Bank of Valletta p.l.c.

Annual Report & Financial Statements

2014

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BOARD OF DIRECTORS

John Cassar White (Chairman)
Joseph Borg
Roberto Cassata
Mario Grima
Taddeo Scerri
Paul Testaferrata Moroni Viani
George Wells
Franco Xuereb
Joseph M Zrinzo

COMPANY SECRETARY

Catherine Formosa

EXECUTIVE COMMITTEE

Charles Borg (Chief Executive Officer)
Michael Borg Costanzi
Joseph M Camilleri
Romeo Cutajar
Victor Denaro
Kenneth Farrugia
Michael Galea
Elvia George
Mario Mallia
Peter Perotti
Anthony Scicluna
Joseph Agius (*Appointed 6 October 2014*)

Kenneth B Micallef (Secretary)

AUDITORS

Deloitte Audit Limited
Deloitte LLP (United Kingdom)

LEGAL COUNSEL

Michael Borg Costanzi
Louis de Gabriele
Camilleri Preziosi Advocates

NOTICE OF MEETING

The Annual General Meeting of the Bank will be held at the Grand Master Suite, Hilton Malta, St Julians, on Wednesday 17 December 2014 at 16.30hrs.

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Il-Belt Valletta VLT 1130, Malta
Registration Number C 2833

Board of Directors & Secretary

John Cassar White

Chairman

R&N 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 of the board of Middlesea Insurance p.l.c. John worked with the Bank of Valletta for thirty seven years until 2008. He also served on the board of various 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.

Joseph Borg

C RM NED *

Appointed to the Board in December 1998. Mr Borg currently chairs the Board's Risk Management Committee and is also a member of the Compliance Committee. For a number of years, he chaired the Board's Audit Committee and was a member of the Remuneration Committee. Mr Borg is the managing director of FXB Group of Companies. He served on the Council and the Gozo Committee of the Malta Federation of Industries and is presently the vice-president of the Gozo Business Chamber. He has also been a director of the Oasi Foundation since its inception.

Roberto Cassata

NED *

Appointed to the Board in September 2003. Dr Cassata is an auditor and accountant by profession and also studied Economics at the Palermo State University. Throughout his career Dr Cassata held various senior positions within the UniCredit Group where he is presently Head of Public Sector Sicilia of UniCredit S.p.A. Dr Cassata has also worked with PricewaterhouseCoopers where he was, amongst others, responsible for the Sicilian Operational Department.

Mario Grima

C RM NED *

Mario Grima was appointed to the Board in December 2013. Mr Grima chairs the Compliance Committee and is also a member of the Risk Management Committee. He had served on the BOV Board between 1996 and 2001 and was employed with the Bank for 37 years. He retired from the Bank in 2011 and his last post was that of 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. 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.

Taddeo Scerri

A R&N NED *

Appointed to the Board in April 2013. Mr Scerri currently chairs the Board's Audit Committee and is a member of the Board's Remuneration and Nominations Committee and of the Bank's Asset and Liability Committee (ALCO). He is a qualified accountant and is the Managing Partner of RSM Malta. He is Chairman of the Malta Football Association Members Club Licencing Board and is also a member of the Association's Finance Committee.

Paul Testaferrata Moroni Viani

C RM NED *

Appointed to the Board in December 2007. Mr Testaferrata Moroni Viani is a member of the Bank's Risk Management Committee and Compliance Committee. He was a member of the Remuneration Committee for a number of years. He is a director of companies forming part of the Mercury p.l.c. Group and also sits on the boards of various other companies, including GO p.l.c., Middlesea Insurance p.l.c. and Vltava Fund SICAV p.l.c.

George Wells

A RM NED *

Appointed to the Board in December 2005. Mr Wells is a Chartered Management Accountant and currently a member of the Board's Audit Committee and the Risk Management Committee. He was also a member of the Bank's Asset and Liability Committee (ALCO) for a number of years. Mr Wells had served as Deputy Chairman and a Council member of the Malta Stock Exchange. He was formerly also a director on various companies in the UK and Executive Director of Stainless Steel Products Limited, subsidiary company of Jacuzzi Brands Inc. Group of Companies of the USA.

Franco Xuereb

C RM NED

Appointed to the Board in December 2012. Mr Xuereb is currently a member of the Board's Risk Management Committee and a member of the Compliance Committee. Mr Xuereb is Chairman of the BOV Employees' Foundation and has worked at BOV since 1983. He graduated with honours in Business Management from the University of Malta in 1988 and has held various posts within the BOV Group including General Manager and Director of BOV Stockbrokers Limited. He is currently Executive Head of the Bank's Investment Operations Department. Mr Xuereb served as a BOV Board member in 2005 and 2008. Between 2005 and 2010 he also sat on the Board of Directors of Growth Investments Limited. He has participated in various courses both locally and abroad and has, on numerous occasions, been invited as guest speaker at various seminars and conferences.

Joseph M Zrinzo

A R&N NED *

Appointed to the Board in December 2013. Mr Zrinzo is currently a member of the Board's Audit Committee and a member of the Remuneration and Nominations Committee. Mr Zrinzo served as a BOV Board member between 1996 and 1998 and was founder member of The Malta Shareholders Association. Mr Zrinzo at present 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. Mr Zrinzo has a vast experience of international trade having operated businesses with European, North African and Middle-East Companies.

Catherine Formosa

Group Company Secretary

Appointed BOV Group Company Secretary in October 2009. Dr Formosa 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 Formosa read law at the University of Malta and joined the Bank in June 2000 where she headed the Legal Advice Section at the Bank's Legal Office. Before joining the Bank, Dr Formosa worked at the Tax and Legal Department of PricewaterhouseCoopers. She is also a visiting lecturer at the Faculty of Laws at the University of Malta.

A	Member of the Audit Committee
C	Member of the Compliance Committee
R&N	Member of the Remuneration and Nominations Committee
RM	Member of the Risk Management Committee
NED	Non-executive Director
*	Independent

Chairman's Statement

John Cassar White

Deposits rose by €900 million to €7.1 billion as at end September 2014

A SATISFACTORY RESULT FOR FY 2014

Bank of Valletta (BOV) Group registered a pre-tax profit of €104.1 million for the financial year which ended on 30 September 2014, compared to €115.8 million last year. The Board views this as a satisfactory result which was achieved in a challenging environment of historically low interest rates, sweeping changes in banking regulation, increasing regulatory and supervisory costs, and rising geo-political risk in North Africa and Eastern Europe. Core operating profit, which excludes fair value movements and profits from associated companies, increased marginally to €87.9 million.

The loan portfolio rose by 5% year-on-year, and stands at €3.9 billion. Demand for credit increased across all segments, with the main growth being recorded in the home loans portfolio. Deposits rose by €900 million to €7.1 billion as at end September 2014, the main increase being recorded in short term products. Growth in deposits was equally distributed over the different customer segments, with strong increases being registered on the household, business retail, corporate and institutional sectors.

A detailed analysis of the Group's performance for the year is given by the CEO in his report.

COMPREHENSIVE ASSESSMENT 2014

As from the first week of November 2014, the European Central Bank (ECB) took over the responsibility for European banking supervision as part of the Single Supervisory Mechanism (SSM). The ECB, in liaison with the national competent authorities of participating EU countries, will directly supervise 120 banks deemed as significant credit institutions. In addition, the ECB will oversee the less significant credit institutions, which will continue to be supervised by the national competent authorities. BOV will be supervised directly by the ECB, in view of its standing as the largest credit institution in Malta.

Before assuming its new supervisory responsibilities, the ECB conducted what it termed as a "Comprehensive Assessment" of the euro area banking system – a financial health check on banks that started in November 2013 and took twelve months to complete, ending in October 2014. The Assessment consisted of two pillars, namely a point-in-time Asset Quality Review (AQR) that assessed the quality and the value of the banks' exposure to counterparties; and a forward-looking stress test that examined the resilience of banks' balance sheets to adverse stress scenarios. The results were published on 26 October 2014.

The Comprehensive Assessment re-affirmed that the Group's capital base exceeds the regulatory capital requirement, even under a hypothetical high stress scenario. At the start of the AQR, at 31 December 2013, BOV had a Common Equity Tier 1 (CET1) ratio of 11.2%. As a result of collateral revaluation during the AQR, the ratio was lowered to 10.7%, and this was taken as BOV's opening CET1 ratio for the purpose of the stress test.

The stress test contemplated a 'baseline scenario' and a more severe 'adverse scenario', both spread over three years. Taking into account the AQR results, the application of the baseline scenario resulted in a CET1 ratio of 11.9%, being the lowest capital level over the three-year period. This outcome ratio was a full 3.9 percentage points over the ECB's hurdle rate of 8.0%. The application of the adverse scenario resulted in a CET1 ratio of 8.9%, also significantly higher than the hurdle of 5.5%.

The Board noted with satisfaction the outcome of the Comprehensive Assessment. In our opinion, this result will serve to boost market confidence in the strength and stability not only of BOV, but of the entire Maltese financial system.

The AQR also identified an under-provision for doubtful debts amounting to €16.4 million, comprising €13.1 million on collective provisions and €1.8 million on specific provisions. This under-provision resulted from the netting protocols found in the AQR methodology, whereby no netting of over and under provisions was allowed across the different portfolios. Excess provisions on some portfolios were not offset against understated provisions on other portfolios. If over- and under-provisions could have been offset under the AQR methodology, the Bank would have ended up with an over-provision of €5.77 million (after tax). The under-provisions for doubtful debts are related to the prudential nature of the AQR and are not accounting provisions.

The Bank's Non-Performing Exposure (NPE) ratio, which relates non-performing exposures to total loans, was calculated under the AQR methodology at 18.3%, up from 11.8% as at December 2013. Part of this difference would be attributable to differences in methodology between the AQR protocol and the European Banking Authority regulation followed by BOV. There may, however, be other qualitative factors which the Bank will evaluate when more information becomes available to it as part of the supervisory dialogue.

We view the Comprehensive Assessment as a positive experience from which many lessons can be drawn, especially with regards to the improvement of risk policies, provisioning models, data governance framework, valuation protocols and processes in line with best international practice. BOV will be guided in this endeavour by the dialogue with the Joint Supervisory Team as part of the SSM.

CAPITAL MANAGEMENT AND DIVIDEND DISTRIBUTION

Strengthening the capital base remains one of the Bank's top priorities. Notwithstanding the transition during this year to the tougher CRD IV capital requirements, BOV managed to register a CET1 ratio of 11.7% on a CRD IV basis; its total capital ratio stood at 14.5%.

The Bank's dividend policy attempts to balance the dividend expectations of the market with the need to continue building up the Bank's capital base through the retention and ploughback of earnings. The Board of Directors is this year recommending a final gross dividend of €0.0925 per share which, taken together with the gross interim dividend of €0.0425 per share paid in May 2014, makes a total gross dividend of €0.135 per share. The total dividend for the year represents a gross yield of 6.05% by reference to the closing share price of €2.23 per share at 30 September 2014 and a net dividend cover of 2.4 times.

In arriving at its recommendation, the Board took account of the under-provision of €16.4 million (€10.6 million after tax) which resulted from the AQR methodology. This amount was carved out of the year's distributable profits and set aside as a Pillar 2 capital allocation, until more detailed information is forthcoming from the Joint Supervisory Team.

As in previous years, the Board is also recommending a bonus issue of 1 share for every 11 shares held on 16 January 2015 by capitalisation of reserves amounting to €30 million increasing the permanent capital from €330 million to €360 million.

Barring unforeseen developments, the Group is on track to fully implementing the normal CRD IV capital requirements by January 2019. There remains, however, the question of whether BOV will be subjected to an additional capital buffer in view of its standing as a domestically significant bank – and of what the amount of such additional buffer would be.

STRENGTHENING CORPORATE GOVERNANCE

The Board's strategic priority is to safeguard the stability and sustainability of the Bank, as Malta's largest financial institution, for the long-term. A major requisite in this regard is the development and maintenance of a robust governance structure. The Group has this year embarked on the reform of its governance structure to align it with best international practices. The Board has sought independent expert and supervisory advice in this respect, and is now also being guided by the consultative document Corporate Governance Principles for Banks issued by the Basel Committee on Banking Supervision in October 2014.

The revised structure involved the creation of the role of the Chief Operating Officer (COO), who reports directly to the Chief Executive Officer (CEO), and the regrouping of the current responsibilities and functions of the Chief Officers under three roles, namely the Chief Risk Officer (CRO), the Chief Financial Officer (CFO) and the Chief Business Development Officer (CBDO). The first two report directly to the COO, while the CRO reports directly to the Board of Directors in line with regulatory recommendations. The CEO, the COO, the CRO, the CFO and the CBDO will constitute the Bank's Management Board. The Bank is currently in the process of filling these posts.

The principal aim of the governance reform is to develop a more focused corporate governance structure, as well as to ensure greater efficiency in dealing with the various major challenges that the Bank will be facing over the coming years.

Another major reform taking place within the Bank is the restructuring of the credit function. The aim here is to draw a clear line between the origination of credit, and the sanctioning thereof. The reform aims to extend the "four eye approach" to business lending, and to embed the culture of accountability for credit decisions taken. The quality of customer service, and the promptness of responses to credit proposals, will be safeguarded through Service Level Agreements which shall be binding on both front and back office functions. The Credit reform will also do away with certain organisational structures that may not be conducive to efficient customer service.

OTHER STRATEGIC PRIORITIES

The long-term sustainability of the Bank also demands the maintenance of a strong IT infrastructure and the development of an IT strategy closely aligned with business strategy. The Bank is in the process of developing a robust IT architecture, built around a core banking solution, which will enable organic development of IT systems in response to the ever-changing needs of business. This intertwining of IT and business strategies should be one of the main tasks of the new Management Board in the years ahead.

Other strategic objectives concern human resources, processes and data management. The Bank will continue to build up and retain a professional and motivated workforce with the right mix of skills and experiences. Career development, ongoing training and succession planning will be the three pillars upon which HR strategy will be built. Priority will also be given to process management and to the constant re-engineering of those processes through which products and services are distributed to the Bank's customers, while identifying and mitigating operational risks within those processes.

Finally, the Bank will strengthen its data governance framework, with the twin aims of improving data quality and ensuring ready accessibility of relevant and accurate data to business users. Concerns about the general quality of data within the European banking system have been voiced by the ECB following the Comprehensive Assessment. The Bank will take careful note of any supervisory comments on data quality, and incorporate such feedback into its data management strategy.

OUTLOOK

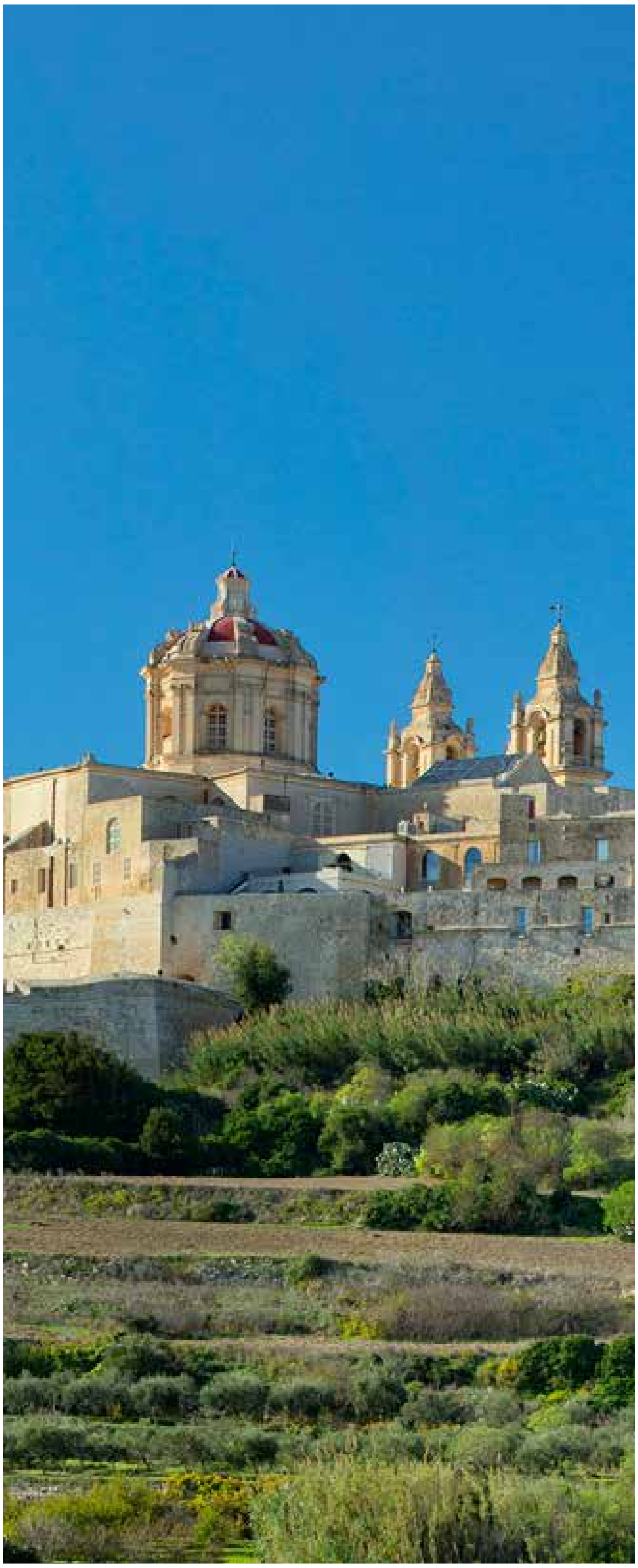
In the first half of the year, global economic growth was considerably lower than expected mainly as a result of rising geopolitical tensions. In the euro area, economic activity remained subdued mostly due to the sluggishness of domestic demand. Labour market conditions remained weak while inflation remained low to the point of raising concerns about potential deflationary pressures.

In Malta, economic activity continued to outperform that of the euro area driven by buoyant domestic demand. Real GDP growth is expected to reach 3% in 2014 as a result of strong investment expenditure. Despite its relative strong economic performance, Malta needs to continue to tackle structural challenges in order to maintain healthy public finances and strengthen the country's external competitiveness.

BOV plays a critical role in the local economy and this makes it important for the Bank to consistently maintain a prudent business model supported by a cautious risk appetite.

A FINAL WORD

My final word is one of gratitude – to the thousands of BOV customers who do business with us on a daily basis, and to whom we pledge our commitment for a quality service; to the supervisory authorities for their guidance and advice; and to all the Group employees, without whose commitment and hard work these results would not have been possible.



John Cassar White
Chairman
5 November 2014

CEO Review

Charles Borg

I am pleased to report that the BOV Group has registered an operating profit before tax of €104.1 million for the financial year ended 30 September 2014

INTRODUCTION

Despite operating in a challenging environment characterised by low interest rates, severe geo-political tensions and weak demand, Bank of Valletta continued to perform well in all areas of its operations.

Balance sheet growth was sustained and the Bank continued to register positive increases in all areas of commission and fee income. Concurrently, we have continued to invest in strengthening our governance structures and support infrastructure as we continue to focus on the long term sustainability of our organisation.

THE ECONOMIC ENVIRONMENT

During the period under review, the Maltese economy grew at a solid pace with real growth rates of between 3% and 4%. It is noteworthy to mention that the Bank's loan book during the same period registered a higher level of growth (5%) compared with the Gross Domestic Product (GDP) growth in the same period.

In line with trends in the Euro area, the rate of inflation remained at very low levels, averaging below 1%. This mirrored the historically low interest rate scenario that we continued to experience across all major global economies during this financial year. The gradual global economic recovery has suffered a number of setbacks during the course of the year and is now believed to be weaker and more uneven going forward. As a result, interest rates have reached record lows, with euro rates even going into negative territory. Nevertheless, deposits continued to grow at a significant rate, with the Bank's deposit base increasing by more than €900 million over the previous year.

REVIEW OF PERFORMANCE

Bank of Valletta Group reported profit before tax of €104.1 million for the financial year ended 30 September 2014. This represents a decrease of €12 million when compared to the €115.8 million pre-tax profit for financial year 2013. This result was achieved despite the challenging economic scenario within which we operated together with the regulatory changes and associated costs that were experienced. Furthermore, as a result of restrained market sentiment, the BOV Group did not benefit from favourable market movements experienced during the previous year.

Core Operating Profit of €87.9 million, which excludes price movements and profits from our associated companies, is up by 2% from last year. The drop in interest income, attributed to the persisting low interest rate environment, was mitigated by satisfactory growth in commission and trading income.

The higher impairment charge of last year resulted from an exercise which applied a more conservative view of the value of collateral held on non-performing exposures.

Return on equity of 17.5% (FY 2013: 21.1%) and Cost/Income Ratio of 43.1% (FY 2013: 38.7%) compare favourably with international banks.

BOV Group's results for the financial year are summarised in the table below.

	Sep-14 € million	Sep-13 € million	Change € million	%
Net interest income	126.0	131.0	(5.0)	-4%
Net commission and trading income	74.8	69.7	5.1	7%
Operating expense	(93.5)	(89.1)	(4.4)	-5%
Impairment charge	(19.4)	(25.6)	6.2	24%
Core profit	87.9	86.0	1.9	2%
Fair value movement	9.0	17.4	(8.4)	-48%
Share of profit from associates	7.2	12.4	(5.2)	-42%
Profit before tax	104.1	115.8	(11.7)	-10%

a. Net Interest Income

Net interest margin for the year of €126.0 million represents a decrease of 5% from last year. Lower returns were experienced on both the Retail and the Treasury segments despite the growth in volumes in both areas. The retail margin was particularly impacted as only around one fourth of incoming deposits were deployed in lending. The negative interest introduced by the ECB in June 2014 compounded the pressure on our Treasury operations.

b. Net Commission and Trading Income

Net commission and trading generated income of €74.8 million, represents an increase of 7% over the €69.7 million last year, contributing 37% towards operating income, up from 35% for FY 2013. Strong performance continued to be experienced by all major business lines, except for trade related income on business connected with North Africa. Fee income on investment services, bancassurance and credit card business show satisfactory growth. Foreign exchange earnings are also up, year on year, driven by an increase in the volume of transactions.

c. Operating Expenses

Operating costs for the year amounted to €93.5 million. This represents an increase of 5%, or €4.4 million, over the previous year. The introduction of a new regulatory reporting regime and participation in the Asset Quality Review pushed up regulatory costs substantially. These were also impacted by an increase in the Bank's contribution towards the Deposit Guarantee Scheme resulting from the growth in customer deposits and higher contribution rates. Increases in human resource expense and IT costs were partly offset by the curtailment of the discretionary spend.

In the coming years, substantial investment in IT systems and infrastructure is expected to be made to ensure that BOV's technology platforms are able to meet the ever-increasing needs of our customers and regulatory requirements.

d. Net Impairment Charge

The Asset Quality Review and the stress tests carried out by the European Central Bank earlier this year highlighted the need for banks to adopt a more conservative approach

towards provisioning, an approach which BOV has consistently applied over these past years. Last year, in line with the recommendations made by both local and European regulators, the Bank increased its provisions on individually assessed exposures, and the impairment charge for FY 2013 was mostly specific in nature. The charge of €19.4 million for this year reflects a higher collective charge, as the more conservative view of collateral held was also applied to performing exposures assessed on a collective basis. During FY 2014, the cautious view of provisions required on non-performing exposures was retained.

e. Fair Value Movement & Share of Profit from Associates

While financial markets were generally calm during FY 2014, these favourable market movements were much more subdued than those experienced in the previous year. This influenced the overall performance for FY 2014 as the €9.0 million fair value gains this year are practically half the amount reported last year. The market movements also had an impact on the results of our associates resulting in a share of profit for FY 2014, of €7.2 million, which is 42% less than the €12.4 million registered last year.

f. Review of Financial Position

Total assets as at 30 September 2014 stood at €8.3 billion (September 2013: €7.3 billion), whilst equity attributable to the shareholders of the Bank increased by a further 6% to €613 million.

BOV continued to strengthen its common equity Tier 1 ratio to 11.7% on a CRD IV basis and its total capital ratio which stood at 14.5%. At 30 September 2014, the Group's liquidity position remains strong with a net advances to deposit ratio of 55% and a liquidity ratio of 48.5%.

REVIEW OF BUSINESS OPERATIONS

Customer Deposits

Despite intense competition, Bank of Valletta continued to consolidate its position as the bank of choice for customer deposits. FY 2014 was a record year with customer deposits increasing by €900 million, or 14% over last year, to reach an all-time high of €7.1 billion. This solid performance underlines the strength of the BOV Brand and highlights the confidence it enjoys amongst local and foreign retail and institutional customers. As at the end of the financial year under review, Bank of Valletta was the Bank with the largest deposit base in the market. Excess funds were channelled into good quality short-term investments and liquid assets, in line with the Bank's conservative treasury management policy.

Loans and Advances

Concurrently, our credit portfolio registered an aggregate net increase of €214 million equivalent to a year on year increase of 5%. These positive results were registered in both the business and retail arms with increases of around 3.3% and 8.5% respectively.

The increase registered in the business segment underscores the Bank's continuous commitment to support the local business community by continuing to make credit available in a responsible manner. The increase in business lending has translated in over €400 million in new facilities provided to more than 1,250 local businesses and entities. These funds were distributed amongst various economic sectors, both traditional as well as new emerging sectors which are reshaping the economic landscape. The Bank also ensured realignment of its pricing mechanism to both international and local specific realities with an overarching

reduction in its business base rate twice during this financial year, along with promoting credit products with embedded advantageous interest rates.

During the year under review, the Bank continued to strengthen its position in the market for SME financing. Various products were made available to local SMEs with the main objective of easing their burden related to external financing as well as enhancing their opportunities to borrow. One of the Bank's success stories was the JEREMIE financing product which was fully committed during the current financial year and which featured lower financing costs through decreased interest rates and reduced collateral requirements. Through JEREMIE, the Bank managed to assist 650 SMEs, through 760 loans, for a total equivalent committed amount of €62 million.

Particular emphasis has also been given to start-ups and micro SMEs. By tapping into EU centralised funds, the Bank was in a position to start offering a new risk-sharing instrument branded as the 'BOV Start-Plus Financing Package'. This micro-credit instrument is aimed at start-ups and micro-enterprises which usually find it hard to obtain external financing, but which constitute an important pillar for the country's economic development.

Payments and Cards

FY 2014 was characterised by the SEPA end date for both direct debits and credit transfers. The Bank was engaged in an extensive communication exercise with its customers, providing its support in the process of having the payments systems updated and tested to ensure compatibility with the new SEPA formats. As an early adopter of SEPA payments, we have benefitted from the expertise developed in this business, placing us in a good position to manage the transition efficiently together with our customers.

Concurrently, the Cards business registered another positive performance driven by a sustained increase in cards usage as our customers continued to shift towards using cards for both domestic and international payments. When compared with the previous year, total cards turnover processed by the Bank exceeded the €1 billion mark for the first time, representing an increase of over 12% when compared with the previous year.

During this financial year, we have continued to increase our debit and credit card base and we have also seen healthy increases in our merchant acquiring portfolio. The BOV Loyalty Rewards programme was enhanced with the addition of new partners providing added value to our premium credit card holders. The Bank continued with its significant investment in this business area and will soon be migrating its debit card base onto the new cards IT platform.

Bancassurance

The Bank's Bancassurance business continued to perform well, driven by the attractiveness of life insurance products and the stable bonus rate declared by MSV Life. Commission income from this area of business has increased by 20% when compared to the previous financial year.

Foreign Exchange

The Bank maintained its position as a market leader in the provision of foreign exchange services, both to its retail

as well as its corporate and institutional customers. In this regard, foreign exchange business continued to be the main contributor to non-interest income. During the period under review, exchange income amounted to €17.5 million.

Stockbroking

Our Stockbroking business registered another positive year and we have retained our position as a leading broker both in terms of local stockbroking as well as dealing on the international bond and equity markets.

The Bank will be launching its on line trading platform in the coming months, in line with our policy to offer value-added services to our clients.

Funds Business

Valletta Fund Management Ltd, our Funds Management subsidiary, has undertaken a review of its range of investment funds positioning them under five key pillars - Liquidity Funds, Income Funds, Income and Growth Funds, Growth Funds, and Absolute Return Funds. VFM is currently managing €722 million and servicing over 31,000 investors. Concurrently, Valletta Fund Services Ltd. has continued with its positive trajectory with assets under administration reaching €2.9 billion over the period under review covering the servicing of alternative investment funds, UCITS and private equity funds. VFS is currently providing its services to asset managers based in 12 EU and non EU member states. We believe that this is one of the main growth areas for the BOV Group and we are committed to continue to invest in our fund services business, seeking to attract more foreign business to Malta.

Trade Finance

The Bank's Trade Finance arm continued to perform well despite the challenging environment in the nearby African continent, with the amount of fee income being practically on the same level of previous year.

CAPACITY BUILDING INITIATIVES

Strengthening of our IT Capability

During FY 2014, the Bank conducted an IT review assessment in order to identify areas for improvement which would enable the organisation to move up its service maturity levels and become more effective as a business partner. A number of recommendations have been made, many of which have already been transformed into ongoing prioritised initiatives.

We appreciate that today, IT constitutes a critical capability for all organisations and this applies even more so to the financial services sector. The Bank's investment in IT continues to proceed at a steady pace. In this regard, a number of customer-facing solutions were upgraded during the financial year under review primarily in the areas of Cards, Investments and Multi-channel Banking. We have also continued to support the business to respond to the increasing regulatory demands through the updating of various bank systems so as to facilitate compliance.

Focus on International Corporate Business

During this financial year, the Bank continued to focus on its International Corporate business offering. Our International Corporate Centre (ICC) provides a holistic service proposition to international corporate customers registered in Malta.

Our international corporate clients are involved in diverse business areas including iGaming, insurance, aviation, fund management, and general trading amongst others.

Following a detailed review of the ICC operations undertaken during FY 2014, we are now at an advanced stage in the implementation of a re-structuring exercise with the aim of improving the customer experience whilst strengthening our internal control mechanism with particular focus to anti-money laundering provisions. To this end, we have updated our Customer Acceptance Policy and completed a review of jurisdictions and intermediaries with whom the Bank conducts business. So as to better support the increased business activity and provide additional capacity, the International Corporate Centre is in the process of being relocated to new premises in Zachary Street, Valletta.

Restructuring of Trusts Business

We have also commissioned an independent governance review of our Trusts business. We have implemented the various recommendations that emerged from this exercise thereby continuing to strengthen this business area.

Review of Investments Structure

Another initiative was the completion of a comprehensive review of the Bank's investment advisory services. The review was conducted to take stock of the situation following the restructuring of our Personal Banking model which included the opening of six new Investment Centres offering a full range of advisory services to retail clients. Concurrently, the Bank's Wealth Management Division has undertaken various changes to re-align its service offering in line with the changing regulatory environment, market developments and investor expectations. The Bank continued to invest heavily both in its infrastructure and human resources in this area, ensuring that all licensed personnel receive ongoing and specialised training on market developments, product and service offering and changes in the regulatory environment. Going forward, we are set to continue to give our full focus to this area as we seek to attract high net worth clients to our Wealth Management proposition.

Credit Review

The Bank is also conducting a review of its credit process, as part of its effort to align all of its governance structures and operational processes with best international practice. This review has two main objectives, namely, to strengthen the "four eye" approach to the lending business, and to free up front office functions so that they can focus more on business generation and customer relationship management.

The first objective will be achieved by the introduction of a double vote requirement in the sanctioning of proposals. The second will be met through shifting analytical and support work from the front to the back office, thereby freeing up customer-facing resources in the interests of offering a better service.

STRATEGY & PROCESS MANAGEMENT

The Bank's strategic plan is structured around a set of top level goals and critical success factors which are measured through both financial and non-financial key performance indicators that collectively ensure long-term value creation for all stakeholders. The execution of the strategic plan is two-pronged with business plan initiatives and a number of strategic change programmes having a wider corporate scope and broader strategic implications.

During this financial year, the Bank embarked on a number of strategic change programmes in the areas of Custody, Investment Services, International Corporate Business and Electronic Banking Services. These and other strategic change programmes are supported through a programme governance framework so as to ensure that objectives and intended benefits are reached, thereby delivering value to the business.

During the last financial year the Bank also set up a dedicated unit to review business processes and deliver an improved customer experience. The team members were provided with formal training and achieved certification from The BP Group of the UK in the CEM method (Customer Experience Management method).

During the first few months and in order to establish work practices, the new team focused on various process issues relating to the Bank's retail network. This effort resulted in significant improvements within various customer facing sub-processes.

The unit has also been tasked to review the end-to-end processes related to the Bank's International Corporate Clients business as well as the Bank's Payments Business. The team also assisted in the review of processes related to Business Lending and Valletta Fund Services.

HUMAN RESOURCES

Bank of Valletta considers its employees as the most important asset that provides the Bank with a competitive advantage in the market. Our people distinguish us as a caring, friendly and flexible bank that is focussed on supporting our customers and engaging on long term relationships that are mutually beneficial.

During the period under review, the Bank continued to work towards ensuring an optimal deployment of its human resources. We also continued to update our career development strategies and anticipating skills requirements with a view to ensuring that we would be in a position to meet future resourcing demands.

Our focus remains that of being a good employer, providing equal opportunities to our people. We are steadfast in our commitment to retain high levels of employee motivation and engagement and to provide lifelong learning opportunities to our people and rewards based on performance.

We are proud to be recertified by the National Commission for the Promotion of Equality (NCPE) as an equal opportunities employer through the Equality Mark certification. This highlights our resolve to provide equal access to career opportunities and development irrespective of gender, status or caring responsibilities for our employees. The Equality Mark constitutes an important certificate of the Bank's policies and underlines the capacity of the Bank to remain true to best practices in this area for the forthcoming years.

Furthermore, the Bank today continues to employ people with different abilities in excess of the quota of 2% of the total workforce that is required by Maltese Employment Legislation.

CUSTOMER EXPERIENCE AND INNOVATION

During this financial year, the Bank launched a new web portal that delivers an enriched customer experience. Customer centricity was the core objective in all the aspects of the new web portal's design and structure. Not only does the new bov.com provide access to mainstream internet banking but it is also an effective communications vehicle for the Bank's more specialised services relating to Stockbroking and Wealth Management together with fund business and administration. It also integrates different portals that share information seamlessly with all the information also being completely accessible through any mobile device.

The new bov.com is a point of departure and its platform is designed in a manner which will allow it to evolve in parallel with the continuous development of the Bank. We are proud of this development and truly believe that the new portal will enable the Bank to continue to project itself as a leader in engaging with its customers online.

We continued to strengthen the service offering through our Retail Network and Customer Service Centre with further investment to develop our investment advisory service. Concurrently, the Bank continues to develop its relationship banking model whilst aligning its service offering to the changing requirements of the Bank's customer base.

Furthermore, we have widened the range of products offered from Investment Centres as the Bank continues to enhance its customer value proposition for retail clients in line with market developments. In this regard, our Investment Centres enjoyed their first full year of operation, with very encouraging results in terms of customer satisfaction and business development.

The Bank's Wealth Management Division also enjoyed another strong year in terms of new customer relationships, portfolio performance, customer satisfaction levels and assets under management which have now exceeded the €1 billion mark. All this, whilst implementing a multi-year investment in a state of the art IT infrastructure devoted to the clients' investments business. We launched a number of structured notes for our high net worth clients. Moreover, our Wealth Management Division has introduced a Managed Advisory Service alongside the current Advisory and Discretionary services offered to our customers.

To ensure continuity following the JEREMIE's success, the Bank developed another very attractive product aimed at local SMEs. Leveraging on the TLTRO scheme (targeted longer-term refinancing operations) made available by the European Central Bank (ECB), the Bank has set up a specific pot with the purpose of assisting all local SMEs. The BOV 4 SME financing offers loans at very attractive hybrid pricing mechanism incorporating a fixed rate of four per cent for the initial four years and a highly competitive interest rate thereafter. This pricing mechanism is directed to provide stability in financing costs for SMEs in the initial four years of the funding period.

Particular emphasis has also been given to start-ups and micro-SMEs. By tapping into EU centralised funds, the Bank was in a position to start offering a new risk-sharing instrument branded as the 'BOV Start-Plus Financing Package'. This micro-credit instrument is aimed at start-ups and micro-enterprises which usually find it hard to obtain external financing, but which constitute an important pillar for the country's economic development. The product was launched in January 2014 and a total of 46 SMEs have been assisted for a total committed amount of €750,000 in less than 9 months.

Within the consumer finance segment, the Bank was also very successful and managed to advance more than €350 million over a 12 month period. Concurrently, despite the highly competitive landscape, the Bank managed to continue consolidating its position in the market, especially related to home loans. In this sector, we launched a number of innovative and attractive products during this financial year aimed at different segments of society and addressing different customer needs. On the personal financing side, products were focused for various purposes with the most successful being the ECO loans and motor loans.

We have also continued to invest in our various service delivery channels. The Bank continued with the process of upgrading its ATMs to the new generation Advanced Deposit ATMs which provide customers with real-time cash and cheque deposit features. Furthermore, during the financial year under review, BOV ATMs were equipped with voice technology making them easily accessible to the visually impaired. A series of audio instructions, delivered through headphones, guide the user through various steps to carry out the transaction. When the audio instructions are activated, the ATM screen goes blank safeguarding the privacy of the customer from onlookers.

INVESTMENT IN FACILITIES AND ENVIRONMENTAL MANAGEMENT

During this financial year, the Bank continued to invest in its customer facing and support infrastructure. We were proud to inaugurate the House of the Four Winds that includes modern facilities for our Board of Directors' meetings and also houses the Chairman's Office and the Office of the Company Secretary. Apart from being an architectural statement that integrates naturally into its historical surroundings, the project included the introduction of a new public piazza with Ponsomby's Monument, which was also restored by the Bank, as its focal point. A main feature of the design of the new House of the Four Winds is that it steps back several meters from the bastions, opening up views which were previously hidden by the former building.

Another major project that commenced during the period under review was the re-development of our premises in Gżira which are set to integrate various customer facing activities within a new and modern environment. Other projects included the renovation of our premises in Zachary Street to house our Trusts Unit and the International Corporate Centre.

The Bank continued to invest in initiatives so as to ensure that we reduce our carbon footprint and minimise the impact of our operations on the environment. We have continued with our investment in renewable energy sources. Our PV panel installations, at twenty different locations, have generated more than 140,000 units of electricity resulting in a reduction of circa 130,000kg of CO2 emissions. Furthermore, we have continued to upgrade our air conditioning systems to modern, energy efficient installations and have widened our efforts to the areas of water efficiency and waste separation.

RATING RESULTS

On the 20 January 2014, the international credit rating agency Fitch affirmed its rating of the Bank of Valletta Group at BBB+, with a stable outlook.

In their report, Fitch said it attributed its confirmation of BOV's rating to the Bank's leading domestic franchise, its strong funding base and its satisfactory liquidity position, which benefits from a large and stable customer deposit base. The agency referred to BOV's revenue-generating capacity, which has shown resilience even in a scenario of low interest rates.

Fitch also said that BOV's rating was also influenced by high industry and single-borrower credit concentrations which are derived from the small size of the Maltese economy. The rating agency further commented about the Bank's doubtful loans which they said to have stabilised and are beginning to benefit from an improved provisioning policy implemented by BOV over the past two years.

INTERNATIONAL AND LOCAL ACHIEVEMENTS

During the financial year under review, Bank of Valletta continued to be recognised, both locally and internationally, for its solid performance and innovative spirit.

For the fifth consecutive year, the BOV Group was named 'Best Bank in Malta for 2014' by Global Finance (New York), testimony not only to the health of its balance sheet but also to the level of innovation and customer focus inherent in its application of technological developments and the quality of its customer service. For the second consecutive year, Global Finance also named BOV the 'Best Trade Finance Bank in Malta'. We were proud to have been selected as 'Safest Bank in Malta for 2014' – an award recognising the Bank's prudent approach in the management of its balance sheet as a key pillar in ensuring sustainable growth.

Bank of Valletta was also presented with the eBusiness Award by the Malta Communications Authority for its innovative strategy related to the development of its self-service touch points. The award highlights the Bank's commitment to keep its customer at the core of its operations, irrespective of the channel they uses to interact with the Bank.

Bank of Valletta persevered in its mission to be Malta's Green Bank. Our efforts to put the green stakeholder at par with the other stakeholder groups were recognised when the Bank was awarded the Conservation Award for Sustainable Development during the 7th edition of the Environmental Award for Enterprise organised by the Cleaner Technology Centre. This award recognises the efforts made to reduce the impact that the Bank's operations have on the environment.

As one of the largest organisations in Malta, we take great pride in our people, and try to instil a spirit of comradeship throughout the Group. The high level of institutional pride that exist in our people came out very evidently when the BOV Football team emerged as the winner of the first edition of the Champions Bank 2014 football tournament which was held in Belgrade.

CONCLUSION

At BOV we are passionate about our business. Our philosophy is to create value for our customers, stakeholders and the Maltese economy in a responsible and sustainable manner. This will continue to shape our vision and growth.

The past years have shown that the Bank was resilient to the instability in the financial services markets. The Bank has emerged stronger and is the Bank of first choice in the local market as evidenced by the growing customer base. The trust and confidence shown by our customers will be reciprocated by an even stronger commitment to continue to develop meaningful, long term relationships built on understanding, support and respect underpinned by a superior customer experience.

Conscious of the growing needs and expectations of our customers, we will focus our resources to strengthen our technology and support capabilities, invest in our employees to develop their professional skills and deliver a superior product offering.

We have always believed that the wider community has also been instrumental to our success. We have acknowledged this in the past through our intense and extensive Corporate Social Responsibility (CSR) Programme. We are determined to pursue our goal and obligation to improve the wellbeing of our communities through active support. A section focusing on the Bank's CSR Programme is included as part of this annual report.

The BOV brand and what it stands for represents the shared vision and aspirations of its stakeholders. As a genuine and caring Bank, our job is to make it happen.

All of this would not be possible without the dedication and commitment of the whole BOV Team. First of all, I would like to thank my colleagues who form the Bank's Executive Team for their advice and continuous support. It is through their leadership and unwavering commitment that Bank of Valletta continues to steer forward and to achieve the ambitious objectives that year on year we set for ourselves.

My thanks also go to the Chairman and Board of Directors who have always been supportive to me, for their strong sense of strategic vision and their provision of proper direction which enable the Bank to approach the business in a conservative but very customer centric manner.

A special word of thanks goes to all the Bank's employees for their loyalty and constant dedication towards the organisation and its customers. It is through their efforts that the Bank manages to deliver a customer experience that is built on the principles of our brand promise.

Finally, I would also like to thank our customers for the trust and confidence that they show in the Bank. All our efforts are directed at strengthening the relationship with our customers and every relationship is important to us. This is what drives us to continue to deliver an added value service to continue grow the people's trust and confidence in the BOV Brand.

Charles Borg
Chief Executive Officer
5 November 2014

Corporate Social Responsibility (CSR)

It's all about making it a journey, not a destination

In the dynamic environment in which we operate, profits alone are not deemed an adequate measure of an organisation's performance. Demands for accountability and transparency from both public and private sectors have soared, making it necessary to focus equally on financial and non-financial results, whilst managing stakeholder needs and expectations.

In this context, for Bank of Valletta, being a responsible citizen is not a point of arrival but rather an ongoing journey. It is often recognised that the impact of an organisation is proportionate to its footprint. For an organisation like the Bank of Valletta Group, with over 1,500 in its employ, over 300,000 customers, and the responsibility of being one of the major economic drivers in Malta, that footprint is significant.

By integrating corporate responsibility as a strategic investment in our core business strategy and operations, Bank of Valletta chooses to recognise its social and environmental objectives, alongside financial performance. Other stakeholders like the employees, the customers and our suppliers have to be reckoned with, making Corporate Responsibility an important tool to mediate and achieve an optimum balance in responding to the different needs of the various stakeholders.

In this regard, CSR goes a long way to enabling the Bank to keep sustainable development in focus every day and at every level of the organisational structure.

Committed to remain the Maltese Bank, contributing responsibly to the Maltese society.

Bank of Valletta gave its support to Malta's first Sculpture Garden, inaugurated at Verdala Palace.

Bank of Valletta, as the Maltese Bank, partnered with Joseph Calleja the Maltese Tenor. Together, we also launched the BOV Joseph Calleja Foundation.

The Marigold Foundation - BOV in the Community was launched this year to enhance the structure through which the Bank supports philanthropic projects.

The BOV Joseph Calleja Children's Choir was the protagonist of the Tenor's concert in Summer.

Bank of Valletta continues to support the Malta Philarmonic Orchestra, in a bid to continue creating awareness about local arts and culture.

The BOV Retrospective Art Exhibition celebrating the artistic career of Anthony Mahoney marked its 22nd edition.

Being an actively responsible catalyst in our Communities

Since its early days, the BOV Group has been actively engaged in developing, strengthening and energising our communities. This is how we live up to our brand.

During this financial year, the Bank felt that it had to enhance the structure through which it supports philanthropic projects. It is in this regard that it set up the Marigold Foundation - BOV in the Community which has the objective of helping organisations who are focused on addressing the challenges faced by the Maltese society. The Bank retained its annual appointment with the L-Istrina BOV Piggy Bank Campaign that this year runs into its 11th edition. Featuring a two month campaign through all schools and selected retail outlets, the campaign is intended to raise funds for L-Istrina, a national fund under the auspices of the President of Malta which has the objective to assist those who are most in need in our society.

There is more to being a responsible corporate than philanthropy. Bank of Valletta spreads its effort under seven pillars through the BOV Community Programme. The Bank takes pride in endorsing local talent, helping young artists to take the first critical steps in their careers, whilst celebrating the lives of renowned artists like Anthony Mahoney in the BOV Retrospective Art Exhibition that this year marked its 22nd edition.

Other regular events included the support towards the BOV Opera Festival at the Manoel Theatre, the support extended to the Astra and Aurora theatres in Gozo and that towards the events forming part of Malta's 50th Independence Anniversary celebrations organised by Fondazzjoni Ċelebrazzjonijiet Nazzjonali.

The BOV Joseph Calleja Foundation, a brainchild of the Maltese Tenor whom the Bank is endorsing, was also launched. The Foundation was set up with the dual objective of promoting and supporting exceptional artistic talent and socially supporting underprivileged children.

Education constitutes another pillar of our Programme. Among the various projects supported by the Bank is the National Literacy Strategy which is being spearheaded by the Ministry of Education and Employment in a bid to eradicate illiteracy in our society. Other educational projects that found the Bank's support include the Dinja Waħda programme with BirdLife Malta for primary school children, an underwater archaeology programme that introduces children to Malta's marine heritage and the Hands On Heritage which brings episodes from our past back to life.

Promoting a healthy work-life balance whilst exposing the general public to the fascinating world of sports is what prompts Bank of Valletta to continue supporting the major sporting associations in Malta.

As the patron of heritage, the Bank remains also very active in supporting the conservation of Malta's heritage sites. We are currently supporting two major projects: the restoration of the vault of the Sanctuary in Mellieħa and the restoration of various artefacts in Gozo's Għajnsielem Chapel.

Furthermore the Bank continues to collaborate with business and representative bodies in a bid to continue supporting local entrepreneurs and organisations. This goes beyond projecting itself as the Bank for SMEs with the design of tailor-made financial products and services to help this sector maximise its' potential for growth. One of the main initiatives taken during this financial year was the collaboration with the Chamber of Commerce, Enterprise and Industry to put together a toolkit for SMEs promoting the concept of responsible entrepreneurship amongst the business community, irrespective of size.

The Green Bank

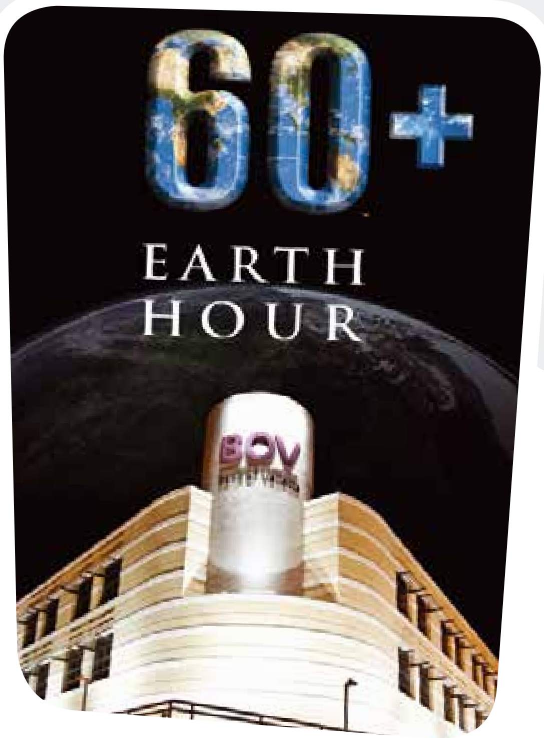
Ensuring that our business remains environmentally sustainable is a responsibility that the BOV Group does not shy away from. At Bank of Valletta, we are continuously evolving our business practices to reduce our environmental impact, by integrating green behaviours into our daily work practices as well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

The Bank's green approach is not a programme with a finite date, but an ongoing commitment to consider the green stakeholder at a par with the interest of the other stakeholder groups. Thus the Bank's Green Manager is responsible for managing its green action plan, whilst Green Leaders across the organisation ensure that everyone feels part of this undertaking. FY 2014 saw Bank of Valletta planting more than 1,500 trees – a tree to represent every employee within the Group. The Bank also participated in the European Week for Waste Reduction, giving our people the opportunity to dispose of unutilised and unwanted electronic goods, so that now they enjoy a second life.

Bank of Valletta also continued to invest in photovoltaic cells at several sites, whilst our water conservation project continues to save the world more water.

Our efforts as a Green Bank were recognised when we were awarded the Conservation Award for Sustainable Development. This award recognises the efforts made to reduce the environmental impact of our processes and practices.

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 and reduce its energy consumption and carbon footprint in the future.



For the third consecutive year, Bank of Valletta switched off the lights of the BOV Centre façade to commemorate Earth Hour for the third consecutive year.

As the Green Bank, Bank of Valletta remains firm in its commitment to consider the environment at a par with other stakeholders.

Our People – Working Together Responsibly

Bank of Valletta's success is inextricably linked with the management of its most valuable asset – its people. In this regard one of its primary challenges is to support its employees from the moment they join the organisation and throughout their entire career with the Group.

Its commitment to a fair human resources policy was recognised this year when the BOV Group obtained recertification of the Equality Mark by the National Commission for the Promotion of Equality (NCPE). The Equality Mark acknowledges the Bank's responsibility to provide equal access to opportunities and career development based on employees' potential, irrespective of their gender and caring responsibilities. Furthermore the Bank invests heavily in the continuous training and development of its employees providing them with the best possible knowledge required to give our customers best of class service whilst increasing their potential to advance in their personal career. Only this year, the Bank launched a BOV Graduate Development Programme, aimed at providing younger recruits with a sound hands-on approach to management.

Nurturing an open culture among our people is critical for the Bank. This goes beyond empowering and involving them in decision-making, but also in creating space for them to grow as individuals and socialise through the BOV Sports and Social Club. This year, the BOV Football team was successful in winning the first edition of the Champions Bank tournament which was held in Belgrade.

Despite the substantial workforce and different lifestyles, BOV makes every effort to ensure every employee feels valued and appreciated, truly contributing towards a learning organisation.

Nurturing an open culture among our people includes creating space for them to grow as individuals.

Serving Customers Responsibly

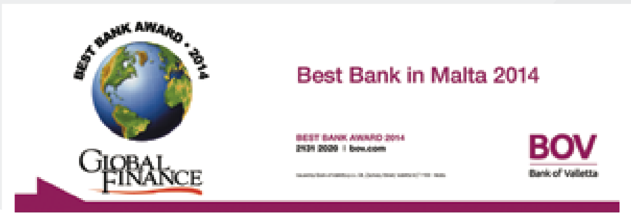
An intimate knowledge of our customer has always been crucial to our vision. This remains true today across our scope of operation - from the team working in every physical branch across the retail network to our spectrum of self-service banking channels that make the most of technological developments to bring convenience and innovation at the customer's fingertips.

This vision is what contributed to Bank of Valletta winning the Best Multi-Channel Strategy Award organised by the Malta Communications Authority. The Bank has always kept the customer at its core, and this strategy led the Bank to register a number of firsts including the first ATMs in 1989, Internet Banking in 2002 and Mobile Banking in 2012. All innovations centred on providing a uniquely positive customer experience, whether the solution targets mainstream or niche markets. Thus this year saw Bank of Valletta investing in a speech-enabled solution for its growing fleet of Advanced Deposit ATMs. In this manner, both visually-impaired and illiterate customers can use the service without resorting to third party assistance.

The Bank's passion for maintaining an open dialogue with each and every one of its customers was the driving force behind the Bank's decision to invest in a complete overhaul of its bov.com. This project, that involved an extensive cross-section of the Bank's business functions, led to an innovative platform that seamlessly integrates the portals of the BOV Group with social media channels providing a two-way communication channel between the Bank and its customers. Innovative features, such as the BOV Click-to-Chat, go a long way in enabling anyone browsing the site to contact a BOV representative from anywhere within the site.

The Bank recognises that change is the only constant, and that the only way to continue to remain the Bank of Choice for its customers is by remaining ahead of times, scanning the environment and anticipating changes in customers' needs. The Bank is committed to do just that, by investing primarily in its human and IT resources to ensure that customers always find the Bank's valid and relevant support whenever they need it.

Bank of Valletta's multi-channel strategy won the Bank the MCA eBusiness Award for Best Multi-Channel Strategy.



Global Finance named Bank of Valletta Best Bank in Malta for 2014 and Best Trade Finance Bank 2014 for Malta.

Looking Ahead Responsibly

Throughout FY 2014, Bank of Valletta Group addressed a number of important milestones relating to its Corporate Responsibility. However, the journey is not over - society will continue to evolve and develop. BOV must continue to respond and react to its environment while anticipating the demands of its stakeholder groups.

We believe we are on the right path, in striking a balance between the demands of the different stakeholder groups, and in retaining an active role in the communities in which we operate, involving our people as we go along.

Bank of Valletta is committed to remain the Bank with a Maltese soul, with roots deep in our rich past but with its gaze firmly riveted into the future. Thus we propose to grow together with and for our stakeholders, contributing responsibly to the Maltese society one step at a time.

As the patron of heritage, BOV remains very active in supporting the conservation of Malta's heritage sites and events that bring past anecdotes back to life.

The BOV Volleyball Marathon is another instance where volunteers come together for a philanthropic cause, dedicating their free time for the community.

L-Istrina BOV Piggy Bank Campaign marks its 11th edition this year, and remains an important highlight of the Bank's social pillar.

Directors' report as at 30 September 2014

The Directors present their 41st Annual Report, together with the audited financial statements of the Bank of Valletta Group and the Bank for the year ended 30 September 2014.

Principal Activities

The Bank of Valletta Group comprises Bank of Valletta p.l.c. (the Bank), Valletta Fund Management Limited and Valletta Fund Services Limited. The Group also has two associated companies, Middlesea Insurance 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 (Cap.371 of the Laws of Malta) and the Investment Services Act (Cap.370 of the Laws of Malta). The Bank is an enrolled tied insurance intermediary of MSV Life p.l.c. under the Insurance Intermediaries Act (Cap.487 of the 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

Valletta Fund Management Limited (VFM) is 60% held by the Bank with the remaining 40% held by Insight Investment Management Limited, one of UK's largest asset managers. VFM provides management services for SICAV companies. Valletta Fund Services Limited (VFS), a fully owned subsidiary of the Bank, provides fund administration services.

The Associates

MSV Life p.l.c. operates as a life assurance company licensed under the Insurance Business Act (Cap.403 of the Laws of Malta). Middlesea Insurance 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 2014 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 €0.0425 per share was paid on 23 May 2014. The Directors propose a final gross dividend of €0.0925 per share, resulting in a total gross dividend for the year of €0.135 per share. The aggregate net dividend for the year is €0.0878 per share, amounting to €28.96 million (2013: €0.1727 gross per share as adjusted for bonus issue resulting in a net payout of €37.05 million). The total dividend is analysed as follows:

	The Bank	
	2014	2013
	€	€
Gross	44,550,000	57,000,000
Tax at source	(15,592,500)	(19,950,000)
Net	28,957,500	37,050,000

Directors' report as at 30 September 2014 (continued)

Board of Directors

The following Directors served on the Board during the period from 1 October 2013:

John Cassar White
Joseph Borg
Roberto Cassata
Ann Fenech (*resigned 19 December 2013*)
Mario Grima (*appointed 19 December 2013*)
George Portanier (*resigned 19 December 2013*)
Taddeo Scerri
Paul Testaferrata Moroni Viani
George Wells
Franco Xuereb
Joseph M Zrinzo (*appointed 19 December 2013*)

Six vacancies will arise on the Board at the forthcoming Annual General Meeting (AGM). Following a call for nominations of Directors, pursuant to Article 60 of the Articles of Association, the Bank received seven valid nominations, including three from incumbent Directors. Pursuant to Article 60, an election will be held during the forthcoming AGM.

Directors' Responsibilities

The Directors are required by the Companies Act (Cap.386 of the 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 (Cap.371 of the Laws of Malta) and the Companies Act (Cap.386 of the 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 the financial statements, it is appropriate to continue adopting the going concern basis in preparing the financial statements.

Auditors

As had been indicated in the Directors' Report as at 30 September 2013, the Bank has this year carried out a tender process for the external audit contract. The tender process was overseen by the Audit Committee and resulted in a recommendation to appoint KPMG as the Group's external auditors, which recommendation was endorsed by the Board. The appointment of KPMG as the Bank's external auditors will be proposed at the forthcoming AGM. Subject to the approval of the shareholders, KPMG will undertake the audit of the BOV Group for the year ending 30 September 2015.

The Bank thanks Deloitte Audit Limited and Deloitte LLP (United Kingdom) for the sterling service and professionalism demonstrated in their external audit role over the past years.

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 40th AGM held on 19 December 2013, on the 17 January 2014, 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 €300,000,000 to €330,000,000 divided into 330,000,000 ordinary shares with a nominal value of €1.00 each fully paid up.

Directors' report as at 30 September 2014 (continued)

At the forthcoming AGM, the Board of Directors is proposing a bonus issue on the 16 January 2015 of 1 share for every 11 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 €330,000,000 to €360,000,000.

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 2014, 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 2014, shareholding in excess of 5% of the issued share capital of the Bank was held 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 the 31 October 2014.

Pursuant to the Bank's Articles of Association, the appointment of Directors to the Board is reserved exclusively 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 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. There is one contract with an employee in the Executive Management grade which contains a severance payment clause.

It is hereby declared that as at 30 September 2014, 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 2014 (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 2014 are contained in the Corporate Governance Statement.

Number of shareholders analysed by range:

	31 October 2014	
Range of shareholding	**Total Shareholders**	**Shares**
1 – 500	1,210	341,704
501 – 1,000	2,218	1,557,773
1,001 – 5,000	8,404	22,113,432
5,001 and over	7,397	305,987,091
Total shareholding	**19,229**	**330,000,000**

Standard Licence Condition 7.35

Pursuant to Standard Licence Condition 7.35, 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 31 October 2014 and signed on its behalf by:

John Cassar White
Chairman

George Wells
Director

Capital & Risk Management Report

30 September 2014

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Capital & risk management report 30 September 2014 (continued)

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/07/2012. The Group publishes these disclosures on an annual basis as part of the Annual Report and Financial Statements.

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). Nonetheless, this Capital and Risk Management Report has been subject to comprehensive internal review procedures and was reviewed by the Bank's Audit Committee and approved by the Board of Directors. The Bank is satisfied that internal verification procedures ensure that these Additional Regulatory Disclosures are presented fairly.

1.2 BOV Risk Management Function

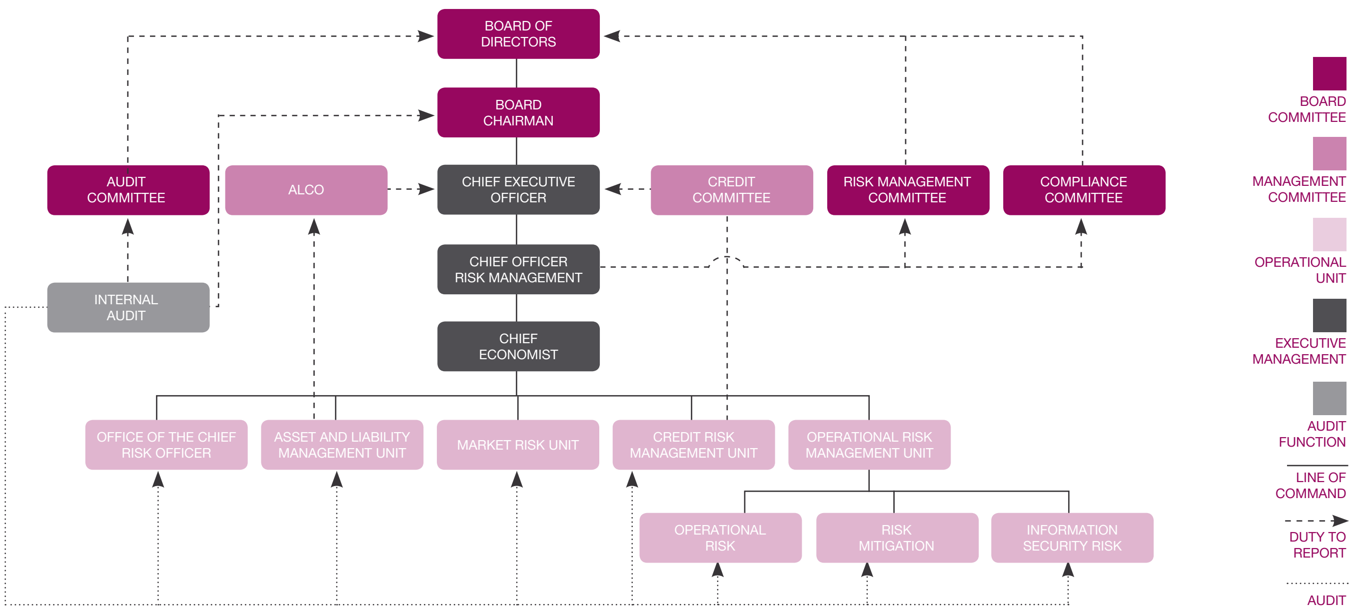
Risk management lies at the heart of the business of financial intermediation. All the Group's activities involve, to varying degrees, taking on and managing risks or combinations of risks. The Group assumes some risks consciously with the aim of managing them to achieve a return in excess of the cost of risk. Such risks provide an opportunity (the expected return) and a threat (the potential loss), and the Group will only assume those risks in respect of which the reward is expected to be greater than the potential loss. These include credit, market, interest rate and insurance risks. The Group's appetite for taking on such risks is formally articulated in the Risk Appetite of the Board of Directors.

Other risks are not taken on deliberately, but are the inevitable consequence of being a financial services provider. These include liquidity, solvency, business continuity, reputational and conduct risk. The Group has no appetite for such risks, and its strategy in their regard is to minimize the losses which may arise therefrom.

The cost of taking on these various risks comprises both "expected" and "unexpected" losses. Expected losses are those that may be anticipated based on historical experience, and are statistically the average of the Group's loss distribution. Such losses are covered through pricing and accounting provisions. Unexpected losses, which represent the deviation of actual losses from the predicted expected losses, are covered by capital. It is the responsibility of the Risk Management function to ensure that both classes of losses are adequately covered at all times.

The objective of the Risk Management function at BOV is not only to minimise the cost of risk, but also to maximise return on assets and liabilities within the risk appetite as articulated by the Board of Directors. 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 Financial Control; and the third line is constituted by Internal Audit, which is the function that provides independent assurance to the Board.

The Risk Management function, within the second line of defence, falls under the responsibility of the Chief Officer Risk Management, and operates within a wider Bank structure that reflects the risk appetite and risk management philosophy articulated by the Board of Directors. The Risk Management function at BOV is represented below:



Capital & risk management report 30 September 2014 (continued)

1.3 BOV Risk Units

The risk management function at BOV is carried out by five operational units:

Office of the Chief Risk Officer (OCRO)

OCRO takes a holistic, enterprise-wide view of the risks taken on by the Group in the carrying out of its business. It is a central unit which is responsible for the management of risk reporting, risk data governance and IT infrastructure. OCRO's brief includes the monitoring of the Group's economic and regulatory environment, with special focus on the local and European economy and on regulation. The Unit is responsible for preparing the Bank to enter the Single Supervisory Mechanism and the Resolution and Recovery regime, both of which are key elements of the European Banking Union. It is also responsible for coordinating 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).

Asset and Liability Management (ALM) Unit

The ALM Unit is responsible for the identification, assessment and reporting of risks related to the balance sheet, including solvency, liquidity and interest rate risks. A key responsibility of ALM is capital management, including capital planning and forecasting. In this context, ALM is responsible for ensuring compliance with the minimum capital and liquidity standards required by the CRD IV package which came into force on 17 July 2013.

The Unit act as the main support function for the Asset and Liability Committee (ALCO) and assists the committee by monitoring and modelling the structure and income-generating capacity of the Group's balance sheet.

Operational Risk Management Unit (ORMU)

ORMU comprises three functions. The core operational risk function is responsible to coordinate and oversee the identification, assessment, management and reporting of operational risks by the business owners. The function is responsible for the implementation of the Operational Risk Management Framework (ORMF). The key elements of the ORMF are process mapping, risk identification, monitoring of key risk indicators, loss database, business continuity and scenario analysis.

The Risk Mitigation function is responsible for the mitigation of operational risks through the procurement of adequate and cost-effective insurance cover. The Information Security Risk function analyses and communicates information security risks and evaluates their potential impact on the business processes and objectives. This function performs risk assessments and recommends security measures and controls that optimise the return on investment and business opportunities.

Market Risk Management Unit (MRMU)

The main objective of MRMU is the management and control of market risk exposures in order to optimise return on risk while maintaining a market profile consistent with the Board's risk appetite. MRMU is responsible for the identification, assessment and reporting of risks in the Bank's investment portfolio. The market risk appetite is articulated at a high level in the Risk Appetite Framework, and in detail in the Treasury Management Policy, which sets limits and controls to safeguard the Bank's investment portfolio. The Unit ensures that the limits established in the Treasury Management Policy are adhered to.

Credit Risk Management Unit (CRMU)

The Unit's objective is to safeguard the soundness of the loan portfolio, to ensure sustainable and quality 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 Policy is designed to ensure that all areas of the Bank 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 Unit also undertakes an independent analysis of loan proposals which fall within the discretionary lending limits of the Credit Committee and of the Board of Directors. In addition, CRMU is responsible for portfolio management at a macro level where particular attention is given to any potential fallout from macroeconomic shocks, industry declines and excessive idiosyncratic risks.

1.4 Board and Senior Management Committees

The Board of Directors

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 normally meets twice a month unless further meetings are required. The Board regularly reviews and evaluates corporate strategy, major operational and financial plans, risk policies, performance objectives and business alternatives. It also monitors corporate performance against budget and past performance, within the parameters of all relevant laws, regulations and codes of best business practice. The Board has a formal schedule of matters reserved to it for decision and also delegates specific responsibilities to a number of Board Committees.

Capital & risk management report 30 September 2014 (continued)

Risk Management Committee

The Risk Management Committee assists the Board in assessing the different types of risks to which the Group is exposed. The 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. 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.

Compliance Committee

The Compliance Committee is responsible for overseeing the Group's compliance with the obligations imposed by legislation, codes, rules and regulations that are relevant to the Group and its business.

Up to financial year 2012, the Risk Management and the Compliance Committees had functioned as a single Risk Management and Compliance Committee. It was decided to segregate these two areas into two separate Board committees, in view of the increasing volume and complexity of regulatory issues impacting the two respective areas.

Audit Committee (AC)

The Audit Committee's Terms of Reference reflect the provisions of the relative Listing Rules. The main role and responsibilities of the Committee 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 Committee is also responsible for managing the Board's relationships with internal and external auditors.

Asset and Liability Committee (ALCO)

The role of ALCO is to manage the Group's balance sheet to achieve an optimal balance between risk and return. It takes an integrated view of asset and liability cash flows, their risks, and the management of such integrated exposures at a consolidated level. 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/or regulation. It gives guidance on risk and return to the business, and exercises executive authority in the area of interest rate management by setting base rates and rates payable on retail deposit products.

Credit Committee

This is a Management committee that has the highest discretionary lending authority following that of the Board of Directors. The role and composition of the Credit Committee is described further in paragraph 2.3.2 below.

1.5 Comprehensive Assessment 2014

The year under review was the year in which the European Union (EU) commenced its implementation of the Banking Union by introducing the three pillars which underlie this project. These consisted of the enactment of the Single Resolution Mechanism (SRM), which will be fully operational from January 2016; the harmonisation of Deposit Guarantee Schemes; and the launching of the Single Supervisory Mechanism (SSM), by means of the Comprehensive Assessment of major European banks carried out by the European Central Bank (ECB). Underlying these pillars is the "Single Rule Book" project, at the core of which lies the adoption by the EU of the Basel III regulatory regime.

Ever since the Basel III Accord was published in December 2010, BOV has given priority to tight capital management, with the primary focus being on strengthening the capital base through a prudent dividend payout policy and the plough back of earnings. The Bank's reported Common Equity Tier 1 (CET 1) ratio of 11.7% is evidence that BOV is today comfortably ahead of the CRD IV implementation schedule.

Barring unforeseen developments, the Bank is on track to fully implementing the normal CRD IV capital requirements, in January 2019. There remains, however, the question of whether BOV will be subjected to an additional capital buffer in view of its standing as a domestically-significant bank - and of what the amount of such additional buffer would be.

On 4 November 2014 the European Central Bank (ECB) will take over the direct supervision of the most 'significant' banks in the European banking union. These include BOV, which, as the largest Maltese bank, qualifies as a significant institution within its domicile. Before assuming its supervisory responsibilities the ECB conducted what was termed as a "Comprehensive Assessment" of the euro area banking system, focusing on 130 banks in 18 member states that constitute around 85 percent of euro area bank assets.

The Comprehensive Assessment comprised two main pillars: an Asset Quality Review (AQR) which had the objective of evaluating the quality of bank exposures to counter parties, including the adequacy of asset and collateral valuation and related provisions; and a stress test, the aim of which was to examine the resilience of banks' balance sheets to stress scenarios.

Capital & risk management report 30 September 2014 (continued)

The results of the Assessment were published on 26 October 2014, and can be summarized under three headings:

Capital Adequacy

At the start of the AQR, at 31 December 2013, BOV had a CET 1 ratio of 11.2%. As a result of collateral revaluation during the AQR, this ratio was lowered to 10.7% for the purpose of the "join-up", being the process whereby the quality-assured stress test results were integrated with the AQR results. This was taken as BOV's opening CET 1 capital ratio for the purposes of the stress test.

The stress test contemplated a 'baseline scenario' and a more severe 'adverse scenario', both spread over three years. The benchmarks stipulated by the ECB were CET 1 ratios of 8.0% and 5.5% respectively. Any bank with a stressed ratio of below these levels would be required to recapitalise.

The baseline scenario, which assumed a three-year horizon, resulted in a CET 1 ratio of 11.93%, being the lowest capital level over the period. This outcome ratio was a full 3.9 percentage points over the benchmark. The adverse scenario gave a ratio of 8.9%, or 3.4 percentage points clear of the benchmark. The Bank therefore has no capital shortfall under any of the stress scenarios.

Provisions for Doubtful Debts

The AQR highlighted an under-provision for doubtful debts amounting to €16.4 million, comprising €13.1 million on collective provisions and €1.8 million on specific provisions. This under-provision results from the netting protocols found in the AQR methodology, whereby no netting of over and under provisions was allowed across the different portfolios. Excess provisions on any portfolios were not offset against understated provisions on other portfolios. If the total provisions held by the Bank were to be compared to the aggregate provisions required by the AQR model, the position of the Bank would be an over-provision of €5.77 million (after tax).

Following this result, the Bank will review its collective provisioning model with a view to aligning it with common best practice.

Non-Performing Exposures

The Bank's Non-Performing Exposure (NPE) ratio, which relates non-performing exposures to total loans, was calculated under the AQR methodology at 18.3%, up from 11.8% as at December 2013. Part of this difference would be attributable to the AQR requirements being more rigid in terms of forbearance and debt service coverage ratios than the normal practices followed by BOV. There may, however, be other qualitative factors which the Bank will evaluate when more information becomes available to it as part of the supervisory dialogue.

BOV will apply the lessons learnt from the Comprehensive Assessment to improve its risk policies, provisioning models, data governance framework, valuation protocols and processes in line with best international practice. It will be guided in this endeavour by the dialogue with the Joint Supervisory Team as part of the SSM.

1.6 Risk Initiatives for Financial Year 2014

During the year, the Risk Management function carried out risk assessments on a number of business areas within the Bank, including the International Corporate Customers (ICC) business. The latter assessment was carried out in conjunction with an independent consultant, and resulted in a number of recommendations to strengthen internal controls over this function, which are now in the process of implementation.

Section 2: Credit Risk

2.1 The Nature of Credit Risk

Credit risk is the risk of incurring a financial loss on loans and receivables resulting from a change in the credit quality of the Bank's debtors (customers, clients or market counterparties), which can ultimately result in default. Credit risk also includes concentration risk which results from a high level of exposure to a single client or a group of connected clients.

The granting of credit is one of the Bank's major sources of income and, as the most significant risk, the Bank dedicates considerable resources to managing it.

2.2 The Management of Credit Risk

The purpose of credit risk management is to keep credit risk exposure to a permissible level in relation to capital, to maintain the soundness of assets, and to ensure returns that are commensurate with the credit risk assumed.

Credit risk is managed and controlled throughout the Bank on the basis of established credit processes, regulatory requirements, and within a framework of credit policies and delegated authorities based on responsibility, skill and experience. These include the application of:

a) high-level credit policies designed to facilitate the identification and mitigation of credit risk;

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b) lending guidelines defining the responsibilities of lending officers that seek to provide a disciplined and focused benchmark for credit 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) a high level reporting system giving a holistic overview of the Bank's credit portfolio quality; and
i) communication and provision of general guidance on all credit-related risk issues, including regulatory changes, to promote consistent and best practice throughout the Bank.

Regulatory capital requirements for credit risk are measured using the Standardised Approach method. Among the risks in which the Bank engages, credit risk generates the largest regulatory capital requirement.

2.3 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:

2.3.1 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; and
d) Trade finance.

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

Policies are revised periodically to keep them abreast with ever changing market conditions. During this financial year the focus was mainly on the review of the Business Lending policy, in particular to bring it in line with the changes in the regulation.

2.3.2 Decision-making Procedures

Lending Authority

A system of discretionary lending limits is in place, governed by the Credit Policy, under which all lending decisions must be approved. Lending officers are each allocated a lending limit according to credit competence, proven judgement, experience and the nature and scale of lending in the business unit where they are posted. Exposures above certain limits require approval by the Credit Committee or the Board. Such proposals are independently reviewed by the Credit Risk Management Unit (CRMU). The credit proposal and CRMU's recommendations thereon are discussed and evaluated by the Credit Committee prior to the sanctioning or otherwise of the request. For proposals above a certain limit authorisation is sought from the Board of Directors.

A "four-eye approach" to credit proposals is applied across all levels of the hierarchy when a credit proposal falls outside the criteria set out in the Bank's Credit Policy.

For unsecured personal lending and for credit card applications, decision-making is simplified through the aid of a credit scorecard which analyses data and grades customers according to their credit-worthiness. The majority of proposals are approved or declined outright through the scorecard. 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.

The Credit Committee

The Credit Committee is the highest lending authority within the organisation after the Board of Directors. It is composed of representatives from the Credit and Risk Units and chaired by the Chief Officer Risk Management. The Credit Committee, which meets on a weekly basis or more regularly, as required, approves or declines lending proposals that fall within its delegated discretionary limit, and makes positive or negative recommendations to the Board on proposals which fall outside its discretionary limits. The Credit Committee further ensures that regulations are adhered to by business units.

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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.

An important tool used by CRMU is the Moody's Risk Analyst software solution. This system determines an appropriate credit grade for both corporate customers (non-SMEs) and SMEs. This system is supported by the use of internal rating systems (IRS) to monitor the quality of individual exposures and of the entire portfolio.

2.3.3 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 accepted by the Bank are listed in the Credit Policy and can be analysed into two groupings:

- Financial and other collateral, which enables the Bank to recover all or part of the outstanding exposure by liquidating the collateral asset provided, in cases where the borrower is unable or unwilling to fulfil its primary obligations. Cash collateral, securities (equities, bonds), collateral assignments of other claims or inventory, equipment and real estate (residential, commercial and industrial properties) typically fall into this category.
- Guarantee collateral, which complements the borrower's ability to fulfil its obligation under the legal contract, may be provided by third parties. Letters of credit, insurance contracts, guarantees and risk participations are included in this category. Guarantor counterparties include banks, parent companies, shareholders and associated counterparties. Guarantors are subject to the same upfront assessment process as the primary debtors.

The Bank is monitoring property prices on a regular basis and such collateral is revalued at the date of review of the facilities if it is found that the carrying value could have changed materially since last valuation.

In line with regulation, property collateral securing facilities of a material amount is subjected to an independent valuation on a more regular basis.

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.

2.3.4 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.

2.3.5 Reviews

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. Hindsight overviews are also used to assess the impact of periodically increased empowerment and sanctioning limits (to the front line management) on the quality of the loan book, and to disseminate the Bank's risk appetite, as well as guidance given by higher levels of sanctioning authority from time to time.

CRMU further monitors corporate clients whose repayments are in arrears. CRMU compiles a report which is raised to the Credit Committee on a monthly basis. 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.

2.3.6 Restructuring of Facilities

Rescheduling/refinancing is one of the management tools used to adjust the maturity structures of principal and interest payments in accordance with changes in the repayment capability of customers. 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. Rigorous

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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.

2.3.7 Rehabilitation Unit

Following the financial crisis and the downturn in specific economic sectors, the Bank felt the need to 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 since 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).

2.3.8 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.

2.3.9 Litigation Unit

When specific accounts become increasingly problematic, even 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 the 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 uncollectible, 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.

2.4 Credit Risk Portfolio Management

CRMU is responsible for monitoring the quality of the Bank’s credit portfolio. As part of this process the unit 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 among other macro analyses.

2.4.1 Loan Portfolio Management and the 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 analysed on a regular basis to determine whether there is impairment in customer’s business which merits a change in rating. These conditions (both financial and business related) are reviewed at least once a year, drawing on the combined expertise of business line staff and CRMU analysts. High quality tools are used to support the rating process, including analysis aids and the Moody’s Risk Analyst. The selection of tools and the choice of technique depend on the nature and level of the inherent risk.

2.4.2 Advances Portfolio

The Bank’s Gross advances portfolio to customers stood at €4.1 billion as at end September 2014, representing an increase of €213.8 million (or 5.5%) over September 2013. Growth was registered in all customer segments, mainly home loans, followed by the business and consumer segments.

Tight control of the loan book has ensured that there has been no significant deterioration in the overall credit quality of the advances portfolio with 80.7% of the total portfolio classified in the regular category (80.2% as at end September 2013).

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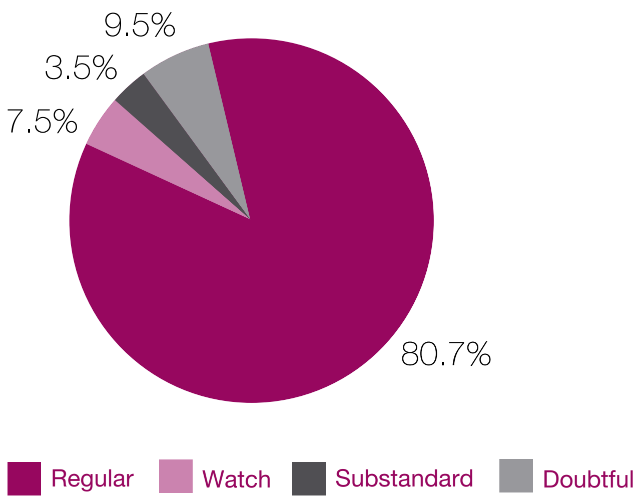
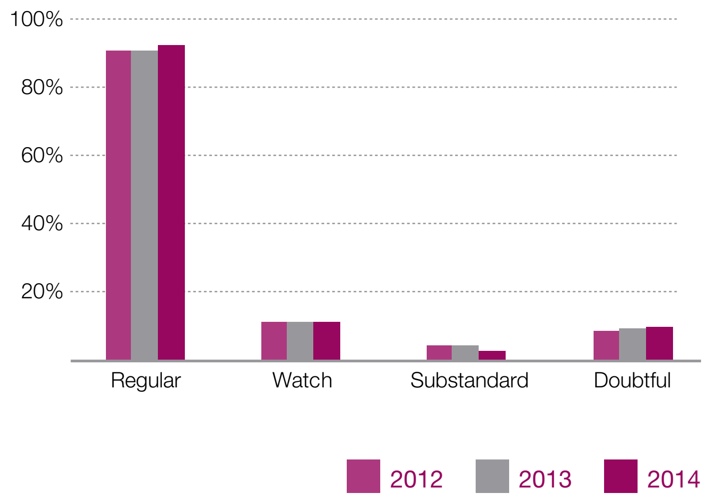
Doubtful loans increased to 9.5% of the loan book as at end September 2014 compared to the 8.9% registered in the previous year. The Bank took a cautious approach and in line with the revised methodology used by the Central Bank of Malta increased its loan loss coverage ratio from 51.1% to 54.0%.

Asset Quality by Credit Rating



Credit Quality of Loan Book (% in total)



The advances portfolio has an average maturity of 17.7 years. Business loans have an average maturity of 10.2 years, home loans an average maturity of 27.1 years, while consumer loans have an average maturity of 5.5 years.

Residual maturity of the Advances portfolio, broken down by exposure classes (€ million)

	Within 3 months	Between 3 months and 12 months	Between 1 and 5 years	Over 5 years	Total
Corporate	113.4	8.7	132.8	206.4	461.3
High Risk Areas	48.7	16.2	43.4	14.7	123.0
Past Due 90 Days+	173.3	8.9	50.1	103.3	335.6
Regional Gvmts or Local Authorities	2.0	-	0.1	15.3	17.4
Retail	98.3	10.5	87.6	281.1	477.5
Secured by Real Estate Property	222.2	24.5	95.3	1,779.0	2,121.0
State/Public Owned Companies	107.6	75.3	21.6	380.6	585.1
	765.5	**144.1**	**430.9**	**2,780.4**	**4,120.9**

Capital & risk management report 30 September 2014 (continued)

Exposures by Industry of the Advances portfolio, broken down by exposure classes (€ million)

	Household and Individuals	Wholesale and Retail Trade	Financial and Insurance	Transport and Storage	Construction	Others	Total
Corporate	9.2	67.3	39.8	187.0	9.1	148.9	461.3
of which SME	-	*62.3*	*26.0*	*128.7*	*6.6*	*96.3*	319.9
High Risk Areas	-	-	-	-	108.0	15.0	123.0
Past Due 90 Days+	65.4	57.6	0.0	7.4	87.9	117.3	335.6
Regional Gvmts or Local Authorities	-	-	-	-	-	17.4	17.4
Retail	358.7	42.6	1.8	6.5	8.6	59.3	477.5
of which SME	*0.0*	*21.9*	*1.6*	*3.9*	*5.3*	*36.2*	*68.9*
Secured by Real Estate Property	1,322.9	208.2	43.7	40.9	77.8	427.5	2,121.0
State/Public Owned Companies	-	-	228.1	70.0	-	287.0	585.1
	1,756.2	**375.7**	**313.4**	**311.8**	**291.4**	**1,072.4**	**4,120.9**

2.4.3 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. On review date, all exposures are assessed to establish whether the debtor is considered to be in a position to meet the outstanding obligations and to establish the appropriate credit grading.

Impaired Exposures

At the time of review of each relationship, the Bank assesses whether there is objective evidence that loans and receivables are impaired. Impairment arises as a result of one or more loss events that adversely impacted the estimated future cash flows of the financial asset or the portfolio, so that discounted future cash flows, from operations and/or from realisation of collateral, are less than the carrying value of the loan. Indications of impairment may include:

- Significant financial difficulty of the obligor
- A breach of contract, such as default or delinquency in interest or principal payments
- Probability that the borrower will enter bankruptcy or other financial reorganisation
- Failure of repeated attempts to restructure the borrowing.

Such exposures are also marked "Impaired" on the Bank's systems.

2.4.4 Approach to Forbearance

Forbearance measures occur in instances where the borrower is considered unable to meet the original terms and conditions of the contract due to financial difficulties. Based on these difficulties and if the Bank considers that repayment is possible within the revised terms of the loan, the Bank may modify the terms and conditions of the contract to allow the borrower sufficient ability to service the debt or refinance the contract. Forbearance modifications during this financial year included amendments to the contractual timings as well as refinancing.

The Bank's policies and practices are based on criteria which, in the judgement of management, indicate that repayment is likely to continue and after the initial period of financial difficulties the customer can revert to the previous terms, with appropriate support where necessary.

Capital & risk management report 30 September 2014 (continued)

Restructuring or refinancing measures are extended following a request by the customer. A financial difficulty test is carried out when changes in the terms and conditions are effected, to determine whether the debtor is in financial difficulties. If the debtor fails the test, the account is to be classified "Forborne". The test also determines the credit quality of the exposure. The financial difficulty test is raised by the Relationship Officer, assessed by Credit and reviewed by CRMU.

2.4.5 Loan Loss Allowances and Coverage

The Provisions Committee is the body responsible for the provisioning methodology. It is composed of representatives from Finance, Risk and Credit and meets regularly to discuss issues and rules relating to provisioning.

The Bank's methodology in respect of impairment allowances complies with the relative International Financial Reporting Standard (IFRS) and also takes into consideration the requirements of the Banking Rule 09 as revised in December 2013.

Impairment allowances are provided against the loan portfolio of the Bank, which comprises two categories, Performing and Non-Performing exposures. The Bank internally classifies the loan book by credit grading and whether exposures are secured or unsecured. The grading is a result of days delinquency or due to qualitative reasons, that is, the debtor is assessed as unlikely to pay its credit obligations in full without realisation of collateral, regardless of the number of days past due.

The Bank's internal rating system comprises the following categories:

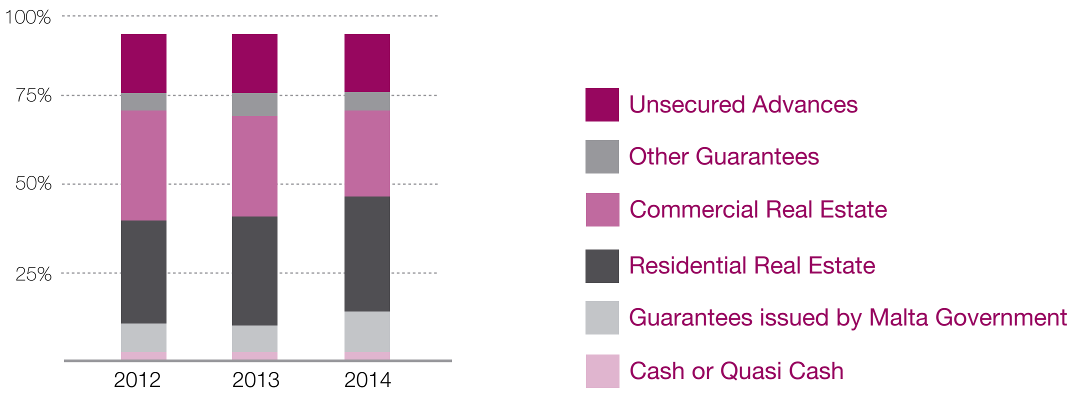
- 'Regular' - for accounts in order
- 'Watch' - between 30 and 60 days in arrears
- 'Substandard' – between 60 and 90 days in arrears, and
- 'Doubtful' - more than 90 days in arrears.

The Performing category includes accounts graded from Regular to Substandard while those in the Doubtful category are classified as Non-Performing Exposures. The latter are sub-classified into Doubtful and Impaired. Impaired exposures are those assessed by the Bank as non-recoverable in full, even after the realisation of collateral, and for which specific provisions are held. Both classes of exposures may include Forborne facilities.

Where a specific provision is not provided, a collective allowance is accounted for against a loan exposure. Although a specific provision is normally held for accounts classified in the Doubtful category, there may be exposures which do not attract a specific provision because in spite of the days delinquency, the Bank assesses full recoverability when including the realisation of collateral. In these cases only a collective provision is charged.

An analysis of the collateral cover reveals that 82.3% of the Bank's advances portfolio is covered by extendible security, out of which 74.0% is in the form of immovable property (residential and commercial).

Advances Coverage - Collateral Cover



2.4.6 Specific Impairment Allowance

A specific impairment allowance may be required following the individual assessment of an exposure for recoverability. In the event that the Bank does not expect to recover its exposure in full, even after realising the collateral held, a provision to cover the shortfall is necessary in line with IAS 39. Interest receivable on these exposures is immediately suspended and not recognised as interest income in the Statement of Profit or Loss.

Capital & risk management report 30 September 2014 (continued)

The specific and collective allowances held as at September 2014 are shown in the table below:

	Specific Allowance		Collective Allowance	
	Stock	Charge	Stock	Charge
	€'000s			
Business	128,056	15,792	50,725	7,363
Home Loans	16,826	6,867	4,503	1,737
Personal	6,684	1,324	4,061	235
Total	151,566	23,983	59,289	9,335

As per note 17 in the Notes to the financial statements, the balance of Specific Allowances at reporting date includes €80.2 million in respect of interest in suspense.

2.4.7 Collective Impairment Allowance

Credit facilities with less than 90 days arrears or those which are tested individually for impairment, and are found not to be individually impaired, are subject to collective impairment assessment. For the purposes of a collective evaluation of impairment, credit facilities are grouped on the basis of similar risk characteristics, taking into account asset type, industry, collateral type, past due status and other relevant factors. When assessing a group of credit facilities for collective impairment, a number of loss events are taken into consideration, including probabilities of default associated with the credit status of that group, and measurable economic conditions including sector performance, which may influence future cash flows from the assessed loans. Any collective impairment allowance found to be necessary is deducted from the total carrying amount of the portfolio.

During the past financial years, the Bank undertook detailed reviews of particular sectors within its portfolio to ascertain that each sector's estimated probability of default reflected the current economic scenario. The exercise carried out in financial year 2011 catered for the real estate sector. During financial years 2012 and 2013, the focus was on the construction and the wholesale and retail sectors, whereas during this financial year, further provisions in respect of exposures related to Libya and provisions to cater for off balance sheet items have now been included to better reflect the probability of default in these sectors.

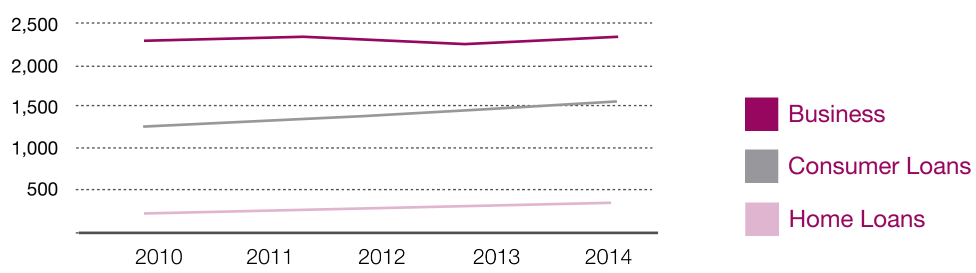
2.4.8 Concentration Risk and Sectorial Overview

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. The Board and senior management are regularly informed on the concentration of the Bank's portfolio through reports prepared at least on a quarterly basis. 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 uses a number of metrics, including the Herfindahl-Hirschman Index (HHI), an internationally accepted indicator of concentration.

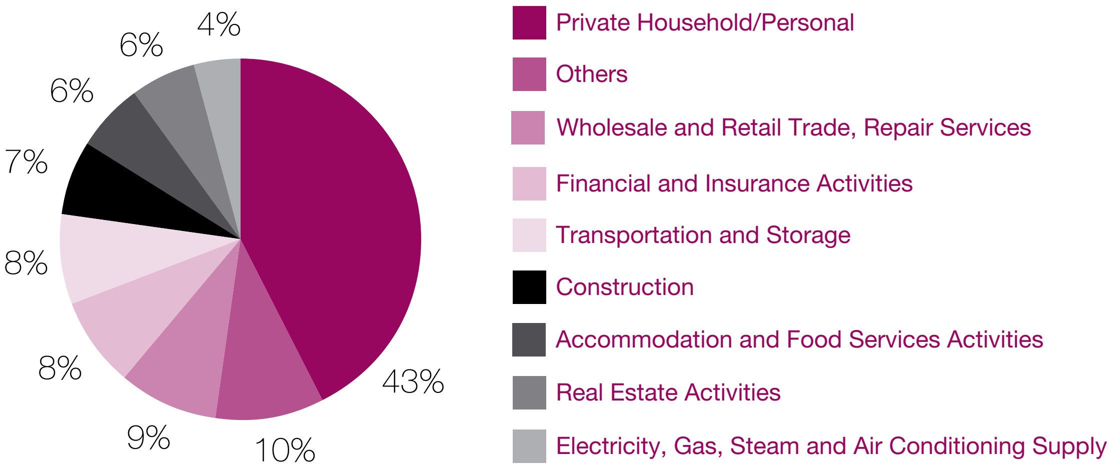
Single name exposures exceeding 10% of Group's own funds are reported individually to the Board of Directors and are monitored on a continuous basis. These exposures are also reported to the Regulatory Authority. The aggregate of the single name exposures exceeding 10% of Own Funds corresponds to 2.1 times the Group's capital base calculated in accordance with CRD IV.

Concentration by Business Segment
€ millions



Capital & risk management report 30 September 2014 (continued)

Sectorial Concentration - Advances
(% of total)



2.4.9 Home Loans

The Bank exercises strict monitoring on the home loans segment, being the largest sector within the credit portfolio, accounting for 37.1% 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 caps on loan-to-value and repayment-to-income ratios. The Loan-to-Value (LTV) ratio, which is one of the most important indicators of default compares well with international benchmarks, with the Bank's average LTV on newly sanctioned loans standing at 74%. The home loans segment is healthy with only 3.50% classified in the doubtful category.

2.4.10 Scenario Testing

Stress testing and scenario analysis are an integral part of the Bank's credit risk management framework, and are applied extensively in credit management. These tests measure the resilience of the Bank's Capital Adequacy Ratio (CAR) in the event of an extreme but plausible shock.

A number of tests are carried out periodically, assuming, amongst others, the following scenarios:

- a general decline in asset quality, i.e. an increase in non-performing loans
- a default event by one of the Bank's large exposures
- a general deterioration in a significant economic sector

These tests are enhanced from time to time towards more forward-looking scenario stress tests taking into account combinations of different events related to credit risk matters. The results of the tests carried out confirm that the credit portfolio's overall quality is robust, and the effect in terms of capital allocation would not be highly material.

Credit Risk Stress Test [1]	Baseline	Negative
Bank CAR as at end September 2014 is 14.3%	**Change in CAR**	**Change in CAR**
1. Increase in doubtful loans [2]	-0.43%	-1.07%
2. Increase in doubtful of Construction and Real Estate [2]	-0.16%	-0.39%

[1] The stress tests do not represent a forecast of future events

[2] In both scenarios 1 and 2 the baseline entails an increase in doubtful of 10% while the negative represents a rise of 25%

2.5 Risk Adjusted Return

The Bank has developed a credit risk loss model with the primary objective of determining the expected loss of the portfolio. As a result the Bank has clear visibility both of cost of risk and of the true risk adjusted return of its credit portfolio.

2.6 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 through CRMU's database, 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 in the junior and more senior levels, as part of this objective.

Capital & risk management report 30 September 2014 (continued)

2.7 Settlement Risk

Settlement risk arises in any situation where a payment is made in expectation of a corresponding receipt. 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.

2.8 Credit Risk in the Investment Portfolio

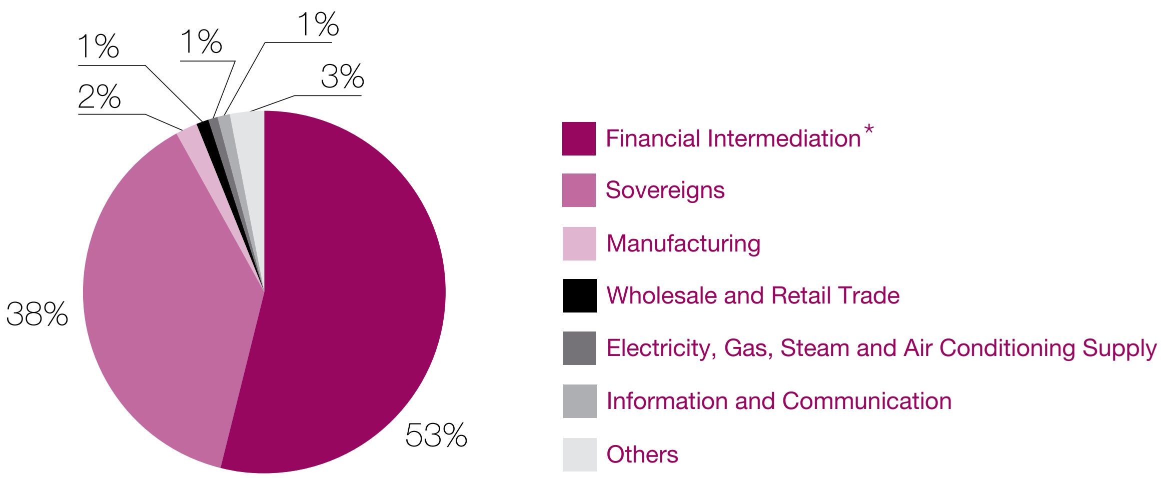
The Bank is exposed to credit risk through its investment activities. These investments include deposits with banks, debt securities, equities, and derivative financial instruments but exclude any working balances such as balances with the Central Bank, current and call accounts. The investment portfolio is managed by the Financial Markets and Investment function (FM&I) and it is the Bank's strategy to hold these instruments till maturity rather than as a trading portfolio.

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, with changes in credit ratings and future outlook monitored daily. Besides MRMU monitors closely the Credit Default Swap (CDS) movements of those counterparties having the largest exposures in the investment portfolio, since an 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 97.58% being of an investment grade (September 2013: 96.04%).

Sectorial Concentration - Investment



* The exposure in financial intermediation includes deposits held with foreign banks with maturities up to three months.

2.8.1 Concentration 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.

Capital & risk management report 30 September 2014 (continued)

2.9 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 following table depicts the derivatives with positive fair values and which are subject to enforceable netting arrangements:

	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities set off in the statement of financial position	Net amounts of financial assets presented in the statement of financial position	Related amounts not set off in the statement of financial position: Financial Instruments	Related amounts not set off in the statement of financial position: Financial collateral received	Net amount
Assets	€ 000	€ 000	€ 000	€ 000	€ 000	€ 000
Derivative financial instruments	18,169	-	18,169	18,169	-	-

The offsetting financial assets and financial liabilities are included in Note 39.8 to the Financial Statements.

The Treasury Management Policy (TMP) limits the use of derivatives to (a) hedge a balance sheet position (b) satisfy customers' requests and (c) 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 dominated in the local currency or in hard foreign currencies.

Wrong way risk arises when the risk factors driving exposure to counterparty are positively correlated with the creditworthiness of that 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. Requests for higher limits are submitted to the Credit Committee or Board of Directors as appropriate. 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 exposures 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. The current replacement cost of contracts with positive values is represented by the current market value to the contract. In order to determine the potential future credit exposure the institution multiplies the notional amounts to pre-defined percentages according to residual maturities.

Section 3: Market Risk

3.1 The Nature of Market Risk

Market risk is the risk that the Bank's earnings or capital will be adversely affected by changes in the level or 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 FM&I. The Bank's strategy is to manage these instruments as an investment portfolio rather than as a trading portfolio. Most of the Bank's trading activity is undertaken to meet the requirements of its customers for foreign exchange and interest rate products.

3.2 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 set 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.

Capital & risk management report 30 September 2014 (continued)

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. MRMU regularly monitors the levels of exposures compared to set limits and where appropriate, escalation procedures are in place.

Excesses are reported monthly to executive management. A detailed report is presented on a regular basis to the Risk Management Committee.

3.3 The Mitigation of Market Risk

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

3.3.1 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 MRMU in co-ordination with FM&I, and is approved by ALCO and the Board of Directors.

3.3.2 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.

3.3.3 Investment Authorisation

FM&I executives are allocated limits according to the TMP. Exposures above the TMP levels require approval by the Credit Committee or by the Board. A 'four-eye' approach is applied when an investment proposal falls outside the criteria set out in the Bank's TMP. MRMU undertakes an independent analysis of proposals which are then submitted to the Credit Committee or the Board for their consideration.

3.3.4 Review of Limits

All credit exposures are regularly reviewed upon changes in credit ratings or outlook with a view to taking early mitigating action. Limits approved by Credit Committee and Board of Directors are reviewed annually in order to reassess the credit risk and align the investment criteria as necessary.

3.4 Interest Rate Risk in the Banking Book

Interest rate risk in the banking book is defined as the exposure of non-trading products to interest rates. It predominantly arises from the mismatch between interest rate-sensitive assets and interest rate-sensitive liabilities.

ALCO assesses interest rate risk with the objective of limiting potential adverse effects of interest rate movements on net interest income and on equity. The committee also monitors interest rate gaps and carries out sensitivity analysis tests based on the potential loss arising from an upward parallel shift of the yield curve with capital being allocated against such potential loss.

3.4.1 Modified Duration

The modified duration is a measure of the price sensitivity to yields. By calculating the Modified Duration, the Bank estimates the changes in the market values of securities in the treasury portfolio and of the interest rate swaps entered into to hedge the interest rate risk, in response to a parallel shift in yields of 100 basis points under the baseline scenario. In the case of the negative scenario, the Bank estimates a 200 basis point increase in yields. 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.

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, where most of the times these were negatively correlated. 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.

Capital & risk management report 30 September 2014 (continued)

Modified Duration Tier 1 as at end September 2014 is 11.7%	Baseline Change in Tier 1	Negative Change in Tier 1
Parallel shift in yields on the investment portfolio	-1.20%	-2.40%

3.4.2 Impact of Interest Rate Risk on Economic Value

The economic value of an instrument represents an assessment of the present value of its expected future cash flows, discounted to reflect market rates. Variations in interest rates affect the underlying value of the bank's assets, liabilities and off-balance sheet instruments. Sensitivity analysis on the Bank's balance sheet is carried out to calculate the estimated impact of an immediate 200 basis points increase in yields on the economic value. Impacts have only been shown in one direction but can be assumed to be reasonably symmetrical. At end September 2014 the impact on economic value was estimated at 0.66% of the Group's regulatory capital base (September 2013: 1.89%).

	30 September 2014	30 September 2013
	€ 000	€ 000
Impact on Capital	3,796	11,180

3.4.3 Impact of Interest Rate Risk on Interest Margin

Changes in interest rate risk also affect the Bank's earnings by changing the net interest margin. Interest rate risk arises from the different repricing characteristics of the Bank's interest-sensitive assets and liabilities and from the mismatch between interest rate-sensitive assets and liabilities. Matching assets and liabilities are offset against each other and internal interest rate swaps are also used to close repricing gaps. The table below shows the sensitivity of net interest margin to parallel increases/decreases of 100 basis points, with a time horizon of one year.

Net effect on Interest Income for 12 months including off-balance sheet exposures

	30 September 2014 € 000	30 September 2013 € 000
Total	**10,960**	**8,638**
EUR	8,670	8,767
GBP	(353)	(656)
USD	1,105	(649)
AUD	1,027	791
CAD	(9)	(89)
JPY	75	127
Other	446	348

3.5 Currency Risk

The Group takes on exposure to the effects of fluctuations 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. The Group exposure to this risk is insignificant.

3.6 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. The Group exposure to this risk is also insignificant.

Capital & risk management report 30 September 2014 (continued)

3.7 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 of 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 (1983-2013). A further one notch downgrade is applied under the negative 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 Capital Adequacy Ratio, are reported to the Risk Management Committee on a regular basis. The results show a very strong investment portfolio that is able to withstand extreme shocks.

Market Risk Stress Test Tier 1 as at end September 2014 is 11.7%	Baseline Change in Tier 1	Negative Change in Tier 1
Parallel shift in credit spread on the investment portfolio[1]	-1.56%	-3.11%
Expected default on the investment portfolio[2]	-0.55%	-0.57%

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

[2] The Moody's default tables for Sovereigns and Corporates (1983 - 2013) under the baseline and a further one notch downgrade in the case of the negative scenario.

Section 4: Operational and Reputational Risks

4.1 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 Group's objective is to contain operational risks within levels deemed acceptable by the Board of Directors and in line with the Group's Risk Appetite Statement. 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.

4.2 The Management of Operational Risk

The Group's 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 lie at 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 in 2008. The ORMF recommends various initiatives including:

Risk Identification - The Operational Risk unit supports the business units in identifying and assessing the operational risk exposure. Risk assessments involve process mapping and risk identification, risk evaluation and recommendations for managing and mitigating the risks. In the past year risk assessments have been carried out on a number of high risk areas and ad hoc as part of the New Product Approval Process.

Loss Database - A loss database has been created and maintained since 2009 and is updated regularly through risk event reporting on internal loss events or near misses.

Key Risk Indicators - KRIs and thresholds have been identified at generic enterprise-wide level and are reported quarterly as a non-financial risk dashboard to the Executive Committee and the Risk Management Committee.

Business Continuity Management - Business Continuity supporting documentation at unit level is in place throughout the organisation. A Business Continuity Management programme is maintained and the Group is implementing a robust enterprise-wide Business Continuity Plan (BCP). BCPs for critical activities are regularly exercised and IT systems tested, thus ensuring timely response to disruptions and effective restoration. The Group's Incident Management Team works in liaison with the Operational Risk unit to effectively manage the organisation's efforts where widespread threats require a more co-ordinated approach.

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

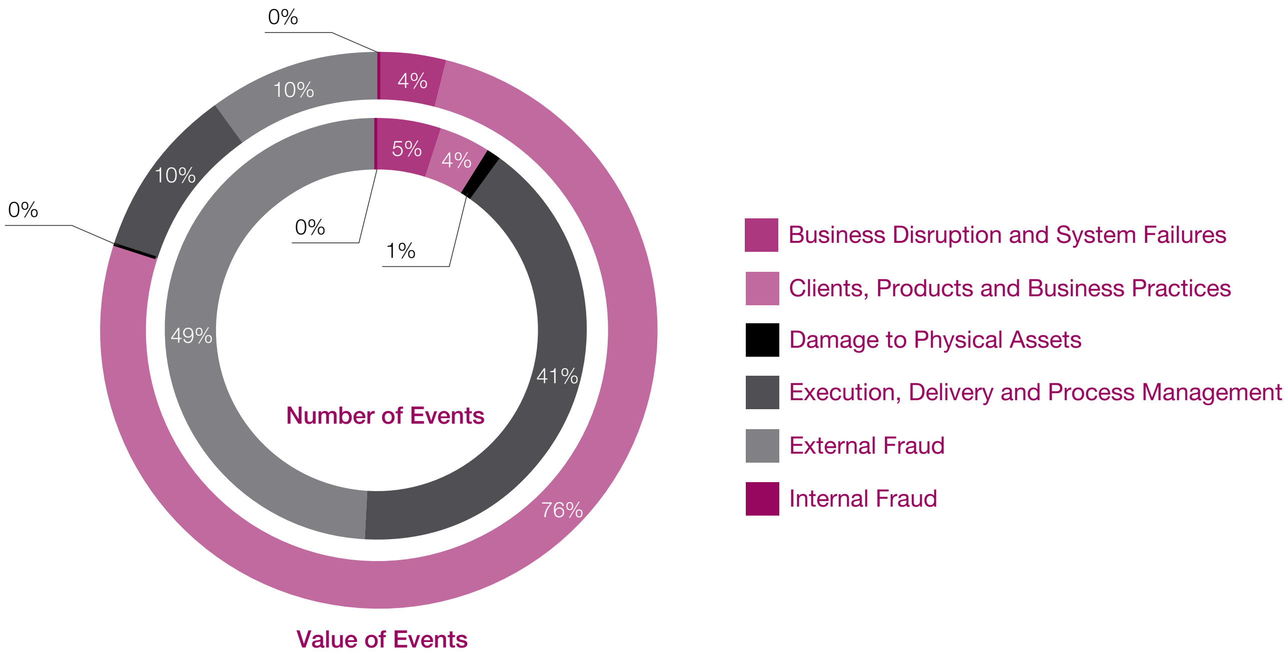
A total of 917 operational risk loss events[1] amounted to actual financial impact of €3.6 million in the past year. This represents an average loss of €3,978 per loss event. The value of cumulative operational losses during this year has improved when compared to the previous year (Sep 2013 €5.8 million). At 1.71% the Group's ratio of operational risk losses to gross income compares well to the benchmark figure of 2.69%[2].

[1] There is no minimum threshold for recording loss events.

[2] ORX Association figures for 60 member banks - average of figures reported between 2008 - 2013 (http://www.orx.org/Pages/orxdata.aspx)

Capital & risk management report 30 September 2014 (continued)

Value and Number of Events by Risk Event Type



The operational risk regulatory requirement for the Group as at September 2014 is €31.8 million (Notional Risk Weighted Assets €397.1 million) which adequately covers both expected and unexpected losses.

4.3 Mitigation of Operational Risk

BOV Group 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 the BOV Group 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 Operational Risk Unit, who work in close liaison with the Group's Insurance Brokers.

4.4 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/IEC 27001/2. The Group has also formulated a Data Protection policy and guidelines document, to ensure compliance to the Data Protection Act and protect the personal information held and processed by the Group.

4.5 Reputational Risk

Reputational risk refers to the risk that a bank may be exposed to negative publicity about its business practices or internal controls, which could have an impact on the liquidity or capital of the firm, or cause a change in its credit rating. BOV's policy is to avoid those transactions and operations that may potentially create an unacceptable level of reputation risk.

BOV adopts the Code of Principles of Good Corporate Governance that show the Group's commitment to high standards of personal ethics and the values of trust, integrity and honesty with its customers, suppliers, employees and shareholders. This commitment ensures that the Group's reputation and that of its customers and employees is continuously safeguarded. In addition, BOV adopts a structured Corporate Social Responsibility Programme which guides the Group's efforts to conduct its operations in an environmentally friendly manner, whilst being socially responsible and contributing to the general well-being of the community in which it operates.

Capital & risk management report 30 September 2014 (continued)

4.6 Conduct Risk

Conduct risk refers to the possibility that the organisation's or individual's actions result in poor outcomes for customers. The BOV Group recognises the relationship between Operational Risk and Conduct Risk since such risks are related to failure to meet obligations towards clients.

The Group's approach is to manage this risk as part of Operational risk and classifies related risk event types within the Clients, Products and Business practices event category.

Governance of Conduct risk falls within the responsibility of the Risk Management Committee in line with other operational risks. The formal risk appetite includes statements aligned with Conduct Risk good practices, emphasising that the Group considers that it cannot survive unless employees:

- Uphold the brand promise (supportiveness, mutuality, long term, straightforward and efficient, added value) when dealing with customers;
- Avoid taking risks that may have an adverse effect on the quality of customer service provided;
- Foster an ethos of ethical conduct, corporate social responsibility and personal integrity.

Identification, assessment and monitoring of these risks takes place as part of the Operational Risk Management Framework implementation particularly at the New Product Approval Process.

Furthermore as from October 2013 BOV launched a strategic initiative Focusing Actions on Customer Experience (FACE) which aims to focus all the organisation's actions on delivering a superior customer experience.

4.7 Remuneration Policy

The Group's Remuneration Policy was approved by the Remuneration Committee and by the Board of Directors during financial year 2012. The Policy 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 Policy deals with the remuneration of all staff members including Executive Management, in accordance with Banking Rule BR/12 and international 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 2014.

The target population defined as Identified Staff for the purposes of this Report represents 3.42% of total number of employees in the Group. Identified staff was determined in line with recommended EBA Regulatory Technical Standard[3] and includes:

- senior executives responsible for business units/business lines or internal Risk, control, compliance and audit;
- executive heads 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.

Other roles that qualified under the Group Remuneration Policy as Responsible Persons, Material Risk Takers or Risk Management and Control staff, but did not qualify as Identified Staff in terms of Article 4.2 (a) and (b) of the EBA Regulatory Technical Standards, have been omitted.

For the purposes of remuneration, Identified Staff have been aggregated and split into business areas according to EBA guidelines[4]. The table below therefore includes total fixed and variable remuneration and number of beneficiaries per and within each business area.

[3] EBA Final Draft Regulatory Technical Standards EBA/RTS/2013/11 dated 16 December 2013.

[4] EBA Guidelines on the remuneration benchmarking exercise EBA/GL/2014/08 dated 16 July 2014.

Capital & risk management report 30 September 2014 (continued)

Remuneration of Identified Staff

	Supervisory Function ^	Management Function ^	Investment Banking ^
Management Body	11	12	-
Number of identified staff	-	-	2
Total fixed remuneration (in €)	€ 266,084*	€ 1,069,538	€ 117,774
Total variable remuneration (in €)	Nil	€ 52,864	€ 4,000

* excludes Health Insurance Benefits

	Retail Banking ^	Asset Management ^	Corporate Functions ^	Independent Control Functions ^
Number of identified staff	16	6	10	10
Total fixed remuneration (in €)	€ 900,194	€ 326,561	€ 562,197	€ 466,074
Total variable remuneration (in €)	€ 25,630	€ 14,241	€ 16,600	€ 15,472

^ as defined in EBA guidelines EBA/GL/2014/08

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 pot attributed to the staff in the Clerical to Senior Management grade is determined in the Collective Agreement and is based on the profit achieved by the Bank. The Bonus Pot is then divided amongst these employees in proportion to the performance achieved by every individual and in accordance with their respective salary grades.

Employees in the Head and in the Executive Head 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 Chief Officers as highlighted under the Remuneration Report.

Performance Management System

Key Performance Indicators (KPIs), by which employee's performance is measured, are reviewed on an annual basis to ensure that these continue to take into account key risks and strategic objectives of the Group. Quality and compliance measures continued to receive strong weighting when setting KPIs. The key risks addressed by these measures relate mainly to the area of investment sales, particularly focusing on clients, products and business practices risk event types to mitigate risks identified in previous financial years.

Defined KPIs take into account the Group's long term interests and values, to avoid rewarding individuals for taking risks in excess of stated risk appetite. Financial and non-financial performance indicators are based on a balanced scorecard approach. Financial targets are balanced by process, customer satisfaction and employee measures to facilitate a balanced view of performance.

Variable remuneration is made as cash payment to all levels of employees including executive management. In accordance with the Remuneration Policy, the variable portion of the employees' remuneration cannot exceed 20% of the fixed remuneration. Where the variable component (comprising performance-based remuneration and sales incentives) is less than 10% of the fixed component, the full amount is paid within a year from the evaluation of performance. Where the variable component is equal to or greater than 10% of the fixed component, payments will be staggered over a three year period.

Section 5: Liquidity Risk

5.1 The Nature of Liquidity Risk

Liquidity risk is the risk that an entity will encounter difficulty to efficiently meet expected and unexpected current and future cash flow and collateral needs without affecting either daily operations or the general financial condition of the entity. It arises if the bank's pool of liquid or marketable assets available is insufficient to fulfil its current or future obligations. Liquidity risk roots from the inability to trade quickly enough an investment at a price close to its fair value, to prevent or minimize a loss.

Capital & risk management report 30 September 2014 (continued)

5.2 The Management of Liquidity Risk

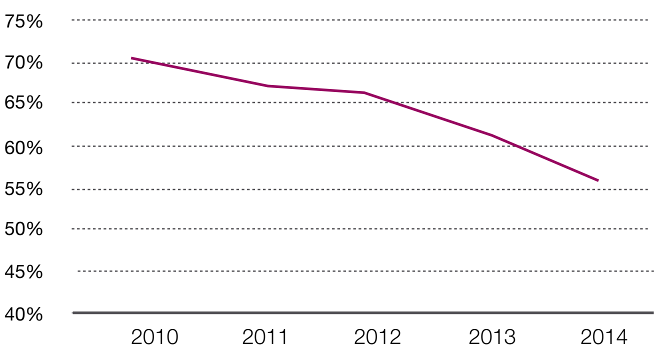
The fundamental role of banks in the transformation of short-term deposits into long-term loans makes banks inherently vulnerable to idiosyncratic and systemic liquidity risk, of both institution-specific and a market nature. On a daily basis, the Group is exposed to address its available cash resources from overnight deposits, current and call deposits, maturing term deposits, loan drawdowns, guarantees and margin and other calls on cash-settled derivatives.

The management of liquidity risk within the Group is the responsibility of the ALCO committee. Effective liquidity risk management helps ensure that the Bank is in a position to fund increases in assets and to meet obligations as they become due, without incurring substantial losses.

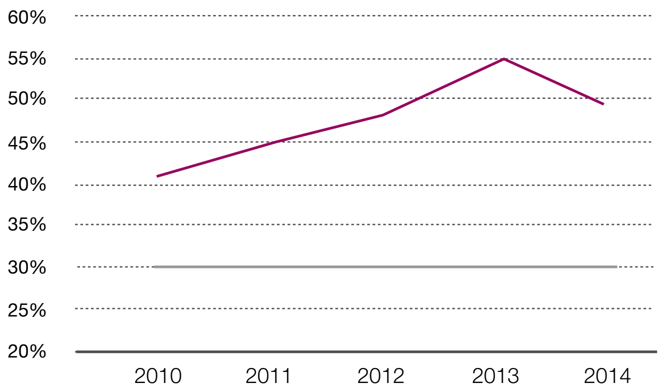
The Bank's conservative approach and its extensive reliance on retail funding ensure that it remains highly liquid and in a position to meet future unexpected stressed conditions. At end September 2014 the loan-to-deposit ratio stood at 56.75% showing that the Group kept it's highly liquid position, with its loan portfolio fully funded by deposits and with no significant dependence on the wholesale market. The Bank maintains a stable base of "core deposits", mainly made up of deposits from the household and SME sectors. The regulatory liquidity ratio, which expresses liquid assets as a proportion of liabilities maturing within three months, stood at 48.6%, well above the statutory minimum of 30%.

The Bank continued its preparation towards the introduction of the new liquidity regulations introduced by the Basel Committee on Banking Supervisions (BCBS) in December 2010, through the "International framework for the liquidity risk measurement, standards, and monitoring" and now embedded in European law, by way of the CRD IV package. The introduction of the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR) is subject to an observation period, during which banks are being subject to various Quantitative Impact Studies (QIS). The Bank has actively participated in all of these studies carried out by the EBA and the local regulator. The LCR will be enforced on 1st January 2015, following a minimum requirement fixed at 60%. The minimum requirement will rise in equal annual increments to 100% on 1 January 2019. BOV has exceeded all levels of liquidity required by regulatory ratios.

Loan to Deposit Ratio



Regulatory Liquidity Ratio



5.3 The Mitigation of Liquidity Risk

The Group mitigates liquidity risk by maintaining a sufficient fund of liquid assets. This is made up of cash, substantial balances with other banks and a pool of financial assets which are eligible as collateral against borrowing from the European Central Bank (ECB) or on the repo markets. ALCO also ensures that there is a wide diversification of funding sources, across various maturity bands.

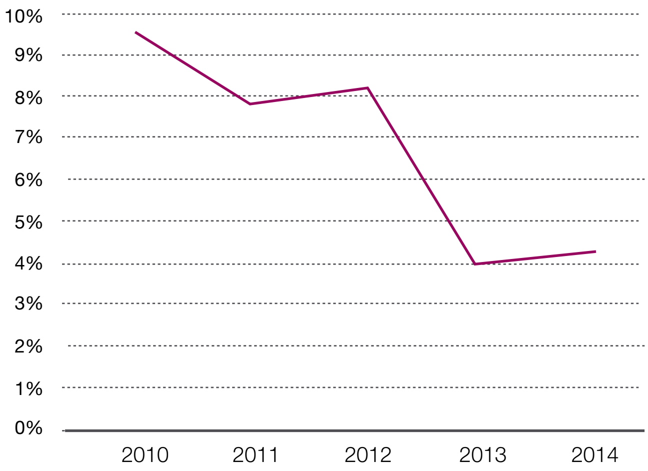
In order to ensure that maturing funds are always available to meet expected demand for cash, the Board sets parameters within which maturities of assets and liabilities may be mismatched. Unmatched positions potentially enhance profitability, but also increase the risk of losses. ALCO monitors the group's liquidity gap analysis on a monthly basis. The mitigation of liquidity risk is also addressed through adequate measures in the Bank's risk appetite framework.

In addition, ALCO maintains an on-going oversight of forecast and actual cash flows, by monitoring the availability of funds to meet commitments associated with financial instruments. The Bank has been successful in its drive to build and maintain a large and stable customer deposit base. This has helped the Bank to eliminate any reliance on wholesale bank funding.

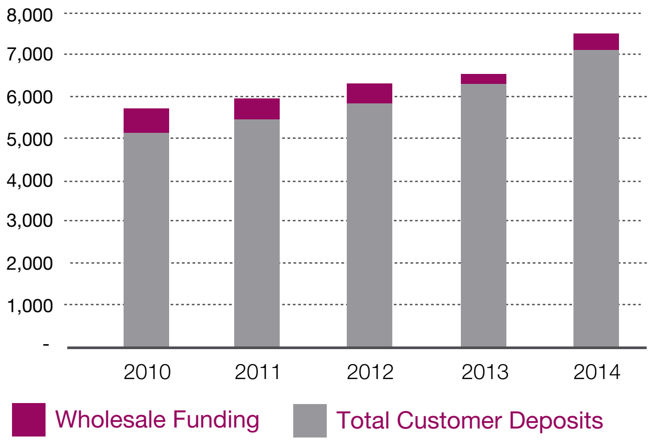
The ALCO committee is updated regularly with scenario and stress tests related to liquidity. These techniques help the bank to evaluate the resilience of its liquidity buffers, and to maintain a constant state of readiness should an exceptionally high demand for liquidity arise at any time.

Capital & risk management report 30 September 2014 (continued)

Wholesale Funding Dependency



Funding Source
€ millions



Section 6: Life Assurance Risk

6.1 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 p.l.c. and Middle Sea Insurance plc.

Life assurance risk is the volatility in the amount and timing of claims caused by unexpected changes in mortality, longevity and morbidity. 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. Longevity risk is the risk of such deviations due to increasing life expectancy trends among policy holders and, resulting in pay-out ratios higher than what was originally accounted for. Morbidity risk is the risk of deviations in timing and amount of cash flows (such as claims) due to the incidence or non-incidence of disability and sickness.

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 the estimate established using statistical techniques.

6.2 The Mitigation of Life Assurance Risk

6.2.1 Risk Governance

MSV has in place a dedicated Risk and Compliance unit, and a Risk and Compliance Board Committee, to assist the Board in the oversight of risk and compliance management, and to oversee the implementation at the company of the Solvency II regulatory regime, which is currently scheduled to come into force in 2016. Forecasts and results of QIS show that the company is expected to achieve compliance with the capital requirements of Solvency II without difficulty.

6.2.2 Underwriting Strategy

Experience shows that 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. The Group has developed its insurance underwriting strategy to diversify the type of insurance risk accepted and within each of these categories to achieve a sufficiently large population to reduce the variability of the expected outcome. Medical selection is also included in the Group's underwriting procedures with premiums varied to reflect the health condition and life expectancy of applicants.

6.2.3 Reinsurance

The Group uses reinsurance to cover all death claims above a pre-defined level. The type of reinsurance cover and the level of retention for each risk are based on the Group'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, excess of loss and catastrophe protection, which limits the liability of the Group to any one individual life or event.

Capital & risk management report 30 September 2014 (continued)

Section 7: 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 is a joint venture, 60% owned by Bank of Valletta p.l.c. and 40% by Insight Investment Management (Global) Limited, one of UK`s largest Asset Managers and a subsidiary of Bank of New York Mellon.

VFM is licensed by the Malta Financial Services Authority to provide investment services and to operate as a 'Maltese Fund Management Company' pursuant to the Undertaking for Collective Investment in Transferable Securities Regulations (UCITS). Risk management is a core part of the company's culture and operations. The Company operates three lines of defence - a robust governance model which includes key control principles and various policies and procedures, risk and compliance functions and internal oversight and group audit reviews. VFM carries out ongoing oversight of its delegated and outsourced functions.

VFM also has a Risk and Regulatory Committee which 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 p.l.c. 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 Corporate Services Division aimed at reviewing the processes and the corresponding control procedures in place. 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.

Section 8: Capital Management

8.1 Capital Management and Forecasting

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. Hence, the prudent and efficient management of capital will always be one of the Group's top priorities, and a fundamental objective of risk management.

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 Group risk management process, capital buffers are continuously monitored by the Board of Directors, by ALCO and by senior management. ALM ensures that the Group is adequately capitalised in order to achieve the strategic objectives set by the Board of Directors while assisting senior management in setting the capital management plan. The main aim of this exercise is to assess the level and quality of the capital buffer for a rolling three year period.

The Group is also expected to retain a comfortable buffer of surplus capital over the forecast period, thus ensuring potential for balance sheet growth and a healthy buffer that can be used during periods of heightened risk levels.

8.2 Capital Resources and Capital Adequacy

In line with new regulations the Group is placing much of its emphasis and monitoring on Core Equity Tier 1 capital. The Group continued to use the Standardised Approach for credit risk and the Basic Indicator Approach for operational risk in order to calculate Pillar 1 minimum capital requirements. No capital is allocated for market risk as the Group does not operate a trading book. For credit risk, risk weights for the Treasury Portfolio are determined according to credit ratings provided by eligible External Credit Assessment Institutions (ECAIs) – Fitch, Moody's and S&P. Regulatory risk weights are used for unrated exposures and the credit 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. 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) with line with the CRD IV 575/2013.

Capital & risk management report 30 September 2014 (continued)

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 Instruments Main Features	BOV Ordinary Shares	5.35% BOV Subordinated Bonds 2019	4.8% BOV Subordinated Bonds 2020
Unique identifier	MT0000020116	MT0000021262	MT0000021270
Governing Law(s) of the instrument	Maltese Law	Maltese Law	Maltese Law
Regulatory Treatment			
Transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2
Post-transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2
Eligible at solo/(sub)consolidated / solo & (sub)consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub)consolidated
Amount recognised in regulatory capital	330,000,000	47,095,890	70,000,000
Nominal amount of instrument	330,000,000	50,000,000	70,000,000
Issue Price	N/A	At par (€100 per bond)	At par (€100 per bond)
Redemption Price	N/A	At €100	At €100
Accounting classification	Share Equity	Liability - amortised cost	Liability - amortised cost
Original date of issuance	26 August 1992	8 June 2009	15 March 2010
Perpetual or dated	N/A	Dated	Dated
Original maturity date	N/A	15 June 2019	15 March 2020
Issuer call subject to prior supervisory approval	No	No	No
Coupons/dividends			
Fixed or floating dividend coupon	Floating	Fixed	Fixed
Coupon rate and any related index	N/A	5.35%	4.80%
Existence of dividend stopper	No	No	No
Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary	Mandatory	Mandatory
Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Mandatory	Mandatory
Existence of step up or other incentive to redeem	N/A	No	No
Noncumulative or cumulative	Non cumulative	Non cumulative	Non cumulative
Convertible or non-convertible	Non convertible	Non convertible	Non convertible
Write-down features	No	No	No
Position in subordinatiion heirarchy in liquidition	Subordinated to BOV subordinated bonds	Subordinated to senior creditors and depositors	Subordinated to senior creditors and depositors
Non-compliant transitional features	No	No	No

The subordinated loan capital in Tier 2 capital represents the subordinated unsecured bonds as disclosed in Note 30 of the Financial Statements. They 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. As the 4.8% Euro subordinated bonds have a remaining maturity over 5 years and have all been fully paid up, the full value of these securities was included. The 5.35% Euro subordinated bonds are redeemable at par on 15 June 2019 and thus the amortised amount was included in the Own Funds figure.

In July 2013 the EBA issued the 'FINAL draft Implementing Technical Standard on Disclosure for Own Funds by institutions under Articles 437 (2) and 492(5) of Regulation (EU) 575/2013 (CRR)'. In order to increase transparency regarding the regulatory capital of European institutions the regulation provided a set of templates which will help to facilitate cross-jurisdictional comparisons. During the period from 1 January to 31 December 2017, which covers the phasing in of the regulatory adjustments, institutions are required to complete the transitional disclosure template.

Capital & risk management report 30 September 2014 (continued)

	€ '000 September
CET1 capital	**464,032**
Common Equity Tier 1 capital: instruments and reserves	**523,107**
Capital instruments and the related share premium accounts	330,988
Retained earnings	158,914
Accumulated other comprehensive income (and other reserves, to include unrealised gains and losses under the applicable accounting standards)	29,024
Funds for general banking risk	3,081
Minority interests	1,101
Common Equity Tier 1 (CET1) capital : regulatory adjustments	**-59,076**
Intangible assets (net of related tax liability) (negative amount)	-11,642
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)	-22,620
Direct and indirect holdings by an institution of CET1 instruments of financial sector entities where the institution has a significant investment in those entitites	0
Amount exceeding the 17.65% threshold (negative amount)	-13,144
Of which: direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities	-6,572
Of which : deferred tax assets arising from temporary differences	-6,572
Regulatory adjustments relating to unrealised gains and losses	-31,245
Amount to be deducted from or added to CET1 capital with regard to additional filters and deductions required pre CRR	19,576
TIER 2 Capital	**111,503**
Capital instruments and the related share premium accounts	117,096
Regulatory adjustments applied to Tier 2 in respect of amounts subject to pre-CRR treatment and transitional treatments subject to phase out	-5,593
TOTAL CAPITAL	**575,535**
Deferred tax assets not deducted from CET1 capital	41,150
Direct holdings by the institution of the CET1 instruments of financial sector entities not included in CET1 capital	41,150
TOTAL Risk Weighted Assets	**3,975,622**
Capital Ratios	
Tier 1 capital	**11.7%**
Total capital	**14.5%**

Refer to Annex 1 for full reconciliation of own funds items to audited financial statements.

8.3 Internal Capital Adequacy Assessment Process (ICAAP)

Under Pillar II of the CRD, the Group is required to enact an Internal Capital Adequacy Assessment Process (ICAAP). The aim of ICAAP is to ensure a better alignment between material risks and regulatory capital, in order to enhance both capital deployment and the risk management and mitigation techniques adopted by the Group. ICAAP is presented to the supervisory authority, which will subject it to a Supervisory Review and Evaluation Process (SREP). BOV has this year prepared the sixth ICAAP capital document, which, was approved by the Board on May 2014 and presented to the MFSA.

The ICAAP is performed annually and is regulated by Banking Rule BR/12/2012. BOV's ICAAP is based upon a 'Pillar 1 Plus' approach whereby the Pillar 1 capital requirements for credit and operational risks are supplemented by the capital allocation for other material risks not fully addressed within Pillar 1. The risks considered for ICAAP include concentration, liquidity, operational, reputational and strategic risks, interest rate risk in the banking book, and risks arising from the macroeconomic environment. The Group uses internal models to quantify the exposure to these risks and assess the need for additional Pillar 2 capital. In accordance with these models the Group allocated additional capital under Pillar 2 for concentration risk in the advances and treasury portfolios, interest rate risk in the banking book and for risks arising from the macroeconomic environment as estimated by the internal stress testing model.

The Board and senior management assumed overall responsibility for the conceptual design and technical details of the ICAAP capital document. The Board discussed, approved, endorsed and delivered the yearly ICAAP submission to the regulatory authorities.

The results of this year's ICAAP show that the Group maintains a comfortable level of excess capital and substantial liquidity that ensures the flexibility and resources needed to achieve the long term strategic objectives of the Group, even in situations of stress.

Corporate governance statement of compliance

A. INTRODUCTION

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

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

Good corporate governance is the responsibility of the Board, and in this regard the Board has carried out a review of the Bank's compliance with the Code during the period under review. 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, 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 Executive Committee, the Asset and Liability Committee, the Audit Committee, the Credit Committee, the Risk Management Committee, the Compliance Committee and the Remuneration and 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 Executive Committee, the current composition of which is set out below, and whose main role and responsibilities are to execute agreed strategy and manage the business.

As announced in Company Announcement number 257 dated 24 October 2014, the Board of Directors has recently approved changes to the Bank's Senior Management organizational structure. The revised structure aims to ensure a more focused corporate governance structure as well as efficiency in dealing with the various major challenges that the Bank faces in the coming decade.

The structure involves the creation of the role of the Chief Operating Officer who will report directly to the Chief Executive Officer and the regrouping of the current responsibilities and functions of the Chief Officers under three roles, namely the Chief Risk Officer, the Chief Financial Officer and the Chief Business Development Officer. The Chief Risk Officer will report directly to the Board's Risk Management Committee.

Corporate governance statement of compliance (continued)

The Chief Executive Officer, the Chief Operating Officer, the Chief Risk Officer, the Chief Finance Officer and the Chief Business Development Officer will constitute the Bank's Management Board.

It is envisaged that the new Senior Management organisational structure will be fully in force during FY 2015.

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.

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, however, attends the Board meetings by invitation, albeit without a vote, in order to ensure his full understanding and appreciation of the Board's policy and strategy. This enables the Chief Executive Officer to provide direct input to the Board's deliberations. In addition, members of the Executive Committee report to the Board on a monthly or quarterly basis.

The composition of the Board is determined by the Bank's Articles of Association where the appointment of Directors to the Board is reserved exclusively to the Bank's shareholders, except in so far as an appointment may be made to fill a casual vacancy on the Board. Prior to being appointed as Directors, nominees undergo a due diligence process by the Malta Financial Services Authority, to establish that they are fit and proper persons pursuant to the Banking Act (Cap.371 of the Laws of Malta) and the Investment Services Act (Cap.370 of the Laws of Malta).

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). 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.

While current thinking and practices internationally suggest that the notion of independence has been tainted in respect of one Director because of his length of service on the Board, the Board is of the opinion that this has not undermined the said Director's ability to consider appropriately the issues which are brought before the Board. On the other hand, the Board believes that by definition, employment with the Bank renders a Director non-independent from the institution. This should not however, in any manner, detract from the non-independent Director's ability to maintain independence of analysis, decision and action.

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

The Board meets twice a month unless further meetings are required.

The Board regularly reviews and evaluates corporate strategy, major operational and financial plans, risk policies, performance objectives and business alternatives. 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.

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: 35 Members Attended**	
John Cassar White	35	
Joseph Borg	31	
Roberto Cassata	8	
Ann Fenech *(resigned on 19 December 2013)*	5	(out of 7)
Mario Grima *(appointed on 19 December 2013)*	28	(out of 28)
George Portanier *(resigned on 19 December 2013)*	7	(out of 7)
Taddeo Scerri	32	
Paul Testaferrata Moroni Viani *	17	(out of 21)
George Wells	32	
Franco Xuereb	33	
Joseph M Zrinzo *(appointed on 19 December 2013)*	28	(out of 28)

** Pursuant to the agreed policy, Paul Testaferrata Moroni Viani does not attend Board meetings during which credit proposals are discussed.*

Corporate governance statement of compliance (continued)

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. It 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 Committee is also responsible for managing the Board's relationships with internal and external auditors.

In terms of Listing Rules 5.117 and 5.118, Taddeo Scerri FCCA, FIA, CPA and George Wells FCMA, FIA, CPA are the Directors whom the Board considers as competent in accounting. Taddeo Scerri and George Wells are considered independent because 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.

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

Members	Meetings Held: 13 Members Attended	
Taddeo Scerri (Chairman)	13	
George Wells	13	
Joseph M Zrinzo	10	(out of 10)

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

The Chief Executive Officer attends the Remuneration and Nominations Committee meetings by invitation. The Company Secretary acts as Secretary to the Remuneration and 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 Officer Risk Management, the Chief Officer Finance, the Chief Officer Legal and Compliance, the Chief Officer IT, the Chief Economist, the Executive Head Group Internal Audit and the Executive Head Compliance 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	
Joseph Borg (Chairman)	6	
Mario Grima	5	(out of 5)
Paul Testaferrata Moroni Viani	5	
George Wells	6	
Franco Xuereb	4	(out of 5)

The Compliance Committee

The primary objective of the Compliance 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 the light of the Bank acting as a credit and financial institution licensed to provide services under different laws and within the framework of the Compliance Function as defined in the Compliance Charter and as approved by the Board of Directors.

The Chief Executive Officer, the Chief Officer Risk Management, the Chief Economist, the Chief Officer Legal and Compliance and the Executive Head Compliance attend the Compliance Committee meetings by invitation. The Company Secretary also acts as Secretary to the Compliance Committee.

Corporate governance statement of compliance (continued)

Members	Meetings Held: 5 Members Attended	
Mario Grima (Chairman)	4	(out of 4)
George Portanier *(resigned on 19 December 2013)*	1	(out of 1)
Joseph Borg	4	
Paul Testaferrata Moroni Viani	4	
Franco Xuereb	5	

Management Committees

The **Executive Committee** meets twice a month, and is responsible for:

i) day-to-day management of the Bank's business;
ii) development and implementation of approved strategy, policies, operational plans and budgets;
iii) monitoring of operational and financial performance;
iv) assessment and control of risk;
v) prioritisation and allocation of resources;
vi) monitoring competitive forces in all areas of operation; and
vii) making recommendations to the Board on matters which are beyond its remit.

The Executive Committee is chaired by the Chief Executive Officer, with all the Chief Officers as members.

[During FY 2015, the Executive Committee will be reconstituted as the Management Board and as mentioned under Principle 2 above, it will be made up of the Chief Executive Officer, the Chief Operating Officer, the Chief Risk Officer, the Chief Finance Officer and the Chief Business Development Officer.]

The **Credit Committee** meets on a weekly basis unless further meetings are required. The Credit Committee is composed of representatives from the Risk and Credit functions, and sanctions credit proposals within a sanctioning limit approved by the Board of Directors. Proposals falling outside this limit are referred, with the Committee's recommendations, to the Board for consideration and determination. The Committee needs to be fully constituted at each meeting, and for this reason each member has an approved substitute. The Credit Committee is chaired by the Chief Officer Risk Management and has as members the Chief Officer Credit, the Executive Head Corporate Finance and two senior managers from the Credit Risk Management Unit.

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 once a month to review Balance Sheet risks and ensures their prudent management. 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. 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. ALCO is chaired by the Chief Officer Risk Management, and has as members a Board Director, the Chief Executive Officer, the Chief Officer Finance, the Chief Officer Financial Markets & Investments, the Chief Officer Credit, the Chief Officer Fund Services, the Chief Economist and the Executive Head Financial Markets & Investments.

The **Provisions Committee** is responsible for the provisioning methodology. The Committee meets on a monthly basis unless further meetings are required. The Provisions Committee is chaired by the Chief Officer Finance and has as members the Chief Officer Risk Management, the Chief Officer Credit, the Chief Economist, the Senior Credit Portfolio Manager and the Head Finance.

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 Committee is chaired by the Chief Executive Officer and has as members the Chief Officer Risk Management, the Chief Officer Finance, the Chief Officer Strategy and Process Management, the Chief Officer IT and the Executive Head IT.

Principle 6: Information and Professional Development

The Chief Executive Officer is appointed by the Board and enjoys the full confidence of the Board. He is responsible for recruitment and selection of Senior Management and consults with the Remuneration and Nominations Committee and with the Board on the appointment of, and on a succession plan for, 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 and the Chief Officers on the activities of their

Corporate governance statement of compliance (continued)

respective business areas. Directors are also provided with a dossier that, apart from incorporating the relevant legislation, rules and bye laws, Memoranda and Articles of Group companies, and policy documents, also includes a report by the Bank's Legal Office on the various laws that Directors need to observe in the carrying out of their duties.

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.

From time to time, the Board organises regular information briefing sessions to ensure that the Directors are made aware of their duties, the Bank's operations and plans, skills and competence of Senior Management, the general business environment and the Board's expectations. Three sessions were in fact held during the period under review, dealing with a range of subjects. 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 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 and Nominations Committee is dealt with under the Remuneration Report, which also includes the Remuneration Statement in terms of Code Provisions 8.A.3 and 8.A.4.

The Bank has opted not to set up a Nomination Committee with the role and functions as set out in the Code. Further explanation is provided under section C of this Statement entitled Non-Compliance with the Code.

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.

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 (Cap.386 of the 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 has strict policies in place which allow it to manage such conflicts, actual or potential, in the best interest of the Bank. These policies include:

i) that a Director is 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;
ii) that the said Director is excused from the meeting and accordingly is not involved in the Bank's Board discussion on the matter; and
iii) that the said Director does not vote on any such matter.

Corporate governance statement of compliance (continued)

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 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' interests in the share capital of the Bank as at 30 September 2014 were as follows:

	Beneficial Interest *
Mario Grima	10,628 shares
Paul Testaferrata Moroni Viani **	7,769 shares
George Wells	8,814 shares
Joseph M Zrinzo	121,481 shares

* Beneficial interest includes any shares held by spouses.
** Paul Testaferrata Moroni Viani is a shareholder in companies which hold BOV Shares.

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

As at 30 September 2014, 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
George Wells	15,000	BOV 4.80% Medium Term Notes 2018
	16,500	BOV 5.35% Subordinated Bonds 2019
	22,400	BOV 4.80% Subordinated Bonds 2020
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

*** These investments include any holdings held by spouses.

Principle 12: Corporate Social Responsibility (CSR)

The Bank recognizes it has an important role to play as an active corporate citizen within the Maltese society. In addition to its commitment to be a key driver of the economy, the Bank also contributes to the social and cultural development of the country through the efficient and effective management of resources for the benefit of all stakeholder groups.

The Bank continuously strives to be the employer of choice for its people, whom it considers to be its primary asset. In a bid to promote a healthy lifestyle and wellbeing for its employees, the Bank has a number of programmes in place to help its people maintain a stress-free balance between their work and private life including subsidies on summer schools and health check-ups. Employees are also encouraged to fulfil their role in the community by participating in events like blood donation drives, dress down days in aid of charities and tree-planting activities organised throughout the year.

The Bank continues to underline its Green agenda, which has been featuring in its Mission Statement for several years. The setting up of the Green Manager role along with the Green Leaders, who are an extension of this role spread amongst the whole organisation, further helps the Bank in its commitment to reduce its carbon footprint whilst instilling more environmental-friendly practices. This philosophy is extended to the supply chain by integrating environmental considerations into all stages of the purchasing process.

The Bank's roots run deep into the community in which it operates. The sound principles of Corporate Social Responsibility (CSR) are put into practice through its extensive Community Programme which is distilled into seven distinct pillars, representing diverse but equally important concerns for the Maltese society. These are:

Arts and Culture – BOV has taken on board a number of artistic initiatives during the financial year under review. These include performances at the Manoel Theatre and the two theatres in Gozo - Astra and Aurora - as well as more intimate concerts featuring some of Malta's talented performers. BOV remains a leading sponsor of the Malta Philharmonic Orchestra. This year it has also collaborated with the Fondazzjoni Celebrazzjonijiet Nazzjonali in organising the concert to celebrate the 50 year anniversary of Malta's Independence. The Bank has continued to endorse the Maltese Tenor Joseph Calleja as well as the BOV Joseph Calleja Children's Choir. The BOV Retrospective Arts Exhibition which this year featured works of art by renowned artist Anthony Mahoney has remained a much sought after annual appointment on the country's cultural calendar.

Corporate governance statement of compliance (continued)

Heritage – The restoration projects at the vault of the Sanctuary in Mellieħa and the masterpieces in Għajnsielem Chapel are moving steadily with the Bank's support. The Bank also partnered with Fondazzjoni Wirt Artna, not only in relation to safeguarding historical gems but also vis-à-vis its Hands-On Heritage which focuses on educating the younger generation about our rich past by offering students the unique opportunity to handle period instruments and tools, and learn how they were used.

Environment – The Bank renewed its backing to Dinja Waħda, a nationwide education and awareness program run across Primary Schools by the NGO BirdLife Malta. Targeting thousands of school children, this program aims to instill in them a deeper appreciation for Malta's fauna and flora. The Bank continued to support the BOV Adventure Park at Ta' Qali in a bid to ensure adequate green space for Maltese families to spend quality time together. Meanwhile, throughout the year, the Bank planted 1,600 trees around the Maltese islands.

Education – The Bank embarked on a collaborative effort with the Ministry for Education and Employment to combat illiteracy through the National Literacy Campaign, which evolved into the Read with Me initiative that materialised into several activities involving volunteers trained to guide parents in reading with their young children, thereby instilling a love for reading at a tender age. Excellence in education was also promoted by sponsoring various educational awards. The BOV Investment Education Project, a project which gives University students reading for a degree in Economics, Management and Accountancy the opportunity to get first-hand experience in the world of financial trading was once again successfully executed.

Social Causes – This year witnessed Bank of Valletta setting up the Marigold Foundation – BOV in the Community to manage requests with a philanthropic purpose by NGOs and individuals. The BOV Joseph Calleja Foundation was also launched during this financial year. This Foundation seeks to assist underprivileged children with artistic and musical aptitude to develop their talents. The L-Istrina BOV Piggy Bank campaign celebrated its 10th anniversary this year. Launched among school children to promote a culture of altruism, this campaign today sees over 6,000 piggy banks distributed among schools and various retail outlets.

Sport – Promoting a healthy lifestyle remains at the top of the Bank's agenda. Witness to this is the support provided to various sporting associations in a bid to encourage the general public to make sports a more integral part of their lifestyle and helping various disciplines reach increasingly higher levels of performance.

Strategic Alliances – Through strategic alliances, the Bank continues to build networks with members of the main representative bodies and business organisations, such as the Malta Chamber of Commerce, Enterprise and Industry, the Malta Hotels and Restaurants Association and the Chamber of Engineers. This year saw the Bank give its support to The Malta Film Commission and to the Today Public Policy Institute.

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 (Performance Evaluation):

The Code recommends that the Board undertakes an annual evaluation of its own performance and that of its committees.

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.

Apart from the review of the Senior Management organization structure referred to earlier, this financial year was characterized by a review of various areas of operation, structures and processes within the Bank, some of which are still ongoing. The Board and the relevant Committees were actively involved in the discussions leading to the implementation of recommendations arising from these reviews. Within this context, it was felt that the evaluation would be beneficial if it is carried out at a later date in order to encapsulate the Board and the Committee's views on their performance in relation both to their ordinary business as well as the specific reviews being undertaken.

Principle 8B (ii) (a) (Nomination Committee):

Pursuant to the Bank's Articles of Association, the appointment of Directors to the Board is reserved exclusively 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 in accordance with the provisions of the Articles of Association. The nomination of a candidate by a shareholder is to be seconded by a shareholder or shareholders holding at least 5,000 shares.

Corporate governance statement of compliance (continued)

Within this context and in view of the provisions of the Bank's Articles of Association explained above, a Nomination Committee in terms of the Code (namely, as regards its functions vis-à-vis the procedure of nomination of Directors to the Board) would not be able to undertake satisfactorily its full functions and responsibilities as envisaged by the spirit of the Code. The Bank also considers that some of the functions of the Nomination Committee (particularly those relating to succession planning and the appointment of senior management) are already dealt with by the Remuneration and Nominations Committee. The Board will however be reviewing the issue relating to the setting up of a Nomination Committee with the functions as envisaged in terms of the Code particularly also in the light of the provisions contained in CRD IV.

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.

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 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 associated 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 associated life insurance company and a member of the Board of the associated 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 and Compliance; 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 Officer Risk Management, 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 Executive Management. 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.

Corporate governance statement of compliance (continued)

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 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 Board (which may or may not involve an election), the appointment of the auditors and the grant of the authority to the Board to fix the auditors' emoluments. Other business which may be transacted at a general meeting (including at the Annual General Meeting) 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.

Auditors' report on corporate governance

Pursuant to Listing Rules 5.94 and 5.97 of the Malta Financial Services Authority, the directors are required to include in their Annual Report a Statement of Compliance to the extent to which they have adopted the Code of Principles of Good Corporate Governance and the effective measures that they have taken to ensure compliance with these principles.

Our responsibility is laid down in Listing Rule 5.98, which requires us to include a report on the Statement of Compliance.

We read the Statement of Compliance and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information included in the Annual Report.

We are not required to perform additional work necessary to, and we do not, express any opinion on the effectiveness of either the Bank's system of internal control or its corporate governance procedures.

In our opinion, the Statement of Compliance, set out in this Annual Report has been properly prepared in accordance with the requirements of Listing Rules 5.94 and 5.97.

S. Curmi as Director
in the name and on behalf of
Deloitte Audit Limited
Registered auditor,
Deloitte Place,
Mriehel Bypass,
Mriehel BKR 3000,
Malta

M. Rhys
Partner, for and on behalf of
Deloitte LLP
Chartered Accountants,
Hill House,
1, Little New Street,
London EC4A 3TR,
United Kingdom

31 October 2014

Remuneration report as at 30 September 2014

1. Terms of Reference and Membership

The Remuneration and Nominations Committee (the Committee) is charged with overseeing the development and implementation of the remuneration and related policies of the Bank of Valletta Group (the Group).

The Committee is composed of John Cassar White (Chairman), Taddeo Scerri and Joseph M Zrinzo as members, all of whom are independent non-executive directors. The Chief Executive Officer (CEO) attends meetings of the Committee by invitation. The Company Secretary acts as secretary to the Committee.

2. Meetings

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

Members	**Attended**	
John Cassar White (Chairman)	9	
George Portanier (*resigned on 19 December 2013*)	2	(out of 2)
Taddeo Scerri	9	
Joseph M Zrinzo (*appointed on 19 December 2013*)	7	(out of 7)

The Committee determined and/or discussed the following matters:

- Updated Terms of Reference for the Remuneration and Nominations Committee
- Remuneration Report for FY 2013
- Staff upgrades
- CEO and Executives' Performance Bonus FY 2013
- CEO Performance Targets FY 2014
- Grievances exercise
- Revised Travel Policy
- Appointment of Members on the Trusts Committee and the Trusts Approval Committee
- Executives' early retirement requests
- Early retirement annuity payments (retirement prior to 2007)
- Review of the Bank's Senior Management Governance Structure
- Review of the Bank's IT Organisation Structure
- Changes in the IT governance structure and the appointment of a Chief Technology Officer

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 CEO, then establishes the individual remuneration arrangements of the Group's Executive Management, namely the Chief Officers, the Executive Heads and the Heads.

The Committee is also charged with considering and determining any recommendations from the CEO on requests for early retirement. Early retirement schemes are established and defined within the Bank's Collective Agreements. The Committee has access to independent external advice on remuneration matters as and when required.

A Group's Remuneration Policy was approved by the Committee and by the Board during the first quarter of FY 2012. 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 significant changes are intended to be effected thereto in FY 2015.

Hereinafter, for the purposes of this Remuneration Statement, references to "Senior Executives" shall mean the CEO and the Chief Officers.

Remuneration report as at 30 September 2014 (continued)

The terms and conditions of employment of Senior Executives are set out in their respective indefinite contracts of employment with the Bank. As a general rule, 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 CEO's remuneration is reviewed and approved by the Committee. The CEO is eligible for an annual bonus entitlement by reference to the attainment of pre-established objectives and targets as approved by the Committee.

The Chief Officers are eligible for an annual salary increase within a maximum salary range approved by the Committee. This increase is computed on the basis of the same percentage salary increase granted to staff members in terms of the relative Collective Agreement, adjusted to reflect the individual performance of the Chief Officer as approved by the Committee.

The Chief Officers are also eligible for an annual bonus entitlement determined by the Bank's performance and the individual performance of the Chief Officers.

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.

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 2014 are reported below under section 3.3 in terms of Code Provisions 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. This amount was fixed at an aggregate sum of €290,000 per annum at the 39th Annual General Meeting held on the 19 December 2012.

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

**John Cassar White opted to waive fees due to him as chairman of the Remuneration and Nominations Committee*

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 emoluments received by Directors during FY 2014 are reported below under section 3.3 in terms of Code Provisions 8.A.5.

Remuneration report as at 30 September 2014 (continued)

3.3 Code Provision 8.A.5

Senior Executives' Emoluments

Fixed Remuneration	Variable Remuneration	Share Options	Others
€1,069,538	€52,864	None	Non-cash benefits referred to above under 3.1

Directors' Emoluments

Fixed Remuneration	Variable Remuneration	Share Options	Others
€274,873*	None	None	Non-cash benefits referred to above under 3.2

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

Directors' emoluments including benefits – FY 2014	**€**
John Cassar White	78,337
Joseph Borg	26,272
Roberto Cassata	17,500
Ann Fenech (*resigned on 19 December 2013*)	4,094
Mario Grima (*appointed on 19 December 2013*)	20,048
George Portanier (*resigned on 19 December 2013*)	5,833
Taddeo Scerri	29,415
Paul Testaferrata Moroni Viani	25,310
George Wells	25,061
Franco Xuereb	23,887
Joseph M Zrinzo (*appointed on 19 December 2013*)	19,116
Total	274,873

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

We have audited the accompanying financial statements of Bank of Valletta p.l.c. ('the Bank') and its Group (together 'the Group') set out on pages 46 to 115, which comprise the statements of financial position as at 30 September 2014, and the statements of profit or loss, statements of profit or loss and other comprehensive income, statements of changes in equity and statements of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

As explained more fully in the statement of Directors' Responsibilities on page 2, the directors of the Bank are responsible for the preparation of the Group and the Bank financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Companies Act (Cap.386 of the Laws of Malta), and 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. 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 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 the auditor's 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, the auditor considers internal control relevant to the 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 internal control of the Bank and the Group. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors 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.

Opinion

In our opinion the financial statements give a true and fair view of the financial position of Bank of Valletta p.l.c and its Group as at 30 September 2014 and of the Group's and the Bank's financial performance and cash flows for the year then ended in accordance with IFRSs as adopted by the EU and have been properly prepared in accordance with the requirements of the Companies Act (Cap.386 of the Laws of Malta).

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

Report on other legal and regulatory requirements

Auditors' responsibility

The Banking Act (Cap.371 of the Laws of Malta) requires us to report whether we have obtained all the information and explanations which to the best of our knowledge and belief are necessary for the purposes of our audit, whether in our opinion proper books of account have been kept by the Bank so far as appears from our examination thereof, whether the financial statements are in agreement with the books, and whether in our opinion, and to the best of our knowledge and according to the explanations given to us, the financial statements give the information required by law in the manner so required and give a true and fair view.

Opinion

We have obtained all the information and explanations which to the best of our knowledge and belief are necessary for the purposes of our audit. In our opinion, proper books of account have been kept so far as appears from our examination thereof and the financial statements are in agreement with the books. In our opinion, the financial statements have been properly prepared in accordance with the Banking Act (Cap.371 of the Laws of Malta) and the Companies Act (Cap.386 of the Laws of Malta).

S. Curmi as Director
in the name and on behalf of
Deloitte Audit Limited
Registered auditor,
Deloitte Place,
Mriehel Bypass,
Mriehel BKR 3000,
Malta

M. Rhys
Partner, for and on behalf of
Deloitte LLP
Chartered Accountants,
Hill House,
1, Little New Street,
London EC4A 3TR,
United Kingdom

31 October 2014

Statements of profit or loss for the year ended 30 September 2014

	Note	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Interest receivable and similar income					
- on loans and advances, balances with Central Bank of Malta and treasury bills	2	153,430	161,709	153,430	161,709
- on debt and other fixed income instruments	2	59,466	60,728	59,466	60,728
Interest payable	3	(86,893)	(91,423)	(86,893)	(91,423)
Net interest income		**126,003**	**131,014**	**126,003**	**131,014**
Fee and commission income		64,112	59,435	56,834	52,519
Fee and commission expense		(8,150)	(7,322)	(8,150)	(7,322)
Net fee and commission income	4	**55,962**	**52,113**	**48,684**	**45,197**
Dividend income		1,372	873	8,496	7,914
Trading profits	5	25,654	31,149	25,621	31,107
Net gain on investment securities and hedging instruments	6	814	2,978	814	2,978
Operating income		**209,805**	**218,127**	**209,618**	**218,210**
Employee compensation and benefits	7	(57,537)	(54,373)	(55,891)	(52,798)
General administrative expenses	7	(28,644)	(28,725)	(27,322)	(27,529)
Amortisation of intangible assets	20	(2,202)	(1,642)	(2,202)	(1,642)
Depreciation	21	(5,116)	(4,398)	(5,013)	(4,296)
Net impairment losses	8	(19,431)	(25,595)	(19,408)	(25,595)
Operating profit		**96,875**	**103,394**	**99,782**	**106,350**
Share of results of associates, net of tax	18	7,227	12,384	-	-
Profit before tax	9	**104,102**	**115,778**	**99,782**	**106,350**
Income tax expense	10	(34,718)	(36,305)	(35,336)	(35,861)
Profit for the year		**69,384**	**79,473**	**64,446**	**70,489**
Attributable to:					
Equity holders of the Bank		68,945	79,055	64,446	70,489
Non-controlling interest		439	418	-	-
		69,384	79,473	64,446	70,489
Earnings per share	11	**20c9**	**24c0**	**19c5**	**21c4**

Statements of profit or loss and other comprehensive income

for the year ended 30 September 2014

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
Profit for the year	69,384	79,473	64,446	70,489
Other comprehensive income				
Items that may be reclassified subsequently to profit or loss:				
Available-for-sale investments				
- change in fair value	6,613	9,210	6,613	9,210
- deferred tax thereon	(2,314)	(3,223)	(2,314)	(3,223)
- change in fair value transferred to profit or loss	(763)	(1,290)	(763)	(1,290)
- deferred tax thereon	267	452	267	452
Items that will not be reclassified to profit or loss:				
Property				
- revaluation	809	6,703	809	6,703
- deferred tax thereon	(97)	(804)	(97)	(804)
Actuarial losses on defined benefit plans	(3,028)	-	(3,028)	-
- deferred tax thereon	1,059	-	1,059	-
Other comprehensive profit for the period, net of tax	2,546	11,048	2,546	11,048
Total comprehensive income	71,930	90,521	66,992	81,537
Attributable to:				
Equity holders of the Bank	71,491	90,103		
Non-controlling interest	439	418		
	71,930	90,521		

Statements of financial position as at 30 September 2014

	Note	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	13	130,966	194,587	130,966	194,587
Financial assets at fair value through profit or loss	14	527,774	581,531	523,480	578,691
Investments	15	2,422,237	1,665,820	2,422,237	1,665,820
Loans and advances to banks	16	1,045,988	860,957	1,045,988	860,957
Loans and advances to customers at amortised cost	17	3,861,532	3,667,739	3,861,532	3,667,739
Investments in associates	18	88,553	84,880	52,870	52,870
Investments in subsidiary companies	19	-	-	1,230	1,393
Intangible assets	20	11,642	11,495	11,642	11,495
Property, plant and equipment	21	88,117	80,123	87,888	79,872
Deferred tax	22	78,550	70,205	78,550	70,205
Assets held for realisation	43	9,755	10,607	9,755	10,607
Other assets		7,659	4,799	7,659	3,868
Prepayments and accrued income	23	24,018	25,215	22,469	25,215
Total Assets		**8,296,791**	**7,257,958**	**8,256,266**	**7,223,319**
LIABILITIES					
Financial liabilities at fair value through profit or loss	14	44,903	30,819	44,903	30,819
Amounts owed to banks	24	86,579	36,040	86,579	36,040
Amounts owed to customers	25	7,119,530	6,219,666	7,120,674	6,220,954
Debt securities in issue	26	95,400	95,400	95,400	95,400
Current tax		16,090	4,697	15,934	5,065
Deferred tax	22	5,100	5,003	5,100	5,003
Other liabilities	27	130,168	108,864	130,068	108,765
Accruals and deferred income	28	27,643	29,235	27,174	28,962
Financial liabilities designated for hedge accounting	29	36,909	31,229	36,909	31,229
Subordinated liabilities	30	120,000	120,000	120,000	120,000
Total Liabilities		**7,682,322**	**6,680,953**	**7,682,741**	**6,682,237**
EQUITY					
Attributable to equity holders of the Bank:					
Called up share capital	31	330,000	300,000	330,000	300,000
Share premium account		988	988	988	988
Revaluation reserves	32	29,136	24,621	29,024	24,509
Retained earnings		253,245	250,735	213,513	215,585
		613,369	576,344	573,525	541,082
Non-controlling interest		1,100	661	-	-
Total Equity		**614,469**	**577,005**	**573,525**	**541,082**
Total Liabilities and Equity		**8,296,791**	**7,257,958**	**8,256,266**	**7,223,319**
MEMORANDUM ITEMS					
Contingent liabilities	33	233,451	213,598	233,451	213,598
Commitments	34	1,647,091	1,190,714	1,647,091	1,190,714

These financial statements were approved by the Board of Directors and authorised for issue on 31 October 2014 and signed on its behalf by:

J. Cassar White
Chairman

G. Wells
Director

C. Borg
Chief Executive Officer

Statements of changes in equity for the year ended 30 September 2014

	Attributable to Shareholders 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 30 September 2012	**270,000**	**988**	**13,573**	**236,196**	**520,757**	**243**	**521,000**
Profit for the year	-	-	-	79,055	**79,055**	418	**79,473**
Other comprehensive income							
Available-for-sale investments							
- change in fair value, net of tax	-	-	5,987	-	**5,987**	-	**5,987**
- change in fair value transferred to profit or loss, net of tax	-	-	(838)	-	**(838)**	-	**(838)**
Property revaluation							
- property revaluation, net of tax	-	-	5,899	-	**5,899**	-	**5,899**
Total other comprehensive profit	-	-	11,048	-	**11,048**	-	**11,048**
Total comprehensive income for the year	-	-	11,048	79,055	**90,103**	418	**90,521**
Transactions with owners, recorded directly in equity:							
Bonus issue	30,000	-	-	(30,000)	**-**	-	**-**
Dividends - final 2012	-	-	-	(22,816)	**(22,816)**	-	**(22,816)**
- interim 2013 (note 12)	-	-	-	(11,700)	**(11,700)**	-	**(11,700)**
	30,000	-	-	(64,516)	**(34,516)**	-	**(34,516)**
At 30 September 2013	**300,000**	**988**	**24,621**	**250,735**	**576,344**	**661**	**577,005**
Profit for the year	-	-	-	68,945	**68,945**	439	**69,384**
Other comprehensive income							
Available-for-sale investments							
- change in fair value, net of tax	-	-	4,299	-	**4,299**	-	**4,299**
- change in fair value transferred to profit or loss, net of tax	-	-	(496)	-	**(496)**	-	**(496)**
Property revaluation							
- property revaluation, net of tax	-	-	712	-	**712**	-	**712**
Actuarial losses on defined benefit plans, net of tax	-	-	-	(1,969)	**(1,969)**	-	**(1,969)**
Total other comprehensive profit / (loss)	**-**	**-**	**4,515**	**(1,969)**	**2,546**	**-**	**2,546**
Total comprehensive income for the year	**-**	**-**	**4,515**	**66,976**	**71,491**	**439**	**71,930**
Transactions with owners, recorded directly in equity:							
Bonus issue	30,000	-	-	(30,000)	**-**	-	**-**
Dividends - final 2013	-	-	-	(25,350)	**(25,350)**	-	**(25,350)**
- interim 2014 (note 12)	-	-	-	(9,116)	**(9,116)**	-	**(9,116)**
	30,000	-	-	(64,466)	**(34,466)**	-	**(34,466)**
At 30 September 2014	**330,000**	**988**	**29,136**	**253,245**	**613,369**	**1,100**	**614,469**

Statements of changes in equity for the year ended 30 September 2014 (continued)

	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000
The Bank					
At 30 September 2012	**270,000**	**988**	**13,461**	**209,612**	**494,061**
Profit for the year	-	-	-	70,489	**70,489**
Other comprehensive income					
Available-for-sale investments					
- change in fair value, net of tax	-	-	5,987	-	**5,987**
- change in fair value transferred to profit or loss, net of tax	-	-	(838)	-	**(838)**
Property revaluation					
- property revaluation, net of tax	-	-	5,899	-	**5,899**
Total other comprehensive profit	-	-	11,048	-	**11,048**
Total comprehensive income for the year	-	-	11,048	70,489	**81,537**
Transactions with owners, recorded directly in equity:					
Bonus issue	30,000	-	-	(30,000)	**-**
Dividends - final 2012	-	-	-	(22,816)	**(22,816)**
- interim 2013 (note 12)	-	-	-	(11,700)	**(11,700)**
	30,000	-	-	(64,516)	**(34,516)**
At 30 September 2013	**300,000**	**988**	**24,509**	**215,585**	**541,082**
Profit for the year	-	-	-	64,446	**64,446**
Other comprehensive income					
Available-for-sale investments					
- change in fair value, net of tax	-	-	4,299	-	**4,299**
- change in fair value transferred to profit or loss, net of tax	-	-	(496)	-	**(496)**
Property revaluation					
- property revaluation, net of tax	-	-	712	-	**712**
Actuarial losses on defined benefit plans, net of tax	-	-	-	(1,969)	**(1,969)**
Total other comprehensive profit / (loss)	-	-	4,515	(1,969)	**2,546**
Total comprehensive income for the year	-	-	4,515	62,477	**66,992**
Transactions with owners, recorded directly in equity					
Accumulated losses acquired on merger of subsidiary	-	-	-	(83)	**(83)**
Bonus issue	30,000	-	-	(30,000)	**-**
Dividends - final 2013	-	-	-	(25,350)	**(25,350)**
- interim 2014 (note 12)	-	-	-	(9,116)	**(9,116)**
	30,000	-	-	(64,549)	**(34,549)**
At 30 September 2014	**330,000**	**988**	**29,024**	**213,513**	**573,525**

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

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, under the three year transitionary rules, this reserve amounts to €3.1 million.

Statements of cash flows for the year ended 30 September 2014

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
Cash flows from operating activities				
Interest and commission receipts	260,915	264,199	253,631	257,299
Interest, commission and compensation payments	(94,418)	(102,977)	(94,614)	(102,762)
Payments to employees and suppliers	(87,908)	(76,517)	(83,392)	(73,746)
Operating profit before changes in operating assets and liabilities	78,589	84,705	75,625	80,791
(Increase)/decrease in operating assets:				
Loans and advances	(245,922)	31,064	(245,899)	31,064
Reserve deposit with Central Bank of Malta	(8,108)	(3,505)	(8,108)	(3,505)
Fair value through profit or loss financial assets	52,835	166,084	52,835	166,084
Fair value through profit or loss equity instruments	(616)	(5,323)	838	(7,044)
Treasury bills with original maturity of more than 3 months	33,977	(9,985)	33,977	(9,985)
Other assets	(2,008)	4,035	(2,939)	5,821
Increase in operating liabilities:				
Amounts owed to banks and to customers	861,532	306,997	861,388	306,981
Other liabilities	29,266	(10,122)	29,321	(10,041)
Net cash from operating activities before tax	799,545	563,950	797,038	560,166
Tax paid	(32,658)	(54,430)	(33,800)	(53,165)
Net cash from operating activities	766,887	509,520	763,238	507,001
Cash flows from investing activities				
Dividends received	4,926	5,433	8,496	7,914
Interest received from held-to-maturity debt and other fixed income instruments	45,394	37,484	45,394	37,484
Purchase of equity instruments	(200)	-	(200)	-
Purchase of debt instruments	(1,167,952)	(678,365)	(1,167,952)	(678,365)
Proceeds from sale or maturity of debt instruments	475,452	299,081	475,452	299,081
Purchase of property, plant and equipment and intangible assets	(14,649)	(10,414)	(14,570)	(10,376)
Proceeds from disposal of property, plant and equipment	8	-	8	-
Net cash used in investing activities	(657,021)	(346,781)	(653,372)	(344,262)
Cash flows from financing activities				
Dividends paid to Bank's equity holders	(34,466)	(34,516)	(34,466)	(34,516)
Net cash used in financing activities	(34,466)	(34,516)	(34,466)	(34,516)
Net change in cash and cash equivalents	75,400	128,223	75,400	128,223
Cash and cash equivalents at 1 October	937,103	808,880	937,103	808,880
Cash and cash equivalents at 30 September	**1,012,503**	**937,103**	**1,012,503**	**937,103**

Notes to the financial statements 30 September 2014

1. SIGNIFICANT ACCOUNTING POLICIES

1.1 Basis of preparation

Legal Notice 19 of 2009, Accountancy Profession (Accounting and Auditing Standards) Regulations, 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 1 October 2008.

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 (Cap. 386) to the extent that the said provisions of the Companies Act 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 (Cap. 371 of the Laws of Malta) and the Companies Act (Cap. 386 of the 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.

During the year under review, the Group and the Bank have applied the following IFRS as adopted by the EU:

IFRS 13 *Fair Value Measurement*, applicable for annual periods beginning on or after 1 January 2013 (with earlier application being permitted). IFRS 13 defines fair value, establishes a single source of guidance for fair value measurements and requires disclosures about fair value measurements. IFRS 13 requires prospective application. In accordance with the transitional provisions set out in the Standard, entities need not apply the disclosure requirements in comparative information provided for periods before the initial application of the Standard. Consequently, the Bank and the Group have not made any new disclosures required by IFRS 13 for the comparative period.

These financial statements incorporate the additional disclosures that are required by the Standard for certain financial and non-financial items;

The Revised IAS 19 *Employee Benefits*, applicable for annual periods beginning on or after 1 January 2013 (with earlier application being permitted). This Standard represents the completion of the International Accounting Standards Board's project to improve the accounting for pensions and other post-employment benefits. Where applicable, the Bank and the Group have revised their accounting policy for post-employment benefits in line with the revised IAS 19, which requires (i) the recognition of changes in defined benefit obligations when they occur, (ii) the recognition of actuarial gains and losses in other comprehensive income and (iii) the acceleration of the recognition of past service costs. In accordance with the transitional provisions, this Standard is required to be applied retrospectively (except as otherwise indicated). The adoption of this Standard resulted in additional disclosures in the notes to the financial statements. The adoption of this Standard did not have a quantitative impact on the Bank's and the Group's financial position at 1 October 2012 and hence it was not considered necessary to present a third statement of financial position as at that date. The following table shows the effect of adopting this Standard on this year's profit for the year and other comprehensive income for the year. The quantitative effect of the revised Standard on the prior year's results would be an increase of €192,000 on profit for the year and a decrease by the same amount on other comprehensive income for the year. This was considered to be immaterial. Given that such adjustments are both reflected in retained earnings, as disclosed in the accounting policies, the Bank and the Group did not adjust the prior year figures.

	The Group and the Bank
	2014
	€000
Decrease in employee compensation and benefits recognised in profit or loss	3,028
Decrease in deferred tax credit recognised in profit or loss	(1,059)
Increase in profit for the year, net of tax	1,969
Increase in actuarial losses recognised in other comprehensive income	(3,028)
Increase in deferred tax credit recognised in other comprehensive income	1,059
Decrease in other comprehensive income for the year, net of tax	(1,969)

Notes to the financial statements 30 September 2014 (continued)

The December 2011 Amendments to IFRS 7, *Disclosures – Offsetting Financial Assets and Financial Liabilities* applicable for annual periods beginning on or after 1 January 2013 (with earlier application being permitted). The Amendments include additional disclosures for (i) all recognised financial instruments that are set off in accordance with IAS 32 and for (ii) recognised financial instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether these are set off in accordance with IAS 32. These Amendments are applied retrospectively.

A number of new International Financial Reporting Standards and amendments and revisions thereto were in issue but not yet effective during the financial year under review. 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 include the following:

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.

On 12 May 2011, the IASB issued *IFRS 10 Consolidated Financial Statements*, *IFRS 11 Joint Arrangements* and *IFRS 12 Disclosure of Interests in Other Entities*. At the same time, the IASB issued a revised version of IAS 27 *Separate Financial Statements* and a revised version of IAS 28 *Investments in Associates and Joint Ventures*. For financial statements prepared in accordance with *International Financial Reporting Standards* as adopted by the EU, the new and revised Standards are applicable for annual periods beginning on or after 1 January 2014, with earlier application being permitted.

IFRS 10 *Consolidated Financial Statements* builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. IFRS 10 introduces a single consolidation model for all entities based on control, irrespective of the nature of the investee (that is, whether an entity is controlled through voting rights of the investors or otherwise). IFRS 10 supersedes SIC-12 Consolidation—*Special Purpose Entities* and parts of IAS 27 *Consolidated and Separate Financial Statements*.

IFRS 12 *Disclosure of Interests in Other Entities* addresses disclosure requirements for certain interests in other entities, including joint arrangements, associates, subsidiaries and unconsolidated structured entities. The objective of IFRS 12 is to require an entity to disclose information that enables users of its financial statements to evaluate (a) the nature of and risks associated with, its interests in other entities; and (b) the effects of those interests on its financial position, financial performance and cash flows.

On 28 June 2012, the IASB issued amendments to IFRS 10, IFRS 11 and IFRS 12 entitled *Consolidated Financial Statements*, *Joint Arrangements* and *Disclosure of Interests in Other Entities: Transition Guidance*. The amendments clarify the transition guidance in IFRS 10 and provide additional transition relief in IFRS 10, IFRS 11 and IFRS 12, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. Furthermore, for disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before IFRS 12 is first applied.

On 16 December 2011, the IASB also issued amendments to IAS 32. These amendments are intended to help investors and other financial statement users to better assess the effect or potential effect of offsetting arrangements on a company's financial position. The amendments to IAS 32 are applicable as of 1 January 2014.

On 20 May 2013, IFRIC 21 Levies was issued. For financial statements prepared in accordance with International Financial Reporting Standards as adopted by the EU, IFRIC 21 is applicable for annual periods beginning on or after 7 June 2014. IFRIC 21 is an interpretation of IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (known as an obligating event). The Interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy.

On 27 June 2013, the IASB issued an amendment to IAS 39, entitled *Novation of Derivatives and Continuation of Hedge Accounting*. This amendment is applicable for annual periods beginning on or after 1 January 2014. This narrow-scope amendment to IAS 39 will allow hedge accounting to continue in a situation where a derivative, which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws or regulation, if specific conditions are met.

Notes to the financial statements 30 September 2014 (continued)

On 29 May 2013, the IASB issued an amendment to IAS 36, entitled *Recoverable Amount Disclosures for Non-Financial Assets*. This amendment is applicable for annual periods beginning on or after 1 January 2014. This narrow-scope amendment to IAS 36 *Impairment of Assets* addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal.

On 31 October 2012, the IASB issued amendments to IFRS 10, IFRS 12 and IAS 27, entitled *Investment Entities*. The amendments define an investment entity and introduce an exception for investment entity parents from consolidating particular subsidiaries. These amendments require investment entities to measure those subsidiaries at fair value through profit or loss in their consolidated and separate financial statements. The amendments also introduce new disclosure requirements for investment entities. The amendments are effective for annual periods beginning on or after 1 January 2014, with earlier application being permitted.

On 28 May 2014, the IASB issued IFRS 15 entitled *Revenue from Contracts with Customers*. The Standard is effective for annual periods beginning on or after 1 January 2017, with earlier application being permitted. IFRS 15 is the result of a convergence project between the IASB and the FASB. IFRS 15 specifies how and when an IFRS reporter will recognise revenue as well as requiring such entities to provide users of financial statements with more informative, relevant disclosures. The standard supersedes IAS 18 *Revenue*, IAS 11 *Construction Contracts* and a number of revenue-related interpretations. This Standard applies to nearly all contracts with customers with the main exceptions being leases, financial instruments and insurance contracts. This Standard has not been endorsed by the EU at the date of authorisation of these financial statements.

On 12 August 2014, the IASB issued Amendments to IAS27 entitled *Equity Method in Separate Financial Statements*. These Amendments will allow entities to use the equity method to account for investments in subsidiaries, joint ventures and associates in their separate financial statements. These Amendments are applicable for annual periods beginning on or after 1 January 2016. These Amendments have not been endorsed by the EU at the date of authorisation of these financial statements.

On 25 September 2014, the IASB issued Amendments to IAS 19 as part of the Annual Improvements to IFRSs 2012 – 2014 Cycle. The Amendments clarify that the high quality corporate bonds used to estimate the discount rate for post-employment benefits should be issued in the same currency as the benefits to be paid. These Amendments would result in the depth of the market for high quality corporate bonds being assessed at currency level. The Amendments apply from the beginning of the earliest comparative period presented in the financial statements in which the Amendments are first applied. Any initial adjustment arising should be recognised in retained earnings at the beginning of that period. The Amendments are effective for annual periods beginning on or after 1 January 2016. These Amendments have not been endorsed by the EU at the date of authorisation of these financial statements.

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 Bank and the Group 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 those entities that are controlled by the Bank. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Bank has the power to govern the financial and operating policies of another entity. 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 results and assets and liabilities of associates and jointly-controlled entities 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. An associate is an entity over which the Group has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies. A joint venture is a contractual arrangement whereby the Group and other parties undertake an economic activity that is subject to joint control. Joint venture arrangements which involve the establishment of a separate entity in which each venturer has an interest are referred to as jointly controlled entities. 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. The significant accounting policies adopted are set out below.

Notes to the financial statements 30 September 2014 (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. If the market for a financial asset is not active, the Group establishes fair value by using valuation techniques commonly used by market participants. 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.

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 does not classify any financial assets as held-to-maturity if it has during the current financial year or during the two preceding financial years, sold or reclassified more than an insignificant amount of held-to-maturity investments before maturity (more than insignificant in relation to the total amount of held-to-maturity investments) other than sales or reclassifications that are specifically exempted for the purpose of this requirement in terms of IAS 39.

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.

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.

Notes to the financial statements 30 September 2014 (continued)

(i) Financial assets carried at amortised cost

There are two components to the Group's impairment allowances on financial assets carried at amortised cost: specific and collective allowances. The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

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 relevant legislation, which 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, but 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)

In the case of loans and advances which encounter actual or apparent financial difficulties, the Group may grant a concession to amend the original contractual timings, where a customer's financial difficulty indicates that with the original terms and conditions of the contract satisfactory repayment may not be possible.

When accounts were 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 third party 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 and recognised in profit or loss as a reclassification adjustment. The cumulative loss is measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss.

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 in profit or loss, the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. 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.

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 plus, 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

Notes to the financial statements 30 September 2014 (continued)

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 classified as 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 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 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

The Group considers the income statement to be the primary report of performance within the annual financial statements and ensures that, as far as practicable, all aspects of its performance are wholly and fairly reflected in profit or loss.

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.

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 from 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.

Notes to the financial statements 30 September 2014 (continued)

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 associates

Investments in subsidiaries and associates are included in the Bank's statement of financial position at cost less any impairment loss which may have arisen. Dividends from the investments are recognised in profit or loss.

Impairment
At the end of each reporting period, the Bank reviews the carrying amount of its investments in subsidiaries and associates 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, plant and equipment

Property, plant and equipment are classified into the following classes – land and buildings, IT infrastructure and equipment and office furniture and fittings.

Property, plant 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, plant and equipment is recognised as an expense when incurred.

Property, plant 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.

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 with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the end of the reporting period. Any surpluses arising on such revaluation are recognised in other comprehensive income and accumulated in equity as a revaluation reserve unless they reverse a revaluation decrease for the same asset previously recognised in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously charged. Any deficiencies resulting from decreases in value are deducted from this revaluation reserve to the extent that the balance held in this reserve relating to a previous revaluation of that asset is sufficient to absorb these, and charged to profit or loss thereafter.

Other tangible assets are stated at cost less any accumulated depreciation and any accumulated impairment losses.

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, plant and equipment and accounted for in accordance with the Group's accounting policy on property, plant and equipment. Where the software is not an integral part of the related hardware, this is classified as an intangible asset.

Notes to the financial statements 30 September 2014 (continued)

Computer software is recognised if it is probable that the expected future economic benefits that are attributable to the asset will flow to the Group and the cost of the asset can be measured reliably.

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.

Computer software is initially measured at cost. After initial recognition, it is carried at cost less any accumulated amortisation and any accumulated impairment losses.

1.12 Depreciation and amortisation

Depreciation on property, plant 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, plant and equipment				
Freehold and long-term leasehold buildings			2%	per annum
IT infrastructure and equipment	10%	-	25%	per annum
Office furniture and fittings	5%	-	10%	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.

1.13 Impairment of property, plant and equipment and intangible assets

At the end of each reporting period the Group reviews the carrying amount of its property, plant 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, as calculated. 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 comprehesive 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. Provisions are not recognised for future operating losses.

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

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

Notes to the financial statements 30 September 2014 (continued)

1.15 Taxation

Current and deferred tax 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 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. It is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

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.

1.16 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 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 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 on an appropriate basis over the relevant period.

1.17 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. 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.

1.18 Employee benefits

The Bank and the Group contribute towards the state pension in accordance with local legislation. The only obligation of the Bank and the Group is to make the required contribution. Costs are expensed in the year in which they are incurred.

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

Notes to the financial statements 30 September 2014 (continued)

1.19 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 90 days; 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 90 days. Amounts owed to banks that are repayable on demand or with a contractual period to maturity of less than 90 days 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.

1.20 Dividends payable

Dividends payable on ordinary shares are recognised as liabilities on the date on which they are declared.

1.21 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.

1.22 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.

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; and
- Level 3 inputs are unobservable inputs for the asset or liability.

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis, the Bank and the Group determine when transfers are deemed to have occurred between Levels in the hierarchy at the end of each reporting period .

1.23 Non current assets and disposal groups held for sale

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the sale is highly probable 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. Non-current assets and disposal groups classified as held for sale are measured at the lower of the assets' previous carrying amount and fair value less costs to sell. 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.

1.24 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 in the assessed group when forecasting future cash flows. The methodology and assumptions for estimating the amount and timing of future cash flows are reviewed regularly in the light of actual loss experience.

Notes to the financial statements 30 September 2014 (continued)

1.24.2 Fair value of financial instruments not quoted in active markets

The fair value of financial instruments that are not quoted in active markets is determined by using valuation techniques. Periodically, the Group calibrates these valuation techniques and tests them for validity. Where possible the valuation techniques used by the Group make use of observable data and incorporate all factors that market participants would consider in setting a price and are consistent with accepted economic methodologies for pricing financial instruments. Management is required to make certain assumptions and estimates in arriving at an appropriate fair value, based on available observable market data. A change in assumptions could affect the reported fair value of these financial instruments. Further disclosures are provided in note 39.

1.24.3 Impairment losses on available-for-sale investments and held-to-maturity 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 of an investment in an equity instrument below its cost. The determination of these loss events requires judgement.

1.24.4 Held-to-maturity investments

The Group follows the guidance in IAS 39, *Financial Instruments: Recognition and Measurement* when classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement regarding the Group's intention and ability to hold such instruments to maturity.

1.24.5 Post-employment benefits

In estimating the value of post-employment benefits towards eligible employees, management exercises judgement in respect of life expectancies, the level of salary at termination of employment dates, and rates applied to discount future cash flows to net present value.

1.24.6 Provision in relation to claims from investors on securities

In estimating the amounts that may be due on claims made by investors on securities, management exercises judgement in respect of the expected outflow after taking into account all information available to it.

1.24.7 Fair value of land and buildings

The fair value of the Bank's and the Group'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 Bank makes use of significant unobservable inputs. A change in such inputs could affect the reported fair value of these land and buildings.

1.24.8 Classification of facilities as forborne

Management follows the European Banking Authority technical standard in identifying 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.

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
2. INTEREST RECEIVABLE AND SIMILAR INCOME				
On loans and advances to banks	755	919	755	919
On loans and advances to customers	151,460	159,726	151,460	159,726
On balances with Central Bank of Malta	993	554	993	554
On treasury bills	222	510	222	510
	153,430	161,709	153,430	161,709
On debt and other fixed income instruments				
- available-for-sale	13,565	14,279	13,565	14,279
- held-to-maturity	42,569	33,502	42,569	33,502
- fair value through profit or loss	12,408	18,512	12,408	18,512
	68,542	66,293	68,542	66,293
Amortisation of discounts and premiums				
- available-for-sale	(818)	(725)	(818)	(725)
- held-to-maturity	(8,258)	(4,840)	(8,258)	(4,840)
	(9,076)	(5,565)	(9,076)	(5,565)
	59,466	60,728	59,466	60,728
	212,896	222,437	212,896	222,437
3. INTEREST PAYABLE				
On amounts owed to banks	17,674	18,702	17,674	18,702
On amounts owed to customers	58,825	62,327	58,825	62,327
On debt securities in issue	4,359	4,359	4,359	4,359
On subordinated liabilities	6,035	6,035	6,035	6,035
	86,893	91,423	86,893	91,423
4. NET FEE AND COMMISSION INCOME				
On loans and advances, similar activities and local business	27,949	25,074	27,949	25,074
On trust, life assurance, fund management and similar activities	17,497	16,023	10,219	9,107
On other activities	10,516	11,016	10,516	11,016
	55,962	52,113	48,684	45,197
5. TRADING PROFITS				
Profit on foreign exchange activities	17,465	16,732	17,459	16,749
Fair value movements and net gains on sale of financial instruments at fair value through profit or loss	8,189	14,417	8,162	14,358
	25,654	31,149	25,621	31,107

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
6. NET GAIN ON INVESTMENT SECURITIES AND HEDGING INSTRUMENTS				
Available-for-sale assets				
- net gain on early redemption	763	1,290	763	1,290
- net revaluation gain/(loss) attributable to hedged risk	5,720	(9,612)	5,720	(9,612)
	6,483	(8,322)	6,483	(8,322)
Derivative financial instruments				
- net (loss)/gain on derivative financial instruments held for hedging	(5,669)	11,300	(5,669)	11,300
	814	2,978	814	2,978
7. ADMINISTRATIVE AND OTHER OPERATING EXPENSES				
Employee compensation and benefits				
- wages and salaries	45,520	44,016	43,973	42,540
- social security costs	2,903	2,874	2,804	2,775
- retirement benefits	5,052	3,462	5,052	3,462
- other staff costs	4,062	4,021	4,062	4,021
	57,537	54,373	55,891	52,798
General administrative expenses	28,644	28,725	27,322	27,529
	86,181	83,098	83,213	80,327

	The Group		The Bank	
	2014	2013	2014	2013
	No. of persons	No. of persons	No. of persons	No. of persons
The average number of employees are analysed as follows:				
Managerial	558	520	539	503
Supervisory and clerical	932	962	895	926
Others	49	54	49	51
	1,539	1,536	1,483	1,480

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
8. NET IMPAIRMENT LOSSES				
Write downs:				
Investments and other assets	-	2,691	-	2,691
Loans and advances to customers				
- specific allowances	22,516	31,767	22,516	31,767
- collective allowances	15,242	6,534	15,242	6,534
- bad debts written off	1,743	1,808	1,720	1,808
	39,501	40,109	39,478	40,109
Reversals of write-downs:				
Investments and other assets	-	(32)	-	(32)
Loans and advances to customers				
- specific allowances	(11,982)	(10,374)	(11,982)	(10,374)
- collective allowances	(5,907)	(5,229)	(5,907)	(5,229)
- bad debts recovered	(2,181)	(1,570)	(2,181)	(1,570)
	(20,070)	(17,173)	(20,070)	(17,173)
Net impairment losses	19,431	25,595	19,408	25,595

9. PROFIT BEFORE TAX

Profit before tax is stated after charging:

	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Total remuneration payable to the external auditors of the parent company				
- the audit of financial statements	219	205	194	180
- other assurance services	24	24	24	24
- other services	163	139	163	139
	406	368	381	343
Directors' emoluments				
- fees	275	268	275	268
- directors' salaries as full-time bank employees	57	53	57	53
	332	321	332	321
Compensation to other key management personnel is analysed as follows				
- short term employee benefits	1,122	1,068	1,032	972
Total remuneration for directors and other key management personnel	1,454	1,389	1,364	1,293

Notes to the financial statements 30 September 2014 (continued)

10. INCOME TAX EXPENSE

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
Current	44,051	45,722	44,669	45,278
Deferred	(9,333)	(9,417)	(9,333)	(9,417)
	34,718	36,305	35,336	35,861

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 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Profit before tax	104,102	115,778	99,782	106,350
Tax at the applicable rate of 35%	36,436	40,522	34,924	37,223
Tax effect of:				
Exempt and untaxed dividends	(117)	(148)	(541)	(1,632)
Share of results of associates	(2,529)	(4,334)	-	-
Withholding tax on property sales	(12)	(9)	(12)	(9)
Depreciation on premises	373	290	373	290
Non-deductable expenses	33	30	33	30
Investment holdings	(21)	(84)	(21)	(84)
Actuarial losses on defined benefit plans	575	-	575	-
Other differences	(20)	38	5	43
Income tax expense	34,718	36,305	35,336	35,861

11. EARNINGS PER SHARE

	The Group		The Bank	
	2014	2013	2014	2013
	cents per share	cents per share	cents per share	cents per share
Earnings per share	20c9	24c0	19c5	21c4

The earnings per share for the Group and for the Bank have been calculated on the profits attributable to shareholders of the Bank and the Group, 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.

Notes to the financial statements 30 September 2014 (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			
	2014	2013	2014	2013
	cents per share	cents per share	€000	€000
Gross of income tax				
- prior year's final paid	11.8	10.6	39,000	35,100
- interim paid	4.3	5.4	14,025	18,000
	16.1	16.0	53,025	53,100
Net of income tax				
- prior year's final paid	7.7	6.9	25,350	22,816
- interim paid	2.8	3.5	9,116	11,700
	10.5	10.4	34,466	34,516

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 2014 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% (2013: 35%).

In respect of the current year, the directors propose that a final gross ordinary dividend of €0.0925 per share amounting to €30.5million (net ordinary dividend of €0.06 per share - €19.8 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 17 November 2014.

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

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
Balances with Central Bank of Malta	63,404	60,232	63,404	60,232
Malta Government Treasury Bills	29,999	100,966	29,999	100,966
Cash	37,563	33,389	37,563	33,389
	130,966	194,587	130,966	194,587

Balances with the Central Bank of Malta include Reserve Deposit amounting to €63.4 million (2013: €55.3 million) in respect of both the Group and the Bank, in terms of Article 37 of the Central Bank of Malta Act (Cap. 204).

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€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	18,169	11,411	18,169	11,411
Financial assets designated at fair value through profit or loss:				
Debt and other fixed income instruments	392,248	441,826	392,248	441,826
Equity and other non-fixed income instruments	68,761	66,362	64,467	63,522
Loans and advances to customers (note 17)	48,596	61,932	48,596	61,932
	509,605	570,120	505,311	567,280
	527,774	581,531	523,480	578,691

Financial assets at fair value through profit or loss with a nominal value of €70 million (2013: €70 million) have been pledged against the provision of credit lines by the Central Bank of Malta.

Financial liabilities at fair value through profit or loss

	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Financial liabilities classified as held for trading:				
Derivative financial instruments	44,903	30,819	44,903	30,819

14.1 Debt and other fixed income instruments

	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Issued by public bodies				
- local general government	116,196	179,527	116,196	179,527
- foreign general government	38,508	18,345	38,508	18,345
	154,704	197,872	154,704	197,872
Issued by other issuers				
- local banks	3,691	3,661	3,691	3,661
- foreign banks	165,086	165,772	165,086	165,772
- foreign other	58,855	64,163	58,855	64,163
- local other	9,912	10,358	9,912	10,358
	237,544	243,954	237,544	243,954
	392,248	441,826	392,248	441,826
Listing status				
- listed on Malta Stock Exchange	129,802	193,546	129,799	193,546
- listed elsewhere	240,259	217,815	240,259	217,815
- foreign unlisted	22,187	30,465	22,190	30,465
	392,248	441,826	392,248	441,826
Summary of movements during the year:				
At the beginning of the year	441,826	605,701	441,826	605,701
Acquisitions	123,097	22,418	123,097	22,418
Disposals	(182,690)	(183,004)	(182,690)	(183,004)
Movement in fair value	5,329	5,057	5,329	5,057
Exchange adjustment	4,686	(8,346)	4,686	(8,346)
At the end of the year	392,248	441,826	392,248	441,826

Notes to the financial statements 30 September 2014 (continued)

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

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
14.2 Equity and other non-fixed income instruments				
Issued by other issuers				
- local banks	621	761	621	761
- foreign banks	1,633	1,063	1,633	1,063
- foreign other	37,841	9,774	37,841	9,774
- local other	28,666	54,764	24,372	51,924
	68,761	66,362	64,467	63,522
Listing status				
- listed on Malta Stock Exchange	29,273	55,498	24,993	52,658
- listed elsewhere	8,937	703	8,937	703
- foreign unlisted	30,551	10,161	30,537	10,161
	68,761	66,362	64,467	63,522
Summary of movements during the year:				
At the beginning of the year	66,362	61,754	63,522	57,193
Acquisitions	31,690	8,530	30,236	8,530
Disposals	(31,074)	(3,207)	(31,074)	(1,486)
Movement in fair value	1,369	(654)	1,369	(654)
Exchange adjustment	414	(61)	414	(61)
At the end of the year	68,761	66,362	64,467	63,522

14.3 Derivative financial instruments

	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Fair value of assets	18,169	11,411	18,169	11,411
Fair value of liabilities	44,903	30,819	44,903	30,819
The above comprise over-the-counter forward exchange contracts and interest rate swaps that have not been designated as hedging instruments stated at fair value with notional amounts analysed with remaining life as follows:				
- less than 3 months	637,129	264,408	637,129	264,408
- between 3 months and 1 year	79,483	334,548	79,483	334,548
- more than 1 year	198,127	277,538	198,127	277,538
	914,739	876,494	914,739	876,494

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
15. INVESTMENTS				
Debt and other fixed income instruments				
- available-for-sale	290,726	312,663	290,726	312,663
- held-to-maturity	2,130,567	1,352,413	2,130,567	1,352,413
Equity and other non-fixed income instruments				
- available-for-sale	944	744	944	744
	2,422,237	1,665,820	2,422,237	1,665,820

Investments with a nominal value of €96.5 million (2013: €135 million) have been pledged against the provision of credit lines by the Central Bank of Malta.

15.1 Debt and other fixed income instruments available-for-sale

Issued by public bodies				
- local general government	193,273	234,364	193,273	234,364
- local public sector	67,703	60,657	67,703	60,657
Issued by other issuers				
- foreign banks	3,967	3,793	3,967	3,793
- foreign others	25,783	13,849	25,783	13,849
	290,726	312,663	290,726	312,663
Listing status				
- listed on Malta Stock Exchange	260,976	295,021	260,976	295,021
- listed elsewhere	25,783	13,849	25,783	13,849
- foreign unlisted	3,967	3,793	3,967	3,793
	290,726	312,663	290,726	312,663
Summary of movements during the year:				
At the beginning of the year	312,663	318,845	312,663	318,845
Acquisitions	24,515	68,782	24,515	68,782
Disposals	(34,587)	(71,295)	(34,587)	(71,295)
Redeemed	(29,405)	(145)	(29,405)	(145)
Amortisation	(818)	(725)	(818)	(725)
Movement in fair value	11,639	(1,699)	11,639	(1,699)
Profit on early redemption	763	1,290	763	1,290
Exchange adjustment	5,956	(2,390)	5,956	(2,390)
At the end of the year	290,726	312,663	290,726	312,663

Notes to the financial statements 30 September 2014 (continued)

15. INVESTMENTS (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
15.2 Debt and other fixed income instruments held-to-maturity				
Issued by public bodies				
- local general government	570,344	462,838	570,344	462,838
- foreign general government	197,182	137,263	197,182	137,263
- foreign public sector securities	-	3,703	-	3,703
	767,526	603,804	767,526	603,804
Issued by other issuers				
- foreign banks	1,085,301	659,694	1,085,301	659,694
- foreign other	277,740	88,915	277,740	88,915
	1,363,041	748,609	1,363,041	748,609
	2,130,567	1,352,413	2,130,567	1,352,413
Listing status				
- listed on Malta Stock Exchange	570,344	462,838	570,344	462,838
- listed elsewhere	1,115,114	666,142	1,115,114	666,142
- foreign unlisted	445,109	223,433	445,109	223,433
	2,130,567	1,352,413	2,130,567	1,352,413

At 30 September 2014, the fair value of held-to-maturity securities, without deducting transaction costs, amounted to €2,186.5 million (2013: €1,389.6 million).

Summary of movements during the year:				
At the beginning of the year	1,352,413	1,016,176	1,352,413	1,016,176
Acquisitions	1,143,437	609,583	1,143,437	609,583
Redemptions	(410,736)	(225,796)	(410,736)	(225,796)
Amortisation	(8,258)	(4,840)	(8,258)	(4,840)
(Loss)/profit on early redemptions	(39)	555	(39)	555
Exchange adjustment	53,750	(43,265)	53,750	(43,265)
At the end of the year	2,130,567	1,352,413	2,130,567	1,352,413

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

Issued by other issuers				
- local other	944	744	944	744
Listing status				
- local unlisted	944	744	944	744
	944	744	944	744
Summary of movements during the year:				
At the beginning of the year	744	3,435	744	3,435
Acquisitions	200	-	200	-
Impairment	-	(2,691)	-	(2,691)
At the end of the year	944	744	944	744

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
16. LOANS AND ADVANCES TO BANKS				
Repayable on call and at short notice	302,874	85,168	302,874	85,168
Term placements with Central Bank of Malta	293,688	585,658	293,688	585,658
Term placements with other banks	433,147	182,154	433,147	182,154
Cheques in course of collection	16,279	7,977	16,279	7,977
	1,045,988	860,957	1,045,988	860,957

17. LOANS AND ADVANCES TO CUSTOMERS

	The Group 2014 €000	The Group 2013 €000	The Bank 2014 €000	The Bank 2013 €000
Repayable on call and at short notice	611,156	602,629	611,156	602,629
Term loans and advances	3,461,230	3,242,646	3,461,230	3,242,646
	4,072,386	3,845,275	4,072,386	3,845,275
Less impairment losses	(210,854)	(177,536)	(210,854)	(177,536)
Net loans and advances at amortised cost	3,861,532	3,667,739	3,861,532	3,667,739
Loans and advances designated at fair value through profit or loss (note 14)	48,596	61,932	48,596	61,932
Total loans and advances	3,910,128	3,729,671	3,910,128	3,729,671
Impairment losses				
- individually assessed allowances	151,565	127,582	151,565	127,582
- collective allowances	59,289	49,954	59,289	49,954
	210,854	177,536	210,854	177,536

The balance of individually assessed allowances at the reporting date includes €80.2million (2013: €66.7million) in respect of interest in suspense which has been netted off against interest receivable. In previous years this interest allowance was netted off from gross amount of loans and advances. Comparative figures reflect this revised presentation.

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
18. INVESTMENTS IN ASSOCIATES				
At the beginning of the year	84,880	77,058	52,870	52,870
Share of results after tax	7,227	12,384	-	-
Dividend received	(3,554)	(4,562)	-	-
At the end of the year	88,553	84,880	52,870	52,870
Amounts include:				
Local listed	22,670	21,317	22,304	22,304
Local unlisted	65,883	63,563	30,566	30,566
	88,553	84,880	52,870	52,870

On the historical cost basis, shares in associates of the Group, would have been included at a cost of €52.9 million (2013: €52.9 million). The fair value of the associated undertaking that is publicly quoted amounted to €26.8 million at 30 September 2014 (2013: €24.3 million). The fair value measurement is a Level 1 input.

Notes to the financial statements 30 September 2014 (continued)

18. INVESTMENTS IN ASSOCIATES (continued)

	Equity Interest		Class	Incorporated in	Nature of Business
	2014	2013			
Name of company	%	%			
Middlesea Insurance 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	
	2014	2013
Name of company	€000	€000
Middlesea Insurance p.l.c.	2,426	3,140
MSV Life p.l.c.	4,801	9,244
	7,227	12,384

*A further 15.54% (2013: 15.54%) is held indirectly via an associated company. Although the Bank has an effective interest of 65.54% (2013: 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 de-facto control and as from financial year 2012 it is being treated as an associate.

The financial statements of the associates are prepared to 31 December. Given that it was impracticable to obtain financial statements to the Group's year end, the published June 2014 interim financial statements were used as a basis to determine the Group's share of results to 30 September 2014.

The registered addresses of the above undertakings are as follows:

Middlesea Insurance p.l.c.	Middlesea House, Floriana FRN 1442, Malta
MSV Life p.l.c.	Pjazza Papa Giovanni XXIII, Floriana FRN 1420, Malta

Summarised financial information extracted from the published condensed financial statements as at 30 June 2014 in respect of the associates:	Associates	Associates
	2014	2013
	€000	€000
Total assets	1,518,143	1,371,045
Total liabilities	1,377,253	1,238,889
Revenues	127,684	104,423
Results for the period	5,933	4,456

	The Group	
	2014	2013
	€000	€000
Share of net assets of associates	88,553	84,880
Share of results of associates	7,227	12,384

Notes to the financial statements 30 September 2014 (continued)

18. INVESTMENTS IN ASSOCIATES (continued)

The share of results of associates 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.

The judgements made by the associates 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 associated company 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.

This valuation assumes a spread of 2% (2013: 2%) between the weighted average projected investment return and the risk adjusted discount factor applied of 7.5% (2013: 7.5%). The calculation also assumes lapse rates varying from 0.5% to 8% per annum (2013: 2% to 10% per annum) and an expense inflation rate of 3.5% (2013: 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 associate 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 associate 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.

19. INVESTMENTS IN SUBSIDIARY COMPANIES

	Equity interest		Class	Incorporated in	Nature of Business
	2014	2013			
Name of company	%	%			
Valletta Fund Management Limited	60	60	Ordinary	Malta	Fund Management
Valletta Fund Services Limited	100	100	Ordinary	Malta	Fund Administration
BOV Investments Limited*	-	100	Ordinary	Malta	Holding Company

	The Bank Equity interest	
	2014	2013
Name of company	€000	€000
Valletta Fund Management Limited	481	481
Valletta Fund Services Limited	749	749
BOV Investments Limited	-	163
	1,230	1,393

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
BOV Investments Limited*	58, Zachary Street, Valletta VLT 1130

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

*BOV Investments Limited was merged into the Bank with effect from 1 October 2013.

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
20. INTANGIBLE ASSETS				
Software				
Cost				
1 October	19,558	15,164	19,558	15,164
Additions	2,349	4,394	2,349	4,394
30 September	21,907	19,558	21,907	19,558
Accumulated amortisation				
1 October	8,063	6,421	8,063	6,421
Charge for the year	2,202	1,642	2,202	1,642
30 September	10,265	8,063	10,265	8,063
Carrying amount at 30 September	11,642	11,495	11,642	11,495

	Land and buildings	IT infrastructure and equipment	Other	Total
	€000	€000	€000	€000
21. PROPERTY, PLANT AND EQUIPMENT				
The Group				
Cost or valuation				
1 October 2012	67,265	12,478	23,423	103,166
Additions	2,540	3,123	2,120	7,783
Disposals	-	-	(69)	(69)
Revaluation	6,703	-	-	6,703
30 September 2013	76,508	15,601	25,474	117,583
Additions	8,074	2,638	1,588	12,300
Disposals	-	-	(83)	(83)
Revaluation	809	-	-	809
30 September 2014	85,391	18,239	26,979	130,609
Comprising:				
At cost	-	18,239	26,979	45,218
At valuation	85,391	-	-	85,391
30 September 2014	85,391	18,239	26,979	130,609
Accumulated depreciation				
1 October 2012	10,932	6,170	16,029	33,131
Provision for the year	828	2,160	1,410	4,398
Disposals	-	-	(69)	(69)
30 September 2013	11,760	8,330	17,370	37,460
Provision for the year	1,067	2,419	1,630	5,116
Disposals	-	-	(83)	(83)
30 September 2014	12,827	10,749	18,917	42,493
Carrying amount at:				
30 September 2013	64,748	7,271	8,104	80,123
30 September 2014	72,564	7,490	8,063	88,117

Notes to the financial statements 30 September 2014 (continued)

21. PROPERTY, PLANT AND EQUIPMENT (continued)

	Land and buildings	IT infrastructure and equipment	Other	Total
The Bank	**€000**	**€000**	**€000**	**€000**
Cost or valuation				
1 October 2012	67,231	11,833	22,026	101,090
Additions	2,540	3,123	2,082	7,745
Disposals	-	-	(69)	(69)
Revaluation	6,703	-	-	6,703
30 September 2013	76,474	14,956	24,039	115,469
Additions	8,074	2,638	1,509	12,221
Disposals	-	-	(83)	(83)
Revaluation	809	-	-	809
30 September 2014	85,357	17,594	25,465	128,416
Comprising:				
At cost	-	17,594	25,465	43,059
At valuation	85,357	-	-	85,357
30 September 2014	85,357	17,594	25,465	128,416
Accumulated depreciation				
1 October 2012	10,844	5,347	15,179	31,370
Provision for the year	828	2,160	1,308	4,296
Disposals	-	-	(69)	(69)
30 September 2013	11,672	7,507	16,418	35,597
Provision for the year	1,067	2,419	1,527	5,013
Disposals	-	-	(82)	(82)
30 September 2014	12,739	9,926	17,863	40,528
Carrying amount at:				
30 September 2013	64,802	7,449	7,621	79,872
30 September 2014	72,618	7,668	7,602	87,888

	The Group		The Bank	
	2014	**2013**	**2014**	**2013**
	€000	**€000**	**€000**	**€000**
Carrying amount of land and buildings occupied for own use	72,564	64,748	72,618	64,802
Future capital expenditure:				
- contracted but not provided for in the financial statements	3,736	3,085	3,736	3,085
- authorised by the directors but not contracted	5,731	6,521	5,731	6,521

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:
2014: Group and Bank €42.9 million (2013: Group and Bank €35.9 million).

Notes to the financial statements 30 September 2014 (continued)

21. PROPERTY, PLANT AND EQUIPMENT (continued)

Property valuations are mainly made 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 2013. Revaluation is effective at 30 September 2014.

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 100/sqm to EUR 500/sqm	The higher the price per square metre the higher the fair value
	Capitalisation rate, ranging from 4.75 to 6%	The higher the capitalisation rate the lower the fair value
Buildings in Residential Area	Price per square metre, ranging from EUR 55/sqm to EUR 165/sqm	The higher the price per square metre the higher the fair value
	Capitalisation rate, ranging from 5.5% to 6.5%	The higher the capitalisation rate the lower the fair value

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
22. DEFERRED TAX				
Deferred taxation is analysed as follows:				
Net deferred tax asset arising on:				
Fair value remeasurement of financial instruments	(2,403)	(381)	(2,403)	(381)
Impairment losses	75,774	64,112	75,774	64,112
Allowance for employee benefits	7,811	8,096	7,811	8,096
Fixed assets	(4,182)	(3,519)	(4,182)	(3,519)
Defined benefit plans	1,060	-	1,060	-
Other temporary differences	490	1,897	490	1,897
	78,550	70,205	78,550	70,205
Deferred tax liability arising on:				
Property revaluation	5,100	5,003	5,100	5,003
23. PREPAYMENTS AND ACCRUED INCOME				
Accrued income	21,487	24,247	21,487	24,247
Prepayments	2,531	968	982	968
	24,018	25,215	22,469	25,215

Notes to the financial statements 30 September 2014 (continued)

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
24. AMOUNTS OWED TO BANKS				
Term deposits	56,533	14,121	56,533	14,121
Repayable on demand	30,046	21,919	30,046	21,919
	86,579	36,040	86,579	36,040
25. AMOUNTS OWED TO CUSTOMERS				
Term deposits	2,479,797	2,460,506	2,479,797	2,460,506
Repayable on demand	4,639,733	3,759,160	4,640,877	3,760,448
	7,119,530	6,219,666	7,120,674	6,220,954
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 2014 is €58.7 million (2013: €58.6 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 2014 is €41.4 million (2013: €40.7 million).

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
27. OTHER LIABILITIES				
Post employment and termination liabilities (see note 35)	25,346	23,132	25,346	23,132
Cash collateral for commitments	19,228	15,401	19,228	15,401
Deposits from companies in formation	6,852	4,238	6,852	4,238
Bills payable	37,933	24,015	37,933	24,015
Accruals and deferred income	8,840	9,005	8,840	9,005
Payment orders outwards	10,968	13,723	10,968	13,723
Other	21,001	19,350	20,901	19,251
	130,168	108,864	130,068	108,765
28. ACCRUALS AND DEFERRED INCOME				
Accrued interest	27,643	29,235	27,174	28,962
29. FINANCIAL LIABILITIES DESIGNATED FOR HEDGE ACCOUNTING				
Derivative financial instruments designated as fair value hedges	36,909	31,229	36,909	31,229
The above comprise over-the-counter interest rate swaps stated at fair value with notional amounts analysed by remaining life as follows:				
- more than 1 year	144,730	141,556	144,730	141,556

Notes to the financial statements 30 September 2014 (continued)

30. SUBORDINATED LIABILITIES

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
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
	120,000	120,000	120,000	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 2014 is €53.5 million (2013: €52.8 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 2014 is €73.2 million (2013: €72.1 million).

31. SHARE CAPITAL

	The Bank	
	2014	2013
	€000	€000
Authorised:		
500,000,000 Ordinary shares of €1.00 each	500,000	500,000
(2013: 500,000,000 Ordinary shares of €1.00 each)		
Issued and paid up:		
330,000,000 Ordinary shares of €1.00 each fully paid	330,000	300,000
(2013: 300,000,000 Ordinary shares of €1.00 each fully paid)		

On 17 January 2014 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 10 shares held, thereby increasing the issued share capital from 300 million shares to 330 million shares, resulting in a paid up capital of €330 million.

On 17 January 2013 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 9 shares held, thereby increasing the issued share capital from 270 million shares to 300 million shares, resulting in a paid up capital of €300 million. On the same date the authorised share capital was increased by €150 million to €500 million.

Notes to the financial statements 30 September 2014 (continued)

	The Group €000	The Bank €000
32. REVALUATION RESERVES		
On land and buildings:		
1 October 2012	17,981	17,951
Property revaluation	6,703	6,703
Deferred tax	(804)	(804)
30 September 2013	23,880	23,850
Property revaluation	809	809
Deferred tax	(97)	(97)
30 September 2014	24,592	24,562
On available-for-sale investments:		
1 October 2012	(4,408)	(4,490)
Fair value adjustments	9,210	9,210
Transfer to profit or loss on disposal	(1,290)	(1,290)
Deferred tax	(2,771)	(2,771)
30 September 2013	741	659
Fair value adjustments	6,613	6,613
Transfer to profit or loss on disposal	(763)	(763)
Deferred tax	(2,047)	(2,047)
30 September 2014	4,544	4,462
Total	29,136	29,024

	The Group		The Bank	
	2014 €000	2013 €000	2014 €000	2013 €000
33. CONTINGENT LIABILITIES				
Acceptances and endorsements	2,642	2,645	2,642	2,645
Guarantees	210,239	191,485	210,239	191,485
Provision for default on forward contracts	10,161	8,350	10,161	8,350
Other contingent liabilities	10,409	11,118	10,409	11,118
	233,451	213,598	233,451	213,598

The majority of contingent liabilities are backed by corresponding obligations from third parties.

34. COMMITMENTS

Documentary credits	76,615	71,196	76,615	71,196
Undrawn formal standby facilities, credit facilities and other commitments to lend	1,537,510	1,093,455	1,537,510	1,093,455
Capital expenditure contracted but not provided for in the financial statements	3,736	3,085	3,736	3,085
Commitments to financial institutions	29,230	22,978	29,230	22,978
	1,647,091	1,190,714	1,647,091	1,190,714

Notes to the financial statements 30 September 2014 (continued)

35. POST EMPLOYMENT AND TERMINATION LIABILITIES

The Bank's and the Group'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 Bank's and the Group's obligation based on the following:
(i) discount rate, determined by reference to market yields at the end of the reporting period on Malta government bonds, used to discount the liability to the net present value
(ii) life expectancy based on the latest publicly available mortality tables,
(iii) the expected terminal salaries and
(iv) the expectation of the respective employees' retirement date. The provision in relation to this plan accounts for 87% (2013 : 85%) of the year end provision for employee and termination benefits in Note 27.

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

The movement in the plans may be analysed as follows:

	The Group and the Bank	
Post Employment and Termination Liabilities	**2014**	**2013**
	€000	**€000**
Present value at 1 October	23,132	24,100
Payments effected	(3,148)	(2,226)
Recognised in profit or loss:		
- Interest expense	927	1,144
- Service cost	8	114
- Terminal benefits	1,398	-
Actuarial gains and losses recognised in other comprehensive income resulting from:		
- Experience adjustments	(178)	-
- Changes in financial assumptions	3,063	-
- Changes in demographic assumptions	144	-
Present value at 30 September	25,346	23,132

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 Bank and the Group in respect of the plan were as follows:

	The Group and the Bank	
	2014	**2013**
Discount rates	2.07%	3.73%
Mortality rates (average age):		
Males	78	78
Females	83	82

Notes to the financial statements 30 September 2014 (continued)

35. POST EMPLOYMENT AND TERMINATION LIABILITIES (continued)

The Group and the Bank are providing sensitivity analyses in connection with each significant actuarial assumption applied in respect of the plan. These analyses are prepared as of the end of the reporting period, showing how the liability would have been affected by hypothetical changes in the relevant actuarial assumptions that were reasonably possible at that date, while holding all other assumptions constant. The analyses 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 analyses, 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 analyses 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 €1.5m (increases by €1.5m)
- 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 €2.6m (decreases by €2.6m).

The weighted average duration of the liability in respect of the plan at 30 September 2014 is 14 years (2013: 15 years).

36. NOTES TO THE CASH FLOW STATEMENTS

	The Group		The Bank	
	2014	2013	2014	2013
	€000	€000	€000	€000
Cash	37,563	33,389	37,563	33,389
Balances with Central Bank of Malta (excluding Reserve Deposit)	-	4,937	-	4,937
Treasury bills (with original maturity of less than 3 months)	26,000	62,990	26,000	62,990
Money at call and short notice	982,847	845,628	982,847	845,628
Amounts owed to banks	(33,907)	(9,841)	(33,907)	(9,841)
Cash and cash equivalents included in the cash flow statement	1,012,503	937,103	1,012,503	937,103
Balances with contractual maturity of more than 3 months	14,468	27,105	14,468	27,105
	1,026,971	964,208	1,026,971	964,208
Equivalent items reported in the statement of financial position:				
Balances with Central Bank of Malta, Treasury bills and cash (excluding Reserve Deposit)	67,562	139,291	67,562	139,291
Loans and advances to banks	1,045,988	860,957	1,045,988	860,957
Amounts owed to banks	(86,579)	(36,040)	(86,579)	(36,040)
	1,026,971	964,208	1,026,971	964,208

Notes to the financial statements 30 September 2014 (continued)

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 associates, the Government of Malta (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 deemed to exercise control, that is, it has the power to govern the financial and operating policies of the entity. These do not include those entities which, while linked to the Government, in the opinion of the Bank, are not controlled by the Government. 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. Transactions between the Bank and its subsidiaries have been eliminated on consolidation.

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

The Group	2014 Related party transactions		2013 Related party transactions	
	€000	% of total	€000	% of total
Interest receivable and similar income: - on loans and advances, balances with Central Bank of Malta and treasury bills				
Associates	30		300	
The Government	1,624		1,469	
Government related entities	16,021		14,052	
Key management personnel	59		45	
Other related parties	769		780	
	18,503	12%	16,646	10%
Interest receivable and similar income: - on debt and other fixed income instruments				
The Government	29,795	50%	32,270	53%
Interest payable				
Associates	2,956		2,280	
The Government	210		258	
Government related entities	240		355	
Key management personnel	10		8	
Other related parties	123		11	
	3,539	4%	2,912	3%
Fee and commission income				
Associates	3,331		2,817	
The Government	60		86	
Government related entities	3,119		2,113	
Key management personnel	5		6	
Other related parties	73		350	
	6,588	10%	5,372	9%
Employee compensation and benefits				
Key management personnel (note 9)	1,454	3%	1,389	3%
General administrative expenses				
Associates	70		72	
Key management personnel	35		25	
Other related parties	110		24	
	215	1%	121	0%

Notes to the financial statements 30 September 2014 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

	2014 Related party transactions €000	2014 % of total	2013 Related party transactions €000	2013 % of total
Movement in impairment allowances				
Associates	(128)		(123)	
The Government	943		870	
Government related entities	128		(8)	
Key management personnel	(2)		(1)	
Other related parties	32		(10)	
	973	5%	728	3%
Balances with Central Bank of Malta treasury bills and cash				
The Government	93,403	71%	161,197	83%
Investments				
The Government	763,647	32%	697,194	42%
Loans and advances to customers				
Associates	-		3,087	
The Government	15,536		9,749	
Government related entities	613,558		453,706	
Key management personnel	3,183		3,632	
Other related parties	17,444		18,603	
	649,721	17%	488,777	13%
Loans and advances to banks				
The Government	293,688	28%	585,658	68%
Impairment allowances				
Associates	-		(64)	
The Government	(973)		(921)	
Government related entities	(227)		(103)	
Key management personnel	(10)		(12)	
Other related parties	(127)		(101)	
	(1,337)	1%	(1,201)	1%
Amounts owed to customers				
Associates	182,912		138,475	
The Government	80,078		87,112	
Government related entities	155,428		62,584	
Key management personnel	1,056		994	
Other related parties	46,516		27,986	
	465,990	7%	317,151	5%
Total Assets less Liabilities				
Associates	(182,912)		(135,452)	
The Government	1,085,223		1,365,765	
Government related entities	457,903		391,019	
Key management personnel	2,117		2,626	
Other related parties	(29,199)		(9,484)	
	1,333,132		1,614,474	

Notes to the financial statements 30 September 2014 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

The Bank	2014 Related party transactions €000	2014 % of total	2013 Related party transactions €000	2013 % of total
Interest receivable and similar income:				
- on loans and advances, balances with Central Bank of Malta and treasury bills				
Associates	30		300	
The Government	1,624		1,064	
Government related entities	16,021		14,052	
Key management personnel	59		45	
Other related parties	769		780	
	18,503	12%	16,241	10%
Interest receivable and similar income:				
- on debt and other fixed income instruments				
The Government	29,795	50%	32,270	53%
Interest payable				
Associates	2,956		2,280	
The Government	210		258	
Government related entities	240		355	
Key management personnel	10		8	
Other related parties	8		8	
	3,424	4%	2,909	3%
Fee and commission income				
Associates	3,331		2,817	
Subsidiaries	2,191		1,927	
The Government	60		86	
Government related entities	3,119		2,113	
Key management personnel	3		6	
Other related parties	47		341	
	8,751	15%	7,290	14%
Dividend income				
Associates	4,815		4,733	
Subsidiaries	2,307		2,308	
	7,122	84%	7,041	89%
Employee compensation and benefits				
Key management personnel (note 9)	1,364	2%	1,293	2%
General administrative expenses				
Associates	70		72	
Key management personnel	29		25	
Other related parties	106		24	
	205	1%	121	0%
Movement in impairment allowances				
Associates	(64)		(123)	
The Government	943		870	
Government related entities	128		(8)	
Key management personnel	(2)		-	
Other related parties	32		(10)	
	1,037	5%	729	3%

Notes to the financial statements 30 September 2014 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

	2014 Related party transactions €000	2014 % of total	2013 Related party transactions €000	2013 % of total
Balances with Central Bank of Malta treasury bills and cash				
The Government	93,403	71%	161,197	83%
Investments				
The Government	763,647	32%	697,194	42%
Loans and advances to customers				
Associates	-		3,087	
The Government	15,536		9,749	
Government related entities	613,558		453,706	
Key management personnel	3,175		3,625	
Other related parties	17,444		18,603	
	649,713	17%	488,770	13%
Loans and advances to banks				
The Government	293,688	28%	585,658	68%
Impairment allowances				
Associates	-		(64)	
The Government	(973)		(921)	
Government related entities	(227)		(103)	
Key management personnel	(10)		(12)	
Other related parties	(127)		(101)	
	(1,337)	1%	(1,201)	1%
Other assets				
Subsidiaries	-	0%	1,140	29%
Amounts owed to customers				
Associates	182,912		138,475	
Subsidiaries	1,144		1,288	
The Government	80,078		87,112	
Government related entities	155,428		62,584	
Key management personnel	1,026		935	
Other related parties	5,937		23,970	
	426,525	6%	314,364	5%
Total Assets less Liabilities				
Associates	(182,912)		(135,452)	
Subsidiaries	(1,144)		(148)	
The Government	1,085,223		1,365,765	
Government related entities	457,903		391,019	
Key management personnel	2,139		2,678	
Other related parties	11,380		(5,468)	
	1,372,589		1,618,394	

Notes to the financial statements 30 September 2014 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

All outstanding balances are secured except for the following:

	The Group and the Bank	
	2014	2013
	€000	€000
Loans and advances to customers:		
- Associates	-	3,087
- Key management personnel	332	404
- Other related parties	623	880
	955	4,371
Details of guarantees received are disclosed below:		
Loans and advances to customers:		
- Amounts guaranteed by The Government	542,979	362,279

	The Group		The Bank	
	Loans and advances	Commitments	Loans and advances	Commitments
	€000	€000	€000	€000
Loans to and commitments on behalf of directors and other key management personnel (including connected persons):				
Directors				
At 1 October 2012	2,051	791	2,051	791
Additions	102	7	102	7
	2,153	798	2,153	798
Less repayments	(143)	(553)	(143)	(553)
At 30 September 2013	2,010	245	2,010	245
Additions	140	220	140	220
	2,150	465	2,150	465
Less repayments	(390)	(10)	(390)	(10)
At 30 September 2014	1,760	455	1,760	455
Other key management personnel (chief officers)				
At 1 October 2012	1,044	14	1,028	14
Additions	661	-	661	-
	1705	14	1689	14
Less repayments	(83)	(6)	(74)	(6)
At 30 September 2013	1,622	8	1,615	8
Additions	97	3	97	3
	1,719	11	1,712	11
Less repayments	(242)	(8)	(243)	(8)
At 30 September 2014	1,477	3	1,469	3

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 2014 (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	
	2014	2013	2014	2013	2014	2013
	€000	€000	€000	€000	€000	€000
Segment net interest income	110,838	117,970	15,165	13,044	126,003	131,014
Segment net commission income	35,927	33,034	20,035	19,079	55,962	52,113
Other segment income	16,278	14,757	11,562	20,243	27,840	35,000
Segment depreciation/amortisation	(4,244)	(3,781)	(3,074)	(2,259)	(7,318)	(6,040)
Other segment costs	(82,012)	(78,795)	(1,614)	(1,584)	(83,626)	(80,379)
Impairment losses	(19,431)	(22,904)	-	(2,691)	(19,431)	(25,595)
Segment operating profit before share of results of associates	57,356	60,281	42,074	45,832	99,430	106,113
Group share of results after tax of associates	-	-	7,227	12,384	7,227	12,384
Common costs					(2,555)	(2,719)
Group profit before tax					104,102	115,778
ASSETS						
Segment total assets	3,934,146	3,754,884	4,078,368	3,240,964	8,012,514	6,995,848
Property, plant and equipment and Intangible assets	62,546	56,546	22,564	22,895	85,110	79,441
Additions to property, plant and equipment and intangible assets	14,503	12,073	146	104	14,649	12,177
Unallocated assets	-	-	-	-	95,965	85,611
Carrying value of associates	-	-	88,553	84,880	88,553	84,880
Total Assets					8,296,791	7,257,957
LIABILITIES						
Segment total liabilities	7,147,172	6,262,914	399,982	304,271	7,547,154	6,567,185
Unallocated liabilities					135,168	113,768
Total Liabilities					7,682,322	6,680,953

The revenue which is reported above represents revenue generated from external customers. There were no inter-segment sales during the year (2013: 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 associates, 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 2014 (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. In this respect, the Bank has set up a Credit Risk Monitoring Unit (CRMU) as a separate department within the Risk Management function.

Credit grading and monitoring systems are in place to accommodate the early identification and management of deterioration in loan quality. In addition, the credit management process is underpinned by an independent system of credit review.

Credit risk analysis is carried out on two levels: the single name; and the bank's lending portfolio review. The Bank uses a number of tools to limit its exposure to undue credit risk. These include the application of:

- High-level credit policies designed to ensure a balanced and managed approach to the identification and mitigation of credit risk;
- Lending guidelines defining the responsibilities of lending officers that seek to provide a disciplined and focused benchmark for credit decisions;
- Independent reviews of credit exposures;
- Sector caps, encompassing both industry and specific product types, to communicate the Board's risk appetite for specific types of business;
- Establishment and maintenance of large exposures and provisioning policies in accordance with regulatory reporting requirements; and
- Communication and provision of general guidance on all credit-related risk issues, including regulatory changes to promote consistent and best practice throughout the Bank.

Where possible the Bank aims to reduce and control risk concentrations. Broadly stated, concentration results when the Bank has a high level of exposure to a single or related group of borrowers, credit exposures secured by a single security, or credit exposures with common characteristics within an industry, such that adverse developments in this exposure would be damaging to the Bank.

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

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

risk concentrations. The CEO and the Board of Directors are regularly informed on the concentration of the Bank's portfolio through reports prepared at least on a quarterly basis.

Presently there is an across the board limit per industry/economic sector on the Group's Loan Portfolio. This is being evolved through the introduction of a more risk-sensitive approach by the setting up of specific limits for each industry/sector. This approach should optimise the risk return trade-off of the Bank's loan portfolio. To address concentration risk in any one particular sector, the loan portfolio is also being monitored by computing the Herfindahl-Hirschman Index and the Lorenz Curve as part of regular credit risk reporting.

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

	The Group	
	2014	2013
	€000	€000
Agriculture	7,877	8,202
Fishing	812	1,186
Mining and quarrying	3,187	3,244
Manufacturing	148,974	151,796
Electricity, gas, steam and air conditioning supply	173,093	78,446
Water supply, sewerage waste management and remediation activities	31,491	31,762
Construction	291,370	305,460
Wholesale and retail trade	375,691	387,474
Transportation and storage	311,804	297,422
Accommodation and food service activities	244,612	277,592
Information and communication	38,368	43,249
Financial and insurance activities	313,438	316,083
Real estate activities	232,118	184,453
Professional, scientific and technical activities	22,749	22,441
Administrative and support service activities	59,627	62,860
Public administration and defence, compulsory social security	17,567	10,199
Education	13,579	13,361
Human health and social work activities	17,950	18,597
Arts, entertainment and recreation	42,955	49,801
Other services activities	17,502	18,925
Households and individuals	1,756,218	1,624,712
Loans and advances to customers	4,120,982	3,907,265
Loans and advances to banks	1,045,988	860,957
	5,166,970	4,768,222

(ii) Other financial assets

The credit risk in respect of other financial assets is mitigated through limits set in the Treasury Management Policy. The Bank assigns limits on the level of credit risk undertaken in relation to any single counterparty or sovereign exposure in accordance with external ratings based on Fitch's ratings or on those of other major rating agencies.

Changes in credit ratings are monitored on a daily basis and are subject to frequent review, when considered necessary. The limits on the level of credit risk are reviewed consistently and approved by the Board of Directors at regular intervals. Actual exposures are monitored against limits on an on going basis. The Bank enters into security transactions only with such authorised counterparties and it invests only in securities or paper with credit quality within specific parameters stated in the Treasury Management Policy.

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

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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% of market value. 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 revaluation process on immovable type of property is currently being enhanced further to ensure that the collateral items always reflect the prevailing market conditions. Two property price indices are currently being developed (one for residential and another for commercial type of property) with the aim of revaluing security items on an annual basis in line with price movements. In line with local regulation guidelines these statistical models are to be used to monitor the property values on a portfolio level.

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

The table below shows the financial effect and main types of collateral held against the Group's customer loan exposures:

The Group	Loans and advances to customers	Undrawn credit facilities and other commitments to lend
As at 30 September 2014	**€000**	**€000**
Loans collateralised by:		
Prime bank guarantees	6,542	49,876
Cash or quasi cash	116,121	36,826
Guarantees and/or letters of comfort issued by the Malta Government, the Central Bank of Malta or Public agencies	543,544	172,374
Guarantees by prime institutions	551	175
Residential property	1,424,156	451,644
Commercial property	1,084,222	343,840
Personal guarantees and others	214,486	68,020
	3,389,622	**1,122,755**

The Group	Loans and advances to customers	Undrawn credit facilities and other commitments to lend
As at 30 September 2013	**€000**	**€000**
Loans collateralised by:		
Prime bank guarantees	3,072	47,411
Cash or quasi cash	113,057	25,555
Guarantees and/or letters of comfort issued by the Malta Government, the Central Bank of Malta or public agencies	346,836	78,397
Guarantees by prime institutions	598	135
Residential property	1,284,611	290,373
Commercial property	1,204,020	272,156
Personal guarantees and others	232,881	52,640
	3,185,075	**766,667**

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 2014 (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 2014					
AAA	-	130,509	25,163	749	156,421
AA- to AA+	-	528,965	71,971	542	601,478
A- to A+	-	888,948	385,073	11,819	1,285,840
Lower than A-	93,403	1,251,308	517,679	369	1,862,759
Unrated	-	13,812	46,102	4,690	64,604
	93,403	2,813,542	1,045,988	18,169	3,971,102
As at 30 September 2013					
AAA	-	159,684	305	132	160,121
AA- to AA+	-	349,738	23,667	271	373,676
A- to A+	-	394,568	204,180	6,790	605,538
Lower than A-	161,198	1,188,643	618,262	21	1,968,124
Unrated	-	14,269	14,543	4,197	33,009
	161,198	2,106,902	860,957	11,411	3,140,468

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

	The Group			
Total Gross Exposures	Total 2014 €000	of which Forborne 2014 €000	Total 2013 €000	of which Forborne 2013 €000
Performing				
Neither past due nor impaired	3,689,343	128,029	3,513,026	142,036
Past due < 90days, but not impaired	40,864	1,243	47,718	5,159
	3,730,207	129,272	3,560,744	147,195
Non performing				
Past due > 90days, but not impaired	107,738	75,929	106,566	67,151
Impaired	283,037	163,255	239,897	139,006
	390,775	239,184	346,463	206,157
Total gross/forborne exposures	4,120,982	368,456	3,907,207	353,352

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

	The Group			
Impairment Allowances on Total/Forborne Exposures	**Total**	**of which Forborne**	**Total**	**of which Forborne**
	2014	**2014**	**2013**	**2013**
	€000	**€000**	**€000**	**€000**
Performing				
Neither past due nor impaired	42,723	6,308	36,915	6,339
Past due < 90days, but not impaired	2,209	47	2,314	210
	44,932	6,355	39,229	6,549
Non performing				
Past due > 90days, but not impaired	14,357	4,887	10,725	7,880
Impaired	151,565	70,005	127,582	65,783
	165,922	74,892	138,307	73,663
Total Allowances	210,854	81,247	177,536	80,212

Net Carrying Amounts of Total/Forborne Exposures				
Performing				
Neither past due nor impaired	3,646,620	121,721	3,476,111	135,697
Past due < 90days, but not impaired	38,655	1,196	45,404	4,949
	3,685,275	122,917	3,521,515	140,646
Non performing				
Past due > 90days, but not impaired	93,381	71,042	95,841	59,271
Impaired	131,472	93,250	112,315	73,223
	224,853	164,292	208,156	132,494
Total Carrying Amounts	3,910,128	287,209	3,729,671	273,140

Interest income recognised during the year 2014 in respect of forborne assets amounts to €20.2 million (2013: €19.6 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**	**Refinancing**	**Modification in Terms**	**Refinancing**
	2014	2014	2013	2013
	€000	€000	€000	€000
Performing				
Personal	6,026	1,208	6,880	812
Business	115,022	7,016	137,218	2,285
	121,048	8,224	144,098	3,097
Non performing				
Personal	17,295	2,396	16,393	1,210
Business	210,636	8,857	187,556	998
	227,931	11,253	203,949	2,208

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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

	Loans & Advances	
	2014	2013
	€000	€000
Neither past due nor impaired:		
Regular	3,316,637	3,121,391
Watch list	293,029	274,315
Sub-Standard	79,677	117,320
	3,689,343	3,513,026

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

Past due but not impaired:		
Past due up to 29 days	14,363	22,808
Past due 30 - 59 days	16,471	15,635
Past due 60 - 89 days	10,030	9,275
	40,864	47,718

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	98,379	113,461
Business	184,658	126,436
	283,037	239,897

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

	2014	2013
	Loans & Advances	Loans & Advances
	€000	€000
1 October	353,352	349,638
Additions	75,827	19,168
Retired from forborne	(60,723)	(15,454)
30 September	368,456	353,352

Notes to the financial statements 30 September 2014 (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
	2014	2014	2013	2013
	€000	€000	€000	€000
Change in allowances for uncollectability:				
At 1 October	127,582	49,954	98,260	48,649
Additions	39,431	15,242	46,320	6,534
Reversals	(15,448)	(5,907)	(16,998)	(5,229)
	23,983	9,335	29,322	1,305
At 30 September	151,565	59,289	127,582	49,954

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 nature and exposure in relation to selected sovereign states by financial asset category of sovereign debt

	The Group				
	Designated at FVTPL	Held-to-Maturity			
	Carrying amount	Gross Carrying amount	Cumulative impairment losses	Net Carrying amount	Fair Value
As at 30 September 2014	€000	€000	€000	€000	€000
Country					
Greece	62	-	-	-	-
Ireland	5,762	-	-	-	-
Italy	2,201	13,992	-	13,992	13,996
Portugal	5,202	-	-	-	-
Spain	6,647	3,948	-	3,948	3,886
	19,874	17,940	-	17,940	17,882
As at 30 September 2013					
Country					
Greece	-	-	-	-	-
Ireland	-	6,997	-	6,997	7,070
Italy	-	2,002	-	2,002	2,033
Portugal	2,991	-	-	-	-
Spain	-	1,999	-	1,999	2,021
	2,991	10,998	-	10,998	11,124

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.2.4 Debt securities - sovereign debt (continued)

The movement in profit or loss and other comprehensive income in relation to selected sovereign debt

	The Group		
	Designated at FVTPL	Held-to- Maturity	
	Fair value movement	Interest income	Impairment reversal
As at 30 September 2014	**€000**	**€000**	**€000**
Country			
Greece	62	-	-
Ireland	812	-	-
Italy	11	-	-
Portugal	31	-	-
Spain	212	4	-
	1,128	4	-
As at 30 September 2013			
Country			
Greece	7	-	-
Ireland	-	280	-
Italy	-	70	-
Portugal	66	-	-
Spain	-	91	-
Cyprus	61	25	32
	134	466	32

The contractual maturity of the selected sovereign debt

	The Group	
	Within 1 year	Over 1 year
As at 30 September 2014	**€000**	**€000**
Country		
Greece	-	62
Ireland	-	5,762
Italy	13,992	2,201
Portugal	3,004	2,198
Spain	3,897	6,698
	20,893	16,921
As at 30 September 2013		
Country		
Ireland	6,997	-
Italy	2,002	-
Portugal	-	2,991
Spain	1,999	-
	10,998	2,991

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.3 Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from an inability to sell a financial asset quickly at close to its fair value. The Group monitors and manages this risk by maintaining sufficient cash and, where possible, financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs. The Group is exposed to daily calls on its available cash resources from overnight deposits, current and call deposits, maturing term deposits, loan drawdowns, guarantees and from margin and other calls on cash-settled derivatives. In order to ensure that maturing funds are always available to meet expected demand for cash, the Board sets parameters within which maturities of assets and liabilities may be mismatched. Unmatched positions potentially enhance profitability, but also increase the risk of losses. In addition, the Group manages its risk to a shortage of funds by monitoring forecast and actual cashflows, by monitoring the availability of raising funds to meet commitments associated with financial instruments and by holding financial assets which are expected to generate cash inflows that will be available to meet cash outflows on liabilities.

The table below analyses Group financial liabilities into relevant maturity groupings, based on the remaining period at the reporting date to the contractual maturity date. The balances in this table will not agree directly to the balances in the statement of financial position as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments. Furthermore, loan commitments do not meet the criteria for recognition in the statement of financial position.

Financial liabilities at fair value through profit or loss and those designated for hedge accounting, disclosed below, represent amounts for which net cash flows are exchanged.

	Due within 3 months	Due between 3 & 12 months	Due between 1 & 5 years	Due after 5 years	Total outflow
	€000	€000	€000	€000	€000
The Group					
At 30 September 2014					
Financial liabilities at fair value through profit or loss	3,297	4,625	16,059	4,647	28,628
Amounts owed to banks	31,041	10,024	15,599	-	56,664
Amounts owed to customers	5,599,631	1,160,923	397,786	2,147	7,160,487
Debt securities in issue	850	3,509	72,837	40,850	118,046
Subordinated liabilities	1,338	4,698	74,140	71,680	151,856
Financial liabilities designated for hedge accounting	2,764	4,532	13,397	15,671	36,364
Other financial liabilities	140,566	11,222	8,216	16,456	176,460
	5,779,487	**1,199,533**	**598,034**	**151,451**	**7,728,505**
Loan commitments	1,537,510				
The Group					
At 30 September 2013					
Financial liabilities at fair value through profit or loss	4,708	7,797	17,363	4,828	34,696
Amounts owed to banks	14,122	-	-	-	14,122
Amounts owed to customers	4,600,219	1,278,826	403,380	2,635	6,285,060
Debt securities in issue	850	3,509	72,837	40,850	118,046
Subordinated liabilities	1,338	4,698	24,140	127,715	157,891
Financial liabilities designated for hedge accounting	3,188	5,476	12,316	8,920	29,900
Other financial liabilities	105,809	12,729	12,230	18,103	148,871
	4,730,234	**1,313,035**	**542,266**	**203,051**	**6,788,586**
Loan commitments	1,093,455				

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

Assets available to meet these liabilities, and to cover outstanding commitments, include balances with Central Bank of Malta, treasury bills and cash, cheques in course of collection, loans to banks and to customers and marketable securities and undrawn credit lines.

The table below analyses the assets and liabilities that are recognised in the statement of financial position into relevant maturity groupings, based on the remaining period at the reporting date to their contractual maturity date.

	Less than 3 months	Between 3 months and 1 year	Between 1 and 5 years	More than 5 years	Other	Total
	€000	€000	€000	€000	€000	€000
The Group						
At 30 September 2014						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	29,999	-	-	-	100,967	**130,966**
Fair value through profit or loss						
- Debt and other fixed income instruments	46,989	47,306	204,865	93,088	-	**392,248**
- Equity and other non-fixed income instruments	-	-	-	-	68,761	**68,761**
- Loans and advances	-	-	-	48,596	-	**48,596**
- Derivative financial instruments	8,012	2,951	7,206	-	-	**18,169**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	4,856	1,121	77,269	207,480	-	**290,726**
- held-to-maturity	158,094	282,150	1,468,674	221,649	-	**2,130,567**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	944	**944**
Loans and advances to banks	986,784	33,825	-	-	25,379	**1,045,988**
Loans and advances to customers	638,867	127,296	407,464	2,687,905	-	**3,861,532**
Investments in associates	-	-	-	-	88,553	**88,553**
Other assets	-	-	-	-	219,741	**219,741**
	1,873,601	**494,649**	**2,165,478**	**3,258,718**	**504,345**	**8,296,791**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	14,213	3,858	12,801	14,031	-	**44,903**
Amounts owed to banks	68,069	18,510	-	-	-	**86,579**
Amounts owed to customers	5,607,588	1,143,448	368,488	6	-	**7,119,530**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	179,001	**179,001**
Financial liabilities held for hedging	-	-	1,548	35,361	-	**36,909**
Subordinated liabilities	-	-	50,000	70,000	-	**120,000**
Non-controlling interest	-	-	-	-	1,100	**1,100**
Equity holders of the Bank	-	-	-	-	613,369	**613,369**
	5,689,870	**1,165,816**	**432,837**	**214,798**	**793,470**	**8,296,791**

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

	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	Total €000
The Group						
At 30 September 2013						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	89,983	10,984	-	-	93,620	**194,587**
Fair value through profit or loss						
- Debt and other fixed income instruments	28,971	115,904	215,370	80,609	972	**441,826**
- Equity and other non-fixed income instruments	-	-	-	-	66,362	**66,362**
- Loans and advances	-	-	-	61,932	-	**61,932**
- Derivative financial instruments	2,914	2,066	579	5,852	-	**11,411**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	6,287	45,343	80,345	84,198	96,490	**312,663**
- held-to-maturity	57,853	229,544	877,931	187,085	-	**1,352,413**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	744	**744**
Loans and advances to banks	841,820	-	-	-	19,137	**860,957**
Loans and advances to customers	610,734	93,645	436,147	2,527,213	-	**3,667,739**
Investments in associates	-	-	-	-	84,880	**84,880**
Other assets	-	-	-	-	202,444	**202,444**
	1,638,562	**497,486**	**1,610,372**	**2,946,889**	**564,649**	**7,257,958**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	3,493	4,212	7,607	15,507	-	**30,819**
Amounts owed to banks	36,040	-	-	-	-	**36,040**
Amounts owed to customers	4,597,491	1,251,108	371,067	-	-	**6,219,666**
Debt securities in issue	-	-	55,400	40,000	-	**95,400**
Other liabilities	-	-	-	-	147,799	**147,799**
Financial liabilities held for hedging		1,181	2,308	27,740	-	**31,229**
Subordinated liabilities	-	-	-	120,000	-	**120,000**
Non-controlling interest	-	-	-	-	661	**661**
Shareholders' funds	-	-	-	-	576,344	**576,344**
	4,637,024	**1,256,501**	**436,382**	**203,247**	**724,804**	**7,257,958**

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

The Bank	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	Total €000
At 30 September 2014						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	29,999	-	-	-	100,967	**130,966**
Fair value assets through profit or loss						
- Debt and other fixed income instruments	46,989	47,306	204,865	93,088	-	**392,248**
- Equity and other non- fixed income instruments	-	-	-	-	64,467	**64,467**
- Loans and advances	-	-	-	48,596	-	**48,596**
- Derivative financial instruments	8,012	2,951	7,206	-	-	**18,169**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	4,856	1,121	77,269	207,480	-	**290,726**
- held-to-maturity	158,094	282,150	1,468,674	221,649	-	**2,130,567**
- Equity and other non-fixed income instruments-available-for-sale	-	-	-	-	944	**944**
Loans and advances to banks	986,784	33,825	-	-	25,379	**1,045,988**
Loans and advances to customers	638,867	127,296	407,464	2,687,905	-	**3,861,532**
Investments in associates and subsidiaries	-	-	-	-	54,100	**54,100**
Other assets	-	-	-	-	217,963	**217,963**
	1,873,601	**494,649**	**2,165,478**	**3,258,718**	**463,820**	**8,256,266**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	14,213	3,858	12,801	14,031	-	**44,903**
Amounts owed to banks	68,069	18,510	-	-	-	**86,579**
Amounts owed to customers	5,608,732	1,143,448	368,488	6	-	**7,120,674**
Debt securities in issue	-	-	95,400	-	-	**95,400**
Other liabilities	-	-	-	-	178,276	**178,276**
Financial liabilities held for hedging	-	-	1,548	35,361	-	**36,909**
Subordinated liabilities	-	-	50,000	70,000	-	**120,000**
Equity holders of the Bank	-	-	-	-	573,525	**573,525**
	5,691,014	**1,165,816**	**528,237**	**119,398**	**751,801**	**8,256,266**

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

The Bank	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	Total €000
At 30 September 2013						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	89,983	10,984	-	-	93,620	**194,587**
Fair value assets through profit or loss						
- Debt and other fixed income instruments	28,971	115,904	215,370	80,609	972	**441,826**
- Equity and other non- fixed income instruments	-	-	-	-	63,522	**63,522**
- Loans and advances	-	-	-	61,932	-	**61,932**
- Derivative financial instruments	2,914	2,066	579	5,852	-	**11,411**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	6,287	45,343	80,345	84,198	96,490	**312,663**
- held-to-maturity	57,853	229,544	877,931	187,085	-	**1,352,413**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	744	**744**
Loans and advances to banks	841,820	-	-	-	19,137	**860,957**
Loans and advances to customers	610,734	93,645	436,147	2,527,213	-	**3,667,739**
Investments in associates and subsidiaries	-	-	-	-	54,263	**54,263**
Other assets	-	-	-	-	201,262	**201,262**
	1,638,562	**497,486**	**1,610,372**	**2,946,889**	**530,010**	**7,223,319**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	3,493	4,212	7,607	15,507	-	**30,819**
Amounts owed to banks	36,040	-	-	-	-	**36,040**
Amounts owed to customers	4,598,779	1,251,108	371,067	-	-	**6,220,954**
Debt securities in issue	-	-	55,400	40,000	-	**95,400**
Other liabilities	-	-	-	-	147,795	**147,795**
Financial liabilities held for hedging	-	1,181	2,308	27,740	-	**31,229**
Subordinated liabilities	-	-	-	120,000	-	**120,000**
Equity holders of the Bank	-	-	-	-	541,082	**541,082**
	4,638,312	**1,256,501**	**436,382**	**203,247**	**688,877**	**7,223,319**

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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: currency risk, interest rate 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 at least annually by Financial Markets & Investments in co-ordination with Market Risk Unit and Finance Department and is approved by the Asset and Liability Management Committee (ALCO) and the Board of Directors. The individual members of the executive committee ensure that market risk appetite is further delegated to an appropriate level within their areas of responsibility.

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 analyses 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 analysis 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 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, in response to a parallel shift in yields of 100 basis points under the baseline scenario. In the case of the negative scenario, the Bank estimates a 200 basis point increase in yields. 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.

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.

Modified Duration	Baseline	Negative
Tier 1 as at end September 2014 is 11.7%	Change in Tier 1	Change in Tier 1
Parallel shift in yields on the investment portfolio	-1.2%	-2.40%
Tier 1 as at end September 2013 is 11.7%	Change in Tier 1	Change in Tier 1
Parallel shift in yields on the investment portfolio	-1.14%	-2.29%

This entails a parallel shift of 100bps under the baseline and 200bps under the negative.

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

(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 2014 and 2013 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. As at 30 September 2014, the impact on economic value is estimated at 0.66% (2013: 1.89%).

	2014	2013
The Group	**€000**	**€000**
Impact on capital	3,796	11,180

(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:

	2014	2013
The Group	**€000**	**€000**
Net effect on Interest Income for 12 months	10,960	8,638

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (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	84,404	8,999	-	-	37,563	**130,966**
Fair value assets through profit or loss						
- Debt and other fixed income instruments	58,679	99,986	36,419	195,535	1,629	**392,248**
- Equity and other non-fixed income instruments	-	-	-	-	68,761	**68,761**
- Loans and advances	48,596	-	-	-	-	**48,596**
- Derivative financial instruments	-	4,220	446	-	13,503	**18,169**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	-	4,856	1,121	258,966	25,783	**290,726**
- held-to-maturity	410,934	857,653	165,084	692,944	3,952	**2,130,567**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	944	**944**
Loans and advances to banks	480,043	212,968	33,825	-	319,152	**1,045,988**
Loans and advances to customers	3,809,773	2,520	22,999	26,240	-	**3,861,532**
Investments in associates	-	-	-	-	88,553	**88,553**
Other assets	-	-	-	-	219,741	**219,741**
Total 2014	**4,892,429**	**1,191,202**	**259,894**	**1,173,685**	**779,581**	**8,296,791**
Total 2013	4,822,909	506,281	264,639	1,165,984	498,145	7,257,958
LIABILITIES and EQUITY						
Financial liabilities at fair value through profit or loss	4,797	8,291	11,511	-	20,304	**44,903**
Amounts owed to banks	11,180	6,282	18,409	20,662	30,046	**86,579**
Amounts owed to customers	4,243,608	419,742	1,140,772	384,938	930,470	**7,119,530**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	179,001	**179,001**
Financial liabilities held for hedging	220	20,042	16,647	-	-	**36,909**
Subordinated liabilities	-	-	-	120,000	-	**120,000**
Non-controlling interest	-	-	-	-	1,100	**1,100**
Equity holders of the Bank	-	-	-	-	613,369	**613,369**
Total 2014	**4,259,805**	**454,357**	**1,187,339**	**621,000**	**1,774,290**	**8,296,791**
Total 2013	3,602,812	434,249	1,255,047	614,854	1,350,996	7,257,958
Interest rate swaps - 2014	**85,379**	**214,659**	**124,589**	**(424,627)**	-	
Interest rate swaps - 2013	31,753	186,466	108,484	(326,703)	-	
Gap - 2014	**718,003**	**951,504**	**(802,857)**	**128,059**	**(994,709)**	
Gap - 2013	1,251,850	258,498	(881,924)	224,427	(852,851)	
Cumulative Gap - 2014	**718,003**	**1,669,507**	**866,650**	**994,709**	**-**	
Cumulative Gap - 2013	1,251,850	1,510,348	628,424	852,851	-	

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (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.

	2014 Euro €000	2014 Other Currencies €000	2014 Total €000	2013 Euro €000	2013 Other Currencies €000	2013 Total €000
The Group						
Assets						
Balances with Central Bank of Malta treasury bills and cash	127,570	3,396	**130,966**	192,087	2,500	**194,587**
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	310,175	82,073	**392,248**	334,702	107,124	**441,826**
- Equity and other non-fixed income instruments	57,600	11,161	**68,761**	64,740	1,622	**66,362**
Loans and advances	48,596	-	**48,596**	61,932	-	**61,932**
- Derivative financial instruments	2,335	15,834	**18,169**	2,693	8,718	**11,411**
- Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	195,258	95,468	**290,726**	236,278	76,385	**312,663**
- held-to-maturity	1,070,124	1,060,443	**2,130,567**	704,559	647,854	**1,352,413**
- Equity and other non-fixed income instruments						
- available-for-sale	944	-	**944**	744	-	**744**
Loans and advances to banks	801,757	244,231	**1,045,988**	646,451	214,506	**860,957**
Loans and advances to customers	3,772,551	88,981	**3,861,532**	3,602,958	64,781	**3,667,739**
Other assets	301,344	6,951	**308,295**	280,773	6,551	**287,324**
	6,688,253	**1,608,538**	**8,296,791**	**6,127,917**	**1,130,041**	**7,257,958**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	22,616	22,287	**44,903**	21,615	9,204	**30,819**
Amounts owed to banks	60,119	26,460	**86,579**	18,465	17,575	**36,040**
Amounts owed to customers	5,949,436	1,170,094	**7,119,530**	5,238,564	981,102	**6,219,666**
Debt securities in issue	95,400	-	**95,400**	95,400	-	**95,400**
Other liabilities	171,508	7,493	**179,001**	134,992	12,807	**147,799**
Financial liabilities held for hedging	17,228	19,681	**36,909**	14,079	17,150	**31,229**
Subordinated liabilities	120,000	-	**120,000**	120,000	-	**120,000**
Equity	612,247	2,222	**614,469**	584,578	(7,573)	**577,005**
	7,048,554	**1,248,237**	**8,296,791**	**6,227,693**	**1,030,265**	**7,257,958**

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 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.5 Transferred financial assets that are not derecognised in their entirety

	The Group and the Bank	
	2014	2013
	€000	€000
Debt securities classified as		
- available-for-sale	-	-
- held-to-maturity	30,944	-
- fair value through profit or loss	-	-
	30,944	-
Amounts owed to banks	30,944	-

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 Bank and the Group 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 note 1.3 and note 1.22.2 to the Financial Statements.

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. 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.

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.

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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.

The following table provides an analysis of the bases described above which have been deployed for valuing financial assets and financial liabilities measured at fair value in the financial statements.

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				
30 September 2014				
Assets				
Financial assets at fair value through profit or loss				
- debt and other fixed income instruments	384,671	7,577	-	392,248
- equity and other non-fixed income instruments	48,681	13,876	6,204	68,761
- loans and advances	-	48,596	-	48,596
- derivative financial instruments	-	18,169	-	18,169
Investments				
Debt and other fixed income instruments				
- available-for-sale	219,057	71,669	-	290,726
	652,409	**159,887**	**6,204**	**818,500**
Liabilities				
Financial liabilities at fair value through profit or loss				
- derivative financial instruments	-	44,903	-	44,903
Financial liabilities designated for hedge accounting				-
- derivative financial instruments	-	36,909	-	36,909
	-	**81,812**	**-**	**81,812**

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (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				
30 September 2013				
Assets				
Financial assets at fair value through profit or loss				
- debt and other fixed income instruments	419,169	22,657	-	441,826
- equity and other non-fixed income instruments	66,362	-	-	66,362
- loans and advances	-	61,932	-	61,932
- derivative financial instruments	-	11,411	-	11,411
Investments				
Debt and other fixed income instruments				
- available-for-sale	252,006	60,657	-	312,663
	737,537	156,657	-	894,194
Liabilities				
Financial liabilities at fair value through profit or loss				
- derivative financial instruments	-	30,819	-	30,819
Financial liabilities designated for hedge accounting				
- derivative financial instruments	-	31,229	-	31,229
	-	62,048	-	62,048

During the year under review financial assets at fair value through profit or loss amounting to €22.7 million were transferred from Level 2 to Level 1(2013: €60.2 million); €3.9 million were transferred from Level 1 to Level 2 (2013: €2.8 million) and €3.6m were transferred from Level 1 to Level 3. The transfer from Level 2 to Level 1 was due to securities which had quoted prices on active markets as at 30 September 2014 and the securities transferred from Level 1 to Level 2 were those that did not have a quoted price in active markets as at the same date.

Financial instruments with a carrying amount of €3.6m were transferred from Level 1 to Level 3 because of a lack of a quoted price in an active market and a lack of observable market data.

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 flnancial Instruments at fair value through profit or loss was effected.

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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, which are not deemed to differ materially from their fair value.

The carrying value approximates the fair value in the case of loans which are repriceable at the Group's discretion. These loans constitute a significant element of the total loan portfolio.

(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.

The following table provides an analysis of financial instruments that are not measured subsequent to initial recogntion at fair value (other than investments in associates and subsidiary undertakings) grouped into Levels 1 to 3.

Bases of valuing financial assets and liabilities measured at fair value

	Fair value measurement				Carrying
	Level 1 €000	**Level 2 €000**	**Level 3 €000**	**Total €000**	**Amount €000**
2014					
Financial assets					
Held-to-maturity investments	1,811,749	374,776	-	2,186,525	2,130,567
Loans and advances to customers	-	3,861,532	-	3,861,532	3,861,532
Loans and advances to banks	-	1,045,988	-	1,045,888	1,045,988
Balances with Central Bank	-	63,404	-	63,404	63,404
Treasury Bills	29,999	-	-	29,999	29,999
Total	1,841,748	5,345,700	-	7,187,448	7,131,490
Financial liabilities					
Amounts owed to banks	-	86,579	-	86,579	86,579
Amounts owed to customers	-	7,119,530	-	7,119,530	7,119,530
Debt securities in issue	100,124	-	-	100,124	95,400
Subordinated liabilities	126,692	-	-	126,692	120,000
Other financial liabilities	-	-	-	-	-
Total	226,816	7,206,109	-	7,432,925	7,421,509

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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
2014					
Opening balance	-	-	-	-	-
Total gains or losses:					
- in profit or loss	-	(1,060,572)	-	-	(1,060,572)
Purchases	-	3,699,636	-	-	3,699,636
Transfers	-	3,565,000	-	-	3,565,000
Closing balance	-	6,204,064	-	-	6,204,064

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 cover in Pillar I. The Board submitted the latest ICAAP capital document to the MFSA in May 2014.

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, the Group has complied with the externally imposed capital requirements.

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

The following table shows the components and basis of calculation of the Group's and the Bank's capital adequacy ratios.

	The Group €000	The Bank €000
Own funds		
Tier 1		
- Paid up capital instruments	330,000	330,000
- Share premium	988	988
- Retained earnings	196,451	190,533
- Accumulated other comprehensive income	4,463	4,463
- Other reserves	24,561	24,562
- Funds for general banking risk	3,081	3,081
- Minority interests	1,101	-
- Deductions:		
Other intangible assets	(11,642)	(11,642)
Deferred tax assets that rely on future profitability and arise from temporary differences	(22,620)	(23,645)
Amount exceeding the 17.65% threshold	(13,144)	(12,903)
Other transitional adjustments	(11,670)	(12,029)
Additional adjustments due to Article 3 CRR	(37,537)	(37,537)
Total Tier 1 Capital	464,032	455,871
Tier 2		
- Capital instruments and subordinated loans	117,096	117,096
- Deductions:		
Other transitional adjustments	(5,593)	(5,593)
Total Tier 2 Capital	111,503	111,503
Total Own Funds	575,535	567,374

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

	The Group		The Bank	
	Face Value €000	Risk Weighted Amounts €000	Face Value €000	Risk Weighted Amounts €000
Assets				
Balances with the Central Bank of Malta, treasury bills and cash	130,966	-	130,966	-
Financial assets at fair value through profit or loss	527,775	255,714	523,481	251,421
Investments	2,422,237	575,695	2,422,237	575,695
Loans and advances to banks	1,045,988	144,901	1,045,988	144,901
Loans and advances to customers	3,861,532	1,904,951	3,861,532	1,904,951
Other assets	308,295	377,755	272,063	373,359
	8,296,793	3,259,016	8,256,267	3,250,327
Off-Balance Sheet Items	-	297,934	-	297,934
Operational Risk		397,105		384,320
Foreign Exchange Risk		786		786
Total Risk Exposure for CVA		20,783		20,783
Total risk weighted assets		3,975,624		3,954,150
Capital Adequacy Ratio*				
30 September 2014				
Tier 1 Ratio		11.7%		11.5%
Total Capital Ratio		14.5%		14.3%
30 September 2013				
Tier 1 Ratio		11.7%		11.6%
Total Capital Ratio		16.5%		16.4%

* September 2014 Capital Ratios are based on CRD IV whereas September 2013 Capital Ratios are based on CRD III.

Notes to the financial statements 30 September 2014 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

Note 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 (Cap. 459 of the 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	
	2014	2013
	€000	€000
Derivative financial assets		
Gross amounts of recognised financial assets	18,169	11,411
Gross amounts of recognised financial liabilities set off in the statement of financial position	-	-
Net amounts of financial assets presented in the statement of financial position	18,169	11,411
Related amounts not set off in the statement of financial position:		
Financial instruments	(18,169)	(11,411)
Financial collateral received	-	-
Net amount	-	-
Derivative financial liabilities		
Gross amounts of recognised financial liabilities	81,812	62,048
Gross amounts of recognised financial assets set off in the statement of financial position	-	-
Net amounts of financial liabilties presented in the statement of financial position	81,812	62,048
Related amounts not set off in the statement of financial position:		
Financial instruments	(18,169)	(11,411)
Financial collateral pledged	(51,468)	(49,293)
Net amount	12,175	1,344

Notes to the financial statements 30 September 2014 (continued)

40. REGISTERED OFFICE

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

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 2014, the total assets held by the Group on behalf of its customers amounted to €337.3 million (2013: €603.7 million).

42. INVESTOR COMPENSATION SCHEME

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.

43. 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. These properties are classified within Level 3 and the techniques and the inputs applied by the Bank in measuring their fair value are similar to those described in Note 21.

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

	2014 €000	2013 €000	2012 €000	2011 €000	2010 €000
Interest receivable and similar income	212,896	222,437	238,545	224,064	219,904
Interest payable	(86,893)	(91,423)	(90,713)	(86,755)	(93,153)
Net interest income	126,003	131,014	147,832	137,309	126,751
Other operating income	83,802	87,113	71,032	36,237	64,440
Other operating charges	(93,499)	(89,138)	(91,665)	(97,179)	(78,796)
Net impairment losses	(19,431)	(25,595)	(22,817)	(16,041)	(12,936)
Share of results of associates	7,227	12,384	6,348	4,047	(542)
Profit before tax	104,102	115,778	110,730	64,373	98,917
Income tax expense	(34,718)	(36,305)	(36,454)	(22,319)	(34,945)
Profit for the year	69,384	79,473	74,276	42,054	63,972
Attributable to:					
Equity holders of the Bank	68,945	79,055	74,995	41,675	63,447
Non-controlling interest	439	418	(719)	379	525
	69,384	79,473	74,276	42,054	63,972
Earnings per share	**20c9**	**24c0**	**22c7**	**12c6**	**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 17 January 2014.

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

B. STATEMENTS OF FINANCIAL POSITION

	2014	2013	2012	2011	2010
	€000	€000	€000	€000	€000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	130,966	194,587	296,134	170,844	135,773
Investments and financial assets at fair value through profit or loss	2,950,011	2,247,351	2,106,740	2,203,539	2,206,942
Loans and advances to banks	1,045,988	860,957	676,639	400,931	264,965
Loans and advances to customers	3,861,532	3,667,739	3,702,217	3,607,064	3,496,744
Investments in associates	88,553	84,880	77,058	71,761	68,689
Property, plant and equipment	99,759	91,618	78,778	77,093	80,496
Current tax	-	-	-	7,143	1,482
Deferred tax	78,550	70,205	63,607	49,148	46,085
Assets held for Realisation	9,755	10,361	8,944	9,759	8,069
Other assets	7,659	5,045	11,418	4,505	4,978
Prepayments and accrued income	24,018	25,215	27,690	25,282	25,241
Total Assets	**8,296,791**	**7,257,958**	**7,049,225**	**6,627,069**	**6,339,464**
LIABILITIES					
Financial liabilities at fair value through profit or loss and held for hedging	81,812	62,048	98,744	76,653	78,559
Amounts owed to banks	86,579	36,040	250,352	260,614	347,369
Amounts owed to customers	7,119,530	6,219,666	5,809,300	5,523,907	5,185,264
Debt securities in issue	95,400	95,400	95,400	55,400	25,701
Current tax	16,090	4,697	13,405	356	187
Deferred tax	5,100	5,003	4,199	4,199	4,272
Other liabilities	130,168	108,864	106,235	78,526	73,429
Accruals and deferred income	27,643	29,235	30,590	33,217	35,635
Subordinated liabilities	120,000	120,000	120,000	120,000	120,000
Total Liabilities	**7,682,322**	**6,680,953**	**6,528,225**	**6,152,872**	**5,870,416**
EQUITY					
Equity attributable to shareholders of the Bank					
Called up share capital	330,000	300,000	270,000	240,000	200,000
Share premium account	988	988	988	988	988
Revaluation reserve	29,136	24,621	13,573	18,036	24,931
Retained earnings	253,245	250,735	236,196	214,211	242,546
	613,369	576,344	520,757	473,235	468,465
Non-controlling interest	1,100	661	243	962	583
Total Equity	614,469	577,005	521,000	474,197	469,048
Total Liabilities and Equity	**8,296,791**	**7,257,958**	**7,049,225**	**6,627,069**	**6,339,464**
MEMORANDUM ITEMS					
Contingent liabilities	233,451	213,598	215,512	191,726	183,803
Commitments	1,647,091	1,190,714	1,049,804	1,066,597	1,096,124

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

C. STATEMENTS OF CASH FLOWS

	2014 €000	2013 €000	2012 €000	2011 €000	2010 €000
Net cash from operating activities	766,887	509,520	397,001	155,525	116,799
Cash flows from investing activities					
Dividends received from equity shares	4,926	5,433	1,723	2,240	5,639
Interest received from investing securities	45,394	37,484	50,165	46,706	45,745
Investment in associates	-	-	-	-	(18,845)
Purchase of equity investments	(200)	-	-	(1,341)	(953)
Proceeds on sale of equity investment	-	-	-	-	-
Net increase in investment securities	(692,500)	(379,284)	(6,575)	(74,265)	(49,697)
Purchase of property, plant and equipment	(14,649)	(10,414)	(7,273)	(9,005)	(4,946)
Proceeds on disposal of property, plant and equipment	8	-	8	6,982	-
Net cash (used in)/from investing activities	(657,021)	(346,781)	38,048	(28,683)	(23,057)
Cash flows from financing activities					
Subordinated funds	-	-	-	-	23,433
Debt securities in issue	-	-	40,000	29,699	-
Dividends paid	(34,466)	(34,516)	(23,010)	(30,550)	(32,690)
Net cash (used in)/from financing activities	(34,466)	(34,516)	16,990	(851)	(9,257)
Increase in cash and cash equivalents	75,400	128,223	452,039	125,991	84,485

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

	2014 %	2013 %	2012 %	2011 %	2010 %
Operating income to total assets	2.70	3.05	3.20	2.68	3.04
Operating expenses to total assets	1.20	1.25	1.34	1.50	1.25
Profit before tax to total assets	1.34	1.62	1.62	0.99	1.58
Profit before tax to capital employed	17.50	21.11	22.28	13.67	21.92
Profit attributable to equity holders to total assets	0.89	1.11	1.10	0.64	1.01
Profit attributable to equity holders to capital employed	11.59	14.41	15.09	8.85	14.06

Group financial highlights in US dollars 30 September 2014

The following figures were converted from Euro to US Dollars using the rate of exchange ruling on 30 September 2014. The rate used was €1 = US$ 1.2600. This does not reflect the effect of the change in the rate of exchange since 30 September 2013 which was €1 = US$ 1.3502.

	2014	2013
	US$'000	**US$'000**
Net income attributable to shareholders of the Bank	86,871	106,740
Net income per share	26c	36c
Gross dividend paid	66,812	71,696
Net dividend paid	43,427	46,604
Gross dividend per share	20c	24c
Total assets	10,453,957	9,799,695
Liquid funds	165,017	262,731
Investments and financial assets at fair value through profit or loss	3,717,014	3,034,373
Advances	6,183,475	6,114,645
Investments in associates	111,577	114,605
Share capital	415,800	405,060
Capital reserves	37,956	34,577
Retained earnings	319,089	338,542

Annex 1

FULL RECONCILIATION OF OWN FUNDS ITEMS TO AUDITED FINANCIAL STATEMENTS

as at 30 September 2014

	Balance Sheet in accordance with IFRS scope of consolidation	Effect of deconsolidation for regulatory consolidation	Balance Sheet in accordance with regulatory scope of consolidation
	2014	2014	2014
	€000	€000	€000
Called up share capital	330,000	-	330,000
Share premium account	988	-	988
Retained earnings	253,245	(36,953)	216,292
of which: expected final dividend	19,841	-	19,841
general banking reserve	3,081	-	3,081
depositor compensation reserves	37,537	-	37,537
Revaluation reserves	29,136	(112)	29,024
of which: property revaluation reserves	24,561	-	24,561
unrealised gains and losses	4,575	(112)	4,463
Non-controlling interest	1,100	-	1,100
Intangible assets	11,642	-	11,642
Deferred tax arising from temporary differences	78,550	-	78,550
Subordinated liabilities	120,000	-	120,000
of which: amortised cost	117,096	-	117,096