Bank of Valletta p.l.c.

Annual Report & Financial Statements

2016

BOV
Bank of Valletta

BOARD OF DIRECTORS

John Cassar White (Chairman)
Barbara Helga Ellul
James Grech
Mario Grima
Alfred Lupi
George Portanier *(up to 16 September 2016)*
Taddeo Scerri
Gabriele Simonetti
Joseph M Zrinzo

COMPANY SECRETARY

Ruth Spiteri Longhurst

MANAGEMENT BOARD

Mario Mallia (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 - Investments)
Albert Frendo (Chief Business Development Officer - Credit)
Elvia George (Chief Finance Officer)

Josianne Brincat (Secretary)

AUDITORS

KPMG

LEGAL ADVISORS

Camilleri Preziosi

NOTICE OF MEETING

The Annual General Meeting of the Bank will be held at the Grand Master Suite, Hilton Malta, St Julians, on Friday 16 December 2016 at 10.00a.m.

CONTENTS

Board of Directors	ii
Chairman's Statement	iv
Chief Executive Officer's Review	viii
Corporate Responsibility	xvi

FINANCIAL STATEMENTS

Directors' report	1
Capital & risk management report	5
Corporate governance statement of compliance	26
Remuneration report	35
Nominations report	38
Auditors' report on corporate governance	39
Statements of profit or loss	40
Statements of profit or loss and other comprehensive income	41
Statements of financial position	42
Statements of changes in equity	43
Statements of cash flows	45
Notes to the financial statements	46
Independent auditors' report to the members of Bank of Valletta p.l.c.	113
The group's five year summary	115
Group financial highlights in US dollars	118

Bank of Valletta p.l.c.
BOV Centre
Triq il-Kanun
Santa Venera SVR 9030
Malta

Tel: (+356) 2275 3000
Fax: (+356) 2275 3711
www.bov.com
E-mail: customercare@bov.com

Bank of Valletta p.l.c.
Registered Office:
58, Triq San Żakkarija
Il-Belt Valletta VLT 1130
Malta
Registration Number C 2833

Board of Directors & Secretary

John Cassar White
Chairman

N R NED *

John Cassar White was appointed Chairman of Bank of Valletta Group in April 2013. He also chairs the boards of MSV Life p.l.c., Valletta Fund Management Limited and Valletta Fund Services Limited, and is a member on the board of Mapfre Middlesea p.l.c. Mr Cassar White worked with the Bank of Valletta for thirty seven years until 2008. He also served on the board on a number of state-owned enterprises and was a director of various investment companies. Until recently he was a lecturer at the Institute of Business and Commerce of MCAST. He holds a BA in Humanities Studies from the University of Malta and is an Associate of the Institute of Financial Services (UK). He has a special interest in business education and financial journalism.

Barbara Helga Ellul
Director

A N NED *

Appointed to the Board in December 2015. Ms Ellul is currently a member of the Audit Committee and the Nominations Committee. She was Managing Director of Playmobil Ltd from 1974 till September 2012. After her retirement she set up her own consultancy company and is board member and chairman of various Maltese businesses. Over the years Ms Ellul held various posts on boards of constituted bodies and government organisations. Until March 2011 she occupied the role of President of the Malta Chamber of Commerce, Enterprise and Industry.

James Grech
Director

RM NED

James was appointed to the BOV Board of Directors in December 2014. He is also the Head of Foreign Bank Relationships, sits on the Risk Management Committee and serves as a member of the Board of Trustees of the BOV Employees' Foundation, a position he has held since August 2010. Professionally, James' career commenced as a management accountant with a local accounting firm. He then joined Bank of Valletta in 1998 and served as Director on the BOV Board from January 2004 until December 2008. During his tenure he occupied senior managerial positions with various branches and departments and served as a member of the Bank's Operational Risk Management and Compliance Committees. James is a director of other local companies, and a recognised member of the Institute of Directors UK. He is also a committee member of ACI Malta, as well as a PTA Committee member of the De La Salle College. James 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. He has lectured on Financial Services at the Malta College of Arts, Science and Technology, and on Corporate Governance at the University of Malta.

Mario Grima
Director

C&CP RM NED *

Appointed to the Board in December 2013. Mr Grima chairs the Risk Management Committee and is also a member of the Compliance and Crime Prevention Committee. He was a member on the BOV Board between 1996 and 2001 and was employed with the Bank for thirty-seven years. He retired from the Bank in 2011 and his last deployment was as Executive Head Operations. He also served on the boards of Middlesea Insurance p.l.c., Middlesea Valletta Life Assurance Co Limited and Malta Freeport Corporation. Whilst at BOV he chaired various committees and was a Trustee Founder Member of the BOV Employees' Foundation for several years. His academic qualifications include a Masters Degree in Business Management from Henley Management College, UK.

Alfred Lupi
Director
R RM NED *

Appointed to the Board in December 2015. Mr Lupi is currently a member of the Risk Management Committee and the Remuneration Committee and also chairs the Audit Committee when reviewing Related Party Transactions. He is a professional accountant with an economics degree and currently engaged in consultancy. Mr Lupi was Chief Financial Officer in two major companies and the Executive Chairman of Pavi Shopping Complex p.l.c. He was a Director of the Central Bank of Malta and served as Acting Governor. Mr Lupi chaired the Accountancy Board and was a member of its Quality Assurance Oversight Committee. Mr Lupi has held a number of board appointments mainly in the financial sector.

Taddeo Scerri
Director
A R NED *

Appointed to the Board in April 2013. Mr Scerri currently chairs the Bank's Audit Committee and is a member of the Bank's Remuneration Committee and of the Bank's Asset and Liability Committee (ALCO). He is a qualified accountant. Mr Scerri was the Managing Partner of RSM Malta until his retirement in end 2015. He was the financial expert on the local UEFA Clubs Licensing Board and was also a member of the Malta Football Association's Finance Committee.

Gabriele Simonetti
Director
NED *

Appointed to the Board in December 2015. Mr Simonetti is Global Head of Trade Finance Services at UniCredit. Mr Simonetti joined Credito Italiano in 1975 and held various roles particularly in its International Division. He then held senior roles within the Group acting amongst others, as Head Correspondent Banking, Head of Product Management, Group Head Global Relationship Management and Sales and Group Global Head of Transactional Sales. Mr Simonetti holds a diploma in general and industrial accountancy.

Joseph M Zrinzo
Director
A C&CP N NED *

Appointed to the Board in December 2013. Mr Zrinzo chairs the Compliance and Crime Prevention Committee and is also a member of the Board's Audit Committee and a member of the Nominations Committee. At present he 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 as an active member of philanthropic associations. Over the years, Mr Zrinzo served as director on boards of various local and international companies, as BOV Board director between 1996 and 1998, as member of Audit, Remuneration and Compliance Committees and was founder member of The Malta Shareholders Association. Mr Zrinzo has a vast experience of international trade having operated businesses with European, North African, Middle-Eastern companies.

George Portanier
Director
C&CP NED *
(up to 16 September 2016)

Appointed to the Board in 2014. Up until his retirement, Mr Portanier was a member of the Compliance and Crime Prevention Committee. He also served as a BOV Board Member between 1992 and 2013. Mr Portanier chaired the Board's Compliance Committee for a number of years. He was also a member of the Executive Committee, a member of the Risk Management and Compliance Committee and the Remuneration and Nominations Committee. Mr Portanier was formerly a director of Portanier Brothers Limited and served as a member of the Local Manufacturers' Committee of the Federation of Industries, as well as a member of the Council of the Federation of Industries. He sits on the Board of other companies and is currently the CEO of the Malta Institute of Taxation.

Ruth Spiteri Longhurst
Group Company Secretary

Appointed BOV Group Company Secretary in April 2016. Dr Spiteri Longhurst is also the Company Secretary of MSV Life p.l.c. (MSV) and secretary to BOV's, MSV's and VFM's Board Committees. 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 14 years.

A	Audit Committee
C&CP	Compliance and Crime Prevention Committee
N	Nominations Committee
R	Remuneration Committee
RM	Risk Management Committee
NED	Non-executive Director
*	Independent

Chairman's Statement

John Cassar White

I am pleased to announce that BOV Group has recorded a profit of €145.9 million for financial year 2016. This includes a one-time gain of €27.5 million resulting from the acquisition of the Bank's shares in VISA Europe, as a result of the takeover of the latter by VISA Inc. in June 2016. When the results are adjusted for this item, one arrives at an operating profit of €118.4 million, as compared to the €117.9 million registered last year. The results translate into a Return on Equity (ROE) ratio of 16.9%, adjusted for the windfall gain, compared to 18.4% last year.

Group total assets have increased by €821 million, or 8.3%, to reach €10.7 billion, a growth that was fuelled primarily by customer deposits, which rose by €621 million and now stand at €9.2 billion. Net total advances have grown by 1.8% to reach €4.1 billion, while equity is up by 8.8% and amounts to €729.2 million.

These results were achieved in a year of continued growth for the Maltese economy – where GDP growth is expected to reach 4.1% in 2016, and is projected at 3.5% for 2017 – but in a challenging international environment marked by low-to-negative interest rates, sluggish Eurozone growth and Brexit-fuelled uncertainty.

It was a year during which the Bank has continued to roll out and implement the strategy that it has embarked upon under my chairmanship. It is a strategy that gives priority to the long-term stability and sustainability of the business. While the Board understands the need for the Bank to deliver an adequate level of profitability and dividend payout year after year – in line with the legitimate expectations of shareholders – it must not allow itself to be distracted from its strategic vision. This may at times entail sacrificing immediate gains in the pursuit of longer term goals, and exiting from certain business lines that are at the periphery of the Bank's risk appetite.

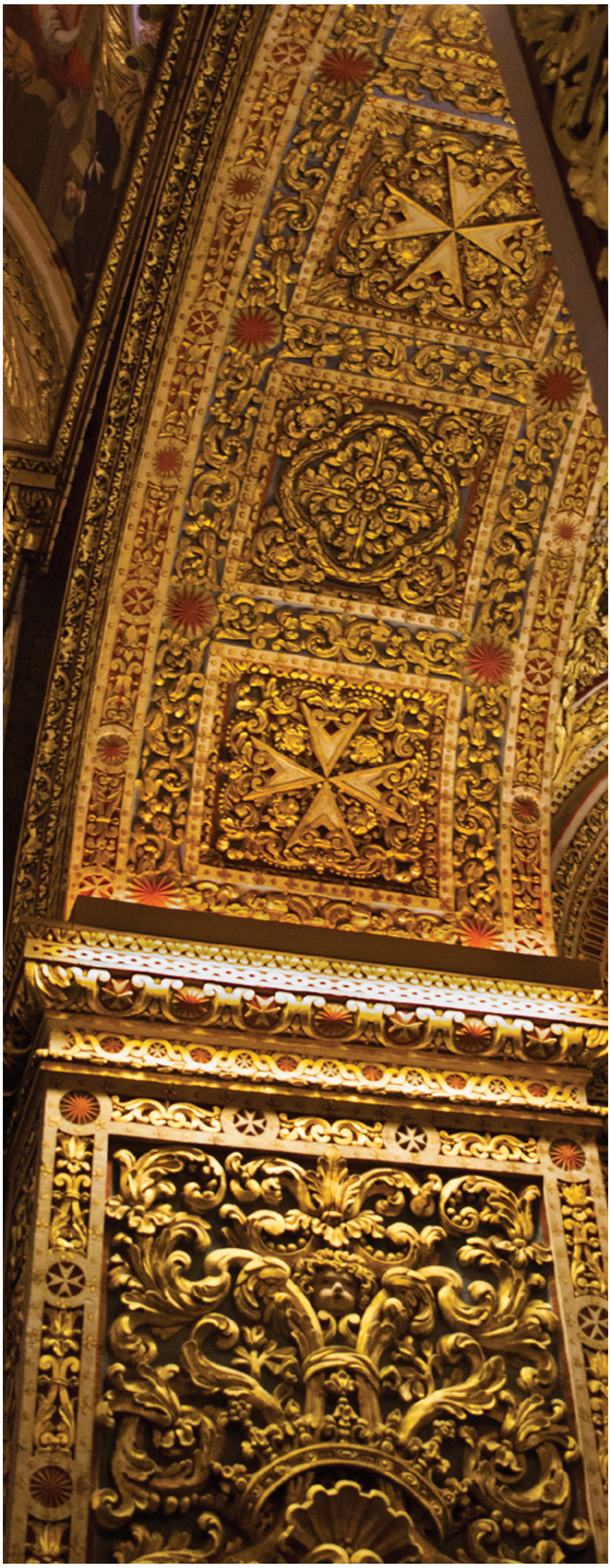
Our strategy for the medium term can be described as one of consolidation – that is, taking stock of the Bank's situation in the current social, economic and regulatory environment, and ensuring that it is adequately resourced to meet the challenges and take up the opportunities that present themselves. It is of utmost importance that the Board communicates its strategic vision to shareholders at every opportunity, so that they can better understand the risks that the Bank faces, as well as the Board's appetite for risk. It is also essential that shareholders are kept informed regarding the progress, or lack thereof, in the achievement of strategic goals.

The aim of our strategy is simple: to ensure BOV's viability in the long term, thereby protecting the interests of our depositors, who have entrusted their money to the institution, and of our shareholders, who have invested in the Bank with the aim of a sustainable and equitable return.

One of the cornerstones of the Bank's strategy for consolidation is its financial sustainability in the long term. In the short term, the Bank's lifeblood is liquidity. Management must ensure that the Bank's liquid resources are enough to meet its liabilities as they fall due. But in the long term, the Bank's viability depends on holding sufficient levels of capital. The level and quality of capital is a measure of the Bank's ability to withstand stress, and to absorb any unexpected losses that it may sustain in the course of business.

One of the cornerstones of the Bank's strategy for consolidation is its financial sustainability in the long term

As a systemically important bank in its local context, BOV is required by the supervisory authorities to maintain levels of capital higher than those set for banks which are less significant. The Bank today is adequately capitalised, with a Core Equity Tier 1 (CET1) ratio of 12.82%. However, the need for capital continues to grow, as evolving regulation is expected to impose higher capital requirements as well as higher risk weightings on assets.



The Bank is therefore giving primary importance to the conservation and generation of capital. Its strategy here is twofold: to retain a greater proportion of earnings as reserves, by gradually easing down its dividend payout ratio over the past few years to levels that can be sustained over the long term; and to issue fresh equity and debt capital over the coming years. As from this year, the Bank's dividend payout ratio is being determined with reference to a target CET1 ratio. Sufficient earnings are retained to enable the Bank to reach its target ratio, with the remaining profit then being deemed eligible for distribution.

A second cornerstone of strategy involves the replacement of the Bank's core IT system. In March 2015, BOV embarked on a programme to replace the existing IT core banking system that has been in place since 1998, with a new core system as part of the Core Banking Transformation (CBT) programme. The Board decision was not only to replace the current IT core system, which in itself is one of the most challenging initiatives a Bank can undertake, but also to "Change the Bank Together". Both were timely bold decisions that require rigorous implementation to achieve the necessary break-through to operate efficiently, become more innovative, adhere to regulatory requirements, address process risks and compete effectively.

Priority is being given to the strengthening of the Bank's Risk Management framework

The Bank has this year selected the final best fit vendor for CBT, and has conducted an in-depth "gap analysis" to ensure that the chosen system meets all requirements. The final contract with vendor will be negotiated and signed by early 2017, whereupon the implementation phase of the CBT programme can then commence.

A third cornerstone relates to the strengthening of the Bank's corporate governance model. Priority is being given to the strengthening of the Bank's Risk Management framework, and of its anti-financial crime defences. Among the measures currently in progress are the setting up of a well-resourced Anti-Financial Crime Department, and the overhaul of the Bank's Risk Appetite Framework (RAF).

The RAF is an articulation of the risks which the Bank wishes to take on in pursuit of its strategic objectives. The risk appetite represents the Bank's "desired level of risk". Risks which fall within the parameters of the RAF are deemed to be acceptable to, and aligned with, the risk appetite of the Board of Directors.

The Bank's RAF will be better articulated and its scope widened in line with the evolving business model. It will be supported by a suite of risk policies. The major policies currently in force cover the Bank's major business lines – credit, sales and treasury management. Other policies deal with outsourcing, conflicts of interest and ethics, capital management, liquidity and remuneration. All policies will be subject to a periodic review.

The final cornerstone of the Bank's consolidation strategy is the ongoing revision of the BOV business model. The model is evolving from one based on growth to one with a focus on quality, with a lower risk profile and, correspondingly, potentially lower returns. The business strategy is therefore to de-risk a number of business areas where the risk-return balance is unfavourable, and, concurrently, to cultivate alternative sources of revenue to supplement profitability.

The Bank is aware that de-risking, coupled with higher levels of capital, may result in a lower ROE. This is consistent with the priority given by the Board to long-term stability and sustainability. The Bank acknowledges, however, that sustainable profitability is key to capital generation. It aims to support its profitability by supplementing margin from its credit business, which is a mature business and where income is under pressure from interest rates at historic lows, with non-interest income generated by investment and wealth management business.

This is the strategy that is designed to take BOV forward in a financial world marked by very rapid changes in technology, customer preferences, industry disrupters and regulation. I am very conscious of the fact that this strategy can only deliver the desired results through the commitment of all stakeholders in the Bank. I would therefore like to thank my fellow Directors, the executive team and the Bank's staff for their hard work; our esteemed customers for their support; and our supervisory authorities for their valued guidance and advice.

John Cassar White
Chairman
28 October 2016

CEO Review

Mario Mallia

THE FINANCIAL YEAR IN PERSPECTIVE

The brief that I received from the Board of Directors when I was appointed as Chief Executive Officer of the Bank in January 2016 was threefold: to consolidate the Bank's governance, risk management and compliance framework; to ensure that the enterprise is adequately resourced in terms of capital, professional skills and IT infrastructure; and to review the Bank's business model with the aim of putting the customer at the centre of the organisation, diversifying sources of revenue, and exiting businesses where the risk being assumed was not justified by the rewards.

These strategic objectives are currently being addressed by my Management Team. The central focus of these objectives is always the customer – all changes, whatever their nature, are ultimately focused on delivering quality customer service within a secure environment. The message I constantly deliver to my staff is that it is the customer, and no one else, who pays our salaries and keeps us in business.

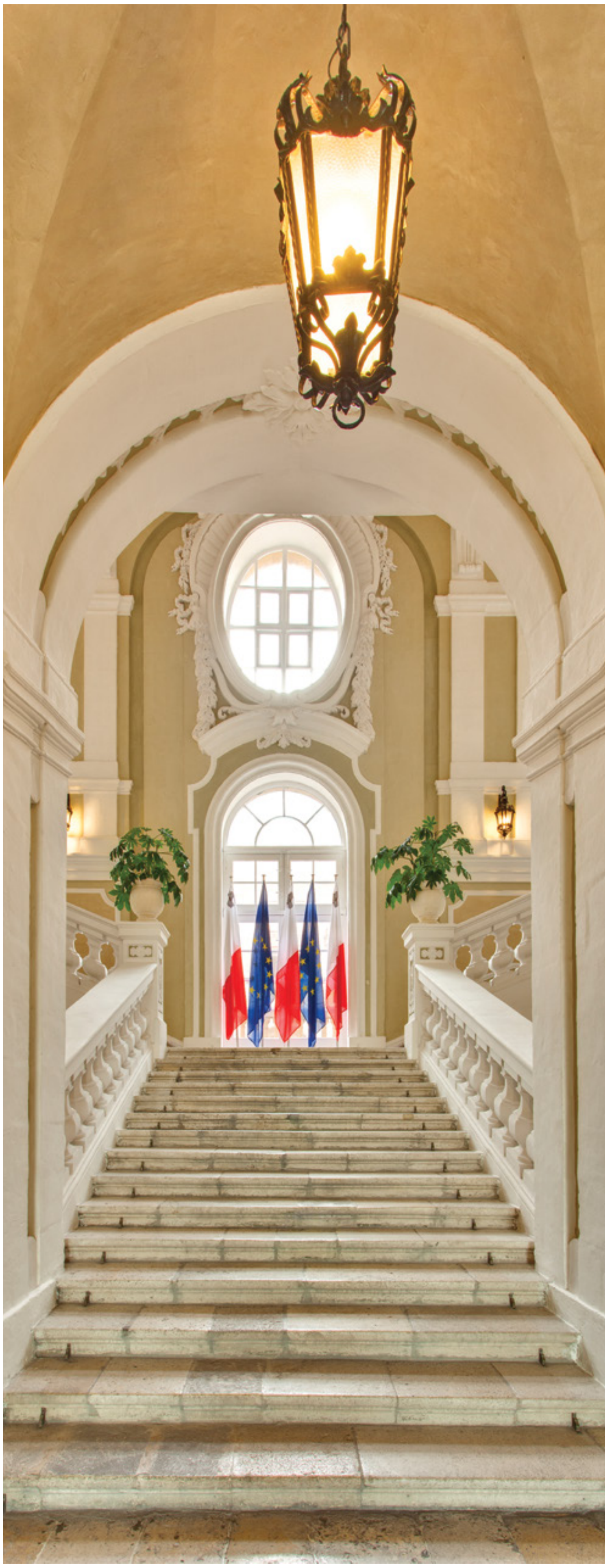
The change which the Bank needs to go through is being driven by executives who are experienced in the discipline of Change Management, and who are charged with ensuring that the change programme is holistic and internally consistent. The largest element by far within this change programme is the Core Banking Transformation programme, which will see the replacement of our core IT system, and the simultaneous upgrade of other key systems used by the business. The Bank has reached the stage where the system provider has been selected, final negotiations are currently underway. We are, simultaneously, undertaking a number of other initiatives, especially in the area of anti-financial crime, with the aim of delivering the objectives required by the Board.

The Bank's strategy is being implemented within an evolving regulatory framework aimed at making banking safer for all stakeholders. BOV, as a systemically important bank for Malta, is gradually strengthening its capital buffers under the direction of the supervisory authorities. We started our capital management programme by strengthening our Tier 2 capital, and have, over the past year, made two offers of subordinated notes totalling €125 million, of which around €112 million was taken up. The notes were classified as complex instruments, because of the embedded "bail in" element (subordination), and the take-up by the smaller retail investors was therefore limited. The next step is to strengthen Tier 1, through a combination of a prudent dividend pay-out policy and the issue of fresh equity instruments to the market.

Credit, investment services and electronic banking are the key areas which underlie the Bank's business model. It is a model which is currently under review so that its sustainability may be safeguarded. The Bank is exiting from certain business lines which are considered to be high risk, and is diversifying into businesses which show promise for the future, in order to offset revenues which come from traditional business areas and which may be reaching a plateau in terms of income generation.

The central focus of these objectives is always the customer

It is important for the Bank to focus on its long-term strategic aims – but without ever losing sight of the business opportunities made available by the current environment. The Bank can only achieve long-term sustainability if it maintains a business model which is relevant to the needs of the market, and which delivers a sustainable return. A good level of capitalisation implies reasonable profitability, as the main source of capital is the retention of earnings. The CEO must keep his gaze on the horizon, but at the same time cannot afford to overlook the business opportunities and the threats that are ever-present in today's fast-changing environment.



My first financial year at the helm of the Bank brought its fair share of good business opportunities, together with some tough challenges. The Maltese economy continued to outperform the rest of the Euro Area, with the gross GDP growth rate reaching 4.1% and the rate of unemployment falling to a record low of 4.9%. Domestic consumption remained strong, accounting for some 80% of this growth, while the highest employment growth rates were recorded in entertainment and recreation, professional services and support service activities. The Island continued to attract significant foreign direct investment, both in the services industries, but also in manufacturing, the most significant being the announced investment by the Crane Currency corporation of Boston in a Malta-based operation. High investor and consumer confidence, coupled with the ample liquidity generated by economic activity, provided good opportunities for the Bank to develop and supply a number of solutions to address the diverse financial needs of our customers.

The year was also marked by a number of challenges, the first of which was the continuing low interest environment. The fact that Maltese banks, like most of the sector in the Euro area, have chosen not to pass on negative policy rates to deposit customers means that their interest margins, and consequently their profitability, are coming under pressure. Low rates put pressure on banks' profitability, particularly on banks which are very reliant on net interest income. The ECB's Chief Economist has been quoted as saying that "the longer low interest rates persist, the greater the challenges for the banking sector." There are no expectations that the current interest rate paradigm will shift anytime soon.

A second source of uncertainty was Brexit. There was no impact on the Bank's business from the immediate fallout of the referendum, since we do not hold open currency positions, and exposures to UK and other equities is strictly limited. Any longer term impact will be indirect, and will only be the result of the as yet hypothetical structural impact of Brexit on the Maltese and Euro Area economies.

REVIEW OF PERFORMANCE

The Group is reporting a profit of €145.9 million, before deducting income tax, for the financial year which ended on 30 September 2016. This result incorporates a one-time gain of €27.5 million, arising from the takeover of VISA Europe, in which BOV is a Principal member, by VISA Inc. The Group's profit, adjusted for this windfall profit, amounts to €118.4 million, as compared to the profit of €117.9 million reported for the previous financial year.

Pre tax profit represents a return on average equity (ROE) of 16.9%*, down from 18.4% for 2015. This decrease is due to equity having grown by 9% to €729.2 million over the year, while the growth in profit has been marginal. Return on average assets, stands at 1.1%*, compared to 1.3% last year. The cost-to-income ratio, which relates costs incurred to revenue generated, amounts to 44.3%*, against 41.8% in 2015.

**Ratios exclude the impact of the gain on the VISA transaction*

Interest margin for the year of €148.8 million is up by 3% over last year. The squeeze on margins can be clearly seen when one compares this growth rate to that of interest-earning assets, which was of over 8%.

Commission income rose by 6%, driven by strong performances on investment services, wealth management and cards. On the other hand, trading and dividend income reduced by 10%, due to lower fair value gains on investments, and lower exchange earnings. Overall, operating income rose by an aggregate of 2%*.

Non-interest expense rose by 4%, driven by HR costs, which increased as a result of two factors: firstly, the new Collective Agreement signed this year, which sought to align salaries with current market rates; and secondly, due to further recruitment in the Bank's control functions. Higher IT related costs were also recorded as the Bank continued with its programme to replace its core banking system. The impairment charge of €23.1 million was lower by 29% compared to last year, when the charge had spiked due to the adoption of a more prudent provisioning methodology.

Group total assets stand at €10.7 billion, up by €821 million, or 8.3%, over September 2015. This growth was financed primarily by incoming customer deposits, which increased by €621 million, or 7%, to reach €9.2 billion; and by the issue of €112 million worth of subordinated debt. These funds were mostly deployed as liquid assets, as gross loans and advances remained stable at their September 2015 level of €4.3 billion.

The Group's Core Equity Tier 1 (CET1) ratio, which is the standard regulatory ratio measuring the capital adequacy of banks, rose to a robust 12.8%, up from 11.3% last year.

During 2016, the Group continued to support the local SME sector through the launch of BOV JAIME

BUSINESS REVIEW

Gross loans and advances remained at approximately the same level of September 2015. However, over €700 million in new lending was drawn down during the year, this amount being almost completely offset by repayments of existing loans. Drawdowns on new business lending exceeded €360 million, while drawdowns on consumer loans, including home loans, exceeded €340 million. Pipeline business is encouraging, and our aim in this regard is to continue diversifying the spread of the loan portfolio to reflect more closely the sectoral spread of the Maltese economy.

**Ratios exclude the impact of the gain on the VISA transaction*

During 2016, the Group continued to support the local SME sector through the launch of BOV JAIME (Joint Assistance Initiative for Maltese Enterprises) Financing Package, a new financing tool arising out of the agreement that was signed between the European Investment Fund (EIF) and Bank of Valletta. Following a competitive tender between banks, BOV was entrusted with the management and administration of the SME Initiative for a total fund of €50 million. The Initiative is a joint financial instrument of the European Commission and the EIB Group (EIF and EIB) which aims to stimulate SME Financing by providing partial risk cover for SME Loans to financial institutions. In February 2016, BOV launched the product, which offers capital expenditure loans on favourable terms and conditions, including a highly competitive interest rate of 3.5% and reduced collateral requirements. Over the life of the product, the Bank is seeking to build a portfolio of loans spread across the highest amount of SMEs, ensuring enhanced access to finance and high outreach within the Business Community.

Following on the lines of a similar scheme managed by BOV over the last years (JEREMIE), this scheme has proved to be successful in the months since inception. In fact, since its launch in February 2016, the Bank has allocated around 46% of the total available scheme funds. As at September 2016, over 210 facilities or €23 million worth of capital expenditure loans had been sanctioned to an array of SMEs operating in various economic sectors, ranging from the traditional to the new economy industries. Over 185 SMEs have to-date benefited from this scheme investing the equivalent of €38 million between them.

The Bank has also undertaken a review of its International Corporate Centre and International Personal Banking Centre, with the aim of strengthening its service delivery to international personal and institutional clients. The Bank is keen to ensure that it remains relevant to the changing needs of these customer segments, mindful of the changes that the wider macro economy is going through. A number of initiatives have been taken forward and will continue in the new financial year to strengthen the Bank's service proposition in this regard.

During the period under review the Bank undertook a number of initiatives to strengthen its banking and investment services proposition. The Bank currently services the investment requirements of its customers through a number of dedicated touch-points. At the retail level, the Bank has continued to sustain the training and periodic updates aimed at its workforce in order to provide a comprehensive suite of investment products aiming to meet customers' respective investment objectives and risk profiles. The Bank's programme in this regard includes briefing sessions on key developments in the world's economies, performance of the capital markets, product reviews, product features as well as the provision of monthly product literature toolkits. These initiatives are structured so as to enable the Bank's professional personnel to be kept abreast of developments and to relay this value added information to customers.

Every year the Bank provides in-depth training in London to a select number of its branch personnel, where they are updated on market performance and related macro and micro economic developments that directly or indirectly impact the Bank's investment products. A number of financial education seminars were organised over the course of this year on topics related to the wider investment opportunities available, with the aim of enhancing financial literacy in the local market. These education initiatives were supported through programmes held on both the audio and audio visual media. It is our firm intention to further strengthen the organisation of educational initiatives, extending this reach to the wider financial planning considerations covering financing and ebanking channels.

The Bank provides a select strata of its customers with an investment advisory service through its six Investment Centres located across Malta and Gozo. The financial advisors located within these Centres are constantly provided with the necessary tools and market-led information to enable them to provide professional investment advice to customers on the various array of instruments and products. These include a comprehensive range of investment funds, bancassurance products as well as the ability for investors to invest directly in bonds and equities in the world's capital markets.

For the discerning and highly affluent investors, the Bank has a fully-fledged Wealth Management Centre that provides a highly personalised service driven by professionalism, trust and long term relationship. In view of the highly bespoke nature of this service, the financial advisors at Wealth Management invest time and effort to get to know their customers, adopting a structured approach which consists of a detailed planning process as well as a fact finding exercise to ensure that the ultimate investment portfolio is tailored to the fully meet the objectives and needs of the customer. This approach is followed by a carefully designed open architecture product strategy which acts as a blue print for structuring the portfolio. The commitment of the financial advisors located at Wealth Management is solely to focus on customer needs, and to proactively provide financial advice as well as discretionary management services within the parameters established by the clients.

Over the course of the year, the Bank has further strengthened its House View Committee as well as its Research and Analysis Committee – two pivotal structures that are key to the overall investment services proposition across the Bank's various customer touchpoints.

We have, this year, announced a partnership with Saxo Bank which enabled us to deliver an alternative channel for customers to trade on the world's equity markets. In December 2015, the Bank announced the launch of eTrader+ powered by Saxo Bank. This new online trading platform is the result of a collaborative agreement reached between the two banks, offering an alternative channel to active traders, who want direct access to trade online. This highly adaptive platform offers key benefits such as the ability to place orders in real time across all major international markets, the possibility of effecting single limit as well as algorithmic or advanced orders and having 24-hour access to market prices for more than 30,000 securities. The platform is intended for the seasoned investor who trades frequently, providing a truly personalised and fully scalable platform that is accessible seamlessly, with all functionality being carried across devices, including tablet and mobile phones (iOS, Android and Windows compatible phones). Customers can now process trade orders for fixed income securities through the internet banking platform and equity securities through the partnership with Saxo Bank.

CONCLUSION

The announcement of the financial results and the declaration of dividends are yearly highlights in the life of the Bank which all stakeholders look forward to. It is the primary responsibility of my Management Team, together with the Board of Directors, to ensure the future sustainability of both performance and dividends. This requires that the Bank is always managed in accordance with a clear strategy, which is kept under constant review, and which seeks to add value to shareholders, even if this could involve sacrificing short term gains for long term value. And the focus of our strategy must always be the customer. We can only deliver value to our shareholders if we deliver value to our customers.

My final word of thanks goes to all staff at BOV, whose dedication and commitment to the Bank I experience first-hand every day; my colleagues on the Management Team for their constant support; the members of the Board of Directors for their insight and advice; and the supervisory authorities, for their oversight. Last but not least I wish to express gratitude to our esteemed customers, who are the ultimate source of the Bank's financial strength.

Mario Mallia
Chief Executive Officer
28 October 2016

Corporate Responsibility (CR)

Every year at this time, we pause to reflect on the state of corporate responsibility (CR) within the Bank and beyond. As CR continues to mature, year after year brings new voices to the table, innovations and more integrated adoption among the world's companies. Challenges remain and grow increasingly more complex. However we cannot shy away from addressing them. At Bank of Valletta, we strive to ensure that our operations reflect our long-standing commitment to operating with integrity, whilst registering progress in environmental sustainability. Stakeholders are becoming increasingly more interested in a company's CR practices. At Bank of Valletta we are proud of what we have achieved to date, and we look forward to continue evolving with the marketplace, whilst remaining true to the high standards that have always been the trademark of Bank of Valletta.

Three Blood Donation Drives were organised during the year. BOV employees responded keenly every time.

VALUING OUR PEOPLE

At Bank of Valletta, we strive to help our employees reach their full potential. We trust in the team, strong in the belief that the best outcomes are achieved when people work together across the organisation. Our people are the face and heart of the organisation. They represent a diverse range of skills and perspectives, thereby helping the Bank to connect with its customers, innovate and grow. They work hard and take pride in getting to know every individual customer, be it personal or business, and building a working relationship to help them grow over the long-term.

At Bank of Valletta we emphasise a culture of belonging and seek to nourish an environment where everyone can flourish, irrespective of their gender, ethnicity, age and physical ability. This is corroborated by the Equality Mark Certificate, which recognises the Bank as a gender equal organisation.

As part of the Bank's commitment towards being a learning organisation, the Bank's Training Academy seeks to ensure that all employees have access to tailor-made courses that enable them to develop both in their personal growth and in their career. Courses focusing on different areas of the financial horizon are delivered throughout the year, at various levels of specialization.

Within the Bank, we believe in the importance of fostering a culture that thrives on ethical values of integrity, honesty and trust. Therefore, this year, the Bank set up an Ethics and Employee Development Unit, reporting directly to the CEO. Although still in its initial stages, the Bank's Training Academy has already included a session 'Ethics at Work' in its induction courses, and there are plans for additional training for all employees. Meanwhile the Bank's Code of Ethics is actively being consolidated and updated.

This year BOV hosted an event for employees who celebrated their 20th, 30th, and even 40th anniversary in the Bank's employ.

CUSTOMER-DRIVEN

Bank of Valletta has always been customer-driven. This means that it invests time and effort to really understand its customers' requirements and circumstances. This knowledge is brought into the design of its products and services, as well as investing in harnessing the latest technology to give customers effective and user-friendly ways to manage their banking requirements.

The collaboration with Saxo Markets brought the Bank's online trading platform eTrader+ powered by Saxo Bank to the market. Targeted at frequent traders, this platform is a highly adaptive platform offering important benefits including 24-hour access to market prices of over 30,000 securities as well as the ability to place orders in real time across all major international markets.

Bank of Valletta continued to sustain its position as the Bank for SMEs by successfully developing the BOV JAIME Financing Package, the first financing package of its kind offered in Malta. It blends reduced collateral requirements with discounted interests for eligible SMEs. Through this initiative, the Bank is assisting over 700 Maltese SMEs by providing EUR50 million worth of financing.

BOV is working to replace its current Core Banking IT system in order to ensure for its customers an omni-channel experience.

BOV was the first bank in Malta to implement the new SME financing initiative - BOV JAIME Financing Package.

BOV becomes the first financial services provider in Malta to offer free life cover with all new BOV Personal Loans, whether fully or partially unsecured.

CUSTOMER-DRIVEN (continued)

This year also witnessed Bank of Valletta introducing free life cover as an additional benefit to all customers applying for a new personal loan. It also remained the only intermediary providing private pension schemes in collaboration with MSV life.

In line with its CR commitment, the Bank collaborated with various constituent bodies to organise educational clinics about financial instruments, in a bid to demystify their complexity, thereby enabling people to take control of their finances by making informed decisions. The turnout for these events shows that there is a demand which the Bank is addressing in a responsible manner.

This year, the Bank is pursuing its focus on harnessing and managing change. The Change Management function oversees all changes within the Bank with a view to ensuring that the holistic planned changes are prioritised and undertaken effectively, efficiently and with minimal disruptions. The first major project spearheaded by the Change Management Team is the Core Banking Transformation project that really puts the customer at the heart of the Bank's operations. The Bank will be investing in a state-of-the-art Core IT Banking programme and replacing legacy application which will significantly improve its operations by delivering a superior customer service. Additional benefits will include straight through processing, simplier access to information and services.

Several teams across the retail network have taken an initiative towards the communities in which they operate.
The spectrum of initiatives undertaken to date is quite broad and touches upon various aspects of community life.

The BOV Joseph Calleja Foundation has this year extended its support to sixteen scholars from Malta and Gozo.

BOV employees, family and friends participated in a warm up at BOV Centre before joining the rest of Malta and Gozo in the President's Fun Run.

ACTIVELY SUPPORTING OUR COMMUNITY

Bank of Valletta is the Maltese Bank. There is more to this than a catch phrase. Bank of Valletta has long realised that as an organisation with roots running deep into the community in which it operates, it cannot consider taking the back seat but must act responsibly.

Bank of Valletta's Community Relations programme is the executive arm of its CR values. The programme provides a framework through which the Bank supports various activities and initiatives within the Maltese society.

BOV is the patron of local arts and culture. Firm in its belief that local talent is an integral part of the Maltese identity, BOV supports exhibitions, concerts and national festivals that put Maltese culture in the limelight. The Maltese Bank also endorses the Maltese Tenor, Joseph Calleja. Together, they founded the BOV Joseph Calleja Foundation which to date supports sixteen scholars in realising their artistic career. Another aim of this Foundation is to use the therapeutic power of music to help the 'vulnerable child' in coming to terms with difficult day to day circumstances.

The Bank's philanthropic contributions are primarily channelled through the Marigold Foundation - BOV in the Community. Set up in 2014 as a voluntary and non-profit making organisation, it seeks to act as a platform accessible to all NGOs operating across Malta and Gozo. Its main goal is to provide them with a stronger voice, empowering them to reach further, whilst supporting them to ensure greater visibility and awareness with the general public about their visions and goals. In addition, the Bank participated in various initiatives, often with the full endorsement and involvement of its people, such as regular blood donation drives and dress downs, initiatives to support Pink October as well as the L-Istrina BOV Piggy Bank campaign which this year marks the 13th edition.

Heritage is another important concern. This year the project at Mellieha Sanctuary which the Bank has been supporting for the past three years came to an end, with the icon of the Mother and Child being restored to its former glory. Education features prominently in the BOV Community Programme and often works in tandem with other pillars. For instance, Discover Valletta is a collaboration between the Bank and Valletta 2018 Foundation, that sees Form 1 students receiving an MP3 player with stories about 24 locations in Valletta. Penned by Trevor Zahra, the stories are meant to encourage students to discover new elements in the capital city, along with hundreds of myths and legends.

The restored 14th century siculo-byzantinesque painting of Our Lady of Mellieha and Child was officially inaugurated by H.E. Fr Charles J Scicluna, Archibishop of Malta during a ceremony held at the Mellieha Sanctuary.

The highlight of this year's Teatru Manoel BOV Performing Arts Festival was Christopher Gluck's Orpée et Eurydice.

The Marigold Foundation helps our communities reach their utmost.

BOV renewed its support towards all the male and female senior football leagues in Malta and Gozo.

SUSTAINING OUR ENVIRONMENT

Ensuring that our business remains environmentally sustainable is a responsibility that the BOV Group does not shy away from. At Bank of Valletta, we are continuously evolving our business practices to reduce our environmental impact, by integrating green behaviours into our daily work practices as well as promoting environmental-friendly products such as the BOV Eco Loan.

The Bank's green approach is not a program with a finite date, but an ongoing commitment to consider the green stakeholder at a par with the interest of the other stakeholder groups.

This year saw Bank of Valletta planting no less than 1,000 trees and shrubs in two separate initiatives, both involving its people, as the Bank uses these initiatives to instil a green conscience in our people as well. As in previous years, the Bank also participated in the European Week for Waste Reduction, giving our people the opportunity to dispose of unutilised and unwanted electronic goods.

The Energy Audit as requested in Legal Notice 196 has been concluded. Meanwhile 15 branches across the Bank's retail network have received an Energy Performance certification issued by authorised engineering companies. The remaining branches will be certified over the coming months.

The Bank also continued to invest in photovoltaic cells at several sites, thereby saving 139,571 in CO_2 emissions over the past year. Its water conservation project continues to save 3,000,000 litres of water annually.

Working smarter in a manner that is sustainable is the way forward. The Bank will continue to identify opportunities and implement initiatives to keep track of its carbon footprint and henceforth work towards neutralising its carbon emissions.

The Bank's green efforts dovetail with team building - 50 plus BOV employees from across the Bank's Investment Centres, accompanied by their children, participated in a tree planting initiative at Fort Rinella.

Bank of Valletta's long working collaboration with Fondazzjoni Wirt Artna, responsible for the conservation of Fort Rinella, led to the inauguration of Soldiers of the Queen , an extensive exhibition showcasing the evolution of the British army during the rule of Queen Victoria.

Through L-Istrina BOV Piggy Bank campaign, school children are encouraged to help people in need by supporting the Malta Community Chest Fund in their small way.

CONCLUSION

Every year when we take stock of what we did, we realise that this is a journey that enriches the organiser the more CR values are integrated into its practices, policies and culture.

At Bank of Valletta, we genuinely believe that it is important for the organisation to play an active role in society on various levels and in different fora, not because it is obliged to, but because it is the ethical way of doing business, and we believe it is core to good corporate governance and concurrently to the BOV culture.

Directors' report as at 30 September 2016

The Directors present their 43rd Annual Report, together with the audited financial statements of the Bank of Valletta Group (the Group) and the Bank for the year ended 30 September 2016.

Principal Activities

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

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 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) as well as custodianship and trustee services.

The Subsidiaries

VFM provides management services for collective investment schemes. During the period under review, the Bank entered into a tripartite share transfer agreement with Insight Investment Management Limited (IIM) and VFM for the acquistion of IIM's 40% shareholding in VFM. As a result, VFM has become a fully owned subsidiary of the Bank.

VFS, is also a fully owned subsidiary of the Bank and provides fund administration services.

The Associates

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.

Operational Overview

A review of the business of the Group for the year ended 30 September 2016 and an indication of future developments are provided in the Chairman's Statement and the Chief Executive Officer's Review, which can be found in the front section of this Annual Report.

Dividends

A gross interim dividend of €0.0391 per share was paid on 27 May 2016. The Directors propose a final gross dividend of €0.0852 per share, resulting in a total gross dividend for the year of €0.1243 per share. The aggregate net dividend for the year is €0.0808 per share, amounting to €31.51 million (2015: €0.0744 net per share as adjusted for bonus issue resulting in a net payout of €29.02 million). The total dividend is analysed as follows:

	The Bank	
	2016	2015
	€	€
Gross	48,477,000	44,640,000
Tax at source	(16,966,950)	(15,624,000)
Net	31,510,050	29,016,000

Directors' report as at 30 September 2016 (continued)

Board of Directors

The following Directors served on the Board during the period from 1 October 2015:

John Cassar White
Alicia Agius Gatt *(resigned on 17 December 2015)*
Joseph Borg *(resigned on 17 December 2015)*
Roberto Cassata *(resigned on 17 December 2015)*
Barbara Helga Ellul *(appointed on 17 December 2015)*
James Grech
Mario Grima
Alfred Lupi *(appointed on 17 December 2015*)
George Portanier *(resigned on 16 September 2016)*
Taddeo Scerri
Gabriele Simonetti *(appointed on 17 December 2015)*
Joseph M Zrinzo

Directors' Responsibilities

The Directors are required by the Companies Act,1994 (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). 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.

During the period under review, the Board of Directors resolved to change the financial reporting date of the Bank from 30 September to 31 December. The objective is to align the Bank's financial year-end with that of the vast majority of its European counterparts. The financial year which started on 1 October 2016 will exceptionally have a duration of 15 months, ending on 31 December 2017. Thereafter, each financial year will commence on 1 January and will end on 31 December.

Auditors

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

Information pursuant to Listing Rule 5.64

The Bank has an authorised share capital of €500,000,000 divided into 500,000,000 ordinary shares with a nominal value of €1.00 each.

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

Following the approval of the shareholders of the Bank during the 42nd AGM held on 17 December 2015, on the 15 January 2016, the amount of €30,000,000 from the Bank's reserves were capitalised for the purpose of a bonus issue of 30,000,000 ordinary shares of a nominal value of €1.00 each fully paid up. Following this allotment, the issued share capital of the Bank increased from €360,000,000 to €390,000,000 divided into 390,000,000 ordinary shares with a nominal value of €1.00 each fully paid up.

At the forthcoming AGM, the Board of Directors is proposing a bonus issue on the 16 January 2017 of 1 share for every 13 shares held. This will result in the issue of an additional 30,000,000 shares and the increase in the issued share capital of the Bank from €390,000,000 to €420,000,000.

Directors' report as at 30 September 2016 (continued)

Clause 4 of the Bank's Memorandum of Association provides that, with the exception of existing large shareholders, presently the Government of Malta (25.23%) and UniCredit S.p.A. (14.55%), 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 3% of the issued share capital of the Bank. As at 30 September 2016, Malta Government Investments Limited, a fully Government owned entity, had a shareholding in the Bank of 0.48%.

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. As also explained in more detail below, shareholders with 10% or more of the shares in issue are entitled to appoint one Director for every 10% holding.

The Directors confirm that as at 30 September 2016, shareholding in excess of 5% of the issued share capital of the Bank was held directly by:

Government of Malta	25.23%
UniCredit S.p.A.	14.55%

There were no changes in shareholders holding 5% or more of the issued share capital up to 28 October 2016.

Pursuant to the Bank's Articles of Association, the appointment of Directors to the Board is reserved to the Bank's shareholders. Shareholders with 10% or more of the shares in issue are entitled to appoint one Director for every 10% holding, whilst the other shareholders are entitled to appoint the remaining Board members at the AGM (by means of an election, if applicable) in accordance with the provisions of the Articles of Association. Shareholders with 10% or more of the shares in issue are not entitled to vote or to aggregate any unutilised excess of votes over 10% to vote at the election. The appointment of the Directors is subject to regulatory approval.

The nomination of a candidate by a shareholder is to be seconded by a shareholder or shareholders holding at least 5,000 shares.

The rules governing the appointment and replacement of the Bank's Directors are contained in Articles 60 to 64 of the Bank's Articles of Association.

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

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 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 the AGM held on the 19 December 2012 and which term expires on the 18 December 2017. This authority is renewable for further periods of five years each.

There are no agreements between the Bank and the Directors on the Bank's Board providing for compensation on termination or cessation of their office for any reason whatsoever.

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 30 September 2016, information required under Listing Rules 5.64.5, 5.64.7 and 5.64.10 is not applicable to the Bank.

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.

Going concern – Listing Rule 5.62

The Directors, after due consideration of the Bank's profitability, liquidity, the statement of financial position, capital adequacy and solvency declare, pursuant to Listing Rule 5.62, that the Bank is in a position to continue operating as a going concern for the foreseeable future.

Directors' report as at 30 September 2016 (continued)

Shareholder Register Information pursuant to Banking Rule 7/2014

Directors' interests in the share capital of the Bank or in related companies as at 30 September 2016 are contained in the Corporate Governance Statement.

Number of shareholders analysed by range:

	28 October 2016	
Range of shareholding	**Total Shareholders**	**Shares**
1 – 500	1,081	294,408
501 – 1,000	2,023	1,501,226
1,001 – 5,000	8,293	23,451,613
5,001 and over	8,128	364,752,753
Total shareholding	**19,525**	**390,000,000**

Standard Licence Condition 7.60

Pursuant to Standard Licence Condition 7.60, it is hereby declared that during the reporting period, there were no breaches of Standard Licence Conditions or other regulatory requirements.

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 28 October 2016 and signed on its behalf by:

John Cassar White
Chairman

Mario Grima
Director

Capital & risk management report 30 September 2016

Section 1: Risk Management

1.1 Overview of Risk Disclosures

This Capital and Risk Management Report has been prepared for the BOV Group in accordance with the Additional Regulatory Disclosures as governed by MFSA Banking Rule BR/07/2014 (Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised under the Banking Act 1994) which follows disclosure requirements of EU Regulation No 575/2013 (Capital Requirements Regulation – CRR). These disclosures are aimed at providing further insight on the capital structure, adequacy and risk management practices.

The Bank publishes these disclosures on an annual basis as part of the Annual Report and Financial Statements in accordance with Article 433 of the CRR. As per banking regulations, this Capital and Risk Management Report is not subject to external audit, except to the extent that any disclosures are equivalent to those made in the Financial Statements which adhere to International Financial Reporting Standards (IFRS) as adopted by EU. Nonetheless, this Capital and Risk Management Report has been verified internally and was approved by the Bank's Audit Committee and the Board of Directors. The Bank is satisfied that internal verification procedures ensure that these Additional Regulatory Disclosures are presented fairly.

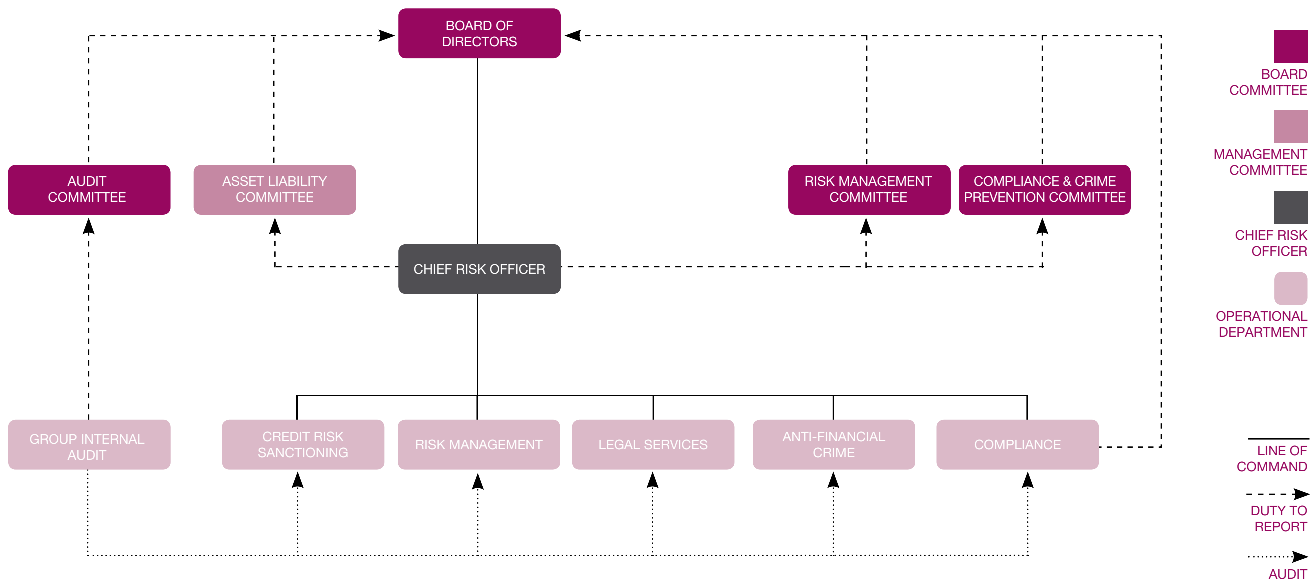
Since November 2014 the Bank, being a systematically significant financial institution, has been placed under the supervision of the Single Supervisory Mechanism (SSM). In compliance with Pillar II requirements of the CRD, the Bank prepares the Internal Capital Adequacy Assessment Process (ICAAP) on an annual basis. The Board of Directors and senior management strongly believe that the ICAAP will continue to act as an important contribution to the strengthening of the risk management practices and capital adequacy of the Bank.

1.2 BOV Risk Management Functions

The Bank assumes some risks consciously with the aim of managing them to achieve a return. Other risks are not taken on deliberately, but are the inevitable consequence of being a financial services provider. Within this context, the Bank's organisational structure is built upon a framework that promotes a transparent and efficient risk culture.

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. The second line is executed by the functions that oversee risks, namely Risk Management, Compliance and Anti-Financial Crime Departments; and the third line is executed by Group Internal Audit, which is the function that provides independent assurance to the Board. This means that responsibility for risk management resides at all levels within the Bank.

The Risk Management Department, within the second line of defence, falls under the responsibility of the Chief Risk Officer (CRO) who is responsible for the following departments: Credit Risk Sanctioning, Risk Management, Legal Services, Anti-Financial Crime and Compliance. The Bank's risk governance structure is represented below:



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 Board of Directors.

Capital & risk management report 30 September 2016 (continued)

The *Risk Management Department* is responsible for the overall risk management of the Bank. In order to ensure integrity, the risk control department operates independently of the Bank's business activities. This Department has a number of units, including:

- *Credit Risk Management Unit (CRMU)*. The Unit's 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. CRMU is responsible for the development and maintenance of the Credit Policy, which sets out the Bank's core values governing the provision of credit. The Unit is also responsible for measuring and managing asset quality in line with the prevailing banking rules.

- *Enterprise Risk Management Unit (ERMU)*. ERMU takes a holistic enterprise-wide view of the risks taken on by the Bank in carrying out its business and ensures that these are consistent with the overall risk appetite framework. It is a central unit which is responsible for the management of risk reporting, risk data governance and portfolio risk management. ERMU acts as the group's liaison with the Joint Supervisory team (JST). The Unit is responsible for regulatory and internal stress tests, including the periodic stress tests conducted by the European Central Bank (ECB) and/or by the European Banking Authority (EBA). The Unit is also actively involved in the compilation and submission of the ICAAP and ILAAP reports of the Bank.

- *Economics & Risk Research Unit.* The Unit brief includes the monitoring of the Bank's economic environment with special focus on the local and European economy. The Unit is responsible for conducting all mathematical, statistical and economic research that is required by the Bank.

- *Operational Risk Management Unit.* The core operational risk function is responsible to coordinate and oversee the identification, assessment, management and reporting of operational risks. The Unit is also responsible for the mitigation of operational risks events through the procurement of adequate and cost-effective insurance cover. The Unit is also responsible for the implementation of the Operational Risk Management Framework. In addition, the Unit has an information security function which analyses and communicates information security risks and evaluates their potential impact on the business processes.

- *Regulatory Advisory Services Unit*. The Unit brief includes the monitoring of the Group's regulatory environment with special focus on banking and investment regulation. The Unit also took a leading role during the finalisation of the Bank's Recovery Plan as required by Directive 2014/59/EU transposed into Maltese Legislation by way of Legal Notice 301 of 2015.

- *Risk Coordination Unit.* The objective of the Unit 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 the business unit.

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.

Anti-Financial Crime Department (AFCD). The function of this Department was previously carried out by the Compliance Unit. The AFCD's key role within the Bank's Enterprise Risk Management framework is that of acting as the Bank's second line of defence in relation to the prevention of money laundering and counter terrorism financing. The AFCD is responsible for the development and implementation of policies, procedures, systems and controls to counteract financial crime, money laundering, counter terrorism financing, bribery and corruption, and fraud. AFCD also ensures that the applicable sanctions are implemented. AFCD is the groups' liaison with the FIAU.

Compliance Department. This Department is responsible to ensure that the Bank and its subsidiaries operate 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 that mitigate reputational and conduct risk. It provides regular training on regulatory obligations and requirements emanating from internal policies and procedures.

A detailed description of the functions of the Board of Directors and the Management Board including the various Board and Management Committees is included in the section Corporate Governance Statement of Compliance on page 27 of the Annual Report and Financial Statements.

Capital & risk management report 30 September 2016 (continued)

Section 2: Capital Management

2.1 Capital Management and Forecasting

The prudent and efficient management of capital is one of the Group's top priorities and a fundamental objective of risk management. The role of capital is to provide the Group with loss-absorbing capacity and potential for growth. It is key to the Group's long-term sustainability. The Group's capital management approach aims to ensure a sufficient level of capitalisation to absorb unexpected losses from its risk exposures while supporting business growth and providing adequate return to shareholders. Capital management has clear Board visibility and is implemented primarily through the capital planning process that determines the optimal amount and mix of capital that should be held by the Group, subject to regulatory limits. Capital management is under the direct control of ALCO.

As part of the risk management process, capital buffers are continuously monitored by the Board of Directors, the Management Board and ALCO. Risk Management Department ensures that the Group is adequately capitalised in order to achieve the strategic objectives set by the Board of Directors while assisting ALCO in setting the capital management plan. The main aim of this exercise is to assess the level and quality of the capital buffer for the medium to long term.

The need to increase capital emanates from new regulations and more risk-sensitive capital models. The Bank's strategy is twofold: retain a greater proportion of distributable profit as reserves and increasing capital through equity and subordinated bond issues.

2.2 Regulatory Capital

The Group's capital base is composed of Common Equity Tier 1 (CET1) and Tier 2, as defined in Part Two of the Capital Requirements Regulation (CRR). In line with new regulations BOV is placing much of its emphasis and monitoring on CET1 capital. This capital is the highest form of quality capital, thus providing the greatest level of protection against losses.

The Group uses the Standardised Approach for credit risk, the Basic Indicator Approach for operational risk and the Basic Method with respect to the Group's foreign exchange risk. No capital is allocated for market risk as the Bank does not operate a trading book. For credit risk, risk weights for the Treasury Portfolio are determined by taking the worst credit rating 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. Under the Basic Indicator Approach for operational risk the Group allocates capital by taking 15% of the average gross income of the preceding three years. 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. In addition to the risks above, 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 line with the CRR, Banking Rule BR/15: 'Capital Buffers of Credit Institutions authorised under the Banking Act, 1994', requires additional buffers: capital conservation buffer; countercyclical buffer; other systemically important institutions (O-SII) buffer; and systemic risk buffer. These buffers are aimed to strengthen the resilience of the Group and have entered into force as from January 2016, with full application by January 2019. Automatic restrictions on capital distributions apply if the Group's CET1 capital falls below the level of its CRD IV combined buffer.

In line 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 & risk management report 30 September 2016 (continued)

Capital Instruments Main Features	BOV Ordinary Shares	5.35% BOV Subordinated Bonds 2019	4.8% BOV Subordinated Bonds 2020	3.5% BOV Subordinated Notes 2030 Series 1	3.5% BOV Subordinated Notes 2030 Series 2
Unique identifier	MT0000020116	MT0000021262	MT0000021270	MT0000021312	MT0000021320
Governing Law(s) of the instrument	Maltese Law	Maltese Law	Maltese Law	Maltese Law	Maltese Law
Regulatory Treatment					
Transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2	Tier 2	Tier 2
Post-transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2	Tier 2	Tier 2
Eligible at solo/(sub)consolidated / solo & (sub)consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated
Amount recognised in regulatory capital	390,000,000	27,068,493	48,405,479	66,920,500	44,670,400
Nominal amount of instrument	390,000,000	50,000,000	70,000,000	66,920,500	44,670,400
Issue Price	N/A	At par (€100 per bond)	At par (€100 per bond)	At par (€100 per bond)	At par (€100 per bond)
Redemption Price	N/A	At €100	At €100	At €100	At €100
Accounting classification	Share Equity	Liability-amortised cost	Liability-amortised cost	Liability-amortised cost	Liability-amortised cost
Original date of issuance	26 August 1992	15 June 2009	15 March 2010	14 December 2015	14 December 2015
Perpetual or dated	N/A	Dated	Dated	Dated	Dated
Original maturity date	N/A	15 June 2019	15 March 2020	8 August 2030	8 August 2030
Issuer call subject to prior supervisory approval	No	No	No	No	No
Coupons/dividends					
Fixed or floating dividend coupon	Floating	Fixed	Fixed	Fixed	Fixed
Coupon rate and any related index	N/A	5.35%	4.80%	3.50%	3.50%
Existence of dividend stopper	No	No	No	No	No
Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary	Mandatory	Mandatory	Mandatory	Mandatory
Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Mandatory	Mandatory	Mandatory	Mandatory
Existence of step up or other incentive to redeem	N/A	No	No	No	No
Noncumulative or cumulative	Non cumulative	Non cumulative	Non cumulative	Non cumulative	Non cumulative
Convertible or non-convertible	Non convertible	Non convertible	Non convertible	Non convertible	Non convertible
Write-down features	No	No	No	No	No
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.
Non-compliant transitional features	No	No	No	No	No

Subordinated bonds are included as part of Tier II Capital as they fully qualify for the provisions listed under CRR (575/2013) Part Two, Title 1, Chapter 4, Article 63. Specifically they 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 5.35% and the 4.8% Euro subordinated bonds are redeemable at par on 15 June 2019 and 15 March 2020 respectively thus the amortised amount was included in the Own Funds figure. During the financial year, the Bank issued more than €110 million in subordinated notes maturing in 2030 with an annual coupon of 3.5%. These notes qualify as part of Tier II capital.

Capital & risk management report 30 September 2016 (continued)

	€ ' 000
	Sep-16
CET1 capital	**589,602**
Common Equity Tier 1 capital: instruments and reserves	**663,385**
Capital instruments and the related share premium accounts	390,988
Retained earnings	232,559
Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under the applicable accounting standards)	35,333
Funds for general banking risk	4,505
Common Equity Tier 1 (CET1) capital : regulatory adjustments	**(73,783)**
Intangible assets (net of related tax liability) (negative amount)	(13,272)
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)	(6,991)
Amount exceeding the 17.65% threshold (negative amount)	(6,820)
of which : Deferred tax assets arising from temporary differences	(3,631)
of which: Significant direct and indirect holdings by the institution of the CET1 instruments of financial sector entities	(3,189)
Regulatory adjustments relating to unrealised gains and losses	(14,088)
Regulatory adjustments relating to Deferred Tax	9,699
Regulatory adjustments relating to significant investment in financial entities	2,129
Amount to be deducted from or added to CET1 capital with regard to additional filters and deductions required pre-CRR	(44,440)
TIER 2 Capital	**184,935**
Capital instruments and the related share premium accounts	187,065
Regulatory adjustments applied to Tier 2 in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out	(2,130)
TOTAL CAPITAL	**774,537**
TOTAL Risk Weighted Assets	**4,598,590**
of which deferred tax assets not deducted from CET1 capital	120,181
of which direct holdings by the institution of the CET1 instruments of financial sector entities not included in CET1 capital	105,554
Capital Ratios and buffers	
Tier 1 capital	12.82%
Total capital	16.84%
Capital Conservation Buffer	1.25%
O-SII Buffer	1.00%

Capital & risk management report 30 September 2016 (continued)

FULL RECONCILIATION OF OWN FUNDS ITEMS TO AUDITED FINANCIAL STATEMENTS

as at 30 September 2016

	Balance Sheet in accordance with IFRS (as adopted by EU) scope of consolidation	Effect of deconsolidation entities for regulatory consolidation	Balance Sheet in accordance with regulatory scope of consolidation
	€ 000	€ 000	€ 000
Called up share capital	390,000	-	390,000
Share premium account	988	-	988
Retained earnings	302,841	(43,273)	259,568
of which: expected final dividend	*21,598*		*21,598*
General banking reserve	*4,505*		*4,505*
Deposits compensation reserve	*44,440*		*44,440*
Revaluation Reserve	35,332	(112)	35,220
of which property revaluation reserve	*27,459*		*27,459*
of which unrealised gains/losses	*7,873*	*(112)*	*7,761*
Non-controlling interest	-		-
Intangible assets	13,272	-	13,272
Deferred tax arising from temporary differences	67,188	-	67,188
Subordinated liabilities	231,591	-	231,591
of which amortised amount	*187,065*		*187,065*

2.3 Capital requirements

The following table supplements the information on the standardised approach, mainly illustrating the capital requirement for credit risk split by the different exposure classes as well as capital for operational risk, foreign exchange risk, counterparty credit risk and Credit Valuation Adjustment (CVA).

As at 30 September 2016	Exposure Value (On + Off balance sheet net of value adjustments and provisions and post CCF)	Risk Weighted Assets	Capital Allocation
	€' 000	€' 000	€' 000
Credit Risk (Standardised Approach)			
Central government or Central banks	2,727,135	12,757	1,021
Regional Government and Local Authorities	326,746	68,346	5,468
Public sector entities	536,181	44,403	3,552
Multilateral Development Banks	172,137	-	-
Institutions	2,172,583	781,390	62,511
Corporates	1,402,811	1,033,291	82,663
Retail	564,476	363,289	29,063
Secured by mortgages on immovable property	2,519,941	1,204,986	96,399
Exposures in default	141,825	137,879	11,030
Items secured with particular high risk	67,762	79,256	6,340
Equity	83,316	67,604	5,408
Other items	386,936	360,430	28,834
	11,101,848	**4,153,630**	**332,290**
Operational risk (Basic Indicator Approach)		433,191	
Foreign Exchange risk (Basic Method)		341	
Counterparty Credit Risk and CVA		11,427	
Total Risk Exposure		**4,598,590**	

Capital & risk management report 30 September 2016 (continued)

2.4 Leverage Ratio

The leverage ratio was introduced into the Basel III framework as a non-risk-based backstop limit, to supplement riskbased capital requirements. Its purpose is to limit the leverage effects in the balance sheet as it is a volume based measure calculated as Tier 1 capital divided by total exposure calculated as the total on-balance sheet assets, plus off balance sheet exposures, such as undrawn commitments, less amounts permitted to be deducted for Tier 1 capital

A monitoring period has been allowed which runs till January 2017, during which time a minimum ratio of 3% should apply. The Group's leverage ratio is determined and monitored on a regular basis, and as at September 2016 stood at 5.34%.

Section 3: Credit Risk

3.1 The Nature of Credit Risk

Credit risk is the risk of suffering financial loss should any of the Bank's customers, clients or market counterparties fail to fulfil their contractual payment obligations. Credit risk also includes concentration risk. The latter arises through a high level of exposure to individual issuers or counterparties (single-name concentration) or a group of connected clients or a high level of exposure within industry sectors and geographical regions (sectorial concentration).

Credit risk is the most significant risk and represents the Bank's largest regulatory capital requirement. Considerable resources are dedicated by the Bank to manage it. Indeed, as at September 2016 the Bank allocated €332.3 million in regulatory capital for credit risk.

3.2 The Management of Credit Risk

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:

1. Maintain a framework of controls to ensure that credit risk-taking is based on sound credit risk management principles;
2. Identify, assess and measure credit risk clearly both on an individual facility level as well as on a portfolio basis avoiding undesirable concentrations;
3. Monitor credit risk while ensuring that risk-reward objectives are met.

The Bank adopts various measures to achieve the above. These include the application of:

a) High-level credit policies designed to facilitate the identification and mitigation of credit risk;
b) Lending guidelines defining the responsibilities of lending officers while holding them accountable for their decisions;
c) Limits on investment, settlement and contingent liability exposures by country and counterparty;
d) Independent reviews (hindsight overviews) of credit exposures;
e) Scoring systems which make use of quantitative modelling based on historical data to generate key predictive figures;
f) An internal rating system based on the counterparty's track record and ability to meet the agreed repayment schedule;
g) Large exposures and loan loss allowance policies in accordance with regulatory requirements;
h) High level reporting giving a holistic overview of the Bank's credit portfolio quality; and
i) Communication and provision of general guidelines including training on all credit-related risk issues, including regulatory changes, to promote consistency and best practice throughout the Bank.

3.3 The Mitigation of Credit Risk in the Loan Book

The main elements making up the internal control framework in respect of credit risk in the loan book are:

3.3.1 Credit Policy

The core values governing the provision of credit are contained in the Bank's credit policy, which is approved by the Board of Directors.

The credit policy is designed to ensure that all functions concerned with the provision of credit work together in a structured manner to achieve satisfactory, consistent and sustainable long-term performance, combining a growing loan portfolio with an acceptable level of credit quality and incidence of bad debts. The policy is underpinned by core principles related to compliance with the Bank's ethical standards, clear definition of responsibilities, the existence and implementation of procedures and thorough analysis of risks. It is rolled down in the form of specific policies tailored to each type of business, namely:

a) Business lending;
b) Consumer lending (Home Loans, Personal Lending and Credit Cards);
c) E-Commerce;
d) Trade finance; and
e) Property Lending.

Procedures for the consideration and monitoring of exceptions to each policy are included in the respective policy document.

Capital & risk management report 30 September 2016 (continued)

Policies are revised periodically to keep them abreast with ever changing market conditions. During this financial year, the focus was mainly on the review and update of the Business Lending Policy, primarily to fine tune processes following the credit reform launched last year.

During this year, the Bank launched the followng policies:

a) Property Lending policy - the main objective being the alignment of all forms of property lending to the Bank's risk appetite;
b) Code of Ethics and Conflicts of Interest Policy has been revised, with the section referring to lending practices updated; and
c) Related Party Transactions policy – for the proper management of related party transactions.

3.3.2 Decision-making Procedures

Last year the Bank embarked on the Credit Reform for business relationships held at Branches, Business Centres and Corporate Finance. This reform enabled the Bank to re-visit some of its practices to make the process more efficient and improved the governance around credit approval. During this year, Trade Finance, Home Loans and Recoveries were also included under the credit reform.

As a result of this credit reform, the Bank has two different functions relating to credit risk. These are the Credit Risk Management Unit (CRMU) and the Credit Risk Sanctioning Department (CRSD).

The main role of CRMU is to act as the monitoring arm of the credit risk function. CRMU aims to safeguard the soundness of the loan portfolio and to ensure sustainable and quality credit growth. It is also responsible for measuring and managing asset quality in line with the prevailing banking rules. The main responsibility of CRSD is to analyse customer requests submitted by business units and give their vote.

Lending Authority

A dual-voting system of lending authority has been put in place last year, governed by the Business Credit Policy, under which all business related lending decisions must be approved. New 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 above a certain limit, authorisation is sought from higher levels in the Bank hierarchy or from the Board of Directors.

During this year, the dual voting was also introduced in Trade Finance, Recoveries and for Consumer Lending exposures exceeding a threshold defined by the Bank. An exception to the rule applies for certain instances outlined in the Credit Policy where requests can be approved through a single vote from the Business side.

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 Management Board.

The dual voting system does not govern other Consumer lending for which a separate discretionary lending limits system applies, in the majority of cases aided 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 limit. 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.

Credit Analysis

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 default history of the sector.

3.3.3 Collateral

Credit risk mitigation 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.

The main types of collateral, including the type of properties accepted by the Bank are listed in the Credit Policy. The Bank is also categorising the collateral held whether movable or immovable as core and non-core.

Collateral is taken into account at forced sale value (the market value of all collateral items is subject to an appropriate haircut), and only accepted as the main source of repayment in property development loans and other exceptional cases. Otherwise, cash generated from operations is regarded as the primary source of repayment.

Capital & risk management report 30 September 2016 (continued)

3.3.4 Covenants

The Bank also mitigates credit risk through the adoption, on the sanctioning of facilities, 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. A breach of these covenants is an event of default which may permit a reduction of the maximum amount of borrowing under the commitment, increases in collateral, repricing and, in a worst case scenario, a call-in of facilities.

3.3.5 Reviews

The credit process provides for at least an annual review of business facilities granted. Review may be more frequent, as required by circumstances such as the emergence of adverse risk factors. Any consequent amendments to internal risk ratings must be implemented.

All credit exposures are regularly reviewed for objective evidence of impairment, either individually or as part of a collective assessment, with a view to taking early recovery action. In addition, hindsight overviews are carried out to strengthen the credit decision-making process, wherein the judgement of the initial decision-maker is reviewed to determine the extent to which that decision-maker was in compliance with Bank policies and procedures in approving the credit application concerned. CRMU carries out hindsight overviews and monitors corporate clients whose repayments are in arrears. The aim of this is to enable the quality of the lending portfolio to be properly and regularly monitored by an independent authority, so that any necessary remedial action can be taken.

Other measures and reviews are undertaken in the credit area to ensure that the Bank's asset quality is in order and in line with the prevailing banking rules. This also includes training to the staff.

3.3.6 Forbearance

Forbearance takes place when a concession is granted by the Bank to borrowers who are considered to be unable to meet the original terms and conditions of the contract due to financial difficulties. This can be due to changing market conditions, delays in receipt of funds from projects and other factors which are not linked to the customer's current or potential credit deterioration. Forbearance is normally granted to the borrowers to allow 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. Where a concession is granted for reasons other than financial difficulty the concession would not amount to forbearance.

A case by case approach is applied for all clients considering each transaction and client specific facts and circumstances. When the concession is due to financial difficulty the account is marked as forborne. As part of its asset quality measure, CRMU reviews the financial difficulty tests and take a final decision as to whether the facility is to be categorised as Forborne.

3.3.7 Rehabilitation Unit

The Bank set up a specialised unit to cater specifically for facilities which are undergoing a period of distress but which, with the appropriate nursing and advice by lending specialists, could be rehabilitated back to financial health.

The objective of this unit, which resides within Corporate Finance, is to provide in-depth monitoring, flexibility and support with the aim of achieving a turnaround with minimal losses while enhancing the relationship with the customer. Ultimately, the Unit acts as a half-way house. Once the account is rehabilitated the relationship will revert to Corporate Finance (or else in case of failure to the Remediation Unit or Litigation Unit).

3.3.8 Remediation Unit

The Remediation Unit has been set up with the primary scope of remediating problematic customer relationships and nursing them back to financial health, without resorting to legal action. This stage works on a framework similar to that engaged within the Rehabilitation Unit, with defined timelines for each relationship transferred.

3.3.9 Litigation Unit

When specific accounts become increasingly problematic and after the nursing of facilities has failed to produce the desired results, the relationship is transferred to Litigation Unit. Notwithstanding the extent of the deterioration on the performance of the facility, the primary aim of the Litigation Unit is to manage the problematic account with the objective of reinstating it to a 'going-concern' status, to be transferred back to the respective business unit.

The Bank's problem loan management process includes negotiation with customers, workout of remedial strategies, review of collateral and security documentation, and a final status report and review. However, in the event that recovery efforts fail, Litigation Unit will aim to maximise the amount recovered by the Bank through realisation of security.

When a loan is uncollectable, it is written off against the related allowance for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to the income statement.

A Write-Offs policy was launched during the year covering credit related write-offs. During this financial year, the Bank has also carried out a write-off exercise on non-performing loans wherein these loans were transferred off-balance sheet.

Capital & risk management report 30 September 2016 (continued)

3.4 Credit Risk Portfolio Management

Risk Management is responsible for monitoring the quality of the Bank's credit portfolio. As part of this process, ERMU presents regular risk reports to the Risk Management Committee, giving a holistic overview of the credit portfolio. This includes the analysis of the credit quality of the loan portfolio, reporting on arrears, concentration risk, business segmental analysis, expected loss and scenario analysis.

3.4.1 Internal Rating System

The Bank has a comprehensive internal rating system designed to accurately reflect the risk inherent in each lending relationship, identify problem loans in a timely and accurate manner and thereby assist in the creation of a quality loan book.

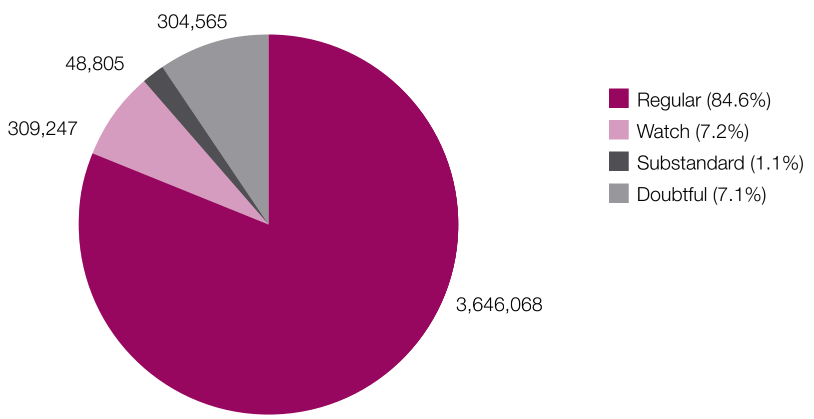
The Bank's loan portfolio is analysed according to the twelve grading levels within the internal credit rating system. These grading levels are then re-grouped into five categories - Regular, Watch, Substandard, Doubtful and Loss - for regulatory and high level internal reporting. The portfolio is further analysed from various aspects to determine any adverse movements which are then investigated and necessary mitigants applied.

The relative rating is primarily determined by the operating performance of the account and by other qualitative criteria. Exposures are analyzed on a regular basis to determine whether there is impairment in customer's business which merits a change in rating. For business related facilities, these criteria (both financial and business related) are reviewed at least once a year.

3.4.2 Advances Portfolio

The Bank's gross advances portfolio to customers stood at €4.31 billion as at end September 2016, representing an increase of €19.3million over September 2015. During this financial year, growth was driven by the increase in the home loan segment, while the business and the personal segments decreased. Tight control of the loan book and the dual sanctioned process resulted in an overall improvement in credit quality of the advances portfolio with 84.6% of the total portfolio classified in the regular category (81.3% as at end September 2015).

Asset Quality by Credit Grading as at Sep-16 (€'000s)



Doubtful loans decreased to 7.1% of the advances portfolio to customers as at end September 2016 compared to the 9.3% registered in the previous year. The decrease includes the results of the write-off exercise performed by the Bank in 2016. The non-performing loans ratio, in accordance with the Banking Rule BR/09 definition, stood at 4.7% of the loan portfolio to customers and banks as at end September 2016.

The Bank took a cautious approach and in line with the revised methodology used by the Central Bank of Malta increased its loan loss coverage ratio from 58.7% to 61%.

The advances portfolio has an average maturity of 17.9 years. Business loans have an average maturity of 9.8 years, home loans an average maturity of 26.8 years, while consumer loans have an average maturity of 7.2 years.

Capital & risk management report 30 September 2016 (continued)

The following tables show the advance portfolio broken by exposure classes as defined under the Capital Requirements Regulation (CRR) when using the standardised approach:

€ millions	within 3 months	between 3 months and 12 months	between 1 and 5 years	over 5 years	Total
Corporate	113	106	107	253	579
High Risk Areas	53	5	13	26	97
Exposure in default	121	11	28	89	249
Regional Government or Local Authorities	2	-	-	13	16
Retail	100	10	83	197	390
Secured by Real Estate Property	204	7	113	2,206	2,530
State/Public Owned Companies	21	-	28	399	448
Total	**614**	**139**	**372**	**3,184**	**4,309**

€ millions	Households & Individual	Financial and Insurance Activities	Wholesale & Retail Trade	Transportation and storage	Construction	Others	Total
Corporate	4	22	100	204	19	231	579
of which SME	-	10	64	130	15	85	304
High Risk Areas	-	-	-	-	84	13	97
Exposure in default	53	5	37	6	63	84	249
Regional Government or Local Authorities	-	-	-	-	-	16	16
Retail	275	3	40	6	8	57	390
of which SME	-	3	23	4	6	36	72
Secured by Real Estate Property	1,697	92	194	36	68	443	2,530
State/Public Owned Companies	-	285	-	23	-	140	448
Total	**2,030**	**407**	**371**	**275**	**242**	**983**	**4,309**

3.4.3 Non-Performing Exposures

The Bank defines non-performing exposures as those that satisfy either or both of the following criteria:

a) Material exposures which are more than 90 days past due;
b) The debtor is assessed as unlikely to pay 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.

The Bank‘s systems will downgrade exposures automatically and the Bank’s relationship officers monitor such exposures and discuss with the customers to potentially recoup the repayments.

3.4.4 Loan Loss Allowances and Coverage

The Provisions Committee is responsible for developing and maintaining the Bank’s provisioning methodology. It is composed of representatives from Finance, Risk and Credit with the latter attending as observers. Following last year’s revision of the provisioning methodology, the Bank kept working on the methodology to reflect the current economic scenario.

Specific Allowances covers two types of exposures:

(i) Impaired exposures on which the Bank does not expect to recover its exposure in full, even after the realisation of collateral.
(ii) Exposures which are deemed to carry a specific risk. Specific risks may vary from time to time and are determined by taking into consideration external and internal factors. External factors include market forces, the performance of specific economic sectors in relation to the gross value added within a particular period of time, and geopolitical circumstances. Internal factors namely include individual significance of exposures and/or day delinquency equal to or greater than 60 days.

Collective Allowances relate to performing exposures which are not deemed to carry any particular specific risk.

Probability of defaults (PDs) based on Moody’s Global Average cumulative Issuer-weighted Default rates 1983-2015 are used for the Bank’s portfolio with an increased weighting in the PDs for the calculation of specific risks provisioning. The loss given default rates are consistent for all exposures. Different rates apply for secured and unsecured portions of exposures.

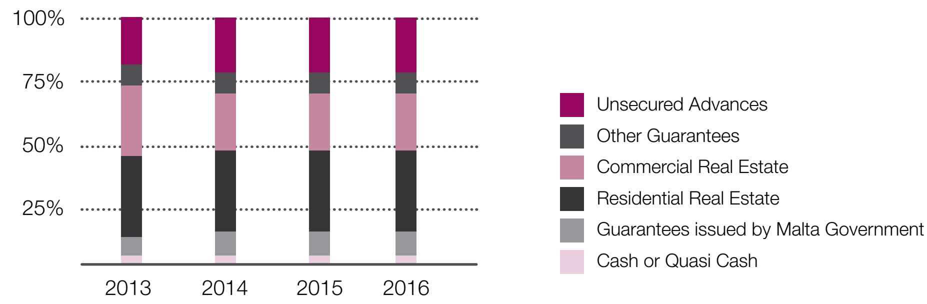
Capital & risk management report 30 September 2016 (continued)

The specific and collective allowances as at end of September 2016 are shown in the table below:

	Specific Allowance (including interest in Suspense)				Collective Allowance	
	Specific Risk		Impaired			
	Balance Sheet	P&L	Balance Sheet	P&L	Balance Sheet	P&L
	€000	€000	€000	€000	€000	€000
Business	(51,727)	(3,745)	(97,953)	24,609	(9,300)	1,930
Home Loans	(3,094)	(224)	(14,330)	3,039	(2,828)	588
Personal	(1,038)	(75)	(2,635)	702	(2,808)	584
Total	**(55,859)**	**(4,044)**	**(114,918)**	**28,350**	**(14,936)**	**3,102**

An analysis of the collateral cover reveals that 82.7% of the Bank's advances portfolio is covered by extendible security, out of which 76.8% is in the form of immovable property (residential and commercial).

Advances Coverage - Collateral Cover



3.4.5 Concentration Risk and Sectorial Overview

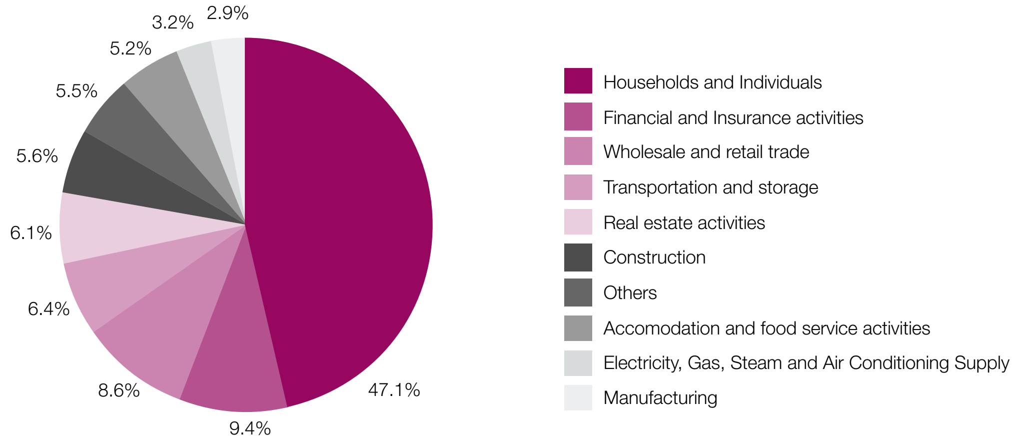
Given the size and nature of the domestic financial sector and the local economy, the Bank is exposed to concentration risk in its credit business. Concentration results when the Bank has a high level of exposure to a single name or to a related group of borrowers, to credit exposures secured by a single security, or to credit exposures with common characteristics within an industry sector.

The Bank's credit risk management approach is to avoid any undue concentrations in its portfolio. There are systems in place to identify material concentrations and to ensure adherence to prudential limits set by the Board of Directors and/or the Regulatory Authority to single borrowers or groups of related borrowers, and the Board and senior management are regularly informed on the concentration of the Bank's lending and investment portfolios. Managing industry and country risk is a key component of the Bank's overall concentration risk management approach. In order to measure its sectorial concentration, the Bank has revised its model to apply the Bank of England concentration risk model in which a capital add-on (%) is applied to the Herfindahl-Hirschman Index (HHI) calculated using risk-weighted assets.

Single name exposures exceeding 10% of Group's own funds are reported individually and are monitored on a continuous basis. These exposures are also reported to the Regulatory Authority. The aggregate of the single name exposures exceeding 10% of Own Funds corresponds to 1.1 times the Group's capital base calculated in accordance with CRR.

As at end September 2016, without taking into account the 'Household and Individuals', the Bank's advance portofolio is well diversified with 'Finance & Insurance Activities' counting for 9.4%, 'Wholesale & Retail Trade' at 8.6% and 'Transportation & Storage' presenting 6.4%. From previous year, the concentration by economic sectors has remained stable. As at end September 2016, the concentration of the Bank's advance portfolio is as follows:

Sectorial Concentration - Advances (% of total)



Capital & risk management report 30 September 2016 (continued)

3.4.6 Home Loans

The Bank exercises strict monitoring on the home loans segment, being the largest sector within the credit portfolio, accounting for 42.6% of total balances. The Bank has in place a specific policy dealing with home loans which sets lending parameters and criteria to ensure the good quality. These criteria revolve around capping on loan-to-value and repayment-to-income ratios. The home loans segment is healthy with only 2.6% classified as doubtful.

3.5 Focus on Training and Cultural Awareness

One of CRMU's high priority objectives is the instilling of cultural awareness on quality lending through training, sharing of information and setting up of workshops both on CRMU's own initiative and jointly with the credit function. CRMU is highly involved in the training of bank lending officers, both at the junior and more senior levels.

3.6 Settlement Risk

Settlement risk arises in any situation where a payment in cash or other financial instruments is made in expectation of a corresponding receipt in cash or other financial instruments. Daily settlement limits are established per counterparty to cover the aggregate of all settlement risks arising from the Bank's market transactions on any single day. Settlement Risk is mitigated through settlement limits assigned to counterparties or by effecting payment on a "delivery versus payment" basis.

3.7 Credit Risk in the Investment Portfolio

The Bank is exposed to credit risk through its investment activities. These investments include deposits with banks, debt securities, equities, and derivative financial instruments but exclude any working balances such as balances with the Central Bank, current and call accounts. The investment portfolio is managed by the Treasury Department and it is the Bank's strategy to buy and hold these instruments till maturity rather than for trading purposes.

Credit risk in the investment portfolio is mitigated through limits set in the Bank's Treasury Management Policy (TMP). The Bank sets limits 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. Limits on the level of credit risk applicable to different ratings are reviewed and approved by the Board of Directors at regular intervals.

The Bank only enters into investment transactions with authorised counterparties, and invests in financial instruments of a credit quality that falls within specific parameters stated in the TMP. Actual exposures are monitored against limits on an on-going basis, while changes in credit ratings and future outlook are monitored daily. Every quarter, ERMU also monitors closely the Credit Default Swap (CDS) movements of the largest counterparties in the investment portfolio, since a general increase in CDS would normally lead to a widening of credit spreads which in turn implies a decline in the market values of securities.

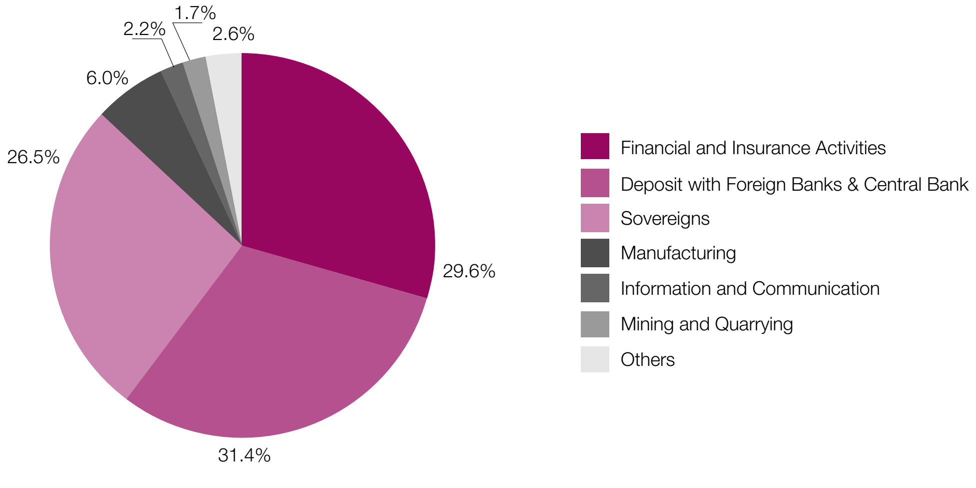
At year end, the Bank's investment portfolio is made up of good quality instruments with 97.63% being of an investment grade (September 2015: 98.38%).

3.7.1 Concentration of Credit Risk in the Investment Portfolio

The Bank's investment portfolio may also be exposed to concentration risk derived from excessive reliance on the same country, counterparty, sector or currency. The TMP has a number of limits set as guidelines aimed at controlling concentration risk. The policy also specifies in detail the appropriate action to be taken in case of a breach of limits. The Board and senior management are regularly informed on the concentration of the Bank's portfolio through reports prepared on a quarterly basis. In line with the large exposure directive, the Bank has no exposure to a single counterparty which exceeds 25% of the Group's regulatory capital. The HHI is also used to measure the concentration risk on the investment portfolio.

The chart below shows the sectorial concentration in the Bank's investment portfolio.

Sectorial Concentration - Investment



Capital & risk management report 30 September 2016 (continued)

3.8 Counterparty Credit Risk on Derivatives

Counterparty credit risk arises from over-the-counter (OTC) derivatives and is the risk that a counterparty to a transaction may default before completing the satisfactory settlement of the transaction. An economic loss occurs if the transaction or portfolio of transactions with the counterparty has a positive economic value at the time of default.

The Treasury Management Policy (TMP) limits the use of derivatives to hedge a balance sheet position, satisfy customers' requests and for the use of structured wealth management products. Counterparty risk related to derivatives is subject to prior approval from the appropriate sanctioning authority as stipulated by the Bank's policies. Derivative instruments must be denominated in the local currency or in hard foreign currencies.

Wrong way risk arises when the probability of default of a particular counterparty is positively correlated to the exposure with the same counterparty, so that the mark-to-market exposure increases at the same time as the riskiness of the counterparty increases. Wrong way risk is addressed by the Bank through the setting up of internal limits and its collateral management procedure. The TMP, which sets the limits on the maximum exposures held in derivatives, assumes that the business relationship with most counterparties is an on-going one; therefore the limits are primarily based on the most conservative long-term credit rating of the counterparty. For requests falling outside the TMP, these are also reviewed by CRSD and approved by the Chief Risk Officer or the Board of Directors according to the exposure. Limits are reviewed annually or more frequently in the event of a downgrade of the counterparty.

Prior to effecting a transaction, the Bank ensures that an ISDA agreement with respective counterparties is in place 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. It is the Bank's policy to revalue all traded transactions and associated collateral positions on a regular 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.

To measure the derivative exposure value in accordance with CRR article 271 the Bank uses the mark-to-market method where the exposure value is taken as the sum of current replacement cost and potential future credit exposure, taking into consideration the netting arrangement in place as per CRR Article 298.

Section 4: Market Risk

4.1 The 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 rates, credit spreads and foreign exchange rates. It arises from both customer and discretionary business and is managed by a variety of different techniques.

The discretionary investment portfolio consists mainly of debt securities and is managed by Treasury Department. The Bank's strategy is to manage these instruments as an investment portfolio rather than as a trading portfolio. The Bank's exposure towards the trading book is null and it is therefore exempted from the trading book capital requirements as set by the CRR.

4.2 The Management of Market Risk

The objective of the Bank is to manage and control market risk exposures in order to optimise return and minimise risk. Market risk is subject to strict controls under the TMP, which sets out the markets and instruments in which risk can be assumed, the types of positions which can be taken and the limits which must be complied with. The TMP also sets out the hedging policy, and also the pricing and validation policy.

ALCO regularly reviews high level market risk exposures and also makes recommendations to the Board of Directors concerning the overall market risk appetite and market risk policy. Exposures at lower levels of delegation are monitored at various intervals according to their volatility. ERMU regularly monitors the levels of exposures compared to set limits and where appropriate, escalation procedures are in place.

4.3 The Mitigation of Market Risk

The main tools used by the Bank to mitigate market risk are:

4.3.1 Treasury Management Policy

The Bank's appetite for market risk is articulated in the Treasury Management Policy (TMP), which is approved by the Board of Directors. The Bank manages market risk through limits set in the TMP which assigns limits on the basis of credit ratings assigned by eligible External Credit Assessment Institutions, comprising Fitch, Moody's and S&P. The policy is reviewed at least annually by ERMU in co-ordination with Treasury Department, and is approved by ALCO and the Board of Directors.

Capital & risk management report 30 September 2016 (continued)

4.3.2 Hedging Instruments

Limits on interest rate and currency positions are laid down by the TMP. Positions resulting from trading activities which exceed these limits are closed either by entering into equal and opposite trades, or through the use of derivative instruments, mainly interest rate swaps and forward currency exchange deals. Credit risk is not hedged but monitored though limits set in the TMP, which also lists the types of approved derivative instruments that may be entered into for hedging purposes.

4.3.3 Investment Authorisation

A 'four-eye' approach is applied when an investment proposal falls outside the criteria set out in the Bank's TMP. CRSD undertakes an independent analysis of proposals which are then approved by the Chief Risk Officer or the Board as appropriate.

4.3.4 Review of Limits

All credit exposures are regularly reviewed upon changes in credit ratings or outlook with a view to taking early mitigating action. When there is a change in rating and in the outlook, CRSD undertakes an independent analysis, which is then presented to the Board. Exposures which are above TMP limits are reviewed annually by Treasury in order to reassess the credit risk and align the investment criteria as necessary.

4.4 Interest Rate Risk in the Banking Book

Interest rate risk is defined as the current or prospective risk towards a bank's financial position arising from unfavourable movements in interest rates. The Bank's exposure towards the trading book is null and it is therefore exempted from the trading book capital requirements as set by the CRR. BOV is exposed to Interest Rate Risk in the Banking Book (IRRBB), arising from the mismatch between interest sensitive assets and liabilities held in the banking book.

The Bank has a detailed Interest Rate Risk Policy which clearly describes the approaches in which the Bank identifies, evaluates, monitors, manages, and reports its interest rate position. The policy also outlines the structure, responsibilities, and controls to manage and oversee the interest rate positions of the Bank.

The Board of Directors 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 ALCO is the main forum wherein, on a monthly basis, the exposure to interest rate risk is monitored and evaluated. ALCO assesses this risk with the objective of limiting potential adverse effects of interest rate movements on net interest income and on equity.

4.4.1 The Measurement of Interest Rate Risk

Risk management processes are in place to control and limit the interest rate risk exposure without negatively affecting the profitability of the Bank. The Bank considers a dual, yet complementary perspectives in the process of controlling and assessing IRRBB. These include the earnings perspective and the economic value perspective.

Impact of Interest Rate Risk through the Earnings Perspective

Changes in the interest rates effect 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. The Bank uses the following techniques to measure the effect that changes in interest rates have on net interest margins:

a) Monitoring of Effective Rates

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

In order to remain within the Bank's guidelines, the Bank consciously chooses low risk/return treasury assets in order to retain high quality of the portfolio. In fact throughout this financial year, the rate on the ECB's marginal lending facility has been lowered 0.25% while the rate on the deposit facility has been lowered to -0.40%. In addition such rates are expected to remain at present levels for an extended period of time.

b) 100bp parallel shift in the yield curve

The Bank also monitors the sensitivity of the financial assets and liabilities to parallel shifts in the yield curve of 100 basis points over a time horizon of one year.

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. An interest rate gap analysis provides for the detection of interest rate risk by concentration in maturities. As at September 2016, the interest gap amounts to €24.5 million as per note 39.4.1. Matching assets and liabilities are offset against each other to close the repricing gaps. As guided by ALCO, the factors affecting interest margin shall be mitigated by appropriate hedging strategies, wherever possible.

Capital & risk management report 30 September 2016 (continued)

Impact of Interest Rate Risk through the Economic Value Perspective

Variations in interest rates affect the present value and timings of future cash flows change. This in turn changes the underlying value of the Bank's assets, liabilities and off-balance sheet items. For this reason, movements in interest rates not only have an effect on the net interest margin, but also on the economic value effect on the Bank.

a) 200bp parallel shift in the yield curve

The balance sheet is asset sensitive, in that when interest rates move up a gain is posted in the accounting income statement, however an economic loss is made due to the fact that net cash flows derived from the balance sheet are discounted at higher rates. In order to calculate the capital allocation needed for IRRBB, the Bank carries out a sensitivity analysis based on a parallel shift of 200 basis-points throughout a time spectrum on a proxy of modified duration of positions situated at the middle of each time band and yielding 5%. As at September 2016 this amounts to €16.6 million as per note 39.4.1.

b) Modified Duration – Treasury Assets

The modified duration is a measure of the price sensitivity to yields. The Bank monitors and manages the modified duration of the treasury portfolio to ascertain that it does not reach uncomfortable and undesired levels. By calculating the Modified Duration, the Bank estimates the impact on P&L and capital as a result of changes in the market values of securities in the treasury portfolio and in the interest rate swaps entered into to hedge the interest rate risk in response to a parallel shift in yields of 100 basis points. As at September 2016 the Modified Duration impact on P&L amounts to (€1.8m) and the impact on capital amounts to (€10.6m) as per note 39.4.1.

The Modified Duration does not represent a forecast of potential losses in the portfolio but rather an analysis of how the market value of the treasury portfolio may change in response to a change in interest rates. In addition, the Bank calculates the modified duration on the unhedged fixed securities which are marked to market by major currencies.

Currency Risk

The Group is exposed to adverse movements in foreign currency exchange rates on its financial position and cash flows. The TMP sets limits on the level of net exposure by currency, which limits are monitored daily.

Equity Risk

Equity risk arises from exposures to fluctuations in equity prices. The TMP sets a limit to holdings in this asset class, which is held for proprietary purposes.

Scenario Testing

In addition to the Modified Duration, other measures are simultaneously being implemented to enable the Bank to exercise greater risk control over its investment portfolio. One of these measures is scenario analysis, which assesses the resilience of the portfolio to extreme but plausible scenarios. The scenarios either capture stressed past events or else plausible future scenarios that are unrelated to past events. In order to carry out this stress testing, the Bank makes use of the Moody's default tables for Corporates and Sovereigns (1983-2015). A further one notch downgrade is applied under the adverse scenario. The testing is done to stress test the resilience of the portfolio and it does not represent a forecast of potential losses in the portfolio.

Results for scenarios, which are expressed in terms of impact on the Common Equity Tier 1 capital, are reported to the Risk Management Committee on a regular basis. The results show a strong investment portfolio that is able to withstand extreme shocks.

Modified Duration Tier 1 as at end September 2016 is 12.8%	Baseline Change in Tier 1	Adverse Change in Tier 1
Parallel shift in yields on the investment portfolio (mitigated by IRSs)[1]	-0.23%	-0.46%
Expected default on the investment portfolio[2]	-0.26%	-0.31%

[1] This entails a parallel shift in yields of 100bps under the baseline and 200bps under the adverse.

[2] The Moody's default tables for Sovereigns and Corporates (1983-2015) under the baseline and a further one notch down grade in the case of the adverse scenario.

Capital & risk management report 30 September 2016 (continued)

Section 5: Operational Risk

5.1 The Nature of Operational Risk

BOV defines operational risk as the risk of potential losses that arise from inadequate or failed internal processes, people and systems or from external events. The Bank's objective is to contain operational risk within acceptable risk tolerance levels. This is achieved through early identification and measurement of risks, monitoring and mitigation by recommending changes to improve controls, performance and procedures, as well as by the procurement of appropriate insurance cover.

5.2 The Management of Operational Risk

The Operational Risk Management Unit (ORMU) is responsible to develop and implement policies and procedures to ensure that operational risks are managed effectively. Although ownership and accountability for operational risk resides with the business level, the ORMU co-ordinates, supervises and drives forward the identification, assessment and monitoring of operational risks and controls. Operational risks within the Group are covered by BOV's Operational Risk Management Framework (ORMF) which was approved by the Board. The ORMF includes risk identification, loss database, key risk indicators (KRIs) and business continuity management (BCM). The Reputation Risk policy was launched during this financial year to establish an effective structure for managing the Group's reputation and to protect the Group's name and goodwill.

ORMU supports the business units in identifying and assessing the operational risk exposure. Risk assessments involve risk identification, risk evaluation and recommendations for managing and mitigating the risks. For the risk identification process, the Bank uses Audit findings, internal loss data analysis and process mapping. The Bank is also compiling a Group Risk Register. A loss database has been created and maintained since 2009 and is updated regularly through risk event reporting on internal loss events and near misses. KRIs and thresholds have been identified at generic enterprise-wide level and are reported regularly. Business Continuity supporting documentation at unit level is in place throughout the organisation. A BCM programme is maintained and the Group is implementing a robust enterprise-wide Business Continuity Plan (BCP). BCPs for critical activities and IT systems are regularly tested, thus ensuring timely response to disruptions and effective restoration. The Group's Incident Management Team works in liaison with the ORMU to effectively manage the organisation's efforts where widespread threats require a more coordinated approach.

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 September 2016 is €34.66 million (Notional Risk Weighted Assets €433.19 million).

5.3 Mitigation of Operational Risk

BOV addresses identified risks where these are not aligned with stated risk appetite by improving processes, investing in technology changes and where necessary tackling human resource vulnerabilities. As part of its BCP BOV maintains and periodically tests contingency facilities to validate the effectiveness of the plan in the event of a disaster. It also mitigates the possibility of higher impact risk events through comprehensive insurance coverage on selected business risks. Insurance cover is under on-going review by a specialised team within ORMU, which works in close liaison with the Group's Insurance Brokers and the different business units.

5.4 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 applies various international standards in its integrated approach, which has the fundamental objective of ensuring the confidentiality, integrity and availability of its information assets.

In order to fulfil the proper handling of information and prevent loss or leakage of information, the Group has developed a number of qualitative measures to reduce such risks through its organisational structure, with officials having specific responsibilities for information security issues, the establishment of information security policies, procedures and standards, awareness training and the implementation of a security infrastructure and systems to ensure a stable information security environment. The approach to the management of information security risks is in line with global standards, in particular ISO 27001. During this financial year, the Information Security Policy has been reviewed and updated extensively, establishing a framework of governance and accountability for information security within the Group.

5.5 Remuneration Policy

The Bank has in place a Remuneration Policy with the aim of 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 Management Board, in accordance with regulation incorporated in the Capital Requirements Directive. Additional disclosure on the governance process related to remuneration has been made under the Remuneration Report section in the financial statements for 2016.

Capital & risk management report 30 September 2016 (continued)

The target population defined as Identified Staff for the purposes of this Disclosure represents 3.8% of total number of employees in the Group. Identified staff was determined in line with recommended EBA Regulatory Technical Standard[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 aggregated and 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. On average the ratio of variable to fixed remuneration for Identified Staff is 3.24%.

Remuneration of Identified Staff

	Supervisory Function^	Management Function^	Investment Banking^	Independent Control Functions^
Management Body	12	7		
Number of identified staff			7	9
Total fixed remuneration (in Eur)	€ 267,298	€ 578,142	€ 389,501	€ 497,511
Total variable remuneration (in Eur)*	Nil	€ 12,000	€ 9,726	€ 14,006
	Retail Banking^	**Asset Management^**	**Corporate Functions^**	**All Others^**
Number of identified staff	15	1	11	2
Total fixed remuneration (in Eur)	€ 934,799	€ 78,331	€ 671,445	€ 117,223
Total variable remuneration (in Eur)*	€ 44,819	€ 2,500	€ 26,750	€ 4,760

**excludes severance payments*
^as defined in EBA guidelines EBA/GL/2014/8

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 year. 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 and members of the Management Board as highlighted under the Remuneration Report.

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 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 measures.

[1] EBA Final Draft Regulatory Technical Standards EBA/RTS/2015/09 dated 16 July 2015
[2] EBA Guidelines on the renumeration benchmaking exercise EBA/GL/2014/08 dated 16 July 2016

Capital & risk management report 30 September 2016 (continued)

Section 6: Liquidity Risk

Liquidity risk is the risk that a bank is unable to meet its expected current or future payment obligations when they fall due and to replace funds when they are withdrawn, even when this occurs unexpectedly. To this end, the objective of the Bank's liquidity risk management is to ensure that all cash flow obligations can be met when due and at a reasonable cost.

The Bank mitigates liquidity risk by maintaining a sufficient fund of liquid assets. The Bank has been successful in its drive to build and maintain a large and stable customer deposit base, helping to eliminate any reliance on wholesale funding.

In the interest of ensuring that maturing funds are always available to meet expected cash demand, the Bank sets parameters within which maturities of assets and liabilities may be mismatched. For this reason, on a monthly basis the group's liquidity gap is analysed.

Currently the Bank has excessive liquidity buffers mainly arising from the marked increase in deposits. In this regard, ALCO continued analysing on a regular basis the best way to utilise the excess liquidity.

Complementing the above, liquidity risk is also mitigated through adequate measures found in the:

- **Treasury Management Policy (TMP)** states the Risk Appetite of the Bank. It sets out limits and controls that ensure a highly liquid investment portfolio.

- **Liquidity Risk management Policy** outlines the liquidity management framework of the Bank developed to identify, evaluate, monitor, manage and report the Bank's liquidity position. The policy also outlines the governance and controls available to manage liquidity risk and oversee the liquidity position of the Bank.

- **Internal Liquidity Adequacy Assessment Process (ILAAP)** designed to ensure that the Bank has a robust liquidity risk management and to demonstrate the Bank's overall liquidity adequacy. The document contains detailed qualitative and quantitative information of the Bank's processes and methodology used to measure and manage liquidity and funding risk. The assessment aims to ensure that the Bank has sufficient liquidity to ensure that liabilities are met in both normal and stressed scenarios. This document is reviewed by the ECB and MFSA.

- **Contingency Funding Plan** sets out the strategies that will be activated in case of excessive liquidity demand. It includes an outlined process and action plan for responding to severe disruptions to a bank's ability to fund some or all of its activities.

6.1 The Management of Liquidity Risk

The management of liquidity risk within the Bank is the responsibility of the ALCO. This committee maintains an ongoing oversight of actual and forecasted cash flows, by monitoring the availability of funds to meet commitments. BOV maintains a portfolio of highly marketable assets that can easily be liquidated. Furthermore, ALCO also ensures that there is a wide diversification of funding sources, across various maturity bands.

The Bank utilises techniques that help to evaluate the resilience of its liquidity buffers and to maintain a constant state of readiness should an exceptionally high demand for liquidity arise at any time.

- **Early warning signals**
  On a daily basis, Treasury Department addresses its available liquidity resources and compiles a forecast that serves as an early warning indicator in the identification of abnormal liquidity activity.

- **Access to the funding market**
  Diversification of the Bank's funding profile is an important element of the liquidity risk management framework. Even though the Bank has excess liquidity, Treasury Department ensure that market access is managed and tested.

  The Bank maintains an ongoing presence in funding markets and taps into as many unsecured credit lines to maintain a strong inter-bank relationship with the fund providers. This is mostly done within the European market. Treasury has a number of Global Master Repurchase Agreements with foreign banks in place that provide access to repo borrowing.

  The Bank has also recently raised funds from the local corporate bond market through the issuance of subordinated notes.

Capital & risk management report 30 September 2016 (continued)

6.2 The Measurement of Liquidity Risk

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. In fact, ALCO monitors the Bank's liquidity gap on a monthly basis. ALCO also maintains an on-going oversight of forecast and actual cash flows, by monitoring the availability of funds to meet commitments associated with financial instruments.

On a monthly basis, the following risk indicators are presented to ALCO in order to evaluate the resilience of the Bank's liquidity position and to maintain a constant state of readiness should an exceptionally high demand for liquidity arise at any time.

- **Loan-to-Deposit ratio (LtD)**
  The LtD ratio assesses the Bank's liquidity position by dividing the bank's total advances by its total deposits. The LtD ratio (net of interest in suspense) has been on the decline throughout this year, thus during the month of September 2016 the LtD increased slightly and stood to 46.3% (September 2015 49.2%) This shows that the Bank kept its highly liquid position during FY 2016, with its loan portfolio fully funded by deposits and with no dependence on the wholesale market. The decrease in the LtD ratio was the result of a significantly higher rise in customer deposits when compared to the increase in the lending portfolio. The Group maintains a stable base of "core deposits".

- **Liquidity Coverage Ratio (LCR)**
  The LCR requires credit institutions to hold sufficient unencumbered high quality liquid assets (HQLA) to withstand severe liquidity outflows 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, which may result in its liquidity coverage ratio falling temporarily below the 100% level.

  As at September 2016 the Bank's calculated LCR in line with the EU delegated act regulation stood at 131%. This is above the minimum level of 100% which will be required at EU level when the rule is fully implemented in 2019.

- **Net Stable Funding Ratio (NSFR)**
  The NSFR is defined as the amount of available stable funding relative to the amount of required stable funding. The NSFR is subject to an observation period and shall be introduced as a binding minimum standard in 2018.

  Albeit it is not yet a binding regulatory standard, the Bank already calculates the NSFR whose results indicate that the institution meets and exceeds the 100% threshold. The Bank officially reports the LCR and NSFR to the Regulatory Authorities on a quarterly basis and also participated in the Basel III Quantitative Impact Study (QIS) exercise, which is repeated semi-annually.

Section 7: Life Assurance Risk

7.1 The Nature of Life Assurance Risk

Life assurance risk is assumed and managed by MSV Life plc (MSV), which is jointly owned by Bank of Valletta plc and Mapfre Middlesea plc.

Life assurance risk includes the volatility in the amount and timing of claims caused by unexpected changes in mortality and the variability in contract holder behaviour (lapse risk). Mortality risk is the risk of deviations in timing and amounts of cash flows (premiums and benefits) due to the incidence or non-incidence of death. Lapse risk is the risk of loss or adverse change in liabilities due to a change in the expected exercise rates of policyholder options. Life assurance risk is also manifested in expense risk. Expense risk arises from the variation in the expenses incurred in servicing insurance contracts.

The amount at risk on each life assurance policy is the difference between the sum assured and the reserve held. On a portfolio basis, the principal risk is that actual claims and benefit payments exceed the carrying amount of the insurance liabilities. This could occur due to the frequency or severity of claims being greater than estimated. Insurance events are fortuitous, and the actual number and amount of claims and benefits will vary from year to year from the estimate established using statistical techniques.

7.2 The Mitigation of Life Assurance Risk

7.2.1 Risk Governance

MSV's Risk Management Framework is a set of policies, processes and reporting procedures necessary to identify, measure, monitor, manage and report, on a continuous basis, the risks to which MSV is or could be exposed, as well as their independencies.

MSV operates a 'three lines of defence model'. All the key functions, as defined under Solvency II, namely Actuarial, Risk, Compliance and Internal Audit are well established. These functions represent the second and third line of defence. All functions have the required regulatory standing and independence to be able to discharge their respective duties and responsibilities. The Risk and Compliance functions have direct access to the Risk and Compliance Committee while the Internal Audit function reports directly to the Audit Committee. These committees meet on a quarterly basis with their remit specified in the respective terms of reference.

Capital & risk management report 30 September 2016 (continued)

7.2.2 Underwriting Strategy

Statistically the larger the portfolio of similar insurance contracts, the smaller the relative variability about the expected outcome. In addition, a more diversified portfolio is less likely to be affected across the board by a change in any subset of the portfolio. MSV has developed its insurance underwriting strategy to diversify the type of insurance risk accepted and to leverage on our reinsurer's experience, knowledge and insight in terms of underwriting requirements. Medical selection is also included in MSV's underwriting procedures with premiums varied to reflect the health condition and life expectancy of applicants.

Factors that aggravate insurance risk include lack of risk diversification in terms of type and amount of risk, and lack of geographical spread. MSV is largely exposed to insurance risk in one geographical area - Malta.

7.2.3 Reinsurance

MSV uses reinsurance to cover death claims. The type of reinsurance cover and the level of retention for each risk are based on MSV's internal risk management assessment, which takes account of the nature of the risk covered and the sum assured. The reinsurance programme is approved by the Board annually. The reinsurance arrangements in place include a mix of treaty, facultative and excess of loss catastrophe protection, which limits the liability of MSV to any one individual life or event.

Section 8: Risk Management in Subsidiary Companies

The Group has two subsidiaries: Valletta Fund Management Limited (VFM) and Valletta Fund Services Limited (VFS).

VFM was set up in 1995 and as from 17 August 2016 is a fully owned subsidiary of Bank of Valletta plc. following the acquisition by Bank of Valletta plc. of the 40% shareholding held by Insight Investment Management (Global) Limited.

VFM is licensed by the Malta Financial Services Authority to provide investment services and to operate as a 'Maltese Fund Management Company' in terms of the Investment Services Act (Marketing of UCITS) Regulations (Subsidiary Legislation 370.18). VFM has three regulatory functions; Asset Management, Risk Management and Compliance. VFM is currently in the process of extending its licence, in order to be able to expand its asset management service offering beyond collective investment schemes, in order to tap the growing demand for bespoke portfolio management services to institutional clients.

Risk Management and Compliance are core functions of the company's culture and operations. The Company has a robust governance model which includes various documented policies and procedures and key internal control principles that enable the portfolio managers to carry out their work in an efficient and diligent way. Moreover, VFM has in place a risk and compliance programme together with a comprehensive risk register identifying primary and consequential risks. The VFM Risk and Regulatory Committee is tasked with the responsibility to manage, develop and operate an appropriate risk control infrastructure. The combination of the qualitative and quantitative risk assessments aims to ensure that the Company operates a robust risk management process to protect its Company in both normal and stressed environments.

On the other hand, VFS was set up in 2006 as a fully owned subsidiary of Bank of Valletta plc to provide asset managers with a comprehensive suite of administration services to investment funds. VFS is recognised to provide fund administration services by the Malta Financial Services Authority. In providing its services, VFS is exposed to both operational and reputation risks, and to a lesser extent also market risks. To mitigate these risks, VFS 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, periodic audits of the Company's various operations are undertaken by the Group's Internal Audit department. VFS has also engaged an independent audit firm to perform an ISAE 3402 examination of its processes and controls on a biennial basis, which consists of an evaluation of the design and operating effectiveness of the controls of the Company. In relation to managing reputation risks, VFS 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.

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

Corporate governance statement of compliance

A. INTRODUCTION

Pursuant to the Malta Financial Services Authority Listing Rules, the 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 reviewed the Bank's compliance with the Code during the period in question. 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 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 and eight Directors (all of whom are non-executive).

The Board is in regular contact with the Chief Executive Officer in order to ensure that the Board is in receipt of timely and appropriate information in relation to the business of the Bank and management performance. This enables the Board to 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 Asset and Liability Committee, the Audit Committee, the Risk Management Committee, the Compliance and Crime Prevention Committee, the Remuneration Committee and the Nominations Committee, each of which operates under formal terms of reference approved by the Board.

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

Principle 2: Chairman and Chief Executive Officer

The Bank's current organisational structure incorporates the position of a Chief Executive Officer. The position of the Chairman and that of the Chief Executive Officer are occupied by different individuals. Their respective positions have been defined with specific roles rendering these positions completely separate from one another. This separation of roles of the Chairman and the Chief Executive Officer avoids concentration of authority and power in one individual and differentiates leadership of the Board from the running of the business.

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 Chief Executive Officer develops a strategy which is agreed to by the Board.

On the other hand, the Chief Executive Officer leads the Bank's Management Board which is the highest decision-making body within the Bank.

The Bank's Management Board was set up by the Board of Directors in November 2014 and assumes the responsibilities which were previously carried out by the Executive Committee.

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

Principle 3: Composition of the Board

The Board considers that the size of the Board, whilst not being too large as to be unwieldy, is appropriate, taking into account the size of the Bank and its operations.

Corporate governance statement of compliance (continued)

The combined and varied knowledge, experience and skills of the Board members provide a balance of competences that are required, and add value to the proper functioning of the Board.

The Board is composed exclusively of non-executive Directors. The Chief Executive Officer and the Chief Risk Officer are in attendance at Board meetings, albeit without a vote, in order to ensure their full understanding and appreciation of the Board's policy and strategy. This enables them to provide direct input to the Board's deliberations. In addition, other members of Senior Management attend Board Meetings by invitation on a regular basis.

The composition of the Board is determined by the Bank's Articles of Association. The Directors are appointed by the shareholders, except in so far as an appointment may be made to fill a casual vacancy on the Board. The number of Directors should not be less than seven and not more than ten, or eleven solely in the circumstances indicated in Article 60.2.5 of the Articles of Association. Every shareholder holding at least ten percent (10%) of the issued capital of the Company is entitled to appoint one Director, for every such ten percent (10%) holding. Every shareholder holding less than ten percent (10%) of the issued capital of the Company is entitled to participate in the voting for the election of the remaining directors who are not appointed as mentioned above. The said shareholders are entitled to elect not more than one Director for every ten percent (10%) shareholding. Shareholders holding at least ten percent (10%) of the issued share capital of the Company are not entitled to participate in the election.

During the period under review, the Board consisted of eight independent Directors (including the Chairman) and one non-independent Director (as indicated on pages (ii) and (iii) of the Annual Report). One of the eight independent Directors resigned on the 16 September 2016. In determining the independence or otherwise of its Directors, the Board has considered, amongst others, the principles relating to independence contained in the Code, the Bank's own practice as well as general good practice principles.

In determining the independence or otherwise of its Directors, the Board has considered the notion of independence as contained in the Code and international practices. The Board is of the opinion that in the case of two of the Directors (Joseph Borg and George Portanier), notwithstanding their length of service on the Board, this has not undermined the said directors' ability to consider appropriately the issues which were brought before the Board. Joseph Borg served as director from 1 October 2015 to 17 December 2015 and George Portanier served as director from 1 October 2015 to 16 September 2016.

On the other hand, the Board believes that by definition, employment with the Bank renders Director James Grech as non-independent from the institution. However, this should not in any manner, detract from said non-independent Director's ability to maintain independence of analysis, decision and action at all times.

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	No of Directorships held – Executive (ED) and non-Executive (NED)
Barbara Helga Ellul	4 NED
James Grech	3 NED
Mario Grima	1 NED
Alfred Lupi	3 NED
George Portanier (resigned on 16 September 2016)	2 NED + 1 ED
Gabriele Simonetti	1 NED
Joseph M Zrinzo	1 NED + 1 ED

John Cassar White and Taddeo Scerri are not subject to the provisions of Article 91 of the CRD IV and Article 14 of the Banking Act 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 three times a month, unless further meetings are required for the Board to discharge its duties effectively. In fact, during the year under review, the Board met 52 times.

The Board regularly reviews and evaluates corporate strategy, major operational and financial plans, risk policies, performance objectives and business alternatives. As noted above, the Board considers and determines credit proposals falling within the Board's credit sanctioning limits. 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.

Corporate governance statement of compliance (continued)

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	Meetings Held: 52 Members Attended	
John Cassar White	49	(out of 51*)
Alicia Agius Gatt *(resigned on 17 December 2015)*	15	(out of 15)
Joseph Borg *(resigned on 17 December 2015)*	13	(out of 15)
Roberto Cassata *(resigned on 17 December 2015)*	2	(out of 15)
Barbara Helga Ellul *(appointed on 17 December 2015)*	31	(out of 37)
James Grech	47	(out of 52)
Mario Grima	43	(out of 52)
Alfred Lupi *(appointed on 17 December 2015)*	34	(out of 36*)
George Portanier *(resigned on 16 September 2016)*	46	(out of 51)
Taddeo Scerri	40	(out of 51*)
Gabriele Simonetti *(appointed on 17 December 2015)*	28	(out of 37)
Joseph M Zrinzo	52	(out of 52)

**During one of the Board of Directors meetings, John Cassar White, Taddeo Scerri and Alfred Lupi declared a conflict of interest and were excused from this particular meeting.*

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:

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 annual and consolidated accounts. The Audit Committee also scrutinizes and approves related party transactions. During the year under review, the Bank adopted a 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 auditors.

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. All three non-executive directors are considered as independent 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.

Taddeo Scerri FCCA, FIA, CPA is a qualified accountant and is the Director whom the Board considers as competent in accounting. Taddeo Scerri is independent of the Bank.

Barbara Helga Ellul is a board member and chairman of various Maltese businesses with experience on boards of constituted bodies and government organisations. She is considered to be a competent member of the Audit Committee of the Bank.

Joseph M Zrinzo has various board directorship experiences on a number of companies. He also served as a member of various committees and is thus considered as competent to be a member of the Audit Committee of the Bank.

The Chief Executive Officer, the Chief Risk Officer, the Chief Finance Officer and a representative of the External Auditors attend the Audit Committee meetings by invitation. The Chief Officer Group Internal Audit also attends the meetings of the Audit Committee. The Company Secretary acts as Secretary to the Audit Committee.

Members	Meetings Held: 16 Members Attended	
Taddeo Scerri (Chairman)	15	(out of 15)
Joseph Borg *(resigned on 17 December 2015)*	2	(out of 2)
Barbara Helga Ellul *(appointed on 11 February 2016)*	11	(out of 12)
Joseph M Zrinzo	16	(out of 16)

Pursuant to the Bank's Related Party Transaction Policy, Alfred Lupi attended 4 Audit Committee meetings which discussed related party transactions. During these 4 Audit Committee meetings, Alfred Lupi substituted Taddeo Scerri as Chairman of the Audit Committee when the Committee discussed related party transactions concerning the Government of Malta or related parties as defined in the Bank's Related Party Transaction Policy.

Corporate governance statement of compliance (continued)

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

The Chief Executive Officer and the Chief Risk Officer attend the Remuneration Committee meetings by invitation. The Company Secretary acts as Secretary to the Remuneration Committee.

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

The Chief Executive Officer attends the Nominations Committee meetings by invitation. The Company Secretary acts as Secretary to the Nominations Committee.

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.

The Chief Executive Officer, the Chief Finance Officer, the Chief Risk Officer, the Chief Officer Group Internal Audit, the Credit Risk Sanctioning Executive, the Executive Risk Management and the Head Enterprise Risk Management attend the Risk Management Committee meetings by invitation. The Company Secretary acts as Secretary to the Risk Management Committee.

Members	**Meetings Held: 6 Members Attended**	
Mario Grima (Chairman)	5	(out of 6)
Alicia Agius Gatt *(resigned on 17 December 2015)*	1	(out of 1)
Joseph Borg *(resigned on 17 December 2015)*	1	(out of 1)
James Grech	6	(out of 6)
Alfred Lupi *(appointed on 11 February 2016)*	5	(out of 5)
George Portanier *(member until 17 December 2015)*	1	(out of 1)

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 (previously The Compliance 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. During the period under review this Committee has changed its name from the Compliance Committee to the Compliance and Crime Prevention Committee. In fact, this Committee is also responsible to assist the Bank in combatting financial crime and money laundering activities.

The Chief Executive Officer, the Chief Risk Officer, the Chief Business Development Officer – Investments, the Legal Executive, the Executive Group Compliance, the Executive Anti-Financial Crime and the Money Laundering Reporting Officer attend the Compliance and Crime Prevention Committee meetings by invitation. The Company Secretary also acts as Secretary to the Compliance and Crime Prevention Committee.

Members	**Meetings Held: 7 Members Attended**	
Joseph M Zrinzo (Chairman) *(appointed on 11 February 2016)*	6	(out of 6)
Alicia Agius Gatt *(resigned on 17 December 2015)*	1	(out of 1)
James Grech *(member until 17 December 2015)*	1	(out of 1)
Mario Grima	7	(out of 7)
George Portanier *(resigned on 16 September 2016)*	7	(out of 7)

Corporate governance statement of compliance (continued)

Management Committees

The **Management Board** is primarily responsible for the management of the Bank and its strategy, financial performance, risk management, human resources, information technology and data management, setting up committees which may become necessary and escalation procedures. The Bank's Management Board meets on a regular basis. It is chaired by the Chief Executive Officer and is composed of the following members:

- The Chief Operations Officer
- The Chief Risk Officer
- The Chief Finance Officer
- The Chief Business Development Officer – Investments
- The Chief Business Development Officer – Credit
- The Chief Technology Officer

The **Credit Committee** was formally dissolved on 31 December 2015. The Bank introduced a dual-voting system of lending authority, governed by the Business Credit Policy. New facilities are sanctioned through a vote by Business Sanctioning Officers and a vote by Risk Sanctioning Officers, in accordance with the relative limits which are set in accordance with the Business Credit Policy. For credit proposals above a certain limit, authorisation is sought from the Chief Officer Corporate Finance and the Chief Risk Officer or from the Board of Directors.

The **Asset and Liability Committee (ALCO)** is responsible for managing the Group's Balance Sheet, so as to achieve an optimal balance between risk and return. This Committee meets at least once a month to review balance sheet risks and ensures their prudent management. The ALCO 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 expansion and regulation. It takes an integrated view of asset and liability cash flows, their uncertainties, and the management of such 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. The ALCO provides guidance in respect of risk and return to the business, and exercises executive authority in the area of interest rate management by setting base rates payable on retail deposit products. It monitors hedging strategies and hedge effectiveness in respect of the risks mentioned above, as well as asset mix, liabilities and balance sheet growth. The ALCO is chaired by the Chief Executive Officer, and has as members a Board Director, the Chief Risk Officer, the Chief Finance Officer, the Chief Business Development Officer - Investments, the Chief Business Development Officer - Credit, the Chief Officer Investment Services and the Chief Officer Treasury.

The **Provisions Committee** is responsible to develop and maintain a provisioning methodology in line with best practice and regulatory expectations. The Committee meets on a monthly basis unless further meetings are required. The Provisions Committee is chaired by the Chief Finance Officer and is composed of members of Senior 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 on a monthly basis unless further meetings are required. The IT Steering Committee is now 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 Board of Directors on the award of contracts that exceed a defined value. The Committee meets at such frequency as necessary. The Committee is chaired by the Chief Operations Officer and is composed of members of Senior Management.

The **Core Banking Transformation Committee** is responsible for the overseeing of the identification and implementation of a new core banking solution that will enhance the customer experience. In addition, 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 and is chaired by the Chief Executive Officer and is composed of members of Senior Management.

The **Anti-Financial Crime Committee (AFCC)** is responsible to discuss and ensure that legal, regulatory and other developments related to money laundering, funding of terrorism and other financial crime matters, are implemented in the Bank's policies and procedures. This Committee is also tasked to set risk appetite for financial crime for the Bank and to ensure that the Bank follows best practice in connection with money laundering, funding of terrorism and other financial crime. When required, the AFCC also holds discussions concerning the regulators' position on certain matters. The AFCC is chaired by the Chief Risk Officer and is composed of members of Senior Management.

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 product is launched by understanding and vetting the product or service. The Committee identifies and mitigates risks which impact both product and Group. The NPAC make the final decision to either approve, decline or recommend changes. The Committee also provides guidance and recommendations in case of a new business line. The NPAC is appointed by the Board of Directors to ensure a risk adequate approach and the necessary degree of intervention in relation to product development. The NPAC is chaired by the Chief Risk Officer and is composed of members of Senior Management.

Corporate governance statement of compliance (continued)

Principle 6: Information and Professional Development

The Chief Executive Officer is appointed by the Board. He is responsible for recruitment and selection of Senior Management and consults with the Nominations 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 and Consultancy Unit specifically set up for this purpose.

On joining the Board, a Director is provided with briefings by the Chief Executive Officer on the activities of the Bank. Directors are also provided with a dossier that, apart from incorporating the relevant legislation, rules and bye laws, and Memoranda and Articles of Group companies, includes also 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 operational risk and training sessions on the Bank's business operations were organised during the year 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

This Principle is dealt with in section C of this Statement entitled Non-Compliance with the Code.

Principle 8: Committees

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

During the period under review, the Nominations Committee was set up by the Board as set out in the Code provisions. Further detail on the Nominations Committee is found 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 recognises 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 period 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 Chief Executive Officer also ensure that sufficient contact is maintained with major shareholders to understand issues and concerns.

Apart from the AGM, the Bank communicates with its shareholders by way of the Annual Report and Financial Statements, by publishing and sending to the shareholders its results on a six-monthly basis and through a bi-annual newsletter to shareholders. The Bank's website (www.bov.com) also contains information about the Bank and its business, including an Investor Relations Section.

In addition, the Bank holds a meeting for stockbrokers and financial intermediaries twice a year to coincide with the publication of its Financial Statements. Other meetings with stockbrokers and financial intermediaries are held as necessary.

The Bank's Investor Relations Officer at 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 year, and are given the opportunity to ask questions at the AGM or submit written questions in advance. In terms of Article 36 of the Articles of Association of the Bank and Article 129 of the Companies Act,1995 (Chapter 386, Laws of Malta), the Board 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

The Directors are strongly aware of their responsibility to act at all times in the interest of the Bank and its shareholders as a whole and of their obligation to avoid conflicts of interest. The latter may, and do arise on specific matters. In such instances, the Bank ensures that such conflicts, actual or potential, are managed in the best interest of the Bank.

Corporate governance statement of compliance (continued)

A Director is therefore required to make full and frank disclosure with respect to any matter where there is a potential or actual conflict, whether such conflict arises from personal interests or the interests of the companies in which such person is a director or officer and the said Director is excused from the meeting and accordingly is not involved in the Bank's Board discussion on the matter and does not vote on any such matter.

On joining the Board and regularly thereafter, the Directors are informed of their obligations on dealing in securities of the Bank within the parameters of the law, including the Listing Rules, as well as the Bank's Code of Conduct for Securities Transactions and Directors follow the required notification procedures.

Directors' interest in the share capital of the Bank as at 30 September 2016 was as follows:

	Beneficial Interest *
Mario Grima	12,560 shares
Alfred Lupi	10,400 shares
Joseph M Zrinzo	143,569 shares

**Includes any shares held by spouses or partners*

James Grech held 11,699,959 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 30 September 2016, the Directors below also held the following:

	Beneficial Interest**	
John Cassar White	10,000	BOV 4.25% Medium Term Notes 2019
Mario Grima	9,200	BOV 4.80% Subordinated Bonds 2020
	20,000	BOV 3.50% Subordinated Notes 2030 Series 2
Joseph M Zrinzo	8,000	BOV 4.80% Medium Term Notes 2018
	11,700	BOV 5.35% Subordinated Bonds 2019
	31,500	BOV 4.80% Subordinated Bonds 2020
	35,000	BOV 3.50% Subordinated Notes 2030 Series 2

***Includes any holdings by spouses or partners*

Principle 12: Corporate Social Responsibility (CSR)

"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 recognises that it has an important role to play in being an active corporate citizen within the Maltese society in which it operates. It is committed to contribute to the overall development of the country through the efficient and effective management of resources for the benefit of all its stakeholders.

The Bank has always regarded its people as the organisation's most valuable asset. Employees that are committed to the Bank's values and vision can make the difference when realising goals and are an important element of the service offered to customers. BOV promotes a healthy lifestyle and well-being for its people, and has a number of programmes in place to help them maintain a stress-free balance between their work and personal life. Employees are also encouraged to fulfill their role in the community. Events like blood donation, dress down days in aid of NGOs and tree-planting are organised throughout the year to get them involved. This year, branch teams were specifically invited to organise events for groups within their community, in a bid to strengthen the link between the Bank and the individual locality. These initiatives proved to be a success, immensely enjoyed by all involved. Shareholders are kept abreast of developments – beyond regulatory requirements – via the BOV Shareholders' Link, while the public is invited to participate in educational sessions to help them become more financially literate and in a better position to make informed decisions.

The Green agenda has long been featuring in the Bank's Mission Statement. This crystallises the Bank's commitment not only to lessen its impact on the environment, but also to actively promote conservation and safeguard the green stakeholder. The Green Manager continued to spearhead the Bank's on-going journey to reduce its carbon footprint whilst instilling more environmental-friendly practices across the Bank.

Corporate governance statement of compliance (continued)

The Bank's role in the community goes beyond caring for its customers who are the lifeblood of the organisation, and to whom the Bank is committed to provide a straightforward and efficient service. The Bank's roots run deep into the community in which it operates. The Bank's extensive Community Programme is its executive arm through which it re-invests an amount of its profits back into the community.

The Bank's Community Programme is distilled into seven distinct pillars, representing diverse but equally important concerns for the Maltese society. These are:

Arts and Culture – During the financial year under review, the Bank supported a spectrum of musical initiatives, from the elaborate festival organised by the Manoel Theatre and the two main Gozo theatres, to more intimate concerts by some of Malta's talented performers. It remained a leading sponsor for the Malta Philharmonic Orchestra. For the Bank it is also a prerogative to help introduce young children to classical music, a goal that it sought to reach through its support towards the Teatru Manoel Toi Toi programme as well as the Ziguzajg International Festival for Children. Moreover, as part of its endorsement of the Maltese Tenor, Bank of Valletta continued to support the BOV Joseph Calleja Children's Choir. Finally the BOV Joseph Calleja Foundation commemorated its fourth anniversary, raising funds to support scholars in reaching their artistic goals, whilst finding ways to use the therapeutic power of music to help vulnerable children in our community.

Heritage – As a patron of the historical treasures these islands are endowed with, Bank of Valletta gives its backing to important restoration projects like the vault of the Sanctuary in Mellieħa which was completed, and the conservation of the Calì masterpieces in Għajnsielem Chapel. The Bank's support to Fondazzjoni Wirt Artna remained consistent. Kindling a passion for our common past in the younger generation is the main goal of the *Hands-on-Heritage* programme which brings what is normally only seen on textbooks or television to life by offering students the unique opportunity to handle period instruments and tools, and learn how they were used.

The Environment – The Bank continued to support the BOV Adventure Park at Ta' Qali, which offers children and family much needed green space where they can enjoy some quality time in open space.

Education – At Bank of Valletta, we continued with our commitment to combat illiteracy by renewing our support for the *Read with Me* programme run by the National Literacy Agency. This programme takes a holistic approach, by involving parents and careworkers, in a bid to instill love for reading among children as young as 0 to 3 years of age. Furthermore, the Bank supported the *Investment Education Project* which sees students reading for a degree in the Faculty of Economics, Management and Accountancy at the University of Malta team up and manage a virtual portfolio using the Bank's trading platform. Meanwhile, excellence in education was promoted through the support of various educational awards.

Social Causes – Bank of Valletta's philanthropic efforts are handled and co-ordinated by The Marigold Foundation – BOV in the Community, which acts as a platform that gives voice and recognition to many associations, entities and NGOs which are doing sterling work in the community in which we operate. The Bank is also a major supporter of the Malta Community Chest Fund, most notably for the past thirteen years through the BOV L-Istrina Piggy Bank campaign which instills from a young age a culture of altruism and solidarity in our society. Through various initiatives the Bank has also supported other NGOs that do valuable work in various spheres in our society. The Bank also promotes a culture of altruism with its staff who have taken wholeheartedly to numerous initiatives that have made an impact in the communities in which they work.

Sport – The Bank promotes a healthy lifestyle by supporting various sporting associations and encourages the Maltese public to participate in sporting initiatives. During the financial year under review, the Bank renewed its support for football, basketball and waterpolo leagues, as well as supporting tennis and sailing.

Strategic Alliances – The Bank bases its operational approach on a Brand Promise which centres on its relationship with its clients. Through strategic alliances, the Bank builds networks with members of the main business organisations, such as the Malta Chamber of Commerce, Enterprise and Industry, the Chamber of Gozo, the Malta Hotels and Restaurants Association and the Chamber of Engineers.

C. NON-COMPLIANCE WITH THE CODE

Principle 3 (executive and non-executive directors on the Board) and 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".

The Board is composed entirely of non-executive Directors. This composition is explained under Principle 3 in Section B. Furthermore, in the context of the appointment of Directors being a matter reserved exclusively to the Bank's shareholders (except where the need arises to fill a casual vacancy) as explained under Principle 3 in Section B, considering that every Director retires from office at the AGM and on the basis of the Directors' non-executive role, there is no succession policy in place.

Principle 7 (Evaluation of the Board's Performance)

During the year under review, the Board did not undertake an evaluation of its own performance, the Chairman's performance and that of its committees.

Principle 9 (Code Provision 9.3)

Code Provision 9.3 requires the Bank to have in place a mechanism to resolve conflicts between minority shareholders and controlling shareholders. This Code Provision is not applicable to the Bank since the Bank has no controlling shareholders.

Corporate governance statement of compliance (continued)

D. INTERNAL CONTROL

Authority to manage the activities of the Bank is delegated to the Chief Executive Officer 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 and equity-accounted investee companies with clear reporting lines and delegation of powers. The Bank's Chairman is the Chairman of the Bank's fund management and fund services subsidiaries, and is also the Chairman of the equity-accounted investee life insurance company and a member of the board of the equity-accounted investee general insurance company.

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

The information 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, the appointment of the auditors and the grant of the authority to the Board to fix the auditors' emoluments. The AGM also deals with the Election of Directors (if any) and decides on the appointment of the Board 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 (46) 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 30 September 2016

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.

The Committee is composed of John Cassar White (Chairman), Alfred Lupi and Taddeo Scerri as members, all of whom are independent non-executive directors. The Chief Executive Officer and the Chief Risk Officer attend meetings of the Committee by invitation. The Company Secretary acts as Secretary to the Committee.

2. Meetings

The Committee held two meetings during the period under review, which meetings were attended as follows:

Members	Meetings Held: 2 Attended	
John Cassar White (Chairman)	2	(out of 2)
Alfred Lupi	2	(out of 2)
Taddeo Scerri	2	(out of 2)

3. Remuneration Statement

3.1 Remuneration Policy – Executive Management

The Board 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 Committee is also charged with considering and determining requests for early retirement, based on exceptional circumstances which must be assessed by the Bank on a case by case basis. The Committee has access to independent external advice on remuneration matters as and when required.

The Remuneration Policy applies consistently to all employees within the Group. Its objective is to align individual rewards with the Group's performance, business strategy, risk appetite, values and long term interests. It also encourages a prudent approach to risk taking. The Remuneration Policy is held under constant review, with the overriding principle being 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 & Risk Management Report.

The Committee considers that the current Executive Management remuneration packages based upon the appropriate local market equivalents are fair and reasonable for the responsibilities involved. The Committee is of the opinion that the remuneration packages are such, so 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.

There have been no significant changes in the Group's Remuneration Policy for Executive Management during the financial year under review and no changes are presently anticipated to be effected thereto in FY 2017.

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

The terms and conditions of employment of Senior Executives are set out in their respective indefinite contracts of employment with the Bank. Such contracts do not contain provisions for termination payments and other payments linked to early termination. Share options and profit sharing are not part of the Group's Remuneration Policy.

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. In so far 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 linkage between remuneration and performance bonus at all staff levels is reasonable and appropriate on the basis that the amount paid by way of performance bonus is not significant.

Remuneration report as at 30 September 2016 (continued)

Non-cash benefits to which Senior Executives are entitled comprise the use of a company car and health insurance. The Death-In-Service Benefit also forms part of the contract of employment of Senior Executives on the same terms applicable to all other Bank employees.

Total emoluments received by Senior Executives during FY 2016 are reported below under section 3.3 in terms of Code Provision 8.A.5.

3.2 Remuneration Policy – Directors

The Board is composed exclusively of non-executive directors. The determination of remuneration arrangements for Board members is a reserved matter for the Board as a whole, following the submission of recommendations by the Committee. 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 67.1 of the Bank's Articles of Association. The aggregate emoluments of all directors of €290,000 per annum was fixed at the 39th Annual General Meeting held on 19 December 2012. This amount excludes the salaries of directors in the Bank's employment.

There were no significant changes in the Group's Remuneration Policy for Directors during the financial year under review and no changes are presently anticipated to be effected thereto in FY 2017.

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

Directors' Fees	**€**
Chairman	75,000
Other Directors	17,500
Board Committees Fees	
Chairman	5,000
Members	3,000

One of the Directors is an employee of the Bank and therefore receives remuneration by virtue of his employment. None of the other Directors have service contracts with either the Bank or any of the Bank's subsidiaries as at the end of the financial year.

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 their capacity as a Director of the Bank, is entitled to profit sharing, share options, pension benefits or any other remuneration. In terms of non-cash benefits, Directors are entitled to health insurance and to a refund of out-of-pocket expenses.

Total fees received by Directors during FY 2016 are reported below under section 3.3 in terms of Code Provision 8.A.5.

3.3 Code Provision 8.A.5

Senior Executives' Emoluments (Management Board)

Fixed Remuneration	Variable Remuneration	Share Options	Others
€578,142	€12,000	None	Non-cash benefits referred to above under 3.1

Sign-on and severance payments

During FY 2016, the Bank made a severance payment of €270,000 to one individual. No sign-on payments were made during the year.

Directors' Fees

Fixed Remuneration	Variable Remuneration	Share Options	Others
€267,298	None	None	Non-cash benefits referred to above under 3.2

Remuneration report as at 30 September 2016 (continued)

For the financial year under review these were paid as follows:

Directors' fees including benefits – FY 2016	**€**
John Cassar White	84,561
Alicia Agius Gatt *(resigned on 17 December 2015)*	5,104
Joseph Borg *(resigned on 17 December 2015)*	5,599
Roberto Cassata *(resigned on 17 December 2015)*	3,709
Barbara Helga Ellul *(appointed on 17 December 2015)*	18,959
James Grech	21,809
Mario Grima	25,748
Alfred Lupi *(appointed on 17 December 2015)*	18,475
George Portanier *(resigned on 16 September 2016)*	20,936
Taddeo Scerri	29,165
Gabriele Simonetti *(appointed on 17 December 2015)*	13,791
Joseph M Zrinzo	28,144
Total	276,000

Nominations report as at 30 September 2016

The Nominations Committee

The Nominations Committee was set up by the Board during the period under review. The Committee follows the Nominations Policy and works under the guidance of its Terms of Reference as approved by the Board.

The Committee is primarily tasked with supporting and advising the Board in ensuring that it is comprised of individuals who are best able to discharge the duties and responsibilities of directors and that the Bank has the appropriate corporate governance standards and practices in place. The Committee is also tasked to conduct a fit and proper exercise for all candidates to ensure that they are suitable for nomination as directors at the Annual General Meeting (AGM) of the Bank. The Committee focuses on the composition, appointments, succession and effectiveness of the Board, whilst overseeing the adoption of appropriate internal policies on the assessment of the suitability of members of the Management Board and Heads of Departments who are considered as key function holders. The Committee reviews the Board's governance arrangements and makes appropriate recommendations to the Board thus ensuring that the Bank's arrangements are consistent with corporate governance standards.

The Committee is chaired by John Cassar White, with Barbara Helga Ellul and Joseph M Zrinzo as members, all independent and non-executive directors. The Chief Executive Officer may attend meetings of the Committee by invitation. The Company Secretary acts as Secretary to the Committee. Members of the Nominations Committee do not attend Committee meetings while their nomination as directors of the Bank is discussed.

Assessment of Board Nominees

Pursuant to recent banking regulatory requirements, the Bank has embarked on a process to review the nominations for director posts for the coming year 2017. This process was carried out by reference to best practice by being thorough and transparent. The process was carried out with the assistance of local and foreign external advisors.

The advert for the election of directors specified that nominations were requested from candidates who occupy or have occupied senior management positions, and who possess expertise and knowledge in financial literacy, asset management, financial stability and risk management, strategic planning, information technology, capital markets/treasury, credit risk, legal, compliance and conduct, regulation and anti-money laundering and financial crime compliance.

Given that all directors are elected through the votes of shareholders at the AGM, the assessment of directors will be concluded by the Regulators following the election of directors during the forthcoming AGM. The Nominations Committee will assist the Regulators in this assessment if so required. The appointment of the board directors will always remain subject to regulatory approval.

Meetings

The Committee held eighteen meetings during the period under review, which meetings were attended as follows:

	Meetings held: 18 Members Attended	
John Cassar White	18	(out of 18)
Barbara Helga Ellul	18	(out of 18)
Joseph M Zrinzo	17	(out of 18)
Mario Grima*	3	(out of 3)

** Mario Grima attended meetings which discussed the assessment of nominees, who were members of the Nominations Committee.*

During its first year of operation, the Committee focused on the assessment of Board nominees, the appointment of Heads of Departments considered to be key function holders and the appointment of members of the Management Board.

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) and (iii) 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.

Policy on Diversity

There is currently no policy on diversity with regards to selection of the members of the Board.

Auditors' report on corporate governance

Report required by Listing Rule 5.98 issued by the Listing Authority in Malta on the Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance (the "Principles") outlined in Appendix 5.1 to Chapter 5 (Continuing Obligations) of the Listing Rules (the "Appendix")

Listing Rule 5.97 requires an Issuer whose securities are admitted to trading on a Regulated Market operating in Malta to prepare a corporate governance statement. In addition, as an Issuer registered in Malta, Listing Rule 5.94 requires that the Bank endeavours to adopt the Principles and to prepare a report explaining how it has complied with the provisions of the Appendix.

Our responsibility as independent auditors of the Bank, is laid down by Listing Rule 5.98, which requires us to issue a report on the accompanying Directors' Statement of Compliance with the Principles.

We read the Directors' Statement of Compliance, and report as to whether this Statement provides the disclosures required by Listing Rule 5.97. We are not required to, and we do not, consider whether the Board's 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 Bank's corporate governance procedures or its risks and control procedures.

In our opinion, the accompanying Directors' Statement of Compliance provides the disclosures required by Listing Rule 5.97 issued by the Listing Authority of Malta.

Noel Mizzi
Partner, for and on behalf of
KPMG
Registered Auditors,
Portico Building,
Marina Street,
Pietà PTA 9044,
Malta

28 October 2016

Statements of profit or loss for the year ended 30 September 2016

	Note	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Interest and similar income					
- on loans and advances, balances with Central Bank of Malta and treasury bills	2	160,195	158,180	160,195	158,180
- on debt and other fixed income instruments	2	54,063	57,432	54,063	57,432
Interest expense	3	(65,429)	(70,834)	(65,429)	(70,834)
Net interest income		**148,829**	**144,778**	**148,829**	**144,778**
Fee and commission income		75,021	70,922	66,840	62,919
Fee and commission expense		(8,936)	(8,346)	(8,936)	(8,346)
Net fee and commission income	4	**66,085**	**62,576**	**57,904**	**54,573**
Dividend income		1,901	2,352	9,635	12,151
Trading profits	5	24,724	34,067	24,724	34,068
Net gain on investment securities and hedging instruments	6	9,046	3,098	9,046	3,098
Gain on Visa transaction	6	27,511	-	27,511	-
Operating income		**278,096**	**246,871**	**277,649**	**248,668**
Employee compensation and benefits	7	(64,168)	(61,700)	(62,036)	(59,994)
General administrative expenses		(40,103)	(38,651)	(39,085)	(37,347)
Amortisation of intangible assets	20	(3,539)	(2,574)	(3,539)	(2,574)
Depreciation	21	(4,968)	(5,107)	(4,899)	(5,022)
Net impairment losses	8	(23,142)	(32,710)	(23,147)	(32,666)
Operating profit		**142,176**	**106,129**	**144,943**	**111,065**
Share of results of equity-accounted investees, net of tax	18	3,730	11,786	-	-
Profit before tax	9	**145,906**	**117,915**	**144,943**	**111,065**
Income tax expense	10	(50,708)	(37,971)	(50,760)	(38,715)
Profit for the year		**95,198**	**79,944**	**94,183**	**72,350**
Attributable to:					
Equity holders of the Bank		94,742	79,378	94,183	72,350
Non-controlling interest		456	566	-	-
		95,198	79,944	94,183	72,350
Earnings per share	11	**24c3**	**20c4**	**24c1**	**18c6**

Statements of profit or loss and other comprehensive income

for the year ended 30 September 2016

	The Group		The Bank	
	2016	**2015**	**2016**	**2015**
	€000	**€000**	**€000**	**€000**
Profit for the year	95,198	79,944	94,183	72,350
Other comprehensive income				
Items that may be reclassified subsequently to profit or loss:				
Available-for-sale investments				
- change in fair value	33,777	9,968	33,777	9,968
deferred tax thereon	(11,822)	(3,488)	(11,822)	(3,488)
- change in fair value transferred to profit or loss	(34,876)	(3,747)	(34,876)	(3,747)
deferred tax thereon	12,206	1,311	12,206	1,311
Items that will not be reclassified to profit or loss:				
Property revaluation	960	1,319	960	1,319
deferred tax thereon and effect of changes in property tax rates	44	718	44	718
Remeasurement of actuarial losses on defined benefit plans	(1,448)	(1,451)	(1,448)	(1,451)
deferred tax thereon	508	508	508	508
Other comprehensive income for the period, net of tax	(651)	5,138	(651)	5,138
Total comprehensive income	94,547	85,082	93,532	77,488
Attributable to:				
Equity holders of the Bank	94,091	84,516	93,532	77,488
Non-controlling interest	456	566	-	-
	94,547	85,082	93,532	77,488

The notes are an integral part of these financial statements.

Statements of financial position

as at 30 September 2016

	Note	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	13	171,050	126,652	171,050	126,652
Financial assets at fair value through profit or loss	14	392,430	417,522	391,292	415,558
Investments	15	3,736,272	3,376,305	3,736,272	3,376,305
Loans and advances to banks	16	2,098,439	1,656,346	2,098,439	1,656,346
Loans and advances to customers at amortised cost	17	4,001,656	4,001,839	4,001,656	4,001,839
Investments in equity-accounted investees	18	97,041	96,904	52,870	52,870
Investments in subsidiary companies	19	-	-	6,230	1,230
Intangible assets	20	13,272	12,722	13,272	12,722
Property and equipment	21	89,574	89,801	89,452	89,651
Current tax		16,061	965	15,091	-
Deferred tax	22	67,188	86,654	67,188	86,654
Assets held for realisation	40	11,973	11,601	11,973	11,601
Other assets		4,818	2,990	4,809	2,990
Prepayments and accrued income	23	23,077	21,661	22,697	22,094
Total Assets		**10,722,851**	**9,901,962**	**10,682,291**	**9,856,512**
LIABILITIES					
Financial liabilities at fair value through profit or loss	14	20,327	25,077	20,327	25,077
Amounts owed to banks	24	250,155	197,760	250,155	197,760
Amounts owed to customers	25	9,181,047	8,559,731	9,184,470	8,563,107
Debt securities in issue	26	95,400	95,400	95,400	95,400
Current tax		-	-	-	71
Deferred tax	22	4,318	4,382	4,318	4,382
Other liabilities	27	173,988	172,905	173,803	172,743
Accruals and deferred income	28	16,215	21,317	15,802	20,725
Derivatives designated for hedge accounting	29	20,649	35,201	20,649	35,201
Subordinated liabilities	30	231,591	120,000	231,591	120,000
Total Liabilities		**9,993,690**	**9,231,773**	**9,996,515**	**9,234,466**
EQUITY					
Called up share capital	31	390,000	360,000	390,000	360,000
Share premium account		988	988	988	988
Revaluation reserves	32	35,332	35,217	35,220	35,105
Retained earnings	32	302,841	272,713	259,568	225,953
Total Equity attributable to equity holders of the Bank		**729,161**	**668,918**	**685,776**	**622,046**
Non-controlling interest		-	1,271	-	-
Total Equity		**729,161**	**670,189**	**685,776**	**622,046**
Total Liabilities and Equity		**10,722,851**	**9,901,962**	**10,682,291**	**9,856,512**
MEMORANDUM ITEMS					
Contingent liabilities	33	225,407	251,670	225,407	251,670
Commitments	34	1,590,156	1,612,122	1,590,156	1,612,122

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 28 October 2016 and signed on its behalf by:

J. Cassar White
Chairman

M. Grima
Director

M. Mallia
Chief Executive Officer

Statements of changes in equity for the year ended 30 September 2016

	Attributable to Equity holders of the Bank						
	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000	Non-controlling Interest €000	Total Equity €000
The Group							
At 1 October 2014	**330,000**	**988**	**29,136**	**253,245**	**613,369**	**1,100**	**614,469**
Profit for the year	-	-	-	79,378	**79,378**	566	**79,944**
Other comprehensive income							
Available-for-sale investments							
- change in fair value, net of tax	-	-	6,480	-	**6,480**	-	**6,480**
- change in fair value transferred to profit or loss, net of tax	-	-	(2,436)	-	**(2,436)**	-	**(2,436)**
Property revaluation, net of tax	-	-	2,037	-	**2,037**	-	**2,037**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(943)	**(943)**	-	**(943)**
Total other comprehensive income/(loss)	-	-	6,081	(943)	**5,138**	-	**5,138**
Total comprehensive income for the year	-	-	6,081	78,435	**84,516**	566	**85,082**
Transactions with owners, recorded directly in equity:							
Bonus issue	30,000	-	-	(30,000)	**-**	-	**-**
Dividends to equity holders	-	-	-	(28,967)	**(28,967)**	(395)	**(29,362)**
	30,000	-	-	(58,967)	**(28,967)**	(395)	**(29,362)**
At 30 September 2015	**360,000**	**988**	**35,217**	**272,713**	**668,918**	**1,271**	**670,189**
Profit for the year	-	-	-	94,742	**94,742**	456	**95,198**
Other comprehensive income							
Available-for-sale investments							
- change in fair value, net of tax	-	-	21,955	-	**21,955**	-	**21,955**
- change in fair value transferred to profit or loss, net of tax	-	-	(22,670)	-	**(22,670)**	-	**(22,670)**
Property revaluation, net of tax	-	-	1,004	-	**1,004**	-	**1,004**
Release of surplus on sale of property, net of tax	-	-	(174)	174	**-**	-	**-**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(940)	**(940)**	-	**(940)**
Total other comprehensive income/(loss)	-	-	115	(766)	**(651)**	**-**	**(651)**
Total comprehensive income for the year	-	-	115	93,976	**94,091**	**456**	**94,547**
Transactions with owners, recorded directly in equity:							
Acquisition of non-controlling interest	-	-	-	(4,046)	**(4,046)**	(954)	**(5,000)**
Bonus issue	30,000	-	-	(30,000)	**-**	-	**-**
Dividends to equity holders	-	-	-	(29,802)	**(29,802)**	(773)	**(30,575)**
	30,000	-	-	(63,848)	**(33,848)**	(1,727)	**(35,575)**
At 30 September 2016	**390,000**	**988**	**35,332**	**302,841**	**729,161**	**-**	**729,161**

The notes are an integral part of these financial statements.

Statements of changes in equity for the year ended 30 September 2016 (continued)

	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000
The Bank					
At 1 October 2014	**330,000**	**988**	**29,024**	**213,513**	**573,525**
Profit for the year	-	-	-	72,350	**72,350**
Other comprehensive income					
Available-for-sale investments					
- change in fair value, net of tax	-	-	6,480	-	**6,480**
- change in fair value transferred to profit or loss, net of tax	-	-	(2,436)	-	**(2,436)**
Property revaluation, net of tax	-	-	2,037	-	**2,037**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(943)	**(943)**
Total other comprehensive income/(loss)	-	-	6,081	(943)	**5,138**
Total comprehensive income for the year	-	-	6,081	71,407	**77,488**
Transactions with owners, recorded directly in equity:					
Bonus issue	30,000	-	-	(30,000)	**-**
Dividends to equity holders	-	-	-	(28,967)	**(28,967)**
	30,000	-	-	(58,967)	**(28,967)**
At 30 September 2015	**360,000**	**988**	**35,105**	**225,953**	**622,046**
Profit for the year	-	-	-	94,183	**94,183**
Other comprehensive income					
Available-for-sale investments					
- change in fair value, net of tax	-	-	21,955	-	**21,955**
- change in fair value transferred to profit or loss, net of tax	-	-	(22,670)	-	**(22,670)**
Property revaluation, net of tax	-	-	1,004	-	**1,004**
Release of surplus on sale of property, net of tax	-	-	(174)	174	**-**
Remeasurement of actuarial losses on defined benefit plans, net of tax	-	-	-	(940)	**(940)**
Total other comprehensive income/(loss)	-	-	115	(766)	**(651)**
Total comprehensive income for the year	-	-	115	93,417	**93,532**
Transactions with owners, recorded directly in equity:					
Bonus issue	30,000	-	-	(30,000)	**-**
Dividends to equity holders	-	-	-	(29,802)	**(29,802)**
	30,000	-	-	(59,802)	**(29,802)**
At 30 September 2016	**390,000**	**988**	**35,220**	**259,568**	**685,776**

The notes are an integral part of these financial statements.

Statements of cash flows for the year ended 30 September 2016

	Note	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Cash flows from operating activities					
Interest and commission receipts		237,321	259,455	229,154	251,459
Interest, commission and compensation payments		(77,205)	(93,171)	(77,026)	(93,294)
Payments to employees and suppliers		(103,563)	(80,704)	(99,601)	(79,677)
Operating profit before changes in operating assets and liabilities		56,553	85,580	52,527	78,488
(Increase)/decrease in operating assets:					
Loans and advances		(53,038)	(322,100)	(53,038)	(322,056)
Reserve deposit with Central Bank of Malta		(8,643)	(15,731)	(8,643)	(15,731)
Fair value through profit or loss financial assets		97,902	122,279	97,902	122,279
Fair value through profit or loss equity instruments		1,303	2,930	477	600
Treasury bills with original maturity of more than 3 months		-	3,999	-	3,999
Other assets		(311)	2,823	(302)	2,823
Increase in operating liabilities:					
Amounts owed to banks and to customers		752,337	1,300,337	752,384	1,302,569
Other liabilities		(33,187)	8,790	(33,120)	8,737
Net cash from operating activities before tax		812,916	1,188,907	808,187	1,181,708
Tax paid		(44,862)	(64,799)	(44,955)	(64,351)
Net cash from operating activities		768,054	1,124,108	763,232	1,117,357
Cash flows from investing activities					
Dividends received		5,628	5,808	9,636	12,151
Interest received from held-to-maturity debt and other fixed income instruments		59,783	58,998	59,783	58,998
Acquisition of non-controlling interest		(5,000)	-	(5,000)	-
Purchase of equity instruments		-	(100)	-	(100)
Purchase of debt instruments		(1,257,546)	(1,560,089)	(1,257,546)	(1,560,089)
Proceeds from sale or maturity of debt instruments		869,184	706,613	869,184	706,613
Proceeds from sale of equity instruments		3,043	-	3,043	-
Proceeds from Visa transaction		22,042	-	22,042	-
Purchase of property and equipment and intangible assets		(8,111)	(9,132)	(8,070)	(9,119)
Proceeds from disposal of property and equipment		598	-	598	-
Net cash used in investing activities		(310,379)	(797,902)	(306,330)	(791,546)
Cash flows from financing activities					
Proceeds from issue of subordinated bonds		111,591	-	111,591	-
Dividends paid to Bank's equity holders		(29,802)	(28,967)	(29,802)	(28,967)
Dividends paid to non-controlling interests		(773)	(395)	-	-
Net cash from/(used in) financing activities		81,016	(29,362)	81,789	(28,967)
Net change in cash and cash equivalents		538,691	296,844	538,691	296,844
Effect of exchange rate changes on cash and cash equivalents		-	64	-	64
Net change in cash and cash equivalents after effect of exchange rate changes		538,691	296,780	538,691	296,780
Net change in cash and cash equivalents		538,691	296,844	538,691	296,844
Cash and cash equivalents at 1 October		1,309,347	1,012,503	1,309,347	1,012,503
Cash and cash equivalents at 30 September	36	**1,848,038**	**1,309,347**	**1,848,038**	**1,309,347**

The notes are an integral part of these financial statements.

Notes to the financial statements 30 September 2016

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 were deemed to have come into force on 17 June 2016.

Article 4 of Regulation 1606/2002/EC requires that, for each financial year 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 and assets and liabilities are measured at historical cost except for the following that are measured at fair value: available-for-sale financial assets, financial instruments classified at fair value through profit or loss, derivatives and land and buildings. Additionally, assets held for realisation are measured at fair value less costs to sell.

During the year under review, the Group and the Bank have applied the following amendments and improvements to International Financial Reporting Standards as adopted by the EU:

- Amendments to IAS 19: *Defined Benefit Plans: Employee Contributions (issued on 21 November 2013).*
- Annual improvements to IFRSs 2010-2012 Cycle *(issued on 12 December 2013).*
- Annual improvements to IFRSs 2011-2013 Cycle *(issued on 12 December 2013).*

A number of new standards and amendments were endorsed by the EU but effective for periods starting on or after 1 January 2016. The directors are assessing the impact that the adoption of these International Financial Reporting Standards will have on the financial statements of the Group and the Bank in the period of initial application. These standards and amendments include the following:

- Amendments to IFRS 10, IFRS 12 and IAS28: *Investment Entities – Applying the consolidation Exception (issued on 18 December 2014)*
- Amendments to IAS 27: *Equity Method in Separate Financial Statements (issued on 12 August 2014)*
- Amendments to IAS 1: *Disclosure Initiative (issued on 18 December 2014)*
- Annual Improvements to IFRSs 2012-2014 Cycle *(issued on 25 September 2014)*
- Amendments to IAS 16 and IAS 38: *Clarification of Acceptable Methods of Depreciation and Amortisation (issued on 12 May 2014)*

In addition, the following new standards and amendments have not yet been endorsed by the EU:

Standards:

On 24 July 2014, the IASB issued the final version of IFRS 9, which brings together the classification and measurement, impairment and hedge accounting phases of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement.

The Standard supersedes all previous versions of IFRS 9. IFRS 9 introduces a logical approach for the classification of financial assets, which is driven by cash flow characteristics and the business model in which an asset is held. This single, principle-based approach replaces existing rule based requirements that are generally considered to be overly complex and difficult to apply. The new model also results in a single, forward-looking 'expected loss' impairment model that will require more timely recognition of expected credit losses. IFRS 9 introduces a substantially reformed model for hedge accounting, with enhanced disclosures about risk management activity. The new model represents a significant overhaul of hedge accounting that aligns the accounting treatment with risk management activities, enabling entities to better reflect these activities in their financial statements. IFRS 9 also removes the volatility in profit or loss that was caused by changes in the credit risk of liabilities elected to be measured at fair value. IFRS 9 is applicable for annual periods beginning on or after 1 January 2018, with earlier application being permitted. This Standard had not yet been endorsed by the EU at the date of authorisation of these financial statements. According to the European Financial Reporting Advisory Group, the Standard is expected to be endorsed by quarter 4 of 2016. The adoption of IFRS 9 may have a material impact on the Bank's financial statements. The Group has already carried out an initial assessment on the impact of the new standard and will be implementing a software solution in the coming months.

IFRS 15 Revenue from Contracts with Customers establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes. IFRS 15 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. However, this standard has not yet been endorsed by the EU at the date of approval of these financial statements.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.1 Basis of preparation (continued)

The Directors anticipate that the adoption of other International Financial Reporting Standards that were in issue at the date of authorisation of these financial statements, but not yet effective, will have no material impact on the financial statements of the Group and the Bank in the period of initial application.

IFRS 16 introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. A lessee measures right-of-use assets similarly to other non-financial assets (such as property, plant and equipment) and lease liabilities similarly to other financial liabilities. As a consequence, a lessee recognises depreciation of the right-of-use asset and interest on the lease liability, and also classifies cash repayments of the lease liability into a principal portion and an interest portion and presents them in the statement of cash flows applying IAS 7 Statement of Cash Flows. Assets and liabilities arising from a lease are initially measured on a present value basis. The measurement includes non-cancellable lease payments (including inflation-linked payments), and also includes payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease, or not to exercise an option to terminate the lease.

This new standard substantially carries forward the lessor accounting requirements in IAS 17. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. Additionally, this standard requires (i) lessees to apply judgement in deciding upon the information to disclose to meet the objective of providing a basis for users of financial statements to assess the effect that leases have on the financial position, financial performance and cash flows of the lessee, and (ii) lessors to disclose enhanced information about lessor's risk exposure, particularly to residual value risk.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Earlier application is permitted for entities that apply IFRS 15 Revenue from Contracts with Customers at or before the date of initial application of IFRS 16. This standard has not yet been endorsed by the EU at the date of authorisation of these financial statements. The Group is currently assessing the potential impact on its consolidated and separate financial statements resulting from the application of this standard.

Amendments:

- Amendments to IAS 12: *Recognition of Deferred Tax Assets for Unrealised Losses (issued on 19 January 2016)*
- Amendments to IAS 7: *Disclosure Initiative (issued on 29 January 2016)*
- Amendments to IFRS 15: *Revenue from Contracts with Customers (issued on 12 April 2016)*

Other than specifically mentioned above, the impact that the adoption of these standards and amendments will have on the financial statements of the Group and the Bank is currently being assessed by the directors. The directors anticipate that the adoption of other International Financial Reporting Standards that were in issue at the date of authorisation of these financial statements, but not yet effective, will have no material impact on the financial statements of the Group and the Bank in the period of initial application.

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 Group 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 Group 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 below.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.3 Financial assets at fair value through profit or loss, investment securities and loans and receivables

The Group classifies its financial assets in the following categories: (i) financial assets at fair value through profit or loss; (ii) investment securities; and (iii) loans and receivables. The classification depends on the purpose for which the investments were acquired.

1.3.1 Financial assets at fair value through profit or loss

This classification includes financial assets classified as held for trading, and those designated 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 assets at fair value through profit or loss are initially recognised and are subsequently measured at fair value 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. Interest receivable on financial assets at fair value through profit or loss is included with interest receivable and similar income. All related realised and unrealised gains and losses are included in trading profits in the year in which they arise.

Portfolios of over-the-counter derivatives that are exposed to credit risk and are managed by the Group on the basis of the net exposure to credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for a particular risk exposure. Those portfolio-level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

1.3.2 Investment securities

Investment securities are classified into two sub-categories: held-to-maturity and available-for-sale financial assets. Non-derivative investment securities, with fixed or determinable payments and fixed maturity, where the Group has both the positive intent and the ability to hold them to maturity, other than those that upon initial recognition are designated as at fair value through profit or loss, those that are designated as available-for-sale financial assets and those that meet the definition of loans and receivables, are classified as held-to-maturity financial assets. Investment securities intended to be held for an indefinite period of time, but which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or market prices are classified as available-for-sale financial assets. All investment securities are initially measured at fair value plus transaction costs, if any, that are directly attributable to their acquisition.

Those investment securities classified as available-for-sale financial assets are subsequently measured at fair value based on quoted bid prices in an active market, or by reference to a valuation technique if the market is not active, with the exception of equity instruments that do not have a quoted price in an active market for an identical instrument (ie. a Level 1 input) and whose fair value cannot be measured reliably which are measured at cost less any impairment losses. Gains and losses arising from changes in the fair value of securities classified as available-for-sale that are not designated as hedged items in a fair value hedge are recognised in other comprehensive income, except for impairment losses and foreign exchange gains and losses on monetary items, until the security is derecognised, at which time the related accumulated fair value adjustments previously recognised in other comprehensive income are included in profit or loss as a reclassification adjustment within net gains or losses on investment securities. With respect to available-for-sale securities that are designated as hedged items in a fair value hedge, gains and losses arising from changes in fair value attributable to the hedged risk are accounted for in profit or loss. Fair value movements attributable to other factors, such as changes in credit status, are recognised in other comprehensive income, except for impairment losses and foreign exchange gains and losses on monetary items. Interest calculated using the effective interest method is recognised in profit or loss.

Those investment securities classified as held-to-maturity financial assets are subsequently measured at amortised cost using the effective interest method, less any impairment losses. Interest calculated using the effective interest method and impairment losses are recognised in profit or loss.

The Bank, in line with IAS39, does not classify financial assets as held-to-maturity if it has during the current financial year or during the two preceding years, sold or reclassified more than an insignificant amount of the held-to-maturity portfolio other than sales or reclassifications that are specifically exempted for the purpose of this requirement. Significance is measured in relation to the total amount of held-to-maturity investments.

1.3.3 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that are held for trading or are designated upon initial recognition as at fair value through profit or loss or as available-for-sale financial assets or those for which the Group may not recover substantially all of its initial investment other than because of credit deterioration. These mainly comprise loans and advances to banks and customers.

Loans and receivables are initially measured at fair value plus transaction costs, if any, that are directly attributable to their acquisition, and are subsequently measured at amortised cost using the effective interest method, less any impairment losses. Gains and losses are recognised in profit or loss when the financial asset is derecognised or impaired and through the amortisation process using the effective interest rate.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.3 Financial assets at fair value through profit or loss, investment securities and loans and receivables (continued)

1.3.3 Loans and receivables (continued)

Impairment
The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets are impaired. A financial asset or a group of financial assets are impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a ‘loss event’) and that loss event(s) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

(i) Financial assets carried at amortised cost

The Group considers evidence of impairment for loans and advances at both a specific asset and a collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances that are not individually significant are collectively assessed for impairment by grouping together loans and advances with similar risk characteristics.

For held-to-maturity securities carried at amortised cost and quoted in an active market, if there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset’s carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset’s original effective interest rate, by reference to the asset’s quoted market price.

For individually significant loans and receivables, if there is objective evidence that an impairment loss has been incurred, the amount of loss is measured in line with Banking Rule 09 ‘Measures Addressing Credit Risks arising from the Assessment of the Quality of Asset Portfolios of Credit Institutions Authorised under the Banking Act 1994’ (Chapter 371, Laws of Malta) which is in line with the IAS 39. The measurement of the loss amount takes account of the repayment history of the borrower and the value of collateral held against borrowings. Financial assets which do not attract a specific allowance are categorised according to credit risk characteristics and the amount of loss thereon is measured by taking account of the probability of default and loss given default for similar assets, after considering the level of collateral held.

The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases, and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through an allowance account, so that the reversal does not result in a carrying amount that exceeds what the amortised cost would have been had the impairment not been recognised at the date the impairment is reversed. The amount of the reversal is recognised in profit or loss.

(ii) Impairment losses on restructured/refinanced corporate assets (forbearance)

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised. If the cash flows of the renegotiated asset 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 and the new financial asset is recognised at fair value.

In the case of loans and advances which encounter 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.

A concession refers to either of the following:
- a modification of 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.

When accounts are classified as ‘non-performing’ assets, prior to the restructuring, they continue to be assessed for impairment individually taking into account the value of the collateral held as confirmed by professional valuations and the available cash flow to service debt over the period of the restructuring. If classified as ‘performing’ assets, restructured loans continue to be assessed for impairment collectively for inherent losses under the Group’s normal collective assessment methodology.

(iii) Available-for-sale financial assets

When a decline in the fair value of an available-for-sale financial asset has been recognised in other comprehensive income and there is objective evidence that the asset is impaired, the cumulative loss is reclassified from equity to profit or loss. The cumulative loss is measured as the difference between the acquisition cost, (net of any principal repayment and amortisation), and the current fair value, less any impairment losses previously recognised in profit or loss.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.3 Financial assets at fair value through profit or loss, investment securities and loans and receivables (continued)

1.3.3 Loans and receivables (continued)

Impairment (continued)

(iii) Available-for-sale financial assets (continued)

Impairment losses recognised in profit or loss on equity instruments are not reversed through profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available-for-sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, then the impairment loss is reversed through profit or loss; otherwise, any increase in fair value is recognised through OCI. Any subsequent recovery in the fair value of an impaired available-for-sale equity security is always recognised in OCI. Changes in impairment attributable to application of the effective interest method are reflected as a component of interest income. The impairment loss on investments in equity instruments that do not have a quoted market price in an active market for an identical instrument (ie. a Level 1 input) and whose fair value cannot be reliably measured is recognised in profit or loss and is not reversed in a subsequent period.

The Group writes off a loan or an investment debt security, either partially or in full, and any related allowance for impairment losses, when Group Credit determines that there is no realistic prospect of recovery.

1.4 Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into, and the definitions of a financial liability and an equity instrument.

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.

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.

Equity instruments are recorded at the proceeds received, net of direct issue costs.

1.5 Recognition, derecognition and offsetting of financial assets and financial liabilities

Financial assets and financial liabilities are recognised when a Group entity becomes a party to the contractual provisions of the instrument.

All loans and receivables 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.

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. A financial liability is derecognised when it is extinguished. This occurs when the obligation specified in the contract is discharged, cancelled or expires.

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.

1.6 Classification of financial assets and financial liabilities at fair value through profit or loss upon initial recognition

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 either:

- 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; or

- a group of financial assets, financial liabilities or both, is managed and its performance is evaluated on a fair value basis, in accordance with the Group's documented risk management and investment strategy, and information about the group is provided internally on that basis to key management personnel, including the Board of Directors and Chief Executive Officer.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.7 Derivative financial instruments

Derivative financial instruments are initially recognised and subsequently measured at fair value. Fair values are obtained from quoted market prices in active markets and through the use of discounted cash flow models where an active market does not exist. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The method of recognising the fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged.

Certain derivative instruments are not designated in a hedge relationship for accounting purposes. The Group classifies forward exchange contracts, options and certain interest rate swaps as at fair value through profit or loss, and accordingly any changes in their fair value are included in trading profits.

The Group designates certain interest rate swaps as hedges of the exposure to variability in the fair value of certain available-for-sale financial assets, which arises from interest rate movements. Changes in the fair value of interest rate swaps that are designated and qualify as fair value hedging instruments, together with any changes in the fair value of the hedged items that are attributable to the hedged risk, are recognised in profit or loss.

1.8 Sale and repurchase agreements

Securities sold subject to a linked repurchase agreement ('repos') are retained in the financial statements 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.

1.9 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 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.

1.10 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.

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.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.10 Property and equipment (continued)

Other tangible assets are stated at cost less any 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.

1.11 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 enbodied in the specific asset to which it relates.

Computer software is initially measured at cost. It is subsequently carried at cost less any 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.

1.12 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 appriopriate.

1.13 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.

1.14 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.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.14 Provisions, contingent liabilities and contingent assets (continued)

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

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. Contingent assets are not recognised. Contingent assets are disclosed where an inflow of economic benefits is probable.

'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.

1.15 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 one year from the date of classification. An impairment loss is recognised in profit or loss. 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.

1.16 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 90 days 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.

1.17 Dividends payable

Interim dividends are approved by the directors and recognised when paid. Final dividends are recognised as liability upon approval by the shareholders at the Annual General Meeting.

1.18 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.

1.19 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.

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.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.19 Fair value (continued)

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 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 Bank incorporate all factors that market participants would consider in setting a price and are consistent with accepted economic methodologies for pricing financial instruments.

1.20 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 also dealt with in other comprehensive income or in equity, as appropriate.

Current tax
Current tax is based on the taxable result for the year. The taxable result for the year 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.

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.

1.21 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.

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.

Fees and commissions that are earned on the execution of a significant act (for example, fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as an arrangement for the acquisition of shares or other securities) are recognised as revenue when the significant act has been completed. Fees and commissions that are earned as services are provided to the customer are recognised as revenue as the services are provided. Where fees are charged to cover the cost of a continuing service, these are recognised in proportion to the costs required to render the services over the relevant period.

Notes to the financial statements 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.22 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.

1.23 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 year in which they are incurred in profit or loss.

For the Bank's and the Group'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 reflected 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, the Group and the Bank did not involve a qualified actuary in the measurement of their post-employment benefit obligations.

1.24 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 the remaining notes to the financial statements.

1.24.1 Impairment losses on loans and advances

The Group reviews its loan portfolio on an ongoing basis to assess whether there is any objective evidence of impairment. Objective evidence that individual loans and advances are impaired includes observable data that comes to the attention of the Group about loss events, such as repayments falling into arrears, a deterioration in the financial situation of the principal debtor or guarantor, economic conditions which may adversely affect the borrower's business activity or market, technological change and changes in the fair value of collateral. With respect to a group of loans and receivables, loss events include probabilities of default associated with the credit status of that group and measurable economic conditions which may influence future cash flows from the assessed loans. Management uses estimates based on historical loss experience for assets with credit risk characteristics similar to those of the assessed group when forecasting future cash flows. The exercise of judgement is an inherent aspect in assessing provisions required and is applied in determing the underlying value of collateral held and the period over which colleteral or other projected cashflows are expected to be realised. For collective provisioning estimation uncertainty is mainly around the application of probability of default to loans with similar credit risk characteristics. The methodology and assumptions for estimating the amount and timing of future cash flows are reviewed regularly in the light of actual loss experience.

1.24.2 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 30 September 2016 (continued)

1. SIGNIFICANT ACCOUNTING POLICIES (continued)

1.24 Judgements in applying accounting policies and key sources of estimation uncertainty (continued)

1.24.3 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.

1.24.4 Impairment losses on held-to-maturity investments and on available-for-sale investments

In the case of financial assets that are either classified as held-to-maturity investments or as available-for-sale investments, objective evidence of impairment includes observable data about the following loss events, as applicable – significant financial difficulty of the issuer (or counterparty), a breach of contract, it becoming probable that the borrower will enter bankruptcy or other financial reorganisation, the disappearance of an active market for that financial asset because of financial difficulties or observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets. In addition to the above loss events, objective evidence of impairment for an investment in an equity instrument includes information about significant changes with an adverse effect that have taken place in the technological, market, economic or legal environment in which the issuer operates or a significant or prolonged decline in the fair value below its cost. The determination of these loss events is based on the analysis of the amortised cost amount against the fair value of the individual security to assess whether declines in value are indicative of impairment.

1.24.5 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.

1.24.6 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.

1.24.7 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. 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 these 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.

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
2. INTEREST AND SIMILAR INCOME				
On loans and advances to banks	1,984	1,067	1,984	1,067
On loans and advances to customers	158,211	157,096	158,211	157,096
On treasury bills	-	17	-	17
	160,195	158,180	160,195	158,180
On debt and other fixed income instruments				
- available-for-sale	10,945	12,636	10,945	12,636
- held-to-maturity	48,016	45,695	48,016	45,695
- fair value through profit or loss	6,873	9,758	6,873	9,758
	65,834	68,089	65,834	68,089
Amortisation of discounts and premiums				
- available-for-sale	(2,463)	(913)	(2,463)	(913)
- held-to-maturity	(9,308)	(9,744)	(9,308)	(9,744)
	(11,771)	(10,657)	(11,771)	(10,657)
	54,063	57,432	54,063	57,432
	214,258	215,612	214,258	215,612
3. INTEREST EXPENSE				
On amounts owed to banks	8,481	5,283	8,481	5,283
On interest rate swaps	7,372	11,123	7,372	11,123
On amounts owed to customers	30,984	42,922	30,984	42,922
On debt securities in issue	4,359	4,359	4,359	4,359
On subordinated liabilities	8,758	6,035	8,758	6,035
Negative interest on loans to banks, treasury bills and balances with Central Bank of Malta	5,475	1,112	5,475	1,112
	65,429	70,834	65,429	70,834
4. NET FEE AND COMMISSION INCOME				
On loans and advances, similar activities and local business	31,678	30,045	31,678	30,045
On trust, life assurance, fund management and similar activities	21,641	19,435	13,460	11,432
On other activities	12,766	13,096	12,766	13,096
	66,085	62,576	57,904	54,573
5. TRADING PROFITS				
Net income on foreign exchange activities	20,327	22,361	20,341	22,368
Fair value movements and net gains on sale of financial instruments at fair value through profit or loss	4,397	11,706	4,383	11,700
	24,724	34,067	24,724	34,068

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
6. NET GAIN ON INVESTMENTS AND HEDGING INSTRUMENTS				
Available-for-sale assets				
- net gain on disposal	9,263	3,747	9,263	3,747
- net revaluation gain attributable to hedged risk	2,877	3,205	2,877	3,205
	12,140	6,952	12,140	6,952
Derivative financial instruments				
- net loss on derivative financial instruments held for hedging	(3,094)	(3,854)	(3,094)	(3,854)
	9,046	3,098	9,046	3,098
Gain on Visa transaction	27,511	-	27,511	-

Gain on Visa transaction arises on the disposal of the Bank's membership interest in Visa Europe. In June 2016 Visa Inc. completed the acquisition of Visa Europe. This transaction resulted in a receipt of an upfront cash consideration, preference shares and a deferred cash payment. The total income on this transaction, recognised in profit for the year, amounts to €27.5 million. The preference shares have been recognised at the value provided to all holders by Visa and adjusted by a haircut of 50%, to reflect litigation and liquidity risks.

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
7. EMPLOYEE COMPENSATION AND BENEFITS				
Employee compensation and benefits				
- wages and salaries	53,435	46,478	51,402	44,871
- social security costs	3,218	2,923	3,119	2,824
- retirement benefits	3,397	8,792	3,397	8,792
- other staff costs	4,118	3,507	4,118	3,507
	64,168	61,700	62,036	59,994

	The Group		The Bank	
	2016	2015	2016	2015
	No. of persons	No. of persons	No. of persons	No. of persons
The average number of employees are analysed as follows:				
Managerial	521	544	501	527
Supervisory and clerical	949	877	906	843
Others	48	51	43	46
	1,518	1,472	1,450	1,416

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
8. NET IMPAIRMENT LOSSES				
Loans and advances to customers				
- specific allowances	53,323	89,317	53,323	89,317
- collective allowances	1,579	8,910	1,579	8,910
- bad debts written off	52,581	5,897	52,581	5,853
	107,483	104,124	107,483	104,080
Reversals of write-downs:				
Investments and other assets				
- specific allowances	(107)	-	(102)	-
Loans and advances to customers				
- specific allowances	(77,629)	(19,200)	(77,629)	(19,200)
- collective allowances	(4,681)	(50,161)	(4,681)	(50,161)
- bad debts recovered	(1,924)	(2,053)	(1,924)	(2,053)
	(84,234)	(71,414)	(84,234)	(71,414)
Net impairment losses	23,142	32,710	23,147	32,666

During the financial year ending 30 September 2016 a number of long outstanding non performance exposures, which were mostly provided for, were written off. As a result, the allowances held in respect of those exposures were duly reversed.

During the financial year ended 30 September 2015 the Bank has adopted a new provisioning methodology which focuses more on the assessment of individual exposures, rather than a collective assessment. Collective allowances have been retained for losses incurred on performing exposures but cannot as yet be specifically identified. Those exposures which are deemed to carry a particular specific risk, are now subjected to an assessment to estimate the specific provision required. This new methodology resulted in €44m of provisions previously treated as collective provisions now deemed to be individual in nature.

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
9. PROFIT BEFORE TAX				
Profit before tax is stated after charging:				
Total remuneration payable to the external auditors of the parent company				
- the audit of financial statements	210	201	186	177
- other assurance services	143	29	138	27
- tax advisory services	15	-	9	-
- other services	48	6	48	6
	416	236	381	210
Directors' emoluments				
- fees	276	274	276	274
- directors' salaries as full-time bank employees	55	51	55	51
	331	325	331	325
Compensation to other key management personnel is analysed as follows				
- other fees	39	46	-	-
- short term employee benefits	632	498	632	498
	671	544	632	498
Total remuneration for directors and other key management personnel	1,002	869	963	823

Notes to the financial statements 30 September 2016 (continued)

10. INCOME TAX EXPENSE

	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Current				
- for the year	31,677	47,744	31,729	48,488
- over provision in prior years	(1,307)	-	(1,307)	-
Deferred	20,338	(9,773)	20,338	(9,773)
	50,708	37,971	50,760	38,715

The charge for income tax is based on the taxable profit for the year 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 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Profit before tax	145,906	117,915	144,943	111,065
Tax at the applicable rate of 35%	51,067	41,270	50,730	38,873
Tax effect of:				
Exempt and untaxed dividends	(117)	(100)	(1,044)	(1,065)
Share of results of equity-accounted investees	(1,306)	(4,125)	-	-
Withholding tax on property sales	173	(36)	173	(36)
Depreciation on premises	303	286	303	286
Non-deductable expenses	821	34	821	34
Investment holdings	21	231	21	231
Actuarial losses on defined benefit plans	1,060	386	1,060	386
Over provision in prior years	(1,307)	-	(1,307)	-
Other differences	(7)	25	3	6
Income tax expense	50,708	37,971	50,760	38,715

11. EARNINGS PER SHARE

	The Group 2016 cents per share	The Group 2015 cents per share	The Bank 2016 cents per share	The Bank 2015 cents per share
Earnings per share	24c3	20c4	24c1	18c6

The earnings per share for the Group and for the Bank have been calculated on the profits attributable to shareholders of the Group and the Bank, as shown in the statements of profit or loss, divided by the 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 disclosed in note 31.

Earnings per share was calculated on profit attributable to shareholders of the Group €94,742,000 (2015: €79,378,000) and the Bank €94,183,000 (2015: €72,350,000) divided by 390,000,000 shares outstanding as at 30 September 2016.

Notes to the financial statements 30 September 2016 (continued)

12. DIVIDENDS

The amount of dividends recognised as distributions to equity holders during the year, and the related amount per share, are as follows:

	The Bank			
	2016	2015	2016	2015
	cents per share	cents per share	€000	€000
Gross of income tax				
- prior year's final paid	7.8	7.8	30,600	30,525
- interim paid	3.9	3.9	15,249	14,040
	11.7	11.7	45,849	44,565
Net of income tax				
- prior year's final paid	5.1	5.1	19,890	19,841
- interim paid	2.5	2.3	9,912	9,126
	7.6	7.4	29,802	28,967

The calculation of the dividend per share for all periods presented was adjusted retrospectively in view of the increase in the number of ordinary shares outstanding as at 30 September 2016 as a result of the bonus issue of shares, as disclosed in note 31.

For tax purposes, the dividend is being paid out of profits taxed at 35% (2015: 35%).

In respect of the current year, the directors propose that a final gross ordinary dividend of €0.0852 per share amounting to €33.2 million (net ordinary dividend of €0.055 per share - €21.6 million) be paid to shareholders. This dividend is subject to approval by shareholders at the Annual General Meeting and has not been included as a liability in these financial statements. The proposed dividend is payable to all shareholders on the register of members on 16 December 2016.

13. BALANCES WITH CENTRAL BANK OF MALTA, TREASURY BILLS AND CASH

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
Balances with Central Bank of Malta	87,779	79,284	87,779	79,284
Malta Government Treasury Bills	39,017	6,002	39,017	6,002
Cash	44,254	41,366	44,254	41,366
	171,050	126,652	171,050	126,652

Balances with the Central Bank of Malta include Reserve Deposit amounting to €87.8 million (2015: €79.1 million) in respect of both the Group and the Bank, in terms of Regulation (EC) No. 1745/2003 of the European Central Bank. Balances with Central Bank of Malta and Malta Government Treasury Bills are subject to negative interest rates.

Notes to the financial statements 30 September 2016 (continued)

	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
14. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS				
Financial assets at fair value through profit or loss				
Financial assets classified as held for trading:				
Derivative financial instruments	5,365	15,156	5,365	15,156
Financial assets designated at fair value through profit or loss:				
Debt and other fixed income instruments	186,015	275,935	186,015	275,935
Equity and other non-fixed income instruments	79,734	77,210	78,596	75,246
Loans and advances to customers (note 17)	121,316	49,221	121,316	49,221
	387,065	402,366	385,927	400,402
	392,430	417,522	391,292	415,558

No financial assets at fair value through profit or loss have been pledged against the provision of credit lines by the Central Bank of Malta (2015: nil).

	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Financial liabilities at fair value through profit or loss				
Financial liabilities classified as held for trading:				
Derivative financial instruments	20,327	25,077	20,327	25,077

14.1 Debt and other fixed income instruments

	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Issued by public bodies				
- local general government	56,238	70,809	56,238	70,809
- foreign general government	34,199	38,443	34,199	38,443
	90,437	109,252	90,437	109,252
Issued by other issuers				
- local banks	4,508	3,662	4,508	3,662
- foreign banks	49,289	102,593	49,289	102,593
- foreign other	33,206	50,570	33,206	50,570
- local other	8,575	9,858	8,575	9,858
	95,578	166,683	95,578	166,683
	186,015	275,935	186,015	275,935
Listing status				
- listed on Malta Stock Exchange	69,321	84,329	69,321	84,329
- listed elsewhere	113,399	168,505	113,399	168,505
- foreign unlisted	3,295	23,101	3,295	23,101
	186,015	275,935	186,015	275,935
Summary of movements during the year:				
At the beginning of the year	275,935	392,248	275,935	392,248
Acquisitions	7,710	64,731	7,710	64,731
Disposals	(95,821)	(183,997)	(95,821)	(183,997)
Movement in fair value	(1,742)	(2,077)	(1,742)	(2,077)
Exchange adjustment	(67)	5,030	(67)	5,030
At the end of the year	186,015	275,935	186,015	275,935

Notes to the financial statements 30 September 2016 (continued)

14. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
14.2 Equity and other non-fixed income instruments				
Issued by other issuers				
- local banks	12,936	598	12,936	598
- foreign banks	14,527	2,084	14,527	2,084
- foreign other	26,576	38,568	26,576	38,568
- local other	25,695	35,960	24,557	33,996
	79,734	77,210	78,596	75,246
Listing status				
- listed on Malta Stock Exchange	38,634	36,561	37,496	34,597
- listed elsewhere	16,306	16,622	16,306	16,622
- foreign unlisted	24,794	24,027	24,794	24,027
	79,734	77,210	78,596	75,246
Summary of movements during the year:				
At the beginning of the year	77,210	68,761	75,246	64,467
Acquisitions	1,550	7,900	1,550	7,900
Disposals	(2,853)	(10,830)	(2,027)	(8,500)
Movement in fair value	4,527	10,947	4,527	10,947
Exchange adjustment	(700)	432	(700)	432
At the end of the year	79,734	77,210	78,596	75,246

14.3 Derivative financial instruments

	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
Fair value of assets	5,365	15,156	5,365	15,156
Fair value of liabilities	20,327	25,077	20,327	25,077

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:

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
- less than 3 months	546,091	788,851	546,091	788,851
- between 3 months and 1 year	67,599	29,943	67,599	29,943
- more than 1 year	192,015	221,857	192,015	221,857
	805,705	1,040,651	805,705	1,040,651

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
15. INVESTMENTS				
Debt and other fixed income instruments				
- available-for-sale	272,243	257,453	272,243	257,453
- held-to-maturity	3,460,446	3,117,808	3,460,446	3,117,808
Equity and other non-fixed income instruments				
- available-for-sale	3,583	1,044	3,583	1,044
	3,736,272	3,376,305	3,736,272	3,376,305

Investments with a nominal value of €74.1 million (2015: €86.1 million) have been pledged against the provision of credit lines by the Central Bank of Malta.

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
15.1 Debt and other fixed income instruments available-for-sale				
Issued by public bodies				
- local general government	179,461	168,572	179,461	168,572
- local public sector	88,805	84,854	88,805	84,854
Issued by other issuers				
- foreign banks	3,977	4,027	3,977	4,027
	272,243	257,453	272,243	257,453
Listing status				
- listed on Malta Stock Exchange	268,266	253,426	268,266	253,426
- foreign unlisted	3,977	4,027	3,977	4,027
	272,243	257,453	272,243	257,453
Summary of movements during the year:				
At the beginning of the year	257,453	290,726	257,453	290,726
Acquisitions	150,745	27,319	150,745	27,319
Disposals	(130,842)	(77,879)	(130,842)	(77,879)
Redeemed	(12,094)	(5,893)	(12,094)	(5,893)
Amortisation	(2,463)	(913)	(2,463)	(913)
Movement in fair value	1,780	9,429	1,780	9,429
Profit on disposal	7,365	3,747	7,365	3,747
Exchange adjustment	299	10,917	299	10,917
At the end of the year	272,243	257,453	272,243	257,453

Notes to the financial statements 30 September 2016 (continued)

15. INVESTMENTS (continued)

	The Group		The Bank	
	2016	**2015**	**2016**	**2015**
	€000	**€000**	**€000**	**€000**
15.2 Debt and other fixed income instruments held-to-maturity				
Issued by public bodies				
- local general government	484,791	566,137	484,791	566,137
- foreign general government	671,749	454,641	671,749	454,641
	1,156,540	1,020,778	1,156,540	1,020,778
Issued by other issuers				
- foreign banks	1,653,880	1,439,507	1,653,880	1,439,507
- foreign other	650,026	657,523	650,026	657,523
	2,303,906	2,097,030	2,303,906	2,097,030
	3,460,446	3,117,808	3,460,446	3,117,808
Listing status				
- listed on Malta Stock Exchange	484,791	566,137	484,791	566,137
- listed elsewhere	2,252,717	1,889,877	2,252,717	1,889,877
- foreign unlisted	722,938	661,794	722,938	661,794
	3,460,446	3,117,808	3,460,446	3,117,808

At 30 September 2016, the fair value of held-to-maturity securities, without deducting transaction costs, amounted to €3,511.4 million (2015: €3,169.5 million).

	The Group		The Bank	
	2016	**2015**	**2016**	**2015**
	€000	**€000**	**€000**	**€000**
Summary of movements during the year:				
At the beginning of the year	3,117,808	2,130,567	3,117,808	2,130,567
Acquisitions	1,106,801	1,532,770	1,106,801	1,532,770
Redemptions	(726,248)	(622,841)	(726,248)	(622,841)
Amortisation	(9,308)	(9,744)	(9,308)	(9,744)
Loss on early redemptions	-	(9)	-	(9)
Exchange adjustment	(28,607)	87,065	(28,607)	87,065
At the end of the year	3,460,446	3,117,808	3,460,446	3,117,808

15.3 Equity and other non-fixed income instruments available-for-sale

	The Group		The Bank	
	2016	**2015**	**2016**	**2015**
	€000	**€000**	**€000**	**€000**
Issued by other issuers				
- local other	-	1,044	-	1,044
- foreign other	3,583	-	3,583	-
	3,583	1,044	3,583	1,044
Listing status				
- local unlisted	-	1,044	-	1,044
- foreign listed	3,583	-	3,583	-
	3,583	1,044	3,583	1,044
Summary of movements during the year:				
At the beginning of the year	1,044	944	1,044	944
Shares acquired under Visa transaction	3,583	-	3,583	-
Other Acquisitions	-	100	-	100
Disposals	(1,044)	-	(1,044)	-
At the end of the year	3,583	1,044	3,583	1,044

Notes to the financial statements 30 September 2016 (continued)

16. LOANS AND ADVANCES TO BANKS

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
Repayable on call and at short notice	181,645	390,506	181,645	390,506
Term placements with Central Bank of Malta	1,619,029	887,629	1,619,029	887,629
Term placements with other banks	283,450	359,461	283,450	359,461
Cheques in course of collection	14,315	18,750	14,315	18,750
	2,098,439	1,656,346	2,098,439	1,656,346

Balances with Central Bank of Malta with a value of €9.1million (2015: €9.1million) have been pledged in favour of the Depositor Compensation Scheme.

Balances with a value of €40.4 million (2015: €69.9 million) were held as collateral against derivative contracts.

Balances held with Central Bank of Malta and with other banks are subject to negative interest rates.

17. LOANS AND ADVANCES TO CUSTOMERS

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
Repayable on call and at short notice	504,272	564,017	504,272	564,017
Term loans and advances	3,683,096	3,676,132	3,683,096	3,676,132
	4,187,368	4,240,149	4,187,368	4,240,149
Less impairment losses	(185,712)	(238,310)	(185,712)	(238,310)
Net loans and advances at amortised cost	4,001,656	4,001,839	4,001,656	4,001,839
Loans and advances designated at fair value through profit or loss (note 14)	121,316	49,221	121,316	49,221
Total loans and advances	4,122,972	4,051,060	4,122,972	4,051,060
Impairment losses				
- individually assessed allowances	170,776	220,272	170,777	220,272
- collective allowances	14,936	18,038	14,935	18,038
	185,712	238,310	185,712	238,310

The balance of individually assessed allowances at the reporting date includes €53.6 million (2015: €78.8million) in respect of interest in suspense which has been netted off against interest receivable.

During the financial year ending 30 September 2016 a number of long outstanding non performance exposures, which were mostly provided for, were written off. As a result, the allowances held in respect of those exposures were duly reversed.

Notes to the financial statements 30 September 2016 (continued)

18. INVESTMENTS IN EQUITY-ACCOUNTED INVESTEES

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
At the beginning of the year	96,904	88,553	52,870	52,870
Share of results, net of tax	3,730	11,786	-	-
Dividend received	(3,593)	(3,435)	-	-
At the end of the year	97,041	96,904	52,870	52,870
Amounts include:				
Local listed	24,483	25,243	22,304	22,304
Local unlisted	72,558	71,661	30,566	30,566
	97,041	96,904	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 (2015: €52.9 million).

The fair value of the equity-accounted investees' that is publicly quoted amounted to €60.0 million at 30 September 2016 (2015: €65.2 million).

The fair value measurement is a Level 1 input.

	Equity Interest		Class	Incorporated in	Nature of Business
	2016	2015			
Name of company	%	%			
Mapfre Middlesea p.l.c.	31.08	31.08	Ordinary	Malta	Insurance
MSV Life p.l.c.*	50.00	50.00	Ordinary	Malta	Life Assurance

	Group's share of results	
	2016	2015
Name of company	€000	€000
Mapfre Middlesea p.l.c.	333	3,667
MSV Life p.l.c.	3,397	8,119
	3,730	11,786

*A further 15.54% (2015: 15.54%) is held indirectly via another equity-accounted investee. Although the Bank has an effective participating interest of 65.54% (2015: 65.54%), it does not exercise control over the financial and operating decisions of the entity as it only has the right for equal representation on the Board of Directors of the company together with the other shareholders. Furthermore, as from 1 October 2011 the Bank is deemed to exercise significant influence on 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 financial year 2012 it is being treated as an equity-accounted investee.

The financial statements of the equity-accounted investees are prepared to 31 December. Given that it was impracticable to obtain financial statements to the Group's year end, the published June 2016 interim financial statements were used as a basis to determine the Group's share of results to 30 September 2016.

The registered addresses of the above undertakings are as follows:

Mapfre Middlesea p.l.c.	Middlesea House, Floriana FRN 1442, Malta
MSV Life p.l.c.	Level 7, The Mall, Floriana FRN 1420, Malta

Notes to the financial statements 30 September 2016 (continued)

18. INVESTMENTS IN EQUITY-ACCOUNTED INVESTEES (continued)

Summarised financial information extracted from the published interim condensed financial statements as at 30 June 2016 in respect of the equity-accounted investees:

	Equity-accounted investees 2016 €000	Equity-accounted investees 2015 €000
Total assets	1,899,580	1,747,824
Total liabilities	1,741,420	1,591,460
Revenues	170,891	196,359
Results for the period	4,020	9,770

	The Group	
	2016 €000	2015 €000
Share of net assets of equity-accounted investees	97,041	96,904
Share of results of equity-accounted investees	3,730	11,786

The share of results of equity-accounted investees comprise the Group's share of profits and the Group's share of the movement in the valuation of the in-force business of the entities, for the twelve month period June 2015 to June 2016. Due consideration was given to market information published in the period up to the publication date of the Group.

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 entity 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 16% of the result for the year. The PVIF represents 33% of the carrying value of the investments in equity-accounted investees.

This valuation assumes a spread of 2% (2015: 2%) between the weighted average projected investment return and the risk adjusted discount factor applied of 7.5% (2015: 7.5%). The calculation also assumes lapse rates varying from 0.5% to 8% per annum (2015: 0.5% to 8% per annum) and an expense inflation rate of 3.5% (2015: 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 30 September 2016 (continued)

19. INVESTMENTS IN SUBSIDIARY COMPANIES

	Equity interest		Class	Incorporated in	Nature of Business
	2016	2015			
Name of company	%	%			
Valletta Fund Management Limited	100	60*	Ordinary	Malta	Fund Management
Valletta Fund Services Limited	100	100	Ordinary	Malta	Fund Administration

	The Bank	
	2016	2015
Name of company	€000	€000
Valletta Fund Management Limited	5,481	481
Valletta Fund Services Limited	749	749
	6,230	1,230

The registered address of the above unlisted undertakings is as follows:

Valletta Fund Management Limited	TG Complex, Suite 2, Level 3, Brewery Street, Mriehel BKR 3000
Valletta Fund Services Limited	TG Complex, Suite 2, Level 3, Brewery Street, Mriehel BKR 3000

All subsidiaries prepare their financial statements to the same date, 30 September.

In August 2016, the Group acquired an additional 40% interest in Valletta Fund Management Limited for a cash consideration of €5 million. The Group:
- derecognised a Non-controlling Interest of €954,000, comprising of Non-controlling Interest to date of acquisition less dividends paid to the Non-controlling Interest;
- recognised a decrease of €4,046,000 in Retained Earnings.

*The total assets and liabilites of Valletta Fund Management Limited amounted to €3.5 million (2015: €4.8 million) and €0.8 million (2015: €1.6 million) respectively. Profit for the year amounted to €1.3 million (2015: €1.4 million).

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
20. INTANGIBLE ASSETS				
Software				
Cost				
1 October	25,561	21,907	25,561	21,907
Additions	4,089	3,654	4,089	3,654
30 September	29,650	25,561	29,650	25,561
Accumulated amortisation				
1 October	12,839	10,265	12,839	10,265
Charge for the year	3,539	2,574	3,539	2,574
30 September	16,378	12,839	16,378	12,839
Carrying amount at 30 September	13,272	12,722	13,272	12,722
Future capital expenditure:				
- contracted but not provided for in the financial statements	112	376	112	376
- authorised by the directors but not contracted for	1,199	908	1,199	908

Notes to the financial statements 30 September 2016 (continued)

21. PROPERTY AND EQUIPMENT

	Land and buildings €000	IT infrastructure and equipment €000	Other €000	Total €000
The Group				
Cost or valuation				
30 September 2014	85,391	18,239	26,979	130,609
Additions	1,685	2,365	1,428	5,478
Disposals	-	-	(5)	(5)
Revaluation	1,319	-	-	1,319
30 September 2015	88,395	20,604	28,402	137,401
Additions	931	2,211	880	4,022
Disposals	(532)	-	-	(532)
Revaluation	960	-	-	960
30 September 2016	89,754	22,815	29,282	141,851
Accumulated depreciation				
30 September 2014	12,827	10,749	18,917	42,493
Provision for the year	825	2,642	1,640	5,107
30 September 2015	13,652	13,391	20,557	47,600
Provision for the year	865	2,597	1,506	4,968
Disposals	(291)	-	-	(291)
30 September 2016	14,226	15,988	22,063	52,277
Carrying amount at:				
30 September 2014	72,564	7,490	8,062	88,116
30 September 2015	74,743	7,213	7,845	89,801
30 September 2016	75,528	6,827	7,219	89,574
The Bank				
Cost or valuation				
30 September 2014	85,357	17,594	25,465	128,416
Additions	1,680	2,366	1,419	5,465
Revaluation	1,319	-	-	1,319
30 September 2015	88,356	19,960	26,884	135,200
Additions	931	2,211	839	3,981
Disposals	(532)	-	-	(532)
Revaluation	960	-	-	960
30 September 2016	89,715	22,171	27,723	139,609
Accumulated depreciation				
30 September 2014	12,739	9,926	17,862	40,527
Provision for the year	820	2,642	1,560	5,022
30 September 2015	13,559	12,568	19,422	45,549
Provision for the year	865	2,597	1,437	4,899
Disposals	(291)	-	-	(291)
30 September 2016	14,133	15,165	20,859	50,157
Carrying amount at:				
30 September 2014	72,618	7,668	7,603	87,889
30 September 2015	74,797	7,392	7,462	89,651
30 September 2016	75,582	7,006	6,864	89,452

Notes to the financial statements 30 September 2016 (continued)

21. PROPERTY AND EQUIPMENT (continued)

	The Group		The Bank	
	2016	**2015**	**2016**	**2015**
	€000	**€000**	**€000**	**€000**
Carrying amount of land and buildings occupied for own use	75,528	74,743	75,582	74,797
Future capital expenditure:				
- contracted but not provided for in the financial statements	3,465	3,612	3,465	3,612
- authorised by the directors but not contracted for	2,555	-	2,555	-

Land and buildings are revalued by a professionally qualified architect 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:
2016: Group and Bank €43.8 million (2015: Group and Bank €43.7 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 30 September 2015. Revaluations are carried out during the year and, as at September 2016, there were no material changes from date of valuation.

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 EUR 50/sqm to EUR 789/sqm	The higher the price per square metre the higher the fair value
	Capitalisation rate, ranging from 5% to 8%	The higher the capitalisation rate the lower the fair value
Buildings in Residential Area	Price per square metre, ranging from EUR 10/sqm to EUR 250/sqm	The higher the price per square metre the higher the fair value
	Capitalisation rate, ranging from 5.5% to 6%	The higher the capitalisation rate the lower the fair value

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
22. DEFERRED TAX				
Deferred taxation is analysed as follows:				
Net deferred tax asset arising on:				
Fair value movement of financial instruments	(4,221)	(4,605)	(4,221)	(4,605)
Impairment losses	66,947	85,384	66,947	85,384
Allowance for employee benefits	6,960	8,825	6,960	8,825
Excess of capital allowances over depreciation	(4,563)	(4,529)	(4,563)	(4,529)
Defined benefit plans	2,075	1,567	2,075	1,567
Other temporary differences	(10)	12	(10)	12
	67,188	86,654	67,188	86,654
Deferred tax liability arising on:				
Property revaluation	4,318	4,382	4,318	4,382

	The Group and the Bank			
	At 1 October 2015	Recognised in profit or loss	Recognised in equity	At 30 September 2016
	€000	€000	€000	€000
Movement in temporary differences relating to:				
Fair value movement of financial instruments	(4,605)	-	384	(4,221)
Impairment losses	85,384	(18,437)	-	66,947
Allowance for employee benefits	8,825	(1,865)	-	6,960
Excess of capital allowances over depreciation	(4,529)	(34)	-	(4,563)
Defined benefit plans	1,567	-	508	2,075
Property revaluation	(4,382)	20	44	(4,318)
Other temporary differences	12	(22)	-	(10)
	82,272	(20,338)	936	62,870

	The Group and the Bank			
	At 1 October 2014	Recognised in profit or loss	Recognised in equity	At 30 September 2015
	€000	€000	€000	€000
Movement in temporary differences relating to:				
Fair value movement of financial instruments	(2,428)	-	(2,177)	(4,605)
Impairment losses	75,775	9,609	-	85,384
Allowance for employee benefits	7,811	1,014	-	8,825
Excess of capital allowances over depreciation	(4,182)	(347)	-	(4,529)
Defined benefit plans	1,059	-	508	1,567
Property revaluation	(5,100)	-	718	(4,382)
Other temporary differences	515	(503)	-	12
	73,450	9,773	(951)	82,272

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 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
23. PREPAYMENTS AND ACCRUED INCOME				
Accrued income	18,788	20,061	18,788	20,061
Prepayments	4,289	1,600	3,909	2,033
	23,077	21,661	22,697	22,094
24. AMOUNTS OWED TO BANKS				
Term deposits	118,202	95,608	118,202	95,608
Repayable on demand	131,953	102,152	131,953	102,152
	250,155	197,760	250,155	197,760
25. AMOUNTS OWED TO CUSTOMERS				
Term deposits	2,084,220	2,248,019	2,084,220	2,248,019
Repayable on demand	7,096,827	6,311,712	7,100,250	6,315,088
	9,181,047	8,559,731	9,184,470	8,563,107
26. DEBT SECURITIES IN ISSUE				
4.80% Euro debt securities	55,400	55,400	55,400	55,400
4.25% Euro debt securities	40,000	40,000	40,000	40,000
	95,400	95,400	95,400	95,400

The 4.8% Euro unsubordinated bonds are redeemable at par on 27 August 2018 and are listed on the Malta Stock Exchange. The fair value of these unsecured bonds as at 30 September 2016 is €58.1 million (2015: €58.3 million).

The 4.25% Euro unsubordinated bonds are redeemable at par on 17 May 2019 and are listed on the Malta Stock Exchange. The fair value of these unsecured bonds as at 30 September 2016 is €40.9 million (2015: €42.1 million).

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
27. OTHER LIABILITIES				
Post employment and termination liabilities (see note 35)	25,813	26,666	25,813	26,666
Cash collateral for commitments	33,252	32,933	33,252	32,933
Deposits from companies in formation	3,498	9,448	3,498	9,448
Bills payable	41,401	43,938	41,401	43,938
Accruals and deferred income	22,256	18,859	22,256	18,859
Payment orders outwards	23,026	20,424	23,026	20,424
Other	24,742	20,637	24,557	20,475
	173,988	172,905	173,803	172,743
28. ACCRUALS AND DEFERRED INCOME				
Accrued interest	16,215	21,317	15,802	20,725
29. DERIVATIVES DESIGNATED FOR HEDGE ACCOUNTING				
Derivative financial instruments designated as fair value hedges	20,649	35,201	20,649	35,201

The above comprise over-the-counter interest rate swaps stated at fair value with notional amounts analysed by remaining life as follows:

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
- less than 3 months	-	4,700	-	4,700
- between 3 months and 1 year	-	8,304	-	8,304
- more than 1 year	63,197	138,133	63,197	138,133

30. SUBORDINATED LIABILITIES

5.35% Euro subordinated unsecured bonds	50,000	50,000	50,000	50,000
4.80% Euro subordinated unsecured bonds	70,000	70,000	70,000	70,000
3.50% Euro subordinated unsecured bonds	111,591	-	111,591	-
	231,591	120,000	231,591	120,000

The 5.35% Euro subordinated bonds are redeemable at par on 15 June 2019 and are listed on the Malta Stock Exchange. The fair value of these unsecured bonds as at 30 September 2016 is €52.6 million (2015: €53.4 million).

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 30 September 2016 is €73.5 million (2015: €75.3 million).

The 3.5% Euro subordinated bonds, which were issued during this financial year, 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 30 September 2016 is €109.4 million (2015: nil).

	The Bank	
	2016	2015
31. SHARE CAPITAL	€000	€000
Share capital		
Authorised:		
500,000,000 Ordinary shares of €1.00 each	500,000	500,000
(2015: 500,000,000 Ordinary shares of €1.00 each)		
Issued and paid up:		
390,000,000 Ordinary shares of €1.00 each fully paid	390,000	360,000
(2015: 360,000,000 Ordinary shares of €1.00 each fully paid)		

Notes to the financial statements 30 September 2016 (continued)

31. SHARE CAPITAL (continued)

On 15 January 2016 the Bank made a bonus issue of 30 million fully paid ordinary shares of a nominal value of €1.00 per share, representing one bonus share for every 12 shares held, thereby increasing the issued share capital from 360 million shares to 390 million shares, resulting in a paid up capital of €390 million.

On 16 January 2015 the Bank made a bonus issue of 30 million fully paid ordinary shares of a nominal value of €1.00 per share, representing one bonus share for every 11 shares held, thereby increasing the issued share capital from 330 million shares to 360 million shares, resulting in a paid up capital of €360 million.

32. OTHER RESERVES

Retained Earnings
Retained earnings represent the profits retained over the years and primarily comprise the profit attributable to equity holders after deducting dividends paid and transfers to share capital in respect of bonus issues. 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, in line with the three year transitional rules, this reserve amounts to €4.5 million.

Revaluation Reserves
Revaluation reserves represent fair value movements on land and buildings and available-for-sale investments, net of tax, which are recognised in Other Comprehensive Income

	The Group	The Bank
	€000	€000
On land and buildings:		
1 October 2014	24,592	24,561
Property revaluation	1,319	1,319
Deferred tax	718	718
30 September 2015	26,629	26,598
Property revaluation	960	960
Deferred tax and effect of changes in property tax rates	44	44
Release of surplus on sale of property, net of tax	(174)	(174)
30 September 2016	**27,459**	**27,428**
On available-for-sale investments:		
1 October 2014	4,544	4,463
Fair value adjustments	9,968	9,968
Transfer to profit or loss on disposal	(3,747)	(3,747)
Deferred tax	(2,177)	(2,177)
30 September 2015	8,588	8,507
Fair value adjustments	33,777	33,777
Transfer to profit or loss on disposal	(34,876)	(34,876)
Deferred tax	384	384
30 September 2016	**7,873**	**7,792**
Total	**35,332**	**35,220**

Notes to the financial statements 30 September 2016 (continued)

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
33. CONTINGENT LIABILITIES				
Acceptances and endorsements	2,502	1,768	2,502	1,768
Guarantees	209,209	225,936	209,209	225,936
Provision for default on forward contracts	1,356	13,288	1,356	13,288
Other contingent liabilities	12,340	10,678	12,340	10,678
	225,407	251,670	225,407	251,670

Contingent liabilities are backed by corresponding obligations from third parties.

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
34. COMMITMENTS				
Documentary credits	110,671	153,299	110,671	153,299
Undrawn formal standby facilities, credit facilities and other commitments to lend	1,467,135	1,429,943	1,467,135	1,429,943
Capital expenditure contracted but not provided for in the financial statements	3,577	3,988	3,577	3,988
Commitments to financial institutions	8,773	24,892	8,773	24,892
	1,590,156	1,612,122	1,590,156	1,612,122

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 provision in relation to this plan accounts for 90% (2015 – 87%) of the year end provision for employee and termination benefits in Note 27.

The Group and the Bank also operate an early retirement scheme whereby accepted applicants are given a lump sum payment of three times their terminal salary, or are paid two thirds of their terminal salary on a monthly basis until reaching retirement age.

Furthermore, the Group and the Bank makes payments to certain eligible employees in consideration of the liquidation of a defunct pension scheme.

Notes to the financial statements 30 September 2016 (continued)

35. POST EMPLOYMENT AND TERMINATION LIABILITIES (continued)

The movement in the plans may be analysed as follows:

	The Group and the Bank	
Post Employment and Termination Liabilities	**2016**	**2015**
	€000	**€000**
Present value at 1 October	26,666	25,346
Payments effected	(5,698)	(8,923)
Recognised in profit or loss:		
- Interest expense	448	1,455
- Service cost	3	3
- Terminal benefits	2,946	7,334
Remeasurement of actuarial gains and losses recognised in other comprehensive income resulting from:		
- Experience adjustments	144	(32)
- Changes in financial assumptions	1,398	1,290
- Changes in demographic assumptions	(94)	193
Present value at 30 September	25,813	26,666

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	
	2016	**2015**
Discount rates	0.37%	1.27%
Life expectancy (years):		
Males	78	78
Females	83	83

The Group and the Bank are providing sensitivity analysis in connection with each significant actuarial assumption applied in respect of the plan. These analysis 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 €1.4m (increases by €1.6m)
- 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 €3.6m (decreases by €3.6m).

The weighted average duration of the liability in respect of the plan at 30 September 2016 is 12 years (2015 :13 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.

Notes to the financial statements 30 September 2016 (continued)

36. NOTES TO THE CASH FLOW STATEMENTS

	The Group		The Bank	
	2016	2015	2016	2015
	€000	€000	€000	€000
Cash	44,254	41,366	44,254	41,366
Balances with Central Bank of Malta (excluding Reserve Deposit)	-	149	-	149
Treasury bills (with original maturity of less than 3 months)	39,017	6,002	39,017	6,002
Money at call and short notice	1,896,720	1,443,337	1,896,720	1,443,337
Amounts owed to banks	(131,953)	(181,507)	(131,953)	(181,507)
Cash and cash equivalents included in the cash flow statement	**1,848,038**	**1,309,347**	**1,848,038**	**1,309,347**
Balances with contractual maturity of more than 3 months	83,517	196,756	83,517	196,756
	1,931,555	1,506,103	1,931,555	1,506,103
Equivalent items reported in the statement of financial position:				
Balances with Central Bank of Malta, Treasury bills and cash (excluding Reserve Deposit)	83,271	47,517	83,271	47,517
Loans and advances to banks	2,098,439	1,656,346	2,098,439	1,656,346
Amounts owed to banks	(250,155)	(197,760)	(250,155)	(197,760)
	1,931,555	1,506,103	1,931,555	1,506,103

37. RELATED PARTY TRANSACTIONS

During the current and the prior year, the Group and the Bank entered into transactions during the course of their normal business, with key management personnel, equity-accounted investees, the Government of Malta ("The Government") (which has a 25.23% holding in the Bank), Government related entities 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 dependents.

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.

Notes to the financial statements 30 September 2016 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The amounts due to or from related parties are settled in cash and the amount of related party transactions and outstanding balances are disclosed below:

The Group	2016 Related party transactions		2015 Related party transactions	
	€000	% of total	€000	% of total
Interest and similar income:				
- on loans and advances, balances with Central Bank of Malta and treasury bills				
The Government	636		577	
Government related entities	16,251		16,941	
Key management personnel	4		6	
Other related parties	376		1,009	
	17,267	11%	18,533	12%
Interest and similar income:				
- on debt and other fixed income instruments				
The Government	26,322	49%	29,213	51%
Interest expense				
Equity-accounted investees	1,073		2,172	
The Government	4,655		1,145	
Government related entities	220		367	
Key management personnel	11		10	
Other related parties	4		9	
	5,963	9%	3,703	5%
Fee and commission income				
Equity-accounted investees	5,895		4,851	
The Government	68		45	
Government related entities	416		685	
Key management personnel	2		1	
Other related parties	10		15	
	6,391	9%	5,597	8%
Employee compensation and benefits				
Key management personnel	1,002	2%	869	1%
General administrative expenses				
Equity-accounted investees	123		77	
Key management personnel	38		36	
Other related parties	199		108	
	360	1%	221	1%
Movement in impairment allowances				
The Government	(20)		(3)	
Government related entities	1,789		8,823	
Other related parties	(398)		253	
	1,371	6%	9,073	28%

Notes to the financial statements 30 September 2016 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Group	2016 Related party balances €000	2016 % of total	2015 Related party balances €000	2015 % of total
Balances with Central Bank of Malta, treasury bills and cash				
The Government	126,796	74%	85,286	67%
Financial assets at fair value through profit or loss				
The Government	56,238	14%	70,809	17%
Investments				
The Government	664,252	18%	734,709	22%
Loans and advances to customers				
The Government	16,597		16,192	
Government related entities	464,658		499,773	
Key management personnel	1,433		764	
Other related parties	5,393		20,904	
	488,081	12%	537,633	13%
Loans and advances to banks				
The Government	1,619,029	77%	887,629	54%
Impairment allowances				
The Government	(146)		(166)	
Government related entities	(11,808)		(10,019)	
Other related parties	(20)		(418)	
	(11,974)	6%	(10,603)	4%
Amounts owed to customers				
Equity-accounted investees	229,000		209,977	
The Government	298,137		86,171	
Government related entities	110,393		178,995	
Key management personnel	2,034		1,312	
Other related parties	6,036		9,464	
	645,600	7%	485,919	6%
Total Assets less Liabilities				
Equity-accounted investees	(229,000)		(209,977)	
The Government	2,184,629		1,708,288	
Government related entities	342,457		310,759	
Key management personnel	(601)		(548)	
Other related parties	(663)		11,022	
	2,296,822		1,819,544	
Commitments				
Equity-accounted investees	378		4,329	
The Government	13,809		5,448	
Government related entities	106,803		212,962	
Key management personnel	492		731	
Other related parties	9,248		7,569	
	130,730	8%	231,039	14%

Notes to the financial statements 30 September 2016 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Bank	2016 Related party transactions		2015 Related party transactions	
	€000	% of total	€000	% of total
Interest and similar income:				
- on loans and advances, balances with Central Bank of Malta and treasury bills				
The Government	636		577	
Government related entities	16,251		16,941	
Key management personnel	4		6	
Other related parties	186		1,009	
	17,077	11%	18,533	12%
Interest and similar income:				
- on debt and other fixed income instruments				
The Government	26,322	49%	29,213	51%
Interest expense				
Equity-accounted investees	1,073		2,172	
The Government	4,655		1,145	
Government related entities	220		367	
Key management personnel	9		9	
Other related parties	3		9	
	5,960	9%	3,702	5%
Fee and commission income				
Equity-accounted investees	5,895		4,851	
Subsidiaries	2,860		2,542	
The Government	68		45	
Government related entities	416		685	
Key management personnel	2		1	
Other related parties	9		15	
	9,250	14%	8,139	13%
Dividend income				
Equity-accounted investees	4,103		3,832	
Subsidiaries	3,631		5,989	
	7,734	80%	9,821	81%
Employee compensation and benefits				
Key management personnel	963	2%	823	1%
General administrative expenses				
Equity-accounted investees	123		77	
Key management personnel	37		36	
Other related parties	199		108	
	359	1%	221	1%
Movement in impairment allowances				
The Government	(20)		(3)	
Government related entities	1,789		8,823	
Other related parties	(417)		253	
	1,352	6%	9,073	28%

Notes to the financial statements 30 September 2016 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Bank	2016 Related party balances €000	2016 % of total	2015 Related party balances €000	2015 % of total
Balances with Central Bank of Malta, treasury bills and cash				
The Government	126,796	74%	85,286	67%
Financial assets at fair value through profit or loss				
The Government	56,238	14%	70,809	17%
Investments				
The Government	664,252	18%	734,709	22%
Loans and advances to customers				
The Government	16,597		16,192	
Government related entities	464,658		499,773	
Key management personnel	1,251		673	
Other related parties	186		20,904	
	482,692	12%	537,542	13%
Loans and advances to banks				
The Government	1,619,029	77%	887,629	54%
Impairment allowances				
The Government	(146)		(166)	
Government related entities	(11,808)		(10,019)	
Other related parties	(1)		(418)	
	(11,955)	6%	(10,603)	4%
Amounts owed to customers				
Equity-accounted investees	229,000		209,977	
Subsidiaries	3,423		3,376	
The Government	298,137		86,171	
Government related entities	110,393		178,995	
Key management personnel	1,806		1,242	
Other related parties	4,297		9,301	
	647,056	7%	489,062	6%

Notes to the financial statements 30 September 2016 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Bank	2016 Related party balances €000	% of total	2015 Related party balances €000	% of total
Total Assets less Liabilities				
Equity-accounted investees	(229,000)		(209,977)	
Subsidiaries	(3,423)		(3,376)	
The Government	2,184,629		1,708,288	
Government related entities	342,457		310,759	
Key management personnel	(555)		(569)	
Other related parties	(4,112)		11,185	
	2,289,996		1,816,310	
Commitments				
Equity-accounted investees	378		4,329	
The Government	13,809		5,448	
Government related entities	106,803		212,962	
Key management personnel	427		708	
Other related parties	5,543		7,564	
	126,960	8%	231,011	14%

	The Group 2016 €000	The Group 2015 €000	The Bank 2016 €000	The Bank 2015 €000
All outstanding balances are secured except for the following:				
Loans and advances to customers:				
- Key management personnel	21	32	11	32
- Other related parties	5	1,179	5	1,179
	26	1,211	16	1,211
Details of guarantees received are disclosed below:				
Loans and advances to customers:				
- Amounts guaranteed by The Government	528,441	521,215	528,441	521,215

Notes to the financial statements 30 September 2016 (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 1 October 2014	1,760	455	1,760	455
Additions	204	134	204	111
	1,964	589	1,964	566
Less reductions/repayments	(1,734)	(240)	(1,825)	(240)
At 30 September 2015	230	349	139	326
Additions	365	87	263	39
	595	436	402	365
Less reductions/repayments	(186)	(240)	(175)	(234)
At 30 September 2016	409	196	227	131
Other key management personnel (chief officers)				
At 1 October 2014	1,477	3	1,469	3
Additions	275	381	275	381
	1,752	384	1,744	384
Less reductions/repayments	(1,218)	(2)	(1,210)	(2)
At 30 September 2015	534	382	534	382
Additions	640	47	640	47
	1,174	429	1,174	429
Less reductions/repayments	(150)	(133)	(150)	(133)
At 30 September 2016	1,024	296	1,024	296

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 30 September 2016 (continued)

38. SEGMENTAL INFORMATION BY CLASSES OF BUSINESS

The Group's reportable segments consist of those which are customer-oriented and those arising on the Group's proprietary business and comprise: (i) credit, deposit-taking and other retail and (ii) financial markets, investments and non-retail.

Interest income is the main revenue generating activity for both segments. The customer-oriented segment also has income derived from fees and commissions and earnings arising on foreign exchange transactions.

	Credit, deposit-taking and other retail		Financial markets, investments and non-retail		Group Total	
	2016	2015	2016	2015	2016	2015
	€ 000	€ 000	€ 000	€ 000	€ 000	€ 000
Net interest income	143,863	124,867	4,966	19,911	148,829	144,778
Net fee and commission income	41,186	40,229	24,899	22,347	66,085	62,576
Trading income	18,065	19,092	11,373	3,417	29,438	22,509
Income from financial assets at FVTPL	-	-	4,332	14,656	4,332	14,656
Gain on Visa transaction	27,511	-	-	-	27,511	-
Other income	-	-	1,901	2,352	1,901	2,352
Depreciation/amortisation	(4,526)	(3,687)	(3,981)	(3,994)	(8,507)	(7,681)
Other costs	(97,548)	(94,143)	(1,513)	(1,455)	(99,061)	(95,598)
Impairment (losses)/reversal	(23,249)	(32,710)	107	-	(23,142)	(32,710)
Operating profit before share of results of equity-accounted investees	105,302	53,648	42,084	57,234	147,386	110,882
Group share of results after tax of equity-accounted investees	-	-	3,730	11,786	3,730	11,786
Common costs					(5,210)	(4,753)
Group profit before tax					145,906	117,915
ASSETS						
Total assets	4,146,060	4,072,723	6,276,875	5,527,604	10,422,935	9,600,327
Property and equipment and Intangible assets	70,949	71,594	23,786	22,609	94,735	94,203
Additions to property and equipment and intangible assets	7,956	8,219	155	913	8,111	9,132
Unallocated assets	-	-	-	-	100,029	101,396
Carrying value of equity-accounted investees	-	-	97,041	96,904	97,041	96,904
Total Assets					10,722,851	9,901,962
LIABILITIES						
Total liabilities	9,197,253	8,581,049	618,130	474,402	9,815,383	9,055,451
Unallocated liabilities					178,307	176,322
Total Liabilities					9,993,690	9,231,773

The revenue which is reported above represents revenue generated from external customers. There were no inter-segment sales during the year (2015: 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 without allocation of common costs, results of equity-accounted investees and income tax expense.

For the purpose of monitoring segment performance and allocating resources between segments, all assets and liabilities are allocated to reportable segments other than deferred tax, other assets and other liabilities.

There are no material activities which are carried out outside Malta.

Notes to the financial statements 30 September 2016 (continued)

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 income statement 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.

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.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

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.

The following industry concentrations in connection with loans and advances to banks and customers are considered significant:

	The Group	
	2016	2015
	€000	€000
Agriculture	7,497	8,309
Fishing	3,716	2,158
Mining and quarrying	4,100	3,931
Manufacturing	125,793	143,990
Electricity, gas, steam and air conditioning supply	139,482	86,314
Water supply, sewerage waste management and remediation activities	22,680	30,092
Construction	242,383	274,586
Wholesale and retail trade	370,721	391,087
Transportation and storage	275,410	283,370
Accommodation and food service activities	221,999	224,698
Information and communication	23,417	35,229
Financial and insurance activities	407,120	395,140
Real estate activities	262,998	263,526
Professional, scientific and technical activities	24,943	23,100
Administrative and support service activities	45,774	60,300
Public administration and defence, compulsory social security	14,222	16,738
Education	13,192	13,483
Human health and social work activities	20,168	19,036
Arts, entertainment and recreation	36,182	37,499
Other services activities	17,139	18,535
Households and individuals	2,029,748	1,958,249
Loans and advances to customers	4,308,684	4,289,370
Loans and advances to banks	2,098,439	1,656,346
	6,407,123	5,945,716

(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.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

(ii) Other financial assets (continued)

The level of concentration in respect of other significant financial assets is disclosed in the remaining notes to the financial statements.

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.

Loan commitments
The maximum exposure to credit risk arising on loan commitments and other credit related commitments that are irrevocable over the life of the respective facilities is the full amount of the committed facilities.

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.

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. The haircut that the Bank applies on immovable property, which is the main type of collateral taken by the Bank, currently amounts to 30% on market value of commercial property and 10% on market value of residential property. 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 30 September 2016**	**Loans and advances to customers**	**Undrawn credit facilities and other commitments to lend**
	€000	**€000**
Loans collateralised by:		
Prime bank guarantees	1,058	358
Cash or quasi cash	123,619	41,804
Guarantees and/or letters of comfort issued by the Malta Government,		
the Central Bank of Malta or public agencies	526,269	177,965
Residential property	1,675,477	566,588
Commercial property	1,053,599	356,291
Personal guarantees and others	177,557	60,044
	3,557,579	**1,203,050**

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.1 Credit risk management and exposure (continued)

(ii) Other financial assets (continued)

The Group	**Loans and advances to customers**	**Undrawn credit facilities and other commitments to lend**
As at 30 September 2015	**€000**	**€000**
Loans collateralised by:		
Prime bank guarantees	1,455	484
Cash or quasi cash	124,423	44,116
Guarantees and/or letters of comfort issued by the Malta Government, the Central Bank of Malta or public agencies	540,397	182,743
Guarantees by prime institutions	3,879	1,312
Residential property	1,479,888	500,448
Commercial property	1,051,130	355,456
Personal guarantees and others	191,822	64,867
	3,392,994	**1,149,426**

Residential lending

The table below stratifies credit exposures, covered by residential property, to retail 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.

Residential lending and commitments for residential lending

	2016	**2015**
	€000	**€000**
Less than 25%	160,354	156,478
25% to 50%	488,236	492,432
51% to 75%	758,454	682,012
76% to 90%	1,028,534	935,279
	2,435,578	**2,266,201**

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.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 Credit Quality

(i) Debt securities and other bills 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 30 September 2016					
AAA	-	346,790	26,141	35	372,966
AA- to AA+	-	747,210	90,039	540	837,789
A- to A+	-	1,560,560	294,672	3,070	1,858,302
Lower than A-	126,796	1,264,144	1,669,374	145	3,060,459
Unrated	-	-	18,213	1,575	19,788
	126,796	3,918,704	2,098,439	5,365	6,149,304
As at 30 September 2015					
AAA	-	254,448	16,564	632	271,644
AA- to AA+	-	682,370	132,256	591	815,217
A- to A+	-	1,431,352	437,290	7,047	1,875,689
Lower than A-	85,286	1,283,026	1,049,753	4,449	2,422,514
Unrated	-	-	20,483	2,437	22,920
	85,286	3,651,196	1,656,346	15,156	5,407,984

(ii) Loans and advances to customers analysed into performing and non-performing exposures

	The Group			
Total Gross/Forborne Exposures	Total 2016 €000	of which Forborne 2016 €000	Total 2015 €000	of which Forborne 2015 €000
Performing				
Neither past due nor impaired	3,965,323	47,003	3,830,349	69,383
Past due < 90 days, but not impaired	38,796	454	54,098	1,810
	4,004,119	47,457	3,884,447	71,193
Non performing				
Past due > 90 days, but not impaired	92,040	49,157	122,048	88,236
Impaired	212,525	113,208	282,875	137,440
	304,565	162,365	404,923	225,676
Total Gross/Forborne Exposures	4,308,684	209,822	4,289,370	296,869

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 Credit Quality (continued)

(ii) Loans and advances to customers analysed into performing and non-performing exposures (continued)

Impairment Allowances on Total/Forborne Exposures	The Group			
	Total 2016 €000	of which Forborne 2016 €000	Total 2015 €000	of which Forborne 2015 €000
Performing				
Neither past due nor impaired	34,414	3,092	40,852	5,410
Past due < 90 days, but not impaired	2,250	36	4,049	202
	36,664	3,128	44,901	5,612
Non performing				
Past due > 90 days, but not impaired	34,131	10,654	24,952	11,197
Impaired	114,917	63,610	168,457	88,354
	149,048	74,264	193,409	99,551
Total Impairment Allowances	185,712	77,392	238,310	105,163

Net Carrying Amounts of Total/Forborne Exposures				
Performing				
Neither past due nor impaired	3,930,908	43,911	3,789,497	63,973
Past due < 90 days, but not impaired	36,545	418	50,049	1,608
	3,967,453	44,329	3,839,546	65,581
Non performing				
Past due > 90 days, but not impaired	57,909	38,503	97,096	77,039
Impaired	97,610	49,598	114,418	49,086
	155,519	88,101	211,514	126,125
Total Net Carrying Amounts	4,122,972	132,430	4,051,060	191,706

Interest income recognised during the year 2016 in respect of forborne assets amounts to €11.6 million (2015: €16.8 million).

The tables above analyse the loan book into performing and non-performing exposures together with the related allowances. Impairment allowances comprise both collective and specific.

Gross Forborne Exposures	Modification in Terms 2016 €000	Refinancing 2016 €000	Modification in Terms 2015 €000	Refinancing 2015 €000
Performing				
Personal	3,652	577	6,782	808
Business	42,413	815	58,390	5,213
	46,065	1,392	65,172	6,021
Non performing				
Personal	31,494	446	39,397	1,997
Business	129,987	438	180,657	3,625
	161,481	884	220,054	5,622

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.2 Credit Quality (continued)

(iii) Loans and advances to customers by internal rating based on the Banking directives/rules

	Loans & Advances	
	2016	**2015**
	€000	**€000**
Neither past due nor impaired:		
Regular	3,634,542	3,476,316
Watch list	288,758	294,161
Sub-Standard	42,023	59,872
	3,965,323	3,830,349

The neither past due nor impaired balances include performing forborne facilities.

Past due but not impaired:		
Past due up to 29 days	16,120	15,207
Past due 30 - 59 days	17,020	24,761
Past due 60 - 89 days	5,656	14,130
	38,796	54,098

A financial asset is past due when a counterparty has failed to make a payment when contractually due.

Individually impaired gross loans by segment:		
Personal	171,993	227,255
Business	40,532	55,620
	212,525	282,875

Impaired 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.

Collateral for impaired loans
As detailed above, a variety of types of collateral are accepted including property, securities, cash, guarantees and insurance.

(iv) Movement in forbearance activity during the year

	Loans & Advances	
	2016	**2015**
	€000	**€000**
1 October	296,869	368,456
Additions	26,154	23,979
Retired from forborne	(113,201)	(95,566)
30 September	209,822	296,869

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.3 Movement in allowance accounts for loans and advances to customers

	The Group			
	Individually assessed allowances	Collective allowances	Individually assessed allowances	Collective allowances
	2016	2016	2015	2015
	€000	€000	€000	€000
Change in allowances for uncollectability:				
At 1 October	220,272	18,038	151,565	59,289
Additions	69,074	1,579	97,059	8,910
Reversals	(118,570)	(4,681)	(28,352)	(50,161)
	(49,496)	(3,102)	68,707	(41,251)
At 30 September	170,776	14,936	220,272	18,038

39.2.4 Debt securities

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.

The tables below analyse debt securities by sector, classification and residency.

	The Group and The Bank		
Sector	**Held-to-maturity**	**Available-for-sale**	**Fair Value through Profit or Loss**
	€000	€000	€000
2016			
Banks	1,653,880	3,977	53,797
Government	1,156,540	179,461	90,437
Public	-	88,805	-
Others	650,026	-	41,781
	3,460,446	272,243	186,015

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.4 Debt securities (continued)

Sovereign Debt (continued)

	The Group and The Bank		
	Held-to-maturity	Available-for-sale	Fair Value through Profit or Loss
	€000	€000	€000
2015			
Banks and Central Banks	1,439,507	4,027	106,255
Government	1,020,778	168,572	109,252
Public	-	84,854	-
Others	657,523	-	60,428
	3,117,808	257,453	275,935

	The Group and The Bank		
Residency	Held-to-maturity	Available-for-sale	Fair Value through Profit or Loss
	€000	€000	€000
2016			
Malta	484,791	268,266	69,321
Monetary Union member states	1,058,278	-	53,798
Rest of the world	1,917,377	3,977	62,896
	3,460,446	272,243	186,015
2015			
Malta	566,137	253,426	84,329
Monetary Union member states	960,883	-	71,478
Rest of the world	1,590,788	4,027	120,128
	3,117,808	257,453	275,935

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.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Group

At 30 September 2016	Due within 3 months €000	Due between 3 & 12 months €000	Due between 1 & 5 years €000	Due after 5 years €000	Gross nominal outflow €000	Carrying amount €000
Financial liabilities at fair value through profit or loss	2,053	3,617	11,154	8,503	25,327	20,327
Amounts owed to banks	246,465	24	753	-	247,242	250,155
Amounts owed to customers	7,725,817	1,195,034	287,916	2,781	9,211,548	9,181,047
Debt securities in issue	850	3,509	101,459	-	105,818	95,400
Subordinated liabilities	1,338	4,698	136,768	146,742	289,546	231,591
Derivatives designated for hedge accounting	1,364	1,949	7,866	10,856	22,035	20,649
Other financial liabilities	174,230	5,935	7,864	14,741	202,770	194,521
	8,152,117	**1,214,766**	**553,780**	**183,623**	**10,104,286**	**9,993,690**
Loan commitments	1,467,135					

At 30 September 2015						
Financial liabilities at fair value through profit or loss	2,373	4,502	16,309	3,206	26,390	25,077
Amounts owed to banks	181,643	533	15,843	-	198,019	197,760
Amounts owed to customers	7,068,022	1,125,575	411,895	2,471	8,607,963	8,559,731
Debt securities in issue	850	3,509	105,818	-	110,177	95,400
Subordinated liabilities	1,338	4,698	141,465	-	147,501	120,000
Derivatives designated for hedge accounting	2,648	4,103	13,002	13,930	33,683	35,201
Other financial liabilities	165,629	7,613	7,926	14,984	196,152	198,604
	7,422,503	**1,150,533**	**712,258**	**34,591**	**9,319,885**	**9,231,773**
Loan commitments	1,429,943					

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.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

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 At 30 September 2016	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	39,017	-	-	-	132,033	**171,050**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	9,924	26,424	124,890	24,777	-	**186,015**
- Equity and other non-fixed income instruments	-	-	-	-	79,734	**79,734**
- Loans and advances	-	-	-	121,316	-	**121,316**
- Derivative financial instruments	3,472	610	1,283	-	-	**5,365**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	48,387	3,977	36,229	183,650	-	**272,243**
- held-to-maturity	171,798	562,940	2,533,287	192,421	-	**3,460,446**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	3,583	**3,583**
Loans and advances to banks	2,000,527	82,000	-	-	15,912	**2,098,439**
Loans and advances to customers	517,983	125,253	345,240	3,013,180	-	**4,001,656**
Investments in equity-accounted investees	-	-	-	-	97,041	**97,041**
Other assets	-	-	-	-	225,963	**225,963**
	2,791,108	**801,204**	**3,040,929**	**3,535,344**	**554,266**	**10,722,851**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	2,860	371	5,813	11,283	-	**20,327**
Amounts owed to banks	142,322	103,225	4,608	-	-	**250,155**
Amounts owed to customers	7,731,659	1,184,350	264,949	89	-	**9,181,047**
Debt securities in issue	-	-	95,400	-	-	**95,400**
Other liabilities	-	-	-	-	194,521	**194,521**
Derivatives held for hedging	-	-	616	20,033	-	**20,649**
Subordinated liabilities	-	-	120,000	111,591	-	**231,591**
Equity holders of the Bank	-	-	-	-	729,161	**729,161**
	7,876,841	**1,287,946**	**491,386**	**142,996**	**923,682**	**10,722,851**

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Group

At 30 September 2015	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	6,002	-	-	-	120,650	**126,652**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	32,073	46,681	142,232	54,949	-	**275,935**
- Equity and other non-fixed income instruments	-	-	-	-	77,210	**77,210**
- Loans and advances	-	-	-	49,221	-	**49,221**
- Derivative financial instruments	11,436	862	2,852	6	-	**15,156**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	12,155	-	61,430	183,868	-	**257,453**
- held-to-maturity	171,552	420,976	2,305,450	219,830	-	**3,117,808**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	1,044	**1,044**
Loans and advances to banks	1,441,529	160,000	-	-	54,817	**1,656,346**
Loans and advances to customers	548,182	116,277	432,884	2,904,496	-	**4,001,839**
Investments in equity-accounted investees	-	-	-	-	96,904	**96,904**
Other assets	-	-	-	-	226,394	**226,394**
	2,222,929	**744,796**	**2,944,848**	**3,412,370**	**577,019**	**9,901,962**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	4,951	878	7,103	12,145	-	**25,077**
Amounts owed to banks	182,760	-	15,000	-	-	**197,760**
Amounts owed to customers	7,059,553	1,107,476	392,636	66	-	**8,559,731**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	198,604	**198,604**
Derivatives held for hedging	5	272	1,797	33,127	-	**35,201**
Subordinated liabilities	-	-	120,000	-	-	**120,000**
Non-controlling interest	-	-	-	-	1,271	**1,271**
Equity holders of the Bank	-	-	-	-	668,918	**668,918**
	7,247,269	**1,108,626**	**536,536**	**140,738**	**868,793**	**9,901,962**

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Bank

At 30 September 2016	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	39,017	-	-	-	132,033	**171,050**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	9,924	26,424	124,890	24,777	-	**186,015**
- Equity and other non-fixed income instruments	-	-	-	-	78,596	**78,596**
- Loans and advances	-	-	-	121,316	-	**121,316**
- Derivative financial instruments	3,472	610	1,283	-	-	**5,365**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	48,387	3,977	36,229	183,650	-	**272,243**
- held-to-maturity	171,798	562,940	2,533,287	192,421	-	**3,460,446**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	3,583	**3,583**
Loans and advances to banks	2,000,528	82,000	-	-	15,911	**2,098,439**
Loans and advances to customers	517,984	125,253	345,240	3,013,179	-	**4,001,656**
Investments in equity-accounted investees and subsidiaries	-	-	-	-	59,100	**59,100**
Other assets	-	-	-	-	224,482	**224,482**
	2,791,110	**801,204**	**3,040,929**	**3,535,343**	**513,705**	**10,682,291**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	2,860	371	5,813	11,283	-	**20,327**
Amounts owed to banks	142,321	103,226	4,608	-	-	**250,155**
Amounts owed to customers	7,735,082	1,184,350	264,949	89	-	**9,184,470**
Debt securities in issue	-	-	95,400	-	-	**95,400**
Other liabilities	-	-	-	-	193,923	**193,923**
Derivatives held for hedging	-	-	616	20,033	-	**20,649**
Subordinated liabilities	-	-	120,000	111,591	-	**231,591**
Equity holders of the Bank	-	-	-	-	685,776	**685,776**
	7,880,263	**1,287,947**	**491,386**	**142,996**	**879,699**	**10,682,291**

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

The Bank

At 30 September 2015	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	6,002	-	-	-	120,650	**126,652**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	32,073	46,681	142,232	54,949	-	**275,935**
- Equity and other non-fixed income instruments	-	-	-	-	75,246	**75,246**
- Loans and advances	-	-	-	49,221	-	**49,221**
- Derivative financial instruments	11,436	862	2,852	6	-	**15,156**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	12,155	-	61,430	183,868	-	**257,453**
- held-to-maturity	171,552	420,976	2,305,450	219,830	-	**3,117,808**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	1,044	**1,044**
Loans and advances to banks	1,441,529	160,000	-	-	54,817	**1,656,346**
Loans and advances to customers	548,181	116,277	432,884	2,904,497	-	**4,001,839**
Investments in equity-accounted investees and subsidiaries	-	-	-	-	54,100	**54,100**
Other assets	-	-	-	-	225,712	**225,712**
	2,222,928	**744,796**	**2,944,848**	**3,412,371**	**531,569**	**9,856,512**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	4,951	878	7,103	12,145	-	**25,077**
Amounts owed to banks	182,760	-	15,000	-	-	**197,760**
Amounts owed to customers	7,062,929	1,107,476	392,636	66	-	**8,563,107**
Debt securities in issue	-	-	95,400	-	-	**95,400**
Other liabilities	-	-	-	-	197,921	**197,921**
Derivatives held for hedging	5	272	1,797	33,127	-	**35,201**
Subordinated liabilities	-	-	120,000	-	-	**120,000**
Equity holders of the Bank	-	-	-	-	622,046	**622,046**
	7,250,645	**1,108,626**	**631,936**	**45,338**	**819,967**	**9,856,512**

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

A new requirement introduced in 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.

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				
At 30 September 2016				
Equity instruments	-	-	83,317	83,317
Debt Securities	187,360	187,360	3,731,344	3,663,690
Loan and advances	-	-	6,309,190	-
Other assets	-	-	411,640	-
	187,360	**187,360**	**10,535,491**	**3,747,007**
The Group				
At 30 September 2015				
Equity instruments	-	-	78,254	78,254
Debt Securities	135,283	135,283	3,515,913	3,564,929
Loan and advances	-	-	5,737,470	-
Other assets	-	-	435,042	-
	135,283	**135,283**	**9,766,679**	**3,643,183**
The Bank				
At 30 September 2016				
Equity instruments	-	-	82,179	82,179
Debt Securities	187,360	187,360	3,731,344	3,663,690
Loan and advances	-	-	6,309,190	-
Other assets	-	-	372,218	-
	187,360	**187,360**	**10,494,931**	**3,745,869**
The Bank				
At 30 September 2015				
Equity instruments	-	-	76,290	76,290
Debt Securities	135,283	135,283	3,515,913	3,564,929
Loan and advances	-	-	5,737,470	-
Other assets	-	-	391,556	-
	135,283	**135,283**	**9,721,229**	**3,641,219**

The Group does not encumber any of the collateral received or any of its debt securities issued.

As at 30 September 2016, the Group and the Bank did not have any outstanding liabilities associated with encumbered assets and collateral received.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk (continued)

Asset Encumbrance (continued)

The Group and the Bank undertake the following types of encumbrance:

(i) Pledging of debt securities against the provision of credit lines by the Central Bank of Malta; and
(ii) Pledging of balances held with the Central Bank of Malta and debt securities in favour of the Depositor Compensation Scheme.

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 will 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 Group manages this risk by using sensitivity analysis using modified duration and interest rate repricing gaps.

For financial instruments held or issued, the Group has used techniques that measure the change in the fair value and cash flows of the Group's financial instruments at the reporting date for hypothetical changes in the relevant market risk variables. The sensitivity due to changes in the relevant risk variables is set out below. The amounts generated from the analysis are forward-looking estimates of market risk assuming certain market conditions. Actual results in the future may differ materially from those projected results due to the inherent uncertainty of global financial markets. The sensitivity analyses are for illustrative purposes only, as in practice market rates rarely change in isolation and are likely to be interdependent.

The Bank makes use of a variety of measurement techniques including sensitivity analyses using Modified Duration and interest rate risks on economic value and interest margin.

(i) Modified Duration

The Modified Duration is a measure of the price sensitivity to yields. By calculating the Modified Duration, the Bank estimates the impact on Profit or Loss and Capital of changes in the market values of the securities in the treasury portfolio and of the interest rate swaps entered into to hedge the interest rate risk of the treasury portfolio, in response to a parallel shift in yields of 100 basis points. The Modified Duration does not represent a forecast of potential losses in the portfolio, but rather an analysis of how the market value of the treasury portfolio may change in response to a change in interest rates.

In addition, the Bank calculates the Modified Duration on the unhedged fixed securities which are marked to market by major currencies.

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.4 Market risk (continued)

39.4.1 Interest rate risk (continued)

(i) Modified Duration (continued)

As with most financial management tools, Modified Duration also has its limitations. The market value of a bond is dependent on many variables apart from the duration calculation and rarely correlates perfectly with the duration number. With rates not moving in parallel shifts and the yield curve constantly changing, duration can be used to determine how the market values of bonds may (but not necessarily will) react.

The Group	2016 €000	2015 €000
Modified Duration		
Impact on Profit or Loss	(1,809)	(1,869)
Impact on Capital	(10,613)	(10,728)

The nominal amount of floating rate notes as at 30 September 2016 is €2,590.4 million (2015: €2,241.3 million).

(ii) Impact of interest rate risk on economic value

The estimated impact of an immediate 200 basis point increase in yields on economic value for the years ended 30 September 2016 and 2015 is shown below. Economic value is defined as the present value of the expected future cash flows to be generated by the investment portfolios concerned. Impacts have only been shown in one direction but can be assumed to be reasonably symmetrical. Sensitivity analysis is carried out monthly, and sensitivity is expressed as a percentage of the Group's regulatory capital base.

The Group	2016 €000	2015 €000
Impact on capital	16,582	1,811

(iii) Impact of interest rate risk on interest margin

Interest rate risk arising from the different repricing characteristics of the Group's interest-sensitive assets and liabilities, and from the mismatch between interest rate sensitive liabilities and interest rate sensitive assets, is managed centrally by ALCO. Matching assets and liabilities are offset against each other and internal interest rate swaps are also used to close repricing gaps.

The net effect of a 100 bps increase/decrease on the interest margin for twelve months, arising from repricing gaps, is as follows:

The Group	2016 €000	2015 €000
Net effect on Interest Income for 12 months	24,451	23,325

Notes to the financial statements 30 September 2016 (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	103,777	23,018	-	-	44,255	**171,050**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	27,234	39,738	7,996	109,682	1,365	**186,015**
- Equity and other non- fixed income instruments	-	-	-	-	79,734	**79,734**
- Loans and advances	121,316	-	-	-	-	**121,316**
- Derivative financial instruments	57	1,727	-	-	3,581	**5,365**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	-	48,386	3,977	219,880	-	**272,243**
- held-to-maturity	830,240	1,700,094	210,622	719,490	-	**3,460,446**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	3,583	**3,583**
Loans and advances to banks	1,742,104	78,375	82,000	-	195,960	**2,098,439**
Loans and advances to customers	3,733,822	24,604	107,875	135,355	-	**4,001,656**
Investments in equity-accounted investees	-	-	-	-	97,041	**97,041**
Other assets	-	-	-	-	225,963	**225,963**
Total 2016	**6,558,550**	**1,915,942**	**412,470**	**1,184,407**	**651,482**	**10,722,851**
Total 2015	5,944,047	1,629,178	411,900	1,047,221	869,616	9,901,962
LIABILITIES and EQUITY						
Financial liabilities at fair value through profit or loss	5,479	3,609	4,677	3,375	3,187	**20,327**
Amounts owed to banks	9,609	103,225	-	4,608	132,713	**250,155**
Amounts owed to customers	4,980,567	337,502	1,176,473	282,621	2,403,884	**9,181,047**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	194,521	**194,521**
Derivatives held for hedging	-	20,033	616	-	-	**20,649**
Subordinated liabilities	-	-	-	231,591	-	**231,591**
Equity holders of the Bank	-	-	-	-	729,161	**729,161**
Total 2016	**4,995,655**	**464,369**	**1,181,766**	**617,595**	**3,463,466**	**10,722,851**
Total 2015	4,614,848	416,016	1,140,007	632,528	3,098,563	9,901,962
Interest rate swaps - 2016	**91,548**	**188,167**	**35,678**	**(315,394)**	-	
Interest rate swaps - 2015	84,548	241,213	93,848	(419,609)	-	
Gap - 2016	**1,654,849**	**1,637,542**	**(756,037)**	**254,794**	**-**	
Gap - 2015	1,414,338	1,447,886	(634,082)	(4,372)	-	
Cumulative Gap - 2016	**1,654,849**	**3,292,391**	**2,536,354**	**2,791,148**	**-**	
Cumulative Gap - 2015	1,414,338	2,862,224	2,228,142	2,223,770	-	

Notes to the financial statements 30 September 2016 (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 30 September. Included in the table are the Group's assets and liabilities at carrying amounts, analysed into relevant currency groupings.

The Group 30 September 2016	EUR €000	USD €000	GBP €000	AUD €000	Other Currencies €000	Total €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	168,063	663	971	851	502	**171,050**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	146,312	30,172	3,625	5,903	3	**186,015**
- Equity and other non-fixed income instruments	67,640	4,860	3,090	-	4,144	**79,734**
- Loans and advances	121,316	-	-	-	-	**121,316**
- Derivative financial instruments	676	1,707	2,140	370	472	**5,365**
Investments						
- available-for-sale	181,385	89,784	772	302	-	**272,243**
- held-to-maturity	1,916,235	1,004,014	243,621	186,601	109,975	**3,460,446**
- Equity and other non-fixed income instruments						
- available-for-sale	-	3,583	-	-	-	**3,583**
Loans and advances to banks	1,839,274	83,533	87,787	8,435	79,410	**2,098,439**
Loans and advances to customers	3,940,654	31,179	28,753	-	1,070	**4,001,656**
Other assets	316,059	3,771	1,651	1,031	492	**323,004**
	8,697,614	**1,253,266**	**372,410**	**203,493**	**196,068**	**10,722,851**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	16,595	1,677	1,572	427	56	**20,327**
Amounts owed to banks	95,466	143,723	5,978	1,534	3,454	**250,155**
Amounts owed to customers	7,776,994	864,603	328,029	75,648	135,773	**9,181,047**
Debt securities in issue	95,400	-	-	-	-	**95,400**
Other liabilities	181,654	8,039	996	1,045	2,787	**194,521**
Derivatives held for hedging	616	20,131	(73)	(25)	-	**20,649**
Subordinated liabilities	231,591	-	-	-	-	**231,591**
Equity	702,831	22,323	11,017	14,549	(21,559)	**729,161**
	9,101,147	**1,060,496**	**347,519**	**93,178**	**120,511**	**10,722,851**

	USD	GBP	AUD	Other Currencies
Net on balance sheet financial position	192,770	24,891	110,315	75,557
Notional amount of derivative instruments	(216,983)	(31,032)	(125,136)	(52,944)
Net open position	(24,213)	(6,141)	(14,821)	22,613

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.4 Market risk (continued)

39.4.2 Currency risk (continued)

The Group 30 September 2015	EUR €000	USD €000	GBP €000	AUD €000	Other Currencies €000	Total €000
Assets						
Balances with Central Bank of Malta, treasury bills and cash	123,268	1,578	1,411	125	270	**126,652**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	211,262	50,019	5,861	8,790	3	**275,935**
- Equity and other non-fixed income instruments	63,704	4,031	5,189	-	4,286	**77,210**
- Loans and advances	49,221	-	-	-	-	**49,221**
- Derivative financial instruments	404	8,348	3,923	1,520	961	**15,156**
Investments						
- available-for-sale	170,481	85,812	884	276	-	**257,453**
- held-to-maturity	1,732,469	889,916	268,044	166,453	60,926	**3,117,808**
- Equity and other non-fixed income instruments						
- available-for-sale	1,044	-	-	-	-	**1,044**
Loans and advances to banks	1,287,301	106,887	86,493	3,701	171,964	**1,656,346**
Loans and advances to customers	3,934,393	27,157	39,179	-	1,110	**4,001,839**
Other assets	317,131	3,191	1,664	954	358	**323,298**
	7,890,678	**1,176,939**	**412,648**	**181,819**	**239,878**	**9,901,962**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	17,400	3,646	3,547	374	110	**25,077**
Amounts owed to banks	49,205	108,009	35,177	1,705	3,664	**197,760**
Amounts owed to customers	7,235,210	781,311	360,565	63,503	119,142	**8,559,731**
Debt securities in issue	95,400	-	-	-	-	**95,400**
Other liabilities	172,225	16,893	5,671	1,486	2,330	**198,605**
Derivatives held for hedging	16,458	18,841	(73)	(25)	-	**35,200**
Subordinated liabilities	120,000	-	-	-	-	**120,000**
Equity	689,002	7,797	(2,251)	(7,410)	(16,950)	**670,189**
	8,394,900	**936,497**	**402,636**	**59,633**	**108,296**	**9,901,962**

	USD	GBP	AUD	Other Currencies
Net on balance sheet financial position	240,442	10,012	122,186	131,582
Notional amount of derivative instruments	(260,146)	(15,260)	(113,346)	(112,853)
Net open position	(19,704)	(5,248)	8,840	18,729

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 available for sale 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 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.5 Transferred financial assets that are not derecognised in their entirety

	The Group and the Bank	
	2016	2015
	€000	€000
Debt securities classified as		
- held-to-maturity	103,226	37,537
	103,226	37,537
Amounts owed to banks	103,226	37,537

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 financial assets at fair value through profit and loss and 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, 1.19 and 1.24 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 30 September 2016 (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 30 September 2016				
Assets				
Financial assets at fair value through profit or loss				
- debt and other fixed income instruments	173,065	12,950	-	186,015
- equity and other non-fixed income instruments	50,294	23,762	5,678	79,734
- loans and advances	-	121,316	-	121,316
- derivative financial instruments	-	5,365	-	5,365
Investments				
Debt and other fixed income instruments				
- available-for-sale	179,461	92,782	-	272,243
Equity and other non-fixed income instruments				
- available-for-sale	-	-	3,583	3,583
	402,820	**256,175**	**9,261**	**668,256**
Liabilities				
Financial liabilities at fair value through profit or loss	-	20,327	-	20,327
Derivatives designated for hedge accouting	-	20,649	-	20,649
	-	**40,976**	**-**	**40,976**
The Group				
At 30 September 2015				
Assets				
Financial assets at fair value through profit or loss				
- debt and other fixed income instruments	265,139	10,796	-	275,935
- equity and other non-fixed income instruments	59,941	11,950	5,319	77,210
- loans and advances	-	49,221	-	49,221
- derivative financial instruments	-	15,156	-	15,156
Investments				
Debt and other fixed income instruments				
- available-for-sale	168,575	88,878	-	257,453
	493,655	**176,001**	**5,319**	**674,975**
Liabilities				
Financial liabilities at fair value through profit or loss	-	25,077	-	25,077
Derivatives designated for hedge accounting	-	35,201	-	35,201
	-	**60,278**	**-**	**60,278**

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.6 Fair value of financial instruments (continued)

During the year under review financial assets at fair value through profit or loss amounting to €14.1 million were transferred from Level 1 to Level 2 (2015: €2.9 million) and €1.1 million transferred from Level 3 to Level 2 (2015: no change). The transfer from Level 1 to Level 2 was due to securities which did not have a quoted price on active markets as at year end and securities transferred from Level 3 to Level 2 were those which had observable inputs as at the same date. During the same year no change in levels was made in financial assets classified as available-for-sale.

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 available-for-sale are carried at their fair value.

(i) Investments - Debt and other fixed income instruments held to maturity
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.

(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.

(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 30 September 2016 (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				Carrying
	Level 1 €000	Level 2 €000	Level 3 €000	Total €000	Amount €000
2016					
Financial assets					
Held-to-maturity investments	2,857,554	653,881	-	3,511,435	3,460,446
Financial liabilities					
Debt securities in issue	99,000	-	-	99,000	95,400
Subordinated liabilities	235,500	-	-	235,500	231,591
	334,500	-	-	334,500	326,991

	Fair value measurement				Carrying
	Level 1 €000	Level 2 €000	Level 3 €000	Total €000	Amount €000
2015					
Financial assets					
Held-to-maturity investments	2,491,217	678,312	-	3,169,529	3,117,808
Financial liabilities					
Debt securities in issue	100,964	-	-	100,964	95,400
Subordinated liabilities	128,700	-	-	128,700	120,000
	229,664	-	-	229,664	215,400

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

	Fair value through profit or loss		Available-for-sale investments		
	Debt and other fixed income instruments €000	Equity and other non-fixed income instruments €000	Debt and other fixed income instruments €000	Equity and other non-fixed income instruments €000	Total €000
2016					
Opening balance	-	5,319	-	-	5,319
- in profit or loss	-	(12)	-	-	(12)
Purchases	-	1,550	-	-	1,550
Transfers	-	(1,104)	-	-	(1,104)
Sales	-	(75)	-	-	(75)
Consideration	-	-	-	3,583	3,583
Closing balance	-	5,678	-	3,583	9,261

	Fair value through profit or loss		Available-for-sale investments		
	Debt and other fixed income instruments €000	Equity and other non-fixed income instruments €000	Debt and other fixed income instruments €000	Equity and other non-fixed income instruments €000	Total €000
2015					
Opening balance	-	6,204	-	-	6,204
- in profit or loss	-	595	-	-	595
Sales	-	(1,480)	-	-	(1,480)
Closing balance	-	5,319	-	-	5,319

Notes to the financial statements 30 September 2015 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.6 Fair value of financial instruments (continued)

The unrealised gains/losses as of 30 September 2016 and 30 September 2015 were immaterial.

Consideration in Equity and other non-fixed income instruments refer to preferred stock in Visa Inc. convertible into ordinary shares.

The instruments classified within Level 3 comprise externally managed funds. Approximately 50% of the carrying amount represents funds with underlying investments which mainly comprise properties with the remaining 50% representing a European fund which invests in projects related to energy, climate change and infrastructure having 65% of its assets focused on new projects, with the remaining 35% focused on replacement, modernisation and capacity enhancement. The Bank has determined that the reported net asset value of these funds represents their fair value at the end of the reporting period. For one of the property funds, the Bank has adjusted the reported net asset value to take cognisance of factors which resulted in a lower fair value for the fund; in respect of another property fund, the fair value of the Bank's interest was determined to be nil in view of the fact that the value of the Fund's reported liabilities approximated the value of its reported assets. The net asset value of these funds was determined using statements or other information provided by the fund managers. The Bank considers that such valuations may rely significantly on the judgments and estimates made by the fund managers and given the level of subjectivity involved, these are included within Level 3.

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 May 2015.

Capital management is under the direct control of the Asset and Liability Committee (ALCO). During the financial year, ALCO has monitored the adequacy of the Group's capital and gave strategic direction on the most efficient use of capital.

During the year under review and during the comparative period, there were no reported breaches in respect of the externally imposed capital requirements. The Group utilises the standardised method of calculating risk weighted assets, therefore the amounts are presented using the formulae of the CRR.

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	390,000	390,000
- Share premium	988	988
- Retained earnings*	232,559	228,958
- Accumulated other comprehensive income	7,905	7,792
- Other reserves	27,428	27,428
- Funds for general banking risk	4,505	4,505
- Deductions:		
Other intangible assets	(13,272)	(13,272)
Deferred tax assets that rely on future profitability and arise from temporary differences	(6,991)	(7,004)
Instruments of financial sector entities where the institution has a significant investment amount exceeding the 17.65% threshold	(6,820)	(6,820)
Other transitional adjustments	(2,260)	(2,260)
Additional adjustments due to Article 3 CRR	(44,440)	(44,440)
Total Tier 1 Capital	589,602	585,875

**Retained earnings include current year's profit which is subject to regulatory approval.*

Notes to the financial statements 30 September 2016 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.7 Capital risk management (continued)

	The Group €000	The Bank €000
Tier 2		
- Capital instruments and subordinated loans	187,065	187,065
- Deductions:		
Other transitional adjustments	(2,130)	(2,130)
Total Tier 2 Capital	184,935	184,935
Total Own Funds	774,537	770,810

Further information on the Group's and the Bank's capital adequacy ratios may be found in section 2.2 in the Capital and Risk Management report, which are subject to internal verification as set out in paragraph 1.1 of that report.

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	
	2016 €000	2015 €000
Derivative financial assets		
Gross amounts of recognised financial assets	5,365	15,156
Net amounts of financial assets presented in the statement of financial position	5,365	15,156
Related amounts not set off in the statement of financial position:		
Financial instruments	(5,365)	(15,156)
Net amount	-	-

Financial liabilities subject to offsetting, enforcable master netting arrangements and similar agreements

	2016 €000	2015 €000
Derivative financial liabilities		
Gross amounts of recognised financial liabilities	40,976	60,278
Net amounts of financial liabilities presented in the statement of financial position	40,976	60,278
Related amounts not set off in the statement of financial position:		
Financial instruments	(5,365)	(15,156)
Financial collateral pledged	(40,380)	(69,951)
Net amount	(4,769)	(24,829)

Notes to the financial statements 30 September 2016 (continued)

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, which is generally not more than twelve months 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.

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 30 September 2016, the total assets held by the Group on behalf of its customers amounted to €267.0 million (2015: €302.5 million).

The Bank is party to certain legal proceedings arising out of its normal business operations. Apart from the matter which relates to trust activities described below, the Board of Directors considers that none of these matters are material, either individually or in the aggregate. The recognition of provisions is determined in accordance with the accounting policies set out in Note 1.

In November 2014, court action was instituted against the Bank by the curator of a failed group whilst under the trust of the Bank, by virtue of which a claim of €363 million was made. On the basis of legal opinions, the directors concluded that the Bank has a strong legal position and accordingly assessed the risk of an economic outflow from such claim to be improbable.

42. REGULATORY COMPENSATION SCHEMES

As at 30 September 2016, the Bank holds debt securities and cash balances which, in terms of the Depositor Compensation Scheme - Special Contribution, are pledged in terms of the 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 €4.6 million (2015: €8.1 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. REGISTERED OFFICE

The registered and principal office of the Bank is 58, Zachary Street, Valletta VLT1130, Malta.

Independent auditors' report to the members of Bank of Valletta p.l.c

Report on the financial statements

We have audited the accompanying financial statements of Bank of Valletta p.l.c. (the "Bank") and of the Group of which the Bank is the parent, as set out on pages 40 to 112, which comprise the statements of financial position as at 30 September 2016 and the statements of profit or loss, profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

As explained more fully in the Directors' Responsibilities Statement included in the Directors' Report set out on page 2, the directors are responsible for the preparation of financial statements that (a) give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU, and (b) are 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), and, as regards the financial statements of the Group, Article 4 of the IAS Regulation. They are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. This report, including the opinion, has been prepared for and only for the Bank's members as a body in accordance with Article 179 of the Act and Article 31 of the Banking Act, 1994 (Chapter 371, Laws of Malta), and may not be appropriate for any other purpose.

In addition, we read the other information contained in the Annual Report 2016 and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent material misstatements of fact or material inconsistencies with the financial statements.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation of financial statements that give a true and fair view 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Independent auditors' report to the members of Bank of Valletta p.l.c

Opinion on financial statements

In our opinion, the financial statements:
- give a true and fair view of the Group's and the Bank's financial position as at 30 September 2016, and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU; and
- have been properly prepared in accordance with the Companies Act, 1995 (Chapter 386, Laws of Malta), the Banking Act, 1994 (Chapter 371, Laws of Malta), and, as regards the financial statements of the Group, Article 4 of the IAS Regulation.

Report on other legal and regulatory requirements
Matters on which we are required to report by the Banking Act, 1994 (Chapter 371, Laws of Malta)

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;
- the Bank's financial statements are in agreement with the books of account; 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.

Matters on which we are required to report by exception by the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act"), other than those reported upon above

We have nothing to report in respect of the following matters where the Act requires us to report to you if, in our opinion:
- the information given in the Directors' Report for the financial year for which the financial statements are prepared is not consistent with the financial statements; or
- certain disclosures of directors' remuneration specified by the Act are not made.

Noel Mizzi
Partner, for and on behalf of
KPMG
Registered Auditors,
Portico Building,
Marina Street,
Pietà PTA 9044,
Malta

Jonathan Bingham
Partner, for and on behalf of
KPMG LLP
Chartered Accountants,
15 Canada Square,
Canary Wharf,
London E14 5GL,
United Kingdom

28 October 2016

The Group's five year summary - extracted from the respective audited financial statements

A. STATEMENTS OF PROFIT OR LOSS

For the year ended 30 September

	2016 €000	2015 €000	2014 €000	2013 €000	2012 €000
Interest and similar income	214,258	215,612	212,925	222,446	238,561
Interest expense	(65,429)	(70,834)	(86,922)	(91,432)	(90,729)
Net interest income	148,829	144,778	126,003	131,014	147,832
Other operating income	101,756	102,093	83,802	87,113	71,032
Gain on Visa transaction	27,511	-	-	-	-
Other operating charges	(112,778)	(108,032)	(93,499)	(89,138)	(91,665)
Net impairment losses	(23,142)	(32,710)	(19,431)	(25,595)	(22,817)
Share of results of equity-accounted investees	3,730	11,786	7,227	12,384	6,348
Profit before tax	145,906	117,915	104,102	115,778	110,730
Income tax expense	(50,708)	(37,971)	(34,718)	(36,305)	(36,454)
Profit for the year	95,198	79,944	69,384	79,473	74,276
Attributable to:					
Equity holders of the Bank	94,742	79,378	68,945	79,055	74,995
Non-controlling interest	456	566	439	418	(719)
	95,198	79,944	69,384	79,473	74,276
Earnings per share	**24c3**	**20c4**	**17c7**	**20c3**	**19c2**

The earnings per share figures have been adjusted retrospectively to reflect the increase in the number of ordinary shares following capitalisation of retained earnings and a bonus issue which occurred on 15 January 2016.

The Group's five year summary - extracted from the respective audited financial statements

B. STATEMENTS OF FINANCIAL POSITION

	2016	2015	2014	2013	2012
	€000	€000	€000	€000	€000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	171,050	126,652	130,966	194,587	296,134
Investments and financial assets at fair value through profit or loss	4,128,702	3,793,827	2,950,011	2,247,351	2,106,740
Loans and advances to banks	2,098,439	1,656,346	1,045,988	860,957	676,639
Loans and advances to customers	4,001,656	4,001,839	3,861,532	3,667,739	3,702,217
Investments in equity-accounted investees	97,041	96,904	88,553	84,880	77,058
Property and equipment	102,846	102,523	99,759	91,618	78,778
Current tax	16,061	965	-	-	-
Deferred tax	67,188	86,654	78,550	70,205	63,607
Assets held for realisation	11,973	11,601	9,755	10,361	8,944
Other assets	4,818	2,990	7,659	5,045	11,418
Prepayments and accrued income	23,077	21,661	24,018	25,215	27,690
Total Assets	**10,722,851**	**9,901,962**	**8,296,791**	**7,257,958**	**7,049,225**
LIABILITIES					
Financial liabilities at fair value through profit or loss and derivatives held for hedging	40,976	60,278	81,812	62,048	98,744
Amounts owed to banks	250,155	197,760	86,579	36,040	250,352
Amounts owed to customers	9,181,047	8,559,731	7,119,530	6,219,666	5,809,300
Debt securities in issue	95,400	95,400	95,400	95,400	95,400
Current tax	-	-	16,090	4,697	13,405
Deferred tax	4,318	4,382	5,100	5,003	4,199
Other liabilities	173,988	172,905	130,168	108,864	106,235
Accruals and deferred income	16,215	21,317	27,643	29,235	30,590
Subordinated liabilities	231,591	120,000	120,000	120,000	120,000
Total Liabilities	9,993,690	9,231,773	7,682,322	6,680,953	6,528,225
EQUITY					
Called up share capital	390,000	360,000	330,000	300,000	270,000
Share premium account	988	988	988	988	988
Revaluation reserve	35,332	35,217	29,136	24,621	13,573
Retained earnings	302,841	272,713	253,245	250,735	236,196
Total Equity attributable to equity holders of the Bank	729,161	668,918	613,369	576,344	520,757
Non-controlling interest	-	1,271	1,100	661	243
Total Equity	729,161	670,189	614,469	577,005	521,000
Total Liabilities and Equity	**10,722,851**	**9,901,962**	**8,296,791**	**7,257,958**	**7,049,225**
MEMORANDUM ITEMS					
Contingent liabilities	225,407	251,670	233,451	213,598	215,512
Commitments	1,590,156	1,612,122	1,647,091	1,190,714	1,049,804

The Group's five year summary - extracted from the respective audited financial statements (continued)

C. STATEMENTS OF CASH FLOWS

	2016 €000	2015 €000	2014 €000	2013 €000	2012 €000
Net cash from operating activities	768,054	1,124,108	766,887	509,520	397,001
Cash flows from investing activities					
Dividends received from equity shares	5,628	5,808	4,926	5,433	1,723
Interest received from investing securities	59,783	58,998	45,394	37,484	50,165
Acquisition of non-controlling interest	(5,000)	-	-	-	-
Purchase of equity investments	-	(100)	(200)	-	-
Proceeds from Visa transaction	22,042	-	-	-	-
Proceeds from sale of equity instruments	3,043	-	-	-	-
Net increase in investment securities	(388,362)	(853,476)	(692,500)	(379,284)	(6,575)
Purchase of property and equipment	(8,111)	(9,132)	(14,649)	(10,414)	(7,273)
Proceeds on disposal of property and equipment	598	-	8	-	8
Net cash (used in)/from investing activities	(310,379)	(797,902)	(657,021)	(346,781)	38,048
Cash flows from financing activities					
Proceeds from issue of subordinated bonds	111,591	-	-	-	-
Debt securities in issue	-	-	-	-	40,000
Dividends paid	(30,575)	(29,362)	(34,466)	(34,516)	(23,010)
Net cash from/(used in) financing activities	81,016	(29,362)	(34,466)	(34,516)	16,990
Increase in cash and cash equivalents	538,691	296,844	75,400	128,223	452,039

D. PERFORMANCE EXPRESSED IN RELATION TO AVERAGE TOTAL ASSETS AND AVERAGE CAPITAL EMPLOYED

	2016* %	2015 %	2014 %	2013 %	2012 %
Operating income to total assets	2.4	2.7	2.7	3.1	3.2
Operating expenses to total assets	1.1	1.2	1.2	1.3	1.3
Profit before tax to total assets	1.1	1.3	1.3	1.6	1.6
Profit before tax to capital employed	16.9	18.4	17.5	21.1	22.3
Profit attributable to equity holders to total assets	0.7	0.9	0.9	1.1	1.1
Profit attributable to equity holders to capital employed	11.0	12.4	11.6	14.4	15.1

**Ratios exclude gain on Visa transaction.*

Group Financial Highlights in US dollars 30 September 2016

The following figures were converted from Euro to US Dollars using the rate of exchange ruling on 30 September 2016. The rate used was €1 = US$ 1.1169. This does not reflect the effect of the change in the rate of exchange since 30 September 2015 which was €1 = US$ 1.1208.

	2016	2015
	US$'000	US$'000
Net income attributable to equity holders of the Bank	105,817	88,967
Net income per share	27c	25c
Gross dividend paid	51,209	49,948
Net dividend paid	33,286	32,466
Gross dividend per share	13c	14c
Total assets	11,976,352	11,098,119
Liquid funds	191,046	141,952
Investments and financial assets at fair value through profit or loss	4,611,347	4,252,121
Advances	6,813,196	6,341,694
Investments in equity-accounted investees	108,385	108,610
Share capital	435,591	403,488
Capital reserves	40,566	40,579
Retained earnings	338,243	305,657

BOV

Bank of Valletta