplying the result by the loss expected in the event of default. The calculation is performed over the life of the potential exposure.

Financial instruments at fair value through profit or loss and financial assets which are held for investment purposes as FVOCI are carried at their fair value.

Financial instruments not measured at fair value:

(i) Investments - Debt and other fixed income instruments held to collect
This category of asset is carried at amortised cost. Their fair value is disclosed separately in the respective note to the financial statements.

(ii) Loans and advances to customers
Loans and advances to customers are the largest financial asset held by the Group, and are reported net of allowances to reflect the estimated recoverable amounts. The carrying amount of loans and advances to customers is a reasonable approximation of fair value because these are re-priced to take into account changes in both benchmark rate and credit spreads. Their fair value measurement is a Level 2 input.

(iii) Loans and advances to banks, balances with Central Bank and Treasury Bills
The majority of these assets reprice or mature in less than 1 year. Hence their fair value is not deemed to differ materially from their carrying amount at the respective reporting dates.

(iv) Amounts owed to banks and customers
These liabilities are carried at amortised cost. The majority of these liabilities reprice or mature in less than 1 year. Hence their fair value is not deemed to differ materially from their carrying amount at the respective reporting dates. Their fair value measurement is a Level 2 input.

(v) Debt securities in issue and subordinated liabilities
These liabilities are carried at amortised cost. Their fair value is disclosed separately in the respective notes to the financial statements.

(vi) Other financial liabilities
The fair value of other financial liabilities is not deemed to differ materially from their carrying amount at the respective reporting dates.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.6 Fair value of financial instruments (continued)

Bases of valuing financial assets and liabilities not measured at fair value

The following table provides an analysis of financial instruments that are not measured at fair value subsequent to initial recognition:

	Fair value measurement Level 1 €000	Level 2 €000	Level 3 €000	Total €000	Carrying Amount €000
2019					
Financial assets					
Investments					
Debt and other fixed income instruments					
- Amortised	2,426,519	522,029	-	2,948,548	2,903,359
Financial liabilities					
Subordinated liabilities	231,452	-	-	231,452	234,230
	231,452	-	-	231,452	234,230

	Fair value measurement Level 1 €000	Level 2 €000	Level 3 €000	Total €000	Carrying Amount €000
2018					
Financial assets					
Debt and other fixed income instruments					
- Amortised	2,660,111	516,377	-	3,176,488	3,152,919
Financial liabilities					
Debt securities in issue	40,200	-	-	40,200	40,197
Subordinated liabilities	232,131	-	-	232,131	234,241
	272,331	-	-	272,331	274,438

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

	2019 FVTPL	2019 FVOCI	2018 FVTPL	2018 FVOCI
	Equity and other non-fixed income instruments €000	Equity and other non-fixed income instruments €000	Equity and other non-fixed income instruments €000	Equity and other non-fixed income instruments €000
Opening balance	9,974	-	5,117	5,298
- in profit or loss	6,097	-	1,191	-
Purchases	333	-	-	-
Transfers	-	-	5,695	(5,298)
Sales	(268)	-	(2,029)	-
Closing balance	16,136	-	9,974	-

The instruments classified within Level 3 comprise an externally managed fund and a global payments technology company. The Bank has determined that the reported net asset value of the fund represents its fair value at the end of the reporting period. Meanwhile, the shares held in the technology company are valued using the intrinsic value of the conversion shares less a discount for liquidity and litigation risk. The fair value of these equities was determined using statements or other information provided by the managers. The Bank considers that such valuations may rely significantly on the judgments and estimates made by the managers and given the level of subjectivity involved, these are included within Level 3.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.7 Capital risk management

The Group's capital management approach ensures a sufficient level of capitalisation to manage the risk exposures whilst supporting business growth and providing adequate returns to the shareholders. Risk capital management does not in any way substitute risk mitigation measures. It is vital that the structure of limits and thresholds should be able to prevent concentrations of risk from building up in such a way as to compromise a significant proportion of the Group's capital resources.

On 1 January 2014 the Capital Requirements Directive (CRD) and the Capital Requirements Regulations (CRR) came into effect, constituting the European implementation of the Basel capital and liquidity agreement of 2010. The Group has made the necessary changes in order to ensure that it is compliant with the Pillar I capital requirements set by the CRR. Other material risks are also allocated capital as part of the Internal Capital Adequacy Process (ICAAP) embedded in the Pillar II process. This process helps to measure with greater risk sensitivity the amount of regulatory capital which the Group requires to cover risks assumed in the course of its business, including risks not covered in Pillar I. The Board submitted the latest ICAAP capital document to the JST in April 2018.

Capital management is under the direct control of the Asset and Liability Committee (ALCO). During the financial period, ALCO has monitored the adequacy of the Group's capital and gave strategic direction on the most efficient use of capital.

During the period under review and during the comparative period, there were no reported breaches in respect of the externally imposed capital requirements. The Group uses the Standardised Approach for credit risk, the Basic Indicator Approach for operational risk and the Base Method with respect to the Group's foreign exchange risk in line with CRR requirements.

The following table shows the components and basis of calculation of the Group's and the Bank's own funds.

	The Group **€000**	**The Bank** **€000**
Own funds		
Tier 1		
- Paid up capital instruments	583,849	583,849
- Share premium	49,277	49,277
- Retained earnings*	310,401	311,971
- Accumulated other comprehensive income	14,705	14,593
- Other reserves	40,193	40,193
- Funds for general banking risk	5,271	5,271
- Deductions:		
Prudential Valuation fair valued assets and liabilities	(596)	(554)
Other intangible assets	(60,463)	(60,463)
Depositor Compensation Scheme Reserve	(43,250)	(43,250)
Total Tier 1 Capital	899,387	900,887

**Retained earnings include current period profit which is subject to regulatory approval.*

Tier 2		
- Capital instruments and subordinated loans	164,472	164,472
Total Tier 2 Capital	164,472	164,472
Total Own Funds	1,063,859	1,065,359

Further information on the Group's and the Bank's capital adequacy ratios may be found in section 3.2 in the Capital and Risk Management report, which are subject to internal verification as set out in paragraph 1.1 of that report.

Notes to the financial statements 31 December 2019 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.8 Offsetting financial assets and financial liabilities

The derivative financial assets with a positive carrying amount and the derivative financial liabilities with a negative carrying amount do not meet the offsetting criteria in IAS 32 and hence they are presented separately in the Statement of Financial Position. These instruments are subject to the ISDA Master Agreement. The ISDA Master Agreement provides, amongst others, for the netting of termination values for purposes of determining a single lump-sum termination amount upon the insolvency of a counterparty. By virtue of the Set-off and Netting on Insolvency Act, 2003 (Chapter 459, Laws of Malta), the close-out netting provisions contained in the ISDA Master Agreement are valid and enforceable under Maltese law. The set-off provisions under the ISDA Master Agreement can be triggered where an event of default, credit event upon merger or any termination event has been declared.

The Bank also has in place credit support annexes "CSAs" with a number of its financial counterparties for purposes of the collateralisation of exposures between the Bank and its counterparties. The CSA is a schedule to the ISDA Master Agreement. By virtue of such CSAs, a party to a derivative that has an exposure to its counterpart, will post collateral to its counterpart to cover such exposure by way of an outright title transfer of such collateral. All CSAs that the Bank has in place are of a two-way nature.

In the case of non-financial counterparties, the Bank enters into pledging collateral arrangements with the counterparties, in favour of the Bank. Such pledging agreements are of a one-way nature, in favour of the Bank.

	The Group	
	2019	2018
	€000	€000
Derivative financial assets		
Gross amounts of recognised financial assets	1,275	4,391
Net amounts of financial assets presented in the statement of financial position	1,275	4,391
Related amounts not set off in the statement of financial position:		
Financial instruments	(1,275)	(4,391)
Net amount	-	-

Financial liabilities subject to offsetting, enforcable master netting arrangements and similar agreements

	2019	2018
Derivative financial liabilities		
Gross amounts of recognised financial liabilities	24,870	19,018
Net amounts of financial liabilities presented in the statement of financial position	24,870	19,018
Related amounts not set off in the statement of financial position:		
Financial instruments	(1,275)	(4,391)
Financial collateral pledged	(29,789)	(22,909)
Net amount	(6,194)	(8,282)

40. ASSETS HELD FOR REALISATION

The assets held for realisation mainly comprise immovable properties that were held as collateral for outstanding loans, which properties were taken into the possession of the Bank following defaults by the counterparty. The Bank's policy is to dispose of such assets within a reasonable timeframe from the date of classification, unless events or circumstances which are beyond the Bank's control extend the period to complete the sale. Such assets meet the criteria for classification as non-current assets held for sale in accordance with IFRS 5.

During the current financial year €6.6 million were reclassifed from Property and equipment to Assets held for realisation (note 21).

41. TRUST ACTIVITIES

The Group acts as trustee and provides trust activities that result in the holding and placing of assets on behalf of third parties. Trust assets are not assets of the Group and therefore they are not included in its Statement of Financial Position.

Income derived from trust assets is excluded from revenue. Fees arising from the rendering of trustee services are recognised in the Group's profit or loss.

At 31 December 2019, the total assets held by the Group on behalf of its customers amounted to €104.9 million (2018: €126.8 million).

Details on significant claims related to trusts are given in note 33.

Notes to the financial statements 31 December 2019 (continued)

42. REGULATORY COMPENSATION SCHEMES

As at 31 December 2019, no balances with Central Bank of Malta have been pledged in favour of the Depositor Compensation Scheme (refer to note 16).

In accordance with the provisions of the Investor Compensation Scheme Regulations, 2003, issued under the Investment Services Act, 1994, licence holders are required to transfer a variable contribution to an Investor Compensation Scheme Reserve and place the equivalent amount with a bank, pledged in favour of the Scheme. Alternatively licence holders can elect to pay the amount of variable contribution directly to the Scheme.

Bank of Valletta p.l.c. has elected to pay the amount of the variable contribution directly to the Scheme.

Regulatory contributions amounting to €12.6 million (2018: €10 million), included with administrative expenses, reflect the Group's annual obligations arising from the recent EU Directives on Deposit Guarantee Scheme and Single Resolution Fund.

43. EVENTS SUBSEQUENT TO THE FINANCIAL REPORTING DATE

The events subsequent to the reporting date, notably the COVID-19 outbreak, will most likely have a substantial negative impact on both global and local economies. The existing capital buffers, together with measures made available by the regulatory authorities provide significant mitigation against the additional challenges of this unprecedented event. An adverse influence on 2020 performance is highly probable but a clear determination of the overall financial impact cannot be made at this early stage. There are uncertainties on both the duration of the crisis and the extent of the impact on the local economy as well as, the scale and effectiveness of mitigating measures provided by the local and EU authorities. The directors do not consider that any adjustments are required to the financial statements at this stage. The Bank has already taken steps and intends to launch further initiatives to continue to support the local economy as well as to help safeguard the well-being of its employees and its customers.

44. REGISTERED OFFICE

The registered and principal office of the Bank is 58, Triq San Zakkarija, Il-Belt Valletta, VLT1130, Malta.

Independent auditors' report to the Shareholders of Bank of Valletta p.l.c.

1 Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Bank of Valletta p.l.c. (the "Bank" or the "Company") and of the Group of which the Company is the parent, which comprise the statements of financial position as at 31 December 2019, the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements:

(a) give a true and fair view of the financial position of the Bank and the Group as at 31 December 2019, and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS") as adopted by the EU; and

(b) have been properly prepared in accordance with the provisions of the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act") and the Banking Act, 1994 (Chapter 371, Laws of Malta) (the "Banking Act") and, additionally, specifically in relation to those of the Group, with the requirements of Article 4 of the Regulation on the application of IFRS as adopted by the EU.

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 *Auditors' responsibilities for the audit of the financial statements* section of our report. During the course of our audit, we maintained our independence from the Company and the Group in accordance with the International Ethics Standards Board *for Accountants' Code of Ethics for Professional Accountants,* together with the ethical requirements that are relevant to our audit of the *financial statements in accordance with the Accountancy Profession (Code of Ethics for Warrant Holders) Directive* issued in terms of the Accountancy Profession Act (Chapter 281, Laws of Malta) ("APA"), and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current year (selected from those communicated to the audit committee), and include a description of the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

We summarise below the key audit matters, together with our response by way of the audit procedures we performed to address that matter in our audit, and key observations arising with respect to such risks of material misstatement.

Measurement of impairment allowances on loans and advances to customers at amortised cost, including off-balance sheet elements of those exposures and related disclosures

Accounting policy notes 1.4.3 to the financial statements and notes 8, 17, 33, 34 and 39.2 for further disclosures.

Expected credit loss allowance on 'Loans and advances to customers at amortised cost' (Bank and Group: €4.7 billion) amounted to €108.3 million. Expected credit loss provision on 'Financial guarantees contracts and loan commitments' (Bank and Group: €2.2 billion) amounted to €15.8 million.

The calculation of the expected credit loss ("ECL") involves a number of complex, judgemental and highly sensitive assumptions. Of all the Group's financial instruments, the major impact, in terms of complexities around the measurement of the ECL and of the materiality of the resultant allowances, was in relation to the loans and advances to customers' portfolio (and the related off-balance sheet elements). In that regard, our key areas of audit focus in the Group's calculation of the ECL were the following:

— Significant judgement linked with the selection of (i) forward looking macroeconomic scenarios, (ii) the associated scenario probabilities and (iii) the material economic variables which drive the scenarios and the related weightings.
— Identification of a significant increase in credit risk ("SICR") is also a key area of judgement within the Group's ECL calculation, as the application of those criteria determines whether a twelve month or lifetime provision is recorded.
— Use of complex and inherently judgemental modelling techniques to estimate ECLs which involve determining Probabilities of Default ("PD"), Loss Given Default ("LGD") and Exposures at Default ("EAD"). In particular, the PD models are the key drivers of the Group's ECL calculation and are therefore the most significant judgemental element of the Group's ECL modelling approach.
— Qualitative adjustments to the model-driven ECL raised by the Group to address known impairment model limitations or emerging trends. Those adjustments are inherently uncertain and significant judgement is involved in the estimation process.
— Individually assessed stage 3 exposures may be materially misstated if individual impairments are not appropriately identified and estimated. The calculation of expected credit losses on stage 3 exposures includes a range of estimates of future cash flows and valuation of collateral, which are inherently uncertain and judgemental.

Independent auditors' report to the Shareholders of Bank of Valletta p.l.c. (continued)

Key audit matters (continued)

The disclosures regarding the application of IFRS 9 are crucial in explaining the key judgements made, as referred to in this key audit matter, and inputs used to generate the IFRS 9 ECL results.

Our response

As part of our procedures:

- We tested the design and implementation as well as the operating effectiveness of relevant manual controls and automated (that is, Information Technology based) controls. More specifically, the following controls were covered:
  - sanctioning of facilities in line with the established authorisation limits as per the Group's credit policy;
  - the Group's review and approval of loan credit ratings;
  - monitoring control performed on delinquent personal facilities maintained across the Group;
  - the Group's review control over the completeness and accuracy of loan exposures keyed into the ECL model;
  - the monthly review performed by Chief Finance Officer of ECL movements;
  - the validation of internally generated macro-economic forecasts thorough comparison with externally observable data; and
  - the Provisions Committee's bi-annual review of ECL movements, management overlays and other adjustments.

- We involved our own financial risk modelling specialists in evaluating the appropriateness of the Group's IFRS 9 impairment methodologies (including the SICR criteria used). We used our experience of the Group to independently assess PD, LGD and EAD assumptions. We assessed the reasonableness of the model predictions by comparing them against actual results. We made enquiries of the Chief Finance Officer as to the reasons for any significant variations identified and assessed the reasonableness of the explanations provided, against the specialists' expectations on the direction and extent of variations identified. We have also requested workings from the Group's expert to demonstrate and/or simulate the variations noted from prior year and, for a sample of exposures, we performed re-computations to validate the results.

- We involved our economics specialist to assist in assessing:
  - the appropriateness of the methodology for determining the macroeconomic scenarios used and the reasonableness of the probability weightings applied to them; and
  - the key macroeconomic variables (as set out in note 39.2.1.2.6 to the financial statements) as well as the accuracy of macroeconomic data feeding the ECL model.

- In evaluating the Group's credit grading process, we performed assessments (referred to as credit reviews) on a sample of corporate exposures selected qualitatively based on risk, including a sample of stage 3 loans and advances to customers. In performing those reviews, we:
  - considered relevant internal information available used in the Group's assessment and any external data in relation to those exposures;
  - evaluated whether those exposures were graded in line with the Group's credit policy; and
  - determined whether a SICR was appropriately identified.

  In addition, for the selected stage 3 corporate exposures, we independently re-performed the impairment calculation to assess the reasonableness of the Bank's related ECL.

- On a sample of loans and advances to customers, we:
  - performed testing over key data elements (EAD, PD and LGD) impacting the ECL calculations to assess the accuracy of information used; and
  - re-performed model calculations for accuracy for all stages.

- We assessed the appropriateness of the adjustments to the model-driven ECL, by evaluating key assumptions, inspecting the calculation methodology and corroborating back to source data.

- We assessed whether the disclosures in relation to IFRS 9 adequately explain the key judgements made and significant inputs used in the recognition of expected credit losses as at the end of the financial reporting period. In particular, we involved our economics specialist to assist us in assessing the appropriateness of the sensitivity analysis disclosures.

We have no key observations to report, specific to this matter.

Recognition and measurement of provisions for litigation and claims, including related disclosures

Accounting policy notes 1.15 and 1.25.5 to the financial statements and note 33 for further disclosures.

Litigation provision of €102,000,000 (2018: €77,000,000) shown as part of 'Provisions' on the face of 'Statements of financial position' and included within the 'Provisions and Contingencies' note, together with significant claims disclosures.

Independent auditors' report to the Shareholders of Bank of Valletta p.l.c. (continued)

Key audit matters (continued)

The Group is exposed to various litigation and claims, which may potentially have a material impact on the financial statements as a whole, and which are subject to varying degrees of complexity.

Significant judgement is involved in determining whether an obligation is a present obligation or a possible one. That assessment determines whether such obligation is recognised as a provision (in the statement of financial position) or is disclosed in the notes as a contingent liability. The measurement of any such provision, which is based on the determination of the extent of the outflow of economic resources, is subject to significant estimation uncertainty.

In the event that it is not probable that an outflow of resources will be required to settle a present obligation and there is more than a remote likelihood of an adverse outcome for a possible obligation, the related contingent liability disclosure is necessary to understand the risks and potential effects on the financial statements.

Our response

As part of our procedures, we evaluated the assessment made by the Group's internal legal counsel, the Chief Executive Officer, Chief Finance Officer, Chief Risk Officer and the Chairman of the Board on the (i) status of the litigation claims as well as the (ii) action being taken by the Group in relation to those claims.

Specifically for the significant litigation claims, we directly obtained written opinions from, and held discussions with, the Group's external legal counsel, and evaluated their views on the outcome of such claims. Additionally, we challenged the directors' best estimate of the provisions recognised by corroborating their responses directly with the Group's external legal advisors.

We assessed whether the financial statements, in relation to the significant litigation claims adequately disclose the amount of provision, the potential liabilities and the significant uncertainties that exist.

We have no key observations to report, specific to this matter.

Impact of the IT access controls over the Group's financial reporting

Section 8.3 of the Capital and risk management report

Information security risk disclosures included within the Capital and risk management report

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A significant component of the general IT controls environment is internal access controls. These controls aim to prevent unauthorised employee access to the Group's applications, operating systems and data impacting financial reporting.

The Group is directing its focus on enhancing the robustness of the controls over internal access to the Group's IT systems, particularly those related to user access granting and access revocation.

As part of our audit strategy, we seek to place reliance on a number of IT systems supporting the Group's financial reporting, considering the design, implementation and operating effectiveness of controls existing in those systems. In the event that we are unable to rely on such controls, performing alternative procedures requires significant audit effort.

Our response

As part of our procedures:

- We tested the design, implementation and operating effectiveness of the following access controls for the systems relied upon for audit purposes:
  - creation, modification and revocation of user access rights;
  - systems administrator rights;
  - systems' enforcement of the Bank's password complexity policy; and
  - access to migrate or conduct changes to application systems.
- Where the above tests were inconclusive, we conducted additional assessments through a retrospective review, to evaluate whether, for automated controls relied upon:
  - generic elevated system privileges were used by unauthorised personnel; and
  - system access assigned to terminated employees was used prior to access rights being revoked.
- Where it was not possible to perform such retrospective reviews, we conducted alternative audit procedures that did not rely on IT systems in relation to various financial statement captions, as relevant.

We have no key observations to report, specific to this matter.

Other matter - The impact of uncertainties due to the global Coronavirus pandemic on our audit

Uncertainties related to the consequential economic effects of the Coronavirus pandemic are relevant to understanding our audit of the financial statements. All audits assess and challenge the reasonableness of estimates made by the directors, such as recoverability of loans and advances to customers, and related disclosures and the appropriateness of the going concern basis of preparation of the financial statements. All of these depend on assessments of the future economic environment and the Group's future prospects and performance.

The Coronavirus outbreak is one of the most significant economic events for the World, and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes consequences, with the full range of possible effects unknown. We applied a standardised firm-wide approach in response to that uncertainty when assessing the Group's future prospects and performance. However, no audit should be expected to predict the unknowable factors or all possible future implications for a company and this is particularly the case in relation to the economic effects of the pandemic.

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Independent auditors' report to the Shareholders of Bank of Valletta p.l.c. (continued)

Other information

The directors are responsible for the other information which comprises the:

- Contents and General Information;
- Board of Directors and Group Company Secretary;
- Chairman's Statement;
- Chief Executive Officer's Review;
- Management Board;
- Corporate Social Responsibility;
- Directors' Report;
- Capital and Risk Management Report;
- Corporate Governance Statement of Compliance;
- Remuneration Report;
- Nominations Report;
- The Group's five year summary; and
- Group's Financial Highlights in US dollars.

but does not include the financial statements and our auditors' report thereon.

Our opinion on the financial statements does not cover the other information and, other than in the case of the Directors' report on which we report separately below in our 'Opinion on the Directors' Report', 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, 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.

Responsibilities of the directors for the financial statements

The directors are responsible for the preparation of financial statements that (a) give a true and fair view in accordance with IFRS as adopted by the EU, and (b) are properly prepared in accordance with the provisions of the Act and the Banking Act, and, additionally, specifically in relation to those of the Group, with the requirements of Article 4 of the Regulation on the application of IFRS as adopted by the EU. The directors are also responsible 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 Company'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 Company and/or the Group or to cease operations, or have no realistic alternative but to do so.

The directors are also responsible for overseeing the financial reporting process.

Auditors' 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 auditors' 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.

As part of an audit in accordance with ISAs, we exercise professional judgement 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.

- Consider the extent of compliance with those laws and regulations that directly affect the financial statements, as part of our procedures on the related financial statement items. For the remaining laws and regulations, we make enquiries of directors and other management, and inspect correspondence with the regulatory authority, as well as legal correspondence. As with fraud, there remains a higher risk of non-detection of other irregularities (whether or not these relate to an area of law directly related to the financial statements), as these may likewise involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

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Independent auditors' report to the Shareholders of Bank of Valletta p.l.c. (continued)

Auditors' responsibilities for the audit of the financial statements (continued)

- 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 Company'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 Company'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 auditors' 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 auditors' report. However, future events or conditions may cause the Company and/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 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 auditors' 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.

2 Opinion on the Directors' Report

The directors are responsible for preparing a directors' report in accordance with the provisions of article 177 of the Act and other applicable legal requirements, and is to include a statement that the Company is a going concern with supporting assumptions or qualifications as necessary, as required by Listing Rule 5.62 issued by the Listing Authority in Malta.

We are required to consider whether the information given in the directors' report for the accounting period for which the financial statements are prepared is consistent with those financial statements; and, if we are of the opinion that it is not, we shall state that fact in our report. We have nothing to report in this regard.

Pursuant to article 179(3) of the Act, other than for the non-financial information that is exclusively required to be disclosed by paragraph 8 of the Sixth Schedule of the Act with respect to the Bank, and paragraph 11 of the Sixth Schedule of the Act with respect to the Group (and on which we report separately below in our 'Report on Other Legal and Regulatory Requirements'), we are also required to:

- express an opinion on whether the directors' report has been prepared in accordance with the applicable legal requirements; and
- state whether, in the light of the knowledge and understanding of the entity and its environment obtained in the course of our audit of the financial statements, we have identified material misstatements in the directors' report, giving an indication of the nature of any such misstatements.

Pursuant to Listing Rule 5.62 of the Listing Rules issued by the Listing Authority in Malta, we are required to review the directors' statement in relation to going concern.

In such regards:

- in our opinion, the directors' report has been prepared in accordance with the applicable legal requirements;
- we have not identified material misstatements in the directors' report; and
- we have nothing to report in relation to the statement on going concern.

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Independent auditors' report to the Shareholders of Bank of Valletta p.l.c. (continued)

3 Report on Other Legal and Regulatory Requirements

Matters on which we are required to report by the Act, specific to public-interest entities

Pursuant to article 179B(1) of the Act, we report as under matters not already reported upon in our 'Report on the Audit of the Financial Statements':

- we were first appointed as auditors by the shareholders on 19 June 2015, and subsequently reappointed at the Company's general meetings for each financial period thereafter. The period of total uninterrupted engagement is five years;
- our opinion on our audit of the financial statements is consistent with the additional report to the audit committee required to be issued by the Audit Regulation (as referred to in the Act); and
- we have not provided any of the prohibited services as set out in the APA.

Matters on which we are required to report by the Act, specific to large undertakings which are public-interest entities and public-interest entities which are parent undertakings of a large group that (individually and on a consolidated basis, respectively) exceed the criterion of an average number of five hundred employees during the financial year

Pursuant to article 179(3) of the Act, we report as under matters not already reported upon in our 'Opinion on the Directors' Report:

The Directors' Report contains the information required by paragraph 8 of the Sixth Schedule, with respect to the Bank and paragraph 11 of the Sixth Schedule with respect to the Group.

Matters on which we are required to report by the Banking Act and by exception by the Act

Pursuant to article 31(3)(a), (b) and (c) of the Banking Act, in our opinion:

- we have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purpose of our audit;
- proper books of account have been kept by the Bank so far as appears from our examination thereof; and
- the Bank's financial statements are in agreement with the books of account.

Furthermore, we have nothing to report in respect of the above matters, where the Act requires us to report to you by exception pursuant to articles 179(10) and 179(11).

Pursuant to article 31(3)(d) of the Banking Act, in our opinion and to the best of our knowledge and belief and, on the basis of the explanations given to us, the financial statements give the information required by law in force in the manner so required.

The Principals authorised to sign on behalf of KPMG on the audit resulting in this independent auditors' report are Noel Mizzi and Jonathan Bingham.

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18 March 2020

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The Group's five year summary - extracted from the respective audited financial statements

A. STATEMENTS OF PROFIT OR LOSS

For the financials years

	2019 12 months to Dec 2019 €000	2018 12 months to Dec 2018 €000	2017 15 months to Dec 2017 €000	2016 12 months to Sep 2016 €000	2015 12 months to Sep 2015 €000
Interest and similar income	206,963	213,896	259,194	214,258	215,612
Interest expense	(54,113)	(57,350)	(76,247)	(65,429)	(70,834)
Net interest income	152,850	156,546	182,947	148,829	144,778
Other operating income	96,914	101,220	117,526	101,756	102,093
Gain on Visa transaction	-	-	-	27,511	-
Other operating charges	(163,018)	(130,598)	(151,251)	(112,778)	(108,032)
Net impairment reversals/(losses)	11,562	10,816	6,227	(23,142)	(32,710)
Litigation Provision	(25,000)	(75,000)	-	-	-
Share of results of equity-accounted investees	15,897	8,214	19,287	3,730	11,786
Profit before tax	89,205	71,198	174,736	145,906	117,915
Income tax expense	(25,713)	(19,788)	(55,238)	(50,708)	(37,971)
Profit for the year	63,492	51,410	119,498	95,198	79,944
Attributable to:					
Equity holders of the Bank	63,492	51,410	119,498	94,742	79,378
Non-controlling interest	-	-	-	456	566
	63,492	51,410	119,498	95,198	79,944
Earnings per share	10.9c	8.8c	20.5c	16.2c	13.6c

The calculation of the earnings per share for all periods presented was adjusted retrospectively in view of the increase in the number of ordinary shares outstanding as a result of the bonus issue of shares.

The Group's five year summary - extracted from the respective audited financial statements (continued)

B. STATEMENTS OF FINANCIAL POSITION

	2019	2018	2017	2016	2015
	€000	€000	€000	€000	€000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	3,669,580	3,400,588	3,066,655	1,790,079	1,014,281
Investments and financial assets at fair value through profit or loss	3,276,299	3,521,161	3,700,832	4,128,702	3,793,827
Loans and advances to banks	501,686	490,644	524,412	479,410	768,717
Loans and advances to customers	4,445,812	4,362,983	4,162,032	4,001,656	4,001,839
Investments in equity-accounted investees	101,479	108,510	109,461	97,041	96,904
Property and equipment	186,659	161,198	133,675	102,846	102,523
Current tax	15,185	7,606	12,034	16,061	965
Deferred tax	76,017	71,769	60,217	67,188	86,654
Assets held for realisation	10,123	4,335	5,972	11,973	11,601
Other assets	42,627	7,880	5,955	4,818	2,990
Prepayments and accrued income	5,142	10,314	39,385	23,077	21,661
Total Assets	**12,330,609**	**12,146,988**	**11,820,630**	**10,722,851**	**9,901,962**
LIABILITIES					
Financial liabilities at fair value through profit or loss and derivatives held for hedging	24,870	19,018	24,010	40,976	60,278
Amounts owed to banks	66,047	146,021	192,196	250,155	197,760
Amounts owed to customers	10,629,719	10,414,908	10,100,625	9,181,047	8,559,731
Debt securities in issue	-	40,197	95,400	95,400	95,400
Deferred tax	5,736	5,743	4,519	4,318	4,382
Other liabilities	189,109	196,421	195,751	173,988	172,905
Provisions	118,109	95,767	2,000	-	-
Accruals and deferred income	484	539	12,451	16,215	21,317
Subordinated liabilities	234,230	234,241	231,591	231,591	120,000
Total Liabilities	11,268,304	11,152,855	10,858,543	9,993,690	9,231,773
EQUITY					
Called up share capital	583,849	530,772	525,000	390,000	360,000
Share premium account	49,277	49,277	45,427	988	988
Revaluation reserve	54,898	50,034	33,194	35,332	35,217
Retained earnings	374,281	364,050	358,466	302,841	272,713
Total Equity attributable to equity holders of the Bank	1,062,305	994,133	962,087	729,161	668,918
Non-controlling interest	-	-	-	-	1,271
Total Equity	1,062,305	994,133	962,087	729,161	670,189
Total Liabilities and Equity	**12,330,609**	**12,146,988**	**11,820,630**	**10,722,851**	**9,901,962**
MEMORANDUM ITEMS					
Contingent liabilities	341,618	335,405	253,851	225,407	251,670
Commitments	1,828,756	1,881,392	1,858,191	1,590,156	1,612,122

The Group's five year summary - extracted from the respective audited financial statements (continued)

C. STATEMENTS OF CASH FLOWS

	2019 €000	2018 €000	2017 €000	2016 €000	2015 €000
Net cash from operating activities	90,157	251,776	1,020,077	768,054	1,124,108
Cash flows from investing activities					
Dividends received from equity shares	24,186	10,774	8,794	5,628	5,808
Interest received from investing securities	50,840	54,953	74,725	59,783	58,998
Acquisition of non-controlling interest	-	-	-	(5,000)	-
Purchase of equity investments	-	-	-	-	(100)
Proceeds from Visa transaction	-	-	-	22,042	-
Proceeds from sale of equity instruments	-	12,296	4,350	3,043	-
Net inflow/(outflow) on investment securities	263,225	129,240	258,283	(388,362)	(853,476)
Purchase of property and equipment	(34,996)	(26,295)	(33,341)	(8,111)	(9,132)
Proceeds on disposal of property and equipment	330	2,000	-	598	-
Net cash (used in)/from investing activities	303,585	182,968	312,811	(310,379)	(797,902)
Cash flows from financing activities					
Proceeds from rights issue	-	-	149,439	-	-
Interest paid on debt securities and subordinated liabilities	(10,050)	(13,414)	(17,875)	-	-
Proceeds from issue of subordinated bonds	-	-	-	111,591	-
Repayment of debt securities	(40,208)	(55,400)	-	-	-
Payment of lease liabilities	(1,475)	-	-	-	-
Dividends paid	-	(17,678)	(33,883)	(30,575)	(29,362)
Net cash (used in)/from financing activities	(51,733)	(86,492)	97,681	81,016	(29,362)
Increase in cash and cash equivalents	342,009	348,252	1,430,569	538,691	296,844

D. PERFORMANCE EXPRESSED IN RELATION TO AVERAGE TOTAL ASSETS AND AVERAGE CAPITAL EMPLOYED

	2019 %	2018 %	2017 %	2016* %	2015 %
Operating income to total assets	2.0	2.2	2.1	2.4	2.7
Operating expenses to total assets	1.3	1.1	1.1	1.1	1.2
Profit before tax to total assets	0.7	0.6	1.2	1.1	1.3
Profit before tax to capital employed	8.7	7.3	16.5	16.9	18.4
Profit attributable to equity holders to total assets	0.5	0.4	0.8	0.7	0.9
Profit attributable to equity holders to capital employed	6.2	5.3	11.3	11.0	12.4

**Ratios exclude gain on Visa transaction.*

Group Financial Highlights in US dollars 31 December 2019

The following figures were converted from Euro to US Dollars using the rate of exchange ruling on 31 December 2019. The rate used was €1 = US$ 1.1153. This does not reflect the effect of the change in the rate of exchange since 31 December 2018 which was €1 = US$ 1.1453.

	2019 US$000	2018 US$000
Net income attributable to equity holders of the Bank	70,813	58,880
Net income per share	13c	11c
Gross dividend paid	-	48,103
Net dividend paid	-	31,267
Gross dividend per share	-	9c
Total assets	13,752,328	13,911,945
Liquid funds	4,092,683	3,894,693
Investments and financial assets at fair value through profit or loss	3,654,056	4,032,786
Advances	5,517,945	5,558,859
Investments in equity-accounted investees	113,180	124,277
Share capital	651,167	607,893
Capital reserves	116,186	113,741
Retained earnings	417,436	416,946

Notes

Issued by Bank of Valletta p.l.c., 58, Triq San Żakkarija, il-Belt Valletta, VLT1130

Bank of Valletta p.l.c. is a public limited company regulated by the MFSA and is licensed 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).
Bank of Valletta p.l.c. is an enrolled tied insurance intermediary of Mapfre MSV Life p.l.c. Mapfre MSV Life is authorised by the MFSA to carry out long term business of insurance under the Insurance Business Act (Cap.403 of the Laws of Malta).
Bank of Valletta p.l.c. is authorised to act as a trustee by the MFSA.