ANNUAL REPORT
2014

mediterraneanbank
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MEDITERRANEAN BANK PLC
ANNUAL REPORT
2014

Company Registration Number: C 34125

Chairman's Statement

The macro-economic stresses that have plagued the Eurozone since the onset of the financial crises in 2009/10 finally show signs of abating through the second half of the financial year.

The impacts of loose monetary policy from the ECB and an extended period of historically low interest rates have driven capital toward riskier assets and thus we have observed a significant rally in peripheral European debt which has stabilised the funding situation of all programme countries and beyond, enabling them to achieve continued access to capital markets at attractive rates for the first time in a number of years. Indeed, through this period, we saw Ireland exit its programme without the need for any back-stop facilities and we shortly expect Portugal to do the same. Concerns remain however in Europe regarding sluggish economic growth with an increasing focus on the threat of pan European deflation, as the core European countries have so far failed to provide a robust economic engine. This has been compounded by the impact of the Euro which has continued to trade as a very strong currency.

Within this context Malta itself continues to outperform economically with annual GDP growth of 2.4% compared with the European Union average of 0.1%. The Maltese banking system continues to operate with strong levels of capital and access to robust liquidity from the deposit-rich domestic market. Likewise, Mediterranean Bank continues to operate with a prudent total capital ratio of 14.25% and an extremely strong liquidity ratio of 148.7%.

DEVELOPMENTS

The financial year 2013/14 has been another significant phase in the rapid development of the Bank. The strong financial results have enabled us to grow our own funds from €123.7 million to €152.4 million, again demonstrating the strong commitment from the shareholders to invest in the growth of the Bank and enable the management team to deploy capital in order to build the Bank's capabilities and the Bank's customer base. This has most notably been demonstrated in two significant events. Firstly in the third quarter of 2013 the Bank opened its Belgian branch under the brand name of MeDirect. Building on the investments and capabilities developed in the Maltese market the Bank has evolved these further and has opened a highly competitive online offering for the Belgian market focused on attractive savings, investments and wealth management products for the mass affluent market. The Board is very pleased with the initial phase of the launch of this business. Secondly, in April 2014, it was announced that the Bank has entered into a purchase agreement for 100 per cent of the share capital of Volksbank Malta, a local banking subsidiary of VB-Holding Aktiengesellschaft which will enable the Bank to expedite the growth of its corporate local lending business in the domestic market. The transaction is expected to be completed in early summer 2014 after the appropriate regulatory process has been finalised.

Francis J. Vassallo
Chairman

OUTLOOK

These two significant corporate developments enable the Board to look forward to the coming year with cautious optimism. The Belgian branch is almost entirely operated from an efficient operating base, enabling the delivery of competitive savings and wealth management products to the Belgian market in a cost effective, transparent and customer friendly manner.

The purchase of Volksbank Malta will help consolidate the Bank's position in the domestic Maltese market, and broaden its contribution to the local economy, while developing further its lending business.

Although challenging for the management team, the Board remains confident that the previous and on-going investments in the necessary personnel and technical skills, will continue to bear fruit and the Bank will continue to enjoy successful development in the medium term.

CONCLUSION

The Board remains conscious of the need to maintain balance sheet discipline whilst continuing to develop the commercial proposition of the Bank. The on-going robustness of capital and liquidity ratios provide a stable foundation from which to produce attractive and sustainable returns. The strategy that has been defined by the Board over the last few years has resulted in significant growth, whilst producing attractive returns and an ability to invest in the capabilities of the Bank. We continue to support this strategy and believe that this will be the most appropriate path for all stakeholders of the Bank to follow.

FRANCIS J. VASSALLO
CHAIRMAN

28 May 2014

Chief Executive Officer's Review

The 2013/14 financial year provided some significant milestones in the development of Mediterranean Bank, both domestically in Malta and internationally with the opening of our Belgian branch.

Over the last three years, we have significantly invested in the infrastructure that has enabled us to enhance our customer offering and geographical reach. In Malta, we have developed a seven branch network focused on providing a first class and personalised customer experience by delivering our market leading savings, investments and wealth management products. These services are supported by our innovative technology platform that provides low cost and transparent execution and reporting facilities for our growing investment client base. In turn, we have now deployed these capabilities to facilitate the growth of our Belgian business where our attractive multi-lingual online offering is meeting early success after its initial launch in late 2013. We believe that the model that we developed to operationally execute from Malta and electronically distribute in Belgium, is a unique one that serves our ability to deliver first-class products at a cost-efficient price point, which will realise our business goals in the coming 12 months. We are already looking forward to the next stage of the development, when we subsidiarise the MeDirect entity and create a fully licensed Belgian bank.

The evolution of the balance sheet as we have grown our customer base, has continued along the path we had defined over 2 years ago. The overall deposit base stood at €777 million, a growth of 37% year on year. The average life of the deposit base stood at 527 days ensuring a highly robust and prudent degree of liquidity on which the bank can rely. As a function of this stability of funding, and an adequate capital base, the corporate portfolio has grown from €402 million to €571 million, including loans and senior secured bonds. This well diversified portfolio will continue to grow over the coming 12 months as we deploy more of our capital into corporate lending. The loans to deposit ratio stood at 0.74.

In order to further enhance our position in the domestic Maltese market, we have entered into an agreement to acquire Volksbank Malta, a banking entity which has specialised in domestic corporate lending since 2004. Using the capital and liquidity available to us we intend to develop this platform to both broaden and deepen our corporate relationships for what will become the Mediterranean Bank group. Our ability to build businesses around core competences has driven our business forward in the past, and will continue to be a key to our future success.

Mark A. Watson
Chief Executive Officer

Balance sheet discipline continues to be managed alongside rigorous cost control which despite on-going and extensive operational investment enabled the Bank to report a PBT for the year of just under €30 million. Operational expenses grew from €23 million to €34 million as a function of a continued investment in our products and services, and the international expansion of the business. We expect this expense growth to abate over the coming period as we focus on the commercial development of the infrastructure we have invested in.

As always, I would like to extend my gratitude to our employees, who continue to develop our high level of customer services that enable the growth of the Bank to continue. Our full time complement of staff has grown from 194 to 227 and whilst we continue to expect some growth in these numbers the pace of that growth should slow somewhat as we benefit from our myriad of investments in our technological capabilities.

We look forward to the new financial year fully aware of the multiple challenges that we have before us but optimistic about the path the Bank has defined, and that the continued focus of our business strategy will reap the rewards of our previous work.

MARK A. WATSON
CHIEF EXECUTIVE OFFICER

28 May 2014

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Statement of Compliance with the Principles of Good Corporate Governance

Introduction

Mediterranean Bank plc (the "Bank") hereby reports on the extent to which the Code of Principles of Good Corporate Governance (the "Code") has been adopted as required by the Listing Rules of the Malta Listing Authority as amended on 29 April 2014.

Compliance with the Code

Principles 1 and 3: Board of Directors and composition of the Board

The Board of Directors (the "Board") is composed of persons with a diverse range of skills and experience acquired in senior roles with international banks and financial organisations, professional firms and governmental entities. At 31 March 2014, the Board consisted of three non-executive members and four executive members. Taking into account certain factors such as the size of the Bank, the size of the Board and the balance of skills and experience represented by its members these are considered to be appropriate for the requirements of the business of the Bank.

In line with the Bank's Articles of Association, the Chairman of the Board and Board directors resign and seek re-election at each Annual General Meeting of the Bank. All directors are required to be fit and proper to direct the business of the Bank.

Principle 2: Chairman and Chief Executive

The positions of Chairman and Chief Executive are held by different individuals, avoiding concentration of authority and power in one individual and differentiating the leadership of the Board from that of the running of the business of the Bank.

Principles 4, 5 and 8: Responsibilities of the Board and Board meetings and committees

The Board has the first level responsibility for executing the four basic roles of corporate governance namely: accountability, monitoring, strategy formulation and policy development.

Functioning of the Board

The Board of Directors reviews and evaluates corporate strategy, major operational and financial plans, risk policy and performance objectives. The Board monitors implementation of its decisions and corporate performance, taking into account the requirements of all relevant laws, regulations and codes of best business practice. In particular, the Board:

- defines the Bank's strategy, policies, management performance criteria and business policies;
- establishes a clear internal and external reporting system so that the Board has continuous access to accurate, relevant and timely information;
- assesses and monitors the Bank's present and future operations, opportunities, threats and risks in the external environment and current and future strengths and weaknesses;
- evaluates management's implementation of the Bank's corporate strategy and financial objectives using key performance indicators;
- ensures that the Bank has appropriate policies and procedures in place to enable the Bank and its staff to comply with the highest standards of corporate conduct, including compliance with applicable laws, regulations and business and ethical standards; and
- ensures that the financial statements of the Bank and the annual audit of such statements are completed within the stipulated time periods.

Statement of Compliance with the Principles of Good Corporate Governance

Functioning of the Board (continued)

Notices of the dates of scheduled meetings of the Board together with supporting materials are circulated to the directors well in advance of such meetings. Advance notice is also given of ad hoc meetings of the Board to allow directors sufficient time to re-arrange their commitments in order to be able to participate. After each Board meeting and before the next meeting, minutes that faithfully record attendance, deliberations and decisions of the Board are prepared and circulated to all directors.

This section provides details of the members of the Board of directors of the Bank and the members of each of the committees of the Board:

Board of Directors

Since the date of the previous annual general meeting of the Bank, 19 Board meetings were held, including eleven regularly scheduled meetings and eight telephone conference calls.

		Meetings attended %	Calls attended %
Francis J. Vassallo	Chairman and Independent Non-Executive Director	100%	63%*
Finlay S. McFadyen	Independent Non-Executive Director	100%	88%
Peter B. Cartwright	Non-Executive Director (resigned 26 February 2014)	100%	100%
Benjamin Hollowood	Non-Executive Director (appointed 30 May 2013)	100%	88%
Mark A. Watson	Executive Director – Chief Executive Officer	100%	88%
Henry C. Schmeltzer	Executive Director – Head of Commercial Strategy and Legal	100%	100%
Joaquin Vicent	Executive Director – Head of Treasury and Investment	100%	100%
Vincent Chatard	Executive Director – Chief Business Development Officer	100%	88%

* Excused for personal reasons.

Committees of the Board

Certain responsibilities of the Board of directors are delegated to Board committees. The Board committees play an essential role in supporting the Board in fulfilling its responsibilities and ensuring that the highest standards of corporate governance are maintained. Each Board committee reports to the Board following each of its meetings and the minutes of meetings of each Board committee meeting are available to the full Board.

Statement of Compliance with the Principles of Good Corporate Governance

Board Committees

A. Audit Committee

As a result of the increased size of the Bank's product base and range of operations, on 27 November 2013, the Bank replaced the Audit and Risk Committee with an Audit Committee and a separate Risk Committee.

The Audit Committee is primarily responsible for reviewing and approving specific matters relating to the audit of the Bank, internal control and risk management systems. In particular, the Audit Committee:

- reviews and approves the annual internal audit plan and subsequent revisions and monitors progress against the annual audit plan;
- ensures that the scope of work performed in accordance with the audit plan is adequate and appropriate;
- vets and approves related party transactions in accordance with Listing Rule 5.138;
- reviews work performed on all audit engagements; and
- reviews and interacts with external auditors on the annual statutory audit to obtain feedback on the internal control framework and financial reporting of the Bank.

The members of the Audit Committee are:

Finlay S. McFadyen	Committee Chairman and Independent Non-Executive Director
Francis J. Vassallo	Member and Independent Non-Executive Director/Board Chairman
Benjamin Hollowood	Member and Non-Executive Director (appointed 30 May 2013)
Peter B. Cartwright	Member and Non-Executive Director (resigned 26 February 2014)

Mr Francis J. Vassallo was appointed by the Board as the independent director who is competent in accounting and/or auditing in terms of listing rules 5.117 and 5.118. Mr Vassallo occupied various senior positions with Chase Manhattan Bank, is ex-Governor of the Central Bank of Malta, ex-Chairman of the Malta Development Corporation and presently a member of numerous boards of directors of entities operating in the financial services industry. Mr Vassallo is deemed independent because he is 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 his judgment.

During the year ended 31 March 2014, four quarterly meetings of the Bank's Audit Committee were held. In addition, the Chairman of the Committee held regular discussions with the Bank's internal auditors without the presence of an executive director.

B. Nomination and Remuneration Committee

The Nomination and Remuneration Committee is described in the Remuneration Report.

The Nomination and Remuneration Committee is composed only of non-executive directors with no personal financial interest. The Chairman is an independent non-executive director.

Statement of Compliance with the Principles of Good Corporate Governance

Board Committees (continued)

C. Risk Committee

The Risk Committee represents the principal forum for overseeing all risks of the Bank. In addition, it is responsible for recommending the Bank's risk appetite to the Board, and deciding risk-related policies and recommendations.

The members of the Risk Committee are:

Benjamin Hollowood	Committee Chairman and Non-Executive Director
Peter B. Cartwright	Member and Non-Executive Director (resigned 26 February 2014)
Finlay McFadyen	Member and Independent Non-Executive Director
Mark A. Watson	Member and Executive Director – Chief Executive Officer

The main objective of the Risk Committee is to ensure that the Bank adheres to the approved risk policy and procedures, and operates within the approved risk appetite of the Board. The key Committee functions are:

- reviews and approves changes to the Bank's risk policy and procedures;
- ensures that the risk functions are appropriately resourced and structured to meet their obligations and are working effectively to maintain an effective control environment;
- reviews any violations to the lending limits;
- reviews the product distribution strategy, including product structure, pricing and targeting; and
- monitors:
    - the effectiveness of risk management processes implemented in support of risk policies;
    - portfolio risk and sector concentration risk, including evolution of the risk profile against plan;
    - credit quality trends;
    - provision levels;
    - interest rate, currency and other market risk;
    - liquidity risk;
    - operational risk; and
    - contingent exposures.

The Chairman of the Committee reports on all matters to the Board after each meeting and notifies the Board of decisions made. The Committee makes whatever recommendations to the main Board that it deems necessary.

Meetings are scheduled quarterly. All attendees and invitees receive copies of the minutes.

Statement of Compliance with the Principles of Good Corporate Governance

Board Committees (continued)

D. Board Executive Committee

The Board Executive Committee was established in order to facilitate the day to day activities of the Bank including approval of asset purchases, approval of the establishment and modification of bank accounts and banking relationships, waiver of specific provisions of compliance requirements, limitation of signatory authorisation, dealing with investment portfolio / trading / operational matters and issuance of certified extracts of Board resolutions.

The members of the Board Executive Committee are:

Mark A. Watson	Chairman and Executive Director – Chief Executive Officer
Henry C. Schmeltzer	Member and Executive Director – Head of Commercial Strategy and Legal
Vincent Chatard	Member and Executive Director – Chief Business Development Officer

The Committee operated throughout the reporting period and met on an ad hoc basis when specific issues were to be considered.

Principal Management Committees

A. Executive Management Committee ("EXCO")

The EXCO takes day-to-day responsibility for the efficient operation of the Bank. In addition, the EXCO is responsible for the formulation and implementation of Board-approved strategies and plans and for ensuring that the Bank's business is operated in accordance with such strategies and plans.

The members of the EXCO include the Bank's Chief Executive Officer (Committee Chairman), Head of Commercial Strategy and Legal Affairs, Head of Treasury and Investment, Chief Business Development Officer, Chief Financial Officer, Chief Risk Officer, Head of Operations, Chief Officer – MeDirect and Head of Administration and Human Resources. The EXCO meets three times each month.

B. Management Credit Committee

The Management Credit Committee is responsible for approving credit recommendations and making other credit decisions under its delegated authority - this includes decisions on individual credits; reviewing and recommending credit to the Board; monitoring adherence to large exposure limits; considering credit hedging strategies; and recommending other concentration limits for Board approval. It also establishes transactional authority for members of the Treasury and Investment Department. In addition, the Management Credit Committee reviews provisioning and lending policies; monitors the Bank's investment portfolios and reviews Management Information reports.

The members of the Management Credit Committee include the Chief Risk Officer (Committee Chairman), the Bank's Chief Executive Officer, and Head of Treasury and Investment. The Committee meets regularly on an ad hoc basis.

Statement of Compliance with the Principles of Good Corporate Governance

Principal Management Committees (continued)

C. Asset and Liability Committee ("ALCO")

ALCO sets and reviews overall policies and objectives for asset and liability management, capital management and allocation; capital usage and efficiency; transfer pricing; risk management; and underwriting, dealing and trading activities according to the risk appetite set by the Board.

The members of ALCO include the Bank's Head of Treasury and Investment (Committee Chairman), Chief Executive Officer, Head of Treasury Operations, Chief Financial Officer and Chief Risk Officer. ALCO schedules meetings monthly but also holds additional ad hoc meetings.

D. Management Operations Committee

The Management Operations Committee considers day-to-day operating procedures of the Bank. Also the Committee follows up on the implementation of any audit agreed actions.

The members of the Management Operations Committee consist of Chief Business Development Officer, Head of Back Office and Settlements, Chief Risk Officer, Chief Financial Officer, General Counsel and Head of Compliance, Head of Risk Architecture, Head of Client Service Group, Head of IT, Head of Banking and Trading Services and Head of Administration.

The Management Operations Committee establishes, monitors and receives feedback in the form of management actions, from specifically created working groups (such as Authorisations working group, eBanking risk working group, Reconciliations working group, Physical security working group and Procedures and processes working group) as may be required in order to ensure that issues relating to operational issues are handled effectively and efficiently.

E. New Customer Products Committee

The New Customer Products Committee has been established to analyse potential new products to be offered by the Bank from a risk, operations, reputation and legal / compliance perspective. The Committee provides its recommendations to the Executive Management Committee including the appropriate policies, procedures and controls that should be adopted in relation to any such new product.

The members of the New Customer Products Committee are the Chief Business Development Officer, Head of Project Management, Head of Client Service Group, Head of Treasury and Investment, Chief Risk Officer, Head of Risk Architecture, Chief Financial Officer, Head of Operations, Head of Back Office and Settlements, Head of Middle Office Operations, Head of Quality Control, General Counsel and Head of Compliance, Head of IT and Head of Business Administration.

Statement of Compliance with the Principles of Good Corporate Governance

Principal Management committees (continued)

F. Treasury Services Committee

The Treasury Services Committee has been established to analyse potential new treasury management products to be used by the Treasury department for liquidity, credit and market risk management from a risk, operations and legal / compliance perspective.

The members are Head of Treasury and Investment, Chief Business Development Officer, Head of Back Office and Settlements, Head of Operations, Chief Officer – MeDirect, Head of Risk Architecture, General Counsel and Head of Compliance, Head of Banking and Trading Services, Head of Project Management and Head of Middle Office Operations.

Code Provision 4.2.7 - Succession Planning

The Bank has established a list of Key Personnel Substitutes to cover instances in which executive directors or other key personnel are temporarily incapacitated or otherwise unable to complete their duties for a significant period of time.

If such directors or key personnel are permanently unable to re-assume their duties, the Bank's management, in consultation with the Board, will designate permanent successors, either from the Bank's existing management team or, if appropriate, by selecting an outside candidate.

Principle 6: Information and professional development

In addition to the responsibilities of the Board previously listed, in line with Principle 6, the Board actively participates in the appointment of senior management. Board members receive regular updates on the Bank's strategic, operational, corporate governance, compliance, risk management and financial plans and objectives.

Principle 7: Evaluation of the Board's performance

On an annual basis, the Board carries out an evaluation procedure whereby Board members are requested to complete a questionnaire of the Board's performance and that of its committees. The evaluation is co-ordinated by the Board's Chairman, a non-executive director and all directors participate in the process as a sub-committee of the Board. Feedback from the evaluation is presented to the Board for analysis.

Principles 9 and 10: Relations with Shareholders and with the market and institutional Shareholders

Through public announcements, the Bank's website, financial reports and interaction with the general media in Malta, the Bank provides the market with regular, timely, accurate, comprehensive and comparable information in sufficient detail to enable investors to make informed investment decisions in respect of the Bank's listed securities**.**

The Bank's controlling institutional shareholder is represented on its Board of directors and actively monitors its investment in the Bank.

Statement of Compliance with the Principles of Good Corporate Governance

Principle 11: Conflicts of interest

The Bank's Articles of Association provide that any director who is in any way, whether directly or indirectly, interested in a transaction or proposed transaction with the Bank must (i) declare to the other directors the nature of such interest, (ii) not participate in or be present for any discussion relative to any such transaction or proposed transaction, and (iii) not vote in respect of any such transaction or proposed transaction.

On joining the Board and regularly thereafter, directors are informed and reminded of their obligations in respect of dealing in securities of the Bank within the parameters of law and the Listing Rules.

Principle 12: Corporate social responsibility

During the year ended 31 March 2014, Mediterranean Bank proudly continued to support and promote Maltese sportive, cultural, and charitable causes and events. The Bank's commitment to these initiatives was once again established through the various sponsorships and donation agreements that support a wide variety of community organisations.

Sports

Mediterranean Bank's patronage of the sporting community was further strengthened with a number of donations to sporting associations and events. The Bank's significant support of the Malta Rugby Football Union (MRFU) has assisted the MRFU to further its ambitions at both an international level as well as at a local level, where the game's popularity continues to rapidly grow. As from February 2012, the MRFU Cup, (local senior division league), has been renamed the Mediterranean Bank Cup.

Other sporting commitments by the Bank are visible through its support of a range of activities which, in the past year, included the Luxol Raiders Women Under-16 Football Team, the annual 10K Running Race and the Malta Optimist Dinghy Association junior races. Mediterranean Bank was also the main sponsor of the Euromed Malta Championship 2013, organised by the Malta Young Sailors Club with the cooperation of the Kunsill Malti Għall-Isport and the Mellieħa Local Council, which was held under the patronage of the Malta Sailing Federation.

Maltese Heritage

The preservation of Malta's national heritage is also important to the Bank and to this end it has supported a number of organisations and initiatives. These include Vitimalta, the largest grape producer organisation on the Maltese Islands. The Bank has also donated towards the Fondazzjoni Xandir Reliġjuż, the Alive Charity Foundation to raise funds for medical research in Malta, St Georges' Basilica and the Valletta Local Council Christmas lights. The Bank also sponsored the printing of the Maltese version of the publication J.F. Kennedy by E. Attard.

Statement of Compliance with the Principles of Good Corporate Governance

Principle 12: Corporate social responsibility (continued)

Performing and Visual Arts

As part of the Bank's on-going corporate social responsibility programme and commitment, it also continues to support and promote the performing and visual arts. In line with this commitment, the Bank is once again the main benefactor of the Manoel Theatre for the coming season of 2014. It also sponsored the 2013 Toi Toi Pantomine for Orphans show. Art that Matters is an art competition organised by the Bank for upcoming artists which was launched at MCAST and executed in collaboration with a prominent gallery.

In January 2014, the Bank once again confirmed its position as main sponsor for the Malta Eurovision Song Festival 2014 which took place the following month in February.

Youth

The Bank has also sponsored a number of youth events and organisations, among them the Salesians Brigade book fair, the Santa Tereża College for Boys excursion, the National Blood Transfusion Centre, and the Maidenstone Singers.

The Bank has also made generous donations towards the LadyBird Foundation through its Christmas campaign where a donation was made against every account opened during the month of December. The Bank also presented a donation to the President's Community Chest Fund Campaign in Istrina.

Listing Rules

At each meeting, the Audit Committee receives notices of and approves all related party transactions and balances.

Other Disclosures

Licence and hosting agreement

On 1 September 2011, the Bank entered into a computer software licence and maintenance agreement with Intelligent Environments Europe Ltd ("IE"), pursuant to which IE licensed to the Bank in perpetuity its Netfinance e-banking application and related software and to provide maintenance services in respect of such applications.

On 24 October 2011, the Bank entered into a hosting services agreement with IE, pursuant to which IE agreed to host the Bank's website and related back end connectors.

Licence and hosting agreement

On 9 December 2011, the Bank entered into a computer software licence and hosting agreement with MBA Systems Limited ("MBA"), pursuant to which MBA licensed to the Bank for use in Malta its Internet Broker IB.Net application and related software and to provide maintenance and hosting services in respect of such applications.

On 19 March 2013, the Bank entered into a further contract with MBA extending the licence and hosting agreement to the Bank's Belgian operations and extending both contracts to 26 November 2015.

Other Disclosures (continued)

Professional services agreement and software licence agreement

On 10 August 2010, Infosys Technologies Limited ("Infosys") and the Bank entered into agreements pursuant to which Infosys (a) granted the Bank a perpetual, irrevocable, non-exclusive, non-transferable, limited licence to use its proprietary software Finacle (a banking software product) in accordance with the terms of the software licence agreement and to provide maintenance services in relation thereto; and (b) agreed to provide the Bank with professional services in relation to the installation, customisation, development, parameterisation, training, testing and implementation of the licensed software, subject to the terms and conditions contained in the said agreement.

Effective 30 November 2011, the Bank's contracts with Infosys were assigned to its affiliate, Medifin Leasing Limited.

Software licence agreement

On 14 August 2009, SunGard Front Arena AB ("SunGard") and the Bank entered into an agreement pursuant to which SunGard provided a personal, non-transferable, non-exclusive, limited-scope, term licence in favour of the Bank, subject to the payment of a licence fee, yearly support fees, as well as professional services fees, expense reimbursements and taxes, all as specified in the agreement. The licence provided to the Bank relates to the Front Arena trading and risk management system under which the Bank can enter and execute new trades, manage asset and liability risk and perform risk and portfolio management.

Consulting and information services

On 1 June 2011, the Bank entered into an agreement with Morningstar Associates Europe Limited ("Morningstar") whereby Morningstar provides consulting services to the Bank in respect of the Bank's wealth management and portfolio planning services. The initial term of the agreement is three years.

On 1 June 2011, the Bank entered into an agreement with Morningstar UK Ltd. to license certain Morningstar analytical tools for use by the Bank in Malta.

On 30 March 2012, the Bank entered into agreements with Morningstar UK Ltd. to license the Morningstar Document Library and certain Morningstar Data Packages.

On 21 May 2012, the Bank entered into an agreement with Morningstar UK Ltd. to license certain Morningstar data feed information for use by the Bank in Malta.

Asset administration agreement

On 25 June 2013, the Bank entered into an asset administration agreement with Virtus Group LP, pursuant to which Virtus Group LP performs certain administrative and other functions relating to its proprietary loan portfolio and other vehicles as requested.

Statement of Compliance with the Principles of Good Corporate Governance

Management's internal controls over financial reporting

The Board is responsible for ensuring that the Bank's senior management develops and implements a sound system of internal controls and for reviewing its effectiveness. Such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can only provide reasonable and not absolute, assurance against material misstatement or loss. The Bank operates a system of internal control which provides reasonable assurance of effective and efficient operations covering all controls, including financial and operational controls and compliance with laws and regulations. Processes are in place for identifying, evaluating and managing the significant risks facing the Bank.

The management of the Bank is responsible for instituting and preserving sufficient internal control over financial reporting. Internal control over financial reporting is a process designed under the supervision of the Chief Financial Officer to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union.

Internal control over financial reporting includes policies and procedures that pertain:

- to maintaining records that, in reasonable detail, accurately and fairly reflect transactions and dispositions of assets;
- to providing reasonable assurances that transactions are recorded as necessary to permit preparation of financial statements in accordance with IFRS;
- to ensuring that receipts and expenditures are made only in accordance with authorisations of management and the respective directors; and
- to providing reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use or disposition of assets that could have a material effect on the financial statements.

Francis J. Vassallo
Chairman

Mark A. Watson
Director and Chief Executive Officer

28 May 2014

Directors' Report

For the year ended 31 March 2014

The directors present their annual report, together with the financial statements of Mediterranean Bank plc (the "Bank") for the year ended 31 March 2014. This report is prepared in terms of the Companies Act, 1995 (Chapter 386, Laws of Malta) and complies with the disclosure requirements of the Sixth Schedule to the same Act.

Board of Directors

In accordance with the Bank's Articles of Association, during the Annual General Meeting to be held on 28 May 2014, all the directors serving at that time will retire and may offer themselves for reappointment.

The directors of the Bank who held office throughout the year ended 31 March 2014 were:

Mr Francis J. Vassallo - Chairman
Mr Mark A. Watson - Chief Executive Officer
Mr Peter B. Cartwright *(Resigned 26 February 2014)*
Mr Benjamin Hollowood *(Appointed 30 May 2013)*
Mr Finlay S. McFadyen
Mr Henry C. Schmeltzer
Mr Joaquin Vicent
Mr Vincent Chatard

Presentational changes in Financial Statements

One of the Bank's two subsidiaries, Mediterranean Global Advisory SA, was liquidated during the year ended 31 March 2014.

The operations of the Bank's other subsidiary, Mediterranean Research Limited, and Medifin Estates, a property leasing partnership established on 5 June 2012, are deemed to be insignificant and, consequently, only the financial statements of the Bank are presented.

Principal activities

The principal activities of the Bank are to provide market leading banking services primarily to the mass affluent sector, focusing primarily on savings, wealth management, investments and corporate banking.

The Bank was granted a licence by the Malta Financial Services Authority ("MFSA") in terms of the Banking Act, Chapter 371 of the laws of Malta, on 14 July 2005. The Bank is licensed amongst other things, to carry out the business of banking, to undertake money transmission services, to issue and administer means of payment, to issue guarantees and commitments, to trade on own account and / or for the account of customers in a number of instruments, to provide portfolio management and advice and to provide safe keeping services. The Bank also holds a Category 2 licence and a Category 4 licence issued by the MFSA which authorise the Bank to provide investment services, to hold or control customers' money and to act as trustee or custodian of collective investment schemes.

Profitability has been achieved through the creation of a diversified investment portfolio comprising a treasury book consisting of high quality, liquid securities, including senior financial instruments, bank covered bonds, public sector bonds and mortgage bonds and a corporate lending portfolio consisting primarily of senior secured loans and bonds. The corporate lending portfolio largely consists of Western European credits and all loans and bonds in the portfolio are denominated in euro or pounds sterling. All of the loans are floating rate instruments and do not bear material interest rate risk.

Directors' Report

For the year ended 31 March 2014

Principal activities (continued)

The Bank's principal customer focus is on savings, investments and wealth management products. The principal customer-related activities of the Bank include the following:

- The provision of term savings and wealth management products;
- The receipt and acceptance of customers' monies for deposit in savings and fixed term deposit accounts denominated in euro and other major currencies;
- Trading for the account of customers in foreign exchange;
- The provision of money transmission services;
- The provision of safe custody services with a wide range of custom-tailored solutions as well as administration and safekeeping of securities;
- The provision of investment advice to customers of the Bank; and
- The provision of senior secured loans.

Review of business development and financial position

During the financial year ended 31 March 2014, the Bank continued to implement its business plan with the aim of sustaining the Bank's long-term profitability by building its customer base in the mass affluent market both in Malta and Belgium and also through a selected corporate sector in Malta. The Bank intends to continue to improve its banking, investment and wealth management services in Malta and internationally.

During the year, the Bank continued to make significant investment in technology that have allowed it to introduce new online banking and investment services, together with systems to support such services. The Bank has implemented (i) an e-banking system that enables the Bank's customers to execute banking transactions online and (ii) an e-brokerage system that enables the Bank's wealth management customers to execute online brokerage transactions in respect of equities, bonds and funds. The Bank offers online goal planning, research and market data as well as analytical tools and capabilities for customers through its wealth management platform.

The Bank's Total Operating Income for the year ended 31 March 2014 was €63.815 million (2013: €54.252 million). This was driven through the Bank's treasury operations and its corporate credit investment portfolio which, combined with its low cost base and excellent customer service, have enabled the Bank to position itself as a market leading provider of savings and term deposit products, primarily in the Maltese market.

The Bank recorded a Profit after Tax for year ended 31 March 2014 of €19.396 million (2013: €20.483 million).

As of 31 March 2014, the Bank's Investment Portfolio stood at €1.478 billion (2013: €1.564 billion) consisting of Held-to-Maturity securities amounting to €984 million (2013: €357 million) net of collective impairment loss of €0.463 million (2013: nil), available-for-sale ("AFS") securities amounting to €492 million (2013: €1,207 million) and other equity instruments at fair value through profit or loss amounting to €2,474 thousand (2013: nil). The fair value of the AFS book was risk managed through interest rate derivatives such as interest rate swaps where the hedge accounting methodology under IAS 39 was adopted. A collective impairment loss allowance of €0.5 million (2013: nil) was accounted for.

The Bank's Corporate Loan portfolio stood at €571.1 million (2013: €402.2 million) as of 31 March 2014, net of collective impairment loss allowances of €0.872 million (2013: €0.676 million) and specific impairment loss allowances of €1.422 million (2013: nil).

Directors' Report

For the year ended 31 March 2014

Review of business development and financial position (continued)

In August 2013, the Bank launched its Belgian branch, which initially offered deposit and investment products including online execution of transactions in equities, bonds and funds. During September 2013, the Bank launched its eWealth platform in the Belgian market, including its suite of financial planning tools and its wide range of research and investment capabilities.

As part of its funding strategy, on 6 June 2013, the Bank issued €240 million Senior Secured Floating Rate notes maturing by 2026, through a fund structure situated in the Netherlands. During July 2013, the Bank repurchased €22 million of such Senior Secured Floating Rate notes.

During June 2013, the Bank issued an additional euro equivalent of €10 million of 7.50% Subordinated bonds due 2019, which during December 2013 were merged with the euro equivalent of €12.5 million bonds that were originally issued on 21 November 2012.

During the year, the Bank bought back a further €1.4 million (2013: €4.1 million) nominal value of its 6.25% Bonds due 2015 through market operations.

The final dividend for the year ended 31 March 2013 was in the form of a €21,000,000 bonus ordinary share issue that was executed on 10 May 2013.

On 28 June 2013 a shareholders' contribution of €1,250,000 was received.

As at 30 October 2013, the Bank's issued share capital was increased by €4,900,000 ordinary A shares and by a further €9,800,000 ordinary A shares on 28 November 2013.

Shareholders' equity at the reporting date amounted to €135.160 million (2013: €115.083 million).

The average number of employees increased from 163 for the year ended 31 March 2013 to 224 for the year ended 31 March 2014. Personnel expenses for the year ended 31 March 2014 amounted to €13.8 million (2013: €11.2 million). The number of employees increased from 194 as at 31 March 2013 to 227 as 31 March 2014.

Strategic development

The Bank's primary strategic objective is to be a leading provider of savings, investment and wealth management products to the mass affluent market, both in Malta and other European Union countries.

Having established its position in the Maltese market initially through its core savings offering, the Bank has invested considerable resources in building an investment services and eWealth Management platform, which provides the Bank's customers with an information rich and cost efficient platform to deliver investment and savings products in a seamless, transparent and user friendly format. The platform allows the Bank to offer its products and services in both the local and international markets. The underlying strategy is designed to meet the long-term savings and investment requirements of its core customer base. The Bank's online investment services platform provides investors with the ability to execute transactions in equities, bonds and funds in a cost efficient and easy to use manner. The Bank's eWealth platform provides customers with a large range of investment research and analysis tools as well as financial planning tools that enable its customers to build portfolios designed to meet their financial goals.

Directors' Report

For the year ended 31 March 2014

Strategic development (continued)

In addition to its efforts in respect of improving and diversifying its customer offering, the Bank continues to diversify its liability structure, while continuing to strengthen its deposit base. The Bank's core deposit offering is a range of attractively priced fixed-term and other savings products. As at 31 March 2014, the Bank's deposit base reached €777 million.

The Bank also continues to access the international wholesale funding markets through bilateral repo lines, access to the Eurex repo platform and a secured 3-year term funding facility with an international counterparty. In addition, as noted above, to support the growth of its lending activities, the Bank issued €240 million of secured notes through a Netherlands funding vehicle.

Supported by a robust liability structure, the asset base of the Bank has continued to grow, having reached €2.2 billion as at 31 March 2014. This growth has been concentrated primarily in the Bank's portfolio of international senior secured corporate loans and bonds, which have been an increasingly important portion of the Bank's asset portfolio. The Bank also continues to focus on its treasury portfolio and its traditional strategy of investing in quality and liquid EU assets.

Mediterranean Bank plc remains committed to operating with strong regulatory ratios and a robust liquidity position. At 31 March 2014 the Bank's regulatory liquidity ratio stood at 148.7%, and it reported a Capital Adequacy Ratio of 14.25%. The growth of the Bank's corporate loan portfolio has resulted, and is expected to continue to result, in greater consumption of capital over the medium term. As a result, it is expected that the Bank will continue to operate at or around its current Capital Adequacy Ratios rather than the higher ratios that have historically been the case. The Bank intends always to operate at Capital Adequacy Ratios that are comfortably in excess of regulatory requirements. Likewise, the Bank's regulatory liquidity ratio is also expected to remain comfortably in excess of regulatory requirements.

Dividends and reserves

No interim dividends were paid during year (2013: €7.146 million). A final dividend of €19.400 million (2013: €21.000 million) equivalent to 20 cents per ordinary share is proposed for approval at the annual general meeting.

Retained earnings as at 31 March 2014 amounted to €19.496 million (2013: €21.191 million).

Standard licence conditions and regulatory sanctions

In accordance with the Investment Services Rules for Investment Services providers regulated by the MFSA, licence holders are required to include in the Directors' Report breaches of standard licence conditions or other regulatory requirements. Accordingly, the directors confirm that no breaches of standard licence conditions or other breach of regulatory requirements were reported which were subject to administrative penalty or regulatory sanction.

Directors' Report

For the year ended 31 March 2014

Outlook and future business developments

The two most significant events that have an immediate impact on the Bank's future outlook and future developments are noted below.

During the third quarter of 2013, the Bank launched its Belgian branch. Based on its investments and capabilities developed within the Maltese Market, the Bank has established a highly competitive online offering for the Belgian market. The Belgian branch is primarily operated from an efficient operating base enabling the delivery of competitive savings and wealth management products to the Belgian market in a cost effective, transparent and customer friendly manner.

As detailed in the "Events after the reporting date" section, during April 2014 the Bank entered into an agreement with VB-Holding Aktiengesellschaft and Mithra Holding Gesellschaft m.b.H. to acquire 100% of the share capital of Volksbank Malta Limited ("VBM") for cash consideration of €35,300,000. The Bank has also agreed to refinance existing debt of VBM to Österreichischen Volksbanken AG, as of the closing date. The purchase is expected to be completed in the coming weeks, subject to receipt of required approvals from relevant governmental and regulatory authorities. The purchase of VBM will consolidate and expedite the Bank's Maltese growth strategy through VBM's portfolio of Maltese clients which is complementary to the Bank's existing customer base and aligned with its future growth strategies.

These two significant corporate developments enable the Board to look forward to the coming year with cautious optimism.

The on-going robustness of capital and liquidity ratios provide a stable foundation from which to produce attractive and sustainable returns. The strategy that has been defined by the Board over the last few years has resulted in significant growth whilst producing attractive returns and an ability to invest in the capabilities of the Bank.

Related parties

During the year ended 31 March 2014, other than the transactions described under note 35 to the financial statements, there were no material changes in related party transactions as compared with those detailed within the financial statements for the year ended 31 March 2013. During this financial year, no related party transactions materially affected the financial position or performance of the Bank, with the exception of dividend payment, increase in share capital and shareholders' contribution, as described in note 26.

Directors' Report

For the year ended 31 March 2014

Events after the reporting date

As previously described above, €19.4 million is proposed for distribution from the retained earnings as a final dividend by way of a bonus share issue. This will transfer substantially all retained earnings as bonus shares.

On 11 April 2014 the Bank entered into an agreement to acquire 100% of the share capital of Volksbank Malta Limited ("Volksbank") for cash consideration of €35.3 million. The Bank expects that the purchase of Volksbank will consolidate and expedite its Maltese growth strategy through Volksbank's portfolio of Maltese customers which is complementary to the Bank's existing client base and aligned with the Bank's future growth strategy.

On 2 May 2014, Mediterranean Research Limited, a dormant subsidiary wholly owned by the Bank, was liquidated.

Subsequent to year end, the Bank bought back a further €71,500 nominal value of its 6.25% Bonds due 2015 through market operations.

There were no other events after the reporting date that would have a material effect on the financial statements.

Going concern

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

Auditors

A resolution to re-appoint KPMG as auditors of the Bank will be proposed at the forthcoming annual general meeting.

Directors' Report
For the year ended 31 March 2014

Statement by the directors pursuant to Listing Rule 5.68

We, the undersigned, declare that to the best of our knowledge, the financial statements were 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 that this report includes a fair review of the performance of the business and the position of the Bank, together with a description of the principal risks and uncertainties that it faces.

Approved by the Board of directors on 28 May 2014 and signed on its behalf by:

Francis J. Vassallo
Chairman

Mark A. Watson
Director and Chief Executive Officer

Registered Office
10, St. Barbara Bastion,
Valletta, VLT 1961
Malta

Directors' Responsibility for the Financial Statements

The Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act") requires the directors of Mediterranean Bank plc (the "Bank") to prepare financial statements for each financial year which give a true and fair view of the financial position of the Bank as at the end of the financial year and of the profit or loss of the Bank for that year in accordance with the requirements of International Financial Reporting Standards as adopted by the European Union.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy, at any time, the financial position of the Bank and to enable them to ensure that the financial statements have been properly prepared in accordance with the provisions of the Act and the Banking Act, 1994.

The directors are also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors, through oversight of management, are responsible for ensuring that the Bank establishes and maintains internal control to provide reasonable assurance with regard to reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Management is responsible, with oversight from the directors, to establish a control environment and to maintain policies and procedures to assist in achieving the objective of ensuring, as far as possible, the orderly and efficient conduct of the Bank's business. This responsibility includes establishing and maintaining controls pertaining to the Bank's objective of preparing financial statements as required by the Act and managing risks that may give rise to material misstatements in those financial statements. In determining which controls should be implemented to prevent and detect fraud, management considers the risks that the financial statements may be materially misstated as a result of fraud.

Signed on behalf of the Board of directors by:

Francis J. Vassallo
Chairman

Mark A. Watson
Director and Chief Executive Officer

28 May 2014

Remuneration Report

Remuneration governance

The primary purpose of the Nomination and Remuneration Committee ("NRC") is to review remuneration levels in the Bank and to consider whether to approve performance-related bonus awards and long-term incentive plan awards.

The NRC receives recommendations from the management of the Bank regarding remuneration levels and the awarding of bonuses. It may request market-related information from time to time to verify the recommendations made by management.

One of the NRC's primary functions is to ensure that the Bank is able to attract and retain suitable employees at all levels at an acceptable cost.

Membership and meetings

The members of the NRC are:

Finlay S. McFadyen	Committee Chairman and Independent Non-Executive Director
Francis J. Vassallo	Independent Non-Executive Director (Chairman of the Board)
Peter B. Cartwright	Non-Executive Director (resigned 26 February 2014)
Benjamin Hollowood	Non-Executive Director (appointed 26 February 2014)

During the year ended 31 March 2014, the NRC met once and this meeting was attended by all members of the NRC.

Remuneration policy statement

The Board is responsible for ensuring that this statement and its contents adhere to all laws, rules and regulations issued by the Malta Financial Services Authority. The Board, directly and through the NRC, carries out effective monitoring and evaluation of the Bank's remuneration system on an on-going basis. The NRC and the Board monitor the on-going performance by management of its supervisory function in respect of design and implementation of a remuneration system.

The NRC is charged with aligning the Bank's remuneration policy and in particular performance-related elements of remuneration, with the best interests of the stakeholders and with the Bank's business strategy and risk tolerance, objectives, values and long-term interests.

Remuneration consists of base salary and, where applicable, performance based bonus awards. Performance-related compensation shall be determined both on (i) a bank wide basis, and (ii) an individual employee basis.

Compliance with the Bank's rules and requirements and involvement on a continuing basis in risk management are taken into account when determining performance-based remuneration for all employees. Other non-financial factors shall also be considered such as skills acquired, personal development, commitment to the Bank's business strategies and policies and contribution to the performance of the team. Performance shall be measured in relation to non-financial and financial goals and, where appropriate, failure to perform in non-financial areas of responsibility shall outweigh success in profit generation in determining compensation. Control functions shall be adequately rewarded in order to ensure that the Bank is able to attract skilled individuals for such roles.

The Bank's remuneration policy has not been changed since its adoption in March 2011. The Bank has no present intention to effect changes in its remuneration policy during the following financial year.

Remuneration Report

(a) Measures of performance as basis for awarding of pay

Base pay is expected to comprise the majority of the Bank's overall compensation cost.

i. All staff

The NRC considers a variety of factors in determining compensation tailored to the role of the individual concerned and takes into account factors such as risk management, development of systems, monitoring of risk and creation of long-term value for the Bank.

ii. Members of management and control functions

Recommendations by management as to remuneration of members of control functions are made by the Chief Executive Officer. Such recommendations are reviewed and approved or rejected by the NRC.

Compensation for employees serving in control functions takes into account broadly based performance measurements, including evaluation of achievements in respect of control function responsibilities. Control function employees are compensated in accordance with their own performance and not in accordance with the performance of the business units they control.

Senior members of management may be eligible to participate in the Bank's Long-term Incentive Plan, enabling such managers to participate in the long-term profitability of the Bank. In addition, the Bank has established an employee benefit trust enabling employees other than senior members of management to participate in this incentive.

iii. Non-executive directors

The remuneration of non-executive directors is not performance based and is not linked to the Bank's short term results. It is determined based on remuneration levels for directors of similar financial companies and takes into account factors such as time invested and responsibilities.

(b) Measures of performance as basis for awarding of bonuses

A bonus pool is established for the Bank as a whole and is calculated at Bank level based on the success of the Bank in meeting its business objectives. These objectives relate, amongst other things, to profitability, sustainability of performance, risk management, building of business lines and creation of long-term shareholder value.

Individuals are compensated out of that bonus pool based on their contribution to the achievement of the Bank's business objectives. Such individual criteria depend on the role of the individual in the Bank.

Control functions are judged on success in developing appropriate policies, developing effective risk management controls and procedures, monitoring risk and building control systems. Whilst the general bonus pool of the Bank will be based on the Bank's financial results, compensation of control functions is not directly tied to the results of any business unit.

Staff savings account

All of the Malta-based Bank's employees are entitled to make monthly deposits of specified amounts direct from after tax payroll into an employee savings account. At the end of each calendar year, the Bank will pay 5% interest on the accumulated savings remaining in the account in December. On such date, amounts remaining in such savings accounts may be withdrawn and the terms of such accounts may be reset.

Remuneration Report

Long-term incentive plan ("LTIP")

The Bank's immediate parent company has established a LTIP for the benefit of senior management and other employees of the Bank. The LTIP enables senior managers and other employees to participate in the long-term value and profitability of the Bank.

Remuneration policy – directors

Based on the recommendations of the NRC, the directors' fees earned by two of the non-executive directors for the year ended 31 March 2014 amounted to €110,012.

Total emoluments earned by four executive directors of the Bank during the year ended 31 March 2014, are reported below:

	€	%
Fixed remuneration	1,057,560	48%
Variable remuneration	945,000	43%
Shares	None	-
Non-cash benefits	190,258	9%
	2,192,818	100%

Non-Cash benefits relate to the gross rent payable on accommodation based in Malta and health and life insurance premiums paid by the Bank on behalf of the directors.

Employment contracts - executive directors

All the executive directors as of 31 March 2014 were engaged under indefinite employment contracts.

Remuneration policy – senior management

Total emoluments received by seven senior management (excluding directors), during the year ended, are reported below:

	€	%
Fixed remuneration	1,074,631	62%
Variable remuneration	623,881	36%
Shares	None	-
Non-cash benefits	27,772	2%
	1,726,284	100%

Non-Cash benefits relate to health and life insurance premiums paid by the Bank on behalf of its senior management.

Remuneration Report

Termination payments

During the year ended 31 March 2014, there were no new sign-on and severance payments made either to directors or members of senior management.

Francis J. Vassallo
Chairman

Mark A. Watson
Director and Chief Executive Officer

28 May 2014

Statement of Financial Position
As at 31 March 2014

	Notes	2014 €000	2013 €000
ASSETS			
Balances with Central Bank of Malta, treasury bills and cash	14	**18,091**	70,055
Loans and advances to financial institutions	15	**87,714**	20,131
Loans and advances to customers	16	**571,144**	402,174
Investments			
- Corporate	17	**293,235**	54,964
- Treasury	17	**1,184,705**	1,509,070
Derivative assets held for risk management	18	**404**	1,152
Derivative assets held for trading	19	**404**	-
Investment in subsidiaries	20	**1**	65
Property and equipment	21	**1,908**	2,485
Intangible assets	22	**128**	228
Other assets	23	**18,889**	13,598
Prepayments and accrued income	24	**23,261**	27,996
Deferred tax assets	25	**3,764**	-
Total assets		**2,203,648**	2,101,918

Statement of Financial Position
As at 31 March 2014

	Notes	2014 €000	2013 €000
EQUITY			
Share capital	26	**98,050**	62,350
Share premium	26	**13,464**	13,464
Shareholders' contribution	26	**9,750**	8,500
Reserve for general banking risks	26	**91**	-
Retained earnings	26	**19,496**	21,191
Fair value reserve	26	**(5,691)**	9,578
Total equity		**135,160**	115,083
LIABILITIES			
Amounts owed to financial institutions	27	**1,008,976**	1,368,995
Amounts owed to customers	28	**776,715**	566,047
Debt securities in issue	29	**230,127**	15,664
Derivative liabilities held for risk management	18	**2,973**	-
Subordinated liabilities	30	**22,385**	12,341
Current tax		**10,794**	7,660
Other liabilities	31	**1,109**	1,100
Accruals	32	**15,409**	9,966
Deferred tax liability	25	**-**	5,062
Total liabilities		**2,068,488**	1,986,835
Total equity and liabilities		**2,203,648**	2,101,918
Contingent assets	16/17	**27,700**	76,000
Contingencies and commitments	16/34	**4,430**	13,285

The notes on pages 30 to 119 are an integral part of these financial statements.

The financial statements on pages 24 to 119 were approved and authorised for issue by the Board of directors on 28 May 2014 and signed on its behalf by:

Francis J. Vassallo Chairman	Mark A. Watson Director and Chief Executive Officer	Edward Jaccarini Chief Financial Officer

Statement of Comprehensive Income
For the Year Ended 31 March 2014

	Notes	2014 €000	2013 €000
Interest income		**64,567**	50,945
Interest expense		**(33,589)**	(27,668)
Net interest income	7	**30,978**	23,277
Net fee and commission income/(expense)	8	**634**	(1,826)
Net trading income	9.1	**2,292**	1,111
Net income from other financial instruments at fair value through profit or loss	9.2	**1,883**	4,156
Other operating income	9.3	**28,028**	27,534
Total operating income		**63,815**	54,252
Net impairment	4/16/17	**(2,081)**	(676)
Administrative and other expenses	10	**(17,186)**	(9,920)
Personnel expenses	11	**(13,785)**	(11,164)
Depreciation and amortisation	21/22	**(877)**	(945)
Operating expenses		**(33,929)**	(22,705)
Profit before income tax		**29,886**	31,547
Income tax expense	12	**(10,490)**	(11,064)
Profit for the year		**19,396**	20,483
Other comprehensive income			
Items that are or may be reclassified to profit or loss			
Fair value reserve – available-for-sale assets			
Net change in fair value		**1,457**	44,505
Income taxes - Net change in fair value		**(510)**	(15,577)
Net amount transferred to profit or loss		**(24,948)**	(28,020)
Income taxes - Net amount transferred to profit or loss		**8,732**	9,807
Other comprehensive income for the year (net of tax)		**(15,269)**	10,715
Total comprehensive income for the year		**4,127**	31,198
Earnings per share (cents)	13	**22c**	36c

The notes on pages 30 to 119 are an integral part of these financial statements.

Statement of Changes in Equity
For the Year Ended 31 March 2014

	Share capital	Share premium	Shareholders' contribution	Retained earnings	Fair value reserve	Total
	€000	€000	€000	€000	€000	€000
Balance as at 1 April 2012	**56,030**	**13,464**	**-**	**7,029**	**(1,137)**	**75,386**
Total comprehensive income for the year:						
Profit for the year	-	-	-	20,483	-	20,483
Other comprehensive income for the year:						
Available-for-sale assets:						
- Net change in fair value	-	-	-	-	28,928	28,928
- Net amount transferred to profit or loss	-	-	-	-	(18,213)	(18,213)
Total comprehensive income for the year, net of tax	**-**	**-**	**-**	**20,483**	**10,715**	**31,198**
Transactions with owners, recorded directly in equity						
Contributions and distributions:						
Issue of share capital (note 26)	6,320	-	-	-	-	6,320
Shareholders' contribution (note 26)	-	-	9,325	-	-	9,325
Dividends to equity holders (note 26)	-	-	(825)	(6,321)	-	(7,146)
Total contributions and distributions	**6,320**	**-**	**8,500**	**(6,321)**	**-**	**8,499**
Balance at 31 March 2013	**62,350**	**13,464**	**8,500**	**21,191**	**9,578**	**115,083**

The notes on pages 30 to 119 are an integral part of these financial statements.

Statement of Changes in Equity
For the Year Ended 31 March 2014

	Share capital	Share premium	Shareholders' contribution	Retained earnings	Reserve for General Banking Risks	Fair value reserve	Total
	€000	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Balance as at 1 April 2013	**62,350**	**13,464**	**8,500**	**21,191**	**-**	**9,578**	**115,083**
Total comprehensive income for the year:							
Profit for the year	-	-	-	19,396	-	-	19,396
Transfer of Retained earnings to Reserve for General Banking Risks	-	-	-	(91)	91	-	-
Other comprehensive income for the year:							
Available-for-sale assets:							
- Net change in fair value	-	-	-	-	-	947	947
- Net amount transferred to profit or loss	-	-	-	-	-	(16,216)	(16,216)
Total comprehensive income for the year, net of tax	**-**	**-**	**-**	**19,305**	**91**	**(15,269)**	**4,127**
Transactions with owners, recorded directly in equity							
Contributions and distributions:							
Issue of share capital (note 26)	14,700	-	-	-	-	-	14,700
Shareholders' contribution (note 26)	-	-	1,250	-	-	-	1,250
Dividends to equity holders (note 26)	21,000	-	-	(21,000)	-	-	-
Total contributions and distributions	**35,700**	**-**	**1,250**	**(21,000)**	**-**	**-**	**15,950**
Balance at 31 March 2014	**98,050**	**13,464**	**9,750**	**19,496**	**91**	**(5,691)**	**135,160**

The notes on pages 30 to 119 are an integral part of these financial statements.

Statement of Cash Flows
For the Year Ended 31 March 2014

	Note	2014 €000	2013 €000
Cash flows from operating activities			
Interest and commission receipts		**78,759**	52,741
Interest and commission payments		**(30,256)**	(30,128)
Payments to employees and suppliers		**(29,064)**	(15,715)
Operating profit before changes in operating assets/liabilities		**19,439**	6,898
(Increase)/decrease in operating assets:			
- reserve deposits with Central Bank of Malta		**(855)**	(1,360)
- loans advanced to customers and financial institutions		**(200,665)**	(297,583)
- investments		**(670,319)**	91,657
Increase in operating liabilities:			
- amounts owed to customers and financial institutions		**290,750**	474,850
Tax paid		**(7,960)**	(4,038)
Net cash (used in)/ generated from operating activities		**(569,610)**	270,424
Cash flows from investing activities			
Acquisition of property and equipment		**(171)**	(431)
Disposal of property and equipment		**9**	-
Acquisition of intangible assets		**(34)**	-
Acquisition of available-for-sale assets		**(335,871)**	(1,170,867)
Disposal of available-for-sale assets		**1,126,144**	941,592
Acquisition of derivative assets held for risk management		**(4,851)**	(13,749)
Advances to parent		**(15)**	(200)
Advances to group companies		**(5,329)**	(2,071)
Net cash generated from/(used) in investing activities		**779,882**	(245,726)
Cash flows from financing activities			
Proceeds from the issue of share capital		**14,700**	6,320
Proceeds from shareholders' contribution		**1,250**	9,325
Proceeds from the issue of debt securities		**237,359**	-
Re-purchase of debt securities		**(22,912)**	(4,095)
Net proceeds from the issue of subordinated debt securities		**9,907**	12,341
Dividends paid		**-**	(7,143)
Net cash from financing activities		**240,304**	16,748
Net increase in cash and cash equivalents		**450,576**	41,446
Cash and cash equivalents at beginning of year		**(575,822)**	(617,268)
Cash and cash equivalents at end of year	33	**(125,246)**	(575,822)

The notes on pages 30 to 119 are an integral part of these financial statements.

Notes to the Financial Statements

For the Year Ended 31 March 2014

1 Reporting entity

Mediterranean Bank plc (the "Bank") is domiciled and incorporated in Malta. The address of the Bank's registered office is 10, St. Barbara Bastion, Valletta, VLT 1961, Malta.

The principal activities of the Bank are to provide market leading banking services primarily to the mass affluent sector, focusing primarily on savings, wealth management, investments and corporate banking.

As a result of the immateriality of the subsidiaries as noted below, the consolidated financial statements of the Group, of which the Bank is the parent, have not been prepared.

Mediterranean Global Advisory SA, a subsidiary, has been liquidated during the year ended 31 March 2014 resulting in a minimal impairment loss as disclosed in note 20.2 Mediterranean Research Limited, another subsidiary, is dormant and is placed on liquidation. The Final meeting of the member of the subsidiary for the voluntary liquidation was held on 2 May 2014. No impairment is deemed necessary.

The subsidiary, Medifin Estates, was set up to lease property and which are then leased back to the Bank. Its operations are deemed to be immaterial, having no impact on the operations of the Bank.

On 7 June 2013, the Bank established a funding structure (Grand Harbour I B.V.) to issue notes secured by identifiable assets. The Bank has retained substantially all risks and rewards of assets, liabilities and related income and expenditure, and as such, all assets, liabilities and related income and expenditure have been recognised within the Bank's financial statements (note 29.3).

2 Basis of preparation

2.1 Statement of compliance

These financial statements have been drawn up in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (the "applicable framework").

All references in these financial statements to IAS, IFRS or SIC/IFRIC interpretations refer to those adopted by the European Union. The principal accounting policies applied in the preparation of these financial statements are set out below and in the relevant notes to the financial statements.

The financial statements have also been drawn up in accordance with the provisions of the Banking Act 1994, chapter 371 of the Laws of Malta and the Companies Act 1995, chapter 386 of the Laws of Malta.

2 Basis of preparation (continued)

2.2 Basis of measurement

The financial statements have been prepared on the historical cost basis except that

- available-for-sale financial instruments are measured at fair value;
- derivative financial instruments are measured at fair value;
- recognised financial assets and financial liabilities designated as hedged items in qualifying fair value hedge relationships are adjusted for changes in fair value attributable to the risk being hedged; and
- equity financial assets are measured at fair value.

2.3 Functional and presentation currency

These financial statements are presented in euro (€), which is the Bank's functional currency. Except as otherwise indicated, financial information presented in euro has been rounded to the nearest thousand.

2.4 Use of estimates and judgements

The preparation of the financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised prospectively.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in note 5.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements and have been applied consistently by Bank.

3.1 Investment in subsidiaries

Investment in subsidiaries is accounted for in these separate financial statements of the Bank at cost less any impairment.

3 Significant accounting policies (continued)

3.2 Foreign currency

Transactions in foreign currencies are translated into the functional currency of the Bank at the spot exchange rates at the date of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between the amortised cost in the functional currency at the beginning of the year, adjusted for effective interest and payments during the year, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the year.

Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the spot exchange rate at the date on which the fair value is determined. Non-monetary items that are measured based on historical cost in a foreign currency are translated using the spot exchange rate at the date of the transaction.

3.3 Interest

Interest income and expense are recognised in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

Interest income and expense presented in the statement of comprehensive income include:

- coupon received and amortisation of discount and/or premium on:

  i. financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis;
  ii. available-for-sale investment securities calculated on an effective interest basis;

- net cash settlement on interest rate swaps designated in a fair value hedge to hedge fair value changes in available-for-sale investment securities; and

- the ineffective portion of fair value changes in the available-for-sale investment securities and qualifying hedging derivatives which are designated in fair value hedges on interest rate risk.

3 Significant accounting policies (continued)

3.4 Fees and commission

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income, including servicing fees, underwriting fees and other investment management fees are recognised as the related services are performed. Other fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

3.5 Net trading income

Net trading income consists of foreign exchange earnings.

3.6 Net income from other financial instruments at fair value through profit or loss

Net income from other financial instruments at fair value through profit or loss relates to non-trading derivatives held for risk management purposes that do not form part of qualifying hedge relationships and financial assets and liabilities designated at fair value through profit or loss. It includes all realised and unrealised fair value changes and foreign exchange derivatives.

3.7 Other operating income

Other operating income mainly comprises of realised gains on disposal of available-for-sale, held-to-maturity investments and redemptions of loans and receivables. Dividend income, which is recognised when the right to receive income is established, is reflected as a component of other operating income.

3.8 Lease payments made

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

3.9 Taxation

Tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that they relate to items recognised directly in equity or in Other Comprehensive Income.

3 Significant accounting policies (continued)

3.9 Taxation (continued)

3.9.1 Current tax

Current tax is the expected tax payable or receivable on the taxable income or loss for the period, using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous periods.

3.9.2 Deferred tax

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax assets and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

3.9.3 Tax exposure

In determining the amount of current and deferred tax, the Bank takes into account the impact of uncertain tax positions and whether additional taxes and interest may be due. This assessment relies on estimates and assumptions and may involve a series of judgements about future events. New information may become available that causes the Bank to change its judgement regarding the adequacy of existing tax liabilities; such changes to tax liabilities will impact tax expense in the period that such a determination is changed.

3 Significant accounting policies (continued)

3.10 Financial assets and financial liabilities

3.10.1 Recognition and initial recognition

The Bank initially recognises loans and advances to customers at the date of transfer of beneficial ownership. Investments and derivative assets and liabilities held for risk management are recognised on date of settlement. Amounts due to customers, debt securities and subordinated liabilities are recognised on the date which they are originated. All other financial assets and liabilities are initially recognised on the trade date at which the Bank becomes part to the contractual provisions of the instrument.

A financial asset or liability is measured initially at fair value plus or minus, in the case of instruments not classified as at fair value through profit or loss, transaction costs that are directly attributable to its acquisition of the asset or issue of the liability.

3.10.2 Classification

Financial assets

The Bank classifies its financial assets in one of the following categories:
- Loans and receivables;
- Held-to–maturity;
- Available-for-sale; or
- At fair value through profit or loss and within the category as:
  - Held-for-trading; or
  - Designated at fair value through profit or loss

See accounting policies 3.10, 3.12, 3.13, 3.14, 3.16 and 3.17.

Financial liabilities

The Bank classifies its non-derivative financial liabilities as measured at amortised cost and classifies its derivative liabilities at fair value through profit or loss.

See accounting policy 3.14, 3.16 and 3.22.

3.10.3 Derecognition

Financial assets

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial assets are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset.

3 Significant accounting policies (continued)

3.10 Financial assets and financial liabilities (continued)

3.10.3 Derecognition (continued)

Financial assets (continued)

Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability in the Statement of Financial Position. On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset transferred) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in Other Comprehensive Income, is recognised in profit or loss.

The Bank enters into transactions whereby it transfers assets recognised on its Statement of Financial Position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised. Transfers of assets with retention of all or substantially all risks and rewards include, for example, securities lending and repurchase transactions.

When assets are sold to a third party with a concurrent total return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to repurchase transactions as the Bank retains all or substantially all the risks and rewards of ownership of such assets.

Similarly, when assets are sold to a funding structure in which the Bank is deemed to have retained all, or substantially all, risks and rewards, the transferred assets are not derecognised.

Financial liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

3.10.4 Offsetting

Financial assets and liabilities are offset and the net amount presented in the Statement of Financial Position when and only when, the Bank has a legal right to set off the recognised amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRSs, or for gains and losses arising from a group of similar transactions.

3 Significant accounting policies (continued)

3.10 Financial assets and financial liabilities (continued)

3.10.5 Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

3.10.6 Fair value measurement (applicable from 1 April 2013)

'Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an on-going basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at a bid price and liabilities and short positions at an ask price.

3 Significant accounting policies (continued)

3.10 Financial assets and financial liabilities (continued)

3.10.6 Fair value measurement (applicable from 1 April 2013) (continued)

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

3.10.7 Identification and measurement of impairment of financial assets, including forbearance

At each reporting date the Bank assesses whether there is objective evidence that financial assets are impaired. A financial asset or a group of financial assets is/are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s) and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a Bank of assets such as adverse changes in the payment status of borrowers or issuers in the Bank, or economic conditions that correlate with defaults in the Bank.

The Bank considers evidence of impairment for assets not measured at fair value through profit or loss at both a specific asset and collective level. All individually significant loans and advances and investment securities are assessed for specific impairment. All individually significant assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are collectively assessed for impairment by grouping together loans and advances with similar risk characteristics.

In assessing collective impairment on these financial assets, the Bank uses published historical default rates relative to the credit quality of the issuer and the duration of the instrument, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical default rates.

The Bank evaluates whether a loss event, including financial difficulties, has an impact on the estimated future cash flows of the financial asset. Accordingly, future estimated cash flows may need to be reduced or delayed, normally implying a decrease of their estimated present value and thus giving rise to an impairment loss which must be recognised.

3 Significant accounting policies (continued)

3.10 Financial assets and financial liabilities (continued)

3.10.7 Identification and measurement of impairment of financial assets, including forbearance (continued)

The Bank measures the amount of the impairment loss 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 original effective interest rate (i.e. the effective interest rate before modification of the terms of the contract).

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised. If the cash flows of the renegotiated asset are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and the new financial asset is recognised at fair value. The impairment loss before an expected restructuring is measured as follows:

- If the expected restructuring will not result in derecognition of the existing asset, then the estimated cash flows arising from the modified financial asset are included in the measurement of the existing asset based on their expected timing and amounts discounted at the original effective interest rate of the existing financial asset.

- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Impairment losses on available-for-sale investment securities are recognised by transferring the cumulative loss that has been recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation and the current fair value, less any impairment loss previously recognised in profit or loss.

If, in a subsequent period, the fair value of an impaired available-for-sale investment security 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, otherwise any increase in fair value should be recognised through Other Comprehensive Income.

Loans that have been identified as forborne retain this designation until payment performance has been observed for an extended period of time.

3 Significant accounting policies (continued)

3.10 Financial assets and financial liabilities (continued)

3.10.7 Identification and measurement of impairment of financial assets, including forbearance (continued)

Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and advances and investment securities as appropriate. Interest on impaired assets continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

The Bank writes-off loans and advances and investment securities when these are determined to be uncollectible (see note 4).

3.10.8 Sale of a financial asset with a total return swap

The Bank sells financial assets that are subject to a concurrent total return swap. In all cases, the Bank retains substantially all the risks and rewards of ownership. Therefore, the Bank continues to recognise the transferred assets in its Statement of Financial Position. The cash received is recognised as a financial asset and a corresponding liability is recognised. The Bank does not separately recognise the total return swap that prevents derecognition of the assets as a derivative because doing so would result in recognising the same rights and obligations twice. Because the Bank sells the contractual rights to the cash flows of the assets it does not have the ability to use the transferred assets during the term of the arrangement.

3.10.9 Designation at fair value through profit or loss

The Bank has designated financial assets and financial liabilities at fair value through profit or loss in either of the following circumstances:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis; or
- the designation eliminates or significantly reduces an accounting mismatch that would otherwise arise.

A description of the basis for each designation is set out in the note for the relevant asset or liability class.

3.11 Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets, including treasury bills, with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value and are used by the Bank in the management of its short-term commitments.

Cash and cash equivalents are measured at amortised cost in the Statement of Financial Position.

3 Significant accounting policies (continued)

3.12 Loans and advances to customers

Loans and advances to customers are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term.

Loans and advances to customers, that are not acquired through a syndicate lending arrangements, are accounted for on acquired date and are initially measured at fair value plus incremental direct transaction costs and subsequently measured at their amortised cost using the effective interest method.

Syndicated loans and advances are accounted for on the acquired date, being the date of transfer of beneficial ownership.

3.13 Investment securities

The Bank's investment securities primarily represent assets classified as held-to-maturity and available-for-sale.

3.13.1 Held-to-maturity

Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity and which are not designated as fair value through profit or loss or as available-for-sale.

Held-to-maturity investments are measured at amortised cost using the effective interest method. A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale and would prevent the Bank from classifying investment securities as held-to-maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not trigger a reclassification:

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;
- sales or reclassifications after the Bank has collected substantially all of the asset's original principal; and
- sales or reclassifications attributable to non-recurring isolated events beyond the Bank's control that could not have been reasonably anticipated.

3 Significant accounting policies (continued)

3.13 Investment securities (continued)

3.13.2 Available-for-sale

Available-for-sale investments are non-derivative investments that are designated as available for sale or are not classified as another category of financial assets. Available-for-sale investments are measured at fair value.

Any foreign exchange gains or losses on available-for-sale investment securities are recognised in profit or loss. Interest income is recognised in profit or loss using the effective interest method.

Other fair value changes are recognised in other comprehensive income until the investment is sold or impaired, whereupon the cumulative gains and losses previously recognised in other comprehensive income are reclassified to profit or loss as a reclassification adjustment.

A non-derivative financial asset may be reclassified from the available-for sale category to the loans and receivables category if it would otherwise have met the definition of loans and receivables and if the Bank has the intention and ability to hold the financial asset for the foreseeable future or until maturity.

3.13.3 Fair value through profit or loss

The Bank designates some investment securities at fair value, with fair value changes recognised immediately in profit or loss as described in 3.10.

3.14 Derivatives held for risk management purposes

Derivatives held for risk management purposes include all derivative financial assets and liabilities that are not classified as trading assets or liabilities. Derivatives held for risk management purposes include:

- Derivatives which are designated as hedging instruments; and
- Derivatives used for risk management purposes but which do not qualify for hedge accounting.

Derivatives held for risk management purposes are measured at fair value in the Statement of Financial Position. All changes in its fair value are recognised immediately in profit or loss as a component of net trading income.

3 Significant accounting policies (continued)

3.15 Hedge Accounting

For accounting purposes there are three possible types of hedges:

(1) Fair Value Hedges: hedges of changes in the fair value of assets, liabilities or unrecognised firm commitments;

(2) Cash Flow Hedges: hedges of the variability of future cash flows from highly probable forecast transactions and floating rate assets and liabilities; and

(3) Hedges of net investments in foreign operations: hedges of the translation adjustments resulting from translating the functional currency financial statements of foreign operations into the presentation currency of the parent.

The Bank makes use of Fair Value Hedge accounting.

IAS 39 prescribes the use of hedge accounting for derivatives which serve to hedge the fair value of assets or liabilities against one or more defined risks. Interest rate swaps are primarily used to hedge fixed rate available-for-sale securities that are subject to interest rate risk. Any changes in the fair value of the hedged asset or hedged liability resulting from an opposite move in the hedged risk are also recognised in profit or loss under 'net trading income'. Any portion of the changes in fair value that are not attributable to the hedged risk are accounted for in accordance with the rules of the valuation category to which the hedged asset or liability belongs.

In fair value hedge accounting an underlying transaction is linked with one or more hedging transactions in a hedging relationship. The carrying amounts of the hedged transactions are adjusted through profit or loss in the event of changes in fair value attributable to the hedged risk.

The application of hedge accounting rules is tied to a number of conditions. These relate above all to the documentation of the hedging relationship and also to its effectiveness. Documentation must include, in particular, the identification of the hedging instrument, the related hedged item or transaction, the nature of the risk being hedged and how effectiveness of the hedge is assessed.

3 Significant accounting policies (continued)

3.15 Hedge Accounting (continued)

IAS 39 requires the effectiveness of a hedge to be demonstrated during the entire term of the hedge in order for hedge accounting rules to be applied. Effectiveness in this context means the relationship between the change in fair value of the hedged item and the change in fair value of the hedging instrument attributable to the risk being hedged.

If these changes offset each other almost fully, a high degree of effectiveness exists. Proof of effectiveness requires, firstly, that a high degree of effectiveness can be expected from a hedge in the future (prospective effectiveness); secondly, when a hedge exists, it must be regularly demonstrated that it was highly effective during the period under review (retrospective effectiveness). Both the retrospective and prospective effectiveness must be within a range of between 80% and 125%.

Hedge effectiveness is assessed at inception and throughout the term of each hedging relationship. Hedge effectiveness is always assessed, even when the terms of the derivative and hedged item are matched.

Hedging derivatives are reported as 'Derivative financial instruments designated as fair value hedges' within 'Derivative assets held for risk management' or 'Derivative liabilities held for risk management'. In the event that a derivative is subsequently de-designated from a hedging relationship, it is transferred to financial assets/liabilities at fair value through profit or loss and reported as 'Derivative assets held for risk management' or 'Derivative liabilities held for risk management'. Subsequent changes in fair value are recognised in net trading income.

Hedge ineffectiveness is reported in net trading income and is measured as the net effect of changes in the fair value of the hedging instrument and changes in the fair value of the hedged item arising from changes in the market rates that correspond to the hedged risk.

If a fair value hedge of a debt instrument is discontinued prior to the instrument's maturity (i.e.: the derivative is terminated, expired or the relationship is de-designated), any remaining fair value adjustments relating to the hedged risk is made to the carrying amount of the debt instrument which is amortised to interest income or expense over the remaining life of the instrument. For other types of fair value adjustments, and whenever a fair value hedged asset or liability is sold or otherwise derecognised, any such adjustments are included in the calculation of the gain or loss on de-recognition.

3 Significant accounting policies (continued)

3.16 Trading assets and liabilities

'Trading assets and liabilities' are those assets and liabilities, including derivative assets and liabilities not acquired for risk management purposes, that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

Trading assets and liabilities are initially recognised and subsequently measured at fair value in the Statement of Financial Position, with transaction costs recognised in profit or loss. All changes in fair value are recognised as part of net trading income in profit or loss. Trading assets and liabilities are not reclassified subsequent to their initial recognition, except that non-derivative trading assets, other than those designated at fair value through profit or loss on initial recognition, may be reclassified out of the fair value through profit or loss – i.e. trading – category if they are no longer held for the purpose of being sold or repurchased in the near term and the following conditions are met.

If the financial asset would have met the definition of loans and receivables (if the financial asset had not been required to be classified as held-for-trading at initial recognition), then it may be reclassified if the Bank has the intention and ability to hold the financial asset for the foreseeable future or until maturity.

If the financial asset would not have met the definition of loans and receivables, then it may be reclassified out of the trading category only in rare circumstances.

3.17 Embedded Derivatives

Derivatives may be embedded in another contractual arrangement (a host contract). The Bank accounts for an embedded derivative separately from the host contract when:

- the host contract is not itself carried at fair value through profit or loss;
- the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract; and
- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract.

Separated embedded derivatives are measured at fair value, with all changes in fair value recognised in profit or loss.

3 Significant accounting policies (continued)

3.18 Property and equipment

3.18.1 Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and any accumulated impairment losses.

Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

When parts of an item of property and equipment have different useful lives, the major components are accounted for as separate items of property and equipment.

The gain or loss on disposal of an item of property and equipment is determined by comparing the proceeds from disposal with the carrying amount of the item of property and equipment and are recognised net within other operating income in profit or loss.

3.18.2 Subsequent costs

The cost of replacing a component of an item of property or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced component is derecognised. Ongoing repairs and maintenance property and equipment are recognised in profit or loss as incurred.

3.18.3 Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each component of an item of property and equipment since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. Leased assets under finance leases are depreciated over the shorter of the lease term and their useful lives.

The estimated useful lives for the current and comparative periods are as follows:

• improvements to premises	4 –10	years
• computer equipment	3 – 5	years
• other equipment	4	years
• fixtures and fittings	10	years
• motor vehicles	5	years

Depreciation methods, useful lives and residual values are reassessed at each financial period-end and adjusted if appropriate.

3 Significant accounting policies (continued)

3.19 Intangible assets

The Bank's intangible assets represent software. Software acquired by the Bank is stated at cost less accumulated amortisation and any accumulated impairment losses.

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful life of the software, from the date that it is available for use since this most closely reflects the expected pattern of consumption of the future economic benefits embodied in the asset. The estimated useful life of the software is 3 to 5 years.

Amortisation methods, useful lives and residual values are reviewed at each financial period-end and adjusted if appropriate.

3.20 Leased assets – lessee

Leases in terms of which the Bank assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

Other leases are operating leases and the operating leased assets are not recognised on the Bank's Statement of Financial Position.

The Bank did not have any finance leases during the years ended 31 March 2014 and 31 March 2013.

3 Significant accounting policies (continued)

3.21 Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. For intangible assets that are not yet available for use, the recoverable amount is estimated each year at the same time.

The recoverable amount of an asset or cash-generating unit ("CGU") is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generate cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets.

An impairment loss is recognised if the carrying amount of an asset or a CGU exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3.22 Amounts owed to financial institutions, amounts owed to customers, debt securities issued and subordinated liabilities

Amounts owed to financial institutions and customers, debt securities issued and subordinated liabilities are the Bank's principal sources of debt funding.

When the Bank sells a financial asset and simultaneously enters into an agreement to repurchase the asset (or a similar asset) at a fixed price on a future date ("repo"), the arrangement is accounted for as a secured loan and the underlying asset continues to be recognised in the Bank’s financial statements.

Amounts owed to financial institutions, amounts owed to customers, debt securities and subordinated liabilities are initially measured at fair value less incremental direct transaction costs and subsequently measured at their amortised cost using the effective interest method.

3 Significant accounting policies (continued)

3.23 Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. 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.

3.24 Employee benefits

The Bank contributes towards the State Pension Defined Contribution plan in accordance with legislation and to which it has no commitment beyond the payment of fixed contributions. Obligations for this defined contribution plan are recognised as an employee benefit expense in profit or loss in the years during which services are rendered by employees.

3.25 Earnings per share

The Bank presents basic earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the year. The Bank does not have any dilutive potential ordinary shares that would otherwise require the presentation of diluted earnings per share. Bonus shares declared and approved after year end are added to the weighted average number of ordinary with no time weighting applied.

3.26 Changes in accounting policies

Except for the changes below, the Bank consistently applied the accounting polices set in this note to all periods presented in these separate financial statements.

The Bank has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of 1 April 2013.

A) IFRS 13, *Fair value Measurement*

IFRS 13 establishes a single framework for measuring fair value and making disclosures about fair value measurements, when such measurements are required or permitted by other IFRSs. In particular, it unifies the definition of fair value as the price at which an orderly transaction to sell an asset or to transfer a liability would take place between market participants at the measurement date. It also replaces and expands the disclosure requirements about fair value measurements in other IFRSs (see below). Accordingly, the Bank has included additional disclosures in this regard.

3 Significant accounting policies (continued)

3.26 Changes in accounting policies (continued)

A) IFRS 13, *Fair value Measurement (continued)*

In accordance with the transitional provisions of IFRS 13, the Bank has applied the new fair value measurement guidance prospectively, and has not provided any comparative information for new disclosures. Notwithstanding the above, the change had no significant impact on the measurements of the Bank's assets and liabilities.

B) Amendments to IFRS 7, Financial Instruments: Disclosures

As a result of the amendments to IFRS, the Bank has expanded disclosures about offsetting financial assets and financial liabilities (see note 4.3.7).

C) Presentation of items of Other Comprehensive Income.

As a result of the amendments to IAS 1, the Bank has modified the presentation of items of OCI in its statement of comprehensive income, to present items that would be reclassified to profit or loss in the future separately from those that would never be. Comparative information has been re-presented on the same basis.

3.27 New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 April 2014 and have not been applied in preparing these financial statements. Those relevant to the Bank are as follows:

The Bank is considering the implications of the EU adopted IFRS 10 Consolidated Financial Statements (issued in May 2011 and amended in June 2012 for its transitional provisions), a new standard with a date of initial application of 1 January 2014, in view of the proposed conversion of its Belgium branch to a subsidiary to be wholly owned by the Bank and its acquisition of Volksbank Malta Limited (note 37).

IFRS 10 (2011) introduces a new control model that focuses on whether an investor has power over an investee, exposure or rights to variable returns from its involvement with the investee and the ability to use its power to affect those returns.

4 Financial risk management

4.1 Introduction and overview

The Bank has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk
- operational risk

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risks and the Bank's management of capital.

4.2 Risk management framework

The Bank recognises the need to have an effective and efficient risk management function and therefore it has adopted a comprehensive process that provides an appropriate balance between the fast growth of the Bank, maximising its profitability and managing the associated risks.

The Bank's objective is to deploy an integrated risk management approach that ensures an awareness of, and accountability for, the risks taken throughout the Bank and also to develop the tools needed to address those risks. This integrated approach is realised through the governance structure of the Bank and relies on three lines of defence – business units management, an independent risk management function, and independent on-going reviews by internal audit.

4.3 Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Bank's loans and advances to customers and other banks and investment debt securities. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.1 Management of credit risk

The Bank's objective is to maximise its investment returns while maintaining a sound and prudent investment profile. To facilitate achieving this target, the Bank invests in a diversified portfolio including both high-quality assets with strong ratings stability and a highly granular portfolio of loans to corporations and securities issued by corporations, whose higher returns are viewed as justifying a greater level of risk.

Specifically, the Bank focuses on secured and unsecured debt securities issued by financial institutions (some of which may carry a government guarantee), supranational agencies and governments. The Bank also provides lending to corporate borrowers, either by subscribing to debt securities or by providing senior loans. The Bank's Credit and Investment Policy permits it, subject to the prior approval of the Board, to manage its credit risk through credit hedges, although to date it has not done so.

The Bank's investments are managed on a portfolio basis, taking into account correlations between asset classes. The Bank diversifies its financial and sovereign exposures to avoid excessive concentration in particular countries or types of financial institutions and by including lending to corporate borrowers in the Bank's portfolio.

The Management Credit Committee is responsible for approving credit recommendations and making other credit decisions under its authority delegated by the Board. This includes decisions on individual credits, reviewing and recommending credit and large exposures to the Board, consideration of credit hedging strategies and recommending other concentration limits for Board approval. It is also responsible for delegating transactional responsibility to the Treasury and Investment department and within the parameters that the Management Credit Committee sets out, the Bank's investment portfolio is managed on a day to day basis by the Head of Treasury and Investment.

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.1 Management of credit risk (continued)

Set out below is an analysis of the gross and net impairment exposure of the Bank's assets:

	2014		2013	
	Gross Exposure	**Net Exposure**	Gross Exposure	Net Exposure
	€000	**€000**	€000	€000
Balances with Central Bank of Malta and treasury bills	**17,907**	**17,907**	69,848	69,848
Cash	**184**	**184**	207	207
Loans and advances to financial institutions	**87,714**	**87,714**	20,131	20,131
Loans and advances to customers: corporate	**570,619**	**568,325**	400,276	399,600
Loans and advances to customers: retail	**2,819**	**2,819**	2,574	2,574
Investments	**1,478,403**	**1,477,940**	1,564,034	1,564,034
Derivative assets held for risk management	**404**	**404**	1,152	1,152
Derivative assets held for trading	**404**	**404**	-	-
Accrued income	**19,164**	**19,164**	23,778	23,778
Loans to related parties (included in other assets)	**18,145**	**18,145**	12,823	12,823
Other non-financial assets	**10,642**	**10,642**	7,771	7,771
	2,206,405	**2,203,648**	2,102,594	2,101,918

4.3.2 Impaired loans and advances and investment securities

All credit exposures have been reviewed on a case by case and collective basis (see accounting policy 3.10.7) in the light of current economic conditions and considered the likelihood that the Bank may be exposed to losses on loans and advances and investment securities. Impaired investment securities and loans are those where a loss event has occurred and the Bank establishes that it is unlikely that it will collect the full principal and/or interest due.

4.3.3 Allowances for impairment

The Bank established an allowance for impairment also at collective levels on its loans and advances to customers and investment securities that represent losses incurred but not yet identified.

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.3 Allowances for impairment (continued)

	Individually assessed allowances	**Collective allowances**	Individually assessed allowances	Collective allowances
	2014	**2014**	2013	2013
	€000	**€000**	€000	€000
Loans and advances to customers: corporate				
At 1 April 2013	**-**	**676**	-	-
Additions	**1,422**	**196**	-	676
At 31 March 2014	**1,422**	**872**	-	676
Investment securities				
At 1 April 2013	**-**	**-**	-	-
Additions	**-**	**463**	-	-
At 31 March 2014	**-**	**463**	-	-
Total allowance for impairment	**1,422**	**1,335**	-	676

During the financial year ended 31 March 2014, there were no forbearance measures and practices undertaken (2013: nil). Accordingly no disclosure of the details of the type of forbearance measures and practices undertaken and how these are managed and monitored by management is applicable as would otherwise be required by ESMA.

4.3.4 Write-off policy

The Bank writes off a loan or an investment debt security balance and any related allowances for impairment losses, when the Bank determines that the balance is uncollectible. This determination is made after considering information such as the occurrence of significant changes in the borrower's/issuer's financial position such that the borrower/issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. No financial asset was written off during the year (2013: nil).

Included with "administrative and other expenses" there is a write-off of €5 thousand which has been incurred upon the liquidation of a dormant subsidiary, Mediterranean Global Advisory SA during the year ended 31 March 2014. The subsidiary was domiciled in Switzerland and wholly owned by the Bank.

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.5 Exposure to sovereign debt of selected Eurozone countries

During the year ended 31 March 2014 the Bank continued to manage down its exposure to Eurozone government bonds not carrying an investment-grade credit rating, and as at 31 March 2014 this exposure was immaterial. The Bank's exposure to sovereign Eurozone government bonds is as follows:

% of Total Debt Securities

	2014	2013
Greece	**0.35%**	0.96%
Portugal	**-**	2.18%
Malta	**7.22%**	1.97%
	7.57%	5.11%

No impairment provisions in respect of these exposures were required during the year ending 31 March 2014 (2013: nil).

In addition, the bank holds Treasury bills as disclosed in note 14.

Notes to the Financial Statements
For the Year Ended 31 March 2014

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.6 Concentration of loans and advances and investment securities and derivative assets

The Bank monitors concentrations of credit risk by sector and by geographical location. An analysis of concentrations of credit risk (net) at the reporting date is shown below.

	Balances with Central Bank of Malta, Treasury bills and Loans and advances to financial institutions		**Loans and advances to customers and related parties**		**Investments & derivative assets**	
	2014	2013	**2014**	2013	**2014**	2013
	€000	€000	**€000**	€000	**€000**	€000
Concentration by type						
Net carrying amount						
Senior bank obligations	**99,624**	49,087	**-**	-	**104,580**	104,477
Covered bonds	**-**	-	**-**	-	**604,822**	1,000,290
Government securities	**5,997**	40,892	**-**	-	**156,678**	130,365
Supranationals and agencies	**-**	-	**-**	-	**312,524**	151,500
Pooled securities	**-**	-	**-**	-	**6,101**	117,433
Secured corporate lending	**-**	-	**568,325**	399,600	**248,059**	54,964
Unsecured corporate lending	**-**	-	**18,145**	12,823	**42,702**	5,005
Retail secured lending	**-**	-	**2,819**	2,574	**-**	-
Equity instruments	**-**	-	**-**	-	**2,474**	-
Warrants	**-**	-	**-**	-	**404**	-
Interest rate swaptions	**-**	-	**-**	-	**404**	-
Interest rate swap	**-**	-	**-**	-	**-**	279
Foreign exchange swaps	**-**	-	**-**	-	**-**	873
	105,621	89,979	**589,289**	414,997	**1,478,748**	1,565,186

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.6 Concentration of loans and advances and investment securities and derivative assets (continued)

Concentration by location

	Balances with Central Bank of Malta and Loans and advances to financial institutions		Loans and advances to customers		Investments & derivative assets	
	€000	€000	**€000**	€000	**€000**	€000
Net carrying amount						
Europe	**98,868**	49,087	**533,926**	385,161	**1,441,579**	1,532,020
North America	**440**	-	**37,218**	17,013	**37,169**	33,166
Australia	**316**	-	**-**	-	**-**	-
	99,624	49,087	**571,144**	402,174	**1,478,748**	1,565,186

All treasury book securities in the portfolio are accepted by the European Central Bank (ECB) as collateral except for the pooled securities with an aggregate carry value of €6.101 million (2013: €40.608 million). Either the securities themselves or the issuers of the securities are rated by at least one of Fitch, Standard & Poor's and Moody's. Senior bank obligations are held with central banks and financial institutions counterparties that are generally rated at least investment grade. Retail secured lending are collateralised by term deposits.

Concentration by location for investment securities is measured based on the location of the issuer of the security. Concentration by location for loans and advances is based on the borrower’s country of domicile. Government and government guaranteed securities include securities issued or guaranteed by regional governments.

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.6 Concentration of loans and advances and investment securities (continued)

The Bank held investment securities with a net carrying amount of €1,478 million as at 31 March 2014 (2013: €1,564 million) net of impairment, an analysis of the credit quality based on rating agency ratings is as follows:

	2014	2013
	€000	€000
Government securities		
A+ or lower	**106,074**	130,365
Other securities		
AA- and higher	**796,439**	1,111,924
A+ or lower	**575,831**	321,745
Total	**1,478,344**	1,564,034

In addition, the bank held treasury bills disclosed in note 14, with a rating of A+ or lower. Loans and advances to financial institutions disclosed in note 15 are classified as 'Regular' by the Bank and above investment grade by reputable credit rating agencies.

An analysis of Loans and advances to customers – corporate by internal credit classification is provided in the table below:

	2014	2013
	€000	€000
Neither past due nor impaired		
Regular	**463,938**	285,969
Focus	**66,132**	69,551
Under surveillance	**32,984**	47,330
Allowance for collective impairment	**(872)**	(676)
Doubtful	**10,384**	-
Allowance for individual impairment	**(1,422)**	-
Net carrying amount	**571,144**	402,174

Other assets of €18.889 million (2013: €13.598 million) consist principally of related party loans amounting to €18.145 million (2013: €12.823 million) which are not externally or internally rated.

Accrued income from investments securities amounting to €11.103 million (2013: €20.108 million) is related to assets classified above investment grade of €1.180 billion (2013: €1.455 billion) with the remaining related to the securities below investment grade.

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.7 Offsetting financial assets and financial liabilities

The disclosures set out in the tables below include financial assets and financial liabilities that:

- are offset in the Bank's statement of financial position; or
- are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments, irrespective of whether they are offset in the statement of financial position.

The similar agreements include derivative clearing agreements and global master repurchase agreements. Similar financial instruments include derivatives, sales and repurchase agreements and reverse sale and repurchase agreements. Financial instruments such as loans and deposits are not disclosed in the tables below unless they are offset in the statement of financial position.

The ISDA and similar master netting arrangements, with the exception of the principal clearing house netting arrangement, do not meet the criteria for offsetting in the statement of financial position. This is because they create for the parties to the agreement of a right to set-off of recognised amounts that is enforceable only following an event of default, insolvency or bankruptcy of the Bank or the counterparties or following other predetermined events. In addition, the Bank and its counterparties do not intend to settle on a net basis or to realise the assets and settle. In the case of the principal clearing house netting arrangement, the Bank is allowed to offset and settle its claims on a net basis at any time vis-à-vis the clearing counterparty.

The Bank receives and gives collateral in the form of cash and marketable securities in respect of the following transactions:

- derivatives; and
- sale and repurchase, and reverse sale and repurchase agreements.

Such collateral is subject to standard industry terms including, when appropriate, an ISDA *Credit Support annex.* This means that securities received/given as collateral can be pledged or sold during the term of the transaction but have to be returned on maturity of the transaction. The terms also give each party the right to terminate the related transactions on the counterparty's failure to post collateral.

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.7 Offsetting financial assets and financial liabilities (continued)

Below is a table showing financial assets subject to offsetting, enforceable master netting arrangements and similar agreements.

31 March 2014

There were no financial assets presented in the Statement of Financial Position in scope of offsetting disclosures.

	Gross amounts of recognised financial liabilities	Gross amounts of recognised financial assets offset in the statement of financial position	Net amounts of financial assets presented in the statement of financial position	Related amounts not offset in the statement of financial position: Financial instruments (including) non-cash collateral)	Cash collateral pledged	Net amount
	€000	€000	€000	€000	€000	€000
Types of financial liabilities						
Repurchase agreements	(932,473)	4,347	(928,126)	1,061,705	-	133,579
Total Return Swaps	(98,267)	31,069	(67,198)	99,575	-	32,377
Derivatives held for risk management						
- Interest rate swaps	(2,798)	-	(2,798)	-	2,383	(415)
	(1,033,538)	**35,416**	**(998,122)**	**1,161,280**	**2,383**	**165,541**

31 March 2013

	Gross amounts of recognised financial assets	Gross amounts of recognised financial liabilities offset in the statement of financial position	Net amounts of financial assets presented in the statement of financial position	Related amounts not offset in the statement of financial position: Financial instruments (including) non-cash collateral)	Cash collateral received	Net amount
	€000	€000	€000	€000	€000	€000
Types of financial assets						
Derivatives held for risk management						
- Interest rate swaps	279	-	279	-	6,308	6,587

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.7 Offsetting financial assets and financial liabilities (continued)

31 March 2013

	Gross amounts of recognised financial liabilities	Gross amounts of recognised financial assets offset in the statement of financial position	Net amounts of financial assets presented in the statement of financial position	Related amounts not offset in the statement of financial position: Financial instruments (including) non-cash collateral)	Cash collateral pledged	Net amount
	€000	€000	€000	€000	€000	€000
Types of financial liabilities						
Repurchase agreements	(1,259,324)	-	(1,259,324)	1,448,320	-	188,996
Total Return Swaps	(82,063)	36,143	(45,920)	120,271	-	74,351
Derivatives held for risk management						
- Interest rate swaps	-	-	-	-	-	-
	(1,341,387)	**36,143**	**(1,305,244)**	**1,568,591**	**-**	**263,347**

Below is a table reconciling the above analysis to the net amounts of financial assets and financial liabilities presented in the Statement of Financial Position.

31 March 2014

	Net amounts	Line item in statement of financial position	Carrying amount in statement of financial position	Financial liabilities not in scope of offsetting disclosures	Note
	€000		€000	€000	
Types of financial liabilities					
Repurchase agreements	928,126	Amounts owed to financial institutions	1,008,976	13,652	27
Total Return Swaps	67,198				
Derivatives held for risk management					
- Interest rate swaps	2,798	Derivative liabilities held for risk management	2,973	175	18

4 Financial risk management (continued)

4.3 Credit risk (continued)

4.3.7 Offsetting financial assets and financial liabilities (continued)

31 March 2013

	Net amounts	Line item in statement of financial position	Carrying amount in statement of financial position	Financial assets not in scope of offsetting disclosures	Note
	€000		€000	€000	
Types of financial assets					
Derivatives held for risk management					
- Interest rate swaps	279	Derivative liabilities held for risk management	1,152	873	18

	Net amounts	Line item in statement of financial position	Carrying amount in statement of financial position	Financial liabilities not in scope of offsetting disclosures	Note
	€000		€000	€000	
Types of financial liabilities					
Repurchase agreements	1,259,324	Amounts owed to financial institutions	1,368,995	63,751	27
Total Return Swaps	45,920				

4 Financial risk management (continued)

4.4 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

4.4.1 Management of liquidity risk

Management of liquidity risk is the responsibility of the Bank's Treasury Department and its Risk Office, under the oversight of its Management Asset-Liability Committee and its Board Risk Committee and under an approach set out in its Treasury Management Policy.

Treasury Management Policy ("TMP")

The Bank's TMP establishes the principles, standards, internal controls, high-level reporting requirements and escalation and approval processes that govern the ongoing management of:

- the Bank's liquidity and asset-liability mix;
- the Bank's market, interest rate and currency risk;
- any credit risk taken on in connection with the activities above.

It is also designed to ensure compliance with all national and international regulations and laws that are applicable to these activities.

Management Asset and Liability Committee

The Bank has established a Management Asset and Liability Committee ("ALCO") which is responsible for the management of funding, liquidity, interest rate and currency risks. ALCO sets and reviews overall policies and objectives for asset and liability management, capital management and allocation; capital usage and efficiency; transfer pricing; risk management; and underwriting, dealing and trading activities according to the risk appetite set by the Board. It also decides on the level of any credit impairments to be taken on the Bank's investments, after receiving recommendations from the Management Credit Committee.

Board Risk Committee

The Board Risk Committee is responsible for setting policies of the Bank in respect of liquidity and funding, interest rate and currency risks of the Bank and for reviewing and approving any changes to the overall asset-liability management strategy of the Bank. As such, it is the board-level committee that oversees the TMP.

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

4.4.1 Management of liquidity risk (continued)

Roles and responsibilities

Management of the Bank's liquidity position and of its market risk is the joint responsibility of its Treasury and Risk functions (under the oversight of ALCO and of the Board Risk Committee), as is management of the credit risk that arises from these activities. In broad terms:

- Treasury has primary responsibility for managing and reporting the Bank's projected liquidity position (the "base case"), and for managing its market risk position on a day-to-day basis; and
- Risk has primary responsibility for defining potential adverse liquidity scenarios that should be considered and for reporting exposure to these scenarios (the "downside case"), as well as for regular formal reporting of the Bank's market risk position.

Funding Strategy

Banks traditionally perform a role of liquidity transformation, whereby they fund through liabilities that are liquid in the short to medium-term, in order to invest in longer-term and less liquid assets. This mismatch of liquid liabilities and less liquid assets is a near-universal feature of bank balance sheets and clearly leads to a risk if liabilities cannot be rolled when they mature (which may be every day in the case of money held in current or savings accounts).

The Bank's strategy to mitigate this risk has three main components:

- Limiting its exposure to customer deposit withdrawal by use of term rather than overnight deposits as its primary instrument of customer funding;
- Limiting its exposure to wholesale funding withdrawal by locking in term funding against less liquid assets and by diversifying its sources of funding; and
- Maintaining a contingency source of funding by ensuring that the bulk of its Treasury portfolio is eligible for funding at the ECB if alternative sources are unavailable.
  The Bank's objective is to maintain a prudent funding structure drawn from diverse funding sources while recognising its position as a regulated credit institution.

Potential funding sources may include, but are not limited to:

- Deposits from retail and corporate customers;
- Bond issuance, either secured, senior unsecured or subordinated;
- Issuance of capital instruments;
- Interbank funding (either secured, for example through repo or TRS, or unsecured); and
- Central Bank funding.

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

4.4.2 Residual contractual maturities of financial liabilities

The below tables show the residual maturities of the Bank's financial liabilities.

31 March 2014

	Carrying amount	Gross nominal outflow	Less than 1 month	1 month to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years
	€000	€000	€000	€000	€000	€000	€000
Non-derivative liabilities							
Amount owed to financial institutions:							
- Due to clearing houses	522,032	525,050	27,059	10,006	208,129	279,856	-
- Due to other banks	486,944	489,151	98,431	256,192	134,528	-	-
Amounts owed to customers	776,715	831,751	203,445	19,693	241,711	366,846	56
Debt securities in issue	14,341	16,456	-	-	958	15,498	-
Debt securities in issue through funding structure	215,786	263,633	-	-	3,532	14,230	245,871
Subordinated liabilities	22,385	32,748	-	-	1,711	6,830	24,207
	2,038,203	**2,158,789**	**328,935**	**285,891**	**590,569**	**683,260**	**270,134**
Derivative liabilities							
Derivative liabilities held for risk management							
- Interest rate swaps	2,798						
- Inflows		28,358	-	-	1,226	18,586	8,546
- Outflows		(30,993)	-	-	(3,808)	(21,801)	(5,384)
- Foreign exchange swaps	175	409	7	402	-	-	-
	2,973	**(2,226)**	**7**	**402**	**(2,582)**	**(3,215)**	**3,162**

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

4.4.2 Residual contractual maturities of financial liabilities (continued)

31 March 2013

	Carrying amount	Gross nominal outflow	Less than 1 month	1 to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years
	€000	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Non-derivative liabilities							
Amount owed to financial institutions:							
- Due to Central Bank of Malta	107,000	107,016	107,016	-	-	-	-
- Due to clearing houses	695,000	696,669	164,269	181,232	205,159	146,009	-
- Due to other banks	566,995	567,467	175,259	299,499	9,789	82,920	-
Amounts owed to customers	566,047	618,039	170,303	15,583	97,703	334,450	-
Debt securities in issue	15,664	18,887	-	-	994	17,893	-
Subordinated liabilities	12,341	18,936	-	-	931	3,725	14,280
	1,963,047	**2,027,014**	**616,847**	**496,314**	**314,576**	**584,997**	**14,280**
Derivative liabilities	**-**	**-**	**-**	**-**	**-**	**-**	**-**

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

4.4.2 Residual contractual maturities of financial liabilities (continued)

The table below sets out the availability of the Bank's financial assets to support future funding.

31 March 2014

	Encumbered		**Unencumbered**		
	Pledged as collateral	**Other[†]**	**Available as collateral**	**Other[‡]**	**Total**
	€000	**€000**	**€000**	**€000**	**€000**
Balances with Central Bank of Malta and treasury bills and cash	5,997	-	-	12,094	18,091
Loans and advances to financial institutions	-	-	-	87,714	87,714
Loans and advances to customers: corporate	389,076	-	-	179,249	568,325
Loans and advances to customers: retail	-	-	-	2,819	2,819
Investments	1,143,915	3,822	298,030	32,173	1,477,940
Derivative assets held for risk management	-	-	-	404	404
Derivative assets held for trading	-	-	-	404	404
Loans and advances to related entities[§]	-	-	-	18,145	18,145
	1,538,988	**3,822**	**298,030**	**333,002**	**2,173,842**

31 March 2013

	Encumbered		**Unencumbered**		
	Pledged as collateral	**Other[†]**	**Available as collateral**	**Other[‡]**	**Total**
	€000	**€000**	**€000**	**€000**	**€000**
Balances with Central Bank of Malta and treasury bills	40,892	-	-	28,956	69,848
Loans and advances to financial institutions	-	-	-	20,131	20,131
Loans and advances to customers: corporate	115,538	-	-	284,062	399,600
Loans and advances to customers: retail	-	-	-	2,574	2,574
Investments	1,450,392	2,678	105,959	5,005	1,564,034
Derivative assets held for risk management	-	-	-	1,152	1,152
Loans and advances to related entities[§]	-	-	-	12,823	12,823
	1,606,822	**2,678**	**105,959**	**354,703**	**2,070,162**

[†] *Represents assets that are not pledged for funding purposes but that the Bank believes it is restricted from using to secure funding, for legal or other reasons.*
[‡] *Represents assets that are not restricted for use as collateral, but the Bank would not consider them as readily available to secure funding in the normal course of business.*
[§] *included in other assets*

Assets pledged as collateral include:

- Assets transferred to Total Return Swap which are not derecognised (note 16.7 and 17.6)
- Assets transferred to a collaterised funding structure which are not derecognised (note 16.6 and 17.5).

4 Financial risk management (continued)

4.4 Liquidity risk (continued)

4.4.2 Residual contractual maturities of financial liabilities (continued)

Liquidity Reporting

In order to ensure that the Bank has adequate liquidity to meet its near-term obligations, Treasury projects the Bank's expected liquidity position for each day over the next week, as well as estimating a "residual" cash balance that takes into account known inflows and outflows (for example settlements of asset purchases or sales) that fall outside this period. It reports using two key metrics:

- Before the relevant liquidity provisions under the Capital Requirements Regulations and Directive become effective in 2015, the Bank is required to maintain its liquid asset ratio of net cash to short-term customer liabilities, in excess of 30%. The calculation of this ratio is performed by Finance and submitted to the MFSA as part of the Bank's statutory monthly returns.

- Liquidity ratio, being the ratio of net cash to wholesale (margin-sensitive) funding. This cash buffer is designed to ensure that the Bank can meet any additional margin requirement that might be imposed by the ECB or by repo counterparties, resulting either from changes in market values of assets or from increases in applicable haircuts.

Liquidity Risk Reporting

The Risk Office is responsible for producing two key reports that describe the key risks to the Bank's liquidity position and quantify its ability to withstand the associated shocks:

- Scenario Analysis report, quantifying the potential liquidity impact of adverse market moves or rating agency actions on the Bank's asset base, and considering a number of scenarios of varying severity;

- Maximum Cumulative Outflow Report, projecting the Bank's cash position in an adverse scenario through time, allowing for the effect of remedial actions that can be taken but taking into account a wide range of potential cash drains including:

    i. Deposit flight (retail and corporate, specific and general)
    ii. Margin postings due to market moves and haircut changes
    iii. Failure of bilateral repo counterparties to roll financing
    iv. Loss of eligibility for ECB financing

4 Financial risk management (continued)

4.5 Market risks

Market risk is the risk that changes in market prices, such as interest rate, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

4.5.1 Management of market risks

As for liquidity risk, management of market risk is the responsibility of the Bank's Treasury Department and its Risk Office, under the oversight of its Management Asset-Liability Committee and its Board Risk Committee and under an approach set out in its Treasury Management Policy.

4.5.2 Currency risk

Foreign exchange risk is the risk that the value of the Bank's positions may fluctuate due to movements in underlying currency exchange rates. Although a large majority of the Bank's assets and liabilities is euro-denominated, the Bank does offer deposits in other major currencies and its loan portfolio includes a number of Sterling-denominated loan assets. The Bank seeks to minimise foreign exchange risk and thus hedges all material exposures in this area through the use of currency swaps and foreign exchange forward contracts.

4 Financial risk management (continued)

4.5 Market risks (continued)

4.5.2 Currency risk (continued)

The following table provides an analysis of the principal financial assets and financial liabilities of the bank into relevant currency groupings.

	31 March 2014			31 March 2013		
	Euro Currency	**Other Currencies**	**Total**	Euro Currency	Other Currencies	Total
	€'000	**€'000 equivalent**	**€'000 equivalent**	€'000	€'000 equivalent	€'000 equivalent
Financial assets						
Balances with Central Bank of Malta, treasury bills and cash	**18,014**	**77**	**18,091**	69,957	98	70,055
Loans and advances to financial institutions	**79,717**	**7,997**	**87,714**	13,538	6,593	20,131
Loans and advances to customers	**431,169**	**139,975**	**571,144**	346,726	55,448	402,174
Investments	**1,392,929**	**85,011**	**1,477,940**	1,559,301	4,733	1,564,034
Derivative assets held for risk management	**404**	-	**404**	279		279
Derivative assets held for trading	**404**	-	**404**	-	-	-
Accrued income	**17,048**	**2,116**	**19,164**	23,778	-	23,778
	1,939,685	**235,176**	**2,174,861**	2,013,579	66,872	2,080,451
Financial liabilities						
Amounts owed to financial institutions	**949,593**	**59,383**	**1,008,976**	1,331,241	37,754	1,368,995
Amounts owed to customers	**649,650**	**127,065**	**776,715**	469,132	96,915	566,047
Debt securities in issue	**230,127**	**-**	**230,127**	15,664	-	15,664
Derivative liabilities held for risk management	**2,973**	**-**	**2,973**	-	-	-
Subordinated liabilities	**20,171**	**2,214**	**22,385**	10,079	2,262	12,341
Accruals	**8,587**	**1,031**	**9,618**	5,842	-	5,842
	1,861,101	**189,693**	**2,050,794**	1,831,958	136,931	1,968,889
Net financial position		**45,483**			(70,059)	
Derivative instruments held for risk management		**(44,905)**			69,756	
Exposure		**578**			(303)	

The Bank uses derivative instruments to hedge movements in foreign currency. As a result the Bank is not materially exposed to fluctuations in foreign currency. The net exposure of all foreign currency amounts to a long position of €0.578 million (2013: short €0.303 million). As a result no currency sensitivity analysis is being presented.

4 Financial risk management (continued)

4.5 Market risks (continued)

4.5.3 Exposure to interest rate risk – non-trading portfolios

Interest Rate Risk Management

Interest rate risk arises as a consequence of the Bank's core businesses where there is a mismatch between the nature of rates received on the Bank's financial assets and the rates paid on the Bank's liabilities. For example, fixed-rate term deposits could be used to fund floating-rate loans, or floating-rate secured funding could be used to finance the purchase of fixed-rate securities.

Treasury, under the oversight of the Head of Treasury and Investment, manages interest rate risk within the prevailing interest rate risk strategy as set by ALCO, and subject to limits recommended by the Chief Risk Officer and approved by ALCO.

Interest Rate Risk Reporting and Analysis

The Risk Office prepares an interest rate risk report of the Bank monthly. The report outputs show the effects of potential yield curve moves on:

- Projected Net Interest Margin
- The Bank's capital position
- The Economic Value of the Bank's financial assets and liabilities, assuming that no fixed-rate deposits are rolled
- The Economic Value of the Bank's financial assets and liabilities, incorporating assumptions around fixed-rate deposit rolls.

4 Financial risk management (continued)

4.5 Market risks (continued)

4.5.3 Exposure to interest rate risk – non-trading portfolios (continued)

A summary of the Bank's interest rate gap position on non-trading portfolios, excluding the effect of interest rate hedging, is as follows:

31 March 2014		**Re-pricing in:**		
	Carrying amount	**Less than 3 months**	**3 months to 1 year**	**More than 1 year**
	€000	**€000**	**€000**	**€000**
Balances with Central Bank of Malta and treasury bills	17,907	15,057	2,850	-
Loans and advances to financial institutions	87,714	87,714	-	-
Loans and advances to customers	571,144	537,426	31,285	2,433
Investments	1,478,344	240,818	19,402	1,218,124
	2,155,109	**881,015**	**53,537**	**1,220,557**
Amounts owed to financial institutions:				
- Due to clearing houses	522,032	37,032	207,000	278,000
- Due to other banks	486,944	353,966	65,595	67,383
Amounts owed to customers	776,715	222,527	236,859	317,329
Debt securities issued	14,341	-	-	14,341
Debt securities issued through funding structure	215,786		215,786	-
Subordinated liabilities	22,385	-	-	22,385
	2,038,203	**613,525**	**725,240**	**699,438**
Interest rate gap	**116,906**	**267,490**	**(671,703)**	**521,119**

4 Financial risk management (continued)

4.5 Market risks (continued)

4.5.3 Exposure to interest rate risk – non-trading portfolios (continued)

31 March 2013		Re-pricing in:		
	Carrying amount	Less than 3 months	3 months to 1 year	More than 1 year
	€000	€000	€000	€000
Balances with Central Bank of Malta and treasury bills	69,848	45,975	19,941	3,932
Loans and advances to financial institutions	20,131	20,131	-	-
Loans and advances to customers	402,174	385,871	13,834	2,469
Investments	1,564,034	401,626	3,699	1,158,709
	2,056,187	**853,603**	**37,474**	**1,165,110**
Amounts owed to financial institutions:				
- Due to Central Bank of Malta	107,000	107,000	-	-
- Due to clearing houses	695,000	345,000	205,000	145,000
- Due to other banks	566,995	551,609	14,649	737
Amounts owed to customers	566,047	185,465	94,932	285,650
Debt securities issued	15,664	-	-	15,664
Subordinated liabilities	12,341	-	-	12,341
	1,963,047	**1,189,074**	**314,581**	**459,392**
Interest rate gap	**93,140**	**(335,471)**	**(277,107)**	**705,718**

Interest rate risk positions are managed by Treasury and Investment department, in conjunction with Risk Management, by strategically positioning the asset and liability interest rate re-pricing profiles as well as by purchases of interest rate derivatives, primarily swaps. The use of derivatives to manage interest rate risk is described in note 18.

In addition, Treasury uses advances to financial institutions and deposits from financial institutions to manage the overall position arising from the Bank's non-trading activities.

4 Financial risk management (continued)

4.5 Market risks (continued)

4.5.3 Exposure to interest rate risk – non-trading portfolios (continued)

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various interest rate scenarios. The estimated impact on NIM as a result of a 100 basis points (bps) movement and on Economic Value as a result of a 100 basis points (bps) parallel fall / rise in the yield curves would be as follows:

31 March 2014

- NIM would decrease by €5.12 million / increase by €4.10 million.
- Economic Value would decrease by €4.65 million / increase by €6.52 million.

These values are presented after taking into account the impact of hedge accounting and it has been assumed in this calculation that market interest rates do not become negative.

31 March 2013

- NIM would decrease by €7.91 million / increase by €8.96 million.
- Economic Value would decrease by €16.96 million / increase by €19.61 million.

Interest rate movements affect reported equity in the following ways:

- Retained earnings arising from increases or decreases in net interest income after taking into consideration the net impact of interest rate hedging instruments; and

- Fair value reserves arising from increases or decreases in fair values of available-for-sale financial instruments reported directly in equity.

As the Bank's expectation is that it will increase its annual reserves by more than the calculated maximum loss under the most severe stress scenario of 100 bps noted above, the Bank should always generate a net positive increase of its reserves.

4 Financial risk management (continued)

4.6 Operational risks

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Bank's operations and are faced by all business entities.

The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity while maintaining risk taking within a tolerable limit.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Bank standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions
- requirements for the reconciliation and monitoring of transactions
- compliance with regulatory and other legal requirements
- documentation of controls and procedures
- requirements for the periodic assessment of operational risks faced and the adequacy of controls and procedures to address the risks identified
- requirements for the reporting of operational losses and proposed remedial action
- development of contingency plans
- training and professional development
- ethical and business standards
- risk mitigation, including insurance where this is effective

A financial measurement of this risk is calculated by the Bank for the purpose of allocating risk capital using the Basic Indicator Approach under the CRR. The capital requirement for operational risk under this method was calculated at €4,417,400 (31 March 2013: €4,387,500).

4 Financial risk management (continued)

4.7 Capital management – regulatory capital

The Bank's regulator, the MFSA, sets and monitors capital requirements for the Bank.

The European Parliament has approved the new capital reforms, referred to as Capital Requirements Regulations (CRR) and Capital Requirements Directive (henceforth 'CRD IV'), on 26 June 2013. These reforms implement the Basel III into Europe with the sole objective to improve the banking sector's ability to absorb shocks arising from financial and/or economic stress which in turn, mitigate spill-over damage to the real economy. The CRD IV legislation has been implement with an effective date of 1 January 2014.

In implementing current capital requirements, the MFSA requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets.

The Bank does not engage in trading and is exempt from having a trading book. Risk-weighted assets on the banking book are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets including balances with counterparties and other illiquid assets.

The Bank complies with the provisions of CRR in respect of regulatory capital and it applies the standardised approach.

For regulatory purposes, the Bank's capital base is divided in two main categories, namely Common Equity Tier 1 Capital and Tier 2 Capital.

- Common Equity Tier 1 Capital which includes ordinary share capital, share premium, retained earnings, shareholders' contribution, fair value reserve and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes including and deductions relating to Reserve for Depositor Compensation Scheme ('Other reserves') and the carrying amounts of investment in subsidiaries that are not included in the regulatory consolidation and certain other regulatory items; and

- Tier 2 Capital consists of subordinated liabilities in issue, which rank behind the claims of all depositors (including financial institutions) and all other creditors.

The Bank's policy is to maintain a sufficient capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

As fully disclosed in note 26 and note 30, the Bank's Regulatory Own Funds was increased through various instruments, being

- increase in ordinary A share capital of €14.70 million;
- increase in shareholders' contribution by €1.25 million; and
- issue of subordinated liabilities €9.98 million.

4 Financial risk management (continued)

4.7 Capital management – regulatory capital (continued)

The Bank has complied with all externally imposed capital requirements throughout the year.

The Bank's regulatory capital position was as follows:

	2014	2013
	€000	€000
Common Equity Tier 1		
Share capital	**98,050**	62,350
Share premium	**13,464**	13,464
Retained earnings brought forward	**191**	708
Profit for the year	**19,305**	20,483
Shareholders' contribution	**9,750**	8,500
Reserve for general banking risk	**91**	-
Fair value reserve	**(5,691)**	9,578
Intangible assets	**(128)**	(228)
Investment in subsidiaries	**(1)**	(65)
Other reserves	**(5,018)**	(3,429)
	130,013	111,361
Tier 2 Capital		
Subordinated liabilities	**22,385**	12,341
Total Own funds	**152,398**	123,702

Capital ratio

Regulatory capital as a % of total risk-weighted assets	**14.25%**	15.66%

5 Use of estimates and judgements

The preparation of the financial statements requires the directors to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities and the disclosure of contingent liabilities, at the end of the reporting period. However, uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods. These disclosures supplement the disclosures on the financial risk management (see note 4).

In the process of applying the Bank's accounting policies, the directors have made the following judgements, which have the most significant effect on the amounts recognised in these financial statements:

5.1 Financial assets and liabilities classification

In classifying financial assets as held-to-maturity, the Bank has determined that it has both the positive intention and ability to hold the assets until their maturity date as required by accounting policy 3.13.1.

5.2 Estimated cash flows

As part of the calculation of the effective interest rate for financial assets and liabilities carried at amortised cost, the Bank takes into account the estimated cash flows considering all contractual terms of the financial instrument (e.g. prepayment, call and similar options), but without inclusion of future credit losses.

In the case where an instrument gives the issuer the option to require the instrument to be redeemed or cancelled early, and the terms of the instrument are such that it is not certain whether the option will be exercised, the probability for the option being exercised will be assessed in determining the estimated cash flows. In the case of held-to-maturity instruments with call options, the estimated cash flows reflect a redemption price at or above its carrying amount.

5.3 Allowances for credit losses

Assets accounted for at amortised cost are evaluated for impairment on the basis described in accounting policy 3.10.7. The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received as described in 5.2. In estimating these cash flows, management also considers the net realisable value of any underlying collateral.

5 Use of estimates and judgements (continued)

5.3 Allowances for credit losses (continued)

Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and advances and investment securities when there is objective evidence to suggest that they contain impaired loans and advances, but individually impaired items cannot yet be identified. In assessing the need for collective loss allowances, management considers factors such as credit quality, portfolio size, concentrations and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical experience (including loss emergence periods) and current economic conditions. The accuracy of the allowances depends on the estimates of future cash flows for specific counterparty allowances and the model assumptions and parameters used in determining collective allowances.

5.4 Effectiveness testing under Hedge Accounting

The following effectiveness tests are performed under Hedge Accounting:

- A prospective effectiveness test: This is a forward-looking test of whether a hedging relationship is expected to be highly effective against market moves.
- A retrospective effectiveness test: This is a backward-looking test of whether a hedging relationship has actually been highly effective over a period: This is specifically defined in terms of an effectiveness ratio between 80% and 125%.

The Bank assesses the effectiveness under the dollar offset methodology; this is a quantitative method that compares the change in fair value or cash flows of the hedging instrument with the change in fair value or cash flows of the hedged Item attributable to the hedged risk. The dollar offset method is performed using different approaches, as follows:

- Prospective effectiveness testing uses the sensitivity analysis approach. This method consists of measuring the effect of a hypothetical shift in the underlying hedged risk (for example, a 1% shift in the yield curve of the interest rate being hedged) on both the hedging Instrument and the hedged Item. Interest rates used in the prospective effectiveness test represent a reasonable proxy for the cost of funding. Bonds were modelled with coupons adjusted down by their credit spreads consistent with the aim of hedging purely the interest rate component of their price risk.
- Retrospective effectiveness testing uses the hypothetical derivative approach, which compares the change in the fair value or cash flows of the hedging Instrument with the change in the fair value or cash flows of a hypothetical derivative matching the terms of the hedged item. Valuations of both the hedging instruments themselves and the hypothetical derivatives are calculated using a market-standard approach.

6 Financial assets and liabilities

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Bank determines fair values using other valuation techniques.

For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

6.1 Valuation

The tables shown in section 6.2 and 6.3 below analyse recurring fair value measurements for financial assets and financial liabilities. These fair value measurements are categorised into different levels in the fair value hierarchy which reflects the significance of the inputs used in making the valuation. The different levels are defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities that the Bank can access at the measurement date.

- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data. Financial instruments which are generally included in this category include less liquid debt securities and over-the-counter derivatives where the fair value is based on observable inputs.

- Level 3: unobservable inputs for the asset or liability. This category includes instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Valuation techniques include net present value and discounted cash flow models and comparison with similar instruments for which market observable prices exist. Assumptions and inputs used in valuation techniques include benchmark interest rates, credit spreads, bond prices and expected price volatilities and correlations.

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

6 Financial assets and liabilities (continued)

6.2 Financial instruments measured at fair value – fair value hierarchy

The following table analyses financial instruments measured at fair value at 31 March 2014, by the level in the fair value hierarchy into which the fair value measurement is categorised. The amounts are based on the values recognised in the Statement of Financial Position.

At 31 March 2014

	Level 1	Level 2	Level 3	Total
	€000	€000	€000	€000
Assets				
Investments				
- Available-for-sale	485,471	6,101	-	491,572
- Equity instruments	2,474	-	-	2,474
Derivative assets held for trading	404	-	-	404
Derivative assets held for risk management	-	404	-	404
Total financial assets carried at fair value	**488,348**	**6,505**	**-**	**494,854**
Liabilities				
Derivative liabilities held for risk management	-	2,973	-	2,973
Total financial liabilities carried at fair value	**-**	**2,973**	**-**	**2,973**

At 31 March 2013

	Level 1	Level 2	Level 3	Total
	€000	€000	€000	€000
Assets				
Investments				
- Available for sale	1,116,825	90,665	-	1,207,490
Derivative assets held for risk management	-	1,152	-	1,152
Total	**1,116,825**	**91,817**	**-**	**1,208,642**
Liabilities				
Derivative liabilities held for risk management	-	-	-	-
Total	**-**	**-**	**-**	**-**

As at 31 March 2014 and at 31 March 2013, the fair value of the available-for-sale (AFS) investment securities represents closing bid price quoted in an active market. These are classified as Level 1, with the exception of investments securities reclassified to AFS in prior year as described in note 17.9, which are classified as Level 2, under the fair value hierarchy in accordance with IFRS 7.

6 Financial assets and liabilities (continued)

6.2 Financial instruments measured at fair value – fair value hierarchy (continued)

Level 2 includes fair value of:

- Investment securities that are valued on the basis of price quotations from an orderly transaction between market participants provided by reputable dealers; and

- Derivatives held for risk management that are based on valuation models and the methodology is to calculate the net present value of a series of expected cash flows, taking into account the different terms of each specific contract/instrument (discounted cash flow – DCF). These models use as their basis independently sourced market parameters including, for example, interest rate yield curves. Market parameters are either directly observable or are implied from instrument prices. The model may perform numerical procedures in the pricing such as interpolation when input values do not directly correspond to the most actively traded market trade parameters.

6.3 Financial instruments not measured at fair value

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorised.

At 31 March 2014

	Level 1	Level 2	Level 3	Total fair values	Total carrying amount
	€000	€000	€000	€000	€000
Assets					
Investment securities at amortised cost	851,386	147,790	-	999,176	983,894
Total	**851,386**	**147,790**	**-**	**999,176**	**983,894**
Liabilities					
Debt securities in issue	14,860	-	-	14,860	14,341
Subordinated liabilities	22,628	-	-	22,628	22,385
Total	**37,488**	**-**	**-**	**37,488**	**36,726**

6 Financial assets and liabilities (continued)

6.3 Financial instruments not measured at fair value (continued)

At 31 March 2013

	Level 1 €000	Level 2 €000	Level 3 €000	Total fair values €000	Total carrying amount €000
Assets					
Investment securities at amortised cost	175,246	163,365	-	338,611	356,544
Total	**175,246**	**163,365**	**-**	**338,611**	**356,544**
Liabilities					
Debt securities in issue	16,302	-	-	16,302	15,664
Subordinated liabilities	12,931	-	-	12,931	12,341
Total	**29,233**	**-**	**-**	**29,233**	**28,005**

Investment securities in inactive markets are based on:

- quoted prices of similar instruments, performing numerical procedures such as interpolation when input values do not directly correspond to the most actively traded market trade parameters; or
- price quotations from an orderly transaction between market participants provided by reputable dealers.

The majority of the 'loans and advances to financial institutions' amounting to €87.714 million (2013: €20.131 million) re-price or mature in less than one year hence their fair value is not deemed to differ materially from their carrying amount at the reporting date.

Loans and advances to customers – retail amounting to €2.819 million (2013: €2.574 million) approximates their fair value because they are re-pricable at the Bank's discretion.

The fair value of 'loans and advances to customers - corporate' with a carry value of €568.325 million (2013: € 399.600 million), net of impairment, and 'debt securities in issue through funding structure' €215.786 million (2013: € nil) cannot be reliably measured due to:

- insufficient publicly available information;
- inactive market; and
- reliable broker quotes are negotiated on a one-to-one basis.

6 Financial assets and liabilities (continued)

6.3 Financial instruments not measured at fair value (continued)

Notwithstanding this, the carrying amount of loans and advances to customers – corporate at the reporting date is deemed a fair approximation of their fair value on the basis that:

- all 'loans and advances to customers – corporate' have a short re-pricing maturity of less than 6 months hence any changes in fair value from market risk will be reflected in the carry value;
- terms and conditions of these loans generally contain interest rate adjustment covenants that provide for changes in interest rate receivable linked to the borrowers' performance and debt levels; and
- credit risk deterioration is assessed and reflected in the carry value as part of the impairment assessment process (Notes 3.10.7, 16.9). Specific impairment allowance of €1.422 million (2013: nil) is disclosed in note 4.3.3.

The Bank does not have the intention to dispose the 'loans and advances to customers – corporate' in the short term and disposal of such instruments is only performed after due consideration is provided on a case by case basis of the underlying commercial viability. Loans and advances amounting to a carry value of €92.917 million were disposed during the year realising profits of €2.615 million.

The majority of the 'amounts owed to financial institutions' amounting to €1.009 billion (2013: €1.369 billion) re-price or mature in less than one year hence their fair value is not deemed to differ materially from their carrying amount at the reporting date. 'Amounts owed to customers' amounting to €776.715 million (2013: €566.047 million) are substantially local deposits where the interest rate market is stable.

6.4 Transfers between levels

The Bank recognised transfer between levels of the fair value hierarchy as of the end of the reporting period during which the transfer has occurred. There were no transfers between Level 1 to Level 2 of the fair value hierarchy during the year ended 31 March 2014.

7 Net interest income

	2014	2013
	€000	€000
Interest income		
Investment securities	**34,847**	36,621
Loans and advances to customers	**29,660**	14,191
Loans and advances to financial institutions	**60**	133
	64,567	50,945
Interest expense		
Amounts owed to customers	**23,435**	17,085
Amounts owed to financial institutions	**4,079**	8,995
Debt securities in issue	**6,075**	1,588
	33,589	27,668
Net interest income	**30,978**	23,277

7.1 Included within loans and advances to customers under interest income for the year ended 31 March 2014 is a total of €0.904 million (2013: €0.339 million) relating to impaired financial assets.

7.2 Included within interest income are fair value losses of €7.303 million (2013: €16.813 million) on derivatives held in a fair value hedge relationship and €7.443 million (2013: €17.282 million) representing net increases in the fair value of the hedged item attributable to the hedged risk. The gains and losses are included in the line item corresponding to where interest income on the hedged item is recognised.

8 Net fee and commission

	2014	2013
	€000	€000
Fee and commission income		
Transaction fee income	**491**	296
Corporate secured lending fees	**1,245**	330
Investment services fees	**142**	-
Underwriting fee income	**-**	300
	1,878	926
Fee and commission expense		
Transaction and custody fees	**832**	569
Corporate secured lending fees	**230**	1,537
Other	**182**	646
	1,244	2,752
Net fee and commission income/(expense)	**634**	(1,826)

8.1 The net fee and commission expense excludes amounts used in determining the effective interest rates on financial assets and financial liabilities that are not at fair value through profit or loss but includes income of €1.245 million (2013: €0.330 million) and expenses of €0.230 million (2013: €1.537 million) relating to such financial assets and liabilities.

9 Net trading income and other operating income

9.1 Net trading income

	2014	2013
	€000	€000
Foreign exchange income	**2,292**	1,111

Foreign exchange income includes gains from foreign exchange in retail.

9.2 Net income from other financial instruments at fair value through profit or loss

	2014	2013
	€000	€000
Derivative assets/liabilities held for risk management		
- interest rate related	**(209)**	3,812
- foreign exchange related	**(786)**	344
Derivative assets held for trading	**404**	-
Equity instruments at fair value through profit or loss	**2,474**	-
	1,883	4,156

9.3 Other operating income

	2014	2013
	€000	€000
Realised gains on disposal of investments	**24,914**	26,464
Realised gains on disposals of loans and advances	**2,615**	989
Realised gain on repurchase of debt securities issued through funding structure	**495**	-
Other income	**4**	81
	28,028	27,534

10 Administrative and other expenses

Administrative and other expenses include:

	2014	2013
	€000	€000
Operating lease charges (note 34)	**3,068**	1,891
Directors' fees (note 35.3)	**110**	110

Administrative and other expenses include fees charged by the Bank's auditors for the year and are as follows:

	Audit services	**Other assurances services**	**Tax advisory services**	**Other non-audit services**
	€000	**€000**	**€000**	**€000**
Year to 31 March 2014				
Auditors' remuneration	**72**	**58**	**10**	**26**
Year to 31 March 2013				
Auditors' remuneration	65	34	9	39

11 Personnel expenses

11.1 Personnel expenses incurred are analysed as follows:

	2014	2013
	€000	€000
Directors' emoluments:		
- salaries	**1,994**	2,190
- defined contribution social security costs	**8**	8
- other	**190**	190
Staff costs:		
- salaries	**11,034**	8,458
- defined contribution social security costs	**451**	246
- other	**108**	72
	13,785	11,164

11 Personnel expenses (continued)

11.2 The weekly average number of persons employed was as follows:

	2014	2013
	No.	No.
Executive and senior management	**14**	14
Other managerial, supervisory and clerical	**200**	139
Other	**10**	10
	224	163

11.3 The number of persons employed at the reporting date was as follows:

	2014	2013
	No.	No.
Management and administration	**227**	194

12 Income tax expense

12.1

	2014	2013
	€000	€000
Current tax expense	**11,091**	11,531
Deferred tax income	**(601)**	(467)
Income tax expense	**10,490**	11,064

12 Income tax expense (continued)

12.2 The income tax expense and the result of accounting profit multiplied by the tax rate applicable in Malta, the Bank's country of incorporation, are reconciled as follows:

	2014	2013
	€000	€000
Profit for the year	**19,396**	20,483
Income tax expense	**10,490**	11,064
Profit before income tax	**29,886**	31,547
Tax at the applicable rate of 35%	**10,460**	11,041
Tax effect of:		
Tax-exempt income	**(72)**	-
Non-deductible expenses	**102**	23
Income tax expense	**10,490**	11,064

13 Earnings per share

The calculation of the Bank's basic earnings per share for the financial year ended 31 March 2014 and 31 March 2013 was based on the profit attributable to ordinary shareholders and a weighted average number of ordinary shares outstanding.

	2014	2013
	No.	No.
Weighted average number of ordinary shares ('000)	**86,534**	56,324

The calculation of the Bank's adjusted basic earnings per share for the financial year ended 31 March 2014 and 31 March 2013 was based on the profit attributable to ordinary shareholders and a weighted average number of ordinary shares outstanding and 19,400,000 shares issued after year end. Accordingly, the adjusted weighted average number of ordinary shares for 31 March 2013 has been restated to include €21 million shares and €19.4 million bonus issue of shares.

	2014	2013
	No.	No.
Adjusted weighted average number of ordinary shares ('000)	**105,934**	96,724

13 Earnings per share (continued)

	2014	2013
	€000	€000
Profit for the year attributable to ordinary shareholders	19,396	20,483

	2014	2013
Earnings per share (cents)	22c	36c
Adjusted earnings per share (cents)	18c	21c

14 Balances with Central Bank of Malta, treasury bills and cash

14.1

	2014	2013
	€000	€000
Balances with Central Bank of Malta	11,910	28,956
Malta Government Treasury Bills	5,997	40,892
Cash	184	207
	18,091	70,055

14.2 Balances with Central Bank of Malta include a reserve deposit of the Bank in terms of Regulation (EC) No 1745/2003 of the European Central Bank amounting to €3.533 million, (2013: €3.074 million) bearing interest at 0.25% (2013: 0.75%) per annum and an overnight deposit amounting to €7.122 million (2013: €25.0 million) bearing no interest (2013: no interest) per annum.

14.3 The Balances with Central Bank of Malta also include a balance of €1.255 million (2013: €0.857 million) which is pledged in favour of the Depositor Compensation Scheme ("DCS") in terms of the Depositor Compensation Scheme Regulations (Subsidiary Legislation, 371.09) of the Laws of Malta.

As at 31 March 2014, in connection with the DCS, investment securities with a carrying amount of €3.822 million (2013: €2.603 million), nominal value €3.500 million (2013: €2.475 million) and a fair value of €3.832 million (2013: €2.678 million) as at 31 March 2014, are pledged in favour of the DCS.

14.4 Malta Government Treasury Bills amounting to €5.997 million (2013: €40.892 million) are expected to be recovered within twelve months after the reporting date.

15 Loans and advances to financial institutions

15.1 Balances

	2014	2013
	€000	€000
At amortised cost:		
Repayable on call and at short notice	**55,662**	8,434
Term loans and advances	**32,052**	11,697
	87,714	20,131

15.2 Balances of loans and advances to financial institutions up to €61,251 (2013: €69,578) are pledged in favour of other banks providing credit card facilities to customers.

15.3 An amount of €1 million (2013: €1 million) has been contributed to a clearing fund held by Eurex Clearing AG, of which the Bank is a member. The clearing fund protects members against losses until they leave the clearing fund.

15.4 Loans and advances to financial institutions as at 31 March 2014 and 31 March 2013 were neither past due nor impaired and there were no forbearance activities.

15.5 As at 31 March 2014, €3.452 million (2013: €7.303 million) are expected to be recovered after more than twelve months after the reporting date.

16 Loans and advances to customers

16.1 Balances

	2014	2013
	€000	€000
At amortised cost:		
Loans and advances: retail	**2,819**	2,574
Loans and advances: corporate	**570,619**	400,276
Less allowance for impairment (note 16.9)	**(2,294)**	(676)
	571,144	402,174

16.2 Loans and advances amounting to €10.473 million (2013: nil) were deemed to be impaired. Specific impairment recorded on these loans and advances amounted to €1.422 million (2013: nil) (note 16.9). No other customers as at 31 March 2014 and 31 March 2013, were deemed to be past due or impaired and there were no forbearance activities.

16.3 Loans and advances to customers: retail are secured by an equivalent amount of customer deposits, included in amounts owed to customers, with the exception of what is described in note 16.4. These deposits are pledged in favour of the Bank.

16.4 Loans and advances to customers: retail include a €17,017 loan sanctioned to a director of the Bank (2013: €100,000). This is secured by a general hypothec and carries an interest rate of 4.5% per annum.

16 Loans and advances to customers (continued)

16.5 As at 31 March 2014, €3.059 million (2013: €8.311 million) of "loans and advances to customers: corporate" and €0.324 million (2013: €0.105 million) of the "loans and advances to customers: retail" are expected to be recovered within 12 months after the reporting date.

16.6 The Bank has established a Collateralised Loan Obligation ("CLO") structure (note 29.3). As risks and rewards are deemed to have been retained by the Bank, €322.846 million (2013: nil) loans and advances to customers are still recognised on the Statement of Financial Position.

16.7 Similarly a number of loans and advances were transferred under a Total Return Swap ("TRS") Facility (note 27). As risks and rewards are deemed to have been retained by the Bank, €66.229 million (2013: €115.538 million), loans and advances to customers are still recognised on the Bank's Statement of Financial Position.

16.8 As at 31 March 2014, €27.7 million (2013: €1 million) of "loans and advances to customers: corporate" were contracted but beneficial ownership was not yet transferred and not recorded as purchases.

There were no contingent disposals as at 31 March 2014 (2013: €10 million) which were disposed but beneficial ownership of which was not yet transferred.

16.9 Allowances for impairment

	2014	2013
	€000	€000
Specific allowances for impairment		
Balance as at 1 April	**-**	-
Impairment charge for the year	**1,422**	-
Balance at 31 March	**1,422**	-
Collective allowances for impairment		
Balance as at 1 April	**676**	-
Impairment charge for the year	**196**	676
Balance at 31 March	**872**	676
Total allowances for impairment	**2,294**	676

17 Investments

	2014	2013
	€000	€000
Corporate	**293,235**	54,964
Treasury	**1,184,705**	1,509,070
	1,477,940	1,564,034

17.1 Analysed as follows:

	2014	2013
	€000	€000
Held-to-maturity investment securities	**983,894**	356,544
Available-for-sale investment securities	**491,572**	1,207,490
Equity instruments at fair value through profit or loss	**2,474**	-
	1,477,940	1,564,034

At 31 March 2014, €1.355 billion (2013: €1.492 billion) of investment securities are expected to be recovered after more than 12 months after the reporting date.

17.2 Held-to-maturity investment securities

17.2.1 Held-to-maturity investment securities net of collective impairment

	2014	2013
	€000	€000
Investment securities	**984,357**	356,544
Collective Impairment (note 4.3.3)	**(463)**	-
	983,894	356,544

17.2.2 Held-to-maturity investment securities by issuer

	2014	2013
	€000	€000
Government securities	**95,020**	65,542
Other securities	**888,874**	291,002
	983,894	356,544

17 Investments (continued)

17.3 Available-for-sale investment securities

	2014	2013
	€000	€000
Government securities	**11,054**	64,823
Other securities	**480,518**	1,142,667
	491,572	1,207,490

17.4 No evidence of specific impairment was identified on investment securities during year ended 31 March 2014.

17.5 The Bank has established a Collateralised Loan Obligation ("CLO") structure (note 29.3). As risks and rewards are deemed to have been retained by the Bank, €53.143 million (2013: nil) investment securities are still recognised on the Statement of Financial Position.

17.6 Similarly a number of securities were transferred under a Total Return Swap ("TRS") Facility (note 27). As risks and rewards are deemed to have been retained by the Bank, €33.346 million (2013: €4.733 million), investment securities are still recognised on the Bank's Statement of Financial Position.

17.7 Most of investment securities are pledged as collateral against the provision of borrowing facilities (note 27), except a carry value of €327.728 million (2013: €111.200 million) which are free and unencumbered securities at 31 March 2014.

Cash value of unutilised borrowing facilities (headroom) at 31 March 2014 amounted to €213,647 million (2013: €113.039 million).

17.8 As at 31 March 2014, the Bank has no commitment (2013: €75 million) to purchase further investment securities.

17.9 Reclassifications out of Held-to-Maturity (HTM) Investment Securities

A number of investment securities were identified for reclassification due to isolated and non-recurring events which could not have been reasonably anticipated. During the year ending 31 March 2014, the Bank reclassified HTM investments to AFS and sold HTM investments.

The events that caused the Bank to reclassify or sell included:

- unexpected withdrawal of eligibility for ECB repo financing that could not reasonably have been foreseen when the investments were originally classified as HTM and that has significantly altered the economic rationale at time of acquisition amounting to €25.159 million (2013: €163.967 million).

- significant credit deterioration in the issuer's creditworthiness since acquisition that could have not been anticipated when the investment was acquired amounting to €12.933 million (2013: Nil). There were no default events on the reclassified HTM positions. No specific impairment provisions were deemed necessary.

All the reclassified HTM investments during the year were disposed of at 31 March 2014.

17 Investments (continued)

17.10 Equity instruments at fair value through profit or loss

	2014	2013
	€000	€000
Unlisted equities issued by a European corporation	**2,474**	-

18 Derivative assets and liabilities held for risk management

18.1 Derivative assets and liabilities held for risk management

	31 Mar 2014		31 Mar 2013	
	Assets	**Liabilities**	Assets	Liabilities
	€000	**€000**	€000	€000
Instrument type:				
Interest rate swaps	**-**	**2,798**	279	-
Interest rate swaptions	**404**	**-**	-	-
Foreign exchange swaps	**-**	**175**	873	-
	404	**2,973**	1,152	-

18.2 The Bank established derivative lines with counterparties to purchase interest rate caps, swaps and swaptions, futures and other appropriate instruments approved for hedging interest rate risk.

18.3 The Bank uses over-the-counter interest rate swaps to hedge its exposure to changes in the fair values of its fixed rate AFS securities attributable to changes in market interest rates. Interest rate swaps are matched to fixed rate AFS securities. Such derivatives are not held for trading purposes and are classified at fair value through profit or loss and are designated in a fair value hedging relationships.

18.4 The Bank uses over the counter cross currency swaps to hedge its exposure to changes in the foreign exchange rates. Such derivatives are not held for trading purposes and are classified at fair value through profit or loss. All cross currency swaps have a maturity of less than three months.

18 Derivative assets and liabilities held for risk management (continued)

18.5 The fair values of derivatives designated as fair value hedges and the related notional amounts analysed by their remaining life, are as follows:

	2014	2013
	€000	€000
Derivative financial instruments designated as fair value hedges		
Interest rate swaps: (liability) / asset	**(2,798)**	279
Notional Amounts		
More than 1 year	**500,000**	900,000

19 Derivative assets held for trading

19.1

	2014	2013
	€000	€000
Other instruments at fair value through profit or loss	**404**	-

19.2 Derivative assets held for trading represent warrants with a maturity of over five years.

20 Investment in subsidiaries

20.1

Name of the subsidiary	Incorporated in	Nature of business	Current equity interest %	2014 €	2013 €
Mediterranean Global Advisory SA	Switzerland	Liquidated/ Dormant	wholly owned	**-**	63,086
Mediterranean Research Limited	United Kingdom	Dormant	wholly owned	**2**	2
Medifin Estates (partnership)	Malta	Operating lease of branches	97%	**1,450**	1,450
				1,452	64,538

20.2 During the year ended 31 March 2014, Mediterranean Global Advisory SA, a company which was incorporated (and domiciled) in Switzerland and wholly owned by the Bank, was liquidated. This resulted in a loss of €4,925 recognised as impairment in the Statement of Comprehensive Income.

20.3 Mediterranean Research Limited was liquidated on 2 May 2014. The operations of Mediterranean Research Limited are being carried out by the Bank. Notwithstanding this, no impairment is deemed necessary.

20.4 Medifin Estates is a partnership set up on 5 June 2012. The subsidiary enters into operating leases for property to be used as branches which are leased back to the Bank.

20.5 On 11 April 2014, the Bank entered into an agreement to acquire Volksbank Malta Limited (note 37.2).

21 Property and equipment

21.1

	Improvements to premises	Computer equipment	Other equipment	Fixtures and fittings	Motor vehicles	Total
	€000	€000	€000	€000	€000	€000
Cost						
At 1 April 2012	1,104	2,206	223	994	175	4,702
Acquisitions	-	14	5	371	39	429
Disposal	-	-	-	(3)	-	(3)
At 31 March 2013	1,104	2,220	228	1,362	214	5,128
At 1 April 2013	1,104	2,220	228	1,362	214	5,128
Acquisitions	-	90	-	71	10	171
Disposal	-	-	-	(14)	-	(14)
At 31 March 2014	**1,104**	**2,310**	**228**	**1,419**	**224**	**5,285**
Depreciation						
At 1 April 2012	596	516	91	477	142	1,822
Charge for the year	115	538	59	95	15	822
Release on disposal	-	-	-	(1)	-	(1)
At 31 March 2013	711	1,054	150	571	157	2,643
At 1 April 2013	711	1,054	150	571	157	2,643
Charge for the year	118	385	47	175	18	743
Release on disposal	-	-	-	(9)	-	(9)
At 31 March 2014	**829**	**1,439**	**197**	**737**	**175**	**3,377**
Carrying amounts						
At 31 March 2012	508	1,690	132	517	33	2,880
At 31 March 2013	393	1,166	78	791	57	2,485
At 31 March 2014	**275**	**871**	**31**	**682**	**49**	**1,908**

21.2 The Bank operates from nine immovable properties which are held under operating lease agreements (see note 34).

21.3 There were no capitalised borrowing costs related to the acquisition of property and equipment during the period (2013: nil).

21.4 There was no property and equipment not put in use at the reporting date.

22 Intangible assets

22.1

	Software
	€000
Cost:	
At 1 April 2012	1,744
At 31 March 2013	1,744
Acquisitions	34
At 31 March 2014	**1,778**
Amortisation:	
At 1 April 2012	1,393
Charge for the year	123
At 31 March 2013	1,516
Charge for the year	134
At 31 March 2014	**1,650**
Carrying amounts:	
At 31 March 2012	351
At 31 March 2013	228
At 31 March 2014	**128**

22.2 There were no capitalised borrowing costs related to the acquisition of software during the year (2013: nil).

22.3 There were no intangible assets not in use at the reporting date.

23 Other assets

23.1

	2014	2013
	€000	€000
Amount receivable from:		
Immediate parent company	**1,497**	1,484
Subsidiary	**-**	20
Other sister companies	**16,648**	11,319
Other assets	**744**	775
	18,889	13,598

23.2 Amounts receivable from immediate parent company, subsidiary and other sister companies are interest free, unsecured and repayable on demand.

24 Prepayments and accrued income

	2014	2013
	€000	€000
Prepayments	**1,780**	1,570
Deferred expense	**2,317**	2,648
Accrued income	**19,164**	23,778
	23,261	27,996

25 Deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2014	2013	**2014**	2013	**2014**	2013
	€000	€000	**€000**	€000	**€000**	€000
Property and equipment	**-**	-	**(265)**	(309)	**(265)**	(309)
Available-for-sale securities	**3,064**	-	**-**	(5,161)	**3,064**	(5,161)
Tax losses carry forward	**-**	170	**-**	-	**-**	170
Impairment allowances	**965**	238	**-**	-	**965**	238
	4,029	408	**(265)**	(5,470)	**3,764**	(5,062)

	Balance 01 Apr 13	Recognised in profit or loss	Recognised in equity	Balance 31 Mar 14
	€000	€000	€000	**€000**
Property and equipment	(309)	44	-	**(265)**
Available-for-sale securities	(5,161)	-	8,225	**3,064**
Tax losses carry forward	170	(170)	-	**-**
Impairment allowances	238	727	-	**965**
	(5,062)	601	8,225	**3,764**

	Balance 01 Apr 12	Recognised in profit or loss	Recognised in equity	Balance 31 Mar 13
	€000	€000	€000	€000
Property and equipment	(368)	59	-	(309)
Available-for-sale securities	612	-	(5,773)	(5,161)
Tax losses carry forward	-	170	-	170
Impairment allowances	-	238	-	238
	244	467	(5,773)	(5,062)

26 Capital and reserves

26.1.1 Share capital

	2014	2013
	No.	No.
Issued and fully paid up:		
Shares of €1 each		
Ordinary 'A' shares	**98,050,106**	62,350,106
Ordinary 'B' share	**1**	1
	98,050,107	62,350,107

26.1.2 Movement in authorised and issued share capital

At 31 March 2014 and 31 March 2013, the authorised share capital consisted of 100,000,000 ordinary shares of €1 each. All issued shares are fully paid-up.

		2014	2013
Fully paid up	**Notes**	**€000**	€000
At beginning of year		**62,350**	56,030
Issued for cash during the year	26.1.4/26.1.5	**14,700**	6,320
Bonus issue	26.1.5	**21,000**	-
At end of year		**98,050**	62,350

26.1.3 Rights and entitlements attached to ordinary shares

The holders of 'A' ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Bank. 'B' ordinary shareholders are not entitled to vote or to receive any dividends distributed.

26.1.4 Increase in issued share capital during year ended 31 March 2013

Furthermore, during the year ended 31 March 2013, by an extraordinary resolution dated 15 March 2013, it was resolved to increase the issued share capital by 6,320,000 ordinary shares to 62,350,107 issued ordinary shares of €1 each.

26.1.5 Increases in issued share capital during year ended 31 March 2014

The directors' proposal for a final net ordinary dividend of €21 million representing €0.33 per share as bonus shares for the year ended 31 March 2013 was approved on 9 May 2013 and executed on 10 May 2013.

As at 30 October 2013, the Bank's issued share capital was increased by €4.9 million ordinary A shares divided into four million nine hundred thousand shares each with a nominal value of one Euro (€1). These were paid in cash, thereby increasing the Bank's issued share capital from €83.3 million to €88.2 million.

26 Capital and reserves (continued)

26.1.5 Increases in issued share capital during year ended 31 March 2014 (continued)

On 27 November 2013, the Bank's shareholders resolved to increase the Bank's share capital, on 28 November 2013, by €9.8 million ordinary A shares divided into nine million eight hundred thousand shares, each with a nominal value of one Euro (€1), through a cash contribution, thereby increasing the Bank's issued share capital from €88.25 million to €98.05 million.

26.1.6 Increases in authorised share capital after the reporting date

On 3 April 2014, by an extraordinary resolution of the shareholders of the Bank, it was resolved to increase the authorised share capital of the Bank by €200 million, up to €300 million.

26.2 Share premium

Share premium as at the reporting date represents the issue of shares as follows:

Issue date	Number of shares	Premium	Share premium
	No.	€	€000
10 August 2010	10,000,000	0.9155	9,155
29 September 2010	19,119,470	0.2254	4,309

			13,464
			=====

26.3 Shareholders' contribution

During the year ended 31 March 2013, by an extraordinary resolution dated 27 March 2013, it was resolved to provide the Bank a shareholders' net contribution of €8.5 million (€9.3 million less repayment during the year ended 31 March 2013 amounting to €0.8 million).

Furthermore, by an extraordinary resolution dated 28 June 2013, it was resolved to provide the Bank a shareholders' contribution of €1.25 million.

The following terms and conditions of the contribution granted renders this instrument to be equity in nature in accordance with the requirements of IAS 32: Financial Instruments - Presentation:

- The Bank has no obligation to bear any servicing cost or transfer any economic benefits of any kind to the Contributor or any other person in return; and

- The Bank has no obligation to repay the Contributions.

The Contribution is also eligible as Own Funds in terms of the new Capital requirements.

26 Capital and reserves (continued)

26.4 The fair value reserve includes the cumulative net change in the fair value of available-for-sale investments, excluding impairment losses, until the investment is derecognised, net of deferred taxation.

26.5 In accordance with the Revised Banking Rule BR/09/2013, credit institutions are required to maintain a reserve for General Banking Risks against non-performing loans to create an additional Pillar 2 buffer. The Bank's reserve was transferred out of the retained earnings. This reserve is distributable if the formal consent of the regulator is obtained. The reserve represents 40% of the regulatory allocation by virtue of paragraphs 38 and 57 of the Banking Rule. The remaining 60% will be split and set aside equally over a period of two years in terms of the Banking Rule. The reserve amounts to €90,327.

26.6 All reserves at the reporting date, except for retained earnings and the shareholders' contribution, are non-distributable. However, the shareholders' contribution reserve is distributable only and only if, the regulatory ratios are not breached and if the terms and conditions permit, as noted in note 26.3.

26.6 Dividends

	2014	2013	**2014**	2013
	% per share	% per share	**€000**	€000
Gross of income tax:				
% per €1 share				
- interim	**-**	18	-	10,994

	2014	2013	**2014**	2013
	cents per share	cents per share	**€000**	€000
Net of income tax:				
cent per €1 share				
- interim	**-**	11	**-**	7,146

The directors have proposed a final net ordinary dividend of €0.20 (2013: €0.33) per share as bonus shares.

27 Amounts owed to financial institutions

	2014	2013
	€000	€000
Repayable on call and at short notice	**13,651**	20,570
Term loans and advances	**995,325**	1,348,425
	1,008,976	1,368,995

27.1 An amount of €928 million (2013: €1,259 million) from term loans and advances are secured by a pledge over the investments (excluding Equity instruments) (note 17).

27.2 An amount of €67 million (2013: €46 million) from term loans represents total return swap payables which are recognised in the Bank's Statement of Financial Position by virtue of the Bank retaining the risks and rewards in the underlying portfolio of loans and advances to customers and investments (notes 16 and 17).

28 Amounts owed to customers

	2014	2013
	€000	€000
Repayable on demand	**176,285**	140,399
Term deposits	**600,430**	425,648
	776,715	566,047

29 Debt securities in issue

29.1

	Note	**2014**	2013
		€000	€000
At amortised cost:			
Debt securities in issue	29.2	**14,341**	15,664
Debt securities in issue through funding structure	29.3	**215,786**	-
		230,127	15,664

29.2 Debt Securities in issue

29.2.1 Movement in Debt securities in issue

	2014	2013
	€000	€000
Balance at the beginning of the year	**15,664**	19,672
Debt securities repurchased and cancelled	**(1,365)**	(4,095)
Transaction cost amortised	**42**	87
Balance at end of year	**14,341**	15,664

29.2.2 The debt securities, which are unsecured, are denominated in Euro, mature on 30 October 2015 and are listed on the Malta Stock Exchange. The interest payable is fixed at 6.25% per annum and the debt securities are redeemable at their nominal value.

29 Debt securities in issue (continued)

29.2.3 The above liabilities will in the event of default or insolvency of the Bank, have a general claim on the assets of the Bank pari passu with other unsecured creditors. Bondholders therefore would rank after all interbank funding lines and repurchase agreements that are collateralised by investments securities through the said funding.

29.2.4 Movement in debt securities - repurchase

During the year ended 31 March 2014, the Bank purchased through market operations a nominal value of €1,403,000 (2013: €4,095,200) of its 6.25% debt securities in issue, for cancellation in accordance with the provisions of section 7.9.8 of the Security Note forming part of the prospectus dated 13 September 2010 (as supplemented on 30 May 2011). All bonds so purchased by the Bank were cancelled.

As at 31 March 2013, the contractual amount due at maturity is €14,539,600 (2013: €15,904,800).

29.2.5 The carrying amount of the debt securities in issue is €198,600 lower than the contractual amount due at maturity (2013: €240,798).

29.2.6 The Bank has not had any defaults of interest or other breaches with respect to its debt securities in issue during the years ended 31 March 2014 and 31 March 2013.

29.3 Debt securities in issue through funding structure

29.3.1 Movement in Debt securities through funding structure

	2014	2013
	€000	€000
Balance at the beginning of the year	**-**	-
Debt securities issued	**240,000**	-
Debt securities repurchased and derecognised	**(22,000)**	-
Transaction costs	**(2,633)**	-
Transaction costs amortised to profit or loss	**419**	-
Balance at end of year	**215,786**	-

29.3.2 During the year ended 31 March 2014, as part of the funding strategy, the Bank established a collateral loan obligation in Netherlands: Grand Harbour I B.V.

The Bank has been assessed to have retained all risks and rewards of the structure.

29 Debt securities in issue (continued)

29.3 Debt securities in issue through funding structure (continued)

29.3.3 The funding structure has issued the following notes, maturing in 2026:

- €240 million Class A1 Senior Secured Floating Rate Notes;
- €15 million Class A2 Senior Secured Floating Rate Notes;
- €35 million Class B Senior Secured Deferrable Floating Rate Notes;
- €22.5 million Class C Senior Secured Deferrable Floating Rate Notes;
- €32.5 million Class D Senior Secured Deferrable Floating Rate Notes;
- €10 million Class E Senior Secured Deferrable Floating Rate Notes;
- €48.35 million Subordinated Notes.

Of these notes, the €240 million Class A1 notes were issued to third parties, with the remaining €163.35 million being retained by the Bank.

In view of the Bank holding 40.50% of the funding of the structure, and in particular, the holding of the mezzanine and the subordinated notes, the Bank is deemed to have retained substantially all risks and rewards of the structure. It is the intention of the Bank to retain all the mezzanine and subordinated notes.

29.3.4 During July 2013, the Bank repurchased €22 million of the Senior Secured Floating Rate notes. An amount of €0.419 million transaction costs has been amortised to profit or loss.

29.3.5 The Bank did not have any defaults of interest or other breaches with respect to its debt securities in issue through the funding structure during the year ended 31 March 2014.

29.3.6 It is expected that the Debt securities issued through funding structure will be repaid within five years from date of issue.

30 Subordinated liabilities

30.1 *Movement in balance*

	2014	2013
	€000	€000
At amortised cost:		
Balance at the beginning of the year	**12,341**	-
Issue of subordinated liabilities		
- nominal value (note 30.2)	**9,984**	12,500
- related transaction costs	**(77)**	(90)
- effect of foreign exchange revaluation	**96**	(69)
- transaction costs amortised to profit or loss	**41**	-
Balance at the end of the year	**22,385**	12,341

30 Subordinated liabilities (continued)

30.2 During June 2013, the Bank issued an additional euro equivalent of €10 million of 7.50% Subordinated bonds due 2019. The debt securities, which are unsecured, mature on 30 December 2019 and are listed on the Malta Stock Exchange. The interest payable is fixed at 7.50% per annum (effective interest rate 7.60%) and is redeemable at their nominal value. During December 2013 these subordinated bonds were merged with the euro equivalent of €12.5 million bonds that were originally issued on 21 November 2012.

30.3 The above liabilities will, in the event of the winding-up of the issuer, be subordinated to the claims of depositors and all other creditors of the issuer. The Bank has not had any defaults of interest or other breaches with respect to its subordinated debt securities during the year ended 31 March 2014.

30.4 As at 31 March 2014, the euro equivalent contractual amount due at maturity is €22.512 million (2013: €12.431 million).

30.5 The carrying amount of the subordinated debt securities in issue is €127 thousand (2013: €90 thousand) lower than the contractual amount due at maturity.

31 Other liabilities

	2014	2013
	€000	€000
Other liabilities	**569**	760
VAT payable	**540**	340
	1,109	1,100

32 Accruals

	2014	2013
	€000	€000
Accrued expenses	**5,791**	4,124
Accrued interest expense	**9,618**	5,842
	15,409	9,966

33 Cash and cash equivalents

Balances of cash and cash equivalents as shown in the statements of cash flows are analysed below:

	2014	2013
	€000	€000
Analysis of cash and cash equivalents:		
Cash in hand	**184**	207
Call deposits	**62,784**	33,387
Repayable on call and at short notice	**(13,651)**	(20,570)
Amounts owed to financial institutions with maturity less than 3 months	**(174,563)**	(588,846)
Per Statement of Cash Flows	**(125,246)**	(575,822)
Adjustment to reflect:		
Balance with Central Bank of Malta	**4,788**	3,934
Malta Government treasury bill with original maturity over 3 months	**5,997**	40,892
Deposits with maturity over 3 months	**32,052**	11,767
Amounts owed to financial institutions with maturity over 3 months	**(820,762)**	(759,580)
Per Statement of Financial Position	**(903,171)**	(1,278,809)

33 Cash and cash equivalents (continued)

	Notes	2014	2013
		€000	€000
Analysed as follows:			
Balances with Central Bank of Malta, treasury bills and cash	14	**18,091**	70,055
Loans and advances to financial institutions	15	**87,714**	20,131
Amounts owed to financial institutions	27	**(1,008,976)**	(1,368,995)
		(903,171)	(1,278,809)

34 Operating leases

The Bank leases a number of branches and office premises under operating leases. The leases typically run for 4 to 10 years, with an option to renew the lease after that date. Some operating lease agreements provide for additional rent payments that are based on changes in a local price index.

Furthermore, the Bank lease IT-infrastructure and software from a related company. The lease term is renewable on a one-year rolling period.

At the end of the reporting year, the future minimum lease payments under non-cancellable operating leases are payable as follows:

	2014	2013
	€000	€000
Within one year	**1,469**	1,039
After one year but not more than five years	**1,873**	1,638
More than five years	**1,088**	608
	4,430	3,285

The amount of operating lease expenses recognised in profit or loss for the year is disclosed in note 10.

35 Related parties

35.1 Immediate and ultimate parent company

The Bank is a wholly owned subsidiary of Medifin Holding Limited. The registered office of the parent company is situated at 10, St. Barbara Bastion, Valletta, Malta.

Medifin Holding Limited prepares consolidated financial statements of the Group of which Mediterranean Bank plc and its subsidiaries form part. These financial statements will be filed and available for public inspection at the Registrar of Companies in Malta.

The ultimate parent company is AnaCap Financial Partners II L.P. Their registered office is situated at Carinthia House, 9 -12 The Grange, St Peter Port, GY1 4BF, Guernsey.

35.2 Transactions with key management personnel

In addition to their salaries (note 11), the Bank also provides non-cash benefits to directors, relating to gross rent payable on accommodation based in Malta and health and life insurance premiums paid by the Bank amounting €190,258 (2013: €189,507).

35.3 Related party balances and transactions

During the course of its business, the Bank conducted business on commercial terms with various related parties.

The following table provides the total amount of transactions and balances, which have been entered into with related parties for the relevant financial year:

35 Related parties (continued)

35.3 Related party balances and transactions (continued)

31 March 2014

Related party	Income from related parties	Expenses charged by related parties	Amounts owed by related parties	Amounts owed to related parties	Transaction type
	€000	€000	€000	€000	
Immediate parent					
	-	-	1,497	-	Other assets
	-	-	-	113	Amounts owed to customers
	6	-	-	-	Fee and commission income
Ultimate parent					
	-	168	-	-	Monitoring fees
Subsidiaries					
	-	-	-	397	Amounts owed to customers
	-	-	-	52	Other liabilities
	-	16	-	-	Interest expense
	-	167	-	-	Administration expenses
	-	5	-	-	Net impairment
Other Group companies					
	-	-	16,648	-	Other assets
	31	-	-	-	Fee and commission income
	-	4,162	-	-	Operating lease expense
	-	-	-	1,842	Amounts owed to customers
	-	17	-	-	Interest expense
Directors					
	-	-	17	-	Loans and advances to customers
	-	-	-	200	Amounts owed to customers
	-	110	-	-	Directors' fees
	1	-	-	-	Interest income
	-	1	-	-	Interest expense
	-	1,994	-	-	Personnel expenses

35 Related parties (continued)

35.3 Related party balances and transactions (continued)

31 March 2014

Related party	Income from related parties	Expenses charged by related parties	Amounts owed by related parties	Amounts owed to related parties	Transaction type
	€000	€000	€000	€000	
Other companies controlled by members of the Board					
	-	-	-	491	Amounts owed to customers
	-	18	-	-	Interest expense
	-	9	-	-	Administration expenses

Furthermore, as detailed in note 26:

- €21 million (2013: €7.146 million) were paid as dividends to the immediate parent which in turn re-invested €21 million (2013: €6.3 million) in ordinary A shares.
- the immediate parent invested €4.9 million and €9.8 million in ordinary A shares during October 2013 and November 2013 respectively.
- the immediate parent made a payment to the Bank as Shareholders' Contributions, amounting to €1.25 million (2013: €9.3 million less repayment of €0.8 million).

35 Related parties (continued)

35.3 Related party balances and transactions (continued)

31 March 2013

Related party	Income from related parties €000	Expenses charged by related parties €000	Amounts owed by related parties €000	Amounts owed to related parties €000	Transaction type
Immediate parent					
	-	-	1,484	-	Other assets
	-	-	-	353	Amounts owed to customers
Ultimate parent					
	-	176	-	-	Monitoring fees
Subsidiaries					
	-	-	-	79	Amounts owed to customers
	-	-	20	-	Other assets
	-	-	-	81	Other liabilities
	-	84	-	-	Administration expenses
Other Group companies					
	-	-	11,319	-	Other assets
	150	-	-	-	Fee and commission income
	-	1,349	-	-	Operating lease expense
	-	-	-	5,604	Amounts owed to customers
	-	2	-	-	Interest expense
Directors					
	-	-	100	-	Loans and advances to customers
	-	110	-	-	Directors' fees
	1	-	-	-	Interest income
	-	2,198	-	-	Personnel expenses

36 Segmental information

The Bank has a single reportable segment represented by the investment in EU sovereign and sovereign related credit, covered bonds, senior secured bonds, high yield bonds, syndicated loans and other similar credit quality instruments. Information about the product and services and geographical areas are set out in notes 4,16,17 and 20 to the financial statements which provide information about the financial risks, credit concentrations by sector and location and revenues from the single reportable segment. The investment portfolio is spread across a large number of exposures diversified in government, financial institutions and other corporates.

In presenting the geographic information below, segment revenues is based on the geographic location of the revenue generating assets.

31 March 2014	**Total €000**	**United Kingdom €000**	**France €000**	**Germany €000**	**Other €000**
Total operating income	63,815	20,505	14,039	3,307	25,964

31 March 2013	**Total €000**	**United Kingdom €000**	**France €000**	**Germany €000**	**Other €000**
Total operating income	54,252	17,560	17,736	942	18,014

37 Events after the reporting date

37.1 As described in notes 13 and 26, €19.4 million will be distributed from the retained earnings as a final dividend by way of a bonus share issue. This will transfer substantially all retained earnings as bonus shares.

37.2 On 11 April 2014, the Bank entered into an agreement with VB-Holding Aktiengesellschaft and Mithra Holding Gesellschaft m.b.H. to acquire 100% of the share capital of Volksbank Malta Limited ("Volksbank Malta") for cash consideration of €35.3 million. Mediterranean Bank has also agreed to refinance existing debt of Volksbank Malta to Österreichischen Volksbanken AG ("Voksbank Austria") as of the closing date.

37.3 As referred to in note 1, on 2 May 2014, Mediterranean Research Limited, a dormant subsidiary wholly owned by the Bank, was liquidated.

37.4 Subsequent to year end, the Bank bought back a further €71,500 nominal value of its 6.25% Bonds due 2015 through market operations.

38 Comparative amounts

Certain comparatives have been reclassified to conform with the current year's presentation.

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Independent Auditors' Report

To the Members of Mediterranean Bank plc

Report on the Financial Statements

We have audited the separate financial statements of Mediterranean Bank plc (the "Bank") as set out on pages 24 to 119, which comprise the statement of financial position as at 31 March 2014 and the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Directors' Responsibility for the Financial Statements

As explained more fully in the Directors' Responsibilities Statement set out on page 19, the directors are responsible for the preparation of financial statements that (a) give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU, and (b) are properly prepared in accordance with the provisions of the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act") and the Banking Act, 1994 (Chapter 371, Laws of Malta). They are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

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

In addition, we read the other information contained in the Annual Report 2014 and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent material misstatements of fact or material inconsistencies with the financial statements.

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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Independent Auditors' Report (continued)

To the Members of Mediterranean Bank plc

Opinion on Financial Statements

In our opinion, the financial statements:

- give a true and fair view of the unconsolidated financial position of the Bank as at 31 March 2014, and of its unconsolidated financial performance and its unconsolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU; and

- have been properly prepared in accordance with the Companies Act, 1995 (Chapter 386, Laws of Malta) and the Banking Act, 1994 (Chapter 371, Laws of Malta).

Report on Other Legal and Regulatory Requirements

Matters on which we are required to report by the Banking Act, 1994 (Chapter 371, Laws of Malta)

In our opinion:

- we have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purpose of our audit;

- proper books of account have been kept by the Bank so far as appears from our examination thereof;

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

- to the best of our knowledge and belief and, on the basis of the explanations given to us, the financial statements give the information required by law in force in the manner so required.

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

We have nothing to report in respect of the following matters where the Act requires us to report to you if, in our opinion:

- the information given in the Directors' Report for the financial year for which the financial statements are prepared is not consistent with the financial statements; or

- certain disclosures of directors' remuneration specified by the Act are not made.

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

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Independent Auditors' Report (continued)

To the Members of Mediterranean Bank plc

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

Our responsibility as independent auditors of the Bank, is laid down by Listing Rule 5.98, which requires us to issue a report on the Directors' Statement of Compliance with the Principles, which is set out on pages 1 to 11.

We review the Directors' Statement of Compliance, and report as to whether this Statement provides the disclosures required by Listing Rule 5.97. We are not required to, and we do not, consider whether the Board's statements on internal control and risk management systems cover all the risks and controls in relation to the financial reporting process, or form an opinion on the effectiveness of the Bank's corporate governance procedures or its risks and control procedures, nor on the ability of the Bank to continue in operational existence.

In our opinion, the Directors' Statement of Compliance set out on pages 1 to 11 provides the disclosures required by Listing Rule 5.97 issued by the Listing Authority of Malta.

Noel Mizzi (Partner) for and on behalf of

KPMG
Registered Auditors

28 May 2014

Additional Regulatory Disclosures in terms of CRR
For the Year Ended 31 March 2014

Contents

Introduction

The European Parliament has approved the new capital reforms, referred to as Capital Requirements Regulation ('CRR') and Capital Requirements Directive ('CRD IV'), on 26 June 2013. These reforms implement the Basel III into Europe with the sole objective to improve the banking sector's ability to absorb shocks arising from financial and/or economic stress which in turn, mitigate spill-over damage to the real economy. The CRD IV legislation has been implemented with an effective date of 1 January 2014. The CRD IV is yet to be transposed onto the Maltese legislation.

Key elements of the CRR include:

- Reduced Capital Resources through changes to the definition of capital and grandfathering of old instruments. Permanent interest bearing shares ('PIBS') and subordinated debt will be phased out over ten years from 2013. Over the period 2014-18, there will be changes and additions to capital deductions from Core Tier 1 and Tier 2 capital including pension deficit, Fair-value reserve[1], assets rated below BB- and Expected Loss.
- Increased Capital Requirements through Asset Value Correlations, Credit Value Adjustments and deduction of Deferred Tax Assets that rely on future profitability and do not arise from temporary differences net of associated tax liabilities.
- New limits and capital buffers: Higher thresholds for all forms of capital with an increased focus on Core Tier 1, with a potential to hold a ratio of up to 12.5% including Capital Conservation, Countercyclical and Systemic Risk Buffers.
- Introduction of the Leverage Ratio, with set minimum Tier 1 leverage ratio of 3%.

Overview

The Board of Directors, after considering (1) the strategies and processes to manage risks to which the Bank is exposed to; (2) the structure and organisation of the risk management function, its authority and statute; (3) the scope and nature of risk reporting and measurement systems; and (4) the policies for hedging and mitigating risk, and the strategies and processes for monitoring the continuing effectiveness of hedges and mitigates; deems that the risk management arrangements of the Bank are adequate and provide assurance that the risk management systems put in place are fit with regard to the Bank's profile and strategy.

Accordingly, these Additional Regulatory Disclosures (the "Disclosures") have been prepared in accordance with the requirements of CRR whereas in the prior year, these were prepared under Banking Rule BR/07, "Publication of Annual report and Audited Financial Statements". Mediterranean Bank plc (the "Bank") updates these Disclosures on an annual basis as part of the Annual Report and Financial Statements preparation. The Disclosures are compiled by the Bank on the basis of its consolidated financial situation, and therefore, reference to the Bank implies the Group in view that the impact of the subsidiaries on the consolidated financial position of the Bank is insignificant.

Consistent with the banking regulations, these Disclosures are not subject to external audit except where they are included within the Bank's Annual Report prepared under International Financial Reporting Standards (IFRS), as adopted by the EU. These Disclosures have been appropriately verified internally by the Bank's management and Audit Committee, including a review by the internal auditor.

[1] In general, this will result from the mark-to-market movement of the Available-for-Sale investments.

1 Risk Management Function

The Board has set up an independent and comprehensive risk management function under the leadership of the Chief Risk Officer. The aim of Risk Management is to create value for shareholders by supporting the institution in achieving its goals and objectives, and ultimately ensuring that the risks are commensurate with the rewards. It works closely with other groups within the Bank and provides independent oversight, analysis and reporting of the Bank's risk profile in all areas.

The Risk Management function is directly responsible for the oversight of market, credit, liquidity and operational risks, and the Chief Risk Officer is fully involved in the oversight of strategy and reputational risks by virtue of his seat on EXCO and his reporting line to the Risk Committee.

As at 31 March 2014, the Bank's Risk Management team comprised seven full-time professionals under the management of the Chief Risk Officer. Their responsibilities are divided as follows:

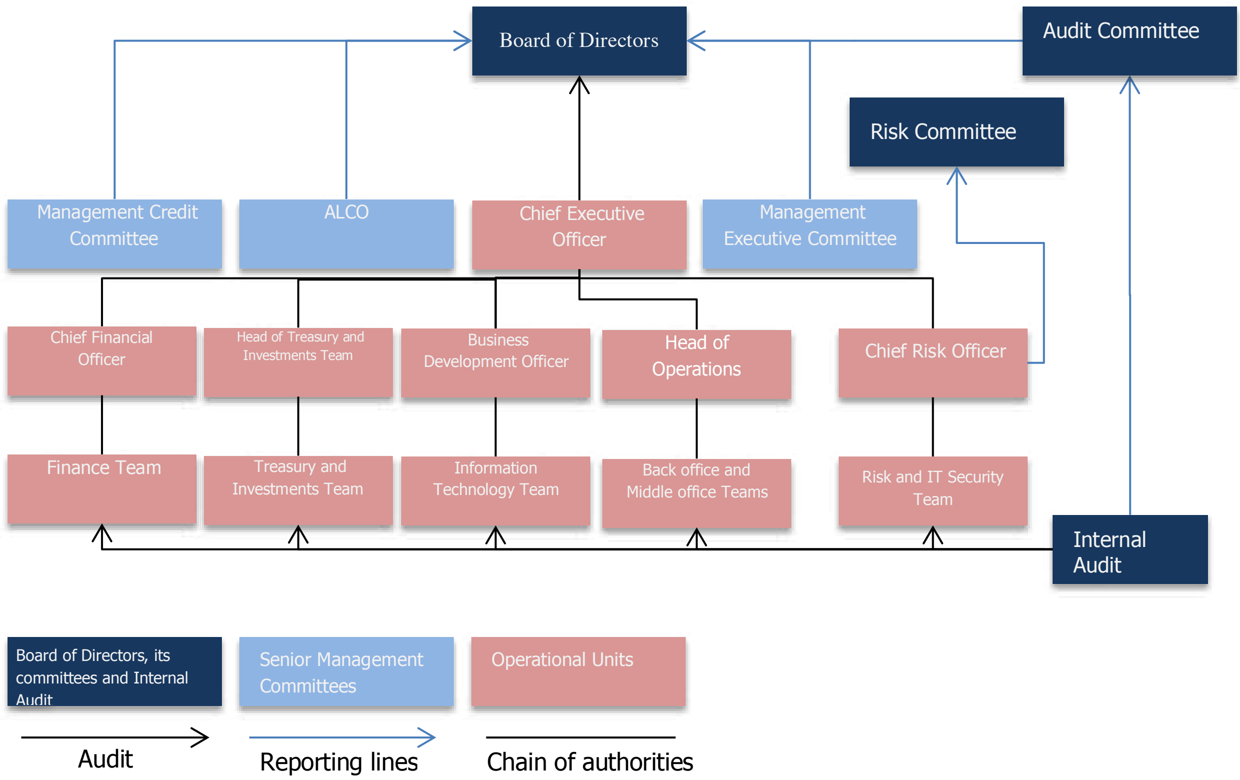
- Risk Architecture (4 staff members) – portfolio-level analysis and risk reporting, Operational Risk management and reporting.
- Risk Analysis (2 staff members) – credit, liquidity and market risk analysis and review, supported by and working with analysts from the Treasury and Investments team as appropriate.
- System Support (1 staff member) – maintenance, enhancement and development of the Bank's primary risk reporting and portfolio management information system. Although using a well-known third-party system, the Bank has taken advantage of its open architecture to develop a number of additional capabilities.
- Information Security Manager (1 staff member) – ensuring that adequate policies, procedures and processes are in place to ensure the integrity of the Bank's information systems and associated data.

The Bank's formal risk reporting schedule and processes have been designed to comply with the Basel Committee's "Principles for effective risk data aggregation and risk reporting" (June 2012, revised January 2013). In particular, reporting frequencies have been established in accordance with Principle 10, with flash reports produced daily (either system-generated or created by operational departments) and more in-depth reports produced weekly or monthly by Risk Management. The latter include interpretation and commentary in accordance with Principle 9.

The Bank recognises the need for an effective and efficient risk management function and therefore has adopted a comprehensive process that provides a right balance between the fast growth rate of the Bank and the underlying risks.

The Bank's objective is to deploy an integrated risk management approach to ensure an awareness of, and accountability for, the risks taken throughout the Bank, whilst developing the necessary tools required to address such risks. Such an integrated approach is realised through the governance structure of the Bank and relies on three principal lines of defence – (1) the management of business units, (2) a fully resourced Risk Management function, and (3) on-going independent reviews carried out by the Internal Audit function.

1.1 Risk Management Governance



The ***Board of Directors*** has a general duty to ensure that the Bank conducts business in accordance with all relevant statutory and regulatory requirements. Its overall responsibility with regard to risk management is the establishment and oversight of the Bank's risk management framework. The Board sets the Bank's strategy and ensures an effective system of internal control and management of business risks, safeguarding a strong capital and liquidity base that is conducted in accordance with the requirements of the Malta Financial Services Authority (MFSA).

As a result of the increased size of the Bank's product base and range of operations, on 27 November 2013, the Bank replaced the Audit and Risk Committee with an Audit Committee and a separate Risk Committee.

The Board has delegated specific powers and authority to the ***Risk Committee*** which is responsible for monitoring compliance with the Bank's risk management policies and procedures and for reviewing the adequacy of the Bank's risk management framework. The Internal Audit Function carries out both regular and ad-hoc reviews of the risk management controls and procedures and reports its findings to the Audit Committee.

The Board has also established the following senior management committees:

1. Management Credit Committee;
2. Asset and Liability Committee (ALCO);
3. Executive Management Committee (EXCO);
4. Management Operations Committee;
5. New Customer Products Committee; and
6. Treasury Services Committee.

The ***Management Credit Committee*** is responsible for approving credit recommendations and making other credit decisions under its delegated authority - this includes decisions on individual credits; reviewing and recommending credit to the Board; monitoring adherence to large exposure limits; consideration of credit hedging strategies; and recommending other concentration limits for Board approval. It also establishes transactional authority for members of the Treasury and Investment Department. In addition, the Management Credit Committee reviews provisioning and lending policies; monitors the Bank's investment portfolios and reviews management information reports.

Asset and Liability Committee (ALCO) is responsible for management of funding, liquidity, interest rate and currency risks. ALCO sets and reviews overall policies and objectives for asset and liability management, capital management and allocation; capital usage and efficiency; transfer pricing; risk management; and underwriting, dealing and trading activities according to the risk appetite set by the Board. It also decides on the level of any credit impairments to be taken on the Bank's investments, after receiving recommendations from the Management Credit Committee.

Executive Management Committee (EXCO) represents the principal forum for conducting the business of the Bank and takes day-to-day responsibility for the efficient running of the business. In addition, the EXCO is responsible for the formulation and implementation of Board approved strategies and plans. The Committee is authorised to take whatever steps are necessary to conduct the business of the Bank within the confines of the Board approved strategy, operating plans and budgets.

Additionally, the Board has set up a number of management level committees with the aim of identifying and addressing matters relating to operational risks namely, the Management Operations Committee, the New Customer Products Committee and the Treasury Services Committee.

A. The **Management Operations Committee** considers day-to-day operating procedures of the Bank. Also the Committee follow-ups on the implementation of audit agreed actions. The Management Operation Committee establishes, monitors and receives feedback in the form of management actions, from specifically created working groups (such as Authorisations working group; e-banking risk working group; Reconciliations working group; Physical security working group and Procedures and processes working group) as may be required in order to ensure that issues relating to operational issues are handled effectively and efficiently.

B. The **New Customer Products Committee** examines potential new products to be offered by the Bank from a risk, operations, reputation and legal/compliance perspective. The Committee provides its recommendations to the Executive Management Committee including the appropriate policies, procedures and controls that should be adopted in relation to any such new product.

C. The **Treasury Services Committee** considers potential new treasury management products to be used by treasury for liquidity, credit and market risk management from a risk, operations and legal/compliance perspective.

1.2 Risk Management Framework and Policies

The two key components of the Bank's risk management framework are

(1) an efficient separation of the Bank's risk management function and its risk taking activities; and

(2) a robust system of formal governance controls including an effective management committee structure, as described above, and a comprehensive set of internal policies.

The Bank's control policies are subject to continuous review and development, under the overall oversight of the Compliance function. Current key policies include the following:

- Terms of Reference for Board and Key Committee Structures
- Code of Ethics
- Conflict of Interest Policy
- Remuneration Policy
- Treasury Management Policy
- Credit and Investment Policy
- Impairment Provisioning Policy
- Customer Due Diligence and Compliance Requirements Policy
- Anti-Fraud Policy
- Cash Handling Policy
- Prevention of Money Laundering and Funding of Terrorism Manual
- Consumer Care Principles
- Outsourcing Policy
- Information Security Policy
- User Information Security Policy
- Admin Security Policy
- Business Continuity and Disaster Recovery Plans
- Staff Compliance Policy
- HR Policy

1.3 Risk Management Initiatives

During the year, a number of specific initiatives were implemented in order to strengthen further the Bank's Risk Management framework.

Organisational structure, policies and procedures

Chairmanship of the Management Credit Committee has passed from the Chief Executive Officer to the Chief Risk Officer, to emphasise the Committee's independence from the Investments function as well as for operational reasons. A number of key risk-related policies have also been rewritten to ensure that the risks inherent within the Bank's activities remain well controlled even as market conditions and the make-up of the Bank's investment portfolio change: notably, new Treasury Management and User Information Security policies have been implemented.

Risk Analysis and Reporting

The Bank has continued to deepen the level of analysis performed in association with, and to support, its periodic risk reporting. This applies across all areas of risk but the most significant changes have related to the Bank's liquidity risk. In particular, results presented in a number of existing reports have now been combined and consolidated into a robust Maximum Cumulative Outflow (MCO) analysis that demonstrates the Bank's projected liquidity position over a range of timescales under base-case and stressed assumptions, and taking into account mitigating actions that could be taken by the Bank, if necessary. These results are presented to ALCO monthly, as well as to the board and shareholder representatives.

2. Own Funds

2.1 Total available capital

The Bank adopts the appropriate processes to ensure that the minimum regulatory requirements are met at all times, through the assessment of its capital resources and requirements given current financial projections. The Bank has a strong track record of robust capital ratios and is confident that it will be positioned to maintain its overall capital strength.

For regulatory purposes, the Bank's capital base is divided in two main categories, namely Common Equity Tier 1 Capital and Tier 2 Capital.

2.1.1 Common Equity Tier 1 - composition

Common Equity Tier 1 Capital which includes:

- ordinary share capital;
- share premium;
- shareholders' contribution;
- retained earnings;
- reserve for general banking risks;
- fair value reserve; and
- other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes including deductions relating to Reserve for Depositor Compensation Scheme and the carrying amounts of investment in subsidiaries that are not included in the regulatory consolidation and certain other regulatory items. [2]

2.1.2 Common Equity Tier 1 Capital – terms and conditions

i. Ordinary Share Capital are equity instruments which fall under the definition of CRR Article 28 (1), *Common Equity Tier 1 Instruments*. The holders of 'A' ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at meetings of the Bank. 'B' ordinary shareholders are not entitled to vote or to receive any dividends distributed.

ii. Share premium reserve is made up of premium paid by shareholders in excess of the nominal value of the 'A' ordinary shares. This reserve can only be applied in the paying up of unissued shares to be issued to members of the Bank as fully paid bonus shares.

[2] More details are included in the notes to the Financial Statements.

iii. Shareholders' contribution ("Contribution") are amounts granted by the shareholders to the Bank whereby the Bank has no obligation to bear any servicing cost or transfer any economic benefits of any kind to the Contributor or any other person in return and has no obligation to repay the Contribution. These terms and conditions of such Contribution renders this instrument to be equity in nature in accordance with the requirements of IAS 32: Financial Instruments – Presentation.

iv. Retained earnings are the part of the distributable items as per the CRR Article (4)(1)(128) definition which are amounts of the profits at the end of the last financial year plus any profits brought forward and reserves available for that purpose before distributions to holders of own funds instruments less any losses brought forward, profits which are non-distributable pursuant to provisions in legislation or the institution's bye-laws and sums placed to non-distributable reserves in accordance with applicable national law or the statutes of the Bank, those losses and reserves being determined on the basis of the individual accounts of the Bank and not on the basis of the consolidated accounts. This balance in this reserve is net of tax.

    The Directors of the Bank, in the annual general meeting, may from time to time recommend dividends to be paid from the retained earnings of the Bank. Such dividends may be in the form of capitalisation of retained earnings to 'A' ordinary shares.

v. Reserve for General Banking risks – in accordance with article 25 of CRR, the Bank has allocated from its Retained Earnings, to a non-distributable reserve, being an amount equivalent to 2.5% of the regulatory allocation for positions on which a specific impairment provision has been attributed. Refer to further details in Note "*Capital and Reserves*" to the financial statements.

vi. The fair value reserve includes the cumulative net change in the fair value of available-for-sale investments, excluding impairment losses, until the investment is derecognised, net of deferred taxation. These relate to the AFS category of EU-endorsed IAS 39.

2.1.3 Tier 2 Capital

Tier 2 Capital consists of subordinated liabilities in issue, which rank behind the claims of all depositors (including financial institutions) and all other creditors. As at 31 March 2014, subordinated liabilities included are debt securities issues which are unsecured and are repayable on 30 December 2019. These bear interest payable of 7.5% and in the event of the winding-up of the issuer, these are subordinated to the claims of depositors and all other creditors of the issuer.

2.2 Own Funds – other disclosures

The Bank does not have items included in the 'total capital' which have values differing from those reported with IFRS compliant Statement of Financial Position.

Retained earnings form part of Own funds only if those profits have been verified by persons independent of the Bank that are responsible for the auditing of the accounts of that Bank; the Bank has demonstrated to the satisfaction of the competent authority that any foreseeable charge or dividend has been deducted from the amount of those profits.

For the year ended 31 March 2014, the dividends declared at year end will in the form of issue of shares and, being capitalised retained earnings, are eligible to be included as part of the CET 1.

2.3 Own Funds

Below is a table showing the composition of the own funds of the Bank in accordance to CRR and the related captions within the Statement of Financial Position of the Annual Report 2014.

TIER 1 CAPITAL	As per Statement of Financial Position	€000
Paid-up capital instruments	Ordinary share capital	98,050
Share premium on paid-up capital instruments above	Share premium	13,464
Paid up capital instruments	Shareholders' contribution	9,750
Previous years retained earnings	Retained earnings	191
Profit or loss attributable to owners of the parent		19,306[3]
Funds for general banking risk	Reserve for general banking risks	90[4]
Accumulated other comprehensive income	Fair value reserve	(5,691)[5]
Other reserves	Depositor Compensation Scheme Reserve	(5,018)
CET 1 deductions		
Other intangible assets gross amount	Intangible assets	(128)
Other deductions	Investment in subsidiaries	(1)
Common Equity Tier 1 Capital		130,013
Tier 1 capital		130,013
TIER 2 CAPITAL		
Dated subordinated loans eligible as Tier 2 capital	Subordinated liabilities	22,385
Tier 2 capital		**22,385**
Total own funds		152,398
Risk weighted assets (RWAs)		**1,069,743**
Total capital ratio		**14.25%**

[3] Includes externally verified profits for the year ended 31 March 2014.
[4] An amount of €90,328 is transferred from "Profit or loss attributable to owners of the parent" to "Funds for General Banking Risk".
[5] Under MFSA circular, unrealised losses are 100% recognised in CET 1 and no transitional period applies.

3. Capital Requirements

Capital Requirements represent the amount of capital resources that a bank must hold as required by the regulator. The scope of permissible CRR approaches and those adopted by the Bank are described below.

- Credit Risk – The Bank calculates its risk weighted credit risk exposure in accordance with the Standardised Approach as per CRR. To calculate the risk-weighted exposure amounts, risk weights are applied based on the exposure class and the related credit quality. Credit quality may be determined by reference to the credit assessments of External Credit Assessment Institutions ('ECAIs') that have been determined as eligible by the MFSA. In the Bank's calculations, Senior Secured Loans and other corporate credit exposures are assigned risk weights corresponding to unrated positions and for the remainder of its securities investment portfolio the Bank has nominated well-known risk rating agencies such as Fitch, Standard and Poor's and Moody's. Accordingly, the Bank complies with the standard association of the external rating of ECAIs with the credit quality steps prescribed in CRR.

- Operational Risk – The Bank calculates its capital requirement using the Basic Indicator Approach, in terms of Article 315. The own funds requirement amounts to 15% of the average three years of the relevant indicator, as defined in Article 316. Elements within the relevant indicator includes Interest receivable and similar income, interest payable and similar charges, income from shares and other variable/fixed-yield securities, commissions and fees receivable/payable, net profit or net loss on financial operations and other operating income, adjusted for, amongst others stipulated in the CRR, profits on sale of non-trading books items and extraordinary or irregular items.

- Counterparty Credit Risk – The Bank adopted the Mark-to-Market Method in order to determine the potential future credit exposure, as per CRR article 274, primarily on its derivative exposures.

- Foreign Exchange Risk – The Bank has adopted the Basic Method to determine its foreign Exchange Risk requirement in accordance with Article 351 of the CRR. Accordingly, the Bank complies with the standard association of the external ratings of ECAIs with the credit quality steps prescribed in the CRR.

- Credit Valuation Adjustment Risk – The Bank uses Standardised Approach, as per CRR article 384.

The following table shows the exposure values after credit risk mitigation associated with each credit quality step, gross of off-balance sheet exposures and after removing asset items deducted from Own Funds.

Credit risk exposure – analysis by credit quality step

	Credit quality step 1 €000	Credit quality step 2 €000	Credit quality step 3 €000	Credit quality step 4 €000	Credit quality step 5 €000	Credit quality step 6 €000	Unrated €000	Total €000
Central Governments or Central Banks	152,779	-	108,099	-	5,136	-	-	266,014
Regional Governments or Local Authorities	-	-	-	50,714	-	-	-	50,714
Administrative Bodies and non-Commercial Undertakings	-	-	-	-	-	-	-	-
Multilateral Development Banks	91,312	-	-	-	-	-	-	91,312
International Organisations	71,963	-	-	-	-	-	-	71,963
Institutions	22,468	287	112,243	-	-	-	92,390	227,388
Corporates	-	-	-	-	-	-	888,349	888,349
Retail	-	-	-	-	-	-	2,819	2,819
Covered Bonds	377,191	211,492	-	-	-	-	-	588,683
Securitisation Positions	6,048	-	-	-	-	-	-	6,048
Equity Exposure	-	-	-	-	-	-	2,474	2,474
Other	-	-	-	-	-	-	13,710	13,710
Total	**721,761**	**211,779**	**220,342**	**50,714**	**5,136**	**-**	**999,742**	**2,209,474**

A breakdown of the Bank's total exposure values, average exposure values over the year, risk-weighted exposure amounts and the minimum capital requirement of 8% are shown in the following table.

	Exposure value €000	Exposure value average €000	Risk weighted assets €000	Capital required €000
Central Governments or Central Banks	266,014	244,278	-	-
Regional Governments or Local Authorities	50,714	50,650	-	-
Administrative Bodies and non-Commercial Undertakings	-	6,568	-	-
Multilateral Development Banks	91,312	90,396	-	-
International Organisations	71,963	61,660	-	-
Institutions	227,388	180,883	22,178	1,774
Corporates	888,349	678,731	885,593	70,848
Retail	2,819	2,697	17	1
Covered Bonds	588,683	802,508	80,018	6,401
Securitisation Positions	6,048	62,201	1,210	97
Equity Exposures	2,474	1,237	2,474	198
Other	13,710	12,473	15,790	1,263
Total	**2,209,474**	**2,194,282**	**1,007,280**	**80,582**

The table below shows the total capital requirements for credit, operational and foreign exchange risks which totalled €85.6 million:

Total capital requirements

	Risk weighted assets €000	Capital required €000
Credit risk	1,007,280	80,582
Operational risk	55,209	4,417
Foreign Exchange risk	-	-
Credit Valuation Adjustment risk	7,254	580
Total	**1,069,743**	**85,579**

Own Funds of the Bank as at 31 March 2014 stood at €152.4 million.

As the Bank does not have a trading book, no capital is allocated for trading book market risk.

4 Internal Capital Adequacy Assessment Process (ICAAP)

ICAAP is a procedure, adopted under Basel II, Pillar 2, to ensure that:

- risks faced by the Bank are appropriately identified, measured, aggregated and monitored;
- the capital coverage determined by internal calculations is sufficient for the fundamental risks the Bank is exposed to; and
- the Bank has an adequate risk management framework in place, which it continuously develops in accordance with the risk factors identified.

The Bank covers Pillar 2 capital requirements through stress testing processes to forecast the Bank's projected capital requirements. Stress testing is a technique used by financial firms to gauge their potential vulnerability to severe but plausible events. This testing process contributes to the strategic planning of the Bank by guaranteeing that it can meet its minimum regulatory capital requirements under a stressed environment.

Under the supervision of a dedicated working Group consisting of the Bank's senior management, the preparation of the ICAAP is carried out by the relevant departments that include: Risk, Finance and Treasury and Investment. After the completion of an iterative process of review and feedback, the senior management team present their observations to the Board of Directors for their consideration. The non-executive Directors play a crucial role in providing the Bank with an independent evaluation of the document, assisted by the Bank's Internal Audit function.

5. Counterparty Credit Risk

5.1 Scope and Nature of Counterparty Credit Risk

Counterparty credit risk ("CCR") refers to the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. The Bank is primarily exposed to counterparty credit risk through derivative exposures, which have largely been limited to interest rate and currency hedges of the Bank's investment portfolio, and to other derivatives exposures that can be priced on a real time basis.

Counterparty credit risk in respect of currency swaps and forwards, interest rate swaps, options, swaptions and any other derivative instruments that entail credit exposures shall only be entered into with counterparties approved by ALCO. Entry into any derivative exposures will be subject to prior implementation of appropriate settlement and risk management infrastructure pursuant to a signed ISDA Agreement.

The Bank's Treasury department ensures that margin calls arising from Bank's repo and derivatives obligations are monitored on a daily basis. Exposure to derivative counterparties and the related credit risk is mitigated through the use of netting and collateralisation agreements. The Bank's Treasury department ensures that it monitors margin calls arising from Bank's repo and derivatives obligations on a daily basis.

5.2 Counterparty Credit Risk Exposure

In order to determine the potential future credit exposure, the notional amounts or underlying values, as applicable, multiplied by the percentages stipulated in Capital Requirements Regulations, Table 1 of Article 274 (2) (c). These are based on contract type and residual maturities.

Below is tabulated the CCR exposure of the Bank as at 31 March 2014:

Contract type	*Residual Maturity*	*Notional Amount (€'m)*	*Applicable percentage*[6]	*Mark-to-Market (€'m)*	*Gross Exposure (€'m)*	*Risk-weight*[7]	**Value (€'m)**
Warrant	Over one year, not exceeding five years	-	-	0.404	0.404	0%	0
Interest Rate Swaps	Over one year, not exceeding five years	130	0.5%	-	0.650	50%	0.325
Interest Rate Swaps	Over five years	370	1.5%	-	5.550	50%	2.775
Swaption	Over one year, not exceeding five years	140	0.5%	0.404	1.104	50%	0.552
Swaption	Over five years	10	1.5%	-	0.150	50%	0.075
Foreign currency contracts	One year or less	98.9	1.0%	-	0.989	20%	0.198
					8.847		3.925

[6] Applicable percentages per Table 1 of Article 274 (2) (c)
[7] Based on counter party ratings

6. Credit Risk

6.1 Scope and Nature of Credit Risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers and other banks, and investment debt securities. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

Credit risk by exposure type

	Statement of financial position value €000	Exposure value €000	Exposure value %
Balances with Central Bank of Malta, treasury bills and cash	18,091	18,091	0.8%
Loans and advances to financial institutions	87,714	87,714	4.0%
Loans and advances to customers	571,144	573,438	26.0%
Investments	1,477,940	1,478,403	66.9%
Derivative assets held for risk management	404	404	0.0%
Derivative assets held for trading	404	404	0.0%
Investment in subsidiaries	1	1	0.0%
Property and equipment	1,908	1,908	0.1%
Intangible assets	128	128	0.0%
Other assets	18,889	18,889	0.9%
Prepayments and accrued income	23,261	23,260	1.1%
Deferred tax assets	3,764	3,764	0.2%
Total assets	**2,203,648**	**2,206,404**	**99.9%**
Off-balance sheet items and value adjustments		8,217	0.3%
Asset items deducted from own funds		(5,147)	(0.2%)
Total exposure		**2,209,474**	**100.0%**

Credit risk arises primarily in the form of deterioration in credit quality leading to an obligor defaulting on debt instruments held in the Bank's investments portfolio or on senior secured loans extended to corporate counterparties.

Additionally, as explained in section Counterparty Risk, the Bank is exposed to credit risk in respect of repo and derivative exposures. The Bank has in place a number of standard master netting agreements for repo counterparties which allows it to assess the related exposure on a net basis.

The Bank analyses and monitors its credit risk exposure by breaking the portfolio down in a number of ways, including:

1. Exposure Class;
2. Geographic Distribution; and
3. Residual Maturity.

1) Credit risk exposure – analysis by exposure class

	Exposure value €000	Exposure percentage %
Central Governments or Central Banks	266,014	12.0%
Regional Governments or Local Authorities	50,714	2.3%
Administrative Bodies and non-Commercial Undertakings	-	0.0%
Multilateral Development Banks	91,312	4.1%
International Organisations	71,963	3.3%
Institutions	227,388	10.3%
Corporates	888,349	40.3%
Retail	2,819	0.1%
Covered Bonds	588,683	26.6%
Securitisation Positions	6,048	0.3%
Equity Exposures	2,474	0.1%
Other	13,710	0.6%
Total	**2,209,474**	**100%**

2) Credit risk exposure – analysis by geographical distribution

	Australia €000	Europe €000	North America €000	Total €000
Central Governments or Central Banks	-	266,014	-	266,014
Regional Governments or Local Authorities	-	50,714	-	50,714
Administrative Bodies and non-Commercial Undertakings	-	-	-	-
Multilateral Development Banks	-	91,312	-	91,312
International Organisations	-	71,963	-	71,963
Institutions	316	218,540	8,532	227,388
Corporates	-	851,016	37,333	888,349
Retail	-	2,819	-	2,819
Covered Bonds	-	554,458	34,225	588,683
Securitisation Positions	-	6,048	-	6,048
Equity Exposures	-	2,474	-	2,474
Other	-	13,710	-	13,710
Total	**316**	**2,129,068**	**80,090**	**2,209,474**

3) Credit risk exposure – analysis by residual maturity

	Less than 1 year €000	**1 to 5 years €000**	**Over 5 years €000**	**Total €000**
Central Governments or Central Banks	15,502	144,703	105,809	266,014
Regional Governments or Local Authorities	-	50,714	-	50,714
Administrative Bodies and non-Commercial Undertakings	-	-	-	-
Multilateral Development Banks	-	-	91,312	91,312
International Organisations	-	43,987	27,976	71,963
Institutions	197,583	24,105	5,700	227,388
Corporates	2,404	724,838	161,107	888,349
Retail	333	2,425	61	2,819
Covered Bonds	-	363,713	224,970	588,683
Securitisation Positions	-	-	6,048	6,048
Equity Exposures	-	-	2,474	2,474
Other	12,339	1,371	-	13,710
Total	**228,161**	**1,355,856**	**625,457**	**2,209,474**

6.2 Managing Credit Risk

6.2.1 Risk Management Objectives

The Bank's objective is to maximise its investment returns while maintaining a sound and prudent investment profile. To facilitate achieving this target, the Bank invests in a diversified portfolio comprising both high-quality assets with strong ratings stability which support the Bank's deposit-taking, and in loans to corporations with appropriate risk characteristics.

Hedging and mitigation of credit risk

The efficient and controlled use of credit risk is a key part of the Bank's business model; risk is primarily mitigated by the use of thorough and robust investment limits and investment approval and portfolio review processes. The Bank's Credit and Investment Policy (see below) permits it, subject to the prior approval of the Board of Directors, to manage its credit risk through credit hedges, although to date it has not done so.

6.2.2 Credit and Investment Policy

The purpose of the Credit and Investment Policy is to establish the credit standards, internal controls, reporting requirements and approval processes that govern the selection and on-going management of the investment assets of the Bank.

The Board of Directors has established limits for exposures to individual credits based on Maltese regulatory requirements (including, without limitation, Banking Rule BR/02 of the Malta Financial Services Authority, governing Large Exposures of Credit Institutions), as well as prudential requirements. Exposure limits are monitored on an on-going basis by the Chief Risk Officer and the Head of Treasury and Investment. Credit and Investment Policy among others outlines the following specific exposures and trading limits:

- Concentration limits;
- Country limits; and
- Minimum credit quality within each asset class.

Limits on counterparty exposure are established by ALCO. Such limits relate to net exposure, after application of cash (and cash equivalent) collateral, as provided in industry-standard documentation such as the ISDA and GMRA agreements, and the Treasury Management Policy (see below).

6.2.3 Treasury Management Policy (TMP)

The purpose of the Treasury Management Policy is to provide a framework within which Treasury is authorised to prudently manage interest rate, foreign exchange, funding, liquidity, counterparty and investment risk, and any other associated risks related to managing the balance sheet position.

The Treasury Management Policy includes the following approved limits:

- Deposit limits;
- Investment limits;
- Repo Counterparty Haircut limits; and
- Foreign Exchange Settlement limits.

6.2.4 Credit Quality Analysis

All securities in the portfolio, as well as corporate loans undergo a thorough analytical credit research process. The research process reviews all securities and corporate loans not only from a credit perspective but also from a legal, financial and ratings perspective. The Treasury and Investment department, which manages the research process, is composed of highly-trained individuals with specialised skill sets and years of experience in the Fixed Income and Corporate Syndicated Loans markets. The research process subjects potential investments to scenario analysis to determine whether they can withstand significant adverse credit and market events. Additionally, the portfolio is subject to a continual and thorough surveillance process in order to identify any securities and loans the performance of which requires increased monitoring.

With the exception of the corporate lending portfolio, most of the securities in the Bank's investment portfolio are accepted by the ECB as eligible collateral and all of the securities (or their issuers) are rated by at least one from Fitch, Standard and Poor's and Moody's rating agencies.

The assessment of asset quality, adequacy of provisions, and the disclosure of credit risk are requirements by IFRS and the MFSA Banking Rule BR/09 "The Credit and Country Risk Provisioning of Credit Institutions Rule"[8]. These regulations require that a specific provision is created where a review of credit facilities reveals that the creditworthiness of a borrower has deteriorated significantly and as a result recovery of a credit facility is in serious doubt.

ALCO determines when financial assets have become impaired individually or collectively and to what extent such impaired assets should be provided for / written down, all in accordance with IFRS and the Bank's Impairment Provisioning Policy. ALCO receives recommendations from the Management Credit Committee and Finance Function to assist it with this determination.

Furthermore, the Audit Committee reviews and challenges where necessary the judgement of management in relation to the Bank's Financial Statements.

6.2.5 Impairment Provisioning Policy

The scope of the Impairment Provisioning Policy is to establish effective provisioning standards, internal controls, reporting requirements and approval processes that will govern the on-going monitoring of credit risk exposures inherent in the investment securities and loan portfolios.

In accordance with the policy, impaired investment securities and loans are those where a loss event has occurred and the Bank establishes that it is unlikely that it will collect the full principal and/or interest due in accordance with the contractual terms of the underlying agreement(s).

[8] MFSA Banking Rule 9, "Measures addressing credit risks arising from the assessment of the quality of asset portfolios of credit institutions", was revised and effective for period ending 31 December 2013.

6.2.6 Reconciliation of collective provision

	Senior secured corporate lending €000	Investment securities €000	Total €000
At 1 April 2013	676	-	676
Additions – charged to profit or loss	196	463	659
At 31 March 2014	**872**	**463**	**1,335**

6.2.7 Specific provision

Throughout the financial year ended 31 March 2014, a specific provision amounting of €1.4 million on a senior secured corporate lending position has been taken.

6.2.8 Forbearance

During the financial year ended 31 March 2014, there were no forbearance activities.

6.3 Settlement Risk

The Bank's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of an entity to honour its obligations to deliver cash, securities or other assets as contractually agreed.

Mitigation of settlement risk

For all types of investment transactions the Bank mitigates this risk by conducting settlements through a settlement / clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval / limit monitoring process described earlier. Furthermore, the Bank has a number of master netting agreements covering repurchase transactions and securities with its counterparties.

6.4 Credit Valuation Adjustment (CVA)

CRR requires financial institutions to calculate own funds requirements for CVA risk, in accordance with article 382, which is a capital charge to reflect potential mark-to-market losses due to counterparty migration risk on bilateral OTC derivative contracts.

Using the regulatory formula, capital required in respect of CVA risk as at 31 March 2014, is calculated to be €580,318 on a total exposure of €7,253,978.

6.5 Exposures in Equities

The Bank's Corporate exposures, within the "Loans and advances to customers: corporates" in the Statement of Financial Position, include ordinary shares which had a nil value on acquisition. Under International Financial Reporting Standards, specifically IAS 39 as adopted by the European Union, de-stapling provisions kick-in and should recognise the ordinary shares separately based on dissimilar economic characteristics and risks.

The mark-to-market value of the exposure in equity is of €2.5 million, fully recognised as capital gains in the profit or loss for the year ended 31 March 2014.

The total Equity holding does not fall under the definition of "qualifying holding"[9] and is below the small trading book business threshold (Article 94 of CRR) given that it is less that 5% of total assets and therefore is not eligible to be part of a trading book.

6.6 Encumbered assets

The table below sets out the availability of the Bank's financial position to support future funding.

31 March 2014

	Encumbered		Unencumbered		
	Pledged as collateral	**Other †**	**Available as collateral**	**Other‡**	**Total**
	€000	**€000**	**€000**	**€000**	**€000**
Balances with Central Bank of Malta and treasury bills and cash	5,997	-	-	12,094	18,091
Loans and advances to financial institutions	-	-	-	87,714	87,714
Loans and advances to customers: corporate	389,076	-	-	179,249	568,325
Loans and advances to customers: retail	-	-	-	2,819	2,819
Investments	1,143,915	3,822	298,030	32,173	1,477,940
Derivative assets held for risk management	-	-	-	404	404
Derivative assets held for trading	-	-	-	404	404
Loans and advances to related entities§	-	-	-	18,145	18,145
	1,538,988	**3,822**	**298,030**	**333,002**	**2,173,842**

†Represents assets that are not pledged for funding purposes but that the Bank believes it is restricted from using to secure funding, for legal or other reasons.
‡Represents assets that are not restricted for use as collateral, but the Bank would not consider them as readily available to secure funding in the normal course of business.
§included in other assets

9 CRR defines "qualifying holding" as a direct or indirect holding in an undertaking which represents 10 % or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of that undertaking;

7 Leverage

CRR requires financial institutions to calculate a non-risk based Leverage Ratio, to supplement risk-based capital requirements. The leverage ratio measures the relationship between the capital resources of the organisation and its total assets. The Leverage Ratio is a new regulatory supervisory tool for the Regulator, the purpose of which is to constrain the build-up of excessive leverage – one of the drivers of the banking crisis – previously not captured within Basel II.

A monitoring period has been allowed which runs from January 2013 to January 2017, during which time a minimum ratio of 3% should apply – this limit will then be reassessed in 2017 before becoming mandatory in 2018.

The Leverage Ratio is a three-month average of capital as proportion of total exposures in which both are defined according to Basel III.

- Capital: Tier 1 capital as per CRR
- Exposures: Total on and off balance sheet exposures less the deductions applied to Tier 1 Capital as per CRR requirements.

$$\text{Leverage ratio} = \frac{\text{Tier 1 Capital}}{\text{Total on} - \text{and off} - \text{balance sheet assets adjusted for deductions}}$$

	Tier 1 Capital[10] €000	Total on/off adjusted assets €000	Leverage ratio %
At 31 March 2014	125,748	2,203,648	5.7%

The Bank's Leverage Ratio is well above the 3% minimum requirement.

[10] Three-month average

8 Liquidity Risk

8.1 Scope and Nature of Liquidity Risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

8.2 Managing Liquidity Risk

8.2.1 Risk Management Objective

The Bank's objective in managing liquidity risk is to ensure that, as far as possible, it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

Management of liquidity risk is the responsibility of the Bank's Treasury Department and the Risk Office, under the oversight of the Board, ALCO, Risk Committee and the Risk Department and under an approach set out in its Treasury Management Policy (TMP).

8.2.2 Treasury Management Policy

The Bank's TMP establishes the principles, standards, internal controls, high-level reporting requirements and escalation and approval processes that govern the on-going management of:

- the Bank's liquidity and asset-liability mix;
- the Bank's market, interest rate and currency risk; and
- any credit risk taken on in connection with the activities above.

It is also designed to ensure compliance with all national and international regulations and laws that are applicable to these activities.

8.2.3 Management Asset-Liability Committee (ALCO)

ALCO that meets at least monthly (and more frequently as necessary) to analyse and review the liquidity position of the Bank, to formulate this strategy to manage and optimise the Bank's asset-liability mix, and to oversee the Bank's market risk position.

As such, ALCO is the executive-level body that oversees the Bank's compliance with the TMP, and that receives much of the analysis specified in it.

8.2.4 Board Risk Committee

The Board Risk Committee is responsible for setting policies of the Bank in respect of liquidity and funding, interest rate and currency risks of the Bank and for reviewing and approving any changes to the overall asset-liability management strategy of the Bank. As such, it is the Board-level committee that oversees the TMP.

8.2.5 Roles and responsibilities

Management of the Bank's liquidity position and of its market risk is the joint responsibility of its Treasury and Risk functions (under the oversight of ALCO and of the Board Risk Committee), as is management of the credit risk that arises from these activities. In broad terms:

- Treasury has primary responsibility for managing and reporting the Bank's projected liquidity position (the "base case"), and for managing its market risk position on a day-to-day basis; and

- Risk has primary responsibility for defining potential adverse liquidity scenarios that should be considered and for reporting exposure to these scenarios (the "downside case"), as well as for regular formal reporting of the Bank's market risk position.

8.2.6 Funding Strategy

Banks traditionally perform a role of liquidity transformation, whereby they fund through liabilities that are liquid in the short to medium-term, in order to invest in longer-term and less liquid assets. This mismatch of liquid liabilities and less liquid assets is a near-universal feature of bank balance sheets and clearly leads to a risk if liabilities cannot be rolled when they mature (which may be every day in the case of money held in current or savings accounts).

The Bank's strategy to mitigate this risk has three main components:

- Limiting its exposure to customer deposit withdrawal by use of term rather than overnight deposits as its primary instrument of customer funding;

- Limiting its exposure to wholesale funding withdrawal by locking in term funding against less liquid assets and by diversifying its sources of funding; and

- Maintaining a contingency source of funding by ensuring that the bulk of its Treasury portfolio is eligible for funding at the ECB if alternative sources are unavailable.

The Bank's objective is to maintain a prudent funding structure drawn from diverse funding sources while recognising its position as a regulated credit institution. Potential funding sources may include, but are not limited to:

- Deposits from retail and corporate customers;
- Bond issuance, either secured, senior unsecured or subordinated;
- Issuance of capital instruments;
- Interbank funding (either secured, for example through repo or TRS, or unsecured); and
- Central bank funding.

Residual contractual maturities of financial liabilities

31 March 2014

	Carrying amount €000	Gross nominal outflow €000	Less than 1 month €000	1 month to 3 months €000	3 months to 1 year €000	1 year to 5 years €000	Over 5 years €000
Non-derivative liabilities							
Amount owed to financial institutions:							
- Due to clearing houses	522,032	525,050	27,059	10,006	208,129	279,856	-
- Due to other banks	486,944	489,151	98,431	256,192	134,528	-	-
Amounts owed to customers	776,715	831,751	203,445	19,693	241,711	366,846	56
Debt securities in issue	14,341	16,456	-	-	958	15,498	-
Debt securities in issue through funding structure	215,786	263,633	-	-	3,532	14,230	245,871
Subordinated liabilities	22,385	32,748	-	-	1,711	6,830	24,207
	2,038,203	**2,158,789**	**328,935**	**285,891**	**590,569**	**683,260**	**270,134**
Derivative liabilities							
Derivative liabilities held for risk management							
- Interest rate swaps	2,798						
- Inflows		28,358	-	-	1,226	18,586	8,546
- Outflows		(30,993)	-	-	(3,808)	(21,801)	(5,384)
- Foreign exchange swaps	175	409	7	402	-	-	-
	2,973	**(2,226)**	**7**	**402**	**(2,582)**	**(3,215)**	**3,162**

Liquidity Reporting

In order to ensure that the Bank has adequate liquidity to meet its near-term obligations, Treasury projects the Bank's expected liquidity position for each day over the next week, as well as estimating a "residual" cash balance that takes into account known inflows and outflows (for example settlements of asset purchases or sales) that fall outside this period. It reports using two key metrics:

- Before the relevant liquidity provisions under the Capital Requirements Regulations and Directive become effective in 2015, the Bank is required to maintain its liquid asset ratio of net cash to short-term customer liabilities, in excess of 30%. The calculation of this ratio is performed by Finance and submitted to the MFSA as part of the Bank's statutory monthly returns. Liquidity ratio, being the ratio of net cash to wholesale (margin-sensitive) funding. This cash buffer is designed to ensure that the Bank can meet any additional margin requirement that might be imposed by the ECB or by repo counterparties, resulting either from changes in market values of assets or from increases in applicable haircuts.

A summary of MFSA Liquidity Asset Ratios during the year is shown below and all measures are well above the statutory minimum of 30%:

	2014
At 31 March	148.7%
Average for the year	129.6%
Maximum for the year	171.1%
Minimum for the year	105.3%

CRR will introduce the Liquidity Coverage Ratio (LCR), which is aimed at ensuring short-term resilience of financial institutions. They will be required to hold at all times liquid assets, the total value of which equal, or are greater than, the net liquidity outflows which might be experienced under stressed conditions over a short period of time (30 days). Net cash outflows are to be computed on the basis of a number of assumptions concerning run-off and draw-down rates. The LCR was being monitored in the EU since January 2013. Calibration is expected to be further undertaken regarding liquid assets and net cash outflows. This fine-tuning will provide input for the level-two regulations to be introduced by the European Commission before January 2015, when the LCR will become binding for all credit institutions in the EU.

The LCR is subject to an observation period and shall be introduced in accordance with a phase-in approach, whereby a minimum requirement of 60% will be required as from 1 January 2015, increasing it gradually to 100% as from 1 January 2018.

The Net Stable Funding Requirement (NSFR) requires that available stable funding (equity and liability financing expected to remain stable over a one-year time horizon) at least equals the matching assets, i.e. illiquid assets which cannot be easily turned into cash over the following 12 months. In the European Union the components of the NSFR are being monitored with a view to introducing a binding requirement in 2018.

9. Market Risk

9.1 Scope and Nature of Market Risk

Market risk is the risk that changes in market prices, such as interest rate, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments.

As for liquidity risk, management of market risk is the responsibility of the Bank's Treasury Department and its Risk Office, under the oversight of its Management Asset-Liability Committee and its Board Risk Committee and under an approach set out in its Treasury Management Policy.

9.2 Managing Market Risks

Risk Management Objectives

The key objective of managing market risk is to maximise the Bank's returns on interest rate and foreign exchange rate risks. With the exception of translation risk arising on the Bank's net investment in its foreign operations (which is negligible), all foreign exchange risk within the Bank is managed and hedged by the Treasury department. Accordingly, the foreign exchange position is treated as part of the Bank's investment portfolio for risk management purposes. The overall authority for market risk is vested in ALCO which is responsible for the development of detailed risk management policies and for the day-to-day review of their implementation.

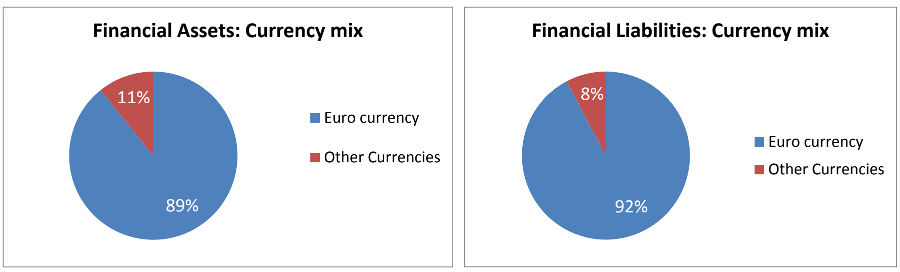
The Bank's *Treasury Management Policy* provides the framework within which treasury prudently manages interest rate, foreign exchange, funding, liquidity, counterparty and investment risk, and any other associated risks related to managing the assets and liabilities presented on the Statement of Financial Position. Regular reviews of the policy are conducted to test robustness of the policy's risk control limits within both normalised and stressed environments.

The Bank's *Asset-Liability Management Policy* establishes the standards, internal controls, reporting requirements and approval processes that govern the on-going management of (i) the liquidity and asset-liability mix of the Bank and (ii) the Bank's market, interest rate and currency risk.

9.3 Foreign exchange Risk

Foreign exchange risk is the risk that the value of the Bank's positions may fluctuate due to movements in underlying currency exchange rates. Although a large majority of the Bank's assets and liabilities is euro-denominated, the Bank does offer deposits in other major currencies and its loan portfolio includes a number of Sterling-denominated loan assets. The Bank seeks to minimise foreign exchange risk and thus hedges all material exposures in this area.

The following diagrams depict an analysis of the financial assets and financial liabilities of the Bank into relevant currency mix.



10. Interest Rate Risk in Non-Trading Book

10.1 Scope and Nature of Interest Rate Risk

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates.

10.2 Managing Interest Rate Risk – risk management

10.2.1 Interest Rate Risk Management

Interest rate risk arises as a consequence of the Bank's core businesses where there is a mismatch between the nature of rates received on the Bank's financial assets and the rates paid on the Bank's liabilities. For example, fixed-rate term deposits could be used to fund floating-rate loans, or floating-rate secured funding could be used to finance the purchase of fixed-rate securities.

Treasury, under the oversight of the Head of Treasury and Investment, manages interest rate risk within the prevailing interest rate risk strategy as set by ALCO, and subject to limits recommended by the Chief Risk Officer and approved by ALCO.

10.2.2 Interest Rate Risk Reporting and Analysis

The Risk Department prepares an interest rate risk report of the Bank on a monthly basis. This report outlines the effects of potential yield curve moves on:

- Projected Net Interest Margin;
- The Bank's capital position;
- The Economic Value of the Bank's financial assets and liabilities, assuming that no fixed-rate deposits are rolled forward; and
- The Economic Value of the Bank's financial assets and liabilities, incorporating assumptions around fixed-rate deposit roll overs.

A summary of the Bank's interest rate gap position on non-trading portfolios is as follows:

31 March 2014		**Re-pricing in:**		
	Carrying amount €000	**Less than 3 months €000**	**3 months to 1 year €000**	**More than 1 year €000**
Balances with Central Bank of Malta and treasury bills	17,907	15,057	2,850	-
Loans and advances to financial institutions	87,714	87,714	-	-
Loans and advances to customers	571,144	537,426	31,285	2,433
Investments	1,478,344	240,818	19,402	1,218,124
	2,155,109	**881,015**	**53,537**	**1,220,557**
Amounts owed to financial institutions:				
- Due to clearing houses	522,032	37,032	207,000	278,000
- Due to other banks	486,944	353,966	65,595	67,383
Amounts owed to customers	776,715	222,527	236,859	317,329
Debt securities issued	14,341	-	-	14,341
Debt securities issued through funding structure	215,786		215,786	-
Subordinated liabilities	22,385	-	-	22,385
	2,038,203	**613,525**	**725,240**	**699,438**
Interest rate gap	**116,906**	**267,490**	**(671,703)**	**521,119**

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to various interest rate scenarios. The estimated impact on Net Interest Margin (NIM) as a result of a 100 and 200 basis points (bps) movement and on Fair Value Reserve as a result of a 100 and 200 basis points (bps) parallel fall or rise in the yield curves, after taking into account the effect of hedge accounting, and making the assumption that market rates will never become negative, would be as follows:

31 March 2014	**100 bps parallel increase €000**	**100 bps parallel decrease €000**	**200 bps parallel increase €000**	**200 bps parallel decrease €000**
Impact on NIM	4,102	(5,122)	8,699	(9,734)
Impact on EV	6,518	(4,653)	15,093	(8,832)

10.2.3 Hedging and mitigation of interest rate risk

Interest rate risk positions are managed by Treasury and Credit and Investments, in conjunction with Risk, by strategically positioning the asset and liability interest rate re-pricing profiles as well as by purchases of interest rate derivatives, primarily swaps and swaptions. In addition, Treasury uses advances to financial institutions and deposits from financial institutions to manage the overall position arising from the Bank's non-trading activities.

11. Operational Risk

11.1 Scope and Nature of Operational Risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Bank's operations and are faced by all business entities.

11.2 Managing Operational Risk

11.2.1 Risk Management Objective

The objective of operational risk management is to manage the likelihood of material financial losses or reputational damage within the Bank's risk tolerance, while aiming to maintain overall cost effectiveness or the use of control procedures that restrict initiative and creativity while maintaining risk taking within a tolerable limit.

Key to achieving this objective is to ensure that the Bank has in place an appropriate and effective controls framework. The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Bank standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorisation of transactions
- requirements for the reconciliation and monitoring of transactions
- compliance with regulatory and other legal requirements
- documentation of controls and procedures
- requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified
- requirements for the reporting of operational losses and proposed remedial action
- development of contingency plans
- training and professional development
- ethical and business standards
- risk mitigation, including insurance where this is effective

11.2.2 Operational Risk Management and Principles

The Bank recognises the importance of having a strong operational risk management and delivers this through its three lines of defence, whose role is to ensure that adequate and appropriate risk management principles are applied across all business lines. The first line of defence is composed of business line management and staff where the primary control is performed. The second line of defence includes the risk management function, HR, finance, IT, legal and compliance, all involved separately in overseeing the business line management. The third line of defence is the audit function which is intended to provide independent assurance.

The operational risk framework is objectively formulated within the context of the Bank's operations and specified risk appetite and tolerance in line with industry standards and is ultimately intended to embed and maintain a strong operational risk and internal control culture.

11.2.3 IT Security Risk Management

The Bank identifies the potential to benefit from technology through increased efficiency and lower risk exposures from an operational perspective. Plans to further automate processes beyond those at the core of the business are in place, and in this respect, the risk management function liaises with the business development function. Moreover, accompanying security risks are being managed by the IT Security team, which is involved in selecting and overseeing the operations of the Bank's security solutions, establishing the Bank's security stance through policy, architecture and awareness, and carrying out vulnerability audits and assessments.

11.2.4 Business Continuity Planning

The Business Continuity Plan (BCP) is intended to provide the Bank with a plan of actions necessary to restore business to a minimum acceptable level in the event of a disruption, with specific focus on the prioritisation of the recovery of the business processes and the technology required to support such processes.

The main objective of the plan is to restore critical business operations in a timely manner in the event of a business disruption by minimising the number of critical decisions to be made at the time of the event by:

- Ensuring that clear instructions regarding the action plan are communicated to staff members and relevant parties; and

- Ensuring that all necessary human resources, material resources and technology are in place to support critical processes.

In the event that any of the critical business units experience a significant disruption, the Business Continuity Team is responsible for directing the business effectively and as efficiently as possible.

The Risk function ensures that the BCP remains effective by keeping the plan up to date as the business evolves, and by testing the plan on a regular basis.

Additionally, the Bank also put in place an IT Disaster Recovery Plan. The plan defines every system and classifies these according to a priority level and an associated level of tolerance to failure. Critical systems are supported by adequate redundancy and a number of backups are held in secure locations. An alternative location equipped with the required IT infrastructure is set up so that the Bank may execute critical business processes in a disaster scenario.

In light of the Bank’s development pace and the low tolerance to business disruption, both the Business Continuity and the IT Disaster Recovery Plans are reviewed on a regular basis.

12. Remuneration Policy and Practices

Information on remuneration policy and practices is disclosed in the Remuneration Report to the Annual Report.

13. Recruitment and Diversity Policy Statement

The Bank recognises that a robust and professional approach to recruitment and selection helps it to attract and appoint individuals with the necessary skills and attributes to support its business goals.

All prospective staff members are subject to a rigorous selection process, taking into account the key activities, tasks and skills required for the position. Multiple interviews are conducted, and the candidate's knowledge, experience, skills, temperament and competency are evaluated against other candidates.

The Bank endeavours to ensure that all appointments (at any level) are made based on the actual knowledge, skills, expertise and merit of the individual involved, in compliance with local legislation and in adherence to this policy and related processes.

The Bank is committed to attracting, developing and retaining diverse leaders. Diversity of thought provides tangible business benefits, including innovation, risk mitigation, better problem solving and improved customer service. To ensure we can foster these talents in an inclusive culture, we continue to recruit and develop the best person for the job, regardless of gender, age, race, family or caring responsibilities, disability and sexual orientation, identity or preference.

14. Other Directorships

The number of other directorships held by members of the Bank's Board are listed in the table below:

Director		**Number of Other Directorships held** No
Francis J. Vassallo	Independent Non-Executive Director	46
Finlay S. McFadyen	Independent Non-Executive Director	1
Benjamin Hollowood	Non-Executive Director	5
Mark A. Watson	Executive Director	3
Henry C. Schmeltzer	Executive Director	2
Joaquin Vincent	Executive Director	2
Vincent Chatard	Executive Director	None

Statements of Comprehensive Income

	31 Mar 2014 €000	31 Mar 2013 €000	31 Mar* 2012 €000	31 Dec 2010 €000	31 Dec 2009 €000
Interest income	64,567	50,945	64,067	41,834	4,544
Interest expense	(33,589)	(27,668)	(34,327)	(14,188)	(1,357)
Net interest income	**30,978**	**23,277**	**29,740**	**27,646**	**3,187**
Net fee and commission income/(expense)	634	(1,826)	(171)	(1,030)	(62)
Net trading income	2,292	1,111	1,252	346	103
Net income from other financial instruments at fair value through profit or loss	1,883	4,156	547	-	-
Other operating income	28,028	27,534	48,931	3,280	116
Total Operating income	**63,815**	**54,252**	**80,299**	**30,242**	**3,344**
Net Impairment	(2,081)	(676)	(62,885)	-	-
Administrative and other expenses	(17,186)	(9,920)	(9,020)	(5,675)	(3,256)
Personnel expenses	(13,785)	(11,164)	(6,461)	(5,137)	(723)
Depreciation and amortisation	(877)	(945)	(772)	(365)	(227)
Operating expenses	**(33,929)**	**(22,705)**	**(79,138)**	**(11,177)**	**(4,206)**
Profit/(loss) before income tax	29,886	31,547	1,161	19,065	(862)
Income tax expense	(10,490)	(11,064)	(453)	(3,955)	-
Profit/(loss) for the financial period	**19,396**	**20,483**	**708**	**15,110**	**(862)**

*15 month period to from 1 January 2011 to 31 March 2012

Statements of Financial Position

	31 Mar 2014	31 Mar 2013	31 Mar* 2012	31 Dec 2010	31 Dec 2009
	€000	€000	€000	€000	€000
Assets					
Balances with Central Bank of Malta, treasury bills and cash	18,091	70,055	63,656	10,526	39,757
Loans and advances to financial institutions	87,714	20,131	27,804	35,801	14,045
Loans and advances to customers	571,144	402,174	27,666	-	9
Investments	1,477,940	1,564,034	1,415,493	1,324,114	636,323
Derivative assets held for risk management	404	1,152	2,572	-	-
Derivative assets held for trading	404	-	-	-	-
Investment in subsidiaries	1	65	63	-	-
Property and equipment	1,908	2,485	2,880	2,682	839
Intangible assets	128	228	351	1,371	246
Other assets	18,889	13,598	15,649	1,728	478
Prepayments and accrued income	23,261	27,996	19,442	14,646	5,750
Deferred income tax asset	3,764	-	244	695	-
Total assets	**2,203,648**	**2,101,918**	**1,575,820**	**1,391,563**	**697,447**
Liabilities					
Amounts owed to financial institutions	1,008,976	1,368,995	1,093,753	1,134,986	578,698
Amounts owed to customers	776,715	566,047	379,555	172,847	72,078
Debt Securities in Issue	230,127	15,664	19,672	14,735	-
Derivative liabilities held for risk management	2,973	-	-	-	-
Subordinated liabilities	22,385	12,341	-	-	-
Current tax	10,794	7,660	166	3,891	-
Other liabilities	1,109	1,100	682	778	859
Accruals and deferred income	15,409	9,966	6,606	4,855	1,552
Deferred tax liability	-	5,062	-	-	-
	2,068,488	**1,986,835**	**1,500,434**	**1,332,092**	**653,187**
Equity					
Share capital	98,050	62,350	56,030	41,030	39,521
Share premium	13,464	13,464	13,464	13,464	13,464
Shareholders' contribution	9,750	8,500	-	-	-
Reserve for general banking risks	91	-	-	-	-
Retained earnings/(accumulated losses)	19,496	21,191	7,029	6,382	(8,729)
Fair value reserve	(5,691)	9,578	(1,137)	(1,410)	-
Exchange differences on consolidation	-	-	-	5	4
	135,160	**115,083**	**75,386**	**59,471**	**44,260**
Total liabilities and equity	**2,203,648**	**2,101,918**	**1,575,820**	**1,391,563**	**697,447**

Statements of Cash Flows

	31 Mar 2014	31 Mar 2013	31 Mar* 2012	31 Dec 2010	31 Dec 2009
	€000	€000	€000	€000	€000
Cash flows from operating activities					
Interest and commission receipts	78,759	52,741	60,158	38,158	1,642
Interest payments	(30,256)	(30,128)	(30,287)	(13,828)	(594)
Payments to employees and suppliers	(29,064)	(15,715)	(26,984)	(9,328)	(3,055)
Operating profit/(loss) before changes in operating assets/liabilities	**19,439**	**6,898**	**2,887**	**15,002**	**(2,007)**
(Increase)/decrease in operating assets:					
- reserve deposits with Central Bank of Malta	(855)	(1,360)	(68)	(1,971)	21
- loans advanced to customers and financial institutions	(200,665)	(297,583)	(27,250)	(1,038)	334
- investment securities	(670,319)	91,657	1,091,620	(694,718)	(638,882)
Increase in operating liabilities:					
- amounts owed to customers and financial institutions	290,750	474,850	(171,114)	291,006	616,229
Tax paid	(7,960)	(4,038)	(3,847)	-	-
Net cash (used in)/generated from operating activities	**(569,610)**	**270,424**	**892,228**	**(391,719)**	**(24,305)**
Cash flows from investing activities					
Acquisition of property and equipment	(171)	(431)	(1,026)	(2,142)	(41)
Disposal of property and equipment	9	-	109	-	-
Acquisition of intangible assets	(34)	-	(4,517)	(1,191)	(197)
Disposal of intangible assets	-	-	5,401	-	-
Acquisition of available-for-sale assets	(335,871)	(1,170,867)	(3,184,077)	(81,489)	(59,525)
Disposal of available-for-sale assets	1,126,144	941,592	1,987,289	84,768	59,641
Acquisition of assets held-for-risk management	(4,851)	(13,749)	(4,728)	-	-
Advances to parent	(15)	(200)	(1,273)	(77)	-
Advances to Group companies	(5,329)	(2,071)	(3,575)	-	-
Net cash used in investing activities	**779,882**	**(245,726)**	**(1,206,397)**	**(131)**	**(122)**
Cash flows from financing activities					
Proceeds from the issue of share capital	14,700	6,320	15,000	1,509	42,584
Proceeds from Shareholder's Contribution	1,250	9,325			
Proceeds from the issue of debt securities	237,359	-	4,937	14,735	-
Re-purchase of debt securities	(22,912)	(4,095)	-	-	-
Proceeds from the issue of subordinated debt securities	9,907	12,341	-	-	-
Interest paid on financial liabilities	-	-	-	-	-
Dividends paid	-	(7,143)	-	-	-
Net cash from financing activities	**240,304**	**16,748**	**19,937**	**16,244**	**42,584**
Net change in cash and cash equivalents	450,576	41,446	(294,232)	(375,606)	18,157
Cash and cash equivalents at beginning	(575,822)	(617,268)	(323,036)	52,570	34,413
Cash and cash equivalents period end	**(125,246)**	**(575,822)**	**(617,268)**	**(323,036)**	**52,570**

*15 month period to from 1 January 2011 to 31 March 2012

Bank Ratios

	31 Mar 2014 %	31 Mar 2013 %	31 Mar* 2012 %	31 Dec 2010 %	31 Dec 2009 %
Net interest income and other operating income to total assets	2.7%	2.4%	1.9%	2.2%	0.9%
Operating expenses to total assets	1.5%	1.1%	5%	1.1%	1.1%
Cost to income ratio	53.2%	41.9%	98.4%	37.0%	125.8%
Profit / (loss) before tax to total assets	1.4%	1.5%	0.08%	1.8%	(0.2%)
Profit / (loss) before tax to equity	22.1%	27.4%	2.25%	36.8%	(3.7%)
Profit / (loss) after tax to equity	14.4%	17.8%	0.05%	29.1%	(3.7%)

	2014 No	2013 No	2012 No	2010 No	2009 No
Shares in issue	98,050,107	62,350,107	56,030,107	41,030,107	39,520,970

	2014 €	2013 €	2012 €	2010 €	2009 €
Net assets per share	1.38	1.85	1.35	1.34	1.45
Earnings /(loss) per share (cents) based on profit after tax	22c	36c	1c	37.4c	(4.4)c

*15 month period to from 1 January 2011 to 31 March 2012

Directors' interest in the share capital of the Bank or in any related company as at 31 March 2014:

Medifin Holding Limited C34111

	Type & Class of Shares	Issued Shares	% Paid Up	Nominal Value Per Share in EUR
Mark Watson Holdings Limited	Ordinary B	627,855	100	1.000000
	Ordinary C	1,200,000	100	0.001000
HCS Holdings Limited	Ordinary B	224,233	100	1.000000
	Ordinary C	540,000	100	0.001000
JVP Holdings Limited	Ordinary B	362,903	100	1.000000
	Ordinary C	870,000	100	0.001000
AnaCap Financial Partners II L.P.	Ordinary A	40,188,556	100	1.000000
	Ordinary D	15,000,000	100	1.000000
XDP Holdings Limited	Ordinary C	180,000	100	0.001000
E- WealthS Ltd	Ordinary C	90,000	100	0.001000
Carey Pensions and Benefits	Ordinary C	120,000	100	0.001000

Mediterranean Bank plc C34125

	Type & Class of Shares	Issued Shares	% Paid Up	Nominal Value Per Share in EUR
Medifin Holding Limited	Ordinary A	98,050,106	100	1.000000

	Number of shares	Number of holders
Class A	98,050,106	1
Class B	1	1

	Number of holders	
Range	**Class "A"**	**Class "B"**
1 - 500	-	1
501 - 1000	-	-
1001 - 5000	-	-
5001 & over	1	-

The holders of ordinary A shares are entitled to one vote for each share. The holder of ordinary B share is not entitled to vote in respect of its shares

Company Secretary

Jaccarini, Edward

Senior Management

Watson, Mark A.	Chief Executive Officer
Bonello Ghio, Lorraine	Head of Administration and Human Resources
Calleja, Raymond	Head of Consumer Banking
Catania, Deo	Head of Operations
Chatard, Vincent	Chief Business Development Officer
Cini, Charles	Head of Corporate Banking
Jaccarini, Edward	Chief Financial Officer
Schmeltzer, Henry C.	Head of Commercial Strategy
Vicent, Joaquin	Head of Treasury and Investment
Wallace, Dominic	Chief Risk Officer
De Pauw, Xavier	Chief Officer – MeDirect

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