Bank of Valletta p.l.c.

Annual Report & Financial Statements

2013

contents

financial statements

BOARD OF DIRECTORS

John Cassar White (Chairman)
Joseph Borg
Roberto Cassata
Ann Fenech
George Portanier
Taddeo Scerri
Paul Testaferrata Moroni Viani
George Wells
Franco Xuereb

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

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 Thursday 19 December 2013 at 16.30 hours.

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Bank of Valletta p.l.c.
Registered Office:
58, Zachary Street
Valletta VLT 1130, Malta
Registration Number C 2833

Bank of Valletta p.l.c. is a public limited company licensed to conduct Investment Services business by the Malta Financial Services Authority.

Bank of Valletta p.l.c. is authorised to act as a trustee by the Malta Financial Services Authority.

Bank of Valletta p.l.c. is an enrolled tied insurance intermediary of MSV Life p.l.c. (MSV). MSV is authorised and regulated by the Malta Financial Services Authority to carry on long term business investment under the Insurance Business Act 1998.

board of directors & secretary

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.

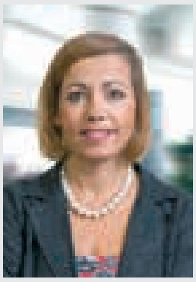
JOHN CASSAR WHITE
CHAIRMAN
R&N NED *

John Cassar White appointed Chairman of Bank of Valletta Group in April 2013. He also chairs the boards of MSV Life p.l.c., Valletta Fund Management Limited and Valletta Fund Services Limited, and is a member on the board of Middlesea Insurance p.l.c. He spent most of his professional career with Bank of Valletta from where he retired in 2008 after having occupied different senior executive positions over a career spanning thirty six years. He also served as director of a number of state-owned companies as well as private investment companies. Up to March 2013, he was a lecturer at the Institute of Business and Commerce of MCAST.

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.

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



ANN FENECH
NED *

Appointed to the Board in December 2012. Dr Fenech is a Managing Partner at Fenech & Fenech Advocates. Before joining the law firm, Dr Fenech worked with law firms in London and in New Orleans. She deals exclusively with ship related issues, having experience in disputes ranging from shipbuilding contracts to collisions, salvage operations and towage. Dr Fenech lectures extensively on the subject in Malta and abroad. She is the President of the Malta Maritime Law Association and a member of the Yachting Section at the Malta Chamber of Commerce and numerous other maritime associations. In June 2012 she was awarded Best in Shipping Law at the European Women in Business Law Awards held in London.

GEORGE PORTANIER
C R&N NED *

Appointed to the Board in May 1992. Mr Portanier currently chairs the Board's Compliance Committee and is also a member of the Remuneration and Nominations Committee. He was a member of the Executive Committee and of the Risk Management and Compliance Committee, for a number of years. Mr Portanier was formerly a director of Portanier Brothers Limited and served as a member of the Local Manufacturers' Committee of the Federation of Industries and of the Council of the Federation of Industries.

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 a member of the Bank's Asset and Liability Committee (ALCO). He is a qualified accountant and is the managing partner of RSM Malta. He is the financial expert on the local UEFA Clubs Licensing Board and is also a member of the Malta Football Association's Finance Committee.

PAUL TESTAFERRATA MORONI VIANI
A C RM NED *

Appointed to the Board in December 2007. Mr Testaferrata Moroni Viani is a member of the Bank's Audit Committee, 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 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.

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.

Chairman's Statement

JOHN CASSAR WHITE

BOV Group has performed satisfactorily recording a profit before tax of €115.8 million

BACKGROUND

The financial year of Bank of Valletta (BOV) Group which ended on 30 September 2013 was, as expected, characterised by sluggish economic activity and increasing regulatory pressures on the global scene as well as a period of uncertainty in anticipation of the local general elections held earlier this year.

In the aftermath of the eurozone sovereign debt crisis the European Union (EU) economy was forecast to slowly return to stability. Banks and other institutions continued with deleveraging their balance sheets and governments persisted with their efforts to consolidate public finances. Growth in credit remained muted despite the accommodative stance of the European Central Bank's (ECB) monetary policy and the persisting low interest rate scenario. Private and public investment as well as consumption continue to be hampered by the uncertainty of the economic outlook which is still weighed down by a weak labour market and the divergencies in unemployment rates across member states.

The policy measures intended to make the EU economy robust and efficient are slowly but surely having an effect. These measures are not limited to the structural and fiscal reforms adopted by the various member states. Possibly the most important factor to stabilise the EU was the Outright Monetary Transactions (OMT) or unlimited bond-buying programme provided by the ECB which gave credence to Mr Draghi's comment that he would do "whatever it takes to save the euro". Although no country has yet applied for help under this programme, its existence has greatly helped to calm financial markets. Other important measures include the decision to set up a Single Supervisory Mechanism as a first step towards a Banking Union, the adoption of the European Stability Mechanism (ESM) as a permanent crisis resolution mechanism for the countries of the euro area and the strengthening of the European Monetary Union (EMU) framework. While financial markets remain fragile, there has been a marked improvement in sentiment as confidence is gradually returning.

The progress achieved at member states' level varies. While countries such as Ireland appear on track for an economic recovery and is preparing to leave the bailout programme by the end of this year, other states, notably Spain, are still struggling to curb rising unemployment rates. High and persistent unemployment could affect the growth potential and has the added risk of becoming structural as the skills of jobless workers depreciate.

BOV GROUP PERFORMANCE

In this challenging economic environment, BOV Group has performed satisfactorily recording a profit before tax of €115.8 million, an increase of 5% when compared to €110.7 million last year. Return on equity stands at 21.1%, slightly below the 22.3% for FY 2012 while the Cost to Income ratio improved from 40.7% last year to 38.7% for FY 2013.

The combined effects of the ongoing low interest scenario and the continued subdued demand for credit, resulted in lower margins being earned both on our investment portfolio and on our loan book. During the year we also experienced the repayment of large ticket items which were not replaced by new demand for lending. The reduction in the loan book was somewhat offset by the increase in demand for home loans where we continued to see satisfactory growth. The drop in net interest income was partly mitigated by higher activity on other product lines which led to an increase in commissions earned. Costs remained under control despite the continued investment in both our people and in IT as well as the higher regulatory costs incurred during the year. The Bank retained its cautious approach towards provisioning in line with the sentiment for tighter provisioning policies which is being expressed by both local and international bodies.

The results for the year include fair value gains of €17.3 million, largely as a result of improved sentiment in financial markets. The latter also influenced BOV's share of profit from its insurance interests which, at €12.4 million, are almost double the amount for FY 2012.

Customer deposits are up by more than €400 million and have exceeded the €6 billion mark. The 7% year on year increase was evenly split between retail and business customers and was practically all in the short term products. The limited opportunities for investment products which meet our cautious risk appetite and the low demand for lending meant that excess incoming funds were channelled into short term assets, increasing the liquidity position of the Bank. This dovetails with our conscious decision to sacrifice short term profitability for liquidity in the preparation for the more stringent regulatory liquidity requirements.

Long term stability remains a primary strategic priority and prudent capital management led to further strengthening of BOV's Common Equity Tier 1 (CET1) ratio which at 30 September 2013 stood at 11.6%, up from the 10.7% last year. Internal capital forecasts, based on core profitability levels barring unforeseen circumstances, show that profit retention is expected to suffice for BOV to be fully compliant with the new capital requirements of Basel III and CRD IV within the established timeframes.

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

DIVIDEND

The Board believes it should continue to balance the Bank's long term sustainability and shareholders' dividend expectations. It is therefore recommending a final gross dividend of €0.13 per share which, taken together with the gross interim dividend of €0.06 per share paid in May 2013, makes for a total gross dividend of €0.19 per share for this financial year (FY 2012: €0.171 as restated for the January 2013 bonus issue). The total dividend for the year would represent a gross yield of 7.8% by reference to the closing share price of €2.42 per share at 30 September 2013 and the net dividend cover will be 2.1x. Similar to previous years, the Board is also recommending a bonus issue of 1 share for every 10 shares held as on 17 January 2014 by capitalisation of reserves amounting to €30 million increasing the permanent share capital from €300 million to €330 million.

SINGLE SUPERVISORY MECHANISM

On 23 October 2013, the ECB announced the details of the comprehensive assessment which it will be conducting in preparation of assuming full responsibility for supervision as part of the Single Supervisory Mechanism. The assessment, to commence in November 2013 and expected to be finalised by November 2014 when the ECB assumes its supervisory role, will be carried out in collaboration with the local regulator.

Bank of Valletta has been identified as a domestic systemically important bank and is one of the three local banks that will take part in this exercise. The assessment will focus on a review of key supervisory risks, including liquidity, leverage and funding, an asset quality review (AQR) to enhance the transparency of bank exposures by reviewing the quality of banks' assets and a stress test to examine the resilience of banks' balance sheet to stress scenarios. ECB President Mario Draghi commented that while the primary objective of this assessment is transparency it is expected that "this assessment will strengthen private sector confidence in the soundness of euro area banks and in the quality of their balance sheets".

BOV has participated in similar exercises over the last few years and welcomes the challenge that this new assessment will undoubtedly provide. The Bank appears to be adequately capitalised but as full details in respect of this assessment are not as yet available, we will be monitoring the situation closely.

OUTLOOK

The EU economy is slowly coming out of negative growth. As confidence continues to recover, prospects for 2014 indicate modest growth in the EU economy. These early stages of recovery have yet to filter through to the labour market. The levels of unemployment remain a serious concern and the prospective recovery depends on the strict implementation of structural reforms which will support growth and lift employment.

The Maltese economy is expected to remain resilient with a forecast GDP growth of 1.7% and stable unemployment levels below the EU average. While progress has been made in implementing the country-specific recommendations, Malta still faces the challenges that affect the long term sustainability of its public finances, the management of government deficit and the strenghtening of its fiscal positon. As an open economy, the need to maintain external competitiveness is essential for Malta's future economic growth.

In the coming year BOV will continue with its prudent business model that underpins its overarching strategic objective of long term sustainability. As Malta's largest financial institution, BOV intends to continue to carry out its role in supporting the local economy while safeguarding its shareholder value through prudent policies and a cautious risk appetite.

CONCLUSION

In conclusion, on behalf of the Board, I would like to thank the previous chairman, Frederick Mifsud Bonnici for his contribution as Chairman, the chief executive, the executive team and all the employees for their contribution towards achieving these results in what was another challenging year. We also thank our many customers for their continued trust in Bank of Valletta and for the business that they bring. Finally, we continue to appreciate the advice provided to us by our regulators and thank them also for their support.

John Cassar White
Chairman
5 November 2013

CEO Review

CHARLES BORG

This was another year that underpinned the strong bond that exists between the Bank and its customers

BACKGROUND

Throughout this financial year, the markets experienced low or even negative GDP growth rates, particularly in many European countries. The United States faced major fiscal headwinds, whereas the eurozone was going through one of its worst recessionary periods as tough austerity measures were introduced to stave off sovereign default in peripheral countries. Although insignificant in terms of size, the Cypriot crisis proved to be daunting as European leaders scrambled to avoid contagion in bigger countries such as Italy and Spain. However, for the first time, depositors with amounts over €100,000, were forced to contribute towards Cyprus's bailout package.

In the wake of all this, the ECB reduced its refinancing rate by 25bps to 0.50% on 2nd May 2013, whilst maintaining its deposit rate at 0%. These record low interest rates prevailed throughout all major economies as central banks continued to support very loose monetary policies. This was coupled with extraordinary liquidity injections as governments tried their utmost to achieve at least modest growth.

Earlier on this year, some international financial commentators tried to compare the Maltese financial sector with that of Cyprus and this created a level of concern to the Maltese authorities and the local banking community. However, the quick response of the Central Bank of Malta and representatives from the banking community, convinced authoritative international agencies such as Bloomberg, Standard and Poor's, Reuters and Fitch Ratings to conclude that there was no comparison between the Cypriot and the Maltese banking system and what happened in Cyprus is not likely to be repeated here in Malta.

This was confirmed by the European Commission in April 2013 when it stated that the 'core domestic banks' in Malta constituted only 220 percent of the GDP as opposed to around 500 percent in Cyprus. Such authoritative opinions put paid to the idea that Malta's banking sector may be 'too big to bail out'. In addition, when one considers the negligible exposure of the Maltese banks to the euro area's peripheral nations, the risk to domestic financial stability appears to be small. Bloomberg commented in its report on Malta on the 23rd May 2013, that 'the same factors that protected the Maltese banks from the ravages of the financial crisis of 2008 – the conservative business models and sound regulation – have functioned just as effectively in the case of the Cyprus crisis'.

REVIEW OF PERFORMANCE

With this background, the BOV Group has recorded a profit before taxation of €115.8 million for the financial year ended 30th September 2013. This represents a 5% increase over the corresponding figure of €110.7 million pre-tax profit reported in the previous financial period. Continued growth in the balance sheet, the increase in the fee and commission income and the positive market movements in the Financial Markets investment book, were the main drivers underlying this positive result.

The Core Operating Profit of €86.5 million, which excludes price movements on the investment portfolio and returns from the associated companies, shows a decrease of 14% from September 2012 (€100.3 million). The prolonged low interest rate scenario has had a negative impact on the interest margins, particularly on the returns of the Financial Markets investment book.

		Sep-13 € million	Sep-12 € million	Change € million	%
Net interest income	(a)	131.0	147.8	*(16.8)*	-11%
Net commission and trading income	(b)	69.7	62.4	*7.3*	12%
Operating expense	(c)	(88.6)	(87.1)	*(1.5)*	2%
Impairment charge	(d)	(25.6)	(22.8)	*(2.8)*	12%
Core Profit		**86.5**	**100.3**	***(13.8)***	**-14%**
Fair value movement	(e)	17.4	8.7	*8.7*	101%
Operating Profit		**103.9**	**109**	***(5.1)***	**-5%**
Share of profit from associates	(f)	12.4	6.3	*6.1*	95%
Net compensation related to LVMMPF and other securities		(0.5)	(4.6)	*4.1*	89%
Profit before tax		**115.8**	**110.7**	***5.1***	**5%**

Key performance indicators remain satisfactory. There was a steady improvement in the Cost/Income Ratio of 38.7%, down from 40.7% in FY 2012. The Return on Equity registered this year is 21.1% (FY 2012: 22.3%), which compares favourably with international banks.

BOV Group's results for the financial year are summarised in the table above. This table should be read in conjunction with the explanatory notes that follow.

(a) Net Interest Income

Net Interest Margin for the year of €131.0 million represents a decrease of 11% when compared to last year. This decrease is mainly attributed to lower returns from the Bank's Treasury assets. The Bank has retained a cautious risk appetite and consciously sacrificed returns for quality of the portfolio. The retail margin also tightened this year as a result of the increase in our retail deposits which were not deployed in lending as demand for credit remained relatively subdued.

The ECB retained its current level of interest rates during the year under review, in a bid to encourage banks to make more credit available within their respective economies. Given the current situation in the eurozone countries, our expectation is that the ECB will retain the current level of interest rates for most of 2014 and possibly going into 2015. Naturally within this scenario, the Bank has to actively manage its interest rates on both sides of its Balance Sheet keeping in mind the expectations of both its depositors and borrowers.

(b) Net Commission and Trading Income

Net commission and trading income increased by 12% from €62.4 million last year to €69.7 million this year. FY 2013 was characterised by stronger performance across all lines of business. We experienced higher interest being shown by Maltese and foreign companies wanting to do business in Libya and other parts of Africa and this resulted in a satisfactory growth in trade related fee income. While the volume of foreign currency transactions has increased, margins were tighter and foreign exchange earnings are marginally below last year. We managed to reverse last year's negative trend in bancassurance and this year we registered an increase in commissions earned on the sale of insurance products. Growth was also registered on other investment related products, with increases in commission income on wealth management and stockbroking as well as our fund management and funds services businesses. Credit related commissions are also up while our card business again shows satisfactory growth as more people use cards as their preferred payment instrument.

We have continued with our IT investment programme for this business area and we are pleased to report that progress has been registered in the implementation of a new card management system.

(c) Operating Expenses

Operating expenses for the year totaled €88.6 million, an increase of 1.7% over the previous year. This was largely due to our increased contribution to the Deposit Guarantee Scheme as a result of the growth in our deposits and higher contribution rates. All other operating expenses remained on the same levels as last year. The Bank has persisted in its efforts to improve its efficiency and curtail its discretionary expenses, and this is evident in this year's results.

The BOV Group continued with its investment in the IT infrastructure to ensure that it remains at the forefront of innovation and technology. These investments in technology will be of significant benefit to the Bank and to its customers.

(d) Net Impairment Charge

Notwithstanding the fact that our economy continues to show resilience, the challenging conditions that we are operating in, compounded by the European sovereign crisis, have invariably influenced the performance of the Maltese economy. We believe that the effects of these external factors will, at some point, result in additional pressures on the quality of our credit book.

We therefore continued, consistent with previous years, to make further specific and collective allowances.

This approach is also very much in line with the recommendations being made by the European Commission in its report on Malta dated 10th April 2013, as well as the statements made by the Governor of the Central Bank of Malta in his presentation of the CBM's annual results on the 9th April 2013.

The European Commission commented that Maltese banks generally have low coverage ratios because they provide only for the unsecured portion of their credit exposures. It therefore recommended that the Maltese banking system strengthens its non-performing loan coverage and exercises tight control over the loan-to-value ratio in the real estate and construction sectors. These recommendations are aligned with the Bank's long term provision coverage strategy, and an impairment charge of €25.6 million is being made for this financial year. This charge for the year comprises both specific and collective impairment charges and the impact of this was an overall increase in our provisions by 12% over the same period last year. The year on year increase arises largely due to the Bank's more conservative view of the value of collateral held on non-performing exposures.

(e) Fair Value Movement

Financial markets performed well during this financial year, buoyed by the ECB's continuing willingness to provide liquidity, and this had a positive effect on the fair value of the Bank's investment portfolio. Most of the markdowns that we experienced between 2008 and 2011 have been recouped. We are reporting a fair value gain of €17.4 million for this financial year, as compared with a fair value gain of €8.7 million last year. This represents more than a 100% increase in positive fair value movement when compared to FY12.

(f) Share of Profit from Associates

BOV has a direct equity stake of 50% in MSV Life plc and a 31.8% stake in Middlesea Insurance plc (MSI). BOV's share of profit from MSV Life and MSI for this financial year amounts to €12.4 million, a strong increase of 95% over the last financial year. These results were influenced by the positive performance of the local and international equity and fixed income markets.

BOV's share of profit from associates is made up as follows:

Share of Profit

	2013 € million	2012 € million
MSV Life	9.3	4.6
MSI	3.1	1.7
Share of profit from associates	12.4	6.3

REVIEW OF FINANCIAL POSITION

Total assets as at 30th September 2013 stood at €7.3 billion (September 2012: €7.0 billion), whilst equity attributable to the shareholders of the Bank increased by a further €55.6 million to €576.4 million, an increase of 11%.

The Bank has continued to manage its Balance Sheet in a deliberate and prudent manner, with the aim of strengthening its core Tier 1 capital and liquidity ratios in line with the CRD IV regulatory regime. Tier 1 capital ratio as at the end of this financial year stood at 11.7%, up from 10.7% last year. The Bank's liquidity ratio remains strong at over 50%. Earlier this year, the Bank repaid its two LTROs amounting to a total of €170 million. The entire Bank's funding is now wholly dependent on customer deposits and long-term senior and subordinated debt, with no reliance on the international money markets. The loan to deposit ratio of 61.7% reflects the prudent approach that the Bank maintained during the period under review. Moreover, most of BOV's investment book continues to be held in high-quality bonds which can be used as collateral with the European Central Bank, thereby giving the Bank ready access to a source of secure additional funding should the need arise.

LOANS AND ADVANCES

Total gross lending stands at €3.8 billion at the year end, a decrease of 0.9% when compared to the September 2012 number. This reflects the subdued demand for credit, particularly in the business segment, coupled with the repayment of a number of large facilities.

The Bank's commitment towards the business community is reflected in the amount of funds injected in the economy through new lending, exceeding €233 million during this financial year. These funds were channelled to various sectors of the economy, both the traditional as well as the emerging sectors, in line with the diversification being experienced in the local economy. Assistance to small and medium size enterprises (SMEs) continued to be at the forefront of the Bank's strategic direction evidenced by the success of the JEREMIE Scheme, a risk sharing instrument specifically aimed at assisting SMEs. The JEREMIE Scheme's total available pot of €51 million was fully committed by June 2013, ten months prior to the actual expiry of the Scheme, through which the Bank assisted more than 530 SMEs in their financing needs.

In August of this year, the JEREMIE Scheme was extended by a further €11 million after the approval of the European Investment Fund. Next year, the Bank intends to further expand its product suite for SMEs through the introduction of another risk sharing product specifically designed for micro start-up enterprises. This should complement further the Bank's strategy of enhanced financial inclusion and access to finance.

Despite the highly competitive landscape, results in the consumer retail segment were satisfactory with an increase exceeding 4% year-on-year. This increase was mainly driven by sustained demand for Home Loans. The Bank has this year integrated the functions responsible for home loans and personal lending into a dedicated Consumer Finance Division aimed at providing a higher value and a holistic service to our retail customer base.

CUSTOMER DEPOSITS

Customer deposits at the year end exceeded the €6 billion mark and stood at €6.2 billion, an increase of €410 million, or 7% over September 2012. The growth in customer deposits came from both retail customers as well as from the corporate and institutional segments. This is indeed very encouraging, particularly in the light of increased competition in this area.

DIVIDEND AND BONUS ISSUE

The Board is of the view that it should continue with its distribution policy whereby the Bank's long term sustainability and dividend expectations are kept in balance. Accordingly, the Board of Directors is recommending a final gross dividend of €0.13 per share which, taken together with the gross interim dividend of €0.06 per share paid in May 2013, makes a total gross dividend of €0.19 per share. The total dividend for the year represents a gross yield of 7.8% by reference to the closing share price of €2.42 per share as at 30th September 2013 and a net dividend cover of 2.1 times.

Similar to previous years, the Board is also recommending a bonus issue of 1 share for every 10 shares held as on 17 January 2014 by capitalisation of reserves amounting to €30 million increasing the permanent capital to €330 million from €300 million.

OPERATIONS AND MULTI-CHANNEL BANKING

During FY13, we continued to focus on strengthening the BOV Brand and on seeking the alignment of our people to offer a consistent, differentiated and valuable customer experience.

In fact this year, we have updated the visual image of the BOV brand to project a fresh and bold identity. The response received is very encouraging and we are confident that we have implemented a brand signature that can support a new cycle of customer centric innovation. It shows that BOV is a forward looking organisation that will continue to play an important role within the increasingly competitive environment in which we are operating.

(i) Cards Business

Our Cards business continued to perform well, driven by a continued shift in consumer preferences towards the usage of cards as the preferred payment instrument. We registered growth of 10% in our credit card client base whilst overall cards turnover increased by 12% over the previous year.

Innovation continued to feature high on the agenda as we continued to implement our multi-year project that is seeing us replace our cards systems, enabling us to better respond to changing customer requirements in a more flexible and timely manner.

Growing the cards business line requires careful management of card fraud related risks. A milestone in fraud-risk management was achieved in the last quarter of FY13, when the Bank introduced 3D Secure for internet purchase authentication on its VISA Classic credit card product. 3D Secure was one of the innovations possible with the introduction of our new Card Management System. We are currently in the process of extending this service across the entire card base.

(ii) Payments Business

In the Payments business area, we have continued to exploit the new opportunities that SEPA offers. Bank of Valletta has been an early provider of SEPA Direct Debits and we have continued to expand this service during the financial year under review. We have also continued to attract new corporate customers who are now using the Bank's electronic payments systems interfaced to their own systems enabling the seamless and straight through processing of bulk payments.

Bank of Valletta has not only been working to meet the SEPA end date but was engaged in an extensive communication campaign amongst all stakeholders that also included one to one meetings with corporate customers in an effort to assist them in the migration.

(iii) Multi-Channel Banking

BOV remains the only bank in Malta to offer mobile banking and real time person to person payments via a dedicated mobile application. During this financial year, we continued to strengthen our first mover advantage. In fact we launched

an enhanced version of BOV Mobile Pay that allows customers to send a message to the payment recipient in addition to the payment. We are pleased with our customers' response to BOV Mobile with over 1,000,000 log-ins being registered merely 18 months from launch. The Bank is continuing to work on a new Internet Banking platform. This platform is designed to replicate the rich functionality of the Bank's existing and award winning internet banking solution, whilst introducing new features that will strengthen our value proposition to our customers.

At the same time, we also continued to invest in our ATM network, deploying 14 new Advanced Deposit ATMs (offering real-time cash and cheque deposit services) during this financial year. We also introduced our second drive-through ATM located at Tal-Barrani Road, Zejtun.

PERSONAL BANKING AND WEALTH MANAGEMENT

The branch network and customer service centre remain central to the delivery of a quality service in the best interests of the Bank's large number of individual and corporate customers. During the last financial year the Bank implemented a number of recommendations by international consultants who were engaged to carry out a comprehensive independent review of the Bank's sales processes across various product lines. As a result, six Investment Centres across Malta and Gozo were opened as one of the initiatives undertaken to reshape the Bank's investment advisory service in line with the changing regulatory environment and investor expectations. These Centres are yielding satisfactory results and the clients who have already availed themselves of the service provided at these Centres have commented favourably on the quality of service being delivered by the Bank's authorised financial advisors.

The Bank's Wealth Management Unit has also realigned its service offering in the light of regulatory and market developments. At Wealth Management an open architecture framework is adopted and each Relationship Manager is authorised and licensed to provide investment advice across in-house and third party products and direct bonds, equities and other investment instruments.

STRATEGY AND PROCESS MANAGEMENT

During this financial year the Bank set up a new unit to facilitate the Group's strategic planning. This unit is also responsible to review in detail our operational processes in order to ensure that strategic objectives are met in an efficient and effective manner. The overarching objective of long term sustainability is based on the core measures of return to shareholders, adequacy of capital and brand value. During FY 2013 a number of strategic initiatives, centered on new services, better value to our clients and higher effectiveness in the way we conduct our business, have been initiated in support of these measures.

At the beginning of this financial year the Bank engaged international consultants to carry out a holistic review of the Bank's positioning in terms of our customer service through our branch network in line with international standards. This review has resulted in various recommendations, which we aim to implement over the coming years. This renewed focus on customer service will be driven through a strategic Bank wide programme internally known as "Project FACE" (Focusing our Actions on Customer Experience).

This programme will incorporate a review of our product and service offerings, as well as the delivery channels used by each segment of our customer base, to ensure that we continue to meet their needs in the future. We shall also be implementing a framework to monitor customer service processes on an on-going basis in order to be in a position to make the necessary amendments to serve our clients even better.

HUMAN RESOURCES

At BOV we continue to believe that the organization is as good as its people. Therefore training and career development are an important part of the Bank's strategy. In fact, during this financial year, the Bank continued to invest in its people to upgrade their skills and competencies. We have trained no less than 4,371 employees throughout the 231 training programmes organised by our Training Centre.

There were various other HR initiatives principally aimed at the development of our employees and to motivate them in their place of work, such as 'job coaching' and 'work attachments'. Over 30% of the Bank's workforce are graduates and these need to have continuous training. This year we introduced a course for graduates to train them on the day-to-day management skills. We plan to expand this training programme to other graduates during this year.

RATING RESULTS

On 25th February 2013, Fitch Ratings affirmed Bank of Valletta's rating at BBB+ with a 'Stable Outlook'. This affirmation by Fitch Ratings assumes even greater significance at a time when many large financial institutions as well as EU sovereign states were either under review or actually being downgraded.

In their report, Fitch confirmed Bank of Valletta's position 'as the largest bank in Malta, with a strong funding base, satisfactory liquidity and good profitability'. In its comments, Fitch Ratings confirmed that the Bank's net interest margin remains high despite the low interest rate environment, and expected the Bank to manage this situation successfully during 2013. They further commented that they expect the Bank to increase its loan impairment charges in order to improve the allowance coverage ratios. This will naturally mean additional pressure on the Bank's future profitability.

Fitch Ratings also commented that the Bank's funding is supported by a large and stable customer deposit base, whilst the loan-to-deposit ratio is very conservative in the 60% region, which implies that the refinancing risk is significantly mitigated by a large pool of unencumbered liquid assets.

INTERNATIONAL AND LOCAL ACHIEVEMENTS

Once again our work has not gone unnoticed by international and local monitors. Bank of Valletta was once again named as the Best Bank in Malta in 2013 by Global Finance (New York), an award that we managed to win for the fourth consecutive year. This award recognises the Bank's efforts to achieve sustained results.

We were also proud to receive the prestigious award for Financial Innovation for our Mobile Banking Service by the Institute of Financial Services (IFS) in the UK. According to the Chairman of IFS (UK), this award was keenly contested this year between three banks, BOV, Barclays and RBS. This was indeed proof that the Bank's BOV Mobile application is very innovative and highly creative.

The Bank also received recognition from its international partners such as JP Morgan and Deutsche Bank for its high quality standards and excellence in straight through payment processing. Bank of Valletta also achieved two prestigious awards in Malta organised by the Foundation for Human Resources Development. These two awards were in the areas of Equal Opportunities and Staff Wellness.

OUR ROLE IN THE COMMUNITY

At Bank of Valletta we believe that part of our success lies with our involvement in our community. Our roots run deep into Maltese society, with a workforce of 1,600 people, servicing circa 300,000 customers and having an extensive retail network - the footprint is considerable.

Bank of Valletta's community relations programme is the executive arm of its Corporate Social Responsibility (CSR) principles. It provides a framework for the equitable distribution of a portion of the Bank's profits into the community. Under the social pillar, philanthropic efforts support the most vulnerable members of the community. The Bank's belief in holistic education fuels its efforts in supporting the National Literacy Project whilst maintaining its own Investor Education Programme. Sports is also an important part of the Bank's CSR programme, together with other businesses and professional bodies. The environment features as a key stakeholder on the Bank's agenda at all levels of operation. Bank of Valletta is proud to be recognised as the patron of local arts and culture, whilst actively supporting the conservation and restoration of heritage sites and artifacts.

For a financial services provider like BOV, where its people constitute the backbone of the organisation, embracing a CSR programme essentially means building an internal culture of commitment to customers and society. For BOV, CSR has become synonymous with the manner in which we manage our business.

THE IMPACT OF EUROPEAN BANKING REGULATION

The recent financial crisis, and the Euro sovereign debt crisis which followed it, have pushed the need for financial reform to the top of the European agenda. In 2012, European leaders took the extraordinary step of proposing the project of a Banking Union for Europe. Their aim was to break the toxic link between banks and sovereign debt, and to prevent a repeat of the crisis that called the survival of the single currency into question.

Since then the project has taken on a more concrete shape, albeit disagreement about some of the proposals remains. The Single Supervisory Mechanism (SSM), which was approved on 15th October 2013 by European finance ministers, is a first step towards realising the Banking Union, which will be based on four pillars - improved bank regulation, centralised bank supervision, a harmonised system for restructuring or closing down troubled banks, and the protection of small depositors.

Under the SSM, the most significant banks in Europe, numbering around 130, will come under the direct supervision of the European Central Bank (ECB). Before assuming this

role, the ECB will conduct a comprehensive assessment of the balance sheets of these banks. The assessment will comprise a supervisory risk assessment, an asset quality review and a stress test. This exercise will start in November 2013 and will last one year, with the ECB expected to take full supervisory responsibility in November 2014.

The ECB has also set an immediate minimum Core Equity Tier 1 ratio of 8% for these banks, thus anticipating the original Basel III capital proposals by five years.

BOV will be one of the 130 European banks to come under ECB supervision, in view of its size when related to Malta's GDP. The SSM will undoubtedly prove challenging, but we also view it as a good opportunity to continue strengthening the excellent reputation which the Bank and the Maltese financial sector enjoy internationally. The Bank has started its preparations for the ECB assessment, and is confident that it will fully meet the high expectations of the pan-European supervisor.

The ECB will undoubtedly give paramount importance to the long term sustainability of the banks under its oversight. In this respect, the Bank has always exercised, and continues to exercise, tight management over the three elements on which sustainability depends – capital, liquidity and asset quality. With regard to capital, we can confirm that BOV is well on its way to meeting the stringent requirements of the EU Capital Requirements Regulation (CRR). The Bank currently expects to meet these requirements from its own profit generation, and without the need to raise fresh equity capital on the market. With regard to liquidity, the Bank has already met CRR minimum requirements, five years in advance of statutory compliance date.

The Bank gives equal priority to maintaining asset quality, operating a classic 'three lines of defence' risk management model. The primary responsibility for taking on credit risk is assumed by the business unit. The second line of defence, oversight, is exercised by the Risk Management and Compliance functions, while independent assurance is provided by Internal Audit, which scrutinises both first and second lines.

LOOKING AHEAD

Since the financial crisis in 2008, the world has gone through unprecedented turmoil, shaking entire industries and instilling uncertainty across all markets. This economic uncertainty is likely to linger over the coming months although the economic outlook for the next two years has started to turn optimistic.

Major central banks are increasingly turning to 'forward guidance' in their efforts to keep short term interest rates low to defend the fragile economic recovery. Most of them are stating that they will not raise interest rates until economic figures, and especially employment, point to a strong recovery. This means that benchmark rates are expected to remain stable during the coming financial year, especially as inflationary pressures remain subdued.

Furthermore, the long running eurozone sovereign crisis continues to create uncertainty, and the austerity measures being adopted by EU member states will take time to have the desired effect. Unemployment, particularly amongst the younger generation in Europe, needs to be addressed with some urgency.

Despite all this, the Maltese economy has remained resilient throughout these years of crisis. The country continued to register economic growth driven mainly by the export-oriented sectors such as tourism and services. The European Commission is projecting economic growth for Malta to increase in 2013-14 and outperform the euro area average. Traditional sectors, such as construction and wholesale and retail, are expected to continue to experience stress.

Malta, with its open economy, needs to ensure that it remains price competitive. The European Economic Advisory Group in its report for 2013 confirmed that Malta, together with Germany and Austria, has seen better economic growth as a result of the condition of the private sector financing and the high level of international competitiveness. Household debt has been increasing over the last few years, but remains below the euro-area average. The European Commission has however warned the Maltese Government that its debt needs to be reined in to ensure the long-term sustainability of public finances, especially in the context of an ageing population that will make pension and healthcare reforms increasingly necessary.

CONCLUSION

The positive results achieved this year would not have been possible without the collective effort of the entire BOV team. I take this opportunity to thank the executive management team for their support, advice and unwavering commitment in steering our organisation forward.

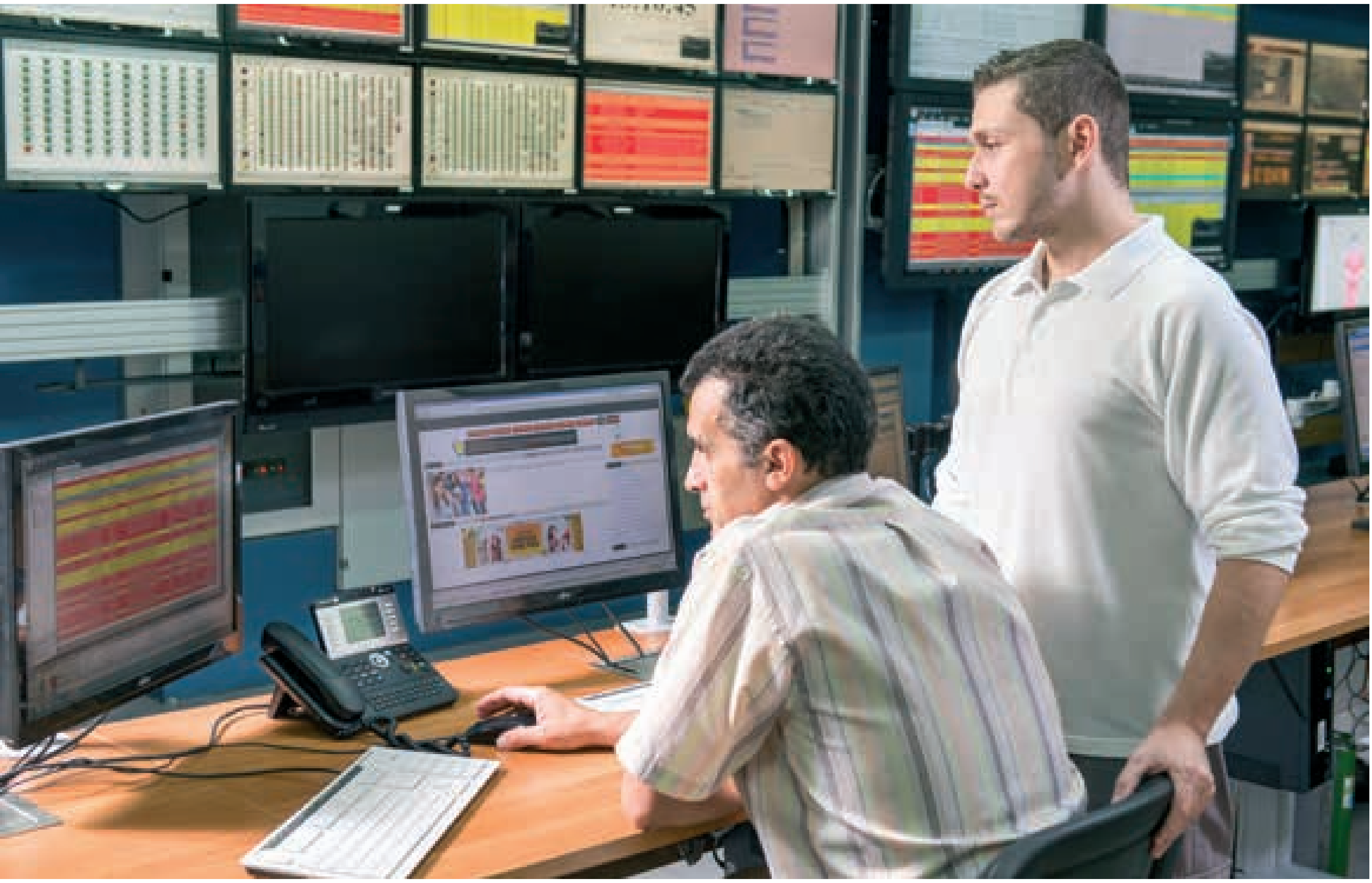
My thanks also go to the Chairman and Board of Directors who have been of constant support to me during this financial year. Their strong sense of strategic purpose and corporate governance was instrumental in providing the proper direction and the setting of a meaningful strategy. This enabled the Bank to continue to balance successfully a conservative approach to our business coupled by a strong drive to meet customers' expectations. My thanks also go to Frederick Mifsud Bonnici who served as Chairman of the Board for the first six months of this financial year.

Last but not least, a special word of thanks is due to our many customers who continue to put their trust and confidence in Bank of Valletta. This was another year that underpinned the strong bond that exists between the Bank and its customers.

Every customer relationship is important for us. Bank of Valletta remains wholly committed to supporting its customers and the Maltese economy in a responsible manner. This constant support and commitment has been clearly recognised and acknowledged by a growing customer base. We have to continue to actively and prudently manage both sides of our balance sheet, maintain high liquidity and strong capital ratios, whilst being conscious of our obligations to all stakeholders – shareholders, employees, depositors and the wider community.

This delicate balance has to be managed at all times. We need to project a message of resilience, strength, vision and growth as we continue to meet the challenges which we will undoubtedly face in the future whilst focusing on maintaining our market position as the Bank of first choice.

Charles Borg
Chief Executive Officer
5 November 2013



strategic priorities

MICHAEL BORG COSTANZI

CHIEF OFFICER LEGAL & COMPLIANCE

In line with what has happened in the past years, during the coming financial year, regulation of the financial services industry should continue to increase. This also means that the directors and senior management need to be trained and kept up-to-date with developments. At the same time, the compliance function will remain high on our agenda. In particular, quality compliance-related management information, together with monitoring and training of our staff, remain vital. In so far as support services are concerned, every effort will be made in order to ensure that a customer centric service of the highest quality is provided to our customers, whether internal or external, at all times. In addition, we intend to improve the way we handle customer issues and benchmark our systems and processes against best practice.

JOSEPH M CAMILLERI

CHIEF OFFICER STRATEGY & PROCESS MANAGEMENT

Bank of Valletta's strategic vision is to consolidate its leadership position, underpinned by excellent financial performance, strong market share and customer service excellence. This will be achieved through initiatives which enhance our offering through various service delivery channels. Customer satisfaction and market trends will be monitored to ensure service levels meets or exceeds client expectations. We shall strengthen our strategic planning, execution and feedback cycle ensuring the strategy remains relevant, and is communicated and implemented effectively. A cost-conscious approach will continue to be fostered by ensuring efficient business processes while investing in business lines which add value to our stakeholders.

ROMEO CUTAJAR

CHIEF OFFICER FINANCIAL MARKETS & INVESTMENTS

Within the context of a low interest rate scenario coupled with tight credit spreads, portfolio management will continue to be challenging. Customer deposits will remain the Bank's main source of funding, and our goal is to continue to be leaders in this market. Through its liquidity management, FM&I will ensure that targets emanating from new regulations are met before coming in force. ICC continues to play a strategic role within the Bank, and our objective is to consolidate our service offering by focusing on a more customer centric structure. We will also be focusing on providing an enhanced stockbroking service to our diverse client base by investing in new delivery channels.

MICHAEL GALEA

CHIEF OFFICER OPERATIONS

During FY 2013, we responded to evolving customer preferences by bringing innovative products and channels to the market whilst sharpening our customer value proposition. Through the EU Representative Office in Brussels, BOV continued to position itself as the reference point for Maltese enterprises when seeking EU funding and related business opportunities. We have also strengthened our operational efficiencies, focusing on delivering a customer experience aligned to our brand promise.

Looking ahead, we will remain focused on strengthening the BOV brand. We will continue to respond to customer needs through a sustained programme of product and channel innovation, whilst continuing to promote a culture of operational efficiency.

ELVIA GEORGE

CHIEF OFFICER FINANCE

The preparation and analysis of financial information, for both executive and line management, remain key deliverables of the Finance function within the BOV Group. The appraisal of investment proposals supported various business owners in making a more informed decision. BOV has been identified as one of the three local banks to participate in the assessment to be carried out as part of the Single Supervisory Mechanism of the ECB. This, coupled with increased regulation, will, in the coming year, provide more challenges particularly in the area of regulatory reporting. The impact of a number of new accounting standards on the Group's financial reporting will also be analysed and implemented over the coming year.

During the year a restructuring exercise was implemented resulting in the amalgamation of the back office functions of retail investment and proprietary operations. The aim of this exercise was to improve operational efficiency and to benefit from synergies expected to arise due following the amalgamation of similar functions. It also enables Custody Compliance to increase its focus on this line of business and further strengthen compliance measures. The new system dedicated to this area of operations is in the final stages of implementation.

MARIO MALLIA

CHIEF OFFICER RISK MANAGEMENT

The Risk Management function will continue to drive the culture change that is seeing Risk evolving from a custodian of limits to a strategic partner of business.

During the year, the Risk Appetite framework for the Bank will be reviewed, with increased focus on ethics, reputational risk and conduct risk.

The CRD IV regulatory regime, including recovery and resolution planning, will continue to be implemented. Other initiatives include the strengthening of economic and regulatory research, within the office of the Chief Economist; and a review of risk mitigation, to ensure optimal insurance coverage of the Bank's major operational risks.

VICTOR DENARO

CHIEF OFFICER
IT & INFORMATION

During the past twelve months, the Bank continued to enhance its increasing popular and award-winning mobile application platform with additional functionality. Besides the successful implementation of a new Card Management System, 3D secure has been added to provide greater security and peace-of-mind when conducting online purchases.

Moreover, the usage of technologically-enabled alternative delivery channels continue to reach exponential growth. Future upgrades will be amplifying customer experience by applying information and context, rather than merely automating business transactions via straight-through-processing, The Bank will advocate, innovate and grow new digital business capabilities to enrich the user experience, better serve customers, target new customer groups and enter or create completely new business growth opportunities.

KENNETH FARRUGIA

CHIEF OFFICER
FUND SERVICES

Bank of Valletta plc has pioneered the development of the funds industry in Malta. In 1995, the Bank set up Valletta Fund Management Limited ("VFM") as Malta's first fund management organisation to provide investors with access to investment opportunities in the domestic and international capital markets through a choice of professionally managed investment solutions. Over the years, VFM has launched various investment funds denominated in the key currencies aiming to meet the changing investor requirements. VFM's core mission is to continuously strive to meet the investment expectations of its clients aiming to deliver consistent and repeatable performance.

In 2006, Bank of Valletta plc also set up Valletta Fund Services Limited ("VFS") to provide domestic and international asset management organisations with a comprehensive range of fund administration services. The Company's strategic priority going forward is to continue playing a leading role in the development of the funds industry aiming to be the fund administrator of choice for fund managers setting up funds in or out of Malta whilst remaining strongly committed to consistently deliver an efficient service and remain responsive to the changing needs of its clients.

ALBERT FRENDO

CHIEF OFFICER
CREDIT

The Bank will step up further its commitment towards the local economy with particular assistance to SMEs. Already 530 businesses have benefitted from JEREMIE leading to a further top up of the scheme for an additional fund of €11.6 million. It is the bank's strategy to tap further on possible EU structured financing packages for specific objectives. The Bank will remain highly active in the provision of consumer finance, most notably home loan, ensuring high valued propositions and lasting relationships with our customers. Heightened efforts in the areas of debt management and collection will continue to ensure that the Bank's asset portfolio be maintained at satisfactory standards despite the difficult economic climate.

PETER PEROTTI

CHIEF OFFICER
PERSONAL
BANKING

Bank of Valletta will continue to invest heavily in its branch network to ensure that the Bank retains its position as Malta's leading provider of financial services and delivers a quality service in the best interests of the Bank's customers.

During the last financial year the Bank opened six new Investment Centres as one of the initiatives undertaken to reshape the Bank's investment advisory service in line with the changing regulatory environment and investor expectations.

Meanwhile a strategic review has been undertaken at Wealth Management to realign the service offering in the light of regulatory and market developments. This year will present further challenges as Wealth Management re-organises its operation to ensure that all compliance and risk management obligations are being honoured. Further changes will be introduced in line with the UK Retail Distribution Review as the Unit adopts a strong and proactive research function and a strategic asset allocation based on an open-architecture model.

ANTHONY SCICLUNA

CHIEF OFFICER
HUMAN
RESOURCES

Our people are the Bank's most important asset. Having an engaged workforce is vital towards the Bank's sustainable growth. HR will be focusing on key employee areas that foster an environment conductive to employee engagement, namely, recruitment and retention, professional and personal development as well as recognition and reward. As a learning organization operating in a very dynamic competitive environment, the Bank will continue to create opportunities for all staff to further develop their knowledge, skills and competencies. This will translate into better opportunities for our people to deliver the organisation's value to the customer.

Corporate Social Responsibility

Why all the fuss?

As a concept, Corporate Social Responsibility (CSR) has been developing since the early 1970s. There are various interpretations and definitions of this concept. However, in general terms it refers to policies and practices adopted by an organisation in governing its relationship with key stakeholders.

Many an organisation has converted to the outlook that profitability and being a responsible citizen is not an inherent fallacy. The impact of an organisation's operations on society is generally proportionate to its footprint. For a company like Bank of Valletta, whose history is inextricably linked to that of the Maltese society, one of the largest employers on the islands, serving circa 300,000 customers and having a retail network spanning 45 branches, business and investment centres, that footprint is considerable.

Nonetheless, CSR does not present an easy 'plug-in' formula which you adhere to and are automatically recognised as a socially responsible organisation. It is within the organisation itself, where policies yield pervasive responsible behaviour that the game starts. For a financial services provider like BOV, where its people constitute the backbone of the organisation, whether they deal directly with the external customer or not, embracing CSR essentially means building an internal culture of commitment to customers and society. An intimate knowledge of the environment in which the Bank operates and customers' specific needs is indispensable to provide customers with reliable service and added value. It is only by achieving internal excellence in this regard that valid society results can be achieved.

For BOV, CSR has become congruent to the manner in which we manage our business. To a great extent the measure of our success is the difficulty experienced in trying to extract CSR-driven action from the day-to-day management of the business.

Here we outline the highlights of our journey this year.

> If you're strong enough, there are no precedents.
>
> – F Scott Fitzgerald

Shareholders

Corporate Social Responsibility does not contradict the profitability motive. Being sustainable and resilient in our operations is critical, and can only be achieved through sound corporate governance. Good corporate citizenship at Bank of Valletta is a natural progression of good managerial practice.

Hallmark of Innovation

Financial World Innovation Awards

Award Winner 2012 - BOV Mobile

You aren't wealthy until you have something money can't buy.

– Garth Brooks

Community

BOV thanks the BOV Joseph Calleja children's choir at a reception held in their honour.

No man is an island even if he lives on one. Bank of Valletta has long realised that as an organisation with indelible ties with the communities with which it operates, it cannot take the back seat but must act responsibly.

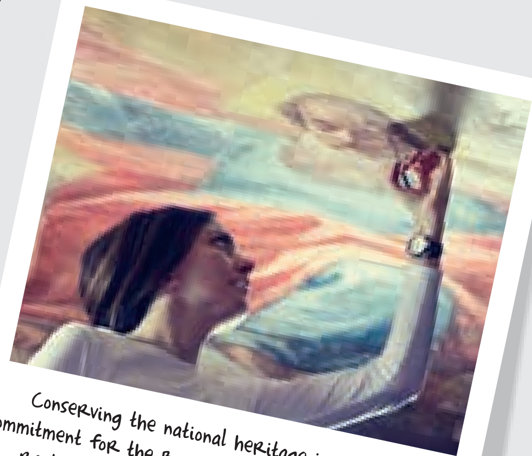
BOV is the patron of local arts and culture. Firm in its belief that local talent is an integral part of the Maltese identity, BOV supports exhibitions, concerts and national festivals that put Maltese culture in the limelight. This year also saw BOV endorsing the internationally-renowned Joseph Calleja. Later in the year, the BOV Joseph Calleja Foundation was launched. This Foundation ties in with the Bank's social arm that invests in NGOs and voluntary organisations which reach out to the most vulnerable members of society. The Bank's belief in holistic education resulted in its endorsement of the National Literacy Project that will come to fruition over the coming months.

BOV actively supports efforts to ensure the national heritage is conserved and presented to the public in the most appropriate way.

Different sport disciplines find the Bank's unyielding support. Bank of Valletta sponsors football, waterpolo and basketball, amongst others.

€4,288.75 were donated to the Appoġġ Children's Fund during a Jeans Day organised by BOV.

L-Istrina BOV Piggy Bank Campaign in full swing across schools in Malta and Gozo raises a total of €732,000. Last year alone €210,000 were donated to this fund.



Conserving the national heritage is an ongoing commitment for the Bank. BOV funds the 18th century restoration works of the Mellieħa Sanctuary.

As a promoter of health and physical activity, BOV continues its support to the Aquatic Sports Association.

Man shapes himself through decisions that shape his environment.

- Reno Dubos

Environment

BOV looks upon the green stakeholder as a key player to be reckoned with. Even if the Bank is a service organisation, it does not shy away from its environmental responsibilities, so much so that it even features as one of the protagonists in its Community Programme.

With the introduction of the Environmental Manager, the Bank crystallised its active commitment towards the conservation of the environment. Over the past year, significant efforts were made towards finding smarter solutions to reduce the Bank's impact on the environment.

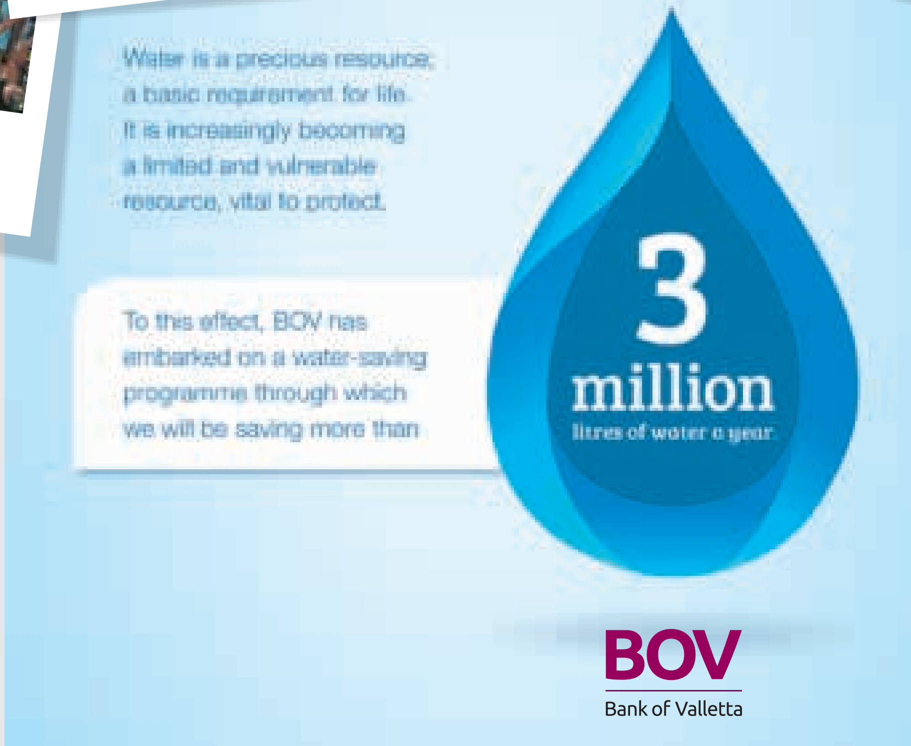
This ethos resulted in a number of activities taking shape this year, which contributed to reducing the Bank's carbon footprint by 144,000 kg. A recently launched water saving programme will yield a total annual saving of 3,000,000 litres of water. These are numbers that matter.

The Bank's green agenda led it to support worthwhile environmentally-friendly initiatives, such as the Dinja Waħda project which is run across all Primary Schools.

Exterior lights at the BOV Head Office were switched off again this year, joining a worldwide initiative marking Earth Hour 2013.

PV panels installed across various BOV sites are reducing CO_2 emissions by circa 100,000kg per annum.

'Green' culture is extended to the children of BOV employees during educational activities which focused on environmental issues.



The BOV Short Film Festival 2013 for BOV employees premiered at the Grandmasters' Suite, Hilton. This red carpet event was organised by the BOV Sports & Social Club.

What we achieve inwardly will change outer reality

– PLUTARCH

People

For BOV, its people are its greatest asset. It may sound cliché, but as a financial services organisation, employees come into play at every junction of the service chain so it can never be otherwise.

Testimony to the Bank's commitment towards its people are the two prestigious awards it brought home in the 11th edition of The Malta People Awards organised by the Foundation for Human Resources Development (FHRD). Our people are the instrument behind our successful growth. The 'Equal Opportunities' award recognises BOV's commitment in ensuring equality, fairness and accountability among its people. The 'Staff Wellness' award confirms the Bank's dedication towards the provision of initiatives that contribute to a holistic approach toward the well-being of BOV employees.

BOV truly believes in building a learning organisation by encouraging the creative thinking of its people, investing in their personal development and creating opportunities for them to broaden their horizons.

BOV places great importance on the healthy lifestyles of its employees. The BOV Health Week included free health checks and screening for its people.

The BOV summer BBQ is a unique opportunity for BOV employees to come together and have fun.

Ten BOV employees forming part of the BOV Staff Volunteers Club clear one of the last remaining intact bomb craters on the island at Fort Rinella.

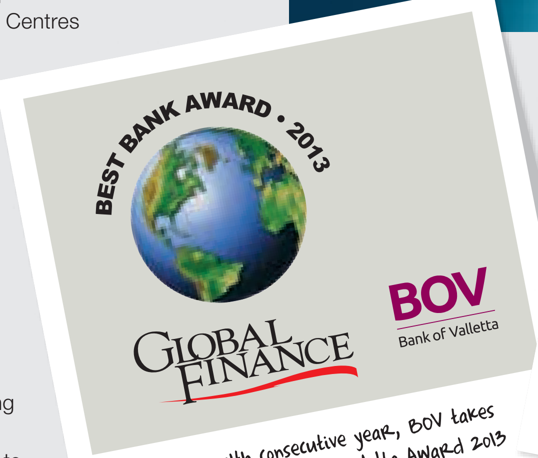
Nothing is so contagious as enthusiasm.

– Samuel Taylor Coleridge

Customers

What has always distinguished Bank of Valletta is that it has always been there for its customers… from the largest investor to the youngest new saver. Enhancing customer experience drives the Bank's innovations and sees it converting its fleet of ATMs, introducing the first Mobile Banking App in Malta and inaugurating six Investment Centres across the islands.

Keeping the customer as its *raison d'être* has always been the main driver behind the Bank's evolution. Last year saw Bank of Valletta move on towards a fresh cycle of change and innovation. It embraced a new bold and fresh visual identity that reflects today's reality, taking into account the Bank's identity and legacy in order to project it forward towards exciting new ventures built around the customer.



For the 4th consecutive year, BOV takes home the Best Bank in Malta Award 2013 which is awarded by Global Finance.

Six new BOV Investment Centres are offering bespoke investment services as part of extensive restructuring of BOV's Investment services.

A socially responsible approach to business needs to be built into the culture of the organisation. This is the journey that BOV embarked upon when it recognised CSR in its Mission Statement in 2006. Since then CSR has become synonymous with the manner in which the Bank manages its business.

Yet the journey goes on. BOV will continue striving to be a trend setter in all it does. As it continues to evolve in response to its market needs, it will remain the innovative, dynamic, forward-looking organisation that it has always been, leading Malta's financial services industry and acting as a catalyst for the country's economic development.

Throughout, it will remain close to its stakeholders, an active citizen within the communities and environment in which it operates, nourishing its people and putting the customer first… always.

The future is purchased by the present.

– Samuel Johnson

The journey continues

BOV
Bank of Valletta

Directors' report as at 30 September 2013

The Directors present their 40th Annual Report, together with the audited financial statements of the Bank of Valletta Group and the Bank for the year ended 30 September 2013.

Principal Activities

The Bank of Valletta Group comprises Bank of Valletta p.l.c. (the Bank), Valletta Fund Management Limited, Valletta Fund Services Limited and BOV Investments 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). It 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. BOV Investments Limited acts as an investment holding company.

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 and reinsurance.

Operational Overview

A review of the business of the Group for the year ended 30 September 2013 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 €0.06 per share was paid on 24 May 2013. The Directors propose a final gross dividend of €0.13 per share, resulting in a total gross dividend for the year of €0.19 per share. The aggregate net dividend for the year is €0.1235 per share, amounting to €37.05 million (2012: €0.171 gross per share as adjusted for bonus issue resulting in a net payout of €33.35 million). The total dividend is analysed as follows:

	The Bank	
	2013	**2012**
	€	**€**
Gross	57,000,000	51,300,000
Tax at source	(19,950,000)	(17,955,000)
Net	37,050,000	33,345,000

Directors' report as at 30 September 2013 (continued)

Board of Directors

The following Directors served on the Board during the period from 1 October 2012:

John Cassar White *(appointed 5 April 2013)*
Frederick Mifsud Bonnici *(resigned 8 April 2013)*
Joseph Borg
Roberto Cassata
Gordon Cordina *(resigned 5 April 2013)*
Ann Fenech *(appointed 19 December 2012)*
George Portanier
Manuel Rizzo *(resigned 19 December 2012)*
Norman Rossignaud *(resigned 19 December 2012)*
Taddeo Scerri *(appointed 5 April 2013)*
Paul Testaferrata Moroni Viani
George Wells
Franco Xuereb *(appointed 19 December 2012)*

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 eleven valid nominations, including five 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 control as the Directors determine is 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

A resolution to reappoint Deloitte Audit Limited (a company forming part of the Deloitte Malta firm) and Deloitte LLP (United Kingdom), as auditors of the Bank will be proposed at the forthcoming AGM. Deloitte Audit Limited and Deloitte LLP have expressed their willingness to remain in office.

The Board has resolved that during Financial Year 2014 a tender process for the external audit contract will be undertaken, with the successful audit firm being proposed to the 2014 Annual General Meeting.

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 39th AGM held on 19 December 2012, on the 17 January 2013, 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 €270,000,000 to €300,000,000 divided into 300,000,000 ordinary shares with a nominal value of €1.00 each fully paid up.

Directors' report as at 30 September 2013 (continued)

At the forthcoming AGM, the Board of Directors is proposing a bonus issue on the 17 January 2014 of 1 share for every 10 shares held. This will result in the issue of an additional 30,000,000 and the increase in the issued share capital of the Bank from €300,000,000 to €330,000,000.

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 2013, 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 2013, 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 2013.

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 2013, 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 2013 (continued)

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 2013 and signed on its behalf by:

John Cassar White
Chairman

Joseph Borg
Director

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CAPITAL AND RISK MANAGEMENT REPORT

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

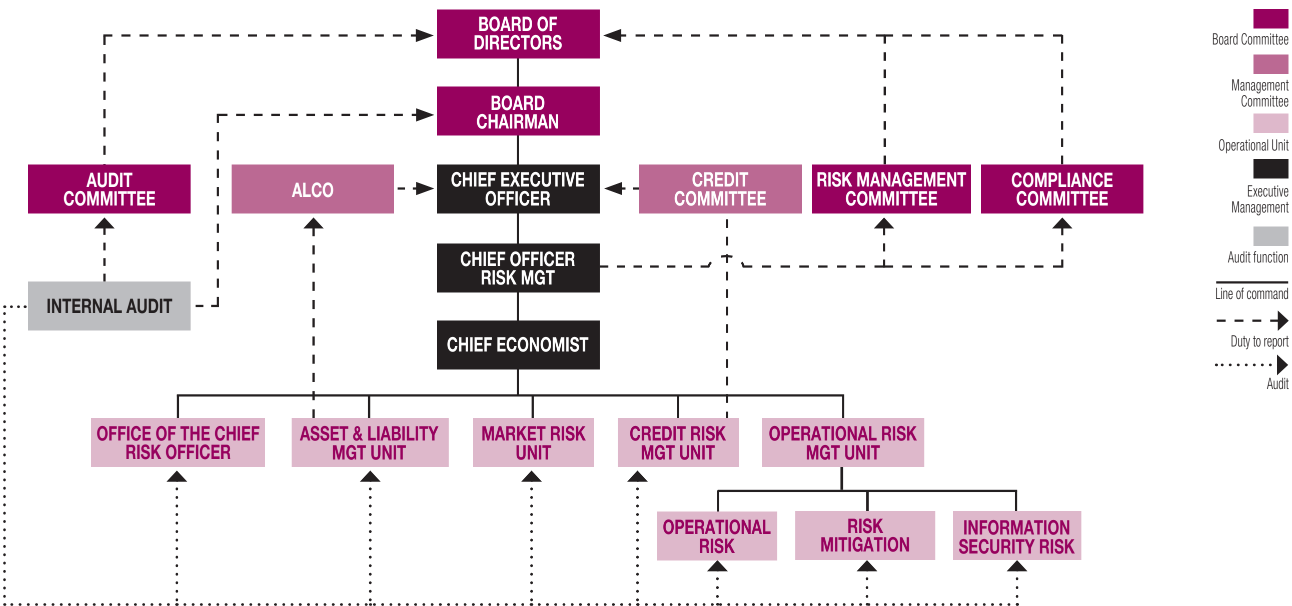
Risk management lies at the heart of the business of financial intermediation. All the Group's activities involve, to varying degrees, taking on and managing risks or combinations of risks.

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 parameters established 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 and Compliance and Financial Control; 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. The Risk Management function at BOV is represented below:



Capital & Risk Management report 30 September 2013 (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 certain loan proposals which fall within the discretionary lending limits of the Credit Committee. 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 2013 (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 Risk Initiatives for Financial Year 2013

During the year, Risk Management continued to drive the bank towards the revised Capital Requirements Directive (CRD IV/CRR) regulatory regime, through on-going monitoring of capital and liquidity buffers, capital forecasts and stress tests. The CRD IV package which transposes – via a Regulation and a Directive – the new global standards on bank capital and liquidity (commonly known as the Basel III agreement) into the EU legal framework, entered into force on 17 July 2013. BOV is already in compliance with the CRD IV minimum liquidity requirements that come into full effect in 2019. On the capital side, the most recent internal capital forecasts continue to show that, barring unforeseen circumstances, the Bank will achieve compliance with CRD IV capital requirements by means of profit generation and retention, and without being required to raise fresh capital on the markets.

The governance structure of the Risk Management function continued to be re-designed in line with current best practice and with the EBA Guidelines on Internal Governance (GL 44) published in September 2011. There were three main changes to the structure during the year. The first was the setting up of the post of Chief Economist, a role taken up by the Executive Head Risk Management. BOV believes that sound economic analysis should underpin all of its business plans, financial budgets and capital forecasts, and the introduction of the post of Chief Economist will be a major step in this regard.

Secondly, the Strategic Planning Unit of the Bank was hived off from the Risk Management function and embedded into a new "Strategy and Process Management" function. The Bank wishes to emphasise the importance that strategy can only be implemented if the necessary processes are in place and functioning effectively.

Thirdly, the Enterprise Risk Management Unit which was set up last year evolved into a new "Office of the Chief Risk Officer" (CRO) – this with a view to strengthening holistic risk management and preparing the Bank for the challenges which will be posed by the Single Supervisory Mechanism (SSM), by means of which BOV will come under the direct supervision of the European Central Bank (ECB). The Office of the CRO brings together a mix of skills – economics, stress-testing, and regulation – which will enable a smooth transition to the SSM.

1.6 Preparations for the Single Supervision Mechanism

One of the outcomes of the Euro sovereign crisis of 2012 is the project of a Banking Union for Europe – a structure intended to carry out effective surveillance and – if needed – crisis management of the banking sector. The key elements of the European

Capital & Risk Management report 30 September 2013 (continued)

Banking Union, which received European Commission approval in October 2013, have been identified as: (1) a Single Supervisory Mechanism (SSM), underpinned by a single rule book of common regulation for all European supervisory bodies; (2) a Single Resolution Mechanism (SRM) for the orderly resolution of problem banks; and (3) a harmonized deposit guarantee system which is funded ex-ante by banks.

The SSM is the first and principal pillar of the proposed Banking Union. It will be composed of the ECB and the supervisory authorities of the member states. The ECB will have ultimate responsibility for the overall functioning of the SSM, but it will be assisted by national supervisory authorities, which have the knowledge of local and regional markets and have a long-established expertise in supervision. The ECB will conduct direct supervision of around 128 significant banks. While this is a fraction of the more than 6,000 banks in the Eurozone, these banks represent approximately 85% of bank assets in Europe. These banks were chosen on a number of criteria stipulated by SSM regulation. The list includes BOV, which was selected for direct ECB supervision in view of its size when related to the GDP of Malta.

Before taking over its supervisory role, the ECB will carry out a comprehensive assessment of the banks that will be subject to its direct supervision. The assessment will consist of three elements: i) a supervisory risk assessment to review, quantitatively and qualitatively, key risks, including liquidity, leverage and funding; ii) an asset quality review (AQR) to enhance the transparency of bank exposures by reviewing the quality of banks' assets, including the adequacy of asset and collateral valuation and related provisions; and iii) a stress test to examine the resilience of banks' balance sheet to stress scenarios. The assessment will be based on a capital benchmark of 8% Common Equity Tier 1.

BOV has put together an inter-disciplinary team, led by the Risk Management Function, to prepare for the SSM, and, in particular, for this comprehensive assessment which will be concluded in October 2014. The team will coordinate the Bank's response to supervisory requirements, liaise with local and European supervisory bodies, and keep the Board of Directors and the Executive Committee constantly updated on developments.

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;
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.

Capital & Risk Management report 30 September 2013 (continued)

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 financial year 2013 the review of the Business, e-Commerce and SEPA Payments policies was continued, in addition to preliminary work on the revision of the Consumer Lending policy.

2.3.2 Decision-making Procedures

Lending authorisation
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. 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 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.

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.

Capital & Risk Management report 30 September 2013 (continued)

- 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.

Collateral values are reviewed on a regular basis and are revalued at time of default if it is found that the carrying value could have changed materially since last valuation.

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 reviews 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 is to ensure that the quality of the lending portfolio is being 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 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 within this financial year 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 the negotiation, 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.

Capital & Risk Management report 30 September 2013 (continued)

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 quarterly risk reporting 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 analysis.

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.

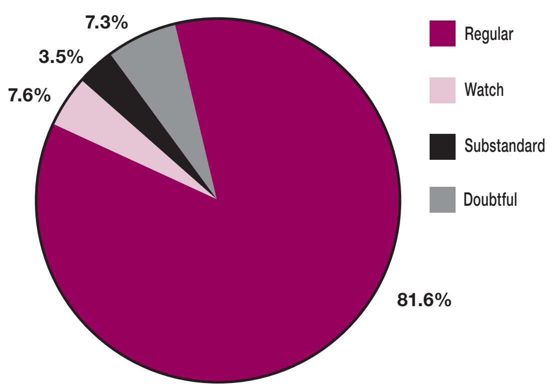
2.4.2 Advances Portfolio

The Bank's advances portfolio to customers stood at €3.8 billion as at end September 2013, representing a decrease of €33.7 million (or 1%) over September 2012. Decreases were mainly registered in the business and consumer segment, whereas the home loans segment continued to experience a steady growth.

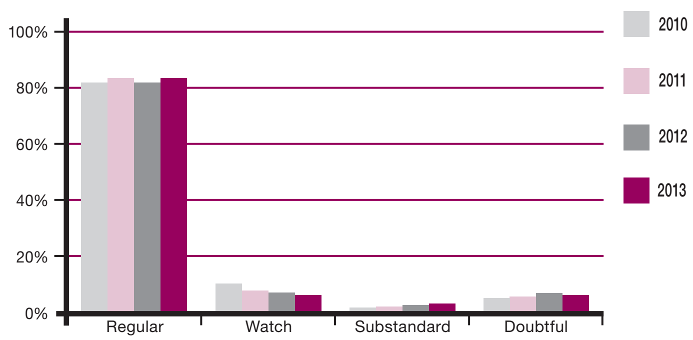
Tight control of the loan book has ensured that there has been no significant deterioration in the overall credit quality of the advances portfolio with 82% of the total portfolio classified in the regular category (81% as at end September 2012).

Doubtful loans decreased to 7.3% of the loan book as at end September 2013 compared to the 7.4% outstanding a year earlier. The Bank took a cautious approach and increased its loan loss coverage ratio from 51.4% to 63.7%.

Asset Quality by Credit Grading



Credit Quality of the Loan Book (% of total)



The advances portfolio has an average maturity of 18 years. Business loans have an average maturity of 10 years, home loans a maturity of 27 years while consumer loans have an average maturity of 5 years.

Residual Maturity of the advances portfolio, broken down by exposure classes (€ million)

	Within 3 months	Between 3 and 12 months	Between 1 and 5 years	Over 5 years	Total
Home Loans	1.1	2.8	13.6	1,382.4	1,399.9
Personal	6.3	59.3	3.5	6.4	75.5
Corporates	43.5	28.0	79.6	79.9	230.9
Retail	273.0	28.7	144.4	267.7	713.8
SME	279.0	32.3	182.9	459.8	954.0
Sovereign	67.7	5.7	21.7	371.1	466.2
	670.6	156.8	445.8	2,567.3	3,840.5

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Exposure by Industry of the advances portfolio, broken down by exposure classes (€ million)	Accommodation & Food Services Activities	Construction	Manufacturing	Households & Individuals	Transport & Storage	Wholesale & Retail Trade	Others	Total
Home Loans	-	-	-	1,399.9	-	-	-	1,399.9
Personal	9.6	-	-	57.3	-	3.7	4.9	75.5
Corporates	73.7	63.1	2.2	-	54.4	10.9	26.6	230.9
Retail	60.7	80.7	51.7	159.5	17.8	197.8	145.5	713.8
SME	117.1	145.7	92.2	-	161.6	163.5	273.9	954.0
Sovereign	-	-	-	-	63.4	-	402.8	466.2
	261.1	289.6	146.1	1,616.8	297.3	375.8	853.8	3,840.5

2.4.3 Impaired Exposures

At each balance sheet date, 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.

The Bank carries out an impairment test on facilities above a certain threshold requested to be rescheduled, to ascertain whether the facilities can be repaid through the operations of the borrower. Should there be warning signs that repayment from operations is uncertain; the facilities are graded “Doubtful” on the Bank’s Internal Rating System. Should repayment remain uncertain, even after taking account of collateral, the loan is marked as “impaired”.

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 financial year ended 2013 included amendments to the contractual timings, hereby referred to as term extensions.

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. Customers are identified for forbearance treatment following initial contact from customer, in the event of payment arrears or when the customer is transferred to debt collections or litigation unit.

2.4.5 Loan Loss Allowances and Coverage

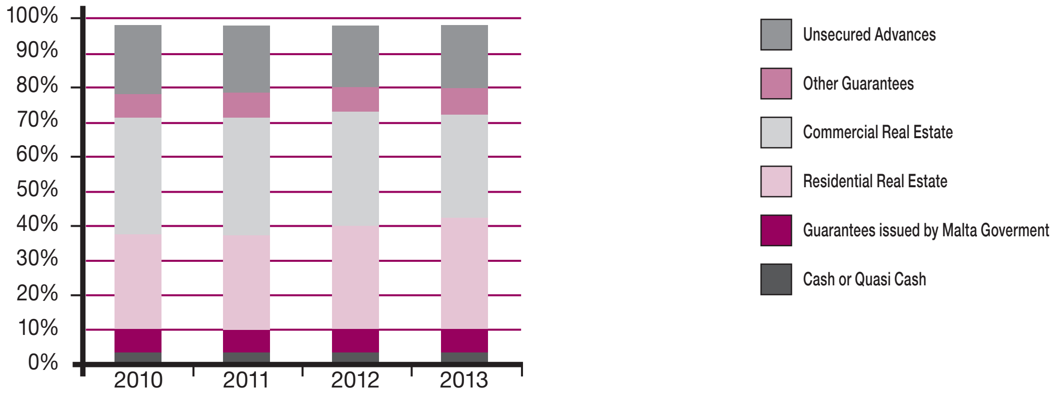
The Bank’s impairment allowance methodologies are compliant with International Financial Reporting Standards (IFRS) and with Banking Rule BR/09. The latter regulation is undergoing extensive revision; the consultation period has expired on the 30 September 2013. Current regulation requires that an impairment allowance is made whenever the likely recoverable amount of a facility falls short of the Bank’s exposure.

As at end September 2013, impairment allowances amounted to 2.9% of the total loan book (2012: 2.3%) and 63.7% of impaired (non-accruing) loans (2012: 51.4%). The significant improvement in the coverage ratio was the result of the cautious approach adopted by the Bank that increased the collective and specific loan loss coverage.

An analysis of the collateral cover reveals that 83% of the Bank’s advances portfolio is covered by extendible security, out of which 78% is in the form of immovable property (residential and commercial).

Capital & Risk Management report 30 September 2013 (continued)

Advances Coverage – Collateral Cover



2.4.6 Specific Impairment Allowance

An impairment allowance is created whenever a loan is graded Doubtful. A loan is graded in this category when:

a) payments of interest and/or capital are overdue by 90 days; or
b) in circumstances where, irrespective of the repayment not being overdue by 90 days, the Bank has reasons to doubt the eventual recoverability of funds.

The Bank determines the percentage of provisioning that should be applied when an account is graded Doubtful, in line with Banking Rule BR/09/2008. An impairment allowance equal to 100% of the outstanding unsecured balance of the loan is made when a loan is graded Doubtful for qualitative reasons. In cases of overdue credit facilities, an allowance is made on the outstanding unsecured balance of the individual credit facility on the following basis:

Over 3 months, but not exceeding 6 months	25%
Over 6 months, but not exceeding 12 months	50%
Over 12 months	100%

Where a credit facility has been graded Doubtful for 12 months, the Bank further provides for 10% of the outstanding balance less specific allowances already applied. Once an account has been graded as Doubtful and provided against, all interest accruing on that account is immediately suspended i.e. such interest is no longer recognised as income or as an asset in the financial statements.

The specific and collective allowances held as at September 2013 are shown in the table below:

€'000s	Specific Allowance		Collective Allowance	
	Stock	Charge	Stock	Charge
Business	53,395	19,731	43,362	1,423
Home Loans	3,536	1,021	2,766	4
Personal	3,914	641	3,826	(122)
Total	60,844	21,393	49,954	1,305

2.4.7 Collective Impairment Allowance

Credit facilities 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. In all instances the collective allowance was increased to better reflect the probability of default in these sectors.

2.4.8 Concentration Risk and Sectorial Overview

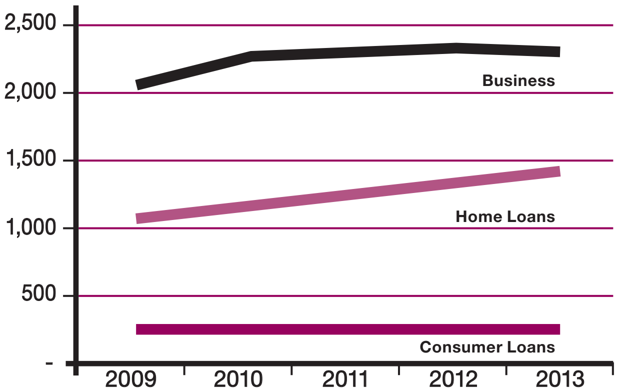
Given the size and nature of the domestic financial sector and the local economy, the Bank is exposed to concentration risk in its credit business. Concentration results when the Bank has a high level of exposure to a single name or to a related group of borrowers, to credit exposures secured by a single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

Capital & Risk Management report 30 September 2013 (continued)

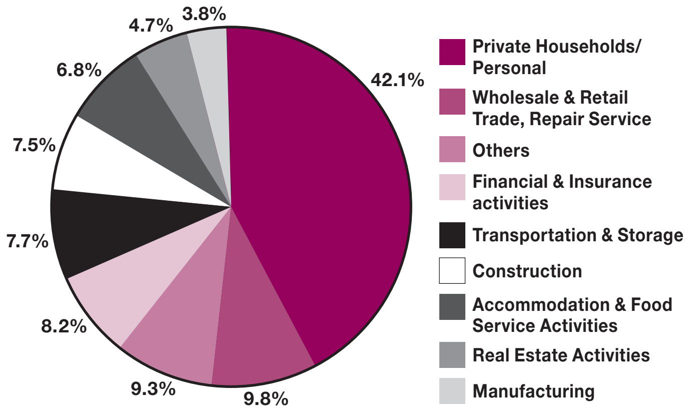
The Bank's credit risk management approach is to avoid any undue concentrations in its portfolio. There are systems in place to identify material concentrations and to ensure adherence to prudential limits set by the Board of Directors and/or the Regulatory Authority to single borrowers or groups of 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 one and half times the Group's capital base.

Concentration by Business Segment (€million)



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 36.0% 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 65%. The home loans segment is healthy with only 3.56% 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] CAR as at end September 2013 is 16.5%	Baseline Change in CAR	Negative Change in CAR
1. Increase in doubtful loans[2]	-0.40%	-1.02%
2. Increase in doubtful loans of the construction and Real Estate Sectors.	-0.16%	-0.39%

[1] The stress tests do not represent a forecast of future events.
[2] In both scenario 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.

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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.

2.7 Settlement Risk

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

2.8 Credit Risk in the Investment Portfolio

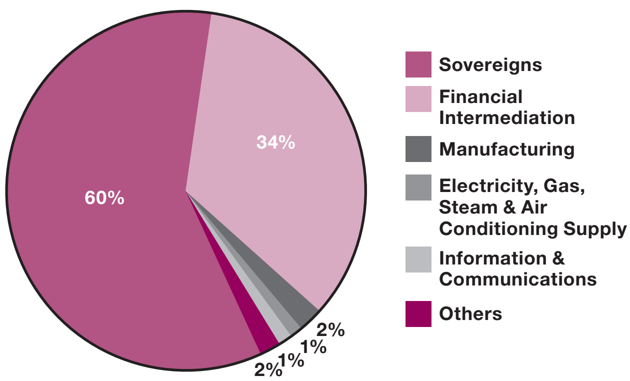
The Bank is exposed to credit risk through its investment activities. These investments include deposits with banks, debt securities, equities, and derivative financial instruments but exclude any working balances such as balances with the Central Bank, current and call accounts. The investment portfolio 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, derivatives and brokers. 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.

Despite the number of downgrades announced in recent months by credit rating agencies, 96.04% of the Bank's investment portfolio was of an investment grade at year end (September 2012: 95.10%).

Sectorial Concentration - Investment



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.

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 Treasury Management Policy (TMP) limits the use of derivatives (a) to hedge a balance sheet position (b) to 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 denominated in the local currency or in hard foreign currencies.

Capital & Risk Management report 30 September 2013 (continued)

Wrong way risk arises when the exposure to a counterparty is positively correlated with general market risk factors, 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. No agreements are needed in the case of currency swaps and foreign exchange forward contracts. 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 derivative exposures, the Bank classifies derivatives into two main groups: forward based and option based. The exposure amount of forward based derivatives is calculated by using the Original Exposure Method where the notional amount of each instrument is multiplied by pre-defined percentages according to maturities. For calculating the exposure value of interest-rate contracts, the Bank uses the residual maturity of the contract, whereas for all other foreign exchange contracts, the original maturity is used. With regards to option based derivatives, short option-based positions (selling options) are excluded since these do not pose a counterparty risk, whereas the exposure of long option positions is calculated by using the Mark-to-Market model.
The table below includes information exclusively related to exposures subject to counterparty risk. All exposures are calculated using the Original Exposure method except the equity options which are marked to market.

Derivative Financial Instruments by Notional Amount and Type								
	€000s							
	< 1 Year		**1 - 2 Years**		**> 2 Years**		**Total**	
	Notional Amount	Exposure Value	Notional Amount	Exposure Value	Notional Amount	Exposure Value	Notional Amount	Exposure Value
Interest Rate Swaps	134,280	671	24,653	247	385,762	30,158	544,695	31,076
Cross Currency Interest Rate Swaps	-	-	-	-	2,081	100	2,081	100
Currency Swaps	298,688	60	-	-	-	-	298,688	60
Foreign Exchange Forwards	54,913	11	28,055	14	-	-	82,968	25
Equity Options	-	-	-	-	3,650	815	3,650	815
	487,880	**742**	**52,708**	**261**	**391,493**	**31,072**		

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.

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.

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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:

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.

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.

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.

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.

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

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. On a monthly basis, ALM carries out sensitivity analysis on the Bank's balance sheet, to calculate the estimated impact of an immediate 200 basis points increase in yields on the economic value. This impact is normally expressed as a percentage of the Group's regulatory capital base. Impacts have only been shown in one direction but can be assumed to be reasonably symmetrical. At end September 2013 the impact on economic value was estimated at 1.89% (September 2012: 0.02%).

Capital & Risk Management report 30 September 2013 (continued)

	30 September 2013 €000s	30 September 2012 €000s
Impact on Capital	11,180	107

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 2013 €000	30 September 2012 €000
Total	**8,638**	**8,739**
EUR	8,767	9,571
GBP	(656)	(709)
USD	(649)	(909)
AUD	791	931
CAD	(89)	(39)
JPY	127	79
Other	348	(185)

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.

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 insignificant.

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. During the year, the Bank has reviewed its scenario analysis to bring it in line with the stress tests carried out by EBA. In order to carry out this stress testing, the Bank makes use of the Moody's default tables for Corporates (1920-2012) and Sovereigns (1983-2012). 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 2013 is 11.7%	Baseline Change in Tier 1	Negative Change in Tier 1
Parallel shift in credit spreads on the investment portfolio[1]	-1.59%	-3.17%
Expected default on the investment portfolio[2]	-0.43%	-0.50%

[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 (1983-2012) and Corporates (1920-2012) under the baseline and a further one notch downgrade in the case of the Negative scenario

Capital & Risk Management report 30 September 2013 (continued)

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. Risk assessments have been carried out on most customer-facing end-to-end processes and are now at various stages of implementation of recommendations.

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 as a non-financial risk dashboard on a bi-monthly basis to the Executive Committee and quarterly to 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 Management (BCP). 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. The operational risk regulatory requirement for the Group as at September 2013 is €30.7 million (Notional Risk Weighted Assets €383.4 million) which adequately covers both expected and unexpected losses.

4.3 Mitigation of Operational Risk

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 bring a potential unacceptable level of reputation risk.

BOV adopts the Code of Principles of Good Corporate Governance that show the commitment of the Group 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 publishes its Corporate Social Responsibility Report which describes the Group's efforts to conduct its operations in a manner that is environmentally and socially responsible and which contributes to society.

Capital & Risk Management report 30 September 2013 (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 to 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 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 covered under Section 4.2 above.

Furthermore as from October 2013 BOV launched a strategic initiative 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 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 2013.

The target population defined as Identified Staff for the purposes of this Report represents 3.69% of total number of employees in the Group. Identified Staff was determined in line with recommended EBA Regulatory Technical Standard[1] and includes:

- senior executives responsible for 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 0.25% 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(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 (CP47/CP46 on data collection for high earners). The table below therefore includes total fixed and variable remuneration and number of beneficiaries per and within each business area.

Remuneration of Identified Staff

	Investment Banking	Retail Banking	Asset Management	All Other[1]
No. of Beneficiaries	2	24	4	29
Fixed remuneration	€122,090	€1,404,509	€232,960	€1,821,269
Variable remuneration	€4,572	€45,314	€25,060	€67,126

[1]Includes Identified Staff from support units, risk management and control functions amongst others.

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 H and EH 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.

1 EBA Consultation Paper EBA/CP/2013/11 dd 21.5.2013

Capital & Risk Management report 30 September 2013 (continued)

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. During the financial year under review, more weighting was given to quality and compliance aspects of KPIs. The key risks addressed related mainly to the area of investment sales, particularly focusing on clients, products and business practices 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. The rollout of risk and compliance weighted KPIs to all the Bank's units is an on-going process, and has reached an advanced stage.

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 may also result from the inability to sell a financial asset quickly at a price close to its fair value.

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. On a daily basis, the Group is exposed to 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.

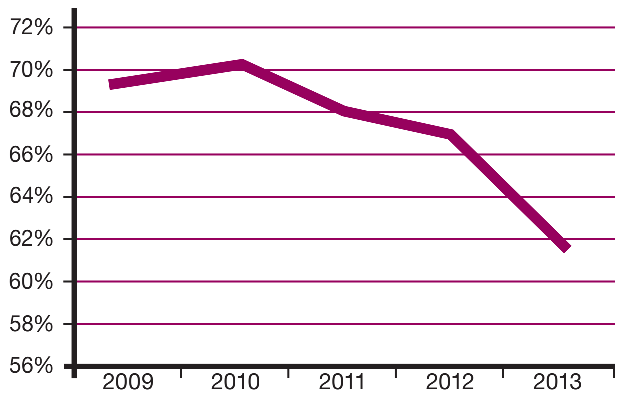
The management of liquidity risk within the Group is the responsibility of the ALCO committee. Effective liquidity risk management helps ensure that the Bank is in a position to fund increases in assets and to meet obligations as they become due, without incurring substantial losses.

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 2013 the loan-to-deposit ratio stood at 61.7% showing that the Group improved its already 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 54.7%, well above the statutory minimum of 30%.

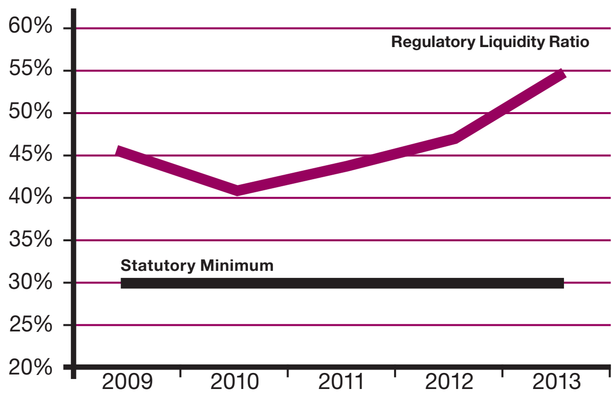
The Bank continued its preparation towards the introduction of the new liquidity regulations introduced by the Basel Committee on Banking Supervisions (BCBS) in December 2010, through the "International framework for the liquidity risk measurement, standards, and monitoring". This document introduced two liquidity ratios, the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). The introduction of these ratios is subject to an observation period, during which banks are being subjected 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. These regulations were somewhat relaxed in April 2013 in the "Report to the G20 Finance Ministers and Central Bank Governors in monitoring and implementation of Basel III regulatory reform" issued by the BCBS.

The LCR and NSFR are now embedded in European law, by way of the CRD IV package. The LCR will be phased in at 60% in 2015, with full implementation of 100% in 2018. BOV has already achieved the minimum levels of liquidity required by both regulatory ratios.

Loans to Deposit Ratio



Regulatory Liquidity Ratio



Capital & Risk Management report 30 September 2013 (continued)

5.3 The Mitigation of Liquidity Risk

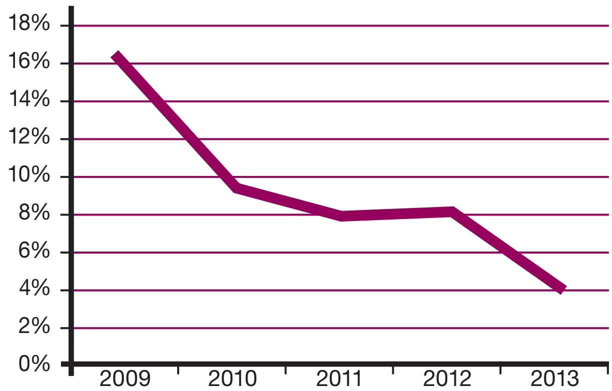
The Group mitigates liquidity risk by maintaining a sufficient fund of liquid assets. This is made up of cash, substantial balances with other banks and a pool of financial assets which are eligible as collateral against borrowing from the European Central Bank (ECB) or on the repo markets. ALCO also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

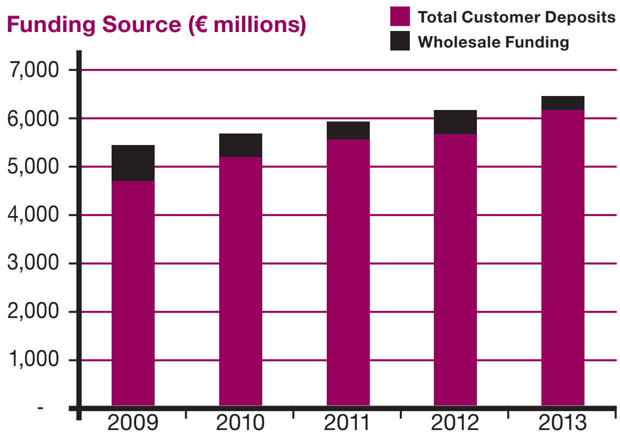
In addition, ALCO maintains an on-going oversight of forecast and actual cash flows, by monitoring the availability of funds to meet commitments associated with financial instruments. The Bank has been successful in its drive to build and maintain a large and stable customer deposit base. This has helped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

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 plc 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.

Capital & Risk Management report 30 September 2013 (continued)

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.

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 jointly owned by Bank of Valletta plc with Insight Investment Management (Global) Limited as minority shareholder. On the other hand, VFS was set up in 2006 as a fully owned subsidiary of Bank of Valletta plc to provide asset managers with a comprehensive suite of administration services to investment funds.

VFM is licensed by the Malta Financial Services Authority to operate as a 'Maltese Management Company' pursuant to the Undertaking for Collective Investment in Transferable Securities Regulations (UCITS). By way of delegation of the investment management activities, VFM manages various collective investment schemes and is also responsible for the promotion thereof in line with the Markets in Financial Instruments Directive (MiFID). In this respect, VFM has an established risk management process aimed at identifying and managing the risks relating to its activities. VFM operates a Risk and Regulatory Committee with the responsibility to monitor and manage the various risks faced by the Company. VFM also has in place a business continuity policy aimed at ensuring the continuity to its activities through the appropriate management of incidences leading to business interruption. Insofar as the Company's fund portfolios are concerned, VFM, in conjunction with its delegates, monitors and assesses their exposure to the various instruments held by the funds managed by the Company ensuring their adherence to the respective investment objective, policies and restrictions.

On the other hand, in providing its fund administration services, VFS is exposed to both operational and reputation risks, and to a lesser extent market risks. To mitigate these risks, VFS has in place compliance and risk monitoring program wherein the Company's various processes and procedures are duly reviewed. In addition, periodic audits of the Company's various operations are undertaken by the Group's Internal Audit department. VFS engaged an independent audit firm to perform an examination of its processes and controls for the period November 2011 to October 2012. This independent examination consisted of an evaluation of the design and operating effectiveness of the controls of the Company and was successfully completed in June 2013. 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 supported by the ALM unit.

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 main assumptions underlying the forecast continue to be based on the projection of the macroeconomic conditions in the local economy, and to a lesser extent in international economies. Three scenarios are considered (baseline, optimistic and pessimistic) to reflect the uncertainties in the macroeconomic environment. The model has been enhanced to cater for the new Capital Requirements under CRD IV. The projections for the period FY 2014- 2016 show that capital ratios are expected to remain strong and well over the statutory minima for all of the horizon 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

During FY 2013, the Group placed much of its emphasis and monitoring on Core Equity Tier 1 capital ratio. 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 are determined according to credit ratings provided by eligible External Credit Assessment Institutions (ECAIs), or by using the applicable regulatory risk weights for unrated exposures. The Group assigns risk weights to the credit risk of the Treasury

Capital & Risk Management report 30 September 2013 (continued)

Portfolio in accordance with the rating assigned by Fitch, Moody's and S&P, all of which are MFSA eligible ECAIs, in accordance with article 3.9 of Appendix 2 – Section 1.4 Credit Risk: Standardised Approach Recognition of ECAIs and Mapping of their Credit Assessment – BR 04/2010.02. The Basic Indicator Approach requires that the Group allocates capital for operational risk 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).

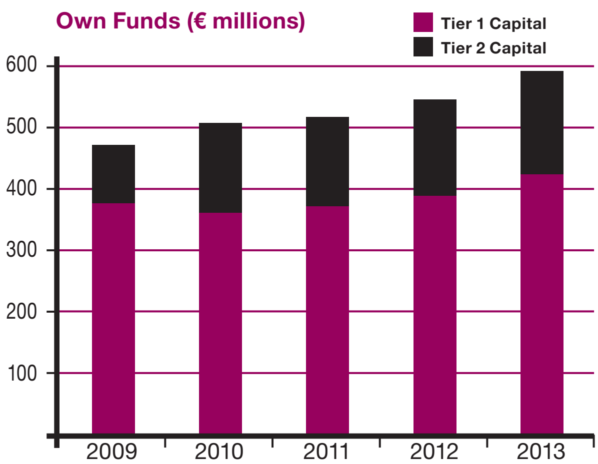
The following table shows the breakdown of the total available capital to the BOV Group as at end September 2013, and its Core Equity Tier 1 capital ratio and Capital Adequacy Ratio at the same date.

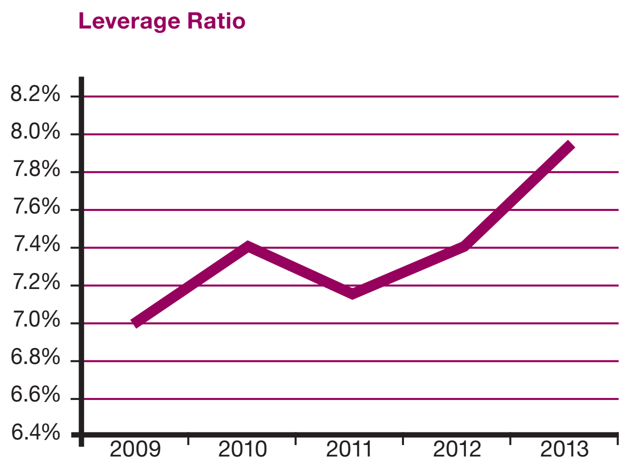
Own funds	**Sep-13 The Group €000**
Tier 1	
Ordinary Shares	300,000
Share Premium	988
Retained Earnings	159,968
Non-controlling interest	661
Deductions	
Intangible Assets	(11,495)
Participations held in insurance undertaking 50%	(26,435)
Unrealised net losses on AFS financial assets	(4,519)
Total Tier 1 Capital	**419,168**
Tier 2	
Available-for-sale Reserve	5,260
Property Revaluation Reserves	23,880
Collective Impairment Allowances	49,954
Subordinated Loan Capital	120,000
Deductions	
Participations held in insurance undertaking 50%	(26,435)
Total Tier 2 Capital	**172,659**
Total Own Funds	**591,827**
Tier 1 Ratio	**11.7%**
Total Capital Ratio	**16.5%**

Capital Allocation by Exposure Class

	Nominal amount	Risk weighted assets	Capital Allocation
	€'000	**€'000**	**€'000**
Central Govt or Central Bank	1,450,049	4,277	342
Regional Govt or Local Authorities	161,609	6,969	557
Institutions (Banks)	825,534	296,464	23,654
Corporates	475,491	370,669	29,654
Retail	1,663,464	1,342,482	107,399
Secured by Real Estate	1,208,674	423,036	33,843
Past Due items	242,410	129,269	10,342
High Risk Areas	87,843	91,648	7,332
Short-term claims on institutions	255,683	51,137	4,091
Other items	887,201	186,802	14,944
Off Balance Sheet items		304,647	24,372
Operational risk		383,350	30,668
		3,590,750	**287,260**

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 under BR/03/2011 Appendix 2 Section 2.1.7. 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. In addition, both issues have an original maturity over 5 years. As these issues have a remaining maturity over 5 years, and they have all been fully paid up, the full value of these securities was included.





The Group also monitors a non-risk-weighted leverage ratio, which relates accounting capital to net tangible assets, as part of its capital management. The Group's accounting leverage ratio stood at 7.95% as at September 2013. As part of its preparations to adhere to the CRD/CRR requirements, the Bank is also monitoring the new regulatory leverage ratio required by law. The group is already fully compliant with this requirement.

Capital & Risk Management report 30 September 2013 (continued)

8.3 EBA Capital Recommendation on the Preservation of Capital

On the 26 June 2013, the European Commission adopted its long-awaited proposal to strengthen the European banking sector through stricter capital requirements, and better liquidity management, obliging more than 8.300 banking institutions to hold more and better quality capital to prevent markets from "drying up" in times of crisis. The Capital Requirements Directive (CRD) and Regulation (CRR) package will enter into force in January 2014, with full implementation in 2019.

In this context of a changing legal framework the EBA decided that the capital buffers established by its December 2011 recommendation should be replaced by a new measure on capital preservation. Under this measure, supervisors are expected to ensure that credit institutions have a Tier 1 capital buffer equal to or above the nominal capital amount needed for meeting the requirements as at June 2012. This nominal floor is being actively monitored by the supervisor in conjunction with the EBA, to ensure that it is maintained.

Competent authorities are also expected to assess the capital plans of credit institutions. These plans should explain how credit institutions will comply with the requirements of the CRD/CRR, and should cover the whole transition period until full implementation and application of the legislation.

8.4 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 fifth ICAAP capital document, which, was approved by the Board on March 2013 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 Chief Officer Risk Management assumed responsibility for ensuring ICAAP implementation and for approving the technical details of the capital allocation. The Executive Head Risk Management also acts as ICAAP Executive and was responsible for the ICAAP project and for liaison with the regulatory authorities. There was constant senior management oversight during the whole implementation phase of the ICAAP exercise.

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.

8.5 Stress Testing

The principal tool used by the Group to assess its state of risk readiness is stress testing. The Group prefers stress testing over other risk measurement techniques such as VAR because it is forward-looking, flexible and easily understood. Stress testing at BOV has been developed from a compliance issue (execution of EBA/ECB-mandated tests) into a tool to provide the Board with an assessment of the resilience and sustainability of the business.

Stress testing – both for regulatory and internal purposes – is conducted the Office of the CRO. Most stress testing today is carried out to assess the resilience of capital buffers, but plans are in hand to extend this technique to liquidity buffers. Stress is assumed to arise from economic, market or operational factors, or from a combination of all.

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 interests 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 composition of which is set out below, and whose main role and responsibilities are to execute agreed strategy and manage the business.

Corporate governance statement of compliance (continued)

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, is invited to attend the Board meetings unless inappropriate to do so, albeit without a vote, in order to ensure his full understanding and appreciation of the Board's policy and strategy, and so that the Chief Executive Officer can 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 (iv) and (v) 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 two of the Directors because of their length of service on the Board (an average of 18 years), the Board is of the opinion that this has not undermined the said Directors' 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.

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

The Board usually meets twice a month unless further meetings are required. A Board Meeting specifically dedicated to Strategy was also held during this financial year.

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: 26 Attended	
John Cassar White *(appointed Chairman on 5 April 2013)*	15	(out of 15)
Frederick Mifsud Bonnici *(resigned on 8 April 2013)*	11	(out of 11)
Joseph Borg	26	
Roberto Cassata	10	
Gordon Cordina *(resigned on 5 April 2013)*	10	(out of 11)
Ann Fenech *(appointed on 19 December 2012)*	14	(out of 19)
George Portanier	25	
Manuel Rizzo *(resigned on 19 December 2012)*	5	(out of 7)
Norman Rossignaud *(resigned on 19 December 2012)* *	Nil	(out of 7)
Taddeo Scerri *(appointed on 5 April 2013)*	10	(out of 15)
Paul Testaferrata Moroni Viani **	17	(out of 17)
George Wells	25	
Franco Xuereb *(appointed on 19 December 2012)*	18	(out of 19)

* Norman Rossignaud did not attend Board meetings due to health reasons

** 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 CPA, FCCA, FIA 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 Executive Head Group Internal Audit, the Chief Executive Officer, the Chief Officer Risk Management, the Chief Officer Finance 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.

	Meetings Held: 9	
Members	**Attended**	
Taddeo Scerri *(Chairman appointed in April 2013)*	6	(out of 6)
Joseph Borg *(Chairman up to March 2013)*	3	(out of 3)
Paul Testaferrata Moroni Viani	9	
George Wells	8	

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

The Chief Executive Officer attends the Remuneration and Nominations Committee meetings where appropriate. The Company Secretary also acts as Secretary to the Remuneration and Nominations Committee.

The Risk Management and Compliance Committee (up to 16 April 2013)

	Meetings held: 3	
Members	**Attended**	
Gordon Cordina *(resigned on 5 April 2013)*	3	
George Portanier	2	(out of 2)
Paul Testaferrata Moroni Viani	3	
George Wells	3	
Franco Xuereb *(appointed on 19 December 2012)*	1	(out of 1)

In April 2013, the Board of Directors resolved to split the functions of the Risk Management and Compliance Committee (RMCC) into two Committees: the Risk Management Committee and the Compliance Committee. The restructuring took place in view of the increase in diversity and complexity of the topics with which the RMCC had been dealing.

The Risk Management Committee (as from 17 April 2013)

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 I.T., 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 also acts as Secretary to the Risk Management Committee.

	Meetings Held: 2
Members	**Attended**
Joseph Borg (Chairman)	2
Paul Testaferrata Moroni Viani	1
George Wells	2
Franco Xuereb	2

Corporate governance statement of compliance (continued)

The Compliance Committee (as from 17 April 2013)

The primary objective of the **Compliance Committee** is to assist and guide the Board of Directors in the discharge of their obligations imposed by regulation from time to time 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 upon invitation. The Company Secretary also acts as Secretary to the Compliance Committee.

	Meetings Held: 2
Members	**Attended**
George Portanier (Chairman)	2
Joseph Borg	1
Paul Testaferrata Moroni Viani	2
Franco Xuereb	2

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.

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 it operates within a Board approved credit-sanctioning limit. Proposals falling outside this limit are referred, with the Committee's recommendations, to the Board for consideration and determination. To operate, the Committee needs to be fully constituted and for this reason each member has an approved specific alternate. The Credit Committee is chaired by the Chief Officer Risk Management and has as members the Chief Officer Credit, the Executive Head Corporate Finance, the Head Credit Risk and a Credit Risk Analyst.

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.

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 (both internal and external) of management and employees is a priority, including through 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 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.

Corporate governance statement of compliance (continued)

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. Four 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.

Principle 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 2013 were as follows:

	Beneficial Interest *	**Non-Beneficial Interest ** **
George Portanier	6,496 shares	-
Paul Testaferrata Moroni Viani ***	7,063 shares	-
George Wells	8,013 shares	-

* *These interests include any shares held by spouses*

** Franco Xuereb held 8,999,968 shares by way of non-beneficial interest in his capacity as one of the five trustees of the BOV Employees' Foundation

*** 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 2013, the Directors below also held the following****:*

John Cassar White	10,000	BOV 4.25% Medium Term Notes 2019
Ann Fenech	39,000	BOV 4.80% Subordinated Bonds 2020
George Wells	16,500	BOV 5.35% Subordinated Bonds 2019
	22,400	BOV 4.80% Subordinated Bonds 2020
	15,000	BOV 4.80% Medium Term Notes 2018

***** These interests include any holdings held by spouses*

Principle 12: Corporate Social Responsibility (CSR)

The Bank recognizes it has an important role to play in being an active corporate citizen within the Maltese society in which it operates. It is committed to contribute to the social, cultural and economic development of the country through the efficient management of resources for the benefit of all its stakeholders.

The Bank has always regarded its people as the organisation's most valuable asset. The Bank promotes a healthy lifestyle and wellbeing for its employees, and has a number of programmes in place to help them maintain a stress-free balance between their work and private life. Employees are also encouraged to fulfil their role in the community. Events like blood donation, dress down days in aid of charities and tree-planting were organised throughout the year to actively involve employees.

The Bank's Green agenda has long been featuring in the Bank's Mission Statement. This crystallises the Bank's commitment not only to lessen its impact on the environment, but also to actively promote conservation and safeguarding the green stakeholder. The appointment of the Green Manager and the Green Leaders paved the way to the Bank's ongoing journey to reduce its carbon footprint whilst instilling more environmental-friendly practices.

The Bank's roots run deep into the community in which it operates. The sound principles of 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 – During the financial year under review, the Bank supported a spectrum of musical initiatives, from the festivals organised by the Manoel Theatre and the two main Gozo theatres, to more intimate concerts by some of Malta's talented performers. It remained a leading sponsor for the Malta Philharmonic Orchestra. The year 2013 saw BOV endorsing the Maltese Tenor, Joseph Calleja, along with the BOV Joseph Calleja Children's Choir. The Bank helped a considerable number of artists with their exhibitions and its own annual event at the BOV Centre featured works by Richard England.

Heritage – The Bank gave its backing to important restoration projects like the vault of the Sanctuary in Mellieħa and the masterpieces in Għajnsielem Chapel. The Bank's support to Fondazzjoni Wirt Artna led to the purchase of two faithful replicas of 24-pounder iron carronades which have now taken residence in the Malta Military Heritage Park at Lascaris, Valletta. Kindling a passion for our common past in the younger generation is the main goal of the *Hands-on-Heritage* programme which offers students the unique opportunity to handle period instruments and tools, and learn how they were used.

The Environment – The Bank once again gave its backing to Dinja Waħda, a nationwide education and awareness campaign run in collaboration with environmental NGO BirdLife Malta, which targets thousands of school children and instils in them appreciation for Malta's fauna and flora. The Bank continued to support the BOV Adventure Park at Ta' Qali, which offers children and family much needed green space.

Corporate governance statement of compliance (continued)

Education – The Bank joined forces with the Ministry for Education and Employment to combat illiteracy through the National Literacy Campaign. BOV renewed its support as the educational partner of the University of Malta in the Degree*Plus* Programme, which gives University students the unique opportunity to gain a holistic education that goes beyond academic qualifications. Excellence in education was also promoted through the support of various educational awards.

Social Causes – Various NGOs and philanthropic organisations benefit from the Bank's assistance towards different projects. Throughout the year under review, the Bank supported id-Dar tal-Providenza, Inspire and Caritas. Through the L-Istrina BOV Piggy Bank Campaign the Bank promoted the culture of generosity amongst school children, while at the same time boosting the children's donations with its own financial support.

Sport – The Bank promotes a healthy lifestyle by supporting various sporting associations and encourages the Maltese public to participate in sporting initiatives. The Bank renewed its support for football, basketball and waterpolo leagues and also supported tennis and sailing.

Strategic Alliances – Through strategic alliances, the Bank builds networks with members of the main business organisations, such as the Malta Chamber of Commerce, Enterprise and Industry, the Malta Hotels and Restaurants Association and the Chamber of Engineers.

C. NON-COMPLIANCE WITH THE CODE

Principle 3 (executive and non-executive directors on the Board) and Principle 4 (Code Provision 4.2.7):

The Code recommends "the development of a succession policy for the future composition of the Board of Directors and particularly the executive component thereof, for which the Chairman should hold key responsibility".

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

Principle 7 (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. In view of the changes in the composition of the Board (including a change in Chairmanship) it was felt that the evaluation would be beneficial if it is carried out at a later date. This would allow the Board Members a more meaningful period of time upon which to base their judgement and opinions on the functioning of the newly composed Board.

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.

Within this context, the Board believes that the setting up of a Nomination Committee with the functions and responsibilities as envisaged by the Code (namely, in relation to the procedure of nomination of Directors to the Board) is currently not suited to the Bank. In view of the provisions of the Bank's Articles of Association explained above, a Nomination Committee in terms of the Code 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 retain under review the issue relating to the setting up of a Nomination Committee in terms of the Code.

Principle 9 (Code Provision 9.3):

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

Corporate governance statement of compliance (continued)

D. INTERNAL CONTROL

Authority to manage the activities of the Bank is delegated to the Chief Executive Officer within the limits set by the Board.

The Board is ultimately responsible for the Bank's systems of internal control and for reviewing their effectiveness. Such systems are designed to manage rather than eliminate the risk of failure to achieve business objectives, and can only provide reasonable as opposed to absolute assurance against material misstatement or loss. Through the Audit Committee and the Risk Management 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 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.

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.

BOV
Bank of Valletta

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 2013

Remuneration report as at 30 September 2013

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), George Portanier and Taddeo Scerri, members, all of whom are independent non-executive directors. The Chief Executive Officer (CEO) attends meetings of the Committee when appropriate. The Company Secretary acts as secretary to the Committee.

The Terms of Reference of the Remuneration Committee were reviewed during FY 2012 in order to better reflect the provisions of the MFSA Code of Corporate Governance, to achieve stricter compliance with Banking Rule 12/2012 and to align them with the Bank's Remuneration Policy. The Terms of Reference were updated further during FY 2013 to reflect the change in name from Remuneration Committee to Remuneration and Nominations Committee.

2. Meetings

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

Members *(composition as from April 2013)*	**Attended**
John Cassar White (Chairman)	3/3
George Portanier	3/3
Taddeo Scerri	3/3
Members *(composition up to March 2013)*	
Frederick Mifsud Bonnici	2/2
Joseph Borg	2/2
Paul Testaferrata Moroni Viani	2/2

The Committee determined and/or discussed the following matters:

- Remuneration Report for FY 2012
- Chairman and Directors' Remuneration
- Remuneration of Senior Executives
- CEO Performance Bonus
- Setting up of Strategy and Process Management Unit
- Appointment of new Chief Officer Strategy and Process Management
- Appointment of new Chief Officer Human Resources
- Appointment of Executive Head Investment Operations Unit
- Company Car and Car Allowance Policy

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 Chief Executive Officer 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.

The Committee considers that the current Executive Management remuneration packages are based upon the appropriate local market equivalents, and are fair and reasonable for the responsibilities involved. The Committee also believes that the remuneration packages are such as to enable the Bank to attract, retain and motivate executives having the appropriate skills and qualities 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. The Remuneration Policy is kept under review; however no significant changes are intended to be effected thereto in FY 2014.

Remuneration report as at 30 September 2013 (continued)

A Group's Remuneration Policy was approved by the Remuneration 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. Work has been completed in relation to various aspects of the Policy and particularly to ensure that individual performance is evaluated according to both quantitative/financial and qualitative/behavioural measures. It is planned that the Policy will be fully implemented by the end of FY 2014. Further detail about the Bank's Remuneration Policy is found in the Capital & Risk Management Report.

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

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 Remuneration 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 are 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 2013 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 in 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 and Frederick Mifsud Bonnici opted to waive fees due to them as chairmen of the Remuneration Committee*

Whilst one of the Directors is an employee of the Bank and therefore receives remuneration by virtue of his employment, none of the Bank's Directors otherwise 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.

Remuneration report as at 30 September 2013 (continued)

Total emoluments received by Directors during FY 2013 are reported below under section 3.3 in terms of Code Provisions 8.A.5.

3.3 Code Provision 8.A.5

Emoluments of Senior Executives

Fixed Remuneration	Variable Remuneration	Share Options	Others
€1,012,289	€55,763	None	Non-cash benefits referred to above under 3.1

Emoluments of Directors

Fixed Remuneration	Variable Remuneration	Share Options	Others
€267,843*	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 2013

	€
John Cassar White (*appointed Chairman on 5 April 2013*)	38,017
Frederick Mifsud Bonnici (*resigned on 8 April 2013*)	40,469
Joseph Borg	26,293
Roberto Cassata	17,500
Gordon Cordina (*resigned on 5 April 2013*)	12,237
Ann Fenech (*appointed on 19 December 2012)*	14,711
George Portanier	23,970
Manuel Rizzo (*resigned on 19 December 2012*)	4,058
Norman Rossignaud (*resigned on 19 December 2012*)	4,874
Taddeo Scerri (*appointed on 5 April 2013*)	13,455
Paul Testaferrata Moroni Viani	27,690
George Wells	26,827
Franco Xuereb (*appointed on 19 December 2012)*	17,742
Total	267,843

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 41 to 99, which comprise the statements of financial position as at 30 September 2013, and 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 International Financial Reporting Standards (IFRS) 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 2013 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 2013

Statements of profit or loss for the year ended 30 September 2013

	Note	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Interest receivable and similar income					
- on loans and advances, balances with Central Bank of Malta and treasury bills	2	161,709	166,497	161,709	166,497
- on debt and other fixed income instruments	2	60,728	72,048	60,728	72,048
Interest payable	3	(91,423)	(90,713)	(91,423)	(90,713)
Net interest income		**131,014**	**147,832**	**131,014**	**147,832**
Fee and commission income		59,435	51,055	52,519	44,857
Fee and commission expense		(7,322)	(6,619)	(7,322)	(6,619)
Net fee and commission income	4	**52,113**	**44,436**	**45,197**	**38,238**
Dividend income		873	672	7,914	2,126
Trading profits	5	31,149	24,721	31,107	24,649
Net gain on investment securities and hedging instruments	6	2,978	1,203	2,978	1,203
Operating income		**218,127**	**218,864**	**218,210**	**214,048**
Employee compensation and benefits	7	(54,373)	(54,914)	(52,798)	(53,405)
General administrative expenses	7	(28,219)	(26,608)	(27,023)	(25,261)
Net compensation in relation to the Property Fund and other securities	7	(506)	(4,555)	(506)	(515)
Amortisation of intangible assets	20	(1,642)	(1,623)	(1,642)	(1,623)
Depreciation	21	(4,398)	(3,965)	(4,296)	(3,866)
Net impairment losses	8	(25,595)	(22,817)	(25,595)	(22,793)
Operating profit		**103,394**	**104,382**	**106,350**	**106,585**
Share of results of associates, net of tax	18	12,384	6,348	-	-
Profit before tax	9	**115,778**	**110,730**	**106,350**	**106,585**
Income tax expense	10	(36,305)	(36,454)	(35,861)	(37,123)
Profit for the year		**79,473**	**74,276**	**70,489**	**69,462**
Attributable to:					
Equity holders of the Bank		79,055	74,995	70,489	69,462
Non-controlling interest		418	(719)	-	-
		79,473	74,276	70,489	69,462
Earnings per share	11	26c4	25c0	23c5	23c2

Statements of profit or loss and other comprehensive income
for the year ended 30 September 2013

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
Profit for the year	79,473	74,276	70,489	69,462
Other comprehensive income				
Items that may be reclassified subsequently to profit or loss:				
Available-for-sale investments				
- change in fair value	9,210	(6,116)	9,210	(6,116)
- deferred tax thereon	(3,223)	2,140	(3,223)	2,140
- change in fair value transferred to profit or loss	(1,290)	(749)	(1,290)	(749)
- deferred tax thereon	452	262	452	262
Items that will not be reclassified to profit or loss:				
Property				
- revaluation	6,703	-	6,703	-
- deferred tax thereon	(804)	-	(804)	-
Other comprehensive profit/(loss) for the period, net of tax	11,048	(4,463)	11,048	(4,463)
Total comprehensive income	90,521	69,813	81,537	64,999

Attributable to:

	2013	2012
Equity holders of the Bank	90,103	70,532
Non-controlling interest	418	(719)
	90,521	69,813

Statements of financial position as at 30 September 2013

	Note	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
ASSETS					
Balances with Central Bank of Malta, treasury bills and cash	13	194,587	296,134	194,587	296,134
Financial assets at fair value through profit or loss	14	581,531	768,284	578,691	763,723
Investments	15	1,665,820	1,338,456	1,665,820	1,338,456
Loans and advances to banks	16	860,957	676,639	860,957	676,639
Loans and advances to customers at amortised cost	17	3,667,739	3,702,217	3,667,739	3,702,217
Investments in associates	18	84,880	77,058	52,870	52,870
Investments in subsidiary companies	19	-	-	1,393	1,393
Intangible assets	20	11,495	8,743	11,495	8,743
Property, plant and equipment	21	80,123	70,035	79,872	69,720
Deferred tax	22	70,205	63,607	70,205	63,607
Other assets		15,406	20,362	14,475	21,217
Prepayments and accrued income	23	25,215	27,690	25,215	27,690
Total Assets		**7,257,958**	**7,049,225**	**7,223,319**	**7,022,409**
LIABILITIES					
Financial liabilities at fair value through profit or loss	14	30,819	60,879	30,819	60,879
Amounts owed to banks	24	36,040	250,352	36,040	250,352
Amounts owed to customers	25	6,219,666	5,809,300	6,220,954	5,810,604
Debt securities in issue	26	95,400	95,400	95,400	95,400
Current tax		4,697	13,405	5,065	12,952
Deferred tax	22	5,003	4,199	5,003	4,199
Other liabilities	27	108,864	106,235	108,765	105,995
Accruals and deferred income	28	29,235	30,590	28,962	30,102
Financial liabilities designated for hedge accounting	29	31,229	37,865	31,229	37,865
Subordinated liabilities	30	120,000	120,000	120,000	120,000
Total Liabilities		**6,680,953**	**6,528,225**	**6,682,237**	**6,528,348**
EQUITY					
Attributable to equity holders of the Bank:					
Called up share capital	31	300,000	270,000	300,000	270,000
Share premium account		988	988	988	988
Revaluation reserves	32	24,621	13,573	24,509	13,461
Retained earnings		250,735	236,196	215,585	209,612
		576,344	520,757	541,082	494,061
Non-controlling interest		661	243	-	-
Total Equity		**577,005**	**521,000**	**541,082**	**494,061**
Total Liabilities and Equity		**7,257,958**	**7,049,225**	**7,223,319**	**7,022,409**
MEMORANDUM ITEMS					
Contingent liabilities	33	213,598	215,512	213,598	215,512
Commitments	34	1,184,279	1,049,804	1,184,279	1,049,804

These financial statements were approved by the Board of Directors and authorised for issue on 31 October 2013 and signed on its behalf by:

J. Cassar White
Chairman

J. Borg
Director

C. Borg
Chief Executive Officer

Statements of changes in equity for the year ended 30 September 2013

	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 2011	**240,000**	**988**	**18,036**	**214,211**	**473,235**	**962**	**474,197**
Profit for the year	-	-	-	74,995	**74,995**	(719)	**74,276**
Other comprehensive income							
Available-for-sale investments							
- change in fair value, net of tax	-	-	(3,976)	-	**(3,976)**	-	**(3,976)**
- change in fair value transferred to profit or loss, net of tax	-	-	(487)	-	**(487)**	-	**(487)**
Total other comprehensive income	-	-	(4,463)	-	**(4,463)**	-	**(4,463)**
Total comprehensive income for the year	-	-	(4,463)	74,995	**70,532**	(719)	**69,813**
Transactions with owners, recorded directly in equity:							
Bonus issue	30,000	-	-	(30,000)	**-**	-	**-**
Dividends - final 2011	-	-	-	(12,480)	**(12,480)**	-	**(12,480)**
- interim 2012 (note 12)	-	-	-	(10,530)	**(10,530)**	-	**(10,530)**
	30,000	-	-	(53,010)	**(23,010)**	-	**(23,010)**
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 income	-	-	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**

Statements of changes in equity for the year ended 30 September 2013 (continued)

	Share Capital €000	Share Premium Account €000	Revaluation Reserves €000	Retained Earnings €000	Total €000
The Bank					
At 30 September 2011	**240,000**	**988**	**17,924**	**193,160**	**452,072**
Profit for the year	-	-	-	69,462	**69,462**
Other comprehensive income					
Available-for-sale investments					
- change in fair value, net of tax	-	-	(3,976)	-	**(3,976)**
- change in fair value transferred to profit or loss, net of tax	-	-	(487)	-	**(487)**
Total other comprehensive loss	-	-	(4,463)	-	**(4,463)**
Total comprehensive (loss)/income for the year	-	-	(4,463)	69,462	**64,999**
Transactions with owners, recorded directly in equity:					
Bonus issue	30,000	-	-	(30,000)	**-**
Dividends - final 2011	-	-	-	(12,480)	**(12,480)**
- interim 2012 (note 12)	-	-	-	(10,530)	**(10,530)**
	30,000	-	-	(53,010)	**(23,010)**
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 income	-	-	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**

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

Statements of cash flow for the year ended 30 September 2013

	Note	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Cash flows from operating activities					
Interest and commission receipts		264,199	259,031	257,299	252,774
Interest, commission and compensation payments		(102,977)	(100,570)	(102,762)	(96,458)
Payments to employees and suppliers		(76,517)	(82,172)	(73,746)	(79,316)
Operating profit before changes in operating assets and liabilities		84,705	76,289	80,791	77,000
Decrease/(increase) in operating assets:					
Loans and advances		31,064	(115,283)	31,064	(115,283)
Reserve deposit with Central Bank of Malta		(3,505)	47,285	(3,505)	47,285
Fair value through profit or loss financial assets		166,084	166,676	166,084	166,676
Fair value through profit or loss equity instruments		(5,323)	(6,856)	(7,044)	(4,523)
Treasury bills with original maturity of more than 3 months		(9,985)	(27,991)	(9,985)	(27,991)
Other assets		4,035	(1,098)	5,821	(3,736)
Increase in operating liabilities:					
Amounts owed to banks and to customers		306,997	260,675	306,981	260,660
Other liabilities		(10,122)	25,622	(10,041)	25,534
Net cash from operating activities before tax		563,950	425,319	560,166	425,622
Tax paid		(54,430)	(28,318)	(53,165)	(29,105)
Net cash from operating activities		509,520	397,001	507,001	396,517
Cash flows from investing activities					
Dividends received		5,433	1,723	7,914	2,126
Interest received from held-to-maturity debt and other fixed income instruments		37,484	50,165	37,484	50,165
Purchase of debt instruments		(678,365)	(364,420)	(678,365)	(364,420)
Proceeds from sale or maturity of debt instruments		299,081	357,845	299,081	357,845
Purchase of property, plant and equipment		(10,414)	(7,273)	(10,376)	(7,192)
Proceeds from disposal of property, plant and equipment		-	8	-	8
Net cash (used in)/from investing activities		(346,781)	38,048	(344,262)	38,532
Cash flows from financing activities					
Proceeds from issue of debt securities		-	40,000	-	40,000
Dividends paid to Bank's equity holders		(34,516)	(23,010)	(34,516)	(23,010)
Net cash (used in)/from financing activities		(34,516)	16,990	(34,516)	16,990
Net change in cash and cash equivalents before effect of exchange rate changes		128,223	452,039	128,223	452,039
Effect of exchange rate changes on cash and cash equivalents		-	(46)	-	(46)
Net change in cash and cash equivalents after effect of exchange rate changes		128,223	452,085	128,223	452,085
Net change in cash and cash equivalents		128,223	452,039	128,223	452,039
Cash and cash equivalents at 1 October		808,880	356,841	808,880	356,841
Cash and cash equivalents at 30 September	36	**937,103**	**808,880**	**937,103**	**808,880**

Notes to the financial statements 30 September 2013

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 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 International Financial Reporting Standards 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 International Financial Reporting Standards 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 International Financial Reporting Standards as adopted by the EU:

The amendments to IAS 1 entitled Presentation of Items of Other Comprehensive Income are effective for annual periods beginning on or after 1 July 2012, with earlier application being permitted. In line with these amendments, the Bank and the Group have elected to introduce new terminologies for the Statements of Profit or Loss and the Statements of Profit or Loss and Other Comprehensive Income. The items included in the other comprehensive income section are being grouped into those that will not be reclassified subsequently to profit or loss and those that will be reclassified subsequently to profit or loss when specific conditions are met, as applicable.

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. These include the following:

By virtue of the December 2011 amendment, IFRS 9 Financial Instruments is applicable for annual periods beginning on or after 1 January 2015, with earlier application being permitted. This Standard represents the completion of the classification and measurement part of the IASB's project to replace IAS 39 Financial Instruments: Recognition and Measurement. This Standard addresses the classification and measurement of certain financial assets and financial liabilities. IFRS 9 requires financial assets that fall within its scope to be classified on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. The Standard requires financial assets to be subsequently measured at amortised cost or at fair value. The new requirements in relation to financial liabilities address the problem of volatility in profit or loss arising from an issuer that measures its own debt at fair value. With the new requirements, any entity choosing to measure a liability at fair value will generally present the portion of the change in its fair value due to changes in the entity's own credit risk in other comprehensive income rather than within profit or loss. The Group and the Bank are assessing the impact of this Standard on the consolidated and the separate financial statements. This Standard had not yet been adopted 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 11 Joint Arrangements classifies joint arrangements on the basis of their substance by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case in terms of IAS 31 Interests in Joint Ventures). Under IFRS 11, joint arrangements are classified as joint ventures or as joint operations. Joint ventures are accounted for using the equity method since the use of proportionate consolidation for such arrangements has been eliminated. Joint operations are accounted for in a manner that is similar to the current accounting treatment applicable for jointly controlled assets and jointly controlled operations. IFRS 11 supersedes IAS 31 Interests in Joint Ventures and SIC-13 Jointly Controlled Entities—Non-monetary Contributions by Venturers.

Notes to the financial statements 30 September 2013 (continued)

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 12 May 2011, the IASB issued IFRS 13 Fair Value Measurement. The standard defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 does not require fair value measurements in addition to those already required or permitted by other IFRSs. The Standard is applicable for annual periods beginning on or after 1 January 2013, with earlier application being permitted.

On 16 June 2011, the IASB issued an amended version of IAS 19 Employee Benefits. This represents the completion of the IASB's project to improve the accounting for pensions and other post-employment benefits. The amended version of IAS 19 comes into effect for financial years beginning on or after 1 January 2013. Earlier application is permitted. The amendment has been endorsed by the EU at the date of authorisation of these financial statements. Where applicable, the Group and the Bank will need to revise their accounting policy for post-employment benefits in line with the revised IAS19, which requires (i) the recognition of changes in defined benefit obligations (and in the fair value of plan assets) when they occur, (ii) the recognition of actuarial gains and losses in other comprehensive income (rather than through profit or loss) and (iii) the acceleration of the recognition of past service costs.

On 16 December 2011, the IASB also issued amendments to IAS 32 and IFRS 7 entitled Offsetting Financial Assets and Financial Liabilities. 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 disclosure requirements also improve transparency in the reporting of how companies mitigate credit risk, including disclosure of related collateral pledged or received. The amendments to IAS 32 and IFRS 7 are applicable on 1 January 2014 and 1 January 2013 respectively.

On 20 May 2013, IFRIC 21 Levies was issued. IFRIC 21 is applicable for annual periods beginning on or after 1 January 2014. This Interpretation has not as yet been endorsed by the European Union at the date of authorisation of these financial statements. 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. The amendment has not as yet been endorsed by the European Union at the date of authorisation of these financial statements. 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.

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. The amendment has not as yet been endorsed by the European Unionat the date of authorisation of these financial statements. 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. These amendments have not as yet been endorsed by the European Union.

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. 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

Notes to the financial statements 30 September 2013 (continued)

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.

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 market price in an active market 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.

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

Notes to the financial statements 30 September 2013 (continued)

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 is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event(s) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

(i) Financial assets carried at amortised cost

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 and whose fair value cannot be reliably measured is recognised in profit or loss and is not reversed in a subsequent period.

Notes to the financial statements 30 September 2013 (continued)

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 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.

Notes to the financial statements 30 September 2013 (continued)

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

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

1.8 Sale and repurchase agreements

Securities sold subject to a linked repurchase agreement ('repos') are retained in the financial statements at fair value through profit or loss or as investment securities as appropriate, and the counterparty liability is included in amounts owed to banks. Securities purchased under agreements to resell ('reverse repos') are not recognised but the amounts paid are recorded as loans and advances to banks. The difference between sale and repurchase price or purchase and subsequent sale price is recognised over the life of the repo/reverse repo agreements using the effective interest method and is treated as interest.

1.9 Investments in subsidiaries and 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 to sell 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

Notes to the financial statements 30 September 2013 (continued)

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.

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 to sell 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 recognisedin 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.

Notes to the financial statements 30 September 2013 (continued)

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

1.15 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 determined. 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 Group contributes towards the state pension in accordance with local legislation. The costs of retirement benefits are charged to profit or loss as they accrue. Any other employee benefits are recognised as a liability by matching the expected cost of such benefit with the economic benefit that is being derived by the Group. The liability at the end of the reporting period represents the obligation of the Group discounted to the net present value after considering the average life expectancy of such employees, where applicable.

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 thestatement of cash flows.

Notes to the financial statements 30 September 2013 (continued)

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 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.

1.22.1 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.

1.22.2 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. 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.

1.22.3 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.

1.22.4 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 judgment regarding the Group's intention and ability to hold such instruments to maturity.

1.22.5 Post-employment benefits

In estimating the fair 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.

1.22.6 Provision in relation to claims from investors on the La Valette Multi Manager Property Fund and other securities

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

Notes to the financial statements 30 September 2013 (continued)

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
2. INTEREST RECEIVABLE AND SIMILAR INCOME				
On loans and advances to banks	919	1,085	919	1,085
On loans and advances to customers	159,726	164,068	159,726	164,068
On balances with Central Bank of Malta	554	1,344	554	1,344
On treasury bills	510	-	510	-
	161,709	166,497	161,709	166,497
On debt and other fixed income instruments				
- available-for-sale	14,279	20,329	14,279	20,329
- held-to-maturity	33,502	30,984	33,502	30,984
- fair value through profit or loss	18,512	24,740	18,512	24,740
	66,293	76,053	66,293	76,053
Amortisation of discounts and premiums				
- available-for-sale	(725)	(1,362)	(725)	(1,362)
- held-to-maturity	(4,840)	(2,643)	(4,840)	(2,643)
	(5,565)	(4,005)	(5,565)	(4,005)
	60,728	72,048	60,728	72,048
	222,437	238,545	222,437	238,545

3. INTEREST PAYABLE

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
On amounts owed to banks	18,702	18,582	18,702	18,582
On amounts owed to customers	62,327	63,437	62,327	63,437
On debt securities in issue	4,359	2,659	4,359	2,659
On subordinated liabilities	6,035	6,035	6,035	6,035
	91,423	90,713	91,423	90,713

4. NET FEE AND COMMISSION INCOME

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
On loans and advances, similar activities and local business	25,074	22,379	25,074	22,379
On trust, life assurance, fund management and similar activities	16,023	14,181	9,107	7,983
On other activities	11,016	7,876	11,016	7,876
	52,113	44,436	45,197	38,238

5. TRADING PROFITS

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Profit on foreign exchange activities	16,732	17,193	16,749	17,189
Fair value movements and net gains on sale of financial instruments at fair value through profit or loss	14,417	7,528	14,358	7,460
	31,149	24,721	31,107	24,649

Notes to the financial statements 30 September 2013 (continued)

	The Group		The Bank	
	2013	**2012**	**2013**	**2012**
	€000	**€000**	**€000**	**€000**
6. NET GAIN ON INVESTMENT SECURITIES AND HEDGING INSTRUMENTS				
Available-for-sale assets				
- net gain on early redemption	1,290	749	1,290	749
- net revaluation (loss)/gain attributable to hedged risk	(9,612)	3,948	(9,612)	3,948
	(8,322)	4,697	(8,322)	4,697
Derivative financial instruments				
- net gain/(loss) on derivative financial instruments held for hedging	11,300	(3,494)	11,300	(3,494)
	2,978	**1,203**	**2,978**	**1,203**

7. ADMINISTRATIVE AND OTHER OPERATING EXPENSES

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Employee compensation and benefits				
- wages and salaries	44,016	43,078	42,540	41,668
- social security costs	2,874	2,715	2,775	2,616
- retirement benefits	3,462	4,956	3,462	4,956
- other staff costs	4,021	4,165	4,021	4,165
	54,373	54,914	52,798	53,405
General administrative expenses	28,219	26,608	27,023	25,261
Net compensation in relation to the Property Fund and other securities*	506	4,555	506	515
	83,098	86,077	80,327	79,181

*The charge in relation to the property fund and other securities of €4.6 million in FY 2012 represents the estimated additional ex gratia compensation to investors who may have been ineligible to invest in the La Valette Multi Manager Property Fund, in line with the Company Announcement issued by the Bank on 28 June 2012, the estimated ex gratia compensation in relation to claims made on other securities, less any recoveries from third parties.
The charge of €0.5 million in FY 2013 represents compensation in relation to claims on securities other than La Valette Multi Manager Property Fund.

	The Group		The Bank	
	2013	**2012**	**2013**	**2012**
	No. of persons	**No. of persons**	**No. of persons**	**No. of persons**
The average number of employees are analysed as follows:				
Managerial	520	507	503	490
Supervisory and clerical	962	960	926	926
Others	54	55	51	52
	1,536	1,522	1,480	1,468

Notes to the financial statements 30 September 2013 (continued)

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
8. NET IMPAIRMENT LOSSES				
Write downs:				
Investments and other assets	2,691	2,797	2,691	2,773
Loans and advances to customers				
- specific allowances	31,767	15,497	31,767	15,497
- collective allowances	6,534	16,316	6,534	16,316
- bad debts written off	1,808	985	1,808	985
	40,109	32,798	40,109	32,798
Reversals of write-downs:				
Investments and other assets	(32)	-	(32)	-
Loans and advances to customers				
- specific allowances	(10,374)	(7,024)	(10,374)	(7,024)
- collective allowances	(5,229)	(2,840)	(5,229)	(2,840)
- bad debts recovered	(1,570)	(2,914)	(1,570)	(2,914)
	(17,173)	(12,778)	(17,173)	(12,778)
Net impairment losses	25,595	22,817	25,595	22,793

9. PROFIT BEFORE TAX

Profit before tax is stated after charging:

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Total remuneration payable to the external auditors of the parent company				
- the audit of financial statements	205	190	180	166
- other assurance services	24	24	24	24
- other services	139	92	139	83
	368	306	343	273
Directors' emoluments				
- fees	268	186	268	186
- directors' salaries as full-time bank employees	53	38	53	38
	321	224	321	224
Compensation to other key management personnel is analysed as follows				
- short term employee benefits	1,068	926	972	833
- post employment benefits	-	52	-	52
	1,068	978	972	885
Total remuneration for directors and other key management personnel	1,389	1,202	1,293	1,109

Notes to the financial statements 30 September 2013 (continued)

10. INCOME TAX EXPENSE

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
Current	45,722	48,510	45,278	49,179
Deferred	(9,417)	(12,056)	(9,417)	(12,056)
	36,305	36,454	35,861	37,123

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		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
Profit before tax	115,778	110,730	106,350	106,585
Tax at the applicable rate of 35%	40,522	38,756	37,223	37,305
Tax effect of:				
Exempt and untaxed dividends	(148)	(128)	(1,632)	(234)
Share of results of associates	(4,334)	(2,222)	-	-
Withholding tax on property sales	(9)	-	(9)	-
Other differences	274	48	279	52
Income tax expense	36,305	36,454	35,861	37,123

11. EARNINGS PER SHARE

	The Group		The Bank	
	2013	2012	2013	2012
	cents per share	cents per share	cents per share	cents per share
Earnings per share	26c4	25c0	23c5	23c2

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 2013 (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			
	2013 cents per share	2012 cents per share	2013 €000	2012 €000
Gross of income tax				
- prior year's final paid	11.7	6.4	35,100	19,200
- interim paid	6.0	5.4	18,000	16,200
	17.7	11.8	53,100	35,400
Net of income tax				
- prior year's final paid	7.6	4.2	22,816	12,480
- interim paid	3.9	3.5	11,700	10,530
	11.5	7.7	34,516	23,010

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 2013 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% (2012: 35%).

In respect of the current year, the directors propose that a final gross ordinary dividend of €0.13 per share amounting to €39.0 million (net ordinary dividend of €0.0845 per share - €25.4 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 19 November 2013.

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

	The Group		The Bank	
	2013 €000	2012 €000	2013 €000	2012 €000
Balances with Central Bank of Malta	60,232	181,049	60,232	181,049
Malta Government Treasury Bills	100,966	78,840	100,966	78,840
Cash	33,389	36,245	33,389	36,245
	194,587	296,134	194,587	296,134

Balances with the Central Bank of Malta include Reserve Deposit amounting to €55.3 million (2012: €51.8 million) in respect of both the Group and the Bank, in terms of Article 37 of the Central Bank of Malta Act (Cap. 204).

14. FINANCIAL INSTRUMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS

	The Group		The Bank	
	2013 €000	2012 €000	2013 €000	2012 €000
Financial assets at fair value through profit or loss				
Financial assets classified as held for trading:				
Derivative financial instruments	11,411	16,909	11,411	16,909
Financial assets designated at fair value through profit or loss:				
Debt and other fixed income instruments	441,826	605,701	441,826	605,701
Equity and other non-fixed income instruments	66,362	61,754	63,522	57,193
Loans and advances to customers (note 17)	61,932	83,920	61,932	83,920
	570,120	751,375	567,280	746,814
	581,531	768,284	578,691	763,723

Financial assets at fair value through profit or loss with a nominal value of €70 million (2012: €12 million) have been pledged against the provision of credit lines by the Central Bank of Malta.

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Notes to the financial statements 30 September 2013 (continued)

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

	The Group		The Bank	
	2013	2012	2013	2012
Financial liabilities at fair value through profit or loss	€000	€000	€000	€000
Financial liabilities classified as held for trading:				
Derivative financial instruments	30,819	60,879	30,819	60,879

14.1 Debt and other fixed income instruments

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Issued by public bodies				
- local general government	179,527	209,957	179,527	209,957
- foreign general government	18,345	26,357	18,345	26,357
	197,872	236,314	197,872	236,314
Issued by other issuers				
- local banks	3,661	3,658	3,661	3,658
- foreign banks	165,772	244,131	165,772	244,131
- foreign other	64,163	111,338	64,163	111,338
- local other	10,358	10,260	10,358	10,260
	243,954	369,387	243,954	369,387
	441,826	605,701	441,826	605,701
Listing status				
- listed on Malta Stock Exchange	193,546	223,876	193,546	223,876
- listed elsewhere	217,815	322,367	217,815	322,367
- foreign unlisted	30,465	59,458	30,465	59,458
	441,826	605,701	441,826	605,701
Summary of movements during the year:				
At the beginning of the year	605,701	743,975	605,701	743,975
Acquisitions	22,418	32,800	22,418	32,800
Disposals	(183,004)	(200,034)	(183,004)	(200,034)
Movement in fair value	5,057	16,157	5,057	16,157
Exchange adjustment	(8,346)	12,803	(8,346)	12,803
At the end of the year	441,826	605,701	441,826	605,701

14.2 Equity and other non-fixed income instruments

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Issued by other issuers				
- local banks	761	680	761	680
- foreign banks	1,063	836	1,063	836
- foreign other	9,774	7,081	9,774	7,081
- local other	54,764	53,157	51,924	48,596
	66,362	61,754	63,522	57,193
Listing status				
- listed on Malta Stock Exchange	55,498	53,837	52,658	49,276
- listed elsewhere	703	-	703	-
- foreign unlisted	10,161	7,917	10,161	7,917
	66,362	61,754	63,522	57,193
Summary of movements during the year:				
At the beginning of the year	61,754	54,122	57,193	51,894
Acquisitions	8,530	12,464	8,530	10,131
Disposals	(3,207)	(5,608)	(1,486)	(5,608)
Movement in fair value	(654)	769	(654)	769
Exchange adjustment	(61)	7	(61)	7
At the end of the year	66,362	61,754	63,522	57,193

Notes to the financial statements 30 September 2013 (continued)

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

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
14.3 Derivative financial instruments				
Fair value of assets	11,411	16,909	11,411	16,909
Fair value of liabilities	30,819	60,879	30,819	60,879
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	264,408	331,239	264,408	331,239
- between 3 months and 1 year	334,548	98,222	334,548	98,222
- more than 1 year	277,538	414,700	277,538	414,700
	876,494	844,161	876,494	844,161

15. INVESTMENTS

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Debt and other fixed income instruments				
- available-for-sale	312,663	318,845	312,663	318,845
- held-to-maturity	1,352,413	1,016,176	1,352,413	1,016,176
Equity and other non-fixed income instruments				
- available-for-sale	744	3,435	744	3,435
	1,665,820	1,338,456	1,665,820	1,338,456

Investments with a nominal value of €135 million (2012: €208 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

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Issued by public bodies				
- local general government	234,364	244,320	234,364	244,320
- local public sector	60,657	70,664	60,657	70,664
Issued by other issuers				
- foreign banks	3,793	3,861	3,793	3,861
- foreign others	13,849	-	13,849	-
	312,663	318,845	312,663	318,845
Listing status				
- listed on Malta Stock Exchange	295,021	314,984	295,021	314,984
- listed elsewhere	13,849	-	13,849	-
- foreign unlisted	3,793	3,861	3,793	3,861
	312,663	318,845	312,663	318,845
Summary of movements during the year:				
At the beginning of the year	318,845	456,805	318,845	456,805
Acquisitions	68,782	-	68,782	-
Disposals	(71,295)	(46,349)	(71,295)	(46,349)
Redeemed	(145)	(90,531)	(145)	(90,531)
Amortisation	(725)	(1,699)	(725)	(1,699)
Movement in fair value	(1,699)	(2,153)	(1,699)	(2,153)
Profit on early redemption	1,290	-	1,290	-
Exchange adjustment	(2,390)	2,772	(2,390)	2,772
At the end of the year	312,663	318,845	312,663	318,845

Notes to the financial statements 30 September 2013 (continued)

15. INVESTMENTS (continued)

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
15.2 Debt and other fixed income instruments held-to-maturity				
Issued by public bodies				
- local general government	462,838	279,148	462,838	279,148
- foreign general government	137,263	122,474	137,263	122,474
- foreign public sector securities	3,703	3,869	3,703	3,869
	603,804	405,491	603,804	405,491
Issued by other issuers				
- foreign banks	659,694	560,095	659,694	560,095
- foreign other	88,915	50,590	88,915	50,590
	748,609	610,685	748,609	610,685
	1,352,413	1,016,176	1,352,413	1,016,176
Listing status				
- listed on Malta Stock Exchange	462,838	279,148	462,838	279,148
- listed elsewhere	666,142	551,647	666,142	551,647
- foreign unlisted	223,433	185,381	223,433	185,381
	1,352,413	1,016,176	1,352,413	1,016,176

At 30 September 2013, the fair value of held-to-maturity securities, without deducting transaction costs, amounted to €1,389.6 million (2012: €1,039.1 million).

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Summary of movements during the year:				
At the beginning of the year	1,016,176	844,837	1,016,176	844,837
Acquisitions	609,583	364,420	609,583	364,420
Redemptions	(225,796)	(220,965)	(225,796)	(220,965)
Amortisation	(4,840)	(2,643)	(4,840)	(2,643)
Profit on early redemptions	555	-	555	-
Impairment	-	(273)	-	(273)
Exchange adjustment	(43,265)	30,800	(43,265)	30,800
At the end of the year	1,352,413	1,016,176	1,352,413	1,016,176

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

	The Group 2013 €000	The Group 2012 €000	The Bank 2013 €000	The Bank 2012 €000
Issued by other issuers				
- local other	744	3,435	744	3,435
Listing status				
- listed on Malta Stock Exchange	-	2,589	-	2,589
- local unlisted	744	846	744	846
	744	3,435	744	3,435
Summary of movements during the year:				
At the beginning of the year	3,435	5,959	3,435	5,935
Impairment	(2,691)	(2,524)	(2,691)	(2,500)
At the end of the year	744	3,435	744	3,435

Notes to the financial statements 30 September 2013 (continued)

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
16. LOANS AND ADVANCES TO BANKS				
Repayable on call and at short notice	85,168	45,591	85,168	45,591
Term placements with Central Bank of Malta	585,658	284,962	585,658	284,962
Term placements with other banks	182,154	334,547	182,154	334,547
Cheques in course of collection	7,977	11,539	7,977	11,539
	860,957	676,639	860,957	676,639
17. LOANS AND ADVANCES TO CUSTOMERS				
Repayable on call and at short notice	589,255	612,955	589,255	612,955
Term loans and advances	3,189,282	3,177,362	3,189,282	3,177,362
	3,778,537	3,790,317	3,778,537	3,790,317
Less impairment losses	(110,798)	(88,100)	(110,798)	(88,100)
Net loans and advances at amortised cost	3,667,739	3,702,217	3,667,739	3,702,217
Loans and advances designated at fair value through profit or loss (note 14)	61,932	83,920	61,932	83,920
Total loans and advances	3,729,671	3,786,137	3,729,671	3,786,137
Impairment losses				
- specific allowances	60,844	39,451	60,844	39,451
- collective allowances	49,954	48,649	49,954	48,649
	110,798	88,100	110,798	88,100

The aggregate amount of advances on which interest has been suspended during the year is €173.2 million (2012: €171.3 million)

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
18. INVESTMENTS IN ASSOCIATES				
At the beginning of the year	77,058	71,761	52,870	52,870
Share of results after tax	12,384	6,348	-	-
Dividend received	(4,562)	(1,051)	-	-
At the end of the year	84,880	77,058	52,870	52,870
Amounts include:				
Local listed	21,317	18,718	22,304	22,304
Local unlisted	63,563	58,340	30,566	30,566
	84,880	77,058	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 (2012: €52.9 million). The fair value of the associated undertaking that is publicly quoted amounted to €24.3 million at 30 September 2013 (2012: €21.6 million).

Notes to the financial statements 30 September 2013 (continued)

18. INVESTMENTS IN ASSOCIATES (continued)

Name of company	Equity Interest 2013 %	Equity Interest 2012 %	Class	Incorporated in	Nature of Business
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

Name of company	Group's share of results 2013 €000	Group's share of results 2012 €000
Middlesea Insurance p.l.c.	3,140	1,711
MSV Life p.l.c.	9,244	4,637
	12,384	6,348

*A further 15.54% (2012: 15.54%) is held indirectly via an associated company. Although the Bank has an effective interest of 65.54% (2012: 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 2013 interim financial statements were used as a basis to determine the Group's share of results to 30 September 2013.

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 2013 in respect of the associates:	Associates 2013 €000	Associates 2012 €000
Total assets	1,371,045	1,271,654
Total liabilities	1,238,889	1,153,082
Revenues	104,423	85,412
Results for the period	4,456	4,631

	The Group 2013 €000	The Group 2012 €000
Share of net assets of associates	84,880	77,058
Share of results of associates	12,384	6,348

Notes to the financial statements 30 September 2013 (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% (2012: 2%) between the weighted average projected investment return and the risk adjusted discount factor applied of 7.5% (2012: 7.5%). The calculation also assumes lapse rates varying from 2% to 10% per annum (2012: 2% to 10% per annum) and an expense inflation rate of 3.5% (2012: 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. Realistic mortality rates were adjusted during 2012 to adopt the AMC00 standard tables. The effect of this change on the value in force was not material.

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

Name of company	Equity Interest 2013 %	Equity Interest 2012 %	Class	Incorporated in	Nature of Business
Valletta Fund Management Limited	60	60	Ordinary	Malta	Fund Management
Valletta Fund Services Limited	100	100	Ordinary	Malta	Fund Administration
BOV Investments Limited	100	100	Ordinary	Malta	Holding Company

Name of company	The Bank 2013 €000	The Bank 2012 €000
Valletta Fund Management Limited	481	481
Valletta Fund Services Limited	749	749
BOV Investments Limited	163	163
	1,393	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 Bank of Valletta

Notes to the financial statements 30 September 2013 (continued)

20. INTANGIBLE ASSETS

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
Software				
Cost				
1 October	15,164	13,345	15,164	13,345
Additions	4,394	3,768	4,394	3,768
Assets retired from active use	-	(1,949)	-	(1,949)
30 September	19,558	15,164	19,558	15,164
Accumulated amortisation				
1 October	6,421	6,747	6,421	6,747
Charge for the year	1,642	1,623	1,642	1,623
Accumulated amortisation on assets retired from active use	-	(1,949)	-	(1,949)
30 September	8,063	6,421	8,063	6,421
Carrying amount at 30 September	11,495	8,743	11,495	8,743

21. PROPERTY, PLANT AND EQUIPMENT

	Land and buildings €000	IT infrastructure and equipment €000	Other €000	Total €000
The Group				
Cost or valuation				
1 October 2011	66,767	14,157	26,305	107,229
Additions	498	2,160	847	3,505
Assets retired from active use	-	(3,839)	(3,569)	(7,408)
Disposals	-	-	(160)	(160)
30 September 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
Comprising:				
At cost	-	15,601	25,474	41,075
At valuation	76,508	-	-	76,508
30 September 2013	76,508	15,601	25,474	117,583
Accumulated depreciation				
1 October 2011	10,238	8,099	18,397	36,734
Provision for the year	694	1,910	1,361	3,965
Accumulated depreciation on assets retired from active use	-	(3,839)	(3,569)	(7,408)
Disposals	-	-	(160)	(160)
30 September 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
Carrying amount at:				
30 September 2012	56,333	6,308	7,394	70,035
30 September 2013	64,748	7,271	8,104	80,123

Notes to the financial statements 30 September 2013 (continued)

21. PROPERTY, PLANT AND EQUIPMENT (continued)

	Land and buildings €000	IT infrastructure and equipment €000	Other €000	Total €000
The Bank				
Cost or valuation				
1 October 2011	66,733	13,512	24,989	105,234
Additions	498	2,160	766	3,424
Disposals	-	-	(160)	(160)
Assets retired from active use	-	(3,839)	(3,569)	(7,408)
30 September 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
Comprising:				
At cost	-	14,956	24,039	38,995
At valuation	76,474	-	-	76,474
30 September 2013	76,474	14,956	24,039	115,469
Accumulated depreciation				
1 October 2012	10,150	7,276	17,646	35,072
Provision for the year	694	1,910	1,262	3,866
Disposals	-	-	(160)	(160)
Accumulated depreciation on assets retired from active use	-	(3,839)	(3,569)	(7,408)
30 September 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
Carrying amount at:				
30 September 2012	56,387	6,486	6,847	69,720
30 September 2013	64,802	7,449	7,621	79,872

	The Group		The Bank	
	2013	**2012**	**2013**	**2012**
	€000	**€000**	**€000**	**€000**
Carrying amount of land and buildings occupied for own use	64,748	56,333	64,802	56,387
Future capital expenditure				
- contracted but not provided for in the financial statements	3,085	3,234	3,085	3,234
- authorised by the directors but not contracted	6,521	7,814	6,521	7,814

Land and buildings were revalued by a professionally qualified architect on an open market value basis as at 30 September 2013. 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:
2013: Group and Bank €35.9 million (2012: Group and Bank €34.3 million)

Notes to the financial statements 30 September 2013 (continued)

	The Group		The Bank	
	2013	2012	2013	2012
	€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	(381)	2,417	(381)	2,417
Impairment losses	64,112	52,511	64,112	52,511
Allowance for employee benefits	8,096	8,435	8,096	8,435
Fixed assets and other temporary differences	(1,622)	244	(1,622)	244
	70,205	63,607	70,205	63,607
Deferred tax liability arising on:				
Property revaluation	5,003	4,199	5,003	4,199
23. PREPAYMENTS AND ACCRUED INCOME				
Accrued income	24,247	26,880	24,247	26,880
Prepayments	968	810	968	810
	25,215	27,690	25,215	27,690
24. AMOUNTS OWED TO BANKS				
Term deposits	14,121	228,264	14,121	228,264
Repayable on demand	21,919	22,088	21,919	22,088
	36,040	250,352	36,040	250,352
25. AMOUNTS OWED TO CUSTOMERS				
Term deposits	2,460,506	2,541,645	2,460,506	2,541,645
Repayable on demand	3,759,160	3,267,655	3,760,448	3,268,959
	6,219,666	5,809,300	6,220,954	5,810,604
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 2013 is €58.6 million (2012: €57.1 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 2013 is €40.7 million (2012: €40.2 million)

Notes to the financial statements 30 September 2013 (continued)

	The Group		The Bank	
	2013	**2012**	**2013**	**2012**
	€000	**€000**	**€000**	**€000**
27. OTHER LIABILITIES				
Post employment liabilities (see note 35)	23,132	24,100	23,132	24,100
Cash collateral for commitments	15,401	13,939	15,401	13,939
Deposits from companies in formation	4,238	7,572	4,238	7,572
Bills payable	24,015	18,816	24,015	18,816
Other	42,078	41,808	41,979	41,568
	108,864	106,235	108,765	105,995
28. ACCRUALS AND DEFERRED INCOME				
Accrued interest	29,235	30,590	28,962	30,102

29. FINANCIAL LIABILITIES DESIGNATED FOR HEDGE ACCOUNTING

	The Group		The Bank	
	2013	**2012**	**2013**	**2012**
	€000	**€000**	**€000**	**€000**
Derivative financial instruments designated as fair value hedges	31,229	37,865	31,229	37,865
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	141,556	141,714	141,556	141,714
30. SUBORDINATED LIABILITIES				
5.35% Euro subordinated unsecured bonds	50,000	50,000	50,000	50,000
4.80% Euro subordinated unsecured bonds	70,000	70,000	70,000	70,000
	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 2013 is €52.8 million (2012: €52.5 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 2013 is €72.1 million (2012: €71.7 million).

	The Bank	
	2013	**2012**
	€000	**€000**
31. SHARE CAPITAL		
Authorised:		
500,000,000 Ordinary shares of €1.00 each (2012: 350,000,000 Ordinary shares of €1.00 each)	500,000	350,000
Issued and paid up:		
300,000,000 Ordinary shares of €1.00 each fully paid (2012: 270,000,000 Ordinary shares of €1.00 each fully paid)	300,000	270,000

Notes to the financial statements 30 September 2013 (continued)

31. SHARE CAPITAL (continued)

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.

On 12 January 2012 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 8 shares held, thereby increasing the issued share capital from 240 million shares to 270 million shares, resulting in a paid up capital of €270 million. On the same date the authorised share capital was increased by €50 million to €350 million.

	The Group €000	The Bank €000
32. REVALUATION RESERVES		
On land and buildings:		
30 September 2011/2012	17,981	17,951
Property revaluation	6,703	6,703
Deferred tax	(804)	(804)
30 September 2013	23,880	23,850
On available-for-sale investments:		
1 October 2011	55	(27)
Fair value adjustments	(6,116)	(6,116)
Transfer to profit or loss on disposal	(749)	(749)
Deferred tax	2,402	2,402
30 September 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
Total	24,621	24,509

	The Group		The Bank	
	2013 €000	2012 €000	2013 €000	2012 €000
33. CONTINGENT LIABILITIES				
Acceptances and endorsements	2,645	3,273	2,645	3,273
Guarantees	191,485	193,517	191,485	193,517
Other contingent liabilities	19,468	18,722	19,468	18,722
	213,598	215,512	213,598	215,512

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

	The Group		The Bank	
	2013 €000	2012 €000	2013 €000	2012 €000
34. COMMITMENTS				
Documentary credits	71,196	89,289	71,196	89,289
Undrawn formal standby facilities, credit facilities and other commitments to lend	1,093,455	950,929	1,093,455	950,929
Capital expenditure contracted but not provided for in the financial statements	3,085	3,234	3,085	3,234
Commitments to financial institutions	16,543	6,352	16,543	6,352
	1,184,279	1,049,804	1,184,279	1,049,804

Notes to the financial statements 30 September 2013 (continued)

35. POST EMPLOYMENT PLANS

The Group operates an early retirement scheme whereby accepted applicants are given a lump sum payment of three times their terminal salary, or are paid two thirds of their terminal salary on a monthly basis until reaching retirement age. Furthermore, the Group makes payments to certain eligible employees in consideration of the liquidation of a defunct pension scheme.

The charge for the year, which amounts to €3.5 million (2012: €4.9 million), is included under staff costs.

The Group's obligation in respect of the above amounts to circa €23.1 million (2012: €24.1 million) and represents the Group's obligation discounted to the net present value, at the rate of 3.73% (2012: 3.95%) for the pension scheme and at the rate of 1.7% (2012: 4%) for the early retirement scheme, after considering the average life expectancy of such employees and expected increases in salaries, where applicable, and is included with other liabilities.

36. NOTES TO THE CASH FLOW STATEMENTS

	The Group		The Bank	
	2013	2012	2013	2012
	€000	€000	€000	€000
Cash	33,389	36,245	33,389	36,245
Balances with Central Bank of Malta (excluding Reserve Deposit)	4,937	129,259	4,937	129,259
Treasury bills (with original maturity of less than 3 months)	62,990	50,849	62,990	50,849
Money at call and short notice	845,628	659,249	845,628	659,249
Amounts owed to banks	(9,841)	(66,722)	(9,841)	(66,722)
Cash and cash equivalents included in the cash flow statement	937,103	808,880	937,103	808,880
Balances with contractual maturity of more than 3 months	27,105	(138,250)	27,105	(138,250)
	964,208	670,630	964,208	670,630
Equivalent items reported in the statement of financial position:				
Balances with Central Bank of Malta, Treasury bills and cash (excluding Reserve Deposit)	139,291	244,343	139,291	244,343
Loans and advances to banks	860,957	676,639	860,957	676,639
Amounts owed to banks	(36,040)	(250,352)	(36,040)	(250,352)
	964,208	670,630	964,208	670,630

Notes to the financial statements 30 September 2013 (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. There were no impairment allowances in respect of amounts due by related parties at the beginning and the end of the period presented and no expense has been recognised for impairment allowances in respect of such amounts in the current and the prior year. The amount of related party transactions and outstanding balances are disclosed below:

The Group	**2013 Related party transactions €000**	**% of total**	**2012 Related party transactions €000**	**% of total**
Interest receivable and similar income:				
- on loans and advances, balances with Central Bank of Malta and treasury bills				
Associates	300		490	
The Government	1,064		1,344	
Government related entities	14,052		19,791	
Key management personnel	45		91	
Other related parties	780		2,341	
	16,241	10%	24,057	14%
Interest receivable and similar income:				
- on debt and other fixed income instruments				
The Government	32,270	53%	32,321	45%
Interest payable				
Associates	2,280		2,700	
The Government	258		93	
Government related entities	355		627	
Key management personnel	8		10	
Other related parties	11		121	
	2,912	3%	3,551	4%
Fee and commission income				
Associates	2,817		2,597	
The Government	86		19	
Government related entities	2,113		2,389	
Key management personnel	6		6	
Other related parties	350		46	
	5,372	9%	5,057	10%
Employee compensation and benefits				
Key management personnel (note 9)	1,389	3%	1,202	2%
General administrative expenses				
Associates	72		75	
Key management personnel	25		3	
Other related parties	24		73	
	121	-	151	1%

Notes to the financial statements 30 September 2013 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

	2013 Related party balances €000	% of total	2012 Related party balances €000	% of total
Balances with Central Bank of Malta treasury bills and cash				
The Government	161,197	83%	259,890	88%
Investments				
The Government	697,194	42%	575,448	43%
Loans and advances to customers				
Associates	3,087		8,746	
The Government	9,749		41,220	
Government related entities	453,706		452,444	
Key management personnel	3,632		3,095	
Other related parties	18,603		49,460	
	488,777	13%	554,965	15%
Amounts owed to customers				
Associates	138,475		118,425	
The Government	87,112		38,712	
Government related entities	62,584		87,212	
Key management personnel	994		893	
Other related parties	27,986		28,311	
	317,151	5%	273,553	5%
Total Assets less Liabilities				
Associates	(135,388)		(109,679)	
The Government	781,028		837,846	
Government related entities	391,122		365,232	
Key management personnel	2,638		2,202	
Other related parties	(9,383)		21,149	
	1,030,017		1,116,750	
The Bank				
Interest receivable and similar income: - on loans and advances, balances with Central Bank of Malta and treasury bills				
Associates	300		490	
The Government	1,064		1,344	
Government related entities	14,052		19,791	
Key management personnel	45		90	
Other related parties	780		921	
	16,241	10%	22,636	14%
Interest receivable and similar income: - on debt and other fixed income instruments				
The Government	32,270	53%	32,321	45%
Interest payable				
Associates	2,280		2,700	
The Government	258		93	
Government related entities	355		627	
Key management personnel	8		10	
Other related parties	8		104	
	2,909	3%	3,534	4%
Fee and commission income				
Associates	2,817		2,597	
Subsidiaries	1,927		1,757	
The Government	86		19	
Government related entities	2,113		2,389	
Key management personnel	6		4	
Other related parties	341		33	
	7,290	14%	6,799	15%

Notes to the financial statements 30 September 2013 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

	2013 Related party transactions €000	% of total	2012 Related party transactions €000	% of total
Dividend income				
Associates	4,733		1,454	
Subsidiaries	2,308		-	
	7,041	89%	1,454	68%
Employee compensation and benefits				
Key management personnel (note 9)	1,293	2%	1,109	2%
General administrative expenses				
Associates	72		75	
Key management personnel	25		3	
Other related parties	24		14	
	121	-	92	-
Balances with Central Bank of Malta treasury bills and cash				
The Government	161,197	83%	259,890	88%
Investments				
The Government	697,194	42%	575,448	43%
Loans and advances to customers				
Associates	3,087		8,746	
The Government	9,749		41,220	
Government related entities	453,706		452,444	
Key management personnel	3,625		3,078	
Other related parties	18,603		21,152	
	488,770	13%	526,640	14%
Other assets				
Subsidiaries	1,140	8%	4,263	20%
Amounts owed to customers				
Associates	138,475		118,425	
Subsidiaries	1,288		1,304	
The Government	87,112		38,712	
Government related entities	62,584		87,212	
Key management personnel	935		775	
Other related parties	23,970		23,402	
	314,364	5%	269,830	5%
Total Assets less Liabilities				
Associates	(135,388)		(109,679)	
Subsidiaries	(148)		2,959	
The Government	781,028		837,846	
Government related entities	391,122		365,232	
Key management personnel	2,690		2,303	
Other related parties	(5,367)		(2,250)	
	1,033,937		1,096,411	

Notes to the financial statements 30 September 2013 (continued)

37. RELATED PARTY TRANSACTIONS (continued)

	The Group and the Bank	
	2013	2012
	€000	€000
All outstanding balances are secured except for the following:		
Loans and advances to customers		
- Associates	3,087	8,746
- Key management personnel	404	377
- Other related parties	880	480
	4,371	9,603
Details of guarantees received are disclosed below:		
Loans and advances to customers		
- Amounts guaranteed by the Government	362,279	394,597

	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 2011	2,499	33	2,499	33
Additions	-	820	-	820
	2,499	853	2,499	853
Less repayments	(448)	-	(448)	-
At 30 September 2012	2,051	853	2,051	853
Additions	102	7	102	7
	2,153	860	2,153	860
Less repayments	(143)	(553)	(143)	(553)
At 30 September 2013	2,010	307	2,010	307
Other key management personnel (chief officers)				
At 1 October 2011	931	28	931	28
Additions	235	-	235	-
	1,166	28	1,166	28
Less repayments	(122)	(21)	(138)	(21)
At 30 September 2012	1,044	7	1,028	7
Additions	661	-	661	-
	1,705	7	1,689	7
Less repayments	(83)	(9)	(74)	(9)
At 30 September 2013	1,622	(2)	1,615	(2)

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 2013 (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	
	2013 €000	2012 €000	2013 €000	2012 €000	2013 €000	2012 €000
Segment net interest income	117,970	114,619	13,044	33,213	131,014	147,832
Segment net commission income	33,034	28,421	19,079	16,015	52,113	44,436
Other segment income	14,757	13,430	20,243	13,166	35,000	26,596
Segment depreciation/amortisation	(3,781)	(3,498)	(2,259)	(2,090)	(6,040)	(5,588)
Other segment costs	(78,795)	(81,419)	(1,584)	(1,558)	(80,379)	(82,977)
Impairment losses	(22,904)	(20,020)	(2,691)	(2,797)	(25,595)	(22,817)
Segment operating profit before share of results of associates	60,281	51,533	45,832	55,949	106,113	107,482
Group share of results after tax of associates	-	-	12,384	6,348	12,384	6,348
Common costs					(2,719)	(3,100)
Group profit before tax					115,778	110,730
ASSETS						
Segment total assets	3,754,884	3,813,828	3,240,964	2,995,596	6,995,848	6,809,424
Property, plant and equipment and Intangible assets	56,546	50,244	22,896	21,261	79,442	71,505
Additions to property, plant and equipment & intangible assets	12,073	7,273	104	-	12,177	7,273
Unallocated assets	-	-	-	-	85,611	83,965
Carrying value of associates	-	-	84,880	77,058	84,880	77,058
Total Assets					7,257,958	7,049,225
LIABILITIES						
Segment total liabilities	6,262,914	5,850,216	304,271	567,815	6,567,185	6,418,031
Unallocated liabilities					113,768	110,194
Total Liabilities					6,680,953	6,528,225

The revenue which is reported above represents revenue generated from external customers. There were no inter-segment sales during the year (2012: 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 2013 (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 (MFSA) to single borrowers or groups of related borrowers and other significant risk concentrations. The CEO and the Board of Directors are regularly informed on the concentration of the Bank's portfolio 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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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

	The Group	
	2013	**2012**
	€000	**€000**
Agriculture	8,162	8,036
Fishing	1,098	1,007
Mining and quarrying	2,068	2,537
Manufacturing	146,086	141,356
Electricity, gas, steam and air conditioning supply	78,414	313,989
Water supply, sewerage waste management and remediation activities	31,730	32,124
Construction	289,577	320,448
Wholesale and retail trade	375,842	388,461
Transportation and storage	297,304	311,561
Accommodation and food service activities	261,058	259,330
Information and communication	43,119	28,655
Financial and insurance activities	316,083	90,661
Real estate activities	181,916	196,533
Professional, scientific and technical activities	22,114	52,477
Administrative and support service activities	58,985	67,311
Public administration and defence, compulsory social security	10,199	10,096
Education	13,316	13,540
Human health and social work activities	18,472	16,612
Arts, entertainment and recreation	49,490	49,086
Other services activities	18,602	18,478
Households and individuals	1,616,834	1,551,939
Loans and advances to customers	3,840,469	3,874,237
Loans and advances to banks	860,957	676,639
	4,701,426	**4,550,876**

The restructuring in one of the facilities having a balance of €230.3 million as at September 2012 resulted in the reclassification of this facility from the Electricity, gas, steam and air conditioning supply sector to the Financial and insurance activities sector in the current financial year.

(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 that falls 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.

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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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.

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

The Group

As at 30 September 2013

	Loans and advances to customers €000	Undrawn credit facilities and other commitments to lend €000
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**

As at 30 September 2012

Prime bank guarantees	1,698	44,153
Cash or quasi cash	116,961	50,539
Guarantees and/or letters of comfort issued by the Malta Government, the Central Bank of Malta or public agencies	383,132	116,385
Guarantees by prime institutions	700	103
Residential property	1,228,716	180,427
Commercial property	1,279,416	218,039
Personal guarantees and others	215,639	31,665
	3,226,262	**641,311**

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 2013 (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 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**
As at 30 September 2012					
AAA	-	178,759	22,304	726	201,789
AA- to AA+	-	292,824	32,239	982	326,045
A- to A+	259,889	1,286,537	564,542	10,081	2,121,049
Lower than A-	-	168,456	50,157	-	218,613
Unrated	-	14,146	7,397	5,120	26,663
	259,889	**1,940,722**	**676,639**	**16,909**	**2,894,159**

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

The Group At 30 September 2013	Loans & advances €000	Impairment allowances €000	Carrying value €000
Performing Exposures			
Neither past due nor impaired	3,374,162	(34,960)	3,339,202
Past due by less than 90 days but not impaired	58,831	(1,082)	57,749
Forborne performing	75,408	(1,698)	73,710
	3,508,401	(37,740)	3,470,661
Non-performing Exposures			
Forborne non-performing	88,709	(5,063)	83,646
Past due by 90 days or more but not impaired	70,200	(7,151)	63,049
Impaired	173,159	(60,844)	112,315
	332,068	(73,058)	259,010
	3,840,469	(110,798)	3,729,671

Interest income recognised during the year 2013 in respect of forborne assets amounts to €8.0 million.

At 30 September 2012	Loans & advances €000	Impairment allowances €000	Carrying value €000
Performing Exposures			
Neither past due nor impaired	3,436,565	(34,984)	3,401,581
Past due by less than 90 days but not impaired	62,718	(1,111)	61,607
Forborne performing	36,597	(1,070)	35,526
	3,535,880	(37,165)	3,498,714
Non-performing Exposures			
Forborne non-performing	89,661	(4,214)	85,448
Past due by 90 days or more but not impaired	77,421	(7,270)	70,151
Impaired	171,275	(39,451)	131,824
	338,357	(50,935)	287,423
	3,874,237	(88,100)	3,786,137

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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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

	Loans & advances	
	2013	**2012**
	€000	**€000**
Neither past due nor impaired:		
Regular	3,104,103	3,162,747
Watch	263,504	298,659
Sub-Standard	81,963	126,166
	3,449,570	3,587,572

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

Individually impaired gross loans by segment:

Personal	81,897	78,757
Business	91,262	92,518
	173,159	171,275

Impaired facilities are those credit facilities with payments of interest and/or capital overdue by 90 days or more or where the Group has reasons to doubt the eventual recoverability of funds.

Collateral for impaired loans

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

(iv) Movement in forbearance activity during the year

	Loans & advances €000
1 October 2012	126,258
Additions	50,536
Retired from forborne	(12,677)
30 September 2013	164,117

Notes to the financial statements 30 September 2013 (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
	2013	2013	2012	2012
	€000	€000	€000	€000
Change in allowances for uncollectability:				
At 1 October	39,451	48,649	30,978	35,173
Additions	31,767	6,534	15,497	16,316
Reversals	(10,374)	(5,229)	(7,024)	(2,840)
	21,393	1,305	8,473	13,476
At 30 September	60,844	49,954	39,451	48,649

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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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 2013	€000	€000	€000	€000	€000
Country					
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
As at 30 September 2012					
Country					
Greece	861	-	-	-	-
Ireland	-	6,993	-	6,993	7,133
Italy	-	5,928	-	5,928	5,978
Portugal	2,925	-	-	-	-
Spain	-	2,001	-	2,001	2,013
Cyprus	3,025	1,749	(170)	1,579	1,593
	6,811	16,671	(170)	16,501	16,717

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/ (charge)
As at 30 September 2013	€000	€000	€000
Country			
Greece	7	-	-
Ireland	-	280	-
Italy	-	70	-
Portugal	66	-	-
Spain	-	91	-
Cyprus	61	25	32
	134	466	32
As at 30 September 2012			
Country			
Greece	(222)	-	(103)
Ireland	-	284	-
Italy	-	379	-
Portugal	76	-	-
Spain	-	89	-
Cyprus	(21)	65	(170)
	(167)	817	(273)

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

The contractual maturity of the selected sovereign debt

	The Group	
	Within 1 year	Over 1 year
As at 30 September 2013	€000	€000
Country		
Ireland	6,997	-
Italy	2,002	-
Portugal	-	2,991
Spain	1,999	-
	10,998	2,991
As at 30 September 2012		
Country		
Greece	-	861
Ireland	-	6,993
Italy	3,922	2,006
Portugal	-	2,925
Spain	-	2,001
Cyprus	1,579	3,025
	5,501	17,811

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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

	Due within 3 months €000	Due between 3 & 12 months €000	Due between 1 & 5 years €000	Due after 5 years €000	Total outflow €000
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				
At 30 September 2012					
Financial liabilities at fair value through profit or loss	5,259	10,491	32,684	11,933	60,367
Amounts owed to banks	44,669	11,060	175,195	-	230,924
Amounts owed to customers	4,328,377	1,062,978	467,231	12,693	5,871,279
Debt securities in issue	1,700	4,359	16,587	101,459	124,105
Subordinated liabilities	1,338	4,698	24,140	133,750	163,926
Financial liabilities designated for hedge accounting	2,831	5,492	16,635	17,458	42,416
Other financial liabilities	101,718	20,631	13,172	19,830	155,351
	4,485,892	**1,119,709**	**745,644**	**297,123**	**6,648,368**
Loan commitments	950,929				

Notes to the financial statements 30 September 2013 (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.

The Group	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 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**
Equity holders of the Bank	-	-	-	-	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 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

The Group	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 2012						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	200,142	7,955	-	-	88,037	**296,134**
Fair value through profit or loss						
- Debt and other fixed income instruments	16,711	108,097	295,547	185,346	-	**605,701**
- Equity and other non-fixed income instruments	-	-	-	-	61,754	**61,754**
- Loans and advances	-	-	-	83,920	-	**83,920**
- Derivative financial instruments	7,107	1,767	2,058	5,977	-	**16,909**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	-	149	197,604	121,092	-	**318,845**
- held-to-maturity	35,384	154,733	689,960	136,099	-	**1,016,176**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	3,435	**3,435**
Loans and advances to banks	658,726	-	523	-	17,390	**676,639**
Loans and advances to customers	683,084	229,607	467,641	2,321,885	-	**3,702,217**
Investments in associates	-	-	-	-	77,058	**77,058**
Other assets	-	-	-	-	190,437	**190,437**
	1,601,154	**502,308**	**1,653,333**	**2,854,319**	**438,111**	**7,049,225**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	5,927	2,429	11,339	41,184	-	**60,879**
Amounts owed to banks	69,297	11,055	170,000	-	-	**250,352**
Amounts owed to customers	4,295,064	1,038,781	462,943	12,512	-	**5,809,300**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	154,429	**154,429**
Financial liabilities held for hedging	-	-	5,457	32,408	-	**37,865**
Subordinated liabilities	-	-	-	120,000	-	**120,000**
Non-controlling interest	-	-	-	-	243	**243**
Equity holders of the Bank	-	-	-	-	520,757	**520,757**
	4,370,288	**1,052,265**	**649,739**	**301,504**	**675,429**	**7,049,225**

Notes to the financial statements 30 September 2013 (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 2013 (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 2012						
Assets						
Balances with Central Bank of Malta, treasury bills and cash	200,142	7,955	-	-	88,037	**296,134**
Fair value assets through profit or loss						
- Debt and other fixed income instruments	16,711	108,097	295,547	185,346	-	**605,701**
- Equity and other non-fixed income instruments	-	-	-	-	57,193	**57,193**
- Loans and advances	-	-	-	83,920	-	**83,920**
- Derivative financial instruments	7,107	1,767	2,058	5,977	-	**16,909**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	-	149	197,604	121,092	-	**318,845**
- held-to-maturity	35,384	154,733	689,960	136,099	-	**1,016,176**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	3,435	**3,435**
Loans and advances to banks	658,726	-	523	-	17,390	**676,639**
Loans and advances to customers	683,084	229,607	467,641	2,321,885	-	**3,702,217**
Investments in associates and subsidiaries	-	-	-	-	54,263	**54,263**
Other assets	-	-	-	-	190,977	**190,977**
	1,601,154	**502,308**	**1,653,333**	**2,854,319**	**411,295**	**7,022,409**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	5,927	2,429	11,339	41,184	-	**60,879**
Amounts owed to banks	69,297	11,055	170,000	-	-	**250,352**
Amounts owed to customers	4,296,368	1,038,781	462,943	12,512	-	**5,810,604**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	153,248	**153,248**
Financial liabilities held for hedging	-	-	5,457	32,408	-	**37,865**
Subordinated liabilities	-	-	-	120,000	-	**120,000**
Equity holders of the Bank	-	-	-	-	494,061	**494,061**
	4,371,592	**1,052,265**	**649,739**	**301,504**	**647,309**	**7,022,409**

Notes to the financial statements 30 September 2013 (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.

During this financial year, the Bank decided to discontinue the calculation of the Value at Risk (VaR) methodology since the Bank's strategy is to hold these instruments till maturity rather than as a trading portfolio. The VaR model was used to measure the interest rate risk on exposures which are carried at fair value and are not hedged, by taking into consideration the volatility of relevant market prices and the correlation of their movements. In addition the Bank recognised that the VaR methodology had also a number of limitations arising from its dependence on historical data, assumed distribution, holding periods and frequency of calculation. Moreover, the VaR did not convey any information about potential loss when the confidence level was exceeded and was not well suited for non-linear positions.

However, 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 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 2013 (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 2013 and 2012 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 2013, the impact on economic value is estimated at 1.90% (2012: 0.02%).

	2013	**2012**
The Group	**€000**	**€000**
Impact on capital	11,180	107

(iii) Impact of interest rate risk on interest margin

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

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

The Group	**€000**	**€000**
Net effect on interest income for 12 months	8,638	8,739

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

(iii) 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	82,230	67,984	10,984	-	33,389	**194,587**
Fair value assets through profit or loss						
- Debt and other fixed income instruments	43,391	105,568	86,940	205,927	-	**441,826**
- Equity and other non-fixed income instruments	-	-	-	-	66,362	**66,362**
- Loans and advances	61,932	-	-	-	-	**61,932**
- Derivative financial instruments	-	4,620	454	315	6,022	**11,411**
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	6,287	-	45,343	261,033	-	**312,663**
- held-to-maturity	235,567	327,860	116,132	672,854	-	**1,352,413**
- Equity and other non-fixed income instruments						
- available-for-sale	-	-	-	-	744	**744**
Loans and advances to banks	756,653	-	-	-	104,304	**860,957**
Loans and advances to customers	3,636,849	249	4,786	25,855	-	**3,667,739**
Investments in associates	-	-	-	-	84,880	**84,880**
Other assets	-	-	-	-	202,444	**202,444**
Total 2013	**4,822,909**	**506,281**	**264,639**	**1,165,984**	**498,145**	**7,257,958**
Total 2012	4,705,222	441,875	162,979	1,302,466	436,683	7,049,225
LIABILITIES and EQUITY						
Financial liabilities at fair value through profit or loss	3,623	10,431	10,143	-	6,622	**30,819**
Amounts owed to banks	14,121	-	-	-	21,919	**36,040**
Amounts owed to customers	3,584,609	403,774	1,234,178	399,454	597,651	**6,219,666**
Debt securities in issue	-	-	-	95,400	-	**95,400**
Other liabilities	-	-	-	-	147,799	**147,799**
Financial liabilities held for hedging	459	20,044	10,726	-	-	**31,229**
Subordinated liabilities	-	-	-	120,000	-	**120,000**
Non-controlling interest	-	-	-	-	661	**661**
Equity holders of the Bank	-	-	-	-	576,344	**576,344**
Total 2013	**3,602,812**	**434,249**	**1,255,047**	**614,854**	**1,350,996**	**7,257,958**
Total 2012	3,383,743	511,341	1,101,417	871,089	1,181,635	7,049,225
Interest rate swaps - 2013	**31,753**	**186,466**	**108,484**	**(326,703)**	**-**	
Interest rate swaps - 2012	44,747	193,473	217,042	(455,262)	-	
Gap - 2013	**1,251,850**	**258,498**	**(881,924)**	**224,427**	**(852,851)**	
Gap - 2012	1,366,226	124,007	(721,396)	(23,885)	(744,952)	
Cumulative Gap - 2013	**1,251,850**	**1,510,348**	**628,424**	**852,851**	**-**	
Cumulative Gap - 2012	1,366,226	1,490,233	768,837	744,952	-	

Notes to the financial statements 30 September 2013 (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.

	2013 Euro €000	2013 Other Currencies €000	2013 Total €000	2012 Euro €000	2012 Other Currencies €000	2012 Total €000
The Group						
Assets						
Balances with Central Bank of Malta treasury bills and cash	192,087	2,500	**194,587**	293,061	3,073	296,134
Financial assets at fair value through profit or loss						
- Debt and other fixed income instruments	334,702	107,124	**441,826**	464,573	141,128	605,701
- Equity and other non-fixed income instruments	64,740	1,622	**66,362**	60,173	1,581	61,754
- Loans and advances	61,932	-	**61,932**	83,920	-	83,920
- Derivative financial instruments	2,693	8,718	**11,411**	2,884	14,025	16,909
Investments						
- Debt and other fixed income financial instruments						
- available-for-sale	236,278	76,385	**312,663**	250,091	68,754	318,845
- held-to-maturity	704,559	647,854	**1,352,413**	526,632	489,544	1,016,176
- Equity and other non-fixed income instruments						
- available-for-sale	744	-	**744**	3,435	-	3,435
Loans and advances to banks	646,451	214,506	**860,957**	344,142	332,497	676,639
Loans and advances to customers	3,602,958	64,781	**3,667,739**	3,626,812	75,405	3,702,217
Other assets	280,773	6,551	**287,324**	261,023	6,472	267,495
	6,127,917	**1,130,041**	**7,257,958**	**5,916,746**	**1,132,479**	**7,049,225**
Liabilities and Equity						
Financial liabilities at fair value through profit or loss	21,615	9,204	**30,819**	46,944	13,935	60,879
Amounts owed to banks	18,465	17,575	**36,040**	208,560	41,792	250,352
Amounts owed to customers	5,238,564	981,102	**6,219,666**	4,847,852	961,448	5,809,300
Debt securities in issue	95,400	-	**95,400**	95,400	-	95,400
Other liabilities	134,992	12,807	**147,799**	135,269	19,160	154,429
Financial liabilities held for hedging	14,079	17,150	**31,229**	10,202	27,663	37,865
Subordinated liabilities	120,000	-	**120,000**	120,000	-	120,000
Equity	584,578	(7,573)	**577,005**	528,100	(7,100)	521,000
	6,227,693	**1,030,265**	**7,257,958**	**5,992,327**	**1,056,898**	**7,049,225**

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.

The 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 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.5 Transferred Financial Assets that are not derecognised in their entirety

	The Group and the Bank	
	2013	2012
	€000	€000
Debt securities classified as		
- held-to-maturity	-	5,368
- fair value through profit or loss	-	5,687
	-	11,055
Amounts owed to banks	-	11,055

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 amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. 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.

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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

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

	Quoted price in active markets [1] €000	Valuation techniques using observable inputs [2] €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 to customers	-	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**
30 September 2012			
Assets			
Financial assets at fair value through profit or loss			
- debt and other fixed income instruments	523,110	82,591	605,701
- equity and other non-fixed income instruments	61,754	-	61,754
- loans and advances to customers	-	83,920	83,920
- derivative financial instruments	-	16,909	16,909
Investments			
Debt and other fixed income instruments			
- available-for-sale	248,181	70,664	318,845
	833,045	**254,084**	**1,087,129**
Liabilities			
Financial liabilities at fair value through profit or loss			
- derivative financial instruments	-	60,879	60,879
Financial liabilities designated for hedge accounting			
- derivative financial instruments	-	37,865	37,865
	-	**98,744**	**98,744**

[1] Level 1 in the fair value hierarchy represents quoted prices (unadjusted) in active markets for identical assets or liabilities.

[2] Level 2 in the fair value hierarchy represents inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (ie as prices) or indirectly (ie derived from prices).

During the year under review financial assets at fair value through profit or loss amounting to €60.2 million were transferred from Level 2 to Level 1 (2012: €93.4 million), and €2.8 million were transferred from Level 1 to Level 2 (2012: €24.3 million). The transfer from Level 2 to Level 1 was due to securities which had quoted prices on active markets as at 30 September 2013 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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

Control Framework

Fair values are subject to a control framework designed to ensure that they are either determined or validated by a function independent of the risk taker and that they are appropriately performed and reviewed by competent personnel. To this end, the determination of fair values is a process which is performed by Financial Markets and Investments and reviewed by Finance. Finance establishes the accounting policies and, in conjunction with Financial Markets and Investments, it establishes the procedures governing valuation, and is responsible for ensuring that they comply with all relevant accounting standards. The valuation techniques and procedures applied are subject to a process of due diligence, which process was duly approved by the Board and the Audit Committee and documented accordingly.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to valuation techniques, independent price determination or validation is utilised, to the extent practicable. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Bank sources alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable. The factors which are mainly considered are the following:

- the extent to which prices may be expected to represent genuine traded or tradable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the end of the reporting period; and
- the manner in which the data was sourced.

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.

Notes to the financial statements 30 September 2013 (continued)

39. FINANCIAL RISK MANAGEMENT (continued)

39.7 Capital risk management

The Group's capital management approach ensures a sufficient level of capitalisation to manage the risk exposures whilst supporting business growth and providing adequate returns to the shareholders. Risk capital management does not in any way substitute risk mitigation measures. It is vital that the structure of limits and thresholds should be able to prevent concentrations of risk from building up in such a way as to compromise a significant proportion of the Group's capital resources.

The Group ensures that it complies with the capital requirements set by the regulator. At the start of the financial period ending on 30 September 08, the Group implemented Banking Rule BR/04/2007 – Capital Requirements of Credit Institutions Authorised Under the Banking Act 1994. The Group thereby became Basel II compliant with respect to Pillar I requirements, allocating regulatory capital against credit risk (using the standardised approach), operational risk (using the basic indicator approach) and market risk. The Group also allocates capital for other material risks as part of the Internal Capital Adequacy Assessment Process (ICAAP) embedded in the Pillar II process. This process helps to measure with greater risk-sensitivity the amount of regulatory capital which the Group requires to cover risks assumed in the course of its business, including risks not covered under Pillar I. The Group believes in the rationale behind the ICAAP, and has undertaken a fully-fledged implementation programme to ensure a better alignment between material risks and regulatory capital, in order to strengthen capital deployment and improve the risk management and mitigation techniques adopted by the institution. The Board submitted the latest ICAAP capital document to the MFSA in March 2013. The next ICAAP will be submitted in the first quarter of the next calendar year.

Capital management is under the direct control of the Asset and Liability Committee (ALCO). During the financial year, ALCO has monitored adequacy of Group capital, gave strategic direction on the most efficient use of capital and identified and quantified changes to risk capital requirements arising from the implementation of Pillar II.

ALCO is supported by the Asset and Liability Management (ALM) Unit in the management of capital. The ALM Unit monitors and forecasts Group capital, including the capital mix and the level and nature of subordinated debt.

During the year under review and during the comparative period, the Group has complied with the externally imposed capital requirements.

The following table shows the components and basis of calculation of the Group and the Bank Capital Adequacy ratios.

	The Group	The Bank
	€000	€000
Own Funds		
Tier 1		
- Ordinary shares	300,000	300,000
- Share premium	988	988
- Retained earnings	159,968	156,828
- Non-controlling interest	661	-
- Deductions:		
Intangible assets	(11,495)	(11,495)
Participations held in insurance undertakings - 50%	(26,435)	(26,435)
Unrealised net losses on AFS financial assets	(4,519)	(4,519)
Total Tier 1 Capital	419,168	415,367
Tier 2		
- Available-for-sale reserve	5,260	5,178
- Property revaluation reserve	23,880	23,850
- Collective impairment allowance	49,954	49,954
- Subordinated liabilities	120,000	120,000
- Deductions:		
Participations held in insurance undertakings - 50%	(26,435)	(26,435)
Total Tier 2 Capital	172,659	172,547
Total Own Funds	591,827	587,914

Notes to the financial statements 30 September 2013 (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	194,587	-	194,587	-
Financial assets at fair value through profit or loss	581,531	266,399	578,691	263,996
Investments	1,665,820	301,910	1,665,820	301,910
Loans and advances to banks	860,957	52,732	860,957	52,732
Loans and advances to customers	3,667,739	2,167,884	3,667,739	2,167,884
Other assets	287,324	113,828	255,525	114,774
	7,257,958	2,902,753	7,223,319	2,901,296
Off-Balance Sheet Items	1,378,249	304,647	1,378,249	304,647
Operational Risk		383,350		381,633
Total risk weighted assets		3,590,750		3,587,576
Capital Adequacy Ratio				
30 September 2013				
Tier 1 Ratio		11.7%		11.6%
Total Capital Ratio		16.5%		16.4%
30 September 2012				
Tier 1 Ratio		10.7%		10.7%
Total Capital Ratio		15.2%		15.2%

40. REGISTERED OFFICE

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

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 2013, the total assets held by the Group on behalf of its customers amounted to €603.7 million (2012: €585.1million).

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.

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

	2013 €000	2012 €000	2011 €000	2010 €000	2009 €000
Interest receivable and similar income	222,437	238,545	224,064	219,904	240,065
Interest payable	(91,423)	(90,713)	(86,755)	(93,153)	(124,694)
Net interest income	131,014	147,832	137,309	126,751	115,371
Other operating income	87,113	71,032	36,237	64,440	57,412
Other operating charges	(89,138)	(91,665)	(97,179)	(78,796)	(77,055)
Net impairment losses	(25,595)	(22,817)	(16,041)	(12,936)	(4,016)
Share of results of associates	12,384	6,348	4,047	(542)	(9,894)
Profit before tax	115,778	110,730	64,373	98,917	81,818
Income tax expense	(36,305)	(36,454)	(22,319)	(34,945)	(32,403)
Profit for the year	79,473	74,276	42,054	63,972	49,415
Attributable to:					
Equity holders of the Bank	79,055	74,995	41,675	63,447	49,014
Non-controlling interest	418	(719)	379	525	401
	79,473	74,276	42,054	63,972	49,415
Earnings per share	**26c4**	**25c0**	**13c9**	**21c1**	**16c3**

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 2013.

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

B. STATEMENTS OF FINANCIAL POSITION

	2013 €000	2012 €000	2011 €000	2010 €000	2009 €000
Assets					
Balances with Central Bank of Malta, treasury bills and cash	194,587	296,134	170,844	135,773	278,270
Investments and financial assets at fair value through profit or loss	2,247,351	2,106,740	2,203,539	2,206,942	2,260,624
Loans and advances to banks	860,957	676,639	400,931	264,965	207,481
Loans and advances to customers	3,667,739	3,702,217	3,607,064	3,496,744	3,245,899
Investments in associates	84,880	77,058	71,761	68,689	54,886
Property, plant and equipment	91,618	78,778	77,093	80,496	81,678
Current tax	-	-	7,143	1,482	-
Deferred tax	70,205	63,607	49,148	46,085	45,640
Other assets	15,406	20,362	14,264	13,047	8,978
Prepayments and accrued income	25,215	27,690	25,282	25,241	37,230
Total Assets	**7,257,958**	**7,049,225**	**6,627,069**	**6,339,464**	**6,220,686**
LIABILITIES					
Financial liabilities at fair value through profit or loss and held for hedging	62,048	98,744	76,653	78,559	56,544
Amounts owed to banks	36,040	250,352	260,614	347,369	668,584
Amounts owed to customers	6,219,666	5,809,300	5,523,907	5,185,264	4,766,278
Debt securities in issue	95,400	95,400	55,400	25,701	24,936
Current tax	4,697	13,405	356	187	507
Deferred tax	5,003	4,199	4,199	4,272	4,272
Other liabilities	108,864	106,235	78,526	73,429	126,574
Accruals and deferred income	29,235	30,590	33,217	35,635	41,789
Subordinated liabilities	120,000	120,000	120,000	120,000	96,567
Total Liabilities	6,680,953	6,528,225	6,152,872	5,870,416	5,786,051
EQUITY					
Equity attributable to shareholders of the Bank					
Called up share capital	300,000	270,000	240,000	200,000	160,000
Share premium account	988	988	988	988	988
Revaluation reserve	24,621	13,573	18,036	24,931	21,810
Retained earnings	250,735	236,196	214,211	242,546	251,199
	576,344	520,757	473,235	468,465	433,997
Non-controlling interest	661	243	962	583	638
Total Equity	577,005	521,000	474,197	469,048	434,635
Total Liabilities and Equity	**7,257,958**	**7,049,225**	**6,627,069**	**6,339,464**	**6,220,686**
MEMORANDUM ITEMS					
Contingent liabilities	213,598	215,512	191,726	183,803	167,875
Commitments	1,184,279	1,049,804	1,066,597	1,096,124	1,049,013

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

C. STATEMENTS OF CASH FLOW

	2013 €000	2012 €000	2011 €000	2010 €000	2009 €000
Net cash from operating activities	509,520	397,001	155,525	116,799	6,149
Cash flows from investing activities					
Dividends received from equity shares	5,433	1,723	2,240	5,639	1,788
Interest received from investing securities	37,484	50,165	46,706	45,745	42,175
Investment in associates	-	-	-	(18,845)	(2,754)
Purchase of equity investments	-	-	(1,341)	(953)	-
Net increase in investment securities	(379,284)	(6,575)	(74,265)	(49,697)	(217,251)
Purchase of property, plant and equipment	(10,414)	(7,273)	(9,005)	(4,946)	(5,651)
Proceeds on disposal of property, plant and equipment	-	8	6,982	-	-
Net cash (used in)/from investing activities	(346,781)	38,048	(28,683)	(23,057)	(181,693)
Cash flows from financing activities					
Subordinated funds	-	-	-	23,433	50,000
Debt securities in issue	-	40,000	29,699	-	-
Dividends paid	(34,516)	(23,010)	(30,550)	(32,690)	(9,970)
Net cash (used in)/from financing activities	(34,516)	16,990	(851)	(9,257)	40,030
Increase/(Decrease) in cash and cash equivalents	128,223	452,039	125,991	84,485	(135,514)

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

	2013 %	2012 %	2011 %	2010 %	2009 %
Operating income to total assets	3.05	3.20	2.68	3.04	2.78
Operating expenses to total assets	1.25	1.34	1.50	1.25	1.24
Profit before tax to total assets	1.62	1.62	0.99	1.58	1.31
Profit before tax to capital employed	21.11	22.28	13.67	21.92	19.79
Profit attributable to equity holders to total assets	1.11	1.10	0.64	1.01	0.79
Profit attributable to equity holders to capital employed	14.41	15.09	8.85	14.06	11.86

The Group's financial highlights in US Dollars 30 September 2013

The following figures were converted from Euro to US Dollars using the rate of exchange ruling on 30 September 2013. The rate used was €1 = US$ 1.3502. This does not reflect the effect of the change in the rate of exchange since 30 September 2012 which was €1 = US$ 1.2922.

	2013 US$'000	2012 US$'000
Net income attributable to shareholders of the Bank	106,740	96,909
Net income per share	36c	36c
Gross dividend paid	71,696	45,744
Net dividend paid	46,604	29,734
Gross dividend per share	24c	17c
Total assets	9,799,695	9,109,009
Liquid funds	262,731	382,664
Investments and financial assets at fair value through profit or loss	3,034,373	2,722,329
Advances	6,114,645	5,658,358
Investments in associates	114,605	99,574
Share capital	405,060	348,894
Capital reserves	34,577	18,816
Retained earnings	338,542	305,212

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