LOMBARD

Lombard Bank Malta p.l.c.

2021

ANNUAL REPORT & FINANCIAL STATEMENTS

LOMBARD

Lombard Bank Malta p.l.c.

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ANNUAL REPORT AND FINANCIAL STATEMENTS 2021

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"Readers are reminded that the official statutory Annual Report and Financial Statements 2021, authorised for issue by the Board of Directors, is in European Single Electronic Format (ESEF) and was published by a Company Announcement on the Malta Stock Exchange and can be found on https://www.lombardmalta.com. A copy of the Independent Auditor's report issued on the official statutory Annual Report and Financial Statements 2021 is included within this printed document and comprises the auditor's report on compliance with the requirements of the European Single Electronic Format Regulatory Technical Standard (ESEF RTS), by reference to the Capital Markets Rules."

Chairman's Statement to the Members

The performance of the Lombard Bank Group in 2021 was again conditioned by a difficult operating environment largely associated with the persistence of the COVID-19 pandemic and its economic repercussions. For Lombard Bank Malta p.l.c. (the Bank) the main sources of pressure on income streams were continuing low to negative interest rates and further increases in operating costs. These were partly offset by a substantial reversal of provisions on the loan book, which had a positive effect on the final results. The Bank's subsidiary, MaltaPost p.l.c., meanwhile continued to face logistical difficulties due to the pandemic and experienced generally higher costs, leading to reduced profitability. In the circumstances, the Group's pre-tax profit of €12.6 million, a year-to-year increase of 22%, must be considered a satisfactory outcome.

For the Bank, net interest income, the largest revenue source by far, resumed its upward trend in 2021 as interest earned on loans and advances rose more than that paid to depositors: the former reflected a sustained demand for credit even though average lending rates eased further, as well as higher earnings on the securities portfolio; the latter resulted from a combination of an expanded deposit base and largely unchanged average interest rates. A return to a rising trend also occurred in net fees and commission income, including from our card, wealth management and investment services operations. While all these revenue sources made a positive contribution to earnings, the Bank's total operating income, at €26.7 million, fell short of the previous year's level which however had included a sizeable one-off inflow.

Operating expenses meanwhile grew further mainly reflecting the cost of attracting and retaining professional expertise in a competitive labour market and the need to invest in new technologies and systems to meet the growing expectations of customers and the demands of regulators. In particular, the Bank introduced an automated anti-money laundering transaction monitoring platform, several upgrades to core networking devices, including additional protection against cyberattacks and biometric authentication systems for online card payments.

At the same time, the prudent stance we took at the peak of the pandemic with regard to provisions against credit exposures, together with the improved outlook for the Maltese economy and judicious management of our loan book, meant that no further exceptional provisions were necessary in 2021. As a result, the Bank's profit before tax increased by 32% to €12.2 million, in line with the Board's objective. This represented a return on equity of 6.2% and boosted shareholders' funds to a new peak of €132 million. The Board believes that these encouraging results confirm the resilience of the Bank's low-risk business model and has recommended, subject to regulatory approval, a gross dividend of 3 cent per share as well as a bonus issue of 1 share for every 75 shares held.

Despite the uncertainty created by the pandemic, the Bank's fundamentals remained strong. Customer confidence was maintained with deposits and lending increasing in tandem such that the relevant ratio was unchanged at a prudent level of 65.7%. The total capital ratio and the liquidity coverage ratio were both well above the statutory minimum levels at 16.2% and 225.3%, respectively while the leverage ratio, at 11.1%, was three-and-a-half times the required level. These solid financial buffers suggest that the Bank has the potential to maintain its growth momentum while keeping within the bounds of the Board's risk appetite.

During 2021 the Bank was faced with additional demands on its human and financial resources due to regulatory and compliance reporting obligations and other related decisions. Among the latter was the unexpected imposition at short notice of higher regulatory capital buffers, which has limited our ability to fully satisfy customer loan demand. Another development whose full impact cannot yet be measured was the decision of the FATF to place Malta on their Grey List. One early consequence was to induce some correspondent banks to terminate their relationships with local banks. At Lombard, our international banking business has experienced a recent decline.

The Bank adapted to this challenging operating environment on different levels. The quality of the loan book continued to improve, particularly through a further reduction in the proportion of so-called Non-Performing Exposures close to the target level set for 2022, in spite of the uncertain economic climate. Another development that has served to mitigate credit risk was the notable increase in household and personal lending in line with our diversification strategy. The strong take up of home loans was particularly welcome since this is a low-risk loan category and also makes a relatively small claim on the Bank's capital base.

During the year the Board also continued to oversee the implementation of the Business Plan 2020-2022 which defines the Bank's strategic priorities. A major focus has been the furtherance of ongoing projects in such business areas as home loans, credit cards and investment services designed to grow their contribution to operating income. Another priority has been the further strengthening of the Bank's governance, risk management and compliance functions. This included the creation of new professional development opportunities at all levels of the Bank, including the Board, the introduction of new policies and controls and the automation of several work processes. A challenge in this regard continues to be the limited availability in the market of specialised expertise. A third prong of the Business Plan is the expansion of our physical network in order to bring Lombard's services and products to a wider customer base. Further properties were acquired for this purpose in prime locations and some existing branches were upgraded. Work in all these areas will continue during the current year.

The year under review has also created challenges for the Bank's subsidiary, MaltaPost p.l.c., deriving mainly from the pandemic. Supply chain disruptions due to reduced air connectivity and a further decline in letter mail volumes combined with the lowest postal tariff rates in the EU all affected revenue flows. Labour and operational costs meanwhile continued to increase, particularly to finance infrastructure projects and the extension of the post office network, all designed to deliver a more efficient customer service and generate more income. As a result the company registered a small decline in pre-tax profits to €2.35 million.

Going forward, while the Bank's time-tested business model based on intermediation between savers and borrowers to finance viable economic activity promises to continue creating shareholder value, the Board is aware of the need to embrace change in the pursuit of long-term sustainability. An important challenge having capital-absorbing implications is the forthcoming introduction of new Basel III standards focussed on asset risk- weighting, particularly involving exposures secured by real estate and equity holdings. Another standard that will impact the manner in which our business is conducted relates to the evolving Environmental, Social & Governance (ESG) requirements. The Bank will continue to follow developments closely so as to ensure that relevant aspects are incorporated in its risk management framework. ESG workshops are planned for 2022 with assistance from external consultants. An ESG action plan will ensure effective implementation. A further change on the horizon promises to be the end of the ECB's current accommodative monetary policy and the unpredictable effects of higher interest rates on business cash flows, particularly in conjunction with the economic fallout of the heightened geopolitical tensions in Europe.

Facing these challenges while continuing to respond to customers' changing needs will require more investment in appropriate technologies and specialised human resources. As we proceed along the chosen growth path, the preservation of stakeholders' assets and the creation of value will remain a guiding principle. While innovative solutions will be sought, however, we will maintain our selective approach to onboarding depositors and borrowers and avoid exposure to economic sectors that have proved to be inherently risky.

The Board will continue to engage in a dialogue with the regulator also with a view to arriving at a meaningful application of the principle of proportionality in recognition of the size and non-complex business model of the Bank.

The Board experienced the sad loss of one of its non-executive members Michael Zammit who passed away while in office in February 2022. During his years in office Mr Zammit shared with the Board his extensive knowledge and experience of business in Malta. On behalf of the Board, I express appreciation for his commitment and the valuable contribution he made to the Bank.

In conclusion, on behalf of the Board I would like to thank the Bank's staff and management team, ably led by the Chief Executive Officer, Joseph Said, whose professional competence and dedication made the past year's encouraging results possible in spite of the disruption caused by the pandemic. I would also like to thank you the Bank's shareholders for your steadfast support and all our customers for their continued loyalty.

Signed on behalf of the Bank's Board of Directors on 20 April 2022 by Michael C. Bonello (Chairman) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Report and Financial Statements 2021.

The results for the financial year ended 31 December 2021 of the Lombard Bank Group combine the financial performance of Lombard Bank Malta p.l.c. together with its subsidiary and associate companies.

Summary Overview

Despite that the year continued to be dominated by challenging conditions, not least due to the uncertainties resulting from the COVID-19 pandemic, the performance of the Group proved to be resilient.

Notwithstanding the stiff competition across the whole spectrum of banking services, we stood firm in refusing to involve ourselves in those areas which could potentially distract us from our straightforward, prudent and conservative business model.

We developed new contacts in retail credit, while in commercial lending our relationships with existing customers remained strong. Improved forward-looking macroeconomic indicators brought about reversals in impairment provisioning when compared to the significant adverse forward-looking metrics as at the end of 2020.

Work on resolution of legacy Non-Performing Loans continued with the NPL stock maintained within the targets set. Prudent management of the loan book and sensible collateral positions ensured new Non-Performing Loans remained within acceptable margins.

Our transaction banking activities were below levels of previous years, mainly due to alternative and competing payment methods and reduced volumes following the grey-listing of Malta.

In our Investments activity, we launched advisory and discretionary services, with both gaining traction as customers chose to avail themselves of our services. Our asset management company and SICAV were authorised by the Malta Financial Services Authority and we now are assessing alternative approaches to adding our own UCITS funds to our suite of products.

We were enrolled as a Tied Insurance Intermediary for long-term insurance business products for IVALIFE Insurance Limited. The insurance products we have been authorised to distribute supplement the service offerings in Retail Lending and Investments activities.

Regulatory engagements were several and focused on areas across the Bank's operational, risk and governance structures, processes and controls. In this regard, considerable resources, time and effort continued to be directed towards ensuring strict compliance with regulatory requirements.

MaltaPost also faced a challenging year, with the continued difficulties caused by supply chain disruptions, as well as the continued decline of Letter Mail volumes and consequent reduction of respective income streams. Postal tariffs remain among the lowest in Europe and a tariff revision is necessary to address the loss-making postal services provided under the Universal Service Obligation. In this regard MaltaPost was in continuous engagement with the Malta Communications Authority so as to implement pricing revisions. As to MaltaPost's involvement in the general and life insurance sector, more time is required to allow these activities to mature to a point where they start contributing positively to the income streams of our subsidiary. For the financial year ended September 2021, MaltaPost realised a pre-tax profit for the year of €2.35 million, a decrease of 15% over the previous year.

Review of Financial Performance

Group Profit before Tax for the 2021 FY stood at €12.64 million, an increase of 22%.

Loans and Advances to Customers rose by 4% reaching €642.89 million. This portfolio was the main driver behind the 4% increase in Interest Receivable and Similar Income on Loans and Advances which now stand at €23.83 million. Interest Expense saw a 2% increase resulting from increased volume of Amounts Owed to Customers, which reached €977.14 million. Net Interest Income when compared to 2020 also increased by 4% to €19.56 million.

Net Fee and Commission Income improved by 10% to reach €5.21 million, supported by new lines of business which started to show a positive trend.

Group Employee Compensation and Benefits increased by 7% to €24.4 million, a reflection of the tight labour market and the need to maintain competitive and suitable compensation to Group staff. The Bank's Cost Efficiency Ratio was 60.8% (FYE 2020: 52.4%) while that of the Group stood at 81.9% (FYE 2020: 75.8%). While operating costs remained well under control, increased fees and costs associated with obligations to satisfy regulatory requirements and the enhancement of Compliance capabilities all contributed to increasing the cost base.

The Bank's Impairment Allowances as determined by International Financial Reporting Standard 9 (IFRS 9) for the year ended 31 December 2021 stood at €26.16 million. Consequently, the change in 'Expected Credit Losses' (ECL) resulted in a net impairment reversal of €1.46 million compared to a charge of €3.97 million in the previous year. At the reporting date, though the level of risk in the lending portfolio increased, the quality of the Bank's financial assets remains sound.

Liquidity and Own Funds

Over the years, the Bank relied on a diversified liquidity funding base which has proven to be relatively stable.

Advances to Deposits Ratio stood at 65.8% compared to 66.0% same period last year.

Total Assets stood at €1,175.39 million (2020: €1,130.96 million), while Equity Attributable to the Shareholders of the Bank rose by 9.0% to €137.3 million. Net Asset Value (NAV) per share stood at €3.07 (2020: €2.85). Group Earnings per Share (EPS) increased to 16.8 cents. Return on Assets (ROA) stood at 0.7% (2020: 0.6%) while post tax Return on Equity (ROE) was 5.7% (2020: 5.4%).

Treasury Management

In determining the placement of funds, our main objective remained that of capital protection. We therefore stood by our prudent approach of investing the bulk of our liquidity in the local economy mainly by way of holdings in Government of Malta securities and in entities listed on the Malta Stock Exchange. The portfolio in quality foreign bonds was retained at constant nominal values.

International money market placements with authorised counterparties remained selective, though practically always in short tenors.

As expected, the grey-listing of Malta impacted our correspondent banking activity. Such counterparty relationships are key to ensuring continued access to international currency and money markets via a network of overseas banks. Some counterparties exited Malta altogether as a jurisdiction, resulting therefore in their terminating relationships also with us. We held several presentations with various overseas banks explaining our risk appetite for business and also the measures we have in place to ensure that our systems and processes were sufficiently robust to combat financial crime effectively.

Risk Management

Risk-taking is an integral aspect of a Bank's intermediation activity and as a result a whole range of financial and non-financial risks need to be managed. This involves, to varying degrees, knowingly accepting and managing such risks. In this regard the Bank continues to implement an Enterprise-wide Risk Management Framework that involves a comprehensive and coordinated approach to identify, monitor and measure potential risks and subsequently mitigate these risks to within the limits of the Bank's own risk appetite. The management and control of risk is encompassed within approved policies and procedures that are integrated in the decision- making processes. Our overall risk management framework lays out this foundation and seeks to maximise return on assets while safeguarding depositors' funds at all times - always in compliance with statutory requirements and within the risk tolerance limits approved by the Board of Directors.

The Risk Management Function reports to the Audit & Risk Committee and Board of Directors and provides a detailed insight into the Bank's risk management environment and situation of tolerance limits as per our Risk Appetite Statement. During the year, the Risk Appetite Statement was reviewed and updated to reflect current views on respective risks and to provide further granularity to the measurement processes.

Solvency requirements show that the Bank's 'Pillar I' Total Capital Ratio ('TCR') at the end of 2021 stood at 16.2% increasing from 15.8% the previous year. The Bank continues to maintain a strong capital position and is fully compliant with regulatory capital requirements. The leverage ratio, that is monitored and reported to the Board regularly, stood at 11.1% which is more than 3 times the minimum regulatory requirement of 3%.

Key liquidity metrics such as the Liquidity Coverage Ratio ('LCR'), the Net Stable Funding Ratio ('NSFR') and the Loan-to-Deposit Ratio are constantly monitored and regularly reported to the Board. The Bank ensures that it remains sufficiently liquid at all times and in line with its risk appetite. At the end of 2021, these key metrics stood at 225.3%, 148.4% and 65.7% respectively and well within our risk appetite.

Also, our Internal Capital Adequacy Assessment Process (ICAAP) is reviewed annually and robust stress testing is regularly carried out on Capital and Liquidity to assess the Bank's resilience to extreme but plausible shocks.

Human Resources

The logistical difficulties presented by the Pandemic resulted in about 50% of staff members working remotely on a roster basis as necessary. This allowed the Bank to operate seamlessly with all branches remaining open for service even during lockdown periods. The commitment and support of those staff members whose work required them to be present at the office is recognised and much appreciated. Also duly acknowledged are the efforts of all staff members to remain safe at the office and outside, and to work diligently and to the highest standards at all times.

Competition for talent remained stiff with our recruitment programme remaining open throughout the year so as to fill vacancies in all areas. The challenge is not limited to merely attracting competent persons of the required skills and competencies but also to retain staff. We remain committed to offer a work environment that meets with the priorities and aspirations of staff, whether these be related to career progression or work-life balance goals.

We provided learning opportunities for staff members to improve their skills and technical qualities.

The staff complement at the Bank stood at 205 as at the end of 2021 while that of the Group reached 1,004. Our staff remains key in the achievement of results and the success of the Group.

Projects

Investment in technology was made in three main areas: renovation of core elements of the infrastructure, meeting the specific needs of certain business lines and improving capabilities in regulatory reporting and financial crime compliance.

In January 2021 our new branch in Attard opened for business, receiving positive feedback from customers. We are confident that a larger part of the community in the area will experience the convenience of our service offerings at this branch. Meanwhile we acquired other properties, in line with our objective of selectively extending our geographic footprint so as to give us representation in those localities that we know would welcome our presence. We continue to believe that in the Maltese market, a physical presence is important, more so by those customers who value the personalised service offered by Lombard Bank. Renovation of property acquired will be staged in a manner which allows for a smooth assimilation of the activity into the Bank's operations.

We continued with our Melita gold bullion coin issue in conjunction with the Central Bank of Malta. The 2021 coin was struck in four denominations, with this issue being well received and sold out soon after it became available. Besides being of interest to local collectors, the issue attracted the interest of overseas collectors. Also, jointly with the Central Bank of Malta we issued the first Melita silver bullion coin, weighing ten ounces.

Our subsidiary MaltaPost proceeded with its project of introducing battery-operated vehicles, with its fleet reaching a total of 54 such vehicles, thereby reducing reliance on the use of vehicles powered by fossil fuels.

Community Involvement

Our commitment to actively support the local community and to place emphasis on assisting socially meaningful projects continued throughout the year. We do so in various ways, including proposals aimed at preserving and enhancing heritage and extending assistance to staff members who on their own initiative support worthy causes.

Outlook

A positive set of results, a healthy brand and sound fundamentals encourage us to face the coming year with optimism. However, prospects much depend on the resilience of the economic recovery and the general operating environment. Other challenges may also arise from likely increases in euro interest rates and the disruption that these may cause once transmitted to the real economy.

We remain committed to our obligations in respect of the environment, social responsibilities as well as matters concerning good governance. In the coming year these issues will be given focus and the manner in which any resulting changes may impact our business model, if at all, needs to be suitably determined.

Meeting with these challenges will require further investment in technology and human resources - which we are determined to address accordingly. We therefore enter 2022 with enthusiasm and determination supported by a solid set of results, healthy ratios, a strong balance sheet, a loyal customer base and a fine team of staff members.

Signed on behalf of the Bank's Board of Directors on 20 April 2022 by Joseph Said (Chief Executive Officer) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Report and Financial Statements 2021.

The Group

The Lombard Bank Group (the Group) consists of Lombard Bank Malta p.l.c. (the Bank), Redbox Limited, Lombard Capital Asset Management Limited, Lombard Select SICAV p.l.c. and the MaltaPost p.l.c. Group.

Principal Activities

The Bank was registered in Malta in 1969 and listed on the Malta Stock Exchange (MSE) in 1994. It is licensed as a credit institution under the Banking Act, 1994 and is an authorised currency dealer and financial intermediary. It is also licensed to carry out investment services in terms of the Investment Services Act, 1994 and is an enrolled Tied Insurance Intermediary of IVALIFE Insurance Limited under the Insurance Intermediaries Act, 2006.

The Bank is a member of the Depositor Compensation Scheme and the Investor Compensation Scheme set up under the laws of Malta. It is also a member of the MSE for the purpose of the carrying out of stockbroking on the MSE. The Bank has a network of branches in Malta and Gozo providing an extensive range of banking and financial services. A list of branches, outlets and departments is found on page 27 of this Annual Report.

During the year under review, Redbox Limited, a company virtually wholly owned by the Bank continued to serve as the special purpose vehicle holding as at 31 December 2021, the Bank's 71.5% shareholding in MaltaPost p.l.c., with the remaining 28.5% of the ordinary share capital of MaltaPost p.l.c. being held by the general public. MaltaPost p.l.c. is Malta's leading postal services company, being the sole licensed Universal Service Provider of postal services in Malta. More information about the MaltaPost Group may be found on www.maltapost.com.

Lombard Select SICAV p.l.c. holds a collective investment scheme licence in terms of the Investment Services Act, 1994.

Lombard Capital Asset Management Limited is licensed to act as a UCITS management company and to provide investment management services to undertakings for collective investment in transferable securities (UCITS schemes).

Review of Performance

An overview of the development in the Bank's business and that of its subsidiaries during the year under review together with an indication of likely future developments may be found in the 'Chief Executive Officer's Review of Operations' of this Annual Report.

Group profit before tax for the financial year ended 31 December 2021 amounted to €12.6 million (2020: €10.4 million). Profit attributable to equity holders of the Bank was €7.5 million (2020: €6.6 million).

Net interest income at €19.6 million was 3.6% higher than the previous year. Increase in credit activity compensated for pressure on interest rates especially in treasury operations. New lines of business contributed to an increase of 10.0% in net fee and commission income.

Net loans and advances to customers increased by 3.5% to €642.9 million. Customer deposits increased by 3.8% to €977.1 million. Group post tax return on equity for 2021 was 5.7% (2020: 5.4%). Group total assets increased to €1,175.4 million (2020: €1,131.0 million). Total capital ratio at 16.2% (2020: 15.8%) exceeded the minimum regulatory requirements.

Bank cost efficiency ratio at 60.8% (2020: 52.4%) was mainly a reflection of human resource expenses as well as increased regulatory compliance costs.

A reversal of €1.5 million was made for 'Expected Credit Losses' (ECL) as determined by International Financial Reporting Standard 9 (IFRS 9) compared to a charge of €4.0 million in the previous year.

In a year of continued and significant disruption arising from the spread of the COVID-19 pandemic, MaltaPost p.l.c. managed lower profitability as increased costs were not recovered through increases in either volumes or price. As traditional postal volumes continued to drop, other non-postal income arose from document management services, bill collection, financial services and insurance.

Equity attributable to equity holders of the Bank grew by a further 9.0% to €137.3 million. Group net asset value (NAV) per share stood at €3.07 (2020: €2.85). Group earnings per share (EPS) increased to 16.8 cents.

Profits after taxation of €7.9 million and €7.8 million for the Group and the Bank, respectively were registered for the twelve months ended 31 December 2021.

Based on the above, as was the case for 2020, a gross dividend of 3 cent per nominal 25 cent share (net dividend of 1.95 cent for a total amount of € 872,956) for the twelve months ended 31 December 2021 is being proposed for approval by shareholders at the 2022 Annual General Meeting, subject to regulatory approval.

Furthermore, a bonus share issue of one (1) share for every seventy five (75) shares held is being proposed by the Board of Directors. The bonus issue will be funded by a capitalisation of reserves amounting to €149,000. Resolutions to this effect will be proposed to the 2022 Annual General Meeting, subject to regulatory approval.

Board of Directors and Senior Management

The composition of the Bank's Board of Directors and Senior Management is shown in the section on 'Company Information' on page 26 of this Annual Report and further information is given in the 'Statement of Compliance with the Principles of Good Corporate Governance'.

Risk Management

The Financial Risk Management note to the Financial Statements (note 2), illustrates the process of how the Group identifies and manages its risks and uncertainties. The main categories of risk described in this note are credit risk, market risk, liquidity risk and operational risk. The same note includes extensive detail of the processes undertaken by the Bank to manage these risks.

The Directors are required by the Companies Act, 1995 to prepare financial statements which give a true and fair view of the state of affairs of the Group and the parent company as at the end of each reporting period and of the profit or loss for that period.

Statement of Directors' Responsibilities for the Financial Statements

In preparing the financial statements, the Directors are responsible for:

- ensuring that the financial statements have been drawn up in accordance with International Financial Reporting Standards as adopted by the EU;
- selecting and applying appropriate accounting policies;
- making accounting estimates that are reasonable in the circumstances; and
- ensuring that the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Group and the parent company will continue in business as a going concern.

The Directors are also responsible for designing, implementing and maintaining such internal controls as they deem necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and that comply with the Companies Act, 1995 and the Banking Act, 1994. They are also responsible for safeguarding the assets of the Group and the parent company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The financial statements of the Bank for the year ended 31 December 2021 are included in this Annual Report and made available on the Bank's website. The Directors are responsible for the maintenance and integrity of the Annual Report on the website in view of their responsibility for the controls over, and the security of, the website. Access to information published on the Bank's website is available in other countries and jurisdictions where legislation governing the preparation and dissemination of financial statements may differ from requirements or practice in Malta.

Statement of the Directors pursuant to Capital Market Rule 5.68

The Directors confirm that, to the best of their knowledge:

- the financial statements give a true and fair view of the financial position of the Bank as at 31 December 2021, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU; and
- the Annual Report includes a fair review of the development and performance of the business and the position of the Bank, together with a description of the principal risks and uncertainties that they faced.

Investment Services Rules for Investment Service Providers

In accordance with Rule R1-2.2.3 of the Investment Services Rules for Investment Service Providers regulated by the Malta Financial Services Authority, licence holders are required to disclose any regulatory breaches of the Rules or other regulatory requirements in this Annual Report. The Directors confirm that during the reporting period, there were no breaches of the Investment Services Rules or other regulatory requirements, which were subject to an administrative penalty or other regulatory sanction other than those in the public domain.

Information provided in accordance with Capital Market Rule 5.70.1

There were no material contracts to which the Bank, or any of its subsidiaries were a party, and in which any one of the Bank's Directors was directly or indirectly interested, except for transactions disclosed in the notes to the financial statements.

Going Concern

In compliance with Capital Markets Rule 5.62 and after having duly considered the Bank's performance, the Directors declare that they expect the Bank will continue to operate as a going concern for the foreseeable future.

Capital Markets Rules – Disclosures

In terms of Capital Markets Rule 5.64, the Directors are required to disclose the following information.

As at the Annual General Meeting held on 28 May 2021, the authorised share capital of the Bank was €20,000,000 made up of 80,000,000 ordinary shares of a nominal value of 25 cent each. As at that date the issued and fully paid-up share capital of the Bank was €11,044,479 divided into 44,177,914 ordinary shares of a nominal value of 25 cent each, all of one class.

Following the approval by the Bank's shareholders at the above-mentioned 2021 Annual General Meeting, the amount of €147,262 from the Bank's Retained Earnings Account was capitalised for the purpose of issuing 589,047 fully paid ordinary shares of a nominal value of €0.25 per share representing 1 bonus share for every 75 shares held allotted to the eligible members appearing on the Bank's Register of Members as at close of trading on the Malta Stock Exchange on 23 June 2021. Following this allotment, and as at 31 December 2021, the Issued and fully paid-up Share Capital of the Bank increased to €11,191,740.25 divided into 44,766,961 ordinary shares of a nominal value of 25 cent each, all of one class.

Amendments to the Memorandum and Articles of Association of the Bank are effected in conformity with the provisions in the Companies Act, 1995. Furthermore, in terms of the Articles of Association:

- Directors may be authorised by the Bank to issue shares subject to the provisions of the Memorandum and Articles of Association and the Companies Act;
- Directors may decline to register the transfer of a share (not being a fully paid share) to a person of whom they do not approve;
- Directors may decline to recognise any instrument of transfer, unless accompanied by the necessary evidence;
- no registration of transfers of shares shall be made and no new particulars shall be entered in the register of members when the register is closed for inspection; and
- the Bank may, from time to time, by extraordinary resolution reduce the share capital, any Capital Reserve Fund, or any Share Premium Account in any manner.

Currently there are no matters that require disclosures in relation to:

- holders of any securities with special rights;
- employee share schemes;
- restrictions on voting rights or relevant agreements thereto; or

- significant agreements to which the Bank is a party and which take effect, alter or terminate upon a change of control of the Bank

The Remuneration Report on page 23 refers to the financial contributions towards retirement gratuities that the Board of Directors approves from time to time. The same Board had previously resolved that a retirement gratuity be eventually paid on an *ex gratia* basis to the Chief Executive Officer on his retirement.

The rules governing the changes in Board membership are contained in the 'Statement of Compliance with the Principles of Good Corporate Governance'.

Shareholders holding five per cent (5%) or more of the share capital of the Bank:

	Shares in Lombard Bank Malta p.l.c.	
	31 December 2021	31 March 2022
National Development & Social Fund (NDSF)	49.01%	49.01%
Virtu Holdings Ltd	9.89%	9.89%
LifeStar Insurance p.l.c	5.59%	5.59%
First Gemini p.l.c.	5.31%	5.31%

Directors' Interest in Group Companies

Joseph Said, who is a Director of the Bank, is also a Director of the following companies that have a shareholding in the Group as follows:

	Shares in Lombard Bank Malta p.l.c. at 31 December 2021*	Shares in MaltaPost p.l.c. at 31 December 2021*
Safaco Ltd	42,751	44,745
First Gemini p.l.c.	2,375,389	36,341

*There were no changes from 31 December 2021 to 31 March 2022.

In addition Joseph Said holds preference shares in Safaco Ltd.

Audit & Risk Committee

The Audit & Risk Committee is composed of non-executive Directors and is intended to ensure effective internal controls, compliance and accountability. The Committee also acts to ensure that high ethical standards are maintained, as explained in the 'Statement of Compliance with the Principles of Good Corporate Governance' in another section of this Annual Report.

Auditors

PricewaterhouseCoopers have expressed their willingness to continue in office as auditors of the Bank and a resolution proposing their reappointment will be put at the forthcoming Annual General Meeting.

Events occurring after the end of the accounting period

There were no significant events affecting the Bank or any of its subsidiary undertakings which have occurred after 31 December 2021.

Non-Financial Statement

The Companies Act requires that a non-financial statement be included in this report containing information on the Group's development, performance, position and impact of its activity, relating to, as a minimum, environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters and this in the form of particular disclosures on certain aspects.

1. Business Model

The Bank is a Malta-based bank and for financial stability purposes is considered by the Central Bank of Malta as a core domestic bank, catering mostly for the local economy, and therefore actively supporting economic actors in their activities. The lending activity of the Bank consists mainly of Commercial and Retail Lending. Commercial Lending is largely characterised by loan facilities to the commercial sector with short to medium term maturities. Retail Lending consists mainly of home loan facilities with medium to long term maturities. Asset diversification strategy is intended to increase the resilience of the Bank's loan book and its lending capacity. The Bank was enrolled as a Tied Insurance Intermediary for long term insurance business and can therefore provide its Home Loan customers with a more comprehensive service offering. Lending is funded by a diversified deposit base and underpinned by solid capital and liquidity ratios. The Bank has never relied, and does not intend to rely, on the interbank market for its funding requirements, and retains ample liquidity from its retail operations. This approach to business underpins the Bank's image and facilitates pricing decisions. In this respect the Bank seeks to progress slowly, prudently yet surely, as evidenced by the quality of its assets and relationships. The Bank follows risk review processes to ensure that business is in line with its risk appetite frameworks and its compliance standards, which themselves are also reviewed periodically in light of regulatory developments and emerging risks. The Bank continues seeking to expand its product and services portfolio into the retail market. In this regard, the Bank has taken steps to widen its investment service offerings by manufacturing its own UCITS funds, and for this reason incorporated its own SICAV and fund manager, Lombard Select SICAV p.l.c. and Lombard Asset Management Limited respectively, both duly licensed by the Malta Financial Services Authority.

The Bank's business model is based on building stakeholder value by delivering financial services and solutions in a prudent manner and by setting the highest standards in professional behaviour and implementing the highest standards of compliance. The Bank's competitive strengths are in its unique business operating model, its conservative outlook towards risk and its robust fundamentals. The characteristics of its business model give the Bank a competitive advantage, enabling it to continue to deliver value to all its stakeholders in a challenging environment which remains highly competitive and increasingly regulated. The Bank's brand, which stands for the provision of personalised and tailored financial services, remains strong.

The Bank's subsidiary, MaltaPost p.l.c. (MaltaPost) is Malta's leading postal services company, being the sole licensed Universal Service Provider of postal services on the Maltese Islands in terms of the Postal Services Act (Chapter 254 Laws of Malta) and under the terms of the Universal Postal Union Convention and Constitution on behalf of the Government of Malta. It has a network of 42 Post Offices and 25 Sub-Post Offices around Malta and Gozo providing an extensive range of postal and financial services.

Postal services remain characterised by a decline in Letter Mail volumes and in the corresponding income. MaltaPost continues to pursue its diversification into logistics, document management, insurance and financial services. In insurance, MaltaPost has a 25% shareholding in IVALIFE Insurance Limited, a company licensed to conduct long-term business of insurance and a 49% shareholding in PostaInsure Agency Limited, an insurance agency for MAPFRE Middlesea p.l.c. Document management services are offered through a fully owned subsidiary, Tanseana Limited. While MaltaPost remains committed to be the trusted postal and logistics operator offering a comprehensive product portfolio, these investments in non-postal sectors are intended to supplement income streams from the core activity.

As evident from the above disclosures, there were no notable changes to the core business strategies and business models of Group entities. The pandemic has not had an impact on the validity of the Group's business models, though consequent to the adverse impact that the pandemic has had on economic growth in Malta, as indeed worldwide, it is expected that the Group will face pressures on income streams in times ahead.

2. Anti-Corruption and Bribery Matters

The Group has a zero tolerance policy to bribery and corruption, financial crime and breaches of the relative laws and regulations. The Group developed and maintains robust policies designed to prevent and detect potential bribery and corruption in the form of an Anti-Bribery and Corruption (ABC) Policy and Whistleblowing Policy.

The implementation of these policies is by means of processes, procedures and respective controls, which are embedded in the Group's structures and manuals in order to ensure that staff members act responsibly within the work place and outside. Guidelines and instructions regarding ABC and Whistleblowing are applicable and available to all staff members. All staff members, including Directors and, where relevant, associated persons are required to comply with the principles outlined. The Group supports a 'speak-up attitude' to encourage reporting of concerns relating to what might appear to be suspected illegal, unethical or otherwise improper acts or their concealment. The same standards are expected from any third parties providing services for or on behalf of the Group. Staff members who fail to comply with the Group's policies and standards may face disciplinary action, up to and including dismissal or termination of employment. Training sessions keep staff members abreast of their obligations at all times.

The Risk Management and Compliance functions exercise oversight over the implementation of respective Policies, the former by including ABC in risk assessments and the latter by ensuring constant standards of compliance. The Risk, Internal Audit and Compliance functions also work together to ensure the proper functioning of these policies. Matters arising, if any, out of the adoption of these policies are reported by the Compliance function in its reports to the Audit & Risk Committee and Board of Directors. Policies are reviewed annually, or more often as required, by the relative business and internal control functions with suitable recommendations, as is necessary, made to the Audit & Risk Committee and the Board of Directors. During the year under review, there were no reported cases on the basis of the abovementioned policies and therefore no necessary investigations.

3. Social and employee-related matters

Social and employee matters are given full attention by the Group. The Group's human capital is a key resource for the carrying out of business. The ability to attract and retain human resources of the right skill- mix and experience condition to a large extent the Group's performance. The risk of not attracting or retaining the appropriate quality staff in line with the Group's business needs is mitigated generally by the approach to managing this resource and specifically through a number of measures. Further information on employees may be found in the Chief Executive Officer's Review, Human Resources on page 6 and note 31 to the Financial Statements.

Collective Agreements are in place at the Bank and MaltaPost, setting the conditions of work and generally regulating the employer/employee relationship. The prevailing Agreements contain a number of measures of assistance to staff members including days of special paid leave additional to those stipulated at law, such as Study Leave, and extended Bereavement Leave. The Group enjoys harmonious industrial relations with the full co-operation of respective trade unions, staff members and their representatives. No industrial disputes were registered in 2021.

Oversight of key indicators, by which human resource performance is evaluated is maintained by the Head of the Human Resources function and reported to senior management and the Risk Management function as appropriate for suitable action if and as required. Performance management takes into consideration leadership competencies required by individual positions as well as the Group's corporate values. The Group does not place quotas on the number of staff members whose personal circumstances require them to work on reduced hours or need to absent themselves from work for an extended period of time on Child Care Leave or other absences related to immediate family matters. In this regard, the Group is committed to supporting and developing family friendly measures further.

The Bank also extends a number of products and services to Group staff members on favourable terms including, among others, advantageous terms on home loans and other personal borrowing. The Group keeps an active line of communication with staff members through circulars, branch / department staff meetings and one-to-one meetings among others, and is committed to maintaining a working environment where staff is valued, respected and supported to fulfil potential.

All members of staff are treated on equal terms with regard to career development and appointments and the Group supports and practices gender equality and diversity. The Group, however, does not set specific targets in this regard, as it firmly believes that progress is dependent largely on skill, competencies, attributes and performance.

The Group abides by all applicable laws, rules and regulations relating to employment. While conscious of the fact that the legal obligations are the minimum acceptable standard, the Group strives to surpass standards in this area and continues to increase awareness among staff. The Group, for example, with about 6%, well exceeds the obligation to have 2% of the total staff complement composed of persons with disabilities. This reaffirms the Group's social outlook and its commitment to create a positive impact in society. Remuneration levels are regularly reviewed to ensure that they are in line with the Group's Remuneration Policy. Rewards reinforce positive conduct and promote Group culture.

Investing in learning and development equips the Group's diverse staff complement with the knowledge and expertise to work in line with applicable internal policies and handbooks. Training programmes are tailored to meet with identified training needs and training facilities are in place for that training delivered in-house. As in previous years, during 2021, Group staff members participated in several training sessions, and this, apart from on-the-job training programmes. Training is driven by the requirement to meet identified training needs rather than by the pursuit of specific numerical targets, which are therefore not set.

The Group maintained measures dedicated to the protection of staff members and customers alike in response to COVID-19. Also, the Bank continued to adopt remote working schedules for those staff members whose work duties lent themselves to teleworking - up to 50% of staff members participated on an alternating basis. The Group followed at all times directions and guidance of the Health Authorities concerning COVID-19 mitigation measures. In cases where premises needed to be sanitised, this was carried out as per Health Authority recommendations.

Regarding consumer relations and protection, the Group adheres to all respective Regulatory requirements such as, *inter alia*, those arising from Markets in Financial Instruments Directive II (MiFID II), as also reflected in the MFSA Conduct of Business Rulebook, the Cross Border Payments Regulation II (CBPR II), Payment Services Directive II (PSD II), Payment Accounts Directive (PAD) and Banking Rule BR/22 Complaints Handling Procedures for Credit Institutions Authorised Under the Banking Act, 1994.

The Group Complaints Management policies and relevant details on respective web sites provide the information required for a consumer to submit complaints. During 2021 the Bank had no complaints referred to the Arbiter for Financial Services. In the case of MaltaPost, customer complaints accounted for 0.002% of all mail items handled.

The Group does not actively push customers away from physical delivery channels. The Bank firmly believes that in the Maltese market a physical presence remains an important element of its offering, more so in respect of customers who expect a personalised service. Maintaining a presence in core community areas is given importance so as to facilitate accessibility and delivery of important services to the community. Of course, its digital banking services will continue to be enhanced and offered where / when preferred.

Please also refer to the Chief Executive Officer's Review, Corporate Social Responsibility on page 6 and to Principle 12 'Corporate Social Responsibility' on page 20 for further information concerning social matters.

The Group is therefore satisfied with its non-financial performance in respect of social and staff related matters.

4. Health and Safety

Maintaining the highest levels of health and safety and physical security of staff is of paramount importance. As a minimum, the Group meets with all the statutory obligations set out in the Occupational Health and Safety Authority Act, 2000. Further measures for the management of health and safety are adopted by way of standards in Collective Agreements, appointment of Health & Safety Officers and appointment of local first aiders and fire wardens. Regular checks of related processes and systems are carried out with outcomes reported to the Health & Safety Officers, who will take action as and if required. Furthermore, health and safety risk assessments are carried out to ensure that situations that may pose risks to the health and safety of staff and others on Group premises are identified and mitigated. Occupational health awareness training is also provided. Some Group staff benefit from personal accident insurance cover and others benefit from private health care insurance, as well as death in service cover.

5. Human Rights

The Group is aware of the importance of ensuring that human rights are upheld across its operations. In this respect the Group carries out its business without discrimination, respecting the standards set by national law or higher standards as applicable, such as effective information and consultation processes, particularly where these affect the place and conditions of work. Business conduct policies are in place to support this stance, which extend also to counterparties. The Group avoids business with counterparties operating in economic sectors that may be linked to or present a significant risk to violation of human rights or to social vices. Additionally, the Bank's AML/CFT processes, inter alia, assist in the identification of the proceeds of potential human rights abuses. Any suspicions resulting from these processes are reported to law enforcement as per current legislative requirements. Services that promote financial inclusion have been introduced also by way of the PostaPay&Save account which serves as a basic payment account. This account was introduced well before this was required by regulation. The account allows persons who were previously unable to open bank accounts to enjoy the facilities of basic payment accounts with relative services. PostaPay&Save accounts have now been opened for more than 12,000 individuals, though about 11,000 remain active.

During the year under review, the Group did not encounter any issues, claims or reports on any human rights related matters and / or violations. A grievance procedure is in place to provide effective remedy as and when needed. The Group is committed to investigate any reports of human rights violations. As previously stated, the Bank has in place a Whistleblowing Policy which covers among others, related issues. In accordance with this Policy reports are submitted to the Heads of Risk Management and Internal Audit. During the year ending 2021, no reports in accordance with this Policy were submitted.

Premises, including self service areas and ATMs, meet all accessibility regulations, apart from where physical restrictions make this impossible, in which case discussions with the relevant regulatory bodies are held. Property added to the Group's real estate during 2021 provides full accessibility to people with disabilities.

6. Environmental Matters

The Group does not execute a formal policy relating to environmental matters given its size, scale and nature of operations. Nonetheless, the Group is mindful of the important role it has to play to contribute towards safeguarding the environment as much as is possible, thereby minimising the environmental impact of its operations. Besides assisting in the reduction of costs, being environmentally friendly and taking measures to reduce its carbon footprint fits within the overall corporate social responsibility initiatives of the Group. The Group continues with its programme of investment aimed at reducing reliance on fossil fuel power as far as practical and opportune.

Relative initiatives included installation of PVA panels and other energy efficient installations such as modern Heating Ventilation Air Conditioning (HVAC) systems and Light Emitting Diodes (LED) light fittings. Waste separation facilities and recycling processes are in place and are ongoing throughout the Group.

The Group operates 54 electric vehicles replacing internal combustion motor vehicles, thereby contributing to reducing emissions. Installation of charging points in parking areas and bicycle racks are further initiatives. The Bank also runs a scheme, which reimburses public transport costs for most staff members so as to encourage reduced use of private motor vehicles when commuting. The scheme effectively provides for free public transport on work days.

Adherence to respective policies is the responsibility of operations management, while oversight is the responsibility of Risk Management Department.

The Group continues with its efforts to preserve buildings of architectural importance now serving as modern and functional branches/offices. 'Restoration with respect' continues to be the Group's motto when acquiring and renovating buildings of architectural heritage value, delivering them back to society in their original splendour.

Preservation and reuse of such property reduces resources and material consumption, generates less waste and consumes less energy than developing greenfield and / or brownfield sites.

MaltaPost runs a postal museum also in a restored building in Valletta housing a collection of artefacts related to Malta's postal history. Additions to the collection of artefacts are made as opportunities arise, thereby enriching further the country's postal heritage.

The Group's business is mostly carried out in Malta. The Malta climate-related risks are not expected to have a consequence on the impairment or fair value of assets, give rise to credit losses and/or potential provisions or contingent liabilities. Therefore the impact of climate change on the financial performance is not expected to be material. That said, like any other business the Group is however not shielded from the economic risks of climate change, which in turn can have an impact on the financial performance.

The Bank is mindful of the evolving Environmental, Social & Governance (ESG) regulatory landscape. It continues following developments closely so as to further determine how ESG considerations influence the manner in which it carries out its business and the extent to which such considerations are incorporated within its risk management framework. ESG workshops are planned for 2022 with assistance from external consultants. An ESG action plan will also ensure effective implementation.

7. Risk Reporting

A Group enterprise-wide risk management framework provides the foundation for the risk management reporting processes. This framework is subject to constant evaluation to ensure it meets the challenges and requirements of the markets in which the Group operates, as also regulatory standards and industry best practices.

The Group's strong governance framework is supplemented by clear organisation structures and reporting lines, and well defined procedures embedded in processes throughout the Group and is subject to ongoing review.

The organisation structure ensures that responsibilities and duties are well-defined and known. Within the functions defined, processes are in place to identify, monitor, manage and report risks. The processes also include internal control mechanisms, together with appropriate administrative and accounting procedures.

The Bank has a formal Risk Management Policy which provides the foundation for achieving a balance between sound practices and profitability by applying strict internal controls and discretionary limits, and optimising the returns thereof, in line with the Bank's risk appetite.

The risk appetite determines the maximum risk assumed to meet business objectives. From time-to-time the risk appetite is updated for the purposes of strategic direction after a thorough analysis of the current risk profile. The risk appetite is reviewed by the Board at least once a year.

The main categories of risk to which the Group is exposed to are:

Capital Risk Management – This is the ability to hold sufficient capital to comply with regulatory requirements, safeguard the Group's ability to continue as a going concern, provide adequate returns for shareholders and to maintain a strong capital base to support the development of the business (Notes to the Financial Statements note 2.7; Additional Regulatory Disclosures notes 6 and 7).

Credit Risk – This is the risk of suffering loss should any of the Group's customers, clients or market counterparties fail to fulfil their contractual obligations to the Group. Credit risk mainly arises from customer loans and advances, but also from exposures arising from investment activities. It constitutes the Bank's single largest risk in view of its significant lending and securities portfolio. To minimise credit risk, facilities are generally adequately secured by tangible security that is reviewed periodically to ensure that the collateral still covers the facilities (Notes to the Financial Statements note 2.3; Additional Regulatory Disclosures note 2).

Market Risk – This is associated with fluctuations in the fair value or future cash flows because of changes in market prices. The Bank does not operate a Trading Book and hence this is limited to Interest Rate Risk, Currency Risk and Equity Price Risk. The Bank is accordingly able to manage the interest rate terms of its financial assets and simultaneously to effect changes to interest terms of liabilities reflecting the Bank's strategy together with market developments (Notes to the Financial Statements note 2.3; Additional Regulatory Disclosures note 2).

Non-Financial Risks – These are the risk of losses resulting from the lack of skilful management or good governance within the Bank and the inadequacy of proper control. Non-financial risks and losses arising therefrom cover a wide spectrum of areas including financial crime, regulatory compliance, fraud, people, systems and processes which would in turn affect income and capital. The Bank's risk appetite, which is determined by the Board and is one of the four pillars of its Risk Management Framework sets the general principles for the Bank's risk-taking activities, to raise awareness across the organisation, and to guide staff members, who are responsible for the risks inherent in day-to-day activities, on acceptable and unacceptable behaviour. The parameters described in the statement are implemented through the Bank's operational policies and procedures, monitoring metrics, and internal controls which are reviewed on an on-going basis. Risk assessments are periodically carried out to ensure that these risks remain within the Risk Appetite. Bearing in mind that the nature and frequency of non-financial risks materialising cannot be predicted, in addition to the above, insurance cover is also in place to cater for operational failures. As part of the Bank's Capital Risk management, a capital charge for unforeseeable losses arising from these risks is also taken (notes to the Financial Statements note 2.6; Additional Regulatory Disclosures note 5).

Compliance Risk – This is the risk of legal sanctions, material financial loss, or loss to reputation the Bank may suffer because of failure to comply with laws, its own regulations, code of conduct, and standards of best/good practice. The Compliance function identifies, assesses, advises, monitors and reports on the Bank's compliance risks. The function is also the central point through which all interaction with regulatory and enforcement bodies are routed.

Financial Crime Risk – This is the risk related to offences such as money laundering, terrorist financing, fraud, bribery and corruption, market abuse and insider trading. The Bank through its various policies and procedures, is committed to combating financial crime and ensuring that its products and services are not misused for the purpose of money laundering, terrorism financing and fraud events.

Information Security Risk – This is the risk of loss caused by deliberate or accidental loss, alteration, falsification or leakage of information or by destruction, disruption, errors or misuse of information systems. The Bank has zero appetite for losses stemming from threats or malicious attacks. An Information & Cyber Security Policy is in place which ensures that robust internal controls and adequate measures are set to mitigate such threats. The need to continuously re-assess controls is paramount to ensure that the Bank's defences continue to address this risk and that losses arising from cyber events remain within its appetite.

Liquidity Risk – This is the risk arising when the Bank is unable to meet current and future payment obligations as they fall due. Liquidity management includes the constant monitoring of liquidity ratios against internal limits as set in the Risk Appetite Statement and regulatory requirements. During the year, the Bank continued to hold strong liquidity positions with a Liquidity Coverage Ratio (LCR) and Net Stability Funding Ratio (NSFR) well above regulatory minima. Through its Assets & Liabilities Committee, the Bank's liquidity profile is managed in such a way that cash flows and all anticipated obligations are met when due (notes to the Financial Statements note 2.5; Additional Regulatory Disclosures note 4).

Key Performance Indicators (KPIs)

The Group has in place a set of key performance indicators (KPIs) that are set by the Board of Directors, monitored by the Risk Management Function and regularly submitted to the Audit & Risk Committee for continuous assessment. They are a set of quantifiable measures which ensure that material risks faced are kept within established parameters as detailed in the Risk Appetite Statement and relevant policies. A selection of key metrics as at 31 December 2021 are presented hereunder.

Solvency	TCR	16.2%
Liquidity	LCR	225.3%
	NSFR	148.4%
Profitability	ROE[1]	5.7%

[1]*After tax*

The KPIs are reported on a regular basis in the form of a Risk scorecard. The scorecard, which takes the form of the "traffic light" approach compares the actual metric to the objectives set. As at the end of December 2021, all KPIs were within acceptable ranges and/or tolerance limits as set within the Bank's Risk Appetite.

EU Taxonomy KPIs

In order to achieve the targets established by the European Union of reaching net zero greenhouse gas ('GHG') emissions by 2050, with an interim target of reducing GHG emissions by 55%, compared to 1990 levels, by 2030, the European Commission ('EC') has developed a taxonomy classification system, by virtue of EU Regulation 2020/852, ('the Taxonomy Regulation' or 'the EU Taxonomy'), which establishes the criteria for determining whether an economic activity qualifies as environmentally sustainable.

The EU Taxonomy establishes criteria in terms of six environmental objectives against which entities will be able to assess whether economic activities qualify as environmentally sustainable. In order to qualify as such, an economic activity must be assessed to substantially contribute to one of these environmental objectives, whilst doing no significant harm to the remaining objectives by reference to technical screening criteria established in delegated acts. The economic activity is also required to meet minimum safeguards established in the taxonomy regulation. The six environmental objectives considered by the EU taxonomy are the following:

i. Climate change mitigation;
ii. Climate change adaptation;
iii. Sustainable use and protection of water and marine resources;
iv. Transition to a circular economy;
v. Pollution prevention and control; and
vi. Protection and restoration of biodiversity and ecosystems.

The EC subsequently adopted the Delegated Act supplementing Article 8 of the Taxonomy Regulation ('the Disclosures Delegated Act') in 2021, which establishes the disclosure requirements of entities within the scope of the Taxonomy Regulation. At this stage, this solely comprises entities subject to an obligation to publish non-financial information pursuant to Article 19a or Article 29a of Directive 2013/34/EU (being those entities subject to the Non-Financial Reporting Directive, 'NFRD').

The Disclosures Delegated Act became applicable for the first time on 1 January 2022, with respect to financial reporting periods ended 31 December 2021, adopting a phased-in approach to the disclosure requirements of key performance indicators. In the first year of its adoption, the Bank is only required to disclose its proportion of exposures towards taxonomy-eligible and non-eligible activities, along with its out-of-scope exposure in accordance with the Disclosure Delegated Act.

Identifying taxonomy-eligible economic activities will serve as a basis for eventually determining taxonomy-alignment of such economic activities with reference to the technical screening criteria established in the Climate Delegated Act and eventually the Environmental Delegated Act to the Taxonomy Regulation, and subsequently the determination of the Bank's Green Asset Ratio ('GAR'), which it will be required to disclose from 1 January 2024.

The following table was prepared in accordance with the disclosure requirement established in the Disclosures Delegated Act. Accordingly, for the purposes of classifying exposures as either taxonomy-eligible or non-eligible, the Bank has only considered the first two environmental objectives established in the Taxonomy Regulation (being climate change mitigation and climate change adaptation), with reference to the Climate Delegated Act. The remaining four environmental objectives will be considered from 1 January 2023, following the adoption of the Environmental Delegated Act, which will establish the list of taxonomy-eligible economic activities (along with the technical screening criteria to determine taxonomy alignment) with respect to the remaining objectives.

	Carrying amount	As a proportion of total assets
	€ 000	%
Taxonomy eligible	196,678	17.3
Taxonomy non-eligible	90,851	8.0
Out-of-scope exposures*	852,085	74.8
of which non-NFRD counterparties	462,605	40.6
of which derivatives	-	-
of which on demand interbank loans	22,916	2.0
of which other assets (incl. cash-related assets)	88,649	7.8
of which trading portfolio	-	-
of which central governments, central banks and supranational exposures	293,647	25.8
Total assets	1,139,614	100.0

**Out of scope exposures consist of (i) non-NFRD counterparties, (ii) derivatives, (iii) on demand interbank loans, (iv) other assets including retail loans not related to residential real estate, house renovation and motor vehicles, and other assets not related to lending or investments, (v) trading portfolio and (vi) governments, central banks and supranational exposures.*

Scope of consolidation

The ratios disclosed above represent the Bank's exposures on a standalone basis as a proportion of its total assets as at 31 December 2021.

Assets in scope

The amounts disclosed above as taxonomy-eligible and taxonomy non-eligible economic activities consider on-balance sheet financial assets not held for trading by the Bank. These include:

i) Loans and advances, debt securities and equity instruments in relation to undertakings that are subject to Non-Financial Reporting Directive;
ii) Real estate collaterals obtained by the Bank by taking possession in exchange for the cancellation of debts;
iii) Loans and advances towards individuals in respect of residential real estate, house renovation and motor vehicles (the latter of which was nil as at 31 December 2021); and
iv) The investment in the Bank's subsidiary.

Other assets which are considered to be out of scope of the Taxonomy Regulation have been disclosed separately in the table above.

Taxonomy-eligible and Taxonomy non-eligible economic activities

Taxonomy-eligible economic activities are those activities for which technical screening criteria have been established by virtue of the Climate Delegated Act, and therefore taxonomy alignment of such activities may be determined. By contrast, taxonomy non-eligible economic activities are those activities which cannot be assessed as environmentally sustainable, or not, for various reasons. In assessing whether, or not, an exposure is taxonomy-eligible, the Bank must consider the activity being financed rather than the principle operating activity of the counterparty. However, due to data limitations this was not always possible in the current year, as explained further below.

Total exposures to undertakings not subject to the Non-Financial Reporting Directive (NFRD)

Exposures to undertakings that are not obliged to publish Non-Financial Reporting information as per Article 19a or Article 29a of Directive 2013/34/EU as a proportion of total assets are also being disclosed.

Data limitations

The Bank relies on various data sources to determine taxonomy-eligible and non-eligible exposures and exposures not subject to NFRD. As scoped-in entities adopt the Taxonomy Regulation requirements in for their own disclosures, this could lead to a lack of comparability between the data reported in the current reporting period and that reported in future periods.

In order to determine the taxonomy-eligibility of exposures, the Bank has relied on the NACE classification of the principal activity of the counterparty. However, this is considered to be work-in-progress, as certain NACE classifications do not necessarily reflect the economic activity for which the exposure has been granted. An assessment has been carried out, on a sampled basis and for significant exposures, where the purpose of the facility differs from the primary economic activity of the entity to ensure the correct classification of taxonomy-eligible financed activities.

As per Article 19a or Article 29a of Directive 2013/34/EU, large public undertakings with more than an average of 500 employees during the reporting year are subject to NFRD. Given limited data availability, it has not been possible to identify with certainty all entities falling within the scope of NFRD. However, a best-effort basis has been carried out to identify those exposures whose undertakings are subject to NFRD, based on the level of individual exposure and the Bank's current knowledge of the respective entity.

The Bank is in the process of implementing procedures to overcome such limitations, adopting methodologies with the aim of improving the accuracy of the information being reported over time.

Additional Voluntary Disclosures in respect of the Bank's subsidiary MaltaPost p.l.c.

The Bank's subsidiary MaltaPost p.l.c. is subject to the NFRD and is therefore also subject to disclosure requirements stemming from the Delegated Act supplementing Article 8 of the Taxonomy Regulation. However, given that MaltaPost p.l.c. is consolidated at the level of the Bank (its parent entity), the company may claim an exemption from such disclosure requirements given that its parent entity complied with the requirements of the Disclosure Delegated Act.

Despite this, the Group have opted to disclose, on a voluntary basis, the disclosure requirements with respect to non-financial undertakings in accordance with the Disclosure Delegated Act for MaltaPost p.l.c. on a stand-alone basis.

As previously explained, the Disclosure Delegated Act adopts a phased in approach to the disclosure requirements of key performance indicators. In the first year of its adoption, non-financial undertakings are only required to disclose their proportion of turnover derived from taxonomy-eligible and non-eligible activities, and the proportion of capital and operating expenditure related to assets which qualify as taxonomy eligible or non-eligible.

The following table was prepared in accordance with the disclosure requirement established in the Disclosures Delegated Act, and as explained in the taxonomy related disclosures of the Bank, only the first two environmental objectives established in the Taxonomy Regulation (being climate change mitigation and climate change adaptation), were considered when determining taxonomy eligibility or non-eligibility.

	Taxonomy eligible activities		Taxonomy non-eligible activities		Total	
	%	€000	%	€000	%	€000
Turnover	88	30,095	20	7,433	100	37,528
CapEx	54	1,828	46	1,539	100	3,367
OpEx	40	726	60	1,104	100	1,830

The amounts disclosed in the table above pertain to the following:

i) Turnover consists of the revenue generated by MaltaPost p.l.c. during the financial year ended 30 September 2021 from all of its business activities. When determining taxonomy eligibility, the company has identified the following economic activities that fall within the scope of the Taxonomy Regulation in the transport sector:
   - 6.4 Operation of personal mobility devices, cycle logistics
   - 6.5 Transport by motorbikes, passenger cars and light commercial vehicles
   - 6.6 Freight transport services by road

ii) CapEx consists of additions to property, plant and equipment and intangible assets during the financial year ended 30 September 2021 considered before depreciation, amortisation and any re-measurements (including those resulting from revaluations and impairments, if applicable).

iii) OpEx consists of direct non-capitalised costs incurred during the financial year ended 30 September 2021 that relate to the day-to-day servicing of assets of property, plant and equipment (including also intangible assets) that are necessary to ensure the continued and effective functioning of such assets.

The determination of taxonomy eligible and non-eligible activities was determined in line with the criteria described above in the taxonomy disclosures of the Bank.

In determining whether an activity should be classified as taxonomy eligible or taxonomy non-eligible with respect to the transport sector, an assessment would need to be made on the specifications of the vehicles used in the activity, with the activity only being considered as taxonomy eligible if certain vehicle criteria are met. MaltaPost p.l.c. is still in the process of compiling the necessary information to complete this assessment. Therefore, the amounts disclosed above as taxonomy eligible were determined on a best effort basis based on the information that the Company has compiled to date. Going forward MaltaPost p.l.c. will continue to enhance its processes and compile further information to improve the accuracy of its Taxonomy reporting in future years, which is being disclosed on a voluntary basis.

8. COVID-19

The Group had already taken measures to manage and mitigate the disruptions caused by COVID-19 when this first broke out in Malta, and though 2021 continued to present challenges in this regard, the Group benefitted from the groundwork laid in 2020. Operational processes which were adapted to the new circumstances were maintained and suitably enhanced where appropriate.

The Group remained sensitive to the fact that it provides essential services to a wide range of customers, and therefore maintained its efforts to limit disruption, ensure business continuity, protect staff members and customers alike.

The Bank maintained its support to those customers mostly affected by the pandemic by way of the dedication of additional financial and other resources, to the extent required. Inevitably, the new realities consequent to the pandemic impacted the local economy and as a result a number of customers too.

The Group continues to take all the necessary measures to limit any possible negative effects while keeping as a foremost consideration the maintenance of business continuity without service interruptions while safeguarding the well-being and health of staff and customers.

Signed on behalf of the Bank's Board of Directors on 20 April 2022 by Michael C. Bonello (Chairman) and Joseph Said (Director and Chief Executive Officer) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Report and Financial Statements 2021.

A. Introduction

In terms of the Capital Markets Rules of the Malta Financial Services Authority (Rule 5.94), Lombard Bank Malta p.l.c. (the Bank), as a company having its securities admitted to trading on a regulated market, is obliged to report on the extent to which it has adopted the 'Code of Principles of Good Corporate Governance' (the Principles) embodied in Appendix 5.1 to Chapter 5 of the same Capital Markets Rules, as well as the measures which have been taken by the Bank to ensure compliance with these Principles.

While the Principles are not mandatory, the Board of Directors of the Bank has endeavoured to ensure that they are upheld to the fullest extent possible, and this while acknowledging that good corporate governance is indeed beneficial to all the Bank's stakeholders. The instances in which the Bank has departed from the Principles are explained below under Section C - 'Non-Compliance with the Code'.

After having carried out a review of the extent to which the Bank has been compliant with the Principles throughout the financial year ended 31 December 2021, the Board of Directors, in terms of Capital Markets Rule 5.97, presents its report as follows:

B. Compliance with the Code

Principle 1: The Board

As at 31 December 2021, the Board of Directors of the Bank consisted of five (5) Directors, four (4) of whom being non-executive Directors together with the Chief Executive Officer of the Bank being also a Director.

Michael Zammit, one of the Bank's non-executive directors, sadly passed away on 3 February 2022 (Refer to Company Announcement LOM 263). Following his demise, the Board of Directors on 15 February 2022 co-opted Peter Perotti as non-executive director of the Bank and as a member of the Bank's Audit & Risk Committee and Suitabilities & Evaluations Committee. (Refer to Company Announcement LOM 264). His fit and proper assessment was approved by the Bank's Suitabilities & Evaluations Committee and upon receipt of regulatory approval on 14 April 2022, his appointment became effective as of such date. (Refer to Company Announcement LOM 265).

The Directors, individually and collectively, are considered fit and proper to direct the business of the Bank, having the necessary skills and experience to be able to do so.

In order to assist it in the execution of its duties and responsibilities, the Board of Directors has set up a number of committees and these include the Audit & Risk Committee, the Assets & Liabilities Committee, the Credit Committee and the Suitabilities & Evaluations Committee, all of which are regulated by their own Terms of Reference as approved and periodically reviewed by the Board.

Principle 2: Chairman And Chief Executive Officer

Different individuals occupy the positions of Chairman and Chief Executive Officer. A clear division of responsibilities exists between the Chairman's responsibility for the running of the Board of Directors and the Chief Executive Officer's responsibility for the running and managing of the Bank's business. This separation of roles of the Chairman and Chief Executive Officer avoids concentration of power, authority and unfettered discretion in one individual alone and differentiates leadership of the Board from the running of the Bank's business.

The Chairman's responsibilities, *inter alia*, include: (i) leading the Board and helping it reach its full potential, particularly by facilitating the effective contribution of Directors and encouraging discussion; (ii) setting of the Agenda for Board meetings; (iii) ensuring that the Directors receive precise, timely and objective information so that they can make sound decisions and effectively monitor the performance of the Bank; (iv) ensuring that all strategic and policy issues are appropriately discussed and formally approved; and (v) maintaining effective communication with the Bank's shareholders at all times.

As stated below, the Chairman meets the independence criteria set out in the Principles. On the other hand, the Chief Executive Officer is responsible for managing the day-to-day business of the Bank in conformity with the agreed plans, policies and strategies approved by the Board.

Principle 3: Composition of the Board

The following Directors served on the Board during the period under review:

Michael C. Bonello
Graham A. Fairclough
Kimon Palamidis
Joseph Said
Michael Zammit*

** As reported above, Michael Zammit passed away on 3 February 2022. Following his demise, the Board of Directors co- opted Peter Perotti as non-executive director of the Bank and as a member of the Bank's Audit & Risk Committee and Suitabilities & Evaluations Committee, subject to regulatory approval which was granted on 14 April 2022, being the effective date of his appointment.*

All Board members are non-executive Directors who are not engaged in the daily management of the Bank, with the exception of Joseph Said who is also Chief Executive Officer of the Bank. Furthermore, the Board considers Michael C. Bonello, and Kimon Palamidis as independent Directors. Before his demise, Michael Zammit was still considered to be independent despite the fact that he had served on the Board for more than twelve consecutive years. Peter Perotti is also considered to be independent. In determining the independence of its members, the Board takes into consideration the relevant criteria and Principles as well as what are generally considered sound, acceptable standards. All non-executive Directors have declared in writing to the Board that they undertake:

- to maintain in all circumstances their independence of analysis, decision and action;
- not to seek or accept any unreasonable advantages that could be considered as compromising their independence; and
- to clearly express their opposition in the event that they find that a decision of the Board may harm the Bank.

It is considered that, in the current circumstances in which the Bank is operating, the size of the Board is sufficient for the requirements of the business and that the balance of skills and experience therein is appropriate to properly enable the Board to carry out its duties and responsibilities. This is considered so also taking into account, *inter alia*, the Bank's simple model and

the principle of proportionality, based on the Bank's size and the nature, scale and complexity of its activities and products.
The composition and election of the Board of Directors is determined by the Bank's Articles of Association wherein it is established that it is the shareholders who must appoint Directors to serve on the Board. Within these parameters, options for further strengthening the Board are always considered. In addition, however, the Bank, by virtue of the Board-appointed Suitabilities & Evaluations Committee, carries out suitability assessments of its existing Directors and any new nominated Directors in order to ensure that the suitability, fit and proper criteria are observed, pursuant to all applicable laws, rules, regulations, guidelines etc.

The overall composition of the Board and the collective knowledge, skills and experience required are evaluated during individual suitability assessments and collective suitability assessments so as to ensure that the Board is effectively discharging all its duties and obligations at all times.

The appointment of Directors to the Board is a matter that is reserved entirely to the Bank's shareholders in terms of the Memorandum and Articles of Association. Therefore diversity, to an extent, depends on the profiles of nominees proposed and their suitability in terms of applicable laws, rules, regulations, guidelines etc. The benefits of diversity, including that in educational and professional backgrounds, age, gender, experience and geographical provenance would be considered by the Suitability and Evaluations Committee in its assessment of suitability of any nominees.

The Board considers that as a policy and as reflected in its Board of Directors' Charter, it endeavours to have a varied board, particularly in terms of diverse educational and professional backgrounds and extensive and specialised experience of its members. The Board is confident that for this reason, and in light of the current circumstances in which it is operating, also taking into account proportionality and the Bank's size and the nature, scale and complexity of its activities and products, it benefits from a satisfactory diversity of skills, knowledge and experience. This allows for a good understanding of current affairs, the Bank's activities, business model, strategy and associated risks and the environment in which the Bank operates and longer-term risks and opportunities related to the Bank's business. It also benefits from international expertise.

The Board is cognisant of the fact that the appropriate mix of Board Members ensures diverse perspectives, experience and knowledge. It continues to remain committed to achieving further diversity among its members particularly in terms of number, age, geographical provenance, gender, experience, educational and professional backgrounds.

Principle 4: The Responsibility of the Board

In pursuing the execution of the four basic roles of corporate governance, namely, accountability, monitoring, strategy formulation and policy development, the Board of Directors, having the first level of responsibility for such execution:

- regularly reviews and evaluates corporate strategy, major operational and financial plans, risk policy, performance objectives and monitors implementation and corporate performance within the parameters of all relevant laws, regulations and codes of best business practice;
- applies high ethical standards and takes into account the interests of stakeholders and acts responsibly and with integrity and on a fully informed basis, in good faith, with due diligence and in the best interests of the Bank and its shareholders;
- recognises that the Bank's success depends upon its relationship with all groups of its stakeholders, including employees, suppliers, customers and the wider community in which the Bank operates;
- monitors effectively the application and implementation by Management of its policies and strategy;
- recognises and supports enterprise and innovation within Management and examines how best to motivate the Bank's Management;
- seeks to establish an effective decision-making process in order to develop the Bank's business efficiently; and
- ensures that a balance is struck between enterprise and control in the Bank.

Furthermore, the Board of Directors:

- defines in clear and concise terms the Bank's strategy, policies, management performance criteria and business policies and effectively monitors the implementation of such by Management;
- establishes a clear internal and external reporting system so that the Board has continuous access to accurate, relevant and timely information;
- has appointed Committees, including the Audit & Risk Committee, Credit Committee, Assets & Liabilities Committee and Suitabilities & Evaluations Committee;
- continuously assesses and monitors the present and future operations' opportunities, threats and risks;
- evaluates the Management's implementation of corporate strategy and financial objectives;
- ensures that the Bank has appropriate policies and procedures in place to assure that the Bank and its employees maintain the highest standards of corporate conduct, including compliance with applicable laws, regulations, business and ethical standards;
- ensures that the financial statements of the Bank and the annual audit thereof are completed within the stipulated time periods; and
- requires Management to constantly monitor performance and report fully and accurately to the Board.

Furthermore, Directors keep themselves updated on an ongoing basis of their statutory and fiduciary duties, the Bank's operations and prospects, the general business environment and skills and competences of Senior Management. The expectations of the Board are also discussed regularly.

Principle 5: Board Meetings

The Board convened fourteen (14) times during the period under review with attendance as follows:

Michael C. Bonello	14
Graham A. Fairclough	14
Kimon Palamidis	14
Joseph Said	14
Michael Zammit	12*

**Michael. Zammit appointed an alternate director for the 2 meetings he did not attend.*

The dates when the Board meetings are scheduled to be held are determined prior to the beginning of the year in question. When required, further meetings are scheduled.

Ahead of Board meetings an agenda and supporting documentation are made available to all Directors. Other than in the case of meetings specially convened to discuss particular matters, generally the agendas of regular Board meetings set out items of a long-term strategic nature, as well as performance-related issues together with credit applications which fall within the discretionary limits of the Board and also include various compliance-related matters. During meetings, Directors are encouraged to present their views pertinent to the subject matter and are given every opportunity to contribute to the relevant issues on the agenda. Following each meeting, minutes which record attendance as well as all decisions taken are circulated to all Board members.

Principle 6: Information and Professional Development

The Board of Directors appoints the Chief Executive Officer. Each newly appointed Member of the Board is briefed by the Chief Executive Officer, Senior Management officials, Heads of Internal Control Functions and any other staff members as necessary, on all aspects of the Bank's business and functions, while the Company Secretary provides each newly appointed Director with relevant corporate governance information and references to relevant Legislation, Rules, Guidelines, the Bank Statute as well as policy documents.

Board members are reminded that the Company Secretary is at their disposal to provide any advice or service that may be required in the discharge of their duties and responsibilities. The Company Secretary is responsible for advising the Board, through the Chairman, on all governance matters. The Secretary is responsible for ensuring that Board procedures are complied with as well as that effective information flows within the Board, its committees and with Senior Management. The Secretary also facilitates induction and assists with professional development, as required.

Directors are given the opportunity to update and develop their skills and knowledge, particularly through detailed presentations, briefings and training by senior executives and other relevant Bank officials. They are invited to attend training sessions organised specifically for the Board and are also informed of and encouraged to attend externally run seminars throughout their directorship. In addition, all Board members may obtain independent professional advice at the Bank's expense.

Furthermore, Directors have access to the advice and services of the external auditors who are invited to attend all Audit & Risk Committee meetings as well as Board meetings when required, including the meetings at which the Bank's financial statements are approved.

The Board continues to be mindful of the crucial importance of recruiting, retaining and motivating quality management. The ongoing training and development of staff at all levels is considered of the utmost importance and this also in the light of the need for orderly succession.

Principle 7: Evaluation of the Board's Performance

An assessment exercise of the Board's performance was carried out through a 'self-evaluation' questionnaire in which Board members participated. Furthermore, assessment exercises of performance of the committees were also carried out by virtue of 'self-evaluation' questionnaires completed by the members and some regular attendees of the Audit & Risk Committee, the Assets & Liabilities Committee and the Credit Committee. These exercises also included an evaluation of the Chairman of each respective Committee. These 'self-evaluation' questionnaires were then set to be analysed by the Suitabilities & Evaluations Committee established by the Board to report to the Board accordingly. This exercise did not reveal the need for any material changes in the Bank's governance structures and organisation.

Principle 8: Committees

The Board has appointed the following committees:

Audit & Risk Committee

The primary purpose of the Audit & Risk Committee is to protect the interests of the Bank's shareholders and to assist the Directors in conducting their role effectively so that the Bank's decision-making capability and the accuracy of its reporting and financial results are maintained at a high level at all times. The Committee assists the Board in fulfilling its supervisory and monitoring responsibility for effective financial reporting, risk management, control and governance and this by, *inter alia*, reviewing any financial information, statements and disclosures to be issued, systems of governance, systems of internal control established by Management and the Board, the risk management processes, the external and internal audit processes as well as the compliance processes. The Audit & Risk Committee met eleven (11) times during the period under review.

With respect to Risk Management, the Committee, *inter alia*, reviews reports from the Risk Management Function which enable the Committee (and the Board) to consider the process of risk identification and management, to assess the risks involved in the Bank's business and to understand how they are controlled and monitored by Management. The Committee also advises the Board on the Bank's overall current and future risk appetite and strategy and assists the Board in overseeing the implementation of that strategy by Management.

During the year under review, the Audit & Risk Committee was composed of the following four (4) non-executive Board members three (3) of whom being independent: Michael C. Bonello, Graham A. Fairclough, Kimon Palamidis and Michael Zammit in accordance with the Audit & Risk Committee's Terms of Reference. As stated earlier, Michael Zammit passed away in February 2022. Peter Perotti was co-opted as a Board member and also as a member of the Bank's Audit & Risk Committee and Suitabilities & Evaluations Committee, subject to regulatory approval which was granted on 14 April 2022, being the effective date of his appointment. He is an independent non-executive Board member.

Kimon Palamidis is the Chairman of this Committee and is considered by the Board to be independent. Together with the other members, he is also competent in accounting and/or auditing in terms of the Capital Markets Rules. The Bank's Head of Internal Audit and Head of Risk attend meetings of the Audit & Risk Committee. The Bank's External Auditors and members of Senior Management and others, including, *inter alia*, the Chief Executive Officer, Chief Financial Officer, Chief Officer Credit and the Compliance Officer, are also invited to attend meetings as is deemed necessary by the Committee. The Company Secretary acts as Secretary to the Audit & Risk Committee.

Assets & Liabilities Committee (ALCO)

Membership of this Committee is made up of a number of Chief Officers and senior officers, including from the Finance and Treasury departments and the Corporate Advisory & Research and Asset and Fund Management functions. The Chief Executive Officer chairs the ALCO whose main objective is to manage risks within approved limits at the same time as maximising returns by efficient and judicious management of the Bank's assets and liabilities. Risk Management officials are also invited to attend meetings. A Secretary is appointed by the Committee.

Credit Committee

The Credit Committee is responsible for considering and approving credit applications within delegated limits of authority. It is composed of a number of Chief Officers and senior officers. The Chief Executive Officer chairs this Committee and a Secretary is appointed by the Committee.

Suitabilities & Evaluations Committee

This Committee is responsible for carrying out suitability assessments of nominated and existing Directors, Key Function holders or any other persons as may be required and also assesses the Board's annual performance and that of its committees following the completion of the self-evaluations by the Board and committee members. The chairman of the Committee is selected by the Board of Directors (currently the non-executive Director and Committee member, Graham A. Fairclough) and the Company Secretary acts as Secretary.

Remuneration Committee

The functions of the Remuneration Committee are carried out by the Board of Directors in view of the fact that the remuneration of Directors for the holding of their office on the Board is not performance-related.

A separate 'Remuneration Report' features on page 23 of this Annual Report in compliance with the Principles.

Principle 9 And 10: Relations with Shareholders and Markets and Institutional Shareholders

The Bank fully appreciates the importance of maintaining open lines of communication with shareholders, the markets and institutional shareholders. The Board, in this regard, considers that throughout the period under review the Bank has continued to communicate appropriately by means of regular company announcements.

The Bank communicates with its shareholders with respect to its Annual General Meetings. The prevailing COVID-19 pandemic has precluded the Bank from holding its recent Annual General Meetings and the forthcoming 2022 Annual General Meeting in person. This notwithstanding, despite being held remotely in terms of the Companies Act (Public Companies – Annual General Meetings) Regulations, 2020 (L.N. 288 of 2020), shareholders are still given the opportunity to participate by sending in questions beforehand and by appointing the Chairman as their proxy and indicating their voting preferences. They can also follow proceedings which shall be live streamed. The AGM documentation is sent to all shareholders at least twenty-one (21) days prior to the holding of the Meeting.

The Bank's website (www.lombardmalta.com), contains information about the Bank and its business and is updated regularly.

It is therefore the Bank's policy:

- to publish information that can have a significant effect on the Bank's share price through the Malta Stock Exchange and immediately after on the Bank's website;
- to make other published information available to the public on the Bank's website;
- to strive for open, transparent communications;
- to ensure continuity and high quality in the information disclosed; and
- to be accessible to all stakeholders.

Minority shareholders are entitled to call special meetings should a minimum threshold of share ownership be established in accordance with the Bank's Memorandum and Articles of Association. Furthermore, minority shareholders may formally present an issue to the Board if they own the predefined minimum threshold of shares.

Principle 11: Conflicts of Interest

The Board of Directors recognises that its members have a primary responsibility to always act in the interest of the Bank and its shareholders as a whole, irrespective of who appointed them to the Board.

Strict policies are in place, particularly in the Board of Directors' Charter, to enable the management of conflict of interest, both actual as well as potential, should the occasion arise.

In addition, the Bank's 'Policy on the Prevention of Market Abuse' was adopted and implemented in conformity with Market Abuse laws and regulations. Directors and staff members are also regularly reminded of their obligations when dealing in securities of the Bank and other scheduled financial instruments.

Joseph Said, who is a Director of the Bank, holds a directorship in two companies that have a shareholding in the Group, as disclosed in the Directors' Report.

Principle 12: Corporate Social Responsibility

The Bank is well aware of the need to adhere to accepted principles of corporate social responsibility and in this regard remains fully committed to conducting its activities ethically at all times. It consistently seeks to contribute to economic and social development while also improving the quality of life of its staff members and their families. These principles also include matters concerning data privacy and protection, diversity and inclusion, talent management, customer relations, innovation, community and staff engagement as well as responsible lending.

The Bank implements these principles of corporate social responsibility through strong governance and risk management practices.

It extends support to various initiatives and projects together with direct community involvement. The Bank is also sensitive to the fact that success in these areas requires investment in the community, customers and staff members while not overlooking the impact that its activities may have on the environment.

C. Non-Compliance with the Code

Principle 4: (Code Provision 4.2.7)

The above Code Provision states, *'The Board should develop a succession policy for the future composition of the Board of Directors and particularly of the executive component thereof, for which the Chairman should hold key responsibility'.*

The appointment of Directors to serve on the Board is a matter which is entirely reserved to the shareholders of the Bank in terms of its Memorandum and Articles of Association (except where the need arises to fill a casual vacancy). The concept of rotation of directors as set out by the Bank's Memorandum and Articles of Association also provides an element of continuity on the Board of Directors. On the basis of the above, the Board does not at this stage consider it necessary to develop a succession policy for the future composition of the Board. This notwithstanding, within the above parameters, options and opportunities for further strengthening the Board continue to be considered.

Principle 8A: (Remuneration Commttee)

The Board did not establish a Remuneration Committee as specified in Code Provision 8.A.1. In terms of Code Provision 8.A.2 of the Principles, given that the remuneration of Directors for the holding of their office on the Board is not performance-related, the functions of the Remuneration Committee are carried out by the Board of Directors.

Principle 8B: (Nomination Committee)

A Nomination Committee has not been set up since the appointment of Directors to the Board is a matter that is reserved entirely to the Bank's shareholders in terms of the Memorandum and Articles of Association.

In this connection every member of the Bank holding in the aggregate at least fifteen percent (15%) of the ordinary issued share capital of the Bank shall be entitled to appoint one (1) Director for each and every fifteen percent (15%) of the ordinary issued share capital owned by that member.

Any fractional shareholding in excess of fifteen percent (15%) not applied in appointing such a Director or Directors, and only that fraction, shall be entitled to vote in the election of the remaining Directors together with the remaining body of shareholders. These are entitled to appoint the remaining Board members in accordance with the provisions of the Bank's statute.

This notwithstanding, in light of regulatory requirements, the Suitabilities & Evaluations Committee referred to above was set up specifically to carry out suitability assessments of nominated and existing Directors, Key Function holders or any other persons as may be required and also to assess the Board's annual performance and that of its committees.

Principle 9: (Code Provision 9.3)

There are no procedures disclosed in the Bank's Memorandum or Articles as recommended in Code Provision 9.3 to resolve conflicts between minority shareholders and controlling shareholders.

D. Internal Control (Capital Markets Rule 5.97.4)

The Board is ultimately responsible for the Bank's internal controls as well as their effectiveness, while authority to operate the Bank is delegated to the Chief Executive Officer. The Bank's system of internal controls is designed to manage all the risks in the most appropriate manner. Such controls, however, cannot completely eliminate the possibility of material error or fraud. The Board, therefore, assumes responsibility for executing the four basic roles of corporate governance, i.e. accountability, monitoring, strategy formulation and policy development.

In summary, the Board is therefore responsible for:

- reviewing the Bank's strategy on an ongoing basis as well as setting the appropriate business objectives in order to enhance value for all stakeholders;
- appointing and monitoring the Chief Executive Officer whose function it is to manage the operations of the Bank; and
- identifying and ensuring that significant risks are managed satisfactorily.

Given the fiduciary responsibility involved, the Board of Directors also sets high business and ethical standards for adoption right across the organisation.

The Board upholds a policy of clear demarcation between its role and responsibilities and those of Management. It has defined the level of authority that it retains over strategy formulation and policy determination together with delegated authority and has vested accountability for the Bank's day-to-day business in the Assets & Liabilities Committee, Credit Committee and in the management team comprising of the:

- Chief Executive Officer; and
- Chief Officers and other officers.

The Board frequently participates in asset allocation decisions as well as credit proposals above a certain threshold, after the appropriate recommendations have been made.

The Bank's internal control framework covering all the Bank's activities ensures:

- effective and efficient operations and prudent conduct of business;
- proper risk management;
- reliable financial and non-financial information; and
- compliance with all internal policies, processes and procedures, laws, rules and regulations.

To this effect, a three-lines-of-defence model has been adopted by the Bank as follows:

- *First line of defence – Business Units / Operations*: This is provided by front line staff members and business unit management. The internal controls and systems, the culture and control environment developed and implemented by these business units play a vital role in anticipating and managing operational risks.
- *Second line of defence – Risk Management & Compliance*: The Bank maintains permanent and effective compliance and risk management functions which report directly to the Audit & Risk Committee and Board of Directors. The Compliance Function identifies, assesses and manages compliance risk. The Risk Management Function is responsible for overseeing

the Bank's activities and for identifying, monitoring, controlling and reporting such risk. Through the Bank's Risk Management Framework, an appropriate balance is struck between sound practices and profitability, by applying strict internal controls and discretionary limits, and optimising the returns thereof, in line with the Bank's risk appetite.

- *Third line of defence – Internal Audit*: This is an integral part of the Bank's control environment and provides Management and the Audit & Risk Committee and Board of Directors with an independent and objective review of the Bank's business activities and support functions.

E. General Meetings (Capital Markets Rule 5.97.6)

General meetings are called by giving at least twenty-one (21) days' notice and conducted in accordance with the provisions contained in the Bank's Articles of Association.

The 'Ordinary Business' which is dealt with at the Annual General Meeting consists of the adoption of the annual financial statements, declaration of a dividend, appointment of Board members, appointment of auditors and the fixing of their remuneration together with the voting of remuneration to the Directors for the holding of their office. All other business shall be deemed 'Special Business'.

All shareholders registered in the shareholders' register on record date as defined in the Capital Markets Rules have the right to attend, participate and vote in the general meeting.

A shareholder or shareholders holding not less than five per cent (5%) of the voting issued share capital of the Bank may: (i) request the Bank to include items on the agenda and; (ii) table draft resolutions for items included in the agenda of a general meeting. Such requests shall be submitted to the Bank at least forty-six (46) days before the date set for the general meeting.

Every shareholder shall be entitled to appoint only one (1) person to act as proxy holder to attend and vote at a general meeting instead of him. The proxy holder shall enjoy the same rights to speak and ask questions in the general meeting as those to which the member thus represented would be entitled.

In view of the continued circumstances arising from the ongoing COVID-19 pandemic, the 2022 Annual General Meeting shall once again be held remotely, in terms of the Companies Act (Public Companies - Annual General Meetings) Regulations, 2020 (L.N. 288 of 2020).

Signed on behalf of the Bank's Board of Directors on 20 April 2022 by Michael C. Bonello (Chairman) and Joseph Said (Director and Chief Executive Officer) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Report and Financial Statements 2021.

As indicated in the 'Statement of Compliance with the Code of Principles of Good Corporate Governance', in terms of the 'Code of Principles of Good Corporate Governance' within the Capital Markets Rules issued by the Malta Financial Services Authority, the Board of Directors performs the functions of a Remuneration Committee on the basis that the remuneration of the Bank's Directors for the holding of their office on the Board, is not performance-related and does not include share options, pension benefits, profit-sharing arrangements or any emolument related to the performance of the Bank. Among the obligations established in the Capital Markets Rules, the Board, where applicable, carries out the main duties established in the Supporting Principles enshrined in Principle 8A of the 'Code of Principles of Good Corporate Governance'. This Remuneration Report was approved by the Board of Directors at the Board Meeting held on 20 April 2022.

Directors

The Bank's *Remuneration Policy for Directors* drawn up in terms of the Capital Markets Rule 12.26A et seq. was approved by the Annual General Meeting on 2 December 2020 and became effective from such date. (Refer to https://www.lombardmalta.com/annual-general-meeting-2020). The result of the vote at the 2020 Annual General Meeting when the Policy was last approved was 33,545,565 votes in favour, 34,325 votes against and 329,087 abstentions.

This document formalised the Bank's policy in this regard and any remuneration paid following approval of the policy was to be in accordance with the same. The remuneration of the Chief Executive Officer ('CEO'), is also considered in the above-mentioned *Remuneration Policy for Directors*.

This Policy is reviewed by the Board on an annual basis and shall be put to a vote by the General Meeting at every material change and, in any case, at least every four years. No changes to the Policy are being proposed for approval at the 2022 Annual General Meeting.

There were no deviations from the procedure for the implementation of the Remuneration Policy for Directors.

In terms of the Bank's Memorandum and Articles of Association, the Bank's shareholders determine the maximum annual aggregate remuneration of the Directors. The maximum amount is established by resolution at each Annual General Meeting of the Bank. The aggregate amount fixed for this purpose during the 2021 Annual General Meeting was one hundred and twenty thousand euro (€120,000).

As per policy, members of the Board, in their role as directors, only receive a fixed fee, the amount of which is determined on the basis of market practice as well as the Bank's size and internal organisation and the nature, scale and complexity of its activities and business model.

The fees paid to Directors for the holding of their office during 2021 amounted to €69,444 (2020: €48,900). This amount is within the limit of €120,000 approved by the Annual General Meeting of 28 May 2021.

It is confirmed that none of the directors in their role as directors of the Bank are entitled to profit-sharing, share options, pension benefits, variable remuneration, any other remuneration or related payments. One director (Graham A. Fairclough) provides specific services to the Group, though he is still considered a non-executive director. Only one of the directors has a service contract with the Bank, which director is the only executive Director and is the CEO Joseph Said.

In terms of Code Provision 8.A.5 of the Malta Financial Services Authority Capital Markets Rules, the total emoluments received by Directors relative to their directorship for the financial year 2021, as compared to 2020, are specified below:

	€	€
	2021	2020
Michael C. Bonello (Chairman)	**25,480**	20,960
Graham A. Fairclough	**10,991**	6,985
Joseph Said	**10,991**	6,985
Michael Zammit	**10,991**	6,985
Kimon Palamidis	**10,991**	6,985
Total	**69,444**	48,900

In determining the remuneration of the CEO, the Board of Directors considers factors which include among others, professional qualifications, experience, initiative, acumen, number of years of service, the design and implementation of the overall business strategy, objectives and risk appetite at Bank as well as Group level. The remuneration of the CEO is fixed with no variable remuneration.

The CEO is also entitled to the use of a company car, health insurance and telecommunication allowance.

In a previous financial year, the Bank had decided to grant the CEO an ex-gratia gratuity upon his eventual retirement, which amount was fully provided for and reflected in the financial statements of previous years.

In terms of Code Provision 8.A.5 of the Capital Markets Rules, during financial year 2021, the total emoluments received by the executive Director from the Group amounted to €361,368 (2020: €357,496), split as follows:

	€	€
	2021	2020
Gross annual, fixed salary & fixed role-based allowances	333,377	333,511
Director Fees - Lombard Bank Malta p.l.c.	10,991	6,985
Chairman / Director Fees MaltaPost p.l.c.	17,000	17,000

The total remuneration for 2021 of the non-executive Director who provided specific services to the Group, amounted to €76,229 (2020: €73,480), split as follows:

	€	€
	2021	2020
Payments for specific services	54,138	55,395
Director Fees - Lombard Bank Malta p.l.c.	10,991	6,985
Director Fees - MaltaPost p.l.c.	7,100	7,100
Company Secretary Fees - MaltaPost p.l.c.	4,000	4,000

There is no formal provision for the reclamation of variable remuneration. In any case, the directors and the CEO do not receive variable remuneration.

The above remuneration levels for 2021 comply with the provisions of the approved *Remuneration Policy for Directors* and take into consideration the interests of all the Bank's stakeholders together with the external context.

Senior Management

Senior Management refers to the Chief Officers of the Bank, excluding the Chief Executive Officer.

The Board of Directors is satisfied that the packages offered to Senior Management continue to ensure that the Bank attracts and retains management staff with the necessary qualities and skills. The Bank's policy remains that of engaging its senior management staff on the basis of indefinite contracts of employment, and this after a period of probation. The terms and conditions of employment of senior management are established in the relative employment contracts. The applicable notice period, after probation, is that provided for in the relevant legislation.

Share options, share incentive schemes and profit sharing do not feature in the Bank's Remuneration Policy, and the individual contracts of employment of senior management do not contain provisions for termination payments and/or other payments linked to early termination other than as determined by the law.

From time to time the Board of Directors of the Bank approves the allocation of a financial contribution towards retirement gratuities that it may decide to grant and/or contribute towards a staff pension fund that may be formally established in the future. Gratuities that it may make, on an ex-gratia basis, to its employees are made accordingly. Amounts contributed for this purpose in respect of 2021 amounted to €100,000 (2020: €66,000). Once contributed, these amounts are held in a separate bank account which is not controlled by the Bank and is therefore not included in the Bank's financial statements. Amounts intended as a contribution to an eventual pension fund will be regulated by rules yet to be determined in light of relevant legislation. No other pension benefits are currently payable by the Bank.

Senior management staff are eligible for annual salary increases, which are not directly performance-related. The remuneration of Senior Management staff members is determined also by the role, responsibilities covered, market practice, seniority, experience and qualifications. Annual bonuses are paid to senior management staff members according to individual overall performance during the previous financial year. Bonus payments do not exceed 100% of the fixed component of the total remuneration for each individual.

Non-cash benefits include private health care insurance as well as death-in-service benefits and personal accident insurance cover.

Total emoluments received by Senior Management, excluding the CEO, during the period under review are as detailed below, in terms of Code Provision 8.A.5.

Fixed remuneration		Variable remuneration		Share options		Others	
2021	2020	**2021**	2020	**2021**	2020	**2021**	2020
€	€	**€**	€	**€**	€	**€**	€
568,000	550,723	98,000	114,000	-	-	-	-

For other employees, fixed pay is determined by a Collective Agreement and annual bonuses are differentiated by individual performance and grade.

The changes effected in the Bank's Remuneration Policy during the financial year under review were such as to align it with regulatory requirements. Furthermore, the Bank does not plan to effect changes in its Remuneration Policy in the forthcoming financial year, unless required to do so in terms of any regulatory obligations or otherwise.

In terms of Chapter 12 of the Capital Markets Rules, this Remuneration Report is being put to an advisory vote at the 2022 Annual General Meeting in accordance with the requirements of the Capital Markets Rule 12.26 L.

The Directors' Remuneration Report for 2020 was approved at the Annual General Meeting held on 28 May 2021, with 10,232,256 votes in favour, 14,538 votes against and 215,314 abstentions. There were no issues raised on the Report during the said Annual General Meeting.

Other information on remuneration in terms of Appendix 12.1 of the Capital Markets Rules

In terms of the requirements within Appendix 12.1 of the Capital Markets Rules, the following tables present the annual change regarding each individual director's remuneration, the performance of the Bank, and of average remuneration on a full-time equivalent basis of employees of the Bank, other than Directors over the two most recent financial years.

	2021	2020	**%**	**% annual change of the Bank's performance based on Profit before tax**	**% annual change of the average remuneration on a full-time equivalent basis of employees of the Bank other than Directors**
	€	€	**change**		**(2020-2021)**
Michael C. Bonello (Chairman)	25,480	20,960	22%		
Graham A. Fairclough	10,991	6,985	57%		
Joseph Said	10,991	6,985	57%	32%	2%
Michael Zammit	10,991	6,985	57%		
Kimon Palamidis	10,991	6,985	57%		
Total	69,444	48,900			

€'000	**2021**		2020		**% change**	
	Group	**Bank**	**Group**	**Bank**	**Group**	**Bank**
Employee remuneration (excluding CEO)	24,027	7,862	22,424	7,312	7%	8%
CEO remuneration	333	333	334	334	0%	0%
Entity's performance – Profit before tax	12,638	12,193	10,372	9,251	22%	32%

The Group's/Bank's performance is measured using Profit before tax.

The contents of the Remuneration Report have been reviewed by PricewaterhouseCoopers, the external auditors, to ensure that the information required in terms of Appendix 12.1 to Chapter 12 of the Capital Markets Rules have been included.

Number of shareholders analysed by range:

Range	31 December 2021 Shareholders	Shares	31 March 2022 Shareholders	Shares
1 – 500	168	28,426	167	28,207
501 – 1000	83	57,957	81	56,935
1001 – 5000	501	1,279,136	498	1,272,620
5001 and over	670	43,401,442	669	43,409,199
Total	**1,422**	**44,766,961**	**1,415**	**44,766,961**

The Bank has one class of shares and each share is entitled to one vote.

Board of Directors	Michael C. Bonello	Chairman
	Graham A. Fairclough	
	Kimon Palamidis	
	Joseph Said	
	Michael Zammit*	

** Michael Zammit passed away on 3 February 2022. Following his demise, the Board of Directors co-opted Peter Perotti as non-executive director of the Bank and as a member of the Bank's Audit & Risk Committee and Suitabilities & Evaluations Committee, subject to regulatory approval which was received on 14 April 2022, being the effective date of his appointment.*

Company Secretary	Helena Said	
Senior Management	Joseph Said	Chief Executive Officer
	David Attard	Chief Officer - Group Corporate Services
	Anthony Bezzina	Chief Officer - Credit
	Paul Debono	Chief Officer - Legal
	Eugenio Farrugia	Chief Operations Officer
	Aurelio Theuma	Chief Financial Officer
	Anthony Zahra	Chief Information Officer

Company Information

Registered Office
67 Republic Street, Valletta VLT 1117
Tel: 25581 117

Branches
67 Republic Street, Valletta VLT 1117
Tel: 25581 100

82 St. Sebastian Street, Qormi QRM 2335
Tel: 25581 360

Ninu Cremona Street, Victoria VCT 2561
Tel: 25581 600

43 Pitkali Road, Attard ATD 2219
Tel: 25581 560

Balzan Valley Road, Balzan BZN 1409
Tel: 25581 500

225A Tower Road, Sliema SLM 1601
Tel: 25581 260

44 Tigne’ Street, Sliema SLM 3174
Tel: 25581 251

24/7 Outlet
Paceville Avenue, St. Julian’s STJ 3103

Credit
9A St. Fredrick Street, Valletta VLT 1470
Tel: 25581 115

Home Loans
4 Main Street, Qormi QRM 1100
Tel: 25581 370

International Business Banking
Graham Street, Sliema SLM 1711
Tel: 25581 250

Legal Office
59 Republic Street, Valletta VLT 1117
Tel: 25581 180

Trade Services
4 Main Street, Qormi QRM 1100
Tel: 25581 380

Wealth Management
Financial Advice & Stockbroking Services: 225A, Tower Road, Sliema SLM 1601
Tel: 25581 167
Portfolio Management: 225A, Tower Road, Sliema SLM 1601
Tel: 25581 288
Research & Corporate Advisory: 225A, Tower Road, Sliema SLM 1601
Tel: 25581 287

FINANCIAL STATEMENTS

For the Year Ended 31 December 2021

2021

Statements of Financial Position
As at 31 December 2021

	notes	Group		Bank	
		2021	2020	**2021**	2020
		€ 000	€ 000	**€ 000**	€ 000
Assets					
Balances with Central Bank of Malta, treasury bills and cash	5	**126,279**	169,687	**125,552**	168,648
Cheques in course of collection		**530**	666	**530**	666
Investments	6	**227,501**	161,424	**224,600**	157,863
Loans and advances to banks	7	**78,279**	96,985	**68,424**	93,641
Loans and advances to customers	8	**642,893**	621,129	**642,895**	621,132
Investment in subsidiaries	9	**-**	-	**15,858**	15,732
Investment in associates	10	**3,006**	1,932	**1,645**	1,645
Intangible assets	11	**2,145**	2,050	**122**	246
Property, plant and equipment	12	**65,346**	50,928	**41,585**	30,446
Assets classified as held for sale	8	**661**	134	**661**	134
Current tax assets		**2,691**	1,156	**2,682**	1,156
Deferred tax assets	14	**9,779**	10,117	**9,283**	9,669
Inventories	15	**1,324**	1,274	**625**	555
Trade and other receivables	16	**10,787**	9,136	**1,606**	1,761
Accrued income and other assets	17	**4,170**	4,337	**3,546**	3,737
Accrued income and other assets	17	**4,170**	4,337	**3,546**	3,737
Total assets		**1,175,391**	1,130,955	**1,139,614**	1,107,031

	notes	Group		Bank	
		2021	2020	**2021**	2020
		€ 000	€ 000	**€ 000**	€ 000
Equity and Liabilities					
Equity					
Share capital	18	**11,192**	11,044	**11,192**	11,044
Share premium	19	**18,530**	18,530	**18,530**	18,530
Revaluation and other reserves	19	**23,668**	18,978	**20,828**	17,076
Retained earnings		**83,910**	77,469	**81,452**	74,692
Equity attributable to equity holders of the Bank		**137,300**	126,021	**132,002**	121,342
Non-controlling interests		**8,470**	7,741	**-**	-
Total equity		**145,770**	133,762	**132,002**	121,342
Liabilities					
Amounts owed to banks	20	**1,224**	5,602	**1,224**	5,602
Amounts owed to customers	21	**977,143**	941,110	**978,365**	948,478
Provisions for liabilities and other charges	22	**2,113**	2,632	**435**	903
Current tax liabilities		**809**	844	**-**	-
Deferred tax liabilities	14	**6,844**	6,448	**5,545**	5,421
Other liabilities	23	**30,649**	29,665	**14,772**	18,842
Accruals and deferred income	24	**10,839**	10,892	**7,271**	6,443
Total liabilities		**1,029,621**	997,193	**1,007,612**	985,689
Total equity and liabilities		**1,175,391**	1,130,955	**1,139,614**	1,107,031
Memorandum items					
Contingent liabilities	25	**13,195**	10,851	**13,360**	10,983
Commitments	25	**195,848**	200,870	**196,413**	200,217

The notes on pages 38 to 139 are an integral part of these financial statements.

These financial statements on pages 29 to 139 were approved and authorised for issue by the Board of Directors on 20 April 2022. The financial statements were signed on behalf of the Bank's Board of Directors by Michael C. Bonello (Chairman) and Joseph Said (Director and Chief Executive Officer) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Report and Financial Statements 2021.

Income Statements
For the Year Ended 31 December 2021

		Group		Bank	
	notes	**2021**	2020	**2021**	2020
		€ 000	€ 000	**€ 000**	€ 000
Interest receivable and similar income					
- on loans and advances, balances with Central Bank of Malta and treasury bills	26	**23,451**	22,799	**23,414**	22,768
- on debt and other fixed income instruments	26	**2,274**	2,099	**2,174**	1,983
Interest expense	26	**(6,169)**	(6,026)	**(6,120)**	(5,968)
Net interest income		**19,556**	18,872	**19,468**	18,783
Fee and commission income	27	**5,424**	5,000	**4,341**	3,887
Fee and commission expense	27	**(213)**	(261)	**(213)**	(261)
Net fee and commission income		**5,211**	4,739	**4,128**	3,626
Postal sales and other revenues	28	**37,371**	34,145	**518**	786
Dividend income	29	**80**	105	**1,738**	1,762
Net trading income	30	**615**	539	**590**	607
Other operating income		**231**	1,942	**286**	2,310
Operating income		**63,064**	60,342	**26,728**	27,874
Employee compensation and benefits	31	**(24,360)**	(22,758)	**(8,195)**	(7,646)
Other operating costs	33	**(24,544)**	(20,706)	**(7,129)**	(6,169)
Depreciation and amortisation	11,12	**(2,719)**	(2,267)	**(927)**	(782)
Provisions for liabilities and other charges	22	**135**	(115)	**250**	(80)
Credit impairment reversals /(losses)	32	**1,464**	(3,973)	**1,466**	(3,946)
Operating profit		**13,040**	10,523	**12,193**	9,251
Share of loss of investment accounted for using the equity method, net of tax	10	**(402)**	(151)	**-**	-
Profit before taxation		**12,638**	10,372	**12,193**	9,251
Income tax expense	34	**(4,759)**	(3,230)	**(4,389)**	(2,792)
Profit for the year		**7,879**	7,142	**7,804**	6,459
Attributable to:					
Equity holders of the Bank		**7,481**	6,640	**7,804**	6,459
Non-controlling interests		**398**	502	**-**	-
Profit for the year		**7,879**	7,142	**7,804**	6,459
Earnings per share	35	**16c8**	14c9		

The notes on pages 38 to 139 are an integral part of these financial statements.

Statement of Comprehensive Income

For the Year Ended 31 December 2021

	notes	Group 2021 € 000	Group 2020 € 000	Bank 2021 € 000	Bank 2020 € 000
Profit for the year		**7,879**	7,142	**7,804**	6,459
Other comprehensive income					
Items that may be reclassified subsequently to profit or loss					
Investments measured at FVOCI					
Net loss in fair value	6	**(2,711)**	(304)	**(2,653)**	(174)
Net gain on financial assets reclassified to profit or loss on disposal		**(168)**	(167)	**(168)**	(167)
Net (loss)/gain attributable to change in credit risk		**(344)**	625	**(343)**	625
Income taxes relating to these items	34	**1,108**	(100)	**1,108**	(100)
Items that will not be reclassified to profit or loss					
Net gain on investments in equity instruments measured at FVOCI	6	**149**	132	**149**	132
Surplus arising on revaluation of land and buildings	12	**8,486**	20	**6,844**	-
Remeasurements of defined benefit obligations		**-**	133	**-**	-
Income taxes relating to these items	34	**(1,491)**	(92)	**(1,219)**	(45)
Other comprehensive income for the year, net of income tax		**5,029**	247	**3,718**	271
Total comprehensive income for the year, net of income tax		**12,908**	7,389	**11,522**	6,730
Attributable to:					
Equity holders of the Bank		**12,137**	6,893		
Non-controlling interests		**771**	496		
Total comprehensive income for the year, net of income tax		**12,908**	7,389		

The notes on pages 38 to 139 are an integral part of these financial statements.

Group

	note	Share capital € 000	Share premium € 000	Revaluation and other reserves € 000	Retained earnings € 000	Total € 000	Non-controlling interests € 000	Total equity € 000
		Attributable to equity holders of the Bank						
At 1 January 2020		11,044	18,530	19,832	69,722	119,128	7,674	126,802
Comprehensive income								
Profit for the year		-	-	-	6,640	6,640	502	7,142
Other comprehensive income								
Fair valuation of financial assets measured at FVOCI:								
Net changes in fair value arising during the year		-	-	(1,096)	-	(1,096)	(37)	(1,133)
Reclassification adjustments:								
- net amounts reclassified to profit or loss on disposal		-	-	(109)	-	(109)	-	(109)
- net amounts reflected directly in retained earnings on disposal		-	-	-	976	976	-	976
Net movement attributable to changes in credit risk		-	-	406	-	406	-	406
Remeasurements of deferred benefit obligations		-	-	65	-	65	25	90
Transfers and other movements		-	-	(120)	131	11	6	17
Total other comprehensive income for the year		-	-	(854)	1,107	253	(6)	247
Total comprehensive income for the year		-	-	(854)	7,747	6,893	496	7,389
Transactions with owners, recorded directly in equity								
Contributions by and distributions to owners								
Dividends to equity holders	36	-	-	-	-	-	(429)	(429)
Total transactions with owners		-	-	-	-	-	(429)	(429)
At 31 December 2020		11,044	18,530	18,978	77,469	126,021	7,741	133,762

The notes on pages 38 to 139 are an integral part of these financial statements.

Statements of Changes in Equity
For the Year Ended 31 December 2021

Group

	notes	Share capital € 000	Share premium € 000	Revaluation and other reserves € 000	Retained earnings € 000	Total € 000	Non-controlling interests € 000	Total Equity € 000
		Attributable to equity holders of the Bank						
At 1 January 2021		**11,044**	**18,530**	**18,978**	**77,469**	**126,021**	**7,741**	**133,762**
Comprehensive income								
Profit for the year		-	-	-	**7,481**	**7,481**	**398**	**7,879**
Other comprehensive income								
Surplus on revaluation of land and buildings, net of tax		-	-	**6,658**	-	**6,658**	**390**	**7,048**
Fair valuation of financial assets measured at FVOCI: Net changes in fair value arising during the year		-	-	**(1,669)**	-	**(1,669)**	**(17)**	**(1,686)**
Reclassification adjustments: - net amounts reclassified to profit or loss on disposal		-	-	**(110)**	-	**(110)**	-	**(110)**
Net movement attributable to changes in credit risk		-	-	**(223)**	-	**(223)**	-	**(223)**
Transfers and other movements		-	-	**34**	**(34)**	-	-	-
Total other comprehensive income for the year		-	-	**4,690**	**(34)**	**4,656**	**373**	**5,029**
Total comprehensive income for the year		-	-	**4,690**	**7,447**	**12,137**	**771**	**12,908**
Transactions with owners, recorded directly in equity								
Contributions by and distributions to owners								
Dividends to equity holders	36	-	-	-	**(858)**	**(858)**	**(429)**	**(1,287)**
Bonus issue		**148**	-	-	**(148)**	-	-	-
Non-controlling interests arising on acquisition of subsidiary	9	-	-	-	-	-	**387**	**387**
Total transactions with owners		**148**	-	-	**(1,006)**	**(858)**	**(42)**	**(900)**
At 31 December 2021		**11,192**	**18,530**	**23,668**	**83,910**	**137,300**	**8,470**	**145,770**

The notes on pages 38 to 139 are an integral part of these financial statements.

Statements of Changes in Equity
For the Year Ended 31 December 2021

Bank

	note	Share capital € 000	Share premium € 000	Revaluation and other reserves € 000	Retained earnings € 000	Total € 000
At 1 January 2020		11,044	18,530	17,901	67,137	114,612
Comprehensive income						
Profit for the year		-	-	-	6,459	6,459
Other comprehensive income						
Fair valuation of financial assets measured at FVOCI:						
Net changes in fair value arising during the year		-	-	(1,002)	-	(1,002)
Reclassification adjustments:						
- net amounts reclassified to profit or loss on disposal		-	-	(109)	-	(109)
Net amounts reflected directly in retained earnings on disposal	6	-	-	-	976	976
Net change attributable to changes in credit risk		-	-	406	-	406
Transfers and other movements		-	-	(120)	120	-
Total other comprehensive income for the year		-	-	(825)	1,096	271
Total comprehensive income for the year		-	-	(825)	7,555	6,730
At 31 December 2020		11,044	18,530	17,076	74,692	121,342

The notes on pages 38 to 139 are an integral part of these financial statements.

Statements of Changes in Equity
For the Year Ended 31 December 2021

Bank	note	Share capital € 000	Share premium € 000	Revaluation and other reserves € 000	Retained earnings € 000	Total Equity € 000
At 1 January 2021		**11,044**	**18,530**	**17,076**	**74,692**	**121,342**
Comprehensive income						
Profit for the year		-	-	-	**7,804**	**7,804**
Other comprehensive income						
Surplus on revaluation of land and buildings, net of tax		-	-	**5,678**	-	**5,678**
Fair valuation of financial assets measured at FVOCI:						
Net changes in fair value arising during the year		-	-	**(1,628)**	-	**(1,628)**
Reclassification adjustments:						
- net amounts reclassified to profit or loss on disposal		-	-	**(109)**	-	**(109)**
Net movement attributable to changes in credit risk		-	-	**(223)**	-	**(223)**
Transfers and other movements		-	-	**34**	**(34)**	-
Total other comprehensive income for the year		-	-	**3,752**	**(34)**	**3,718**
Total comprehensive income for the year		-	-	**3,752**	**7,770**	**11,522**
Transactions with owners, recorded directly in equity						
Contributions by and distributions to owners						
Dividends to equity holders	**36**	-	-	-	**(862)**	**(862)**
Bonus issue		**148**	-	-	**(148)**	-
Total transactions with owners		**148**	-	-	**(1,010)**	**(862)**
At 31 December 2021		**11,192**	**18,530**	**20,828**	**81,452**	**132,002**

The notes on pages 38 to 139 are an integral part of these financial statements.

Cashflow Statements
For the Year Ended 31 December 2021

	notes	Group 2021 € 000	Group 2020 € 000	Bank 2021 € 000	Bank 2020 € 000
Cash flows from operating activities					
Interest and commission receipts		**28,586**	31,337	**28,599**	31,712
Receipts from customers relating to postal sales and other revenue		**36,402**	38,112	**518**	786
Interest and commission payments		**(5,712)**	(5,838)	**(5,714)**	(5,780)
Payments to employees and suppliers		**(44,981)**	(45,053)	**(15,582)**	(14,077)
Cash flows from operating profit before changes in operating assets and liabilities		**14,295**	18,558	**7,821**	12,641
(Increase)/decrease in operating assets:					
Treasury bills		**18,027**	(8,521)	**18,027**	(8,521)
Deposits with Central Bank of Malta		**341**	(786)	**341**	(786)
Loans and advances to banks and customers		**(26,052)**	(72,163)	**(21,552)**	(73,163)
Other receivables		**4**	1,905	**(279)**	1,911
Increase/(decrease) in operating liabilities:					
Amounts owed to banks and to customers		**36,033**	76,107	**29,887**	79,646
Other payables		**(5,142)**	4,739	**(4,859)**	4,736
Net cash generated from operations		**37,506**	19,839	**29,386**	16,464
Income tax paid		**(5,870)**	(5,364)	**(5,516)**	(6,013)
Net cash flows generated from operating activities		**31,636**	14,475	**23,870**	10,451
Cash flows from investing activities					
Dividends received		**81**	105	**1,738**	1,762
Interest received from investments		**3,012**	2,198	**2,863**	2,029
Purchase of investments		**(75,270)**	(67,862)	**(75,270)**	(67,862)
Proceeds from maturity/disposal of investments		**6,760**	16,468	**6,151**	16,237
Purchase of property, plant and equipment and intangible assets		**(7,601)**	(8,942)	**(3,728)**	(6,610)
Proceeds from disposal of property, plant and equipment		**-**	18	-	18
Investments in associate	10	**(1,500)**	(399)	-	-
Investment in subsidiary	9	**-**	-	**(126)**	-
Net cash inflow arising from acquisition of subsidiary	9	**833**	-	**-**	-
Net cash flows used in investing activities		**(73,685)**	(58,414)	**(68,372)**	(54,426)
Cash flows from financing activities					
Dividends paid to equity holders of the Bank	36	**(862)**	-	**(862)**	-
Dividends paid to non-controlling interests		**(429)**	(427)	**-**	-
Principal element of lease payments		**(527)**	(409)	**(203)**	(152)
Net cash flows used in financing activities		**(1,818)**	(836)	**(1,065)**	(152)
Net (decrease)/increase in cash and cash equivalents		**(43,867)**	(44,775)	**(45,567)**	(44,127)
Cash and cash equivalents at beginning of year		**210,127**	254,902	**207,245**	251,372
Cash and cash equivalents at end of year	37	**166,260**	210,127	**161,678**	207,245

The notes on pages 38 to 139 are an integral part of these financial statements.

Notes to the Financial Statements
For the Year Ended 31 December 2021

1 Summary of significant accounting policies

The principal accounting policies adopted in the preparation of these financial statements are set out below. Unless otherwise stated, these policies have been consistently applied to all the years presented and relate to both the Group and the Bank.

1.1 Basis of preparation

The consolidated financial statements include the financial statements of Lombard Bank Malta p.l.c. (the Bank) and its subsidiary undertakings (together referred to as 'the Group' and individually as 'Group entities'). The Bank's financial statements have been prepared in accordance with the requirements of International Financial Reporting Standards (IFRSs) as adopted by the EU and with the requirements of the Banking Act 1994 (Chapter 371 of the Laws of Malta) and the Companies Act, 1995 (Chapter 386 of the Laws of Malta). These consolidated financial statements are prepared under the historical cost convention, as modified by the fair valuation of financial assets and financial liabilities.

The preparation of financial statements in conformity with IFRSs as adopted by the EU requires the use of certain accounting estimates. It also requires the Directors to exercise their judgment in the process of applying the Group's accounting policies (see note 3.1 – Critical accounting estimates, and judgments in applying the Group's accounting policies).

1.2 Standards, interpretations and amendments to published standards effective in 2021

In 2021, the Group adopted amendments and interpretations to existing standards that are mandatory for the Group's accounting period beginning on 1 January 2021. The adoption of these revisions to the requirements of IFRSs as adopted by the EU did not result in changes to the Group's accounting policies impacting the Group's financial performance and position.

Interest Rate Benchmark Reform Phase 2

The IASB published 'Interest Rate Benchmark Reform - Phase 2: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16' in August 2020, which became effective from 1 January 2021. These amendments represent the second phase of the IASB's project on the effects of the interest rate benchmark reform, addressing issues affecting financial statements when changes are made to contractual cash flows because of the reform.

Under these amendments, changes made to a financial instrument that are economically equivalent and required by the interest rate benchmark reform, do not result in the derecognition or a change in the carrying amount of the financial instrument, but instead require the effective interest rate to be updated to reflect the change in the interest rate benchmark.

The Group has evaluated the extent of the discontinuation of the Interbank Offered rates (IBOR) on local loans and advances granted by the Group. The Group's exposure in this respect is insignificant and the Bank expects to migrate all loans by July 2023, in line with the deadline set by the EU.

The Bank's corporate loans and advances that re-price to the EURIBOR reference rate are not a significant part of the portfolio. While not impacted by the benchmark rate reform, going forward, the Group will be including a fallback provision in respect of these facilities that will safeguard the Group and its clients in the unlikely event of a cessation of the EURIBOR reference rate, in line with the recommendations issued by the ECB Working Group on Risk-free Rates.

Considering the Group's insignificant and limited exposure to IBOR, the transition is expected to have an insignificant impact on the Bank's operations and financial position. The Group will continue to monitor the regulatory developments in this respect, with a particular focus on developments relating to the EURIBOR reference rate.

1.3 Standards, interpretations and amendments to published standards that are not yet effective

There were no new standards, amendments and interpretations to existing standards which are mandatory for accounting periods beginning after 1 January 2021 that were published by the date of authorisation for issue of this financial information and which could have a possible significant impact on the Group's financial statements in the period of initial application.

1 **Summary of significant accounting policies** *(continued)*

1.4 Consolidation

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

The Group manages and administers investment vehicles on behalf of investors. The financial statements of these entities are not included in these financial statements, except when the Group controls the entity.

The Group uses the acquisition method of accounting to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition- related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If this aggregate is less than the fair value of the identifiable net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in profit or loss.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The accounting policies of the subsidiaries are consistent with the policies adopted by the Group. In the Bank's separate financial statements, investments in subsidiaries are accounted for by the cost method of accounting, i.e. at cost less impairment. Provisions are recorded where, in the opinion of the Directors, there is an impairment in value. Where there has been an impairment in the value of an investment, it is recognised as an expense in the period in which the diminution is identified. The results of subsidiaries are reflected in the Bank's separate financial statements only to the extent of dividends receivable. On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is charged or credited to profit or loss.

1.5 Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the Board of Directors which is the Group's chief operating decision-maker.

An operating segment's operating results are reviewed regularly by the Board of Directors to make decisions about resources to be allocated to the segment and to assess its performance executing the function of the chief operating decision-maker.

1.6 Foreign currency translation

The financial statements are presented in euro (€), which is the Group's presentation currency.

1.6.1 Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in euro, which is the Group's functional and presentation currency.

1.6.2 Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement.

1 **Summary of significant accounting policies** *(continued)*

1.7 Financial assets

1.7.1 Initial recognition and measurement

The Group recognises a financial asset in its statement of financial position when it becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on the trade date, which is the date on which the Group commits to purchase or sell the asset. Accordingly, the Bank uses trade date accounting for regular way contracts when recording financial asset transactions.

At initial recognition, the Bank measures a financial asset at its fair value plus or minus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset, such as fees and commissions. Transaction costs of financial assets carried at fair value through profit or loss are expensed in profit or loss. At initial recognition, an Expected Credit Loss allowance (ECL) is recognised for financial assets measured at amortised cost and investments in debt instruments measured at FVOCI, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

When the fair value of financial assets differs from the transaction price on initial recognition, the Group recognises the difference as follows:

- when the fair value is evidenced by a quoted price in an active market for an identical asset (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss; and
- in all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

1.7.2 Classification and subsequent measurement

The Group classifies its financial assets in the following measurement categories:

- Fair value through profit or loss (FVPL);
- Fair value through other comprehensive income (FVOCI); or
- Amortised cost.

1.7.2.1 Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds and trade receivables purchased from clients in factoring arrangements without recourse.

Classification and subsequent measurement of debt instruments depend on:

- the Group's business model for managing the asset; and
- the cash flow characteristics of the asset.

Based on these factors the Group classifies its debt instruments into one of the following three measurement categories:

- *Amortised cost:* Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest (SPPI), and that are not designated at FVPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any Expected Credit Loss allowance recognised and measured as described in note 1.7.3. Interest income from these financial assets is included in 'Interest and similar income' using the effective interest rate method.

- *Fair value through other comprehensive income (FVOCI)*: Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVPL, are measured at fair value through other comprehensive income (FVOCI). Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortised cost which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to

1 **Summary of significant accounting policies** *(continued)*

profit or loss and recognised in 'Net Investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

- *Fair value through profit or loss (FVPL)*: Assets that do not meet the criteria for amortised cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognised in profit or loss and presented in the profit or loss statement within 'Net trading income' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Net investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest.

The amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability.

The calculation does not consider Expected Credit Losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees. For purchased or originated credit-impaired (POCI) financial assets - assets that are credit-impaired at initial recognition - the Bank calculates the credit-adjusted effective interest rate, which is calculated based on the amortised cost of the financial asset instead of its gross carrying amount and incorporates the impact of Expected Credit Losses in estimated future cash flows.

When the Bank revises the estimates of future cash flows, the carrying amount of the respective financial assets or financial liability is adjusted to reflect the new estimate discounted using the original effective interest rate. Any changes are recognised in profit or loss.

The Bank reclassifies debt instruments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and none occurred during the period.

(a) *Business model assessment*

Key management personnel determine the Group's business model by considering the way financial instruments are managed in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'other' business model and measured at FVPL. Such assessment is performed at a 'portfolio level' as it best reflects the way the business is managed and information is provided to management.

The information that will be considered in such assessment includes:

- the objectives for the portfolio including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
- the method for the evaluation of the performance of the portfolio and how such performance is reported to the Group's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets. Securities held for trading are held principally for the purpose of selling in the near term or are part of a portfolio of financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking.

1 **Summary of significant accounting policies** *(continued)*

The Bank may also irrevocably designate financial assets at fair value through profit or loss if doing so significantly reduces or eliminates a mismatch created by assets and liabilities being measured on different bases.

(b) *Cash flows that represent solely payment of principal and interest (SPPI)*

In respect of assets where the intention of the business model is to hold the financial assets to collect the contractual cash flows or to hold to collect and to sell, the Group assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the SPPI test). In making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending agreement. 'Principal' is the fair value of the financial asset at initial recognition. It is not the amount that is due under the contractual terms of an instrument. 'Interest' is the compensation for time value of money and credit risk of a basic lending-type return. A basic lending-type return could also include consideration for other basic lending risks (for example, liquidity risk) and consideration for costs associated with holding the financial asset for a particular period of time (for example, servicing or administrative costs) and/or a profit margin. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

Unlike the business model assessment, the SPPI assessment is performed for each individual product or portfolio of products. The following considerations are made when assessing consistency with SPPI:

- contingent events that would change the amount and timing of cash flows such as contractual term resetting interest to a higher amount in the event of a missed payment;
- leverage features, being contractual cash flow characteristics that increase the variability of the contractual cash flows with the result that they do not have economic characteristics of interest;
- contractual terms that allow the issuer to prepay (or the holder to put a debt instrument back to the issuer) before maturity and the prepayment amount substantially represents unpaid amounts of principal and interest, which may include reasonable compensation for early termination of the contract;
- contractual terms that allow the issuer or holder to extend the contractual term and the terms of the extension option result in contractual cash flows during the extension period that are solely payments of principal and interest, which may include reasonable compensation for the extension of the contract; and
- features that modify consideration for the time value of money (for example, periodic reset of interest rates).

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

1.7.2.2 Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective, that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

The Group subsequently measures all equity investments at fair value through profit or loss, except where the Group's management has elected, at initial recognition, to irrevocably designate an equity investment at fair value through other comprehensive income. The Group's policy is to designate equity investments as FVOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal.

Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value. Dividends, when representing a return on such investments, continue to be recognised in profit or loss as other income when the Group's right to receive payments is established.

Gains and losses on equity investments at FVPL are included in the 'Net trading income' line in the income statement.

1.7.3 Impairment of financial assets

The Group assesses on a forward-looking basis the Expected Credit Losses (ECLs) associated with its debt instruments carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Group recognises a loss allowances for such losses at each reporting date. The measurement of ECLs reflects:

1 **Summary of significant accounting policies** *(continued)*

- an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- the time value of money; and
- reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Note 2.3.4 provides more detail of how the Expected Credit Loss allowance is measured.

Expected Credit Loss allowances are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- financial instrument with both a drawn and undrawn component, whereby the Group cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Group presents a combined loss allowance for both components, as a deduction from the gross carrying amount of the drawn component; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position against the carrying amount of the asset because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve, i.e. presented within other comprehensive income.

1.7.4 Modification of loans and advances to customers

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer.

The Group renegotiates loans and advances to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Group's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms, and the debtor is expected to be able to meet the revised terms. The revised terms usually include extending the maturity, revision of interest rate and changing the timing of interest payments. Both retail and corporate loans are subject to the forbearance policy.

When modification happens, the Group assesses whether or not the new terms are substantially different to the original terms. The Group does this by considering, among others, the following factors:

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- Whether any substantial new terms are introduced.
- Significant extension of the loan term when the borrower is not in financial difficulty.
- Significant change in the interest rate
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Group derecognises the original financial asset and recognises a 'new' asset at fair value, and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Group also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, and the Group recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss.
The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit- impaired financial assets). The impact of modifications of financial assets on the Expected Credit Loss calculation is discussed in note 2.3.9.

1 **Summary of significant accounting policies** *(continued)*

1.7.5 Derivative financial instruments

The Group deploys no hedging strategies that achieve hedge accounting in terms of IAS 39.

Derivative financial instruments are initially recognised at fair value on the date on which a derivative contract is entered into, and are subsequently remeasured at their fair value. Fair values are obtained from valuation techniques for over-the-counter derivatives, including discounted cash flow models. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative. Fair values for currency forwards are determined using forward exchange market rates at the end of the reporting period. Discounting techniques, reflecting the fact that the respective exchange or settlement will not occur until a future date, are used when the time value of money has a significant effect on the fair valuation of these instruments.

Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in profit or loss.

The Group uses derivatives such as cross currency swaps and forward foreign exchange contracts.

1.8 Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is possible that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

1.9 Investments in subsidiaries

The Group classifies investments in entities which it controls as subsidiaries.

The Group's investments in subsidiaries are stated at cost less impairment losses in the Group's stand- alone financial statements. Impairment losses recognised in prior periods are reversed through profit or loss if there has been a change in the estimates used to determine the investment's recoverable amount since the last impairment loss was recognised.

1.10 Investment in associate

Associates are all entities over which the Group has significant influence but not control or joint control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting in the consolidated financial statements, after initially being recognised at cost. Under the equity method of accounting, the investment is initially recognised at cost, and the carrying amount is adjusted thereafter to recognise the Group's share of the post-acquisition profits or losses of the investee in profit or loss, and the Group's share of movements in other comprehensive income of the investee in other comprehensive income. The Group's investment in associates includes goodwill identified on acquisition. Dividends received or receivable from associates are recognised as a reduction in the carrying amount of the investment.

When the Group's share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate.

The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount adjacent to 'share of profit/(loss) of investment accounted for using the equity method' in the income statement.

1 **Summary of significant accounting policies** *(continued)*

Profits and losses resulting from upstream and downstream transactions between the Group and its associate are recognised in the Group's financial statements only to the extent of unrelated investor's interests in the associates. Unrealised losses are eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income is reclassified to profit or loss where appropriate.

Dilution gains and losses arising in investments in associates are recognised in the income statement.

In the Bank's separate financial statements, investments in associates are accounted for by the cost method of accounting, i.e. at cost less impairment. Provisions are recorded where, in the opinion of the Directors, there is impairment in value. Where there has been impairment in the value of an investment, it is recognised as an expense in the period in which the diminution is identified. The results of the associate are reflected in the Bank's separate financial statements only to the extent of dividends receivable. On disposal of an investment, the difference between the net disposal proceeds and the carrying amount is charged or credited to profit or loss.

1.11 Intangible assets

1.11.1 Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the identifiable net assets of the acquired subsidiary at the date of acquisition. Goodwill on acquisitions of subsidiaries is included in 'intangible assets'.

Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity include the carrying amount of goodwill relating to the entity sold.

Goodwill is allocated to cash-generating units for the purpose of impairment testing. The allocation is made to those cash-generating units or groups of cash-generating units that are expected to benefit from the business combination in which the goodwill arose, identified according to operating segment. A cash- generating unit to which goodwill has been allocated is tested for impairment annually, and whenever there is an indication that the unit may be impaired by comparing the carrying amount of the unit, including the goodwill, with the recoverable amount of the unit. The recoverable amount is the higher of fair value less costs to sell and value in use.

1.11.2 Computer software

Costs incurred to acquire and bring to use specific software are capitalised and amortised on the basis of the expected useful lives. Software has a maximum expected useful life of four years.

1.12 Property, plant and equipment

All property, plant and equipment used by the Group is initially recorded at historical cost, including transaction costs and borrowing costs. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Freehold and long leasehold properties (land and buildings) comprise mainly branches and offices. Land and buildings are shown at fair value based on periodic valuations by external independent valuers, less subsequent depreciation for buildings. Valuations are carried out on a regular basis such that the carrying amount of property does not differ materially from that which would be determined using fair values at the end of the reporting period. Any accumulated depreciation at the date of revaluation is eliminated against the gross carrying amount of the asset, and the net amount is restated to the revalued amount of the asset.

All other property, plant and equipment is stated at historical cost less accumulated depreciation.
Borrowing costs which are incurred for the purpose of acquiring or constructing a qualifying asset are capitalised as part of its cost. Borrowing costs are capitalised while acquisition or construction is actively underway. Capitalisation of borrowing costs is ceased once the asset is substantially complete, and is suspended if the development of the asset is suspended.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be

1 **Summary of significant accounting policies** *(continued)*

measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance are charged to profit or loss during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of land and buildings are credited to other comprehensive income and shown as a revaluation reserve in shareholders' equity. Decreases that offset previous increases of the same asset are charged to other comprehensive income and debited against the revaluation reserve directly in equity; all other decreases are charged to profit or loss.

Land is not depreciated as it is deemed to have an indefinite life. Depreciation on other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

	Years
Buildings	100 or over period of lease/arrangement
Leasehold property	Over period of lease/arrangement
Computer equipment	4
Other	4 – 8

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (see note 1.13).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised in profit or loss. When revalued assets are sold, the amounts included in the revaluation reserve relating to that asset are transferred to retained earnings.

1.13 Impairment of non-financial assets

Assets that have an indefinite useful life, for example goodwill or certain intangible assets, are not subject to amortisation and are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units). The impairment test also can be performed on a single asset when the fair value less costs to sell or the value in use can be determined reliably. Non-financial assets other than goodwill that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

1.14 Repossessed property

In certain circumstances, property is repossessed following the foreclosure on loans that are in default. Repossessed properties are measured at the lower of carrying amount and fair value less costs to sell.

1.15 Non-current assets held for sale

Non-current assets are classified as assets held for sale and are stated at the lower of carrying amount and fair value less costs to sell when their carrying amount is to be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable.

1.16 Current and deferred income tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

1 **Summary of significant accounting policies** *(continued)*

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period.

Deferred income tax is recognised, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred tax liabilities are not recognised if they arise from the initial recognition of goodwill; deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries, except for deferred income tax liability where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

1.17 Inventories

Inventories are stated at the lower of cost and net realisable value. The cost of postal stationery and inventories held for resale is determined on a weighted average cost basis. The cost of inventories is determined on a first-in first-out basis. The cost of inventories comprise the invoiced value of goods sold and in general includes transport and handling costs. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses.

1.18 Trade and other receivables

Trade receivables are amounts due from customers for merchandise sold or services performed in the ordinary course of business. If collection is expected in one year or less (or in the normal operating cycle of the business if longer), they are classified as current assets. If not, they are presented as non-current assets.

Trade and other receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provisions for impairment. A provision for impairment of trade and other receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or financial reorganisation, and default or delinquency in payments are considered indicators that the receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognised in profit or loss. When a receivable is uncollectible, it is written off against the allowance account for trade and other receivables. Subsequent recoveries of amounts previously written off are credited in profit or loss.

1.19 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new ordinary shares are shown in equity as a deduction, net of tax, from the proceeds.

1 **Summary of significant accounting policies** *(continued)*

1.20 Financial liabilities

1.20.1 Initial recognition and measurement

The Group recognises a financial liability on its statement of financial position when it becomes a party to the contractual provisions of the instrument. Financial liabilities not at fair value through profit or loss are recognised initially at fair value, being the fair value of consideration received, net of transaction costs that are directly attributable to the acquisition or the issue of the financial liability.

1.20.2 Classification and subsequent measurement

Financial liabilities are classified as subsequently measured at amortised cost, except for:

- financial liabilities at fair value through profit or loss: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in the trading booking) and other financial liabilities designated as such at initial recognition. Gains or losses on financial liabilities designated at fair value through profit or loss are presented partially in other comprehensive income (the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability, which is determined as the amount that is not attributable to changes in market conditions that give rise to market risk) and partially profit or loss (the remaining amount of change in the fair value of the liability). This is unless such a presentation would create, or enlarge, an accounting mismatch, in which case the gains and losses attributable to changes in the credit risk of the liability are also presented in profit or loss;
- financial liabilities arising from the transfer of financial assets which did not qualify for derecognition, whereby a financial liability is recognised for the consideration received for the transfer. In subsequent periods, the Group recognises any expense incurred on the financial liability; and
- financial guarantee contracts and loan commitments (see note 1.30).

The Group's financial liabilities were classified as financial liabilities which were not at fair value through profit or loss (classified as 'Other liabilities') under IAS 39. These liabilities were subsequently measured at amortised cost.

Financial liabilities measured at amortised cost comprise principally amounts owed to banks, amounts owed to customers, debt securities in issue together with other liabilities.

1.20.3 Derecognition

The Group derecognises a financial liability from its statement of financial position when the obligation specified in the contract or arrangement is discharged, is cancelled or expires.

The exchange between the Group and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability.

In addition, other qualitative factors, such as the currency that the instrument is denominated in, changes in the type of interest rate, new conversion features attached to the instrument and change in covenants are also taken into consideration. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

1.21 Repurchase and reverse repurchase agreements

Securities sold under agreements to repurchase at a specified future date are not derecognised from the statement of financial position as the Group retains substantially all of the risks and rewards of ownership. The corresponding cash received is recognised in the statement of financial position as an asset with a corresponding obligation to return it, including accrued interest as a liability, reflecting the transaction's economic substance as a loan to the Group. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of agreement using the effective interest rate.

1 **Summary of significant accounting policies** *(continued)*

When the counterparty has the right to sell or repledge the securities, the Bank reclassifies those securities in its statement of financial position to financial assets held for trading pledged as collateral or to financial investments available-for-sale pledged as collateral, as appropriate.

Conversely, securities purchased under agreements to resell at a specified future date are not recognised in the statement of financial position. The consideration paid, including accrued interest, is recorded in the statement of financial position, reflecting the transaction's economic substance as a loan by the Bank. The difference between the purchase and resale prices is recorded in net interest income and is accrued over the life of the agreement using the effective interest rate.

If securities purchased under agreement to resell are subsequently sold to third parties, the obligation to return the securities is recorded as a short sale within financial liabilities held for trading and measured at fair value with any gains or losses included in net trading income.

1.22 Trade and other payables

Trade payables comprise obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities. Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

1.23 Provisions for legal and other claims

Provisions for legal and other claims are recognised when: the Group has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

1.24 Provision for pension obligations

A subsidiary of the Bank provides for the obligation arising in terms of Article 8A of the Pensions Ordinance, (Chapter 93 of the Laws of Malta), covering those former Government employees who opted to become full-time employees of the subsidiary of the Bank, and who continued to be entitled to pension benefits which go beyond the National Insurance Scheme.

The pension related accounting costs are assessed using the projected unit credit method. Under this method, the cost of the subsidiary's obligation is charged to profit or loss so as to spread the cost over the years of service giving rise to entitlement to benefits in accordance with actuarial techniques. The obligation is measured as the present value of the estimated future cash outflows using interest rates of long-term Government bonds which have terms to maturity approximating the terms of the related liability. Subsequent to the adoption of IAS 19 (revised 2011), all actuarial gains and losses are charged or credited to equity in other comprehensive income in the period in which they arise.

1.25 Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised within 'interest income' and 'interest expense' in the profit or loss using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability.

1 **Summary of significant accounting policies** *(continued)*

The calculation does not consider Expected Credit Losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees. For purchased or originated credit-impaired (POCI) financial assets - assets that are credit-impaired at initial recognition - the Group calculates the credit-adjusted effective interest rate, which is calculated based on the amortised cost of the financial asset instead of its gross carrying amount and incorporates the impact of Expected Credit Losses in estimated future cash flows.

1.26 Fees and commissions

Fee and commission income and expense that are an integral part of the effective interest rate on a financial asset or liability are included in the calculation of the effective interest rate and treated as part of effective interest. Other fees and commissions are generally recognised on an accrual basis when the service has been provided.

Fee and commission income, comprising account servicing fees, investment management fees, placement fees and other similar fees, are recognised as the related services are performed.

Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. When a loan commitment is not expected to result in the drawdown of a loan, the related loan commitment fees are recognised on a straight-line basis over the commitment period. Fee and commission expense, relating mainly to transaction and service fees, are expensed as the services are received.

1.27 Postal sales and service income

Postal sales and service revenue comprises the fair value of the consideration received or receivable for the sale of services in the ordinary course of the subsidiary's activities. Revenue is shown net of sales taxes and discounts. It comprises revenue directly received from customers, commissions earned on postal and non-postal transactions and income from foreign outbound mail receivable from overseas postal administrators.

Income from sale of stamps, commission earned on postal and non-postal transactions and revenue from foreign outbound mail from overseas postal administrators is recognised when the service is rendered. Allowance is made for the assessed amount of revenue from prepaid product sales at the end of the reporting period for which the service has not yet been provided. In the case of services rendered to postal administrators in countries subject to severe exchange control restrictions and undue delays in settlement, revenue is not recognised until the subsidiary is in a position to ensure that the economic benefits associated with the transaction will flow to it, which is often upon or shortly before actual receipt.

1.28 Dividend income

Dividends are recognised in profit or loss in 'dividend income' when the entity's right to receive payment is established.

1.29 Leases

1.29.1 When a Group company is the lessee

The Group recognises lease liabilities in relation to leases within 'other liabilities'. The lease liability is measured at the present value of the remaining lease payments, discounted at the Group's incremental borrowing rate. The associated right-of-use (ROU) assets are recognised and included within 'property, plant and equipment' and are measured at the amount equal to the lease liability.

The Group applies the following practical expedients:

- a single discount rate is applied to a portfolio of leases with reasonable similar characteristics;
- an assessment is performed on whether leases are onerous; and
- hindsight is used in determining the lease term where the contract contains options to extend or terminate the lease.

1 **Summary of significant accounting policies** *(continued)*

Lease payments are allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease term.

The lease term is the non-cancellable period of a lease, together with both (a) periods covered by an option to extend the lease if the lessee is reasonably certain to extend that option; and (b) periods covered by an option to terminate the lease if the lessee is reasonably certain not to exercise that option. In assessing the length of the non-cancellable period of a lease, the Group applies the definition of a contract to determine the period for which the contract is enforceable. A lease is no longer enforceable when the lessee and the lessor each has the right to terminate the lease without permission from the other party with no more than an insignificant penalty.

The ROU asset is depreciated over the shorter of the ROU asset's useful economic life and the lease term on a straight-line basis.

The leases with a remaining lease term of less than 12 months are accounted as short-term operating leases.

Payments made under operating leases (net of any incentives received from the lessor) are charged to profit or loss on a straight-line basis over the period of the lease.

1.30 Financial guarantee contracts and loan commitments

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and other bodies on behalf of customers.

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances.

Financial guarantee contracts are initially measured at fair value and subsequently measured at higher of:

- the amount of the loss allowance (calculated as described in note 1.7.3); and
- the premium received on initial recognition less income recognised in accordance with the principles of IFRS 15.

'Loan commitments' are the Bank's commitments to provide credit under pre-specified terms and conditions, and are measured as the amount of the loss allowance (calculated as described in note 1.7.3).

For loan commitments and financial guarantee contracts, the loss allowance is recognised as a provision. However, for contracts that include both a loan and an undrawn commitment and the Bank cannot separately identify the Expected Credit Losses on the undrawn commitment component from those on the loan component, the Expected Credit Losses on the undrawn commitment are recognised together with the loss allowance for the loan. To the extent that the combined Expected Credit Losses exceed the gross carrying amount of the loan, the Expected Credit Losses are recognised as a provision.

1.31 Cash and cash equivalents

Cash and cash equivalents are carried in the statement of financial position at face value. Cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

1.32 Dividend distribution

Dividend distribution to the Bank's shareholders is recognised as a liability in the Group's financial statements in the period in which the dividends are approved by the Bank's shareholders.

2 Financial risk management

2.1 Introduction

2.1.1 Preamble

The Group's business involves taking on risks in a targeted manner and managing them professionally. The core functions of the Group's risk management are to identify all key risks for the Group, measure these risks, manage the risk positions and determine capital allocations. The Group regularly reviews its risk management policies and systems to reflect changes in markets, products and best market practice. The Group's aim is to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Group's financial performance. The Group defines risk as the possibility of losses or profits foregone, which may be caused by internal or external factors.

The Group considers risk management a core competency that helps produce consistently high returns for its various stakeholders. The Group aims to manage all major types of risk by applying methods that meet best practice. The Group considers it important to have a clear distribution of responsibilities within the area of risk management. One of the main tasks of the Group's executive management is to set the framework for this area. An understanding of risk-taking and transparency in risk-taking are key elements in the Group's business strategy and thus in its ambition to be a strong financial entity. The Group's internal risk management processes support this objective.

Risk management within the Bank is mainly carried out on a unified basis, using an integrated and entity-wide framework. This framework is based on local and international guidelines, such as the Basel III Accord, corresponding Directives and Regulations of the European Union, including technical standards, as well as contemporary international banking practices. The Bank has adopted the Standardised Approach and the Basic Method with respect to the calculation of capital requirements in relation to, and management of, credit and market risks, and the Basic Indicator Approach with respect to operational risk. The Bank regularly updates its Internal Capital and Liquidity Adequacy Assessment Processes (ICAAP and ILAAP), that are approved by the Board of Directors.

2.1.2 Organisation

The Bank's Board of Directors is responsible for ensuring that adequate processes and procedures exist to ensure effective internal control systems for the Group. These internal control systems ensure that decision-making capability and the accuracy of the reporting and financial results are maintained at a high level at all times. The Board assumes responsibility for:

- setting business objectives, goals and the general strategic direction for Management with a view to maximise value;
- selecting and appointing the Chief Executive Officer who is entrusted with the day-to-day operations of the Group;
- management of the Group's operations;
- ensuring that significant business risks are identified and appropriately managed; and
- setting the highest business standards and code for ethical behaviour, and monitoring adherence with these.

In deciding how best to discharge its responsibilities, the Board upholds a policy of clear demarcation between its role and responsibilities and those of Management. It has defined the level of authority that it retains over strategy formulation and policy determination, and delegated authority and vested accountability for the Bank's day-to-day business in the Assets & Liabilities Committee and Credit Committee, and, for the Group's day-to-day operations, in an Executive Team comprising the Chief Executive Officer and Chief Officers. The Audit & Risk Committee reviews the processes and procedures to ensure the effectiveness of the Group's system of internal control, as well as the implementation of the Board's risk strategy by management. The Audit & Risk Committee is supported by the Internal Audit, Risk Management and Compliance functions.

Authority to operate the Bank and its subsidiaries is delegated to the Chief Executive Officer within the limits set by the Board. The Board is ultimately responsible for the Group's system of internal control 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 provide only reasonable, and not absolute, assurance against material misstatement or loss.

The Group is committed to the highest standards of business conduct and seeks to maintain these standards across all operations. Group policies and procedures are in place for the reporting and addressing of fraudulent activities.

The Group has an appropriate organisational structure for planning, executing, controlling and monitoring business operations in order to achieve Group objectives.

2 **Financial risk management** *(continued)*

2.1.3 Risk policies

The Bank's Board of Directors is empowered to set out the overall risk policies and limits for all material risk types. The Board also decides on the general principles for managing and monitoring risks. The Board provides written principles for overall risk management, as well as written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments.
Internal controls, procedures and processes are managed within the following areas:

- Finance
- Treasury
- Credit
- Internal Audit
- Risk Management
- Compliance
- Anti-Money Laundering

2.1.4 Risk appetite

The risk appetite determines the maximum risk that the Group is willing to assume to meet business targets. To ensure coherence between the Group's strategic considerations regarding risk-taking and day-to-day decisions, from time to time, the Group formulates and updates its risk appetite for the purposes of strategic direction. The Group's risk appetite is set in a process based on a thorough analysis of its current risk profile. The Group identifies a number of key risk components and for each, determines a target that represents the Group's view of the component in question. The following are the key risk components:

- Credit risk
- Market risk
- Capital risk
- Liquidity risk
- Operational risk
- Information technology risk
- Information management risk
- Financial crime risk
- Compliance risk

2.1.5 Reporting

The Group allocates considerable resources to ensure the ongoing compliance with approved limits and to monitor its asset portfolio. In particular, the Bank has a fixed reporting cycle to ensure that the relevant management bodies, including the Board of Directors and the Executive Team, are kept informed on an ongoing basis of developments in the asset portfolio, such matters as non-performing loans and other relevant information.

2.2 Risk exposures

In terms of the CRR, 'an exposure' is the amount at risk arising from the reporting credit institution's assets and off-balance sheet items. Consistent with this, an exposure would include the amount at risk arising from the Bank's:

- claims on a customer including actual and potential claims which would arise from the drawing down in full of undrawn advised facilities, which the Bank has committed itself to provide;
- contingent liabilities arising in the normal course of business, and those contingent liabilities which would arise from the drawing down in full of undrawn advised facilities which the Bank has committed itself to provide; and
- other on and off-balance sheet financial assets and commitments.

The Group is exposed to a number of risks, which it manages at different organisational levels.

2 **Financial risk management** *(continued)*

The main categories of risk are:

- *Credit risk*: Credit risk stems from the possible non-prompt repayment or non-payment of existing and contingent obligations by the Group's counterparties, resulting in the loss of equity and profit. It is the risk that deterioration in the financial condition of a borrower will cause the asset value to decrease or be extinguished. Country risk and settlement risk are included in this category. Country risk refers to the risk of losses arising from economic or political changes that affect the country from which the asset originates. Settlement risk refers to the risk of losses through failure of the counterparty to settle outstanding dues on the settlement date owing to bankruptcy or other causes.

- *Market risk*: Risk of losses arising from unfavourable changes in the level and volatility of interest rates, foreign exchange rates or investment prices.

- *Liquidity risk*: Liquidity risk may be divided into two sub-categories:
  - Market (product) -Market (product) liquidity risk: Risk of losses arising from difficulty in accessing a product or market at the required time, price and amount.
  - Funding liquidity risk: Risk of losses arising from a timing mismatch between investing, placements and fund raising activities resulting in obligations missing the settlement date or satisfied at higher than normal rates.

- *Operational risk*: Risk of loss resulting from the lack of skilful management or good governance within the Group and the inadequacy of proper control, which might involve internal operations, personnel, systems or external occurrences that in turn affect the income and capital funds of financial institutions. The Bank has adopted an operational risk management framework and procedures, which provide for the identification, assessment, management, monitoring and reporting of the Bank's operational risks.

The Bank's approach to management of the above risks is addressed in this note.

2.3 Credit risk

2.3.1 Introduction

Credit risk is the risk of suffering financial loss, should any of the Group's customers, clients or market counterparties fail to fulfil their contractual obligations to the Group. Credit risk arises mainly from consumer loans and advances and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as financial guarantees and letters of credit.

The Group is also exposed to other credit risks arising from investments in debt securities and other exposures arising from its investing activities.

Credit risk constitutes the Bank's largest risk in view of its significant lending and securities portfolios, which is monitored in a structured and formal manner through several mechanisms and procedures. The credit risk management and control functions are centralised.

2.3.2 Credit risk management

The granting of a credit facility (including loans and advances, loan commitments and guarantees) is based on the Bank's insight into the customer's financial position, which is reviewed regularly to assess whether the basis for the granting of credit has changed. Furthermore, the customer must be able to demonstrate, in all probability, the ability to repay the debt. Internal approval limits are in place starting from Bank operational managers leading up to the Credit Committee and the Board of Directors depending on the magnitude and the particular risks attached to the facility. Facilities are generally adequately secured either by property and/or guarantees and are reviewed periodically by management in terms of the exposure to the Bank and to ensure that collateral still covers the facility.

In order to minimise the credit risk undertaken, counterparty credit limits are defined with respect to investment activities, which limits consider a counterparty's creditworthiness, the value of collateral and guarantees pledged, which can reduce the overall credit risk exposure, as well as the type and the duration of the asset. In order to examine a counterparty's creditworthiness, the following are considered: country risk, quantitative and qualitative characteristics, as well as the industry sector in which the counterparty operates.

2 **Financial risk management** *(continued)*

The Group has set limits of authority and has segregation of duties so as to maintain impartiality and independence during the approval process and control new and existing assets or credit facilities.

The Group manages, limits and controls concentrations of credit risk wherever they are identified in particular, to individual counterparties and groups, and to industries and countries. The Group structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. The exposure to any one borrower including banks and brokers is further restricted by sublimits covering on and off-balance sheet exposures. Actual exposures against limits are monitored at end of day on a daily basis and on a real-time basis too.

The financial years ended 31 December 2021 and 2020 have been characterised by unprecedented economic conditions as a result of the COVID-19 outbreak, which have impacted the Group's customers. In view of the nature and operations of the Bank, the impact was more pronounced at the level of the Bank’s customers in view of the direct impact on the respective business models, income levels and cash flow generation. Whereas economic growth has been registered during 2021 subsequent to the significant 2020 adverse impacts, economic uncertainty still prevails taking cognisance of the forecast conditions as at 31 December 2021.

In view of the above, the Bank has increased the depth of monitoring activities on its loan portfolios and continued to support its customers and to apply adapted credit risk operational processes accordingly. During the years ended 31 December 2021 and 2020, the Bank granted moratoria on capital and/or interest payments and originated new loans to provide relief to customers experiencing liquidity pressures as a result of the prevailing macroeconomic scenario.

From a risk perspective, the pandemic affected the Bank’s corporate book, which has a significant exposure to the local construction and real estate industry (“corporate”), and retail portfolios which typically comprise of the personal, professional and home loans (“retail”) (note 2.3.4.5). This has impacted the performance of the Bank’s expected credit loss models, requiring enhanced monitoring of model outputs and use of alternative mechanisms or controls. In view of the nature of the Bank’s portfolio, where a relatively small number of loans comprise a significant proportion of the loan book value, during the past two years, the Bank continued to apply an individual-debtor-focused credit management process. Such process enabled the identification of any deterioration in credit risk at the level of the Bank’s material exposures at an early stage and the estimation of expected credit loss allowances using the best possible judgement.

Subsequent to the outbreak of COVID-19, the Bank had adapted further its credit risk management processes for the purposes of identifying deterioration in credit risk within its portfolios as early as possible. In this respect, the Bank increased the frequency and depth of monitoring activities on its loan portfolios.

In relation to those customers that requested moratoria, the Bank carried out assessments to determine whether the immediate COVID-19 induced shock may transform into long-term financial difficulties, thereby potentially requiring a downgrade of individual exposures or exposures sharing similar credit risk characteristics to Stage 2 or Stage 3 to reflect the change in the level of credit risk as appropriate.

Sectorial reviews, in particular on exposures connected to the hospitality industry, which have been mostly impacted by the pandemic, are performed to identify customers or groups of customers who are experiencing, or are likely to experience, financial difficulty as a result of COVID-19. Such reviews continued to be monitored on a regular basis during 2021 in order to assess ongoing developments in respect of COVID-19, such as the emergence of new waves of infections or virus strains, the status and efficacy of vaccination programmes, together with the unwinding of government support schemes and regulatory relief measures.

Specifically, with respect to corporate exposures, during 2021, the Bank continued to assess and individually rate on an ongoing basis those borrowers deemed mostly impacted by the pandemic, including the ones which accepted payment deferrals and other relief designed to address short-term liquidity issues, especially those which have extended deferrals following the occurrence of the COVID-19 pandemic, through individual ad-hoc credit assessments on the basis of recently obtained management information including forecasts. Exposures deemed mostly impacted and in respect of which a SICR has been observed are assigned an elevated internal credit rating, requiring closer and more frequent monitoring on a monthly or quarterly basis (depending on the extent of credit risk deterioration).

During 2021, more information became available in respect of the impact of COVID-19 on specific borrowers and industry sectors, enabling management to assess in an enhanced manner borrower-specific credit risk levels and identify SICR or

2 **Financial risk management** *(continued)*

unlikeliness to pay 'UTP' events. The Bank continued to monitor closely corporate exposures previously assigned to any of the underperforming grades (P2, P3) (note 2.3.8) to update credit risk assessments by reference to actual financial performance and, where available, financial forecasts. Moreover, additional borrowers were attributed P2 and P3 internal ratings during 2021 as financial difficulties became more evident by reference to updated financial information.

In relation to retail exposures, the Bank typically resorts more to portfolio measures or reviews in respect of groups of exposures exhibiting shared risk characteristics, unless specific debtor level information which suggests developments in the respective credit risk becomes known to the Bank.

The unprecedented nature of the pandemic induced an elevated level of uncertainty in respect of economic outlook. Whilst economic consensus forecasts have stabilised in recent months and monthly modifications to forecasts have become narrower, the extent to which these forecasts accurately reflect the effects of new virus strains, the distribution and efficacy of vaccines (and vaccine boosters) and eventual business recovery remains uncertain.

The level of local macroeconomic uncertainty increased subsequent to the grey-listing of Malta by the Financial Action Task Force (FATF) in June 2021. The estimated economic impact of grey-listing remains uncertain since this is highly dependent on the speed at which Malta exits grey-listing, the effectiveness of national efforts to address the findings, and the response of foreign investors.

These factors necessitate more regular monitoring and rigorous evaluation of forecast economic conditions, together with heightened expert judgement, in order to best determine the range of possible economic outcomes used for the purposes of estimating ECL. Further information in respect of macroeconomic forecasts reflected within the ECL calculations is provided in note 2.3.4. (Forward looking information incorporated in the ECL model).

2.3.3 Credit risk measurement

The measurement of credit exposure for risk management purposes considers that an exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD). This is similar to the approach used for the purposes of measuring Expected Credit Loss (ECL) under IFRS 9. Refer to note 2.3.4 for more details.

(a) Loans and advances to customers

The Group uses internal credit risk gradings (note 2.3.8) to reflect its assessment of the Probability of Default of individual counterparties. Internal credit risk gradings are based on payment behaviour, loan specific information and expert judgement.

Corporate

Information considered by the Group when determining the internal credit risk grades include the payment behaviour of the borrower and other information about borrowers which impact their creditworthiness, including level of income and/or financial performance.

The Group determines its internal rating grades at a borrower level. The Group incorporates any updated or new information/credit assessments on an ongoing basis. In addition, the Group also updates information about the creditworthiness of the borrower from sources such as financial statements.

The creditworthiness of the borrower is considered in every periodic review - normally on a yearly basis; or more frequently on an exceptions basis. This determines the updated internal credit risk gradings.

Retail

After initial recognition, for retail business, the payment behaviour of the borrower is monitored on an ongoing basis. Any other known information about the borrower which impacts the respective credit worthiness, such as unemployment and previous delinquency history, is also captured.

2 **Financial risk management** *(continued)*

(b) Other financial assets

Other financial assets include Balances with Central Bank of Malta, investments and loans and advances to banks. The Group uses external risk grades to reflect its assessment of the Probability of Default of individual counterparties. These published grades are continuously monitored and updated. The PDs associated with each grade are determined based on realised default rates over the prior 12 months, as published by rating agencies.

In determining the Probability of Default of individual counterparties, the Group distinguishes between exposures considered ‘investment-grade’ and ‘non-investment grade’ based on credit ratings by recognised external rating agencies.

2.3.4 Expected Credit Loss measurement

IFRS 9 outlines a 'three-stage' model for impairment based on changes in credit quality since initial recognition as summarised below:

- a financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Group;
- if a significant increase in credit risk (SICR) since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. Please refer to note 2.3.4.1 for a description of how the Bank determines when a significant increase in credit risk has occurred;
- if the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Please refer to note 2.3.4.2 for a description of how the Group defines credit-impaired and default;
- financial instruments in ‘Stage 1’ have their ECL measured at an amount equal to the portion of lifetime Expected Credit Losses that result from default events possible within the next 12 months. Instruments in ‘Stages 2’ or ‘3’ have their ECL measured based on Expected Credit Losses on a lifetime basis. Please refer to note 2.3.4.3 for a description of inputs, assumptions and estimation techniques used in measuring the ECL;
- a pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward looking information. Note 2.3.4.4 includes an explanation of how the Group has incorporated this in its ECL models; and
- purchased or originated credit-impaired financial assets are those financial assets that are credit-impaired on initial recognition. Their ECL is always measured on a lifetime basis (‘Stage 3’).

Further explanation is also provided in respect of how the Group determines appropriate groupings of loans and advances to customers for ECL measurement (refer to note 2.3.4.5).

The Expected Credit Loss requirements apply to financial assets measured at amortised cost and FVOCI, and certain loan commitments and financial guarantee contracts. At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for ECL resulting from default events that are possible within the next 12 months (12-month ECL). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument (lifetime ECL). Financial assets where 12-month ECL is recognised are considered ‘Stage 1’. Financial assets which are considered to have experienced a significant increase in credit risk would be classified as ‘Stage 2’ and financial assets for which there is objective evidence of impairment, thus considered to be in default or otherwise credit-impaired, would be classified as ‘Stage 3’.

The Group recognises loss allowances at an amount equal to 12-month ECL for debt investment securities that are determined to have low credit risk at the reporting date. The Group considers a debt security to have low credit risk when it is considered ‘investment-grade’, as defined by recognised external rating agencies.

The following diagram summarises the impairment requirements under IFRS 9 (other than purchased or originated credit-impaired financial assets):

Stage 1	**Stage 2**	**Stage 3**
(Initial recognition)	(Significant increase in credit risk since initial recognition)	(Credit-impaired financial assets)
12-month Expected Credit Losses	Lifetime Expected Credit Losses	Lifetime Expected Credit Losses

2 **Financial risk management** *(continued)*

2.3.4.1 Significant increase in credit risk (SICR)

To determine whether the credit risk (i.e. risk of default) on a financial instrument has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information. Such analysis is based on the Group's historical experience, credit assessment and forward-looking information.

The Group primarily identifies whether a SICR has occurred for an exposure within the loans and advances to customers, through the Group's internal risk gradings. The Group allocates each exposure to an internal rating grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. These factors vary depending on the nature of the exposure and the type of borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different internal rating grade.

The Group identifies SICR and classifies such non-defaulted exposures into 'Stage 2' when they fulfil at least one of the following conditions:

- the exposure is considered forborne;
- the credit quality of any other exposure(s) of the same customer is/are not considered 'regular' (except where otherwise stated in the Group's Credit Policy e.g. cash covered facilities); and
- the borrower's internal rating grade is not considered 'performing', as defined in note 2.3.8.

As referred to previously, the COVID-19 pandemic and the consequential economic conditions have exacerbated the level of uncertainty, particularly with respect to the identification of customers that would have experienced a SICR. This is also attributable to limitations in credit information available on customers, particularly where these customers were granted a general payment moratorium.

The Bank's individual-debtor-focused approach enabled the identification of SICR at the level the significant exposures, specifically within its corporate portfolio. In respect of such individually significant loans the Bank assessed and individually rated those borrowers that during 2020 and 2021 requested payment deferrals/moratoria as well as those individually significant borrowers within specific industries which are deemed mostly impacted by the pandemic. These exposures were assessed periodically for SICR and UTP events through individual credit risk assessments, on the basis of recently obtained management information, including forecasts. Exposures in respect of which SICR has been observed were attributed higher ECL, and were assigned an elevated internal rating of P2 or P3, hence requiring closer and more frequent monitoring on a monthly or quarterly basis (depending on the extent of credit risk deterioration) to facilitate timely identification of further deterioration in financial condition. The assessments were performed by the Commercial Credit Department and were discussed and reviewed at Credit Committee or Board level as applicable.

For the purpose of achieving a comprehensive assessment the Bank also utilised segmentation techniques in relation to identifying indicators of SICR or unlikeness-to-pay (UTP) (note 2.3.4.2) within both corporate and retail portfolios.

In relation to retail portfolios, SICR is generally determined on the basis of delinquency related indicators since less information is available at asset level to enable the timely identification of a SICR. In this respect, a set of criteria were established to determine if borrowers which during 2020 and 2021 were granted a general payment moratorium (see note 2.3.9) exhibited signs of SICR or Unlikeliness-to-Pay (UTP). Such criteria include whether the COVID-19 pandemic negatively affects the level of income of the borrower to the extent that the repayment ability of the borrower is jeopardised and whether the economic sector in which the borrower is employed is severely affected. With respect to borrowers who have not requested a moratorium, the Bank continued to apply rigorously its credit assessment and oversight processes, which include monitoring of arrears. Retail borrowers were considered to exhibit signs of SICR and consequently downgraded to Stage 2 if they met the following criteria:

- repayments being past-due by more than 30 days; and
- other qualitative criteria, including but not limited to actual or potential loss of personal income.

During 2021, more information became available in respect of the impact of COVID-19 on specific borrowers and industry sectors, both in terms of actual financial performance and revised forecasts reflecting more accurate impacts of the pandemic when compared to prior year estimates. Credit risk assessments in respect of individually significant loans within the corporate portfolio were updated during the financial year ended 31 December 2021 based on updated financial information, enabling

2 **Financial risk management** *(continued)*

management to better identify SICR or UTP events and resulting in further migrations from stage 1 to 2, as per information presented in note 2.3.10. Such assessments also facilitated the process through which a number of exposures were cured from Stage 2 to 1 after the Bank ascertained that during 2021 the respective debtors did not experience the level of elevated risk which was anticipated in 2020.

In summary, the Bank's monitoring typically includes the assessment of following risk criteria:

Corporate exposures	**Retail exposures**	**All exposures**
- information obtained during periodic review of customer files – e.g. audited financial statements, management accounts, budgets and projections. Examples of areas of particular focus are: gross profit margins, financial leverage ratios, debt service coverage, compliance with contractual conditions, quality of management and senior management changes; - data from credit reference agencies, press articles; - actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities; andindustry of the borrower is significantly impacted by the COVID-19 pandemic.	- internally collected data on customer behaviour – e.g. utilisation of credit card facilities; - affordability metrics; - external data from credit reference agencies including industry-standard credit scores; and - employment of the borrower is significantly impacted by the COVID-19 pandemic.	- payment record – this includes overdue status as well as a range of variables about payment ratios; - utilization of the granted limit; - requests for and granting of forbearance; - existing and forecast changes in business, financial and economic conditions; and - request for a general payment moratorium (as a consequence of the COVID-19 pandemic).

The assessment of SICR incorporates forward-looking information (refer to note 2.3.4.4 for further information) and is performed at the counterparty level on a periodic basis. The criteria used to identify SICR are monitored and reviewed periodically for appropriateness by the independent Risk Management function.

As a backstop, and as required by IFRS 9, the Group presumptively considers that a SICR occurs when an asset is more than 30 days past due. The Group determines days past due by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received.

In the case of other financial assets (including loans and advances to banks and investments in debt securities), the Group applies the low credit risk simplification to all its exposures considered 'investment-grade', thus they are not subject to the SICR assessment. Moving from 'investment-grade' to 'non-investment grade' does not automatically mean that there has been a SICR.

2.3.4.2 Definition of default and credit-impaired assets

The Group's assessment to determine the extent of increase in credit risk of a financial instrument since initial recognition is performed by considering the change in the risk of default occurring over the remaining life of the financial instrument. As a result, the definition of default is important.

The Group applies the definition of default in a consistent manner with internal credit risk management practices for the relevant instruments and the definition considers qualitative and quantitative factors where appropriate.

The Group determines that a financial instrument is credit-impaired (in default and in 'Stage 3' for IFRS 9 purposes) by considering relevant objective evidence, primarily whether:

- contractual payments of either principal or interest are past due for more than 90 days for any material credit obligations to the Group;
- there are other indications that the borrower is unlikely to pay such as that a concession has been granted to the borrower for economic or legal reasons of an enduring nature relating to the borrower's financial condition, which indicates the borrower is in significant financial difficulty (unlikeliness to pay criteria); and
- the loan is otherwise considered to be in default. If unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure is 90 days past due.

2 **Financial risk management** *(continued)*

Therefore, the definitions of credit-impaired and default are aligned so that 'Stage 3' represents all loans which are considered defaulted or credit-impaired.

In assessing whether a borrower is in default, the Group will consider indicators that are:

- qualitative – such as non-adherence to terms and conditions of sanction and/or other breaches of covenants, overdue status and non-payment of another obligation of the same obligor to the Group;
- quantitative – such as changes in probabilities of default; and
- based on data developed internally and obtained from external sources.

The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD) throughout the Bank's expected loss calculations.

As referred to previously, the COVID-19 pandemic and the consequential economic conditions have exacerbated the level of uncertainty, particularly with respect to the identification of customers that would have showed signs of unlikeliness to pay ('UTP'). The Bank also performed assessments to determine whether the short-term economic shock as a result of the pandemic may transform into long-term borrower financial difficulties, thereby potentially requiring a downgrade of individual exposures or exposures sharing similar credit risk characteristics to Stage 3 to reflect the level of change in credit risk.

With respect to the retail portfolio, assessments covered individual exposures meeting certain criteria as reflected previously and were also carried out for groups of exposures sharing common risk characteristics. In relation to the corporate portfolio, the Bank's assessment is highly dependent on individual exposure reviews.

Except for forborne exposures, an instrument is considered to no longer be in default (i.e. to have been cured) when it no longer meets any of the default criteria for a consecutive period of three months. This period has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions.

In the case of forborne exposures, the cure period comprises 12 consecutive monthly repayments made in a timely manner with a minimal grace period of one day (i.e. one or more repayments may be made no more than one day late).

The Group considers other financial assets to be in default when a payment due including a coupon payment is not effected.

2.3.4.3 Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or on a lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected Credit Losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD). When calculating the Bank's ECL, special considerations were made to assess the impact of COVID-19 on ECL. Further details are set out in note 2.3.4.4.

The ECL is determined by projecting the PD, EAD and LGD for each future month and for each individual exposure. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

The 12-month ECL is calculated by multiplying the 12-month PD, LGD, and EAD. Lifetime ECL is calculated on a similar basis for the residual life of the exposure.

The PD, EAD and LGD parameters are derived from internally developed statistical models and other historical data, adjusted to reflect forward-looking information as described below.

The PD represents the likelihood of a borrower defaulting on its financial obligation (as per 'definition of default and credit-impaired' above), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation. Accordingly, the 12-month and lifetime PDs represent the Probability of Default occurring over the next 12 months and the remaining maturity of the instrument, respectively.

2 **Financial risk management** *(continued)*

PD estimates are estimates at a certain date, which, for the loans and advances to customers, are calculated based on statistical rating models and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally-compiled data comprising both quantitative and qualitative factors. The PD calculation is based on a transition matrix approach. The main assumptions underlying such approach is that the PD depends on the particular periods after origination ('months on book') and the current characteristics of the exposure or borrower. Default is considered to be an absorbing state, whereby if an exposure is defaulted, it remains in this state during all next years. Market data is used for the PD of loans and advances to banks and investment securities. If a counterparty or exposure migrates between internal rating grades or external credit ratings, then this will lead to a change in the associated PD.

The lifetime PD is developed by utilising statistical methodologies to analyse historical observed data to estimate the probability of a borrower's transition from one internal rating class to another (or of staying in the same class) within a given horizon. The conditional PD is adjusted to consider forward-looking information through macro-economic modelling.

EAD represents the expected exposure in the event of a default (including any expected drawdowns of committed facilities). The Group derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract. The EAD of a financial asset is the gross carrying amount at default.

EAD is based on the amounts the Group expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For example, for a revolving commitment, the Group includes the current drawn balance plus any further amount that is expected to be drawn up to the current contractual limit by the time of default, should it occur.

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type:

- for amortising products and bullet repayment loans, this is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis; and
- for revolving products, the Exposure at Default is predicted by taking current drawn balance and adding a 'credit conversion factor' which allows for the expected drawdown of the remaining limit by the time of default. These assumptions vary by product type and current limit utilisation band, based on analysis of the Group's recent default data.

The Loss Given Default (LGD) represents the Bank's expectation of the extent of loss on a defaulted exposure. Hence, the LGD represents Expected Credit Losses on the EAD given the event of default, taking into account, among other attributes, the mitigating effect of collateral values at the time it is expected to be realised and the time value of money. The 12-month and lifetime LGD are determined based on the factors which impact the recoveries made post default.

For secured products, LGD is primarily based on collateral type and projected collateral values, historical discounts to market/book values due to forced sales, time to repossession and recovery costs observed. The LGD for exposures secured by real estate will be derived from the adjusted loan-to-value ratio of the individual facilities, and takes into account the expected recovery by applying a costs to sell haircut and a market value haircut to the property value, and by discounting (using the effective interest rate) the updated market value of the property after haircuts, over a period of time equivalent to the perceived time to sell. The LGD for other exposures is based on the Group's perceived risk on the collateral. For unsecured products, LGDs are typically set at product level due to the limited differentiation recoveries achieved across different borrowers. These LGDs are influenced by collective strategies.

The ECL is measured from the initial recognition of the financial asset. The maximum period considered when measuring ECL (be it 12-month or lifetime ECL) is the maximum contractual period over which the Group is exposed to credit risk. With respect to non-revolving credit facilities, the contractual life of the facility is considered. In the case of revolving credit facilities, provided that such facilities do not have a fixed term or repayment structure, the Group defines the lifetime of such exposures as 12 months, in case the next substantive credit review is within the next 12 months. For the credit cards portfolio, the Group also applies a lifetime of 12 months.

Forward-looking economic information is also included in determining the 12-month and lifetime PD and LGD. Refer to note 2.3.4.4 for an explanation of forward-looking information and its inclusion in ECL calculations.

The assumptions underlying the ECL calculations are monitored and reviewed on a regular basis. In fact, the Bank estimates the impact of the COVID-19 pandemic on its ECL by utilising segmentation techniques for the purposes of identifying indicators of SICR within both retail and corporate portfolios. As explained in note 2.3.4.1, during 2020 management has adopted a prudent approach by downgrading a number of retail and corporate customers to Stage 2.

2 **Financial risk management** *(continued)*

For individually significant credit impaired loans, management determines the size of the allowance required based on a range of factors such as the realisable value of security, the viability of the customer's business model and the capacity to generate cash flow to service debt obligations, under different scenarios. Judgement is applied in estimating the expected future cash flows from each borrower and the time to recover these cash flows under the different scenarios as well as to attach probabilities to those scenarios. The assumptions around forecasted recoveries from the sale of collateralised properties, including around valuation haircuts and time to recovery, are key drivers in the estimation of credit loss allowances in respect of individually assessed loans. The heightened level of uncertainty within the local property market, driven by the pandemic, increases the level of expert judgement required to predict with reasonable accuracy the recoverability of exposures through the sale of collateral, since the real impact of the pandemic will not be fully known until market conditions stabilise. To reflect the volatile economic conditions associated with the COVID-19 pandemic, judgemental overlay were applied by management in order to overcome limitations in respect of determining collateral valuations, and the uncertainty around the time to repossess properties held as collateral and to resell such properties in the open market.

2.3.4.4 Forward-looking information incorporated in the ECL model

The calculation of ECL incorporates forward-looking information. The Group performs a historical analysis to identify the key economic variables affecting credit risk and Expected Credit Losses for each portfolio. These economic variables and their associated impact on the PD, EAD and LGD may vary by portfolio.

In this respect, the Group has identified key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has analysed relationships between macro-economic variables, credit risk and credit losses. The key driver is predominantly Gross Domestic Product (GDP) at constant prices.

The impact of this economic variable on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

Three possible scenarios are considered to capture non-linearity across credit portfolios. The 'base line' scenario represents the most-likely outcome. It is based on authoritative sources forecasting these economic variables referred to above and providing the best estimate view of the economy. Apart from the 'base line' scenario, the Group considers two other macro-economic scenarios – Upside and Downside scenarios – which respectively represent a more optimistic and a more pessimistic outcome. Such scenarios reflect the current top and emergent risks and opportunities. The more optimistic and more pessimistic scenarios are economically plausible, and the more pessimistic scenario will not necessarily be as severe as scenarios used in stress testing.

Modelling of the economic scenarios, i.e the forecast values of GDP growth for optimistic and pessimistic scenario, is performed on the basis of the historical values of annual GDP growth and annual forecast values for base scenario, based on the published three-year forecast of the Central Bank of Malta.

The pessimistic and optimistic scenarios represent a sensitivity to the base scenario, and are deemed to represent management's best forecast of an economically plausible upside and downside scenario.

Each scenario is weighted by a probability of occurrence, determined by a combination of macro-economic research and expert credit judgment, taking account the range of possible outcomes each chosen scenario represents. The Group measures ECL as either a probability weighted 12-month ECL (Stage 1), or a probability weighted lifetime ECL (Stages 2 and 3). These probability-weighted ECLs are determined by running each scenario through the relevant ECL model and multiplying the outcome by the appropriate scenario weighting (as opposed to weighting the inputs).

As with any macro-economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of uncertainty and therefore, the actual outcomes may be significantly different to those projected.

The COVID-19 outbreak dominated the political and economic landscape through the financial years ended 31 December 2020 and 2021. The twin shocks of a public health emergency and the resultant economic fallout have been felt around the world during 2020. The sharp contraction in economic activity experienced in both global and local economies has had varying effects on different industry sectors, with borrowers operating or employed within such industry sectors experiencing financial difficulties. Measures designed to soften the extent of the damage to economic activity and the labour market were implemented by the Maltese government, as well as European and local regulatory authorities. Such measures included income support to households, funding support to businesses (including through government guaranteed schemes), as well as the granting of general public moratoria on capital and/or interest repayments in response to the outbreak of the pandemic.

2 **Financial risk management** *(continued)*

The current financial year was characterised by strong economic growth after a complicated winter, as the global and local economies bounced back, particularly in spring and summer, resulting in abnormally high growth rates principally due to a spending spree unfolding as facilitated by successful vaccination campaigns. The strong growth rates during 2021 reflect the dynamics throughout the year, but also the low base value in 2020 due to the economic downturn. This growth is set to significantly slow down as the pandemic situation worsens throughout winter, alongside ongoing supply-chain issues. The autumn wave of infections towards the end of the year was stronger than expected, resulting in stricter government measures. The base assumption is that these measures remain focused on the unvaccinated, as current vaccines are expected to provide a degree of efficacy against the Omicron variant, thus avoiding the need for prolonged, full-scale lockdowns in the euro zone. The rise in infections is being tackled by governments using measures that aim to boost vaccination rates and some level of imposed social distancing rolled out across countries, which will affect economic activity. However, it is forecasted that the effect of the pandemic on aggregate activity will be more contained than in previous outbreaks. The unwinding of government support schemes and regulatory relief measures introduced as a response to the outbreak of COVID-19 also commenced during the current financial year, taking cognisance of the economic developments.

Uncertainty remains with respect to the potential economic impacts of epidemiological assumptions in relation to the pandemic as different regions emerge from the pandemic at different speeds, the progress registered from continued roll-outs of vaccination programmes, the efficacy of such vaccines/boosters upon the emergence of new virus strains, further restrictions imposed at national level by various governments as events unfold, and the unwinding of government support schemes and regulatory relief measures.

The main downside and upside risks to the baseline are still centred on developments surrounding the coronavirus pandemic. Although the baseline outlook foresees the economy weathering the winter outbreak, the pandemic might linger or consumer behaviour may remain cautious, preventing economic activity from fully rebounding to normal levels.

The significant changes in economic and market drivers, customer behaviours and government actions caused by COVID-19 have also impacted the performance of ECL models, since the severity of projections of macroeconomic variables being forecasted in response to the pandemic are outside the historical observations on which the ECL models have been built and calibrated. In this regard, a significant judgement within the Bank's estimation of ECL impairment allowances as at 31 December 2020 and 2021 relates to the determination of forward-looking scenarios reflecting potential future economic conditions under different scenarios and their impact on PDs and LGDs.

The most significant period-end assumptions used for the ECL estimate as at 31 December 2021 and 2020 are set out below. The 'base', 'upside' and 'downside' scenarios were used for all portfolios:

- The 'Base' Scenario captures business-as-usual macro-economic expectations, whereby the current rhythm of economic activity is maintained;
- The 'Downside' Scenario is based on a subdued level of economic activity hypothesized to correspond to prolonged period of an economic contraction;
- The 'Upside' Scenario is based on the assumption that it would be possible to marginally improve further over the already benign economic conditions considered in the 'Base' Scenario.

		As of 31 December 2021	
	2022	**2023**	**2024**
Gross Domestic Product, constant prices (YoY)*			
'Base'	6.50%	5.30%	3.80%
Range of forecasts for alternative scenarios	[4.0 - 9.0]%	[2.8 - 7.8]%	[1.3 - 6.3]%

*YoY = year on year % change

		As of 31 December 2020	
	2021	**2022**	**2023**
Gross Domestic Product, constant prices (YoY)*			
'Base'	5.00%	5.50%	4.70%
Range of forecasts for alternative scenarios	[2.4 - 7.6]%	[2.9 - 8.1]%	[2.1 - 7.3]%

*YoY = year on year % change

2 **Financial risk management** *(continued)*

The weightings assigned to each economic scenario were 64% for the 'Base' Scenario, 18% for the 'Downside' scenario and 18% for the 'Upside' scenario. The number of scenarios used is based on the analysis of each major product type to ensure that non-linearities are captured. The number of scenarios and their attributes are reassessed at each reporting date. The economic scenarios were simulated over a full economic cycle.

The Bank considers the macroeconomic forecasts to represent its best estimate of the possible outcomes after analysing its different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible scenarios.

The Bank's weightings take into account the current performance of the Maltese economy over the foreseeable future and the anticipated recoveries as described above. The Board considers that the probability weightings assigned to the respective scenarios reflect an unbiased evaluation of range of possible outcomes.

As highlighted previously, the impact of the pandemic on the duration and severity of the economic impacts remains uncertain, especially in light of potential subsequent waves of infection or new virus strains, the effectiveness of vaccinations in slowing and eventually reversing the spread of new virus strains, as well as the unwinding of government support schemes and local political decisions. The economic outlook has been further exacerbated in March 2022 following the commencement of war in eastern Europe, which is deemed to be a non-adjustable subsequent event for financial reporting purposes. Such turmoil is anticipated to put further disruption on supply chain and create additional inflationary pressures world-wide.

Based on the above, the estimation of credit loss allowances as of 31 December 2020 and 2021 required an elevated level of subjectivity and expert judgement. Despite the recovery in economic conditions during 2021, principally driven by the effective implementation of vaccination programmes addressing the mutation of COVID-19 variants, ECL estimates remain subject to a high degree of uncertainty. In this respect, judgements applied by management in estimating ECL continue to reflect a degree of caution, both in the determination of probability of defaults, particularly for exposures currently classified as performing, for selection of economic scenarios and in terms of the calibration of scenario weightings.

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative, or political changes, have also been considered, but are not deemed to have a material impact and therefore no adjustment has been made to the ECL for such factors. This is reviewed and monitored for appropriateness on an ongoing basis.

The outcome of the Bank's credit loss allowances estimation process is sensitive to judgements and estimations made through the reflection of several forward-looking economic conditions. Management has assessed the sensitivity of the Bank's expected credit losses by assigning a 100% weighting to the baseline, downside and upside scenarios respectively. The Bank's credit loss allowances would decrease by €17.1 million if the provisions has to be calculated solely on the baseline scenario; ECLs would increase by €7.6 million if these had to be estimated using only the downside scenario and would reduce by €17.4 million if the upside scenario only were to be taken into consideration. This demonstrates the Bank's resilience in overcoming negative shocks and its ability to absorb such allowance changes, if necessary.

2.3.4.5 Categorisation of loans and advances to customers for ECL measurement

As part of the ECL model, the Group classifies its exposures to loans and advances to customers into homogeneous groups with similar credit risk characteristics that include instrument type and credit risk gradings. In this respect, the Group considers the following categories for ECL measurement:

- retail portfolio, which includes loans and advances to individual customers such as mortgages, credit cards and other consumer credit;
- construction and real estate portfolio, which includes loans and advances to customers in respect of financing construction of real estate projects for the purpose of re-sale or rental; and
- corporate portfolio, which includes loans and advances to business entities, other than construction and real estate related borrowers.

2.3.5 Maximum exposure to credit risk

An 'exposure' is defined as the amount at risk arising from the Group's assets and off-balance sheet items. The Group's maximum credit risk with respect to on- and off-balance sheet items can be classified into the following categories:

2 **Financial risk management** *(continued)*

- Financial assets recognised on-balance sheet comprising principally balances with Central Bank of Malta, financial investments and loans and advances to banks and customers. The maximum exposure to credit risk of these financial assets equals their gross carrying amounts.
- Documentary credits and guarantee obligations incurred on behalf of third parties. The latter carry the same credit risk as loans, whilst documentary credits are collateralised by the underlying shipments of goods to which they relate, and therefore carry less risk than a loan to a customer. The maximum exposure to credit risk is the full amount that the Group would have to pay if the guarantees are called upon or if documentary credits are exercised.
- Loan commitments and other credit related commitments that are irrevocable over the life of the respective facilities. The maximum exposure to credit risk is the full amount of the committed facilities. However, the likely amount of loss is less than the total unused commitments as most commitments to extend credit are contingent upon customers maintaining specific credit standards. These exposures are monitored in the same manner in respect of loans and advances.

The Group's credit risk exposures relating to on-balance sheet assets and off-balance sheet instruments, reflecting the maximum exposure to credit risk before collateral held or other credit enhancements, include the following:

	Group				**Bank**			
	2021		2020		**2021**		2020	
	Gross exposure € 000	**ECL allowance € 000**	Gross exposure € 000	ECL allowance € 000	**Gross exposure € 000**	**ECL allowance € 000**	Gross exposure € 000	ECL allowance € 000
Credit risk exposures relating to on-balance sheet assets:								
Subject to IFRS 9 impairment allowance								
Financial assets measured at mortised cost:								
Balances with Central Bank of Malta	**71,805**	**-**	68,417	-	**71,805**	**-**	68,417	-
Cheques in course of collection	**530**	**-**	666	-	**530**	**-**	666	-
Loans and advances to banks	**78,279**	**-**	96,985	-	**68,424**	**-**	93,641	-
Financial investments measured at FVOCI	**275,091**	**(465)**	255,080	(808)	**272,190**	**(465)**	251,518	(808)
Loans and advances to customers	**668,515**	**(25,622)**	647,043	(25,914)	**668,517**	**(25,622)**	647,046	(25,914)
Trade and other receivables	**10,787**	**-**	9,136	-	**1,605**	**-**	1,761	-
Accrued income and other assets	**2,999**	**-**	3,283	-	**2,965**	**-**	3,243	-
Credit risk exposure	**1,108,006**	**(26,087)**	1,080,610	(26,722)	**1,086,036**	**(26,087)**	1,066,292	(26,722)
Credit risk exposures relating to off-balance sheet instruments:								
Contingent liabilities	**13,195**	**(24)**	10,851	(61)	**13,360**	**(24)**	10,983	(62)
Undrawn commitments to lend	**195,264**	**(45)**	197,180	(226)	**196,372**	**(45)**	198,288	(226)
Credit risk exposure	**208,459**	**(69)**	208,031	(287)	**209,732**	**(69)**	209,271	(288)

2 **Financial risk management** *(continued)*

Accrued income substantially arises from loans and advances to customers. Expected Credit Losses in respect of accrued income have been allocated to loans and advances to customers.

2.3.6 Credit concentration risk

Within the Bank, concentration risk of losses results from inadequate diversification of the credit exposures. This risk is managed by actively measuring, reporting and monitoring on a regular and ongoing basis risk concentration levels against reasonable thresholds for industry sectors, counterparties, products, and collateral types.

Credit concentration risk by industry sector

The Bank's financial investments measured at FVOCI (gross of Expected Credit Losses) are composed of local government debt securities and treasury bills, and other debt and equity instruments as shown in the following table:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Government	**221,008**	201,812	**219,345**	199,732
Corporate				
Tourism	**506**	769	**461**	454
Property and construction	**6,049**	6,351	**5,435**	5,753
Financial institutions	**39,681**	39,885	**39,102**	39,317
Other sectors	**7,847**	6,263	**7,847**	6,262
Gross financial investments	**275,091**	255,080	**272,190**	251,518

The industry sector analysis of the Bank's loans and advances to customers (gross of Expected Credit Losses) is described in the following table:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Manufacturing	**9,895**	10,297	**9,895**	10,297
Tourism	**59,430**	47,452	**59,430**	47,452
Trade	**38,147**	49,813	**38,147**	49,813
Property and construction	**236,693**	251,989	**236,693**	251,989
Personal, professional and home loans	**162,282**	128,781	**162,282**	128,781
Financial institutions	**140,253**	132,645	**140,253**	132,645
Other sectors	**21,815**	26,066	**21,817**	26,069
Gross advances to customers	**668,515**	647,043	**668,517**	647,046

Credit concentration risk for counterparties

The majority of the Bank's loans and advances to customers comprise exposures to corporates.

As at 31 December 2021 and 2020, no loans and advances to customers were deemed to be prohibited large exposures, prior to any eligible exemptions, in accordance with the requirements of Part Four: Large Exposures, of the CRR. A limited number of customers account for a certain percentage of the Bank's loans and advances. Whilst no individual customer or group of dependent customers is considered by management as a significant concentration of credit risk in the context of the CRR, these exposures are monitored and reported more frequently and rigorously.

2 **Financial risk management** *(continued)*

Credit concentration risk by geographical region

The Group also monitors credit concentration risk by geographical region. The majority of the Group's exposures are in Malta in view of the Group's lending operations being conducted with Maltese corporate entities. Moreover, the significant part of the Group investments in debt securities are all issued by local government and local corporate entities.

The Group's balances with correspondent banks in different jurisdictions are split by geographical region, as shown in the following table:

	Group		**Bank**	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Loans and advances to banks				
Germany	**16,998**	16,290	**16,998**	16,290
United Kingdom	**12,001**	8,095	**12,001**	8,095
France	**-**	15,888	**-**	15,888
Norway	**1**	1	**1**	1
Spain	**7,614**	13,494	**7,614**	13,494
Belgium	**7,630**	8,171	**7,630**	8,171
Denmark	**-**	3,340	**-**	3,340
Malta	**9,859**	3,346	**4**	2
Switzerland	**13,443**	11,018	**13,443**	11,018
Ireland	**8,830**	-	**8,830**	-
Other	**1,903**	17,342	**1,903**	17,342
Gross loans and advances to banks	**78,279**	96,985	**68,424**	93,641

2.3.7 Information on credit quality of balances with banks, investments and treasury bills

The Group holds debt instruments that are issued by local government, local banks and other local corporate entities. All such securities are listed on the Malta Stock Exchange, which is currently the only locally-based Recognised Investment Exchange (RIE). The other debt securities held by the Group, issued by foreign entities, are listed on other recognised exchanges. The Bank acquires debt securities and similar instruments issued by counterparties having strong financial background. These issuers are approved and regularly reviewed considering the process previously highlighted, focusing on market developments.

Within its daily operations the Bank transacts with banks and other financial institutions. The Bank primarily places short-term funds with pre-approved banks subject to limits in place and subject to the respective institution's credit rating being within controlled parameters. By conducting these transactions the Bank is running the risk of losing funds due to the possible delays in the repayment to the Bank of the existing and future obligations of the counterparty banks. Actual exposures are monitored against the limits on a daily basis and in a real-time manner. The credit status of the pre-authorised banks is monitored on an ongoing basis. At 31 December 2021, loans and advances to banks consisted primarily of term placements maturing within one month.

The Bank runs the risk of loss of funds due to the possible political, economic and other events in a particular country where funds have been placed or invested with several counterparties. Countries are assessed according to their size, economic data and prospects and their credit ratings from international rating agencies. Existing country credit risk exposures are monitored and reviewed periodically. The Bank's assets are predominantly in Malta. The Bank's exposures to other countries are mainly limited to bank balances and money market placements with a total carrying amount of €68,420,000 (2020: €93,639,000) at the end of the reporting period.

At the end of the reporting period, none of these financial assets mentioned were past due or impaired.

The following tables set out information about the credit quality of financial assets of the Bank measured at amortised cost and financial investments at FVOCI. The credit quality of financial assets is based on external credit ratings assigned to issuers or

2 **Financial risk management** *(continued)*

counterparties by recognised external rating agencies:

	2021			
	Stage 1 12-month ECL	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Balances with Central Bank of Malta at amortised cost				
Gross carrying amount	**71,805**	**-**	**-**	**71,805**
Loss allowance	**-**	**-**	**-**	**-**
Carrying amount – net of loss allowance	**71,805**	**-**	**-**	**71,805**

	2020			
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€ 000	€ 000	€ 000	€ 000
Balances with Central Bank of Malta at amortised cost				
Gross carrying amount	68,417	-	-	68,417
Loss allowance	-	-	-	-
Carrying amount – net of loss allowance	68,417	-	-	68,417

2 **Financial risk management** *(continued)*

The credit rating of the Government of Malta as at 31 December 2021 and 2020 was considered as 'investment grade' and hence no loss allowance in respect of balances with the Central Bank of Malta were recognised.

	2021			
	Stage 1 12-month ECL	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Financial investments at FVOCI				
AAA to AA-	**12,228**	-	-	**12,228**
A+ to A-	**220,191**	-	-	**220,191**
BBB+ to BBB-	**22,487**	-	-	**22,487**
Unrated	**17,284**	-	-	**17,284**
Carrying amount – fair value	**272,190**	-	-	**272,190**
Loss allowance	**(465)**	-	-	**(465)**
Carrying amount – net of loss allowance	**271,725**	-	-	**271,725**
Loans and advances to banks at amortised cost				
AAA to AA-	**807**	-	-	**807**
A+ to A-	**55,975**	-	-	**55,975**
BBB+ to BBB-	**11,636**	-	-	**11,636**
Lower than BB-	**2**	-	-	**2**
Unrated	**4**	-	-	**4**
Carrying amount	**68,424**	-	-	**68,424**
Loss allowance	-	-	-	-
Carrying amount – net of loss allowance	**68,424**	-	-	**68,424**

	2020			
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€ 000	€ 000	€ 000	€ 000
Financial investments at FVOCI				
AAA to AA-	10,291	-	-	10,291
A+ to A-	202,073	-	-	202,073
BBB+ to BBB-	22,746	-	-	22,746
Unrated	16,408	-	-	16,408
Carrying amount – fair value	251,518	-	-	251,518
Loss allowance	(808)	-	-	(808)
Carrying amount – net of loss allowance	250,710	-	-	250,710

2 **Financial risk management** *(continued)*

	2020			
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€ 000	€ 000	€ 000	€ 000
Loans and advances to banks at amortised cost				
AAA to AA-	775	-	-	775
A+ to A-	78,710	-	-	78,710
BBB+ to BBB-	14,151			14,151
BB+ to BB-	2	-	-	2
Unrated	3	-	-	3
Carrying amount	93,641	-	-	93,641
Loss allowance	-	-	-	-
Carrying amount – net of loss allowance	93,641	-	-	93,641

As at 31 December 2021 and 2020, there were no purchased credit-impaired assets.

After the end of the reporting period there were no significant changes in credit ratings reflected in the tables above which have a material impact on the credit quality of the financial assets.

2.3.8 Information on credit quality of loans and advances to customers

The Bank manages the credit quality of its loans and advances to customers by using internal risk grades, which provide a progressively increasing risk profile ranging from 'P1' (best quality, less risky) to 'NP'. These risk grades are an essential tool for the Bank to identify both non-performing exposures and better-performing customers. The internal risk grades used by the Bank are as follows:

- Performing: Internal grade 'P1'
- Under performing: Internal grades 'P2', 'P3' and 'PF'; and
- Non-performing: Internal grade 'NP'.

P1

The Bank's loans and advances to customers which are categorised as 'P1' are principally debts in respect of which the payment of interest and/or capital is not overdue by 30 days and no recent history of customer default exists. Management does not expect any losses from non-performance by these customers.

P2

Loans and advances which attract a 'P2' grading are those which are receiving the close attention of the Bank's management and are being reviewed periodically in order to determine whether such advances should be reclassified to either the 'P1' or the 'P3' classification. Credit facilities that attract this category include those where the payment of interest and/or capital becomes overdue by 30 days and over but not exceeding 60 days.

P3

Loans and advances which attract a 'P3' grading are those having the weaknesses inherent in those loans and advances classified as 'P2' with the added characteristics that repayment is inadequately protected by the current sound worth and paying capacity of the borrower. Loans and advances so graded have a well-defined weakness or weaknesses that could jeopardise the repayment of the debt. They are characterised by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Credit facilities that attract this category include those where the payment of interest and/or capital becomes overdue by 60 days and over but not exceeding 90 days.

2 **Financial risk management** *(continued)*

PF

Loans and advances which attract a 'PF' grading are those facilities (other than Non-Performing Exposures) in respect of which forbearance measures have been extended. Forbearance measures consist of concessions towards a debtor facing or about to face difficulties in meeting its financial commitments (financial difficulties).

A concession is deemed to have taken place when any of the following two actions are taken;

(a) a modification of the previous terms and conditions of a contract, as the debtor is considered unable to comply therewith, due to its financial difficulties ('troubled debt') to allow for sufficient debt service ability, that would not have been granted had the debtor not been in financial difficulties; and/or
(b) a total or partial refinancing of a troubled debt contract, that would not have been granted had the debtor not been in financial difficulties.

NP

Loans and advances which attract a 'NP' grading are those facilities where the Bank deems the recoverability of principal to be remote as a result of worsening conditions of loans and advances classified as 'P3'. Credit facilities that attract this category include those where the payment of interest and/or capital becomes overdue by 90 days and over. Accordingly, these loans and advances are generally past due by more than 90 days and comprise those exposures which are deemed by the Bank as credit-impaired (see definition in note 2.3.4.2).

The following table sets out information about the credit quality of financial assets measured at amortised cost. Explanation of the terms: 12-month ECL, lifetime ECL and credit-impaired are included in note 2.3.4.3.

	2021			
	Stage 1 12-month ECL	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Loans and advances to customers at amortised cost				
P1	**504,477**	**4,330**	**-**	**508,807**
P2	**-**	**34,065**	**-**	**34,065**
P3	**-**	**24,285**	**-**	**24,285**
PF	**-**	**49,603**	**-**	**49,603**
NP	**-**	**-**	**51,757**	**51,757**
Gross carrying amount	**504,477**	**112,283**	**51,757**	**668,517**
Loss allowance	**(5,187)**	**(3,361)**	**(17,074)**	**(25,622)**
Carrying amount	**499,290**	**108,922**	**34,683**	**642,895**

2 **Financial risk management** *(continued)*

	2020			
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€ 000	€ 000	€ 000	€ 000
Loans and advances to customers at amortised cost				
P1	522,923	-	-	522,923
P2	-	33,294	-	33,294
P3	-	6,493	-	6,493
PF		17,853		17,853
NP	-	-	66,483	66,483
Gross carrying amount	522,923	57,640	66,483	647,046
Loss allowance	(6,200)	(2,799)	(16,915)	(25,914)
Carrying amount	516,723	54,841	49,568	621,132

As at 31 December 2021, undrawn commitments to lend amounted to €196,372,000 (2020: €198,288,000) and predominantly comprise of sanctioned but not yet drawn facilities which are classified as 'Stage 1' (12-month ECL) upon drawdown by customers. Undrawn facilities in respect of existing 'Stage 2' and 'Stage 3' (Lifetime ECL) facilities as at 31 December 2021 have not been considered significant. ECL allowances on undrawn commitments specifically connected to revolving credit facilities to lend as at 31 December 2021 amounted to €45,000 (2020: €226,000).

Contingent liabilities and financial guarantee contracts as at 31 December 2021 amounting to €13,360,000 (2020: €10,983,000) are all classified as 'Stage 1' (12-month ECL) by the Bank. ECL allowances on contingent liabilities and financial guarantee contracts as at 31 December 2021 amounted to €24,000 (2020: €62,000).

As at 31 December 2021 and 2020, there are no purchased credit-impaired assets.

The following table analyses the impaired loans and advances, gross of impairment allowances, by industry sector:

	2021	2020
	€ 000	€ 000
Manufacturing	**446**	456
Tourism	**2,483**	2,481
Trade	**3,923**	4,672
Property and construction	**35,785**	48,554
Personal, professional and home loans	**3,185**	4,238
Financial institutions	**5,173**	1,929
Other sectors	**762**	4,153
Gross impaired advances to customers	**51,757**	66,483

2 **Financial risk management** *(continued)*

The following table provides a detailed analysis of the credit quality of the Bank's lending portfolio as at 31 December 2021:

	Non-forborne exposures 2021 € 000	Forborne exposures 2021 € 000	Total 2021 € 000
Performing - Stage 1			
Loans which are not past due	**500,928**	-	**500,928**
Loans which are past due by less than 30 days	**3,549**	-	**3,549**
	504,477	-	**504,477**
Performing - Stage 2			
Loans which are not past due			
P1	**4,317**	-	**2,417**
P2	**33,134**	-	**33,134**
P3	**23,795**	-	**23,795**
PF	-	**49,603**	**49,603**
Loans which are past due by less than 90 days			
Past due between 1 and 30 days	**1,380**	-	**1,380**
Past due between 31 and 89 days	**54**	-	**54**
	62,680	**49,603**	**112,283**
Non-performing - Stage 3			
Past due loans by 90 days or more and credit-impaired loans	**40,501**	**11,256**	**51,757**
Gross loans and advances	**607,658**	**60,859**	**668,517**
12-month ECL	**(5,187)**	-	**(5,187)**
Lifetime ECL	**(17,359)**	**(3,076)**	**(20,435)**
Net loans and advances	**585,112**	**57,783**	**642,895**

Interest income recognised during the financial year ended 31 December 2021 in respect of forborne exposures amounted to €2,658,000.

The following table provides a detailed analysis of the credit quality of the Bank's lending portfolio as at 31 December 2020:

2 **Financial risk management** *(continued)*

	Non-forborne exposures 2020 € 000	Forborne exposures 2020 € 000	Total 2020 € 000
Performing - Stage 1			
Loans which are not past due	513,333	-	513,333
Loans which are past due by less than 30 days	9,590	-	9,590
	522,923	-	522,923
Performing - Stage 2			
Loans which are not past due			
P2	31,505	-	31,505
P3	6,202	-	6,202
PF	-	17,853	17,853
Loans which are past due by less than 90 days			
Past due between 1 and 30 days	1,742	-	1,742
Past due between 31 and 89 days	338	-	338
	39,787	17,853	57,640
Non-performing - Stage 3			
Past due loans by 90 days or more and credit-impaired loans	53,173	13,310	66,483
Gross loans and advances	615,883	31,163	647,046
12-month ECL	(6,200)	-	(6,200)
Lifetime ECL	(15,838)	(3,876)	(19,714)
Net loans and advances	593,845	27,287	621,132

Interest income recognised during the financial year ended 31 December 2020 in respect of forborne exposures amounted to €1,994,000.

2.3.9 Modification of financial assets

The contractual terms of a loan may be revised for a number of reasons, including changes in market conditions, customer retention and other factors that are not related to the credit quality of a customer. Forbearance measures comprise concessions made on the contractual terms of a loan in response to a customer's financial difficulties. The Group categorises loans on which concessions have been granted under conditions of financial difficulties as 'forborne loans' when their contractual payment terms have been revised, because of significant concerns about the customer's ability to meet contractual payments when due.

When considering whether there is significant concern regarding a customer's ability to meet contractual loan repayments when due, the Group assesses the customer's delinquency status, account behaviour, repayment history, current financial situation and continued ability to repay.

If the customer is not meeting contractual repayments or it is evident that the client will be unable to do so without the renegotiation, there will be a significant concern regarding the ability to meet contractual payments. Indicators of significant concerns regarding a borrower's ability to pay include:

- the customer is currently in default on any of its debt;
- the customer has declared or is in the process of declaring bankruptcy or entering into a similar process;
- there is significant doubt as to whether the customer will continue to be a going concern; and
- the Group forecasts that the customer's entity-specific cash flows will be insufficient to service the debt (both interest and principal) in accordance with the contractual terms of the existing agreement through maturity.

2 Financial risk management *(continued)*

A range of forbearance measures are employed by the Group in order to improve the management of customer relationships, maximise collection opportunities and, if possible, avoid default or call-in of facilities. They include extended payment terms, a reduction in principal repayments, the deferral of call-in of facilities and other forms of loan modifications. The Group's policies and procedures in this area allow the Group to provide a customer with terms and conditions that are more favourable than those provided initially. Loan forbearance is only granted in situations where the customer has shown a willingness to repay the loan and is expected to be able to meet the revised obligations. The Group's credit risk management policies set out restrictions on the number and frequency of forbearance measures and the minimum period an account must have been opened before any forbearance measure can be considered.

For the purposes of determining whether changes to a customer's agreement should be treated as forbearance the following types of modification could be regarded as concessionary in cases where the customer is in financial difficulty:

- reduction of the stated interest rate for the remaining original life of the debt;
- extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk;
- reduction of the face amount or maturity amount of the debt; and
- reduction of accrued interest.

Term extension is the most common type of modification granted by the Group. Other types of concession, namely transfer to an interest-only arrangement or interest rate changes, occur less often.

In assessing whether forbearance is a sustainable strategy, the customer's entire exposures are reviewed and the customer's ability to meet the terms in relation to the revised obligations and other unchanged credit facilities is considered. In all cases, forbearance is only granted when the customer is expected to be able to meet the revised terms. When considering acceptable modified terms the Group considers the ability of the customer to be able to service the revised interest payments as a necessity. When principal payment modifications are utilised, the Group requires the customer to be able to comply with the revised terms as a necessary pre-condition for the restructuring to proceed.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk.

The risk of default of modified assets is assessed at the reporting date and compared with the risk under the original terms at initial recognition, when the modification is not substantial it does not result in derecognition of the original asset (refer to notes 1.7.4).

The Group monitors the subsequent performance of modified assets and may determine that the credit risk has significantly improved after restructuring:

- modified assets are moved from 'Stage 3' (Lifetime ECL) to 'Stage 1' (12-month ECL) only if they have performed in accordance with the new terms for 36 consecutive months or more; and
- modified assets are moved from 'Stage 2' (Lifetime ECL) to 'Stage 1' (12-month ECL) only if they have performed in accordance with the new terms for 24 consecutive months or more.

The gross carrying amount of such assets held as at 31 December 2021 amounted to €8,151,000 (2020: €11,465,000).

The Group continues to monitor if there is a subsequent significant increase in credit risk in relation to modified assets that moved from Stage 3 (Lifetime ECL) or 'Stage 2' (Lifetime ECL) to 'Stage 1'.

During the financial year ended 31 December 2020, a number of government support schemes and regulatory relief measures were announced in response to the outbreak of the COVID-19 pandemic, one of which being the granting of moratoria on capital and/or interest payments to provide relief to individual and corporate customers during the ensuing macroeconomic recession triggered by the pandemic. In this regard, the Central Bank of Malta issued Directive No. 18 on Moratoria on Credit Facilities in Exceptional Circumstances (Directive No. 18) in order to provide guidance on the treatment of such instances, in line with European Banking Authority (EBA) Guidelines on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis (the EBA Guidelines)[1]. These are referred to as general payment moratoria. In line with the EBA Guidelines and Directive No. 18, exposures meeting established criteria and eligible for the granting of a general payment moratorium are not classified as forborne/renegotiated, unless the borrower was already experiencing

[1] EBA Guideline (EBA/GL/2020/02) published on 2 April 2020, as amended by EBA/GL/2020/08 published on June 2020, and EBA/GL/2020/15 published on 2 December 2020.

2 **Financial risk management** *(continued)*

financial difficulties prior to the pandemic. Nevertheless, the Bank performed an assessment in respect of such exposures in order to determine whether the short-term shock may transform into long-term financial difficulties, thereby potentially requiring a downgrade to stage 2 or stage 3 to reflect the level of credit risk as appropriate. This assessment was performed on a periodic basis at the level of significant corporate exposures, whereas the assessment in respect of retail exposures was performed by reference to shared credit quality characteristics (for instance employment status and sector within which the customer is employed).

In accordance with the requirements of Directive No. 18, applications for new general payment moratoria or for extensions of existing general payment moratoria were accepted until 31 March 2021, with the total duration of the moratorium, inclusive of extensions, being limited to nine months. In this respect, applications for new general payment moratoria or for extensions of general payment moratoria received after 31 March 2021, or extending beyond the maximum duration prescribed by Directive No. 18, are considered to be forbearance measures. In addition, the granting of moratoria which do not meet the conditions of a general payment moratorium are also considered to be forbearance measures.

The movement in the carrying amount of forborne loans and advances, before impairment allowances, is analysed below:

	Forborne exposures 2021 € 000	Forborne exposures 2020 € 000
At 1 January	**31,163**	24,225
Loans to which forbearance measures have been extended during the year	**40,128**	18,087
Repayments and changes in carrying amount	**(2,281)**	316
Retired from forborne	**(8,151)**	(11,465)
At 31 December	**60,859**	31,163

Forborne loans, gross of Expected Credit Losses, are analysed by industry sector as follows:

	2021 € 000	2020 € 000
Manufacturing	**-**	18
Tourism	**7,399**	-
Trade	**2,765**	4,585
Property and construction	**8,917**	6,976
Personal, professional and home loans	**2,099**	2,321
Financial institutions	**35,318**	16,748
Other sectors	**4,361**	515
	60,859	31,163

As at 31 December 2021 and 2020, forborne loans mainly comprise exposures to customers based in Malta.

In addition to the forborne loans as disclosed in the tables above, during 2020 the Bank granted moratoria to 96 obligors in respect of gross exposures amounting to €78.6 million which moratoria met the criteria for a general payment moratorium as established within Directive No. 18 and the EBA guidelines.

As at 31 December 2020, outstanding gross loans and advances subject to general payment moratoria amounted to €65.7 million, of which €0.5 million are classified as Stage 2 and €0.05 million are classified as Stage 3. The allowance for ECL in respect of Stage 1 loans subject to general payment moratoria amounted to €0.3 million, while the ECL in respect of Stage 2 and Stage 3 loans subject to general payment moratoria amounted to €0.2 million and nil respectively.

As at 31 December 2021, there were no outstanding gross loans and advances subject to general payment moratoria.

2 **Financial risk management** *(continued)*

During the financial year ended 31 December 2021, extensions to general payment moratoria in respect of loans subject to general payment moratoria as at 31 December 2020 were granted to 1 obligor in respect of gross exposures amounting to €0.5 million, which extensions met the criteria established within Directive No. 18 and the EBA Guidelines.

During 2021, the Bank also granted new moratoria to 3 obligors in respect of gross exposures amounting to €15.6 million, which moratoria met the criteria for a general payment moratorium as established within Directive No. 18 and the EBA Guidelines.

Out of the outstanding gross loans and advances subject to general payment moratoria at 31 December 2020, €12 million relate to retail mortgage customers and €1.7 million relate to other retail customers. In order to earmark obligors experiencing a significant increase in credit risk and estimate the impact of delayed emergence of defaults in view of these moratoria, and accordingly estimate the ECL referred to above, the Bank assessed these exposures by reference to specific criteria established by management (refer to note 2.3.4.1). In respect of corporate exposures amounting to €52 million, the Bank assessed and individually rated each borrower requesting a general payment moratorium on the basis of recently obtained management information, including forecasts.

Following the expiration of all general payment moratoria during 2021, a post-model mechanism was enhanced to estimate the impact of delayed emergence of default in view of government support measures which were still in force during the year ended 31 December 2021 and also the potential economic impact of Malta's grey-listing by the FATF.

Specifically, the mechanism devised by management considers an overlay which increases the expected credit losses on performing (Stage 1) exposures within both the corporate and retail portfolios, which would have otherwise being subjected to a higher decrease in expected credit losses driven by the forecasted macroeconomic model inputs (note 2.3.4.4). The overlay, which is in the region of €3 million, is based on specific expert-based assumptions intended to account for possible losses which could arise on performing exposures, after taking cognisance of the current level of uncertainty in respect of the duration and economic impact of the pandemic, other developments referred to above, and the level of coverage of expected credit losses on Stage 1 exposures. The Bank specifically focused on those customer segments that are connected to industries which have been more impacted by the COVID-19 pandemic and those to whom a general payment moratorium was granted since the outbreak of the COVID-19 pandemic. The default risk following the eventual uplift of government support measures is deemed to be higher in respect of such customers and, accordingly, the potential impact on ECL as a result of these factors was estimated.

This post-model mechanism addresses the potential limitations in statistical models which could emerge, given that a number of assumptions are being applied during a period of time characterised by a high degree of economic volatility. Forward-looking assumptions entail a higher degree of uncertainty as historical relationships between key variables may not be relevant within the current scenario.

During 2020, the Bank also confirmed its participation in the Malta Development Bank COVID-19 Guarantee Scheme, whereby the risk of newly originated loans under the scheme to viable businesses experiencing liquidity pressures resulting from the effects of the pandemic are mitigated by a government guarantee.

In this respect, as at 31 December 2021, newly originated gross loans subject to the Malta Development Bank COVID-19 Guarantee Scheme amounted to €10.9 million (2020: €7.2 million), of which a maximum amount of €9.8 million (2020: €6.4 million) is considered guaranteed, though subject to an overall capping of €4.9 million (2020: €3.2 million). As at 31 December 2021, newly originated gross loans, under this scheme, classified as Stage 1 and Stage 2, amounted to €5.1 million (2020: €6.7 million) and €5.8 million (2020: €0.5 million) respectively. As at 31 December 2021, there were no (2020: nil) newly originated loans under this scheme classified in Stage 3.

The total ECL allowance in respect of Stage 1 loans subject to the Malta Development Bank COVID-19 Guarantee Scheme amounted to €117,000 (2020: €61,000), while the ECL in respect of Stage 2 loans amounted to €468,000 (2020: €1,000).

2.3.10 Loss allowances

Reconciliation of 12-month and lifetime ECL provision

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between 'Stage 1' and 'Stages 2' or '3' due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent 'step up' (or 'step down') between 12-month and Lifetime ECL;

2 **Financial risk management** *(continued)*

- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period upon full repayment;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis;
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets written off during the period and reversal of allowances related to assets that were written off.

The following tables explain the changes in the loss allowance between the beginning and the end of the annual period:

	2021			
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€ 000	€ 000	€ 000	€ 000
Balances with Central Bank of Malta at amortised cost				
Loss allowance as at 1 January 2021	-	-	-	-
Total net profit and loss charge during the year	-	-	-	-
Loss allowance as at 31 December 2021	-	-	-	-
Financial investments measured at FVOCI				
Loss allowance as at 1 January 2021	808	-	-	808
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	(344)	-	-	(344)
Total net profit and loss charge during the year	(344)	-	-	(344)
Loss allowance as at 31 December 2021	464	-	-	464
Loans and advances to banks at amortised cost				
Loss allowance as at 1 January 2021	-	-	-	-
Total net profit and loss charge during the year	-	-	-	-
Loss allowance as at 31 December 2021	-	-	-	-
Undrawn commitments				
Loss allowance as at 1 January 2021	224	-	2	226
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	(191)	11	(1)	(181)
Total net profit and loss charge during the year	(191)	11	(1)	(181)
Loss allowance as at 31 December 2021	33	11	1	45
Contingent liabilities				
Loss allowance as at 1 January 2021	61	-	-	61
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	(37)	-	-	(37)
Total net profit and loss charge during the year	(37)	-	-	(37)
Loss allowance as at 31 December 2021	24	-	-	24

2 **Financial risk management** *(continued)*

	2021			
	Stage 1 12-month ECL	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Loans and advances to customers at amortised cost				
Loss allowance as at 1 January 2021	**6,200**	**2,799**	**16,915**	**25,914**
Transfers of financial instruments				
Transfer from Stage 1 to Stage 2	**(167)**	**167**	**-**	**-**
Transfer from Stage 1 to Stage 3	**(10)**	**-**	**10**	**-**
Transfer from Stage 2 to Stage 1	**41**	**(41)**	**-**	**-**
Transfer from Stage 2 to Stage 3	**-**	**(8)**	**8**	**-**
Transfer from Stage 3 to Stage 1	**4**	**-**	**(4)**	**-**
Transfer from Stage 3 to Stage 2	**-**	**1,059**	**(1,059)**	**-**
Net remeasurement of ECL arising from stage transfers	**-**	**10**	**1**	**11**
Total remeasurement of loss allowance arising from transfers in stages	**(132)**	**1,187**	**(1,044)**	**11**
New financial assets originated or purchased	**881**	**189**	**54**	**1,124**
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	**(811)**	**(681)**	**954**	**(538)**
Financial assets derecognised	**(951)**	**(133)**	**(417)**	**(1,501)**
Total net profit and loss charge during the year	**(1,013)**	**562**	**(453)**	**(904)**
Other movements				
Write-offs	**-**	**-**	**(81)**	**(81)**
Unwind of discount	**-**	**-**	**693**	**693**
Loss allowance as at 31 December 2021	**5,187**	**3,361**	**17,074**	**25,622**

The movements reflected within the line item “Changes to risk parameters” have been analysed and described in notes 2.3.4.3, 2.3.4.4 and 2.3.9.

2 **Financial risk management** *(continued)*

	2020			
	Stage 1 12-month ECL € 000	Stage 2 Lifetime ECL € 000	Stage 3 Lifetime ECL € 000	Total € 000
Balances with Central Bank of Malta at amortised cost				
Loss allowance as at 1 January 2020	-	-	-	-
Total net profit and loss charge during the year	-	-	-	-
Loss allowance as at 31 December 2020	-	-	-	-
Financial investments measured at FVOCI				
Loss allowance as at 1 January 2020	183	-	-	183
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	625	-	-	625
Total net profit and loss charge during the year	625	-	-	625
Loss allowance as at 31 December 2020	808	-	-	808
Loans and advances to banks at amortised cost				
Loss allowance as at 1 January 2020	-	-	-	-
Total net profit and loss charge during the year	-	-	-	-
Loss allowance as at 31 December 2020	-	-	-	-
Undrawn commitments				
Loss allowance as at 1 January 2020	39	-	-	39
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	185	-	2	187
Total net profit and loss charge during the year	185	-	2	187
Loss allowance as at 31 December 2020	224	-	2	226
Contingent liabilities				
Loss allowance as at 1 January 2020	1	-	-	1
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	60	-	-	60
Total net profit and loss charge during the year	60	-	-	60
Loss allowance as at 31 December 2020	61	-	-	61

2 **Financial risk management** *(continued)*

	2020			
	Stage 1 12-month ECL	Stage 2 Lifetime ECL	Stage 3 Lifetime ECL	Total
	€ 000	€ 000	€ 000	€ 000
Loans and advances to customers at amortised cost				
Loss allowance as at 1 January 2020	3,832	1,346	19,917	25,095
Transfers of financial instruments				
Transfer from Stage 1 to Stage 2	(63)	63	-	-
Transfer from Stage 1 to Stage 3	(183)	-	183	-
Transfer from Stage 2 to Stage 1	45	(45)	-	-
Transfer from Stage 2 to Stage 3	-	(2)	2	-
Transfer from Stage 3 to Stage 1	60	-	(60)	-
Transfer from Stage 3 to Stage 2	-	20	(20)	-
Net remeasurement of ECL arising from stage transfers	-	-	51	51
Total remeasurement of loss allowance arising from transfers in stages	(141)	36	156	51
New financial assets originated or purchased	685	198	6	889
Changes to risk parameters (model inputs: PDs/LGDs/EADs)	2,225	1,326	3,166	6,717
Financial assets derecognised during the year	(401)	(107)	(4,075)	(4,583)
Total net profit and loss charge during the year	2,368	1,453	(747)	3,074
Other movements				
Write-offs	-	-	(3,267)	(3,267)
Unwind of discount	-	-	1,012	1,012
Loss allowance as at 31 December 2020	6,200	2,799	16,915	25,914

2 **Financial risk management** *(continued)*

The unwinding of discount on 'Stage 3' financial assets is reported within 'Interest Income' so that interest income is recognised on the amortised cost basis (after deducting the ECL allowance).

Remeasurement of loss allowances arising from foreign-exchange and other movements were not considered significant.

Changes in the gross carrying amount that contributed to changes in loss allowance

The following table explains changes in the gross carrying amount of the financial assets to help demonstrate their significance to the changes in the loss allowance for the same portfolios as discussed above:

	2021			
	Stage 1 Lifetime ECL	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Balances with Central Bank of Malta				
Gross carrying amount as at 1 January 2021	**68,417**	-	-	**68,417**
New financial assets originated or purchased	**2,375,426**	-	-	**2,375,426**
Financial assets derecognised	**(2,372,038)**	-	-	**(2,372,038)**
Gross carrying amount as at 31 December 2021	**71,805**	-	-	**71,805**
Financial investments measured at FVOCI				
Gross carrying amount as at 1 January 2021	**255,080**	-	-	**255,080**
New financial assets originated	**332,639**	-	-	**332,639**
Financial assets derecognised	**(310,490)**	-	-	**(310,490)**
Other movements	**(2,138)**	-	-	**(2,138)**
Gross carrying amount as at 31 December 2021	**275,091**	-	-	**275,091**
Loans and advances to banks at amortised cost				
Gross carrying amount as at 1 January 2021	**96,985**	-	-	**96,985**
New financial assets originated	**4,833,173**	-	-	**4,833,173**
Financial assets derecognised	**(4,851,879)**	-	-	**(4,851,879)**
Gross carrying amount as at 31 December 2021	**78,279**	-	-	**78,279**

2 **Financial risk management** *(continued)*

	2021			
	Stage 1 12-month ECL	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Loans and advances to customers at amortised cost				
Gross carrying amount as at 1 January 2021	**522,920**	**57,640**	**66,483**	**647,043**
Transfers of financial instruments				
Transfer from Stage 1 to Stage 2	**(39,692)**	**39,692**	**-**	**-**
Transfer from Stage 1 to Stage 3	**(2,774)**	**-**	**2,774**	**-**
Transfer from Stage 2 to Stage 1	**6,392**	**(6,392)**	**-**	**-**
Transfer from Stage 2 to Stage 3	**-**	**(1,246)**	**1,246**	**-**
Transfer from Stage 3 to Stage 1	**4**	**-**	**(4)**	**-**
Transfer from Stage 3 to Stage 2	**-**	**15,036**	**(15,036)**	**-**
Total changes in gross carrying amounts arising from transfers in stages	**(36,070)**	**47,090**	**(11,020)**	**-**
New financial assets originated	**103,553**	**22,383**	**4,553**	**130,489**
Changes in gross carrying amount due to facilities present as at 1 January 2021	**9,310**	**(1,602)**	**(1,781)**	**5,927**
Financial assets derecognised	**(95,238)**	**(13,228)**	**(6,396)**	**(114,862)**
Write-offs	**-**	**-**	**(82)**	**(82)**
Total net change during the year	**(18,445)**	**54,643**	**(14,726)**	**21,472**
Gross carrying amount as at 31 December 2021	**504,475**	**112,283**	**51,757**	**668,515**

2 **Financial risk management** *(continued)*

	2020			
	Stage 1 12-month ECL € 000	Stage 2 Lifetime ECL € 000	Stage 3 Lifetime ECL € 000	Total € 000
Balances with Central Bank of Malta				
Gross carrying amount as at 1 January 2020	74,976	-	-	74,976
New financial assets originated or purchased	220,446	-	-	220,446
Financial assets derecognised during the year	(227,005)	-	-	(227,005)
Gross carrying amount as at 31 December 2020	68,417	-	-	68,417
Financial investments measured at FVOCI				
Gross carrying amount as at 1 January 2020	211,872	-	-	211,872
New financial assets originated or purchased	437,211	-	-	437,211
Financial assets derecognised during the year	(390,901)	-	-	(390,901)
Other movements	(3,102)	-	-	(3,102)
Gross carrying amount as at 31 December 2020	255,080	-	-	255,080
Loans and advances to banks at amortised cost				
Gross carrying amount as at 1 January 2020	121,060	-	-	121,060
New financial assets originated or purchased	756,602	-	-	756,602
Financial assets derecognised during the year	(780,677)	-	-	(780,677)
Gross carrying amount as at 31 December 2020	96,985	-	-	96,985

2 **Financial risk management** *(continued)*

	2020			
	Stage 1 12-month ECL € 000	Stage 2 Lifetime ECL € 000	Stage 3 Lifetime ECL € 000	Total € 000
Loans and advances to customers at amortised cost				
Gross carrying amount as at 1 January 2020	479,831	45,927	51,380	577,138
Transfers of financial instruments				
Transfer from Stage 1 to Stage 2	(24,310)	24,310	-	-
Transfer from Stage 1 to Stage 3	(15,967)	-	15,967	-
Transfer from Stage 2 to Stage 1	18,884	(18,884)	-	-
Transfer from Stage 2 to Stage 3	-	(1,841)	1,841	-
Transfer from Stage 3 to Stage 1	1,141	-	(1,141)	-
Transfer from Stage 3 to Stage 2	-	482	(482)	-
Total changes in gross carrying amounts arising from transfers in stages	(20,252)	4,067	16,185	-
New financial assets originated	98,770	4,926	6,282	109,978
Changes in gross carrying amount due to respect of facilities present as at 1 January 2020	14,206	3,249	5,332	22,787
Financial assets derecognised	(49,635)	(529)	(9,255)	(59,419)
Write-offs	-	-	(3,441)	(3,441)
Total net change during the year	43,089	11,713	15,103	69,905
Gross carrying amount as at 31 December 2020	522,920	57,640	66,483	647,043

Undrawn commitments to lend as at 31 December 2021 amounted to €195,264,000 (2020: €197,180,000) and predominantly comprise of sanctioned but not yet drawn facilities which are classified as 'Stage 1' (12-month ECL) upon drawdown by customers. Changes in gross carrying amount of undrawn commitments to lend mainly relate to existing facilities drawn down by customers and new facilities sanctioned during 2021 and 2020.

Contingent liabilities and financial guarantee contracts as at 31 December 2021 amounting to €13,195,000 (2020: €10,851,000) are all classified as 'Stage 1' (12-month ECL) by the Group. Changes in gross carrying amount of contingent liabilities and financial guarantee contracts mainly related to the expiry or enforcement of existing financial guarantees and the issuance of new financial guarantees during 2021 and 2020.

Changes in gross carrying amount arising from foreign-exchange and other movements were not significant.

2.3.11 Write-off policy

The Group writes off loans and advances to customers when it determines that these are uncollectible and it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-offs.

The Group may write-off financial assets that are still subject to enforcement activity. The Group still seeks to recover amounts it is legally owed in full, but which have been partially written off due to no reasonable expectation of full recovery.

2 **Financial risk management** *(continued)*

2.3.12 Collateral

The Group employs a range of policies and practices to mitigate credit risk. The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. The Group's Board established a policy regarding the acceptability of types of collateral and valuation parameters.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured.

The main types of collateral obtained are as follows:

- for corporate lending, charges over real estate properties, cash or securities;
- for retail lending (including home loans and consumer credit), mortgages over residential properties, cash or securities; and
- for exposures arising from reverse repurchase transactions, a pledge on liquid sovereign debt securities.

Collateral held as security for financial assets other than loans and advances depends on the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured.

Management assesses the market value of collateral as part of the loan origination process. This assessment is reviewed periodically through ongoing credit file reviews. The Group requests additional collateral in accordance with the underlying agreement when necessary.

The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period.

A portion of the Group's financial assets has sufficiently low 'loan-to-value' (LTV) ratios, which result in insignificant loss allowance being recognised in accordance with the Group's Expected Credit Loss model. As at 31 December 2021, the gross carrying amount of such financial assets is €450,511,000 (2020: €466,033,000).

Loans granted as part of the Malta Development Bank COVID-19 Guarantee Scheme (note 2.3.9) are secured by guarantees granted as part of this Scheme and included within Other collateral in the tables below.

2 **Financial risk management** *(continued)*

The Group closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

Credit-impaired assets	Gross exposure € 000	Impairment allowance € 000	Carrying amount € 000	Fair value of collateral held € 000
As at 31 December 2021				
- Overdrafts	**15,303**	**2,655**	**12,648**	**19,744**
- Term loans	**33,394**	**12,656**	**20,738**	**74,474**
Total credit-impaired assets	**48,697**	**15,311**	**33,386**	**94,218**
As at 31 December 2020				
- Overdrafts	15,646	1,742	13,904	22,704
- Term loans	47,140	13,280	33,860	91,048
- Credit cards	1	-	1	13
Total credit-impaired assets	62,787	15,022	47,765	113,765

Financial assets that are credit-impaired but with no collateral is held in this respect, are shown below:

Credit-impaired assets	Gross exposure € 000	Impairment allowance € 000	Carrying amount € 000
As at 31 December 2021			
- Overdrafts	**426**	**380**	**46**
- Term loans	**2,622**	**1,370**	**1,252**
- Credit cards	**12**	**12**	**-**
Total credit-impaired assets	**3,060**	**1,762**	**1,298**
As at 31 December 2020			
- Overdrafts	1,146	399	747
- Term loans	2,537	1,481	1,056
- Credit cards	13	13	-
Total credit-impaired assets	3,696	1,893	1,803

It is the Bank's policy to dispose of properties acquired through judicial action in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the Bank does not occupy properties acquired through judicial action for business use.

2 **Financial risk management** *(continued)*

The following tables show the distribution of LTV ratios for the Group's credit-impaired loans and advances to customers.

	Non-forborne exposures 2021 € 000	**Forborne exposures 2021 € 000**	**Total 2021 € 000**	Non-forborne exposures 2020 € 000	Forborne exposures 2020 € 000	Total 2020 € 000
Performing - Stage 1						
Not collateralised	**36,776**	**-**	**36,776**	49,697	-	49,697
Fully collateralised:						
Less than 50% LTV	**298,058**	**-**	**298,058**	293,679	-	293,679
51% to 75% LTV	**98,708**	**-**	**98,814**	129,905	-	129,905
76% to 90% LTV	**54,011**	**-**	**54,011**	31,942	-	31,942
91% to 100% LTV	**6,190**	**-**	**6,190**	9,522	-	9,522
	456,967	**-**	**456,967**	465,048		465,048
Partially collateralised:						
Greater than 100% LTV	**10,734**	**-**	**10,734**	8,178	-	8,178
Total performing – Stage 1	**504,477**	**-**	**504,477**	522,923	-	522,923
Underperforming – Stage 2						
Not collateralised	**4,902**	**69**	**4,971**	1,568	9	1,577
Fully collateralised:						
Less than 50% LTV	**17,620**	**29,521**	**47,141**	27,403	1,096	28,499
51% to 75% LTV	**33,256**	**860**	**34,116**	6,889	-	6,889
76% to 90% LTV	**-**	**512**	**512**	1,350	-	1,350
91% to 100% LTV	**3,403**	**-**	**3,403**	82	-	82
	54,279	**30,893**	**85,172**	35,724	1,096	36,820
Partially collateralised:						
Greater than 100% LTV	**3,499**	**18,641**	**22,140**	2,495	16,748	19,243
Total performing – Stage 2	**62,680**	**49,603**	**112,283**	39,787	17,853	57,640
Non-Performing – Stage 3						
Not collateralised	**3,051**	**9**	**3,060**	3,513	183	3,696
Fully collateralised:						
Less than 50% LTV	**12,067**	**8,643**	**20,710**	12,602	5,596	18,198
51% to 75% LTV	**2,326**	**1,376**	**3,702**	12,496	4,871	17,367
76% to 90% LTV	**1,492**	**832**	**2,324**	980	876	1,856
91% to 100% LTV	**-**	**-**	**-**	3,145	362	3,507
	15,885	**10,851**	**26,736**	29,223	11,705	40,928
Partially collateralised:						
Greater than 100% LTV	**21,565**	**396**	**21,961**	20,437	1,422	21,859
Total non-performing – Stage 3	**40,501**	**11,256**	**51,757**	53,173	13,310	66,483
At 31 December	**607,658**	**60,859**	**668,517**	615,883	31,163	647,046

2 **Financial risk management** *(continued)*

2.3.13 Trade and other receivables

The Bank's subsidiary assesses the credit quality of its customers taking into account financial position, past experience and other factors. It has policies in place to ensure that sales of products and services are effected to customers with an appropriate credit history in the case of credit sales. The subsidiary monitors the performance of these financial assets on a regular basis to identify incurred collection losses which are inherent in the subsidiary's receivables taking into account historical experience in collection of accounts receivable.

Standard credit terms are in place for individual clients, however, wherever possible, new corporate customers are analysed individually for creditworthiness before the subsidiary's standard payment and service delivery terms and conditions are offered. The entity's review includes external creditworthiness databases when available. The subsidiary establishes an allowance for impairment that represents its estimate of both incurred and expected losses in respect of trade and other receivables. This allowance represents Expected Credit Losses (ECL) against individual exposures. The movement in provisions for impairment in respect of trade receivables is disclosed in note 16. Other overdue trade receivables amounted to €248,000 (2020: €428,000), principally overdue by nine months, but were not impaired.

The subsidiary's receivables, which are not impaired financial assets, are principally in respect of transactions with customers for whom there is no recent history of default. Management does not expect any material losses from non-performance by these customers.

2.3.14 Contingencies and commitments

Guarantees and standby letters of credit carry the same credit risk as loans. Documentary, credit and commercial letters of credit – which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions – are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan. Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments as most commitments to extend credit are contingent upon customers maintaining specific credit standards. These exposures are monitored in the same manner outlined above in respect of loans and advances.

2.4 Market risk

The Group takes on exposure to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices.

Accordingly, market risk for the Group consists of three elements:

- Interest rate risk, which is the risk of losses because of changes in interest rates;
- Exchange rate risk, which is the risk of losses on the Group's positions in foreign currency because of changes in exchange rates; and
- Equity price risk, which is the risk of losses because of changes in investment prices.

2.4.1 Interest rate risk

Interest rate risk is the risk that the value or cash flows of a financial instrument will fluctuate due to changes in market interest rates. Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the fair value of a financial instrument will fluctuate because of changes in market interest rates. The Group, through its banking operations, takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but losses may occur in the event that unexpected movements arise.

2 **Financial risk management** *(continued)*

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice within different time periods or on different terms. The Bank accepts deposits from customers at both fixed and floating rates and for varying terms. This poses a risk to the Bank, which risk is managed by monitoring on a continuous basis the level of mismatch of interest rate repricing taking cognisance of the terms of the Bank's principal assets, loans and advances to customers, that are repriceable at the Bank's discretion. The Bank also invests in highly liquid quality assets and other short-term instruments for the purposes of mitigating exposures to fluctuations in interest rates. The Bank is accordingly in a position to manage the interest rate terms of its financial assets and simultaneously to effect changes to interest terms of liabilities reflecting the Bank's strategy together with market developments. The Group seeks to manage its net interest spread, considering the cost of capital, by investing funds in a portfolio of assets with a longer term than the liabilities funding them (therefore normally giving rise to a negative maturity gap position) but with shorter repricing periods or terms. The Bank manages the shorter term nature of the liabilities funding the assets for the purposes of ensuring a steady base of deposits with differing terms over the medium to longer term. The Bank's Assets & Liabilities Committee is primarily responsible for oversight over the Bank's interest rate risk management process and monitors actively the interest rate risk measures utilised by the Bank.

Credit facilities and commitments to lend funds to customers are granted at prevailing market interest rates at drawdown date.

The following tables summarise the Group's exposures to interest rate risks. These analyse the Group's financial instruments, which were interest-bearing, at their carrying amounts categorised by the earlier of contractual repricing or maturity dates.

Group	**Carrying amount**	**Effective interest rate**	**Less than 3 months**	**Between 3 months and 1 year**	**Between 1 year and 5 years**	**More than 5 years**	**Non-interest bearing**
At 31 December 2021	**€ 000**	**%**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Financial assets							
Balances with Central Bank of Malta, treasury bills and cash	**126,279**	**(0.10)**	**105,362**	**14,033**	**-**	**-**	**6,884**
Debt and other fixed income instruments measured at FVOCI	**218,080**	**1.14**	**531**	**4,091**	**88,095**	**125,363**	**-**
Loans and advances to banks	**78,279**	**0.11**	**75,779**	**2,500**	**-**	**-**	**-**
Loans and advances to customers	**642,893**	**3.72**	**549,358**	**12,607**	**53,233**	**15,990**	**11,705**
Total financial assets	**1,065,531**		**731,030**	**33,231**	**141,328**	**141,353**	**18,589**
Financial liabilities							
Amounts owed to banks	**1,224**	**0.14**	**1,224**	**-**	**-**	**-**	**-**
Amounts owed to customers	**977,143**	**0.77**	**514,225**	**66,209**	**183,384**	**59,676**	**153,649**
Total financial liabilities	**978,367**		**515,449**	**66,209**	**183,384**	**59,676**	**153,649**
Interest repricing gap			**215,581**	**(32,978)**	**(42,056)**	**81,677**	**(135,060)**
Cumulative gap			**215,581**	**182,603**	**140,547**	**222,224**	

2 **Financial risk management** *(continued)*

Group **At 31 December 2020**	**Carrying amount** **€ 000**	**Effective interest rate** **%**	**Less than 3 months** **€ 000**	**Between 3 months and 1 year** **€ 000**	**Between 1 year and 5 years** **€ 000**	**More than 5 years** **€ 000**	**Non-interest bearing** **€ 000**
Financial assets							
Balances with Central Bank of Malta, treasury bills and cash	169,687	(0.20)	148,042	14,030	-	-	7,615
Debt and other fixed income instruments measured at FVOCI	152,182	2.06	237	3,706	45,276	102,963	-
Loans and advances to banks	96,985	0.05	95,485	1,500	-	-	-
Loans and advances to customers	621,129	3.97	514,320	25,756	34,428	35,658	10,967
Total financial assets	1,039,983		758,084	44,992	79,704	138,621	18,582
Financial liabilities							
Amounts owed to banks	5,602	0.10	5,602	-	-	-	-
Amounts owed to customers	941,110	0.69	533,908	69,660	158,805	44,178	134,559
Total financial liabilities	946,712		539,510	69,660	158,805	44,178	134,559
Interest repricing gap			218,574	(24,668)	(79,101)	94,443	(106,977)
Cumulative gap			218,574	193,906	114,805	209,248	

Bank **At 31 December 2021**	**Carrying amount** **€ 000**	**Effective interest rate** **%**	**Less than 3 months** **€ 000**	**Between 3 months and 1 year** **€ 000**	**Between 1 year and 5 years** **€ 000**	**More than 5 years** **€ 000**	**Non-interest bearing** **€ 000**
Financial assets							
Balances with Central Bank of Malta, treasury bills and cash	**125,552**	**(0.10)**	**105,362**	**14,033**	**-**	**-**	**6,157**
Debt and other fixed income instruments measured at FVOCI	**215,179**	**1.09**	**531**	**4,066**	**87,371**	**123,211**	**-**
Loans and advances to banks	**68,424**	**0.09**	**68,424**	**-**	**-**	**-**	**-**
Loans and advances to customers	**642,895**	**3.72**	**549,360**	**12,607**	**53,233**	**15,990**	**11,705**
Total financial assets	**1,052,050**		**723,677**	**30,706**	**140,604**	**139,201**	**17,862**
Financial liabilities							
Amounts owed to banks	**1,224**	**0.14**	**1,224**	**-**	**-**	**-**	**-**
Amounts owed to customers	**978,365**	**0.77**	**514,358**	**66,410**	**183,384**	**59,676**	**154,537**
Total financial liabilities	**979,589**		**515,582**	**66,410**	**183,384**	**59,676**	**154,537**
Interest repricing gap			**208,095**	**(35,704)**	**(42,780)**	**79,525**	**(136,675)**
Cumulative gap			**208,095**	**172,391**	**129,611**	**209,136**	

2 **Financial risk management** *(continued)*

Bank **At 31 December 2020**	**Carrying amount** **€ 000**	**Effective interest rate** **%**	**Less than 3 months** **€ 000**	**Between 3 months and 1 year** **€ 000**	**Between 1 year and 5 years** **€ 000**	**More than 5 years** **€ 000**	**Non-interest bearing** **€ 000**
Financial assets							
Balances with Central Bank of Malta, treasury bills and cash	168,648	(0.20)	148,043	14,029	-	-	6,576
Debt and other fixed income instruments measured at FVOCI	148,621	1.99	-	3,364	44,733	100,524	-
Loans and advances to banks	93,641	0.04	93,641	-	-	-	-
Loans and advances to customers	621,132	3.97	514,322	25,757	34,428	35,658	10,967
Total financial assets	1,032,042		756,006	43,150	79,161	136,182	17,543
Financial liabilities							
Amounts owed to banks	5,602	0.10	5,602	-	-	-	-
Amounts owed to customers	948,478	0.68	537,909	71,660	158,805	44,178	135,926
Total financial liabilities	954,080		543,511	71,660	158,805	44,178	135,926
Interest repricing gap			212,495	(28,510)	(79,644)	92,004	(118,383)
Cumulative gap			212,495	183,985	104,341	196,345	

2 **Financial risk management** *(continued)*

2.4.2 Interest rate profile

At the end of the reporting periods the interest rate profile of the Group's interest-bearing financial instruments was:

Group	**Fixed rate**		**Variable rate**	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Interest-earning assets				
Balances with Central Bank of Malta and treasury bills	**67,151**	123,048	**52,244**	39,024
Debt and other fixed income instruments measured at FVOCI	**218,080**	152,182	**-**	-
Loans and advances to banks	**44,754**	51,227	**33,525**	45,758
Loans and advances to customers	**86,062**	97,233	**545,126**	512,929
	416,047	423,690	**630,895**	597,711
Interest-bearing liabilities				
Amounts owed to banks	**23**	22	**1,201**	5,580
Amounts owed to customers	**358,094**	317,535	**465,400**	489,016
	358,117	317,557	**466,601**	494,596

At the end of the reporting periods the interest rate profile of the Bank's interest-bearing financial instruments was:

Bank	**Fixed rate**		**Variable rate**	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Interest-earning assets				
Balances with Central Bank of Malta and treasury bills	**67,151**	123,047	**52,244**	39,024
Debt and other fixed income instruments measured at FVOCI	**215,179**	148,621	**-**	-
Loans and advances to banks	**42,254**	49,727	**26,170**	43,914
Loans and advances to customers	**86,062**	97,233	**545,128**	512,932
	410,646	418,628	**623,542**	595,870
Interest-bearing liabilities				
Amounts owed to banks	**23**	22	**1,201**	5,580
Amounts owed to customers	**358,294**	321,633	**465,532**	490,919
	358,317	321,655	**466,733**	496,499

2 **Financial risk management** *(continued)*

2.4.3 Fair value sensitivity analysis for fixed rate instruments

The Group's instruments exposing the Bank to fair value interest rate risk consist of quoted debt securities measured at FVOCI (also refer to note 6) since these are fair valued with fair value changes recognised in other comprehensive income. Considering the nature and carrying amount of the investments, with the majority of investments comprising securities issued by the Government of Malta, a sensitivity analysis disclosing how equity would have been affected by changes in interest rates that were reasonably possible at the end of the reporting period is not deemed necessary. All other financial instruments subject to fixed interest rates are measured at amortised cost.

2.4.4 Cash flow sensitivity analysis for variable rate instruments

At the end of the reporting periods, if interest rates had increased/decreased by 100 basis points (assuming a parallel shift of 100 basis points in yields) with all other variables held constant, the pre-tax result for the year would change by the following amounts determined by applying the shift to the net variable interest exposure of the Group/Bank at the end of the reporting periods:

Group	**2021**	2020
	€ 000	€ 000
(+) 100bp	**1,643**	1,031
(-) 100bp	**(1,643)**	(1,031)

Bank	**2021**	2020
	€ 000	€ 000
(+) 100bp	**1,568**	994
(-) 100bp	**(1,568)**	(994)

2.4.5 Currency risk

The Group takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows particularly within the Bank's operations. Foreign exchange risk to the Bank is the risk that earnings and values fluctuate as a result of changes in foreign exchange rates. The Bank's foreign exchange risk arises when financial assets or liabilities are denominated in currencies which are different from the Bank's functional currency.

The Bank essentially manages this risk by ensuring that foreign currency liabilities are utilised to fund assets denominated in the same foreign currency thereby matching asset and liability positions as much as is practicable. This mechanism is reflected in the figures reported in the tables below which present this matching process.

The Bank maintains its exposure to foreign currencies within prescribed limits set by the Bank's ALCO. ALCO sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions which are monitored on a real-time basis.

The Bank enters into forward foreign exchange contracts with customers in the normal course of its business. Generally, it is the Bank's policy to cover the exposure arising from forward contracts. As a result, the Group is not exposed to any significant exchange risk in respect of outstanding derivative financial instruments at the end of the reporting periods. The Bank also retains a deposit margin covering a portion of the notional amount of the respective contract from the customer thereby reducing the extent of credit risk should the derivative client default. The Bank did not have any derivative financial instruments as at 31 December 2021 and 2020.

2 Financial risk management *(continued)*

The following tables summarise the Group's exposures to foreign currency risk. Included in the tables are the Group's financial instruments which are subject to foreign exchange risk at carrying amounts, categorised by currency.

Group **At 31 December 2021**	**Total** **€ 000**	**EUR** **€ 000**	**GBP** **€ 000**	**USD** **€ 000**	**Other** **€ 000**
Financial assets					
Balances with Central Bank of Malta, treasury bills and cash	**126,279**	**106,106**	**11,080**	**9,081**	**12**
Investments measured at FVOCI	**227,501**	**209,654**	**6,668**	**11,179**	**-**
Loans and advances to banks	**78,279**	**21,987**	**20,354**	**32,586**	**3,352**
Loans and advances to customers	**642,893**	**639,443**	**3,118**	**302**	**30**
Other assets	**13,853**	**11,879**	**274**	**1,187**	**513**
Total financial assets	**1,088,805**	**989,069**	**41,494**	**54,335**	**3,907**
Financial liabilities					
Amounts owed to banks	**1,224**	**1,224**	**-**	**-**	**-**
Amounts owed to customers	**977,143**	**881,729**	**40,232**	**51,809**	**3,373**
Other liabilities	**42,297**	**38,913**	**1,137**	**1,895**	**352**
Total financial liabilities	**1,020,664**	**921,866**	**41,369**	**53,704**	**3,725**
Net currency exposure in financial assets/liabilities		**67,203**	**125**	**631**	**182**
Commitments and contingent liabilities	**208,390**	**206,517**	**1,195**	**678**	**-**

Group **At 31 December 2020**	**Total** **€ 000**	**EUR** **€ 000**	**GBP** **€ 000**	**USD** **€ 000**	**Other** **€ 000**
Financial assets					
Balances with Central Bank of Malta, treasury bills and cash	169,687	139,568	14,281	15,825	13
Investments measured at FVOCI	161,424	144,790	6,428	10,206	-
Loans and advances to banks	96,985	31,105	24,508	37,572	3,800
Loans and advances to customers	621,129	617,551	3,031	534	13
Other assets	9,044	7,033	279	1,207	525
Total financial assets	1,058,269	940,047	48,527	65,344	4,351
Financial liabilities					
Amounts owed to banks	5,602	5,602	-	-	-
Amounts owed to customers	941,110	828,588	47,169	61,500	3,853
Other liabilities	41,401	35,792	1,272	3,791	546
Total financial liabilities	988,113	869,982	48,441	65,291	4,399
Net currency exposure in financial assets/liabilities		70,065	86	53	(48)
Commitments and contingent liabilities	207,744	207,203	142	399	-

2 **Financial risk management** *(continued)*

Under the scenario that the euro appreciates by 20% against all currencies the effect would be a decrease of €159,000 (2020: €16,000) in the carrying amount of financial instruments with the adverse impact recognised in profit or loss. Should the euro depreciate against all currencies by 20%, the effect would be a gain of €233,000 (2020: €23,000) in the carrying amount of financial instruments and the favourable impact would be recognised in profit or loss.

The following tables summarise the Bank's exposures to foreign currency risk. Included in the tables are the entity's financial instruments which are subject to foreign exchange risk at carrying amounts, categorised by currency.

Bank **At 31 December 2021**	**Total** **€ 000**	**EUR** **€ 000**	**GBP** **€ 000**	**USD** **€ 000**	**Other** **€ 000**
Financial assets					
Balances with Central Bank of Malta, treasury bills and cash	**125,552**	**105,379**	**11,080**	**9,081**	**12**
Investments measured at FVOCI	**224,600**	**206,753**	**6,668**	**11,179**	**-**
Loans and advances to banks	**68,424**	**12,237**	**20,354**	**32,482**	**3,351**
Loans and advances to customers	**642,895**	**639,445**	**3,118**	**302**	**30**
Other assets	**4,048**	**3,913**	**59**	**76**	**-**
Total financial assets	**1,065,519**	**967,727**	**41,279**	**53,120**	**3,393**
Financial liabilities					
Amounts owed to banks	**1,224**	**1,224**	**-**	**-**	**-**
Amounts owed to customers	**978,365**	**882,951**	**40,232**	**51,809**	**3,373**
Other liabilities	**22,043**	**19,742**	**995**	**1,244**	**62**
Total financial liabilities	**1,001,632**	**903,917**	**41,227**	**53,053**	**3,435**
Net currency exposure in financial assets/liabilities		**63,810**	**52**	**67**	**(42)**
Commitments and contingent liabilities	**209,663**	**207,790**	**1,195**	**678**	**-**

2 **Financial risk management** *(continued)*

Bank **At 31 December 2020**	**Total € 000**	**EUR € 000**	**GBP € 000**	**USD € 000**	**Other € 000**
Financial assets					
Balances with Central Bank of Malta, treasury bills and cash	168,648	138,529	14,281	15,825	13
Investments measured at FVOCI	157,863	141,229	6,428	10,206	-
Loans and advances to banks	93,641	27,632	24,508	37,701	3,800
Loans and advances to customers	621,132	617,554	3,031	534	13
Other assets	4,591	4,466	58	67	-
Total financial assets	1,045,875	929,410	48,306	64,333	3,826
Financial liabilities					
Amounts owed to banks	5,602	5,602	-	-	-
Amounts owed to customers	948,478	835,813	47,169	61,643	3,853
Other liabilities	25,285	21,593	1,047	2,633	12
Total financial liabilities	979,365	863,008	48,216	64,276	3,865
Net currency exposure in financial assets/liabilities		66,402	90	57	(39)
Commitments and contingent liabilities	208,983	208,442	142	399	-

Under the scenario that the euro appreciates by 20% against all currencies the effect would be a decrease of €13,000 (2020: €19,000) in the carrying amount of financial instruments with the adverse impact recognised in profit or loss. Should the euro depreciate against all currencies by 20%, the effect would be a gain of €19,000 (2020: €27,000) in the carrying amount of financial instruments and the favourable impact would be recognised in profit or loss.

2.4.6 Equity price risk

The exposure of the Group to this risk is not significant in view of the extent of the Group's holdings of equity investments measured at FVOCI (refer to note 6) which are not deemed material in the context of the Group's statement of financial position. These investments are principally locally quoted equity instruments issued by local well-known corporates. Frequent management reviews are carried out to ensure continued high quality of the portfolio.

2.5 Liquidity risk

Liquidity risk is defined as the risk of losses due to:

- the Group's funding costs increasing disproportionately;
- lack of funding preventing the Group from establishing new business; and
- lack of funding which will ultimately prevent the Group from meeting its obligations.

In relation to the Bank's operations, liquidity risk is the risk that the Bank is unable to meet its obligations when they fall due as a result of customer deposits being withdrawn, cash requirements from contractual commitments, or other cash outflows. The Group is exposed to daily calls on its available cash resources from overnight deposits, current and call deposits, maturing term deposits, loan draw-downs and guarantees together with other related off-balance sheet instruments. Such outflows would deplete available cash resources for client lending and investments. In extreme circumstances, lack of liquidity could result in sales of assets, or potentially an inability to fulfil lending commitments. The risk that the Group will be unable to do so is inherent in all banking operations and can be affected by a range of institution-specific and market-wide events including, but not limited to, credit events, systemic shocks and natural disasters.

2 **Financial risk management** *(continued)*

The objective of the Group's liquidity and funding management is to ensure that all foreseeable funding commitments and deposit withdrawals can be met when due. It is the Bank's objective to maintain a diversified and stable funding base with the objective of enabling it to respond quickly and smoothly to unforeseen liquidity requirements.

The Group manages this risk by ensuring that its assets and liabilities are matched in terms of maturities as much as is practicable. However, the Bank ought to manage its net interest spread by investing funds in a portfolio of assets with a longer term than the liabilities funding them (therefore giving rise to a negative maturity gap position). To mitigate exposures arising in this respect, the Bank holds significant liquid assets in the form of Malta Government treasury bills, money market placements and other short-term instruments for managing liquidity risk to support payment obligations and contingent funding in a stressed market environment.

The Bank's Advances-to-Deposit ratio of 65.7% (2020: 65.5%) at the end of the reporting period reflects management's prudent stance in the context of liquidity management.

Liquidity Coverage Ratio

The Liquidity Coverage Ratio (LCR) is designed to promote the short-term resilience of a bank's liquidity profile. This ratio became a minimum regulatory standard under the European Commission Delegated Regulation 2015/61.

The LCR aims to ensure that a bank has adequate unencumbered high-quality liquid assets (HQLA) to meet its liquidity requirements within a 30-calendar-day liquidity stress scenario. Generally, HQLA consists of cash or assets that can be converted into cash at little or no loss of value in markets.

The Bank's LCR as at 31 December 2021 was 225.3% (2020: 180.0%). During the financial years ended 31 December 2021 and 2020, the LCR was in excess of both the regulatory minimum and the risk appetite thresholds set by the bank.

Net Stable Funding Ratio

The Net Stable Funding Ratio (NSFR) is a metric showing how a bank is able to maintain sufficient stable funding relative to required stable funding, and reflects a bank's long-term funding profile (typically, with a term of more than one year).

This ratio became a minimum regulatory standard from June 2021, under the European Commission Regulation 2019/876. As at 31 December 2020 the Bank calculated its NSFR ratio in line with the Basel Committee on Banking Supervision (publication 295), given that the European calibration was still subject to implementation by the European Commission.

The Bank's NSFR as at 31 December 2021 was 148.4% (2020: 135.6%). During the financial years ended 31 December 2021 and 2020, the NSFR was in excess of both the regulatory minimum and the risk appetite thresholds set by the bank.

The Bank's ALCO focuses on the Bank's management process with respect to market and funding liquidity risks.

The Group's liquidity management process, focusing on the liquidity of the Bank and that of its principal subsidiary, includes:

- management of day-to-day funding, by monitoring future cash flows to ensure that requirements can be met. This includes replenishment of funds as they mature or are borrowed by customers. The starting point for those projections is an analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets;
- maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- monitoring the liquidity ratios of the Bank against internal and regulatory requirements; and
- managing the concentration and profile of debt maturities.

The Bank also monitors the level and type of undrawn lending commitments and the impact of contingent liabilities such as guarantees as part of the liquidity management process previously referred to. As at 31 December 2021, the Bank had outstanding guarantees on behalf of third parties amounting to €9,320,000 (2020: €8,681,000), which are cancellable upon the request of the third parties. The Group's liquidity exposures arising from these commitments and contingencies are expected to expire principally within a period of twelve months from the end of the reporting period.

The following tables analyse the Group's principal financial assets and liabilities into relevant maturity groupings based on the remaining period at the end of the reporting period to the contractual maturity date.

2 **Financial risk management** *(continued)*

Group **At 31 December 2021**	**Less than 3 months** **€ 000**	**Between 3 months and 1 year** **€ 000**	**Between 1 year and 5 years** **€ 000**	**More than 5 years** **€ 000**	**No maturity date** **€ 000**	**Total** **€ 000**
Financial assets						
Balances with Central Bank of Malta, treasury bills and cash	**105,362**	**14,033**	**-**	**-**	**6,884**	**126,279**
Investments measured at FVOCI	**531**	**4,092**	**88,095**	**125,362**	**9,421**	**227,501**
Loans and advances to banks	**75,779**	**2,500**	**-**	**-**	**-**	**78,279**
Loans and advances to customers	**166,537**	**38,216**	**117,555**	**320,585**	**-**	**642,893**
Other assets	**13,394**	**459**	**-**	**-**	**-**	**13,853**
Total financial assets	**361,603**	**59,300**	**205,650**	**445,947**	**16,305**	**1,088,805**
Financial liabilities						
Amounts owed to banks	**1,224**	**-**	**-**	**-**	**-**	**1,224**
Amounts owed to customers	**667,873**	**66,210**	**183,384**	**59,676**	**-**	**977,143**
Other liabilities	**24,465**	**203**	**1,467**	**8,042**	**8,119**	**42,296**
Total financial liabilities	**693,562**	**66,413**	**184,851**	**67,718**	**8,119**	**1,020,663**
Maturity gap	**(331,959)**	**(7,113)**	**20,799**	**378,229**	**-**	**-**
Cumulative gap	**(331,959)**	**(339,072)**	**(318,273)**	**59,956**	**-**	**-**

Group **At 31 December 2020**						
Financial assets						
Balances with Central Bank of Malta, treasury bills and cash	148,043	14,029	-	-	7,615	169,687
Investments measured at FVOCI	237	3,706	45,276	102,963	9,242	161,424
Loans and advances to banks	95,485	1,500	-	-	-	96,985
Loans and advances to customers	170,456	84,679	126,475	239,519	-	621,129
Other assets	8,605	439	-	-	-	9,044
Total financial assets	422,826	104,353	171,751	342,482	16,857	1,058,269
Financial liabilities						
Amounts owed to banks	5,602	-	-	-	-	5,602
Amounts owed to customers	668,467	69,660	158,805	44,178	-	941,110
Other liabilities	29,579	242	733	7,237	3,610	41,401
Total financial liabilities	703,648	69,902	159,538	51,415	3,610	988,113
Maturity gap	(280,822)	34,451	12,213	291,067	-	-
Cumulative gap	(280,822)	(246,371)	(234,158)	56,909	-	-

2 Financial risk management *(continued)*

Bank	**Less than 3 months**	**Between 3 months and 1 year**	**Between 1 year and 5 years**	**More than 5 years**	**No maturity date**	**Total**
At 31 December 2021	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Financial assets						
Balances with Central Bank of Malta, treasury bills and cash	**105,362**	**14,033**	**-**	**-**	**6,157**	**125,552**
Investments measured at FVOCI	**531**	**4,066**	**87,371**	**123,211**	**9,421**	**224,600**
Loans and advances to banks	**68,424**	**-**	**-**	**-**	**-**	**68,424**
Loans and advances to customers	**166,540**	**38,216**	**117,555**	**320,584**	**-**	**642,895**
Other assets	**3,589**	**459**	**-**	**-**	**-**	**4,048**
Total financial assets	**344,446**	**56,774**	**204,926**	**443,795**	**15,578**	**1,065,519**
Financial liabilities						
Amounts owed to banks	**1,224**	**-**	**-**	**-**	**-**	**1,224**
Amounts owed to customers	**668,896**	**66,409**	**183,384**	**59,676**	**-**	**978,365**
Other liabilities	**9,275**	**203**	**1,467**	**6,546**	**4,552**	**22,043**
Total financial liabilities	**679,395**	**66,612**	**184,851**	**66,222**	**4,552**	**1,001,632**
Maturity gap	**(334,949)**	**(9,838)**	**20,075**	**377,573**	-	-
Cumulative gap	**(334,949)**	**(344,787)**	**(324,712)**	**52,861**	-	-

Bank						
At 31 December 2020						
Financial assets						
Balances with Central Bank of Malta, treasury bills and cash	148,043	14,029	-	-	6,576	168,648
Investments measured at FVOCI	-	3,364	44,733	100,524	9,242	157,863
Loans and advances to banks	93,641	-	-	-	-	93,641
Loans and advances to customers	170,458	84,680	126,475	239,519	-	621,132
Other assets	4,152	439	-	-	-	4,591
Total financial assets	416,294	102,512	171,208	340,043	15,818	1,045,875
Financial liabilities						
Amounts owed to banks	5,602	-	-	-	-	5,602
Amounts owed to customers	673,835	71,660	158,805	44,178	-	948,478
Other liabilities	15,203	242	733	5,497	3,610	25,285
Total financial liabilities	694,640	71,902	159,538	49,675	3,610	979,365
Maturity gap	(278,346)	30,610	11,670	290,368		
Cumulative gap	(278,346)	(247,736)	(236,066)	54,302		

2 **Financial risk management** *(continued)*

Amounts owed to customers of €620,071,000 (2020: €626,844,000) as at 31 December 2021 are repayable on demand and included in the "within 3 months" bucket in the tables. However, the Bank's experience is that a significant portion of such deposits remains stable. Additionally, a significant part of other deposits maturing within 3 months from the end of the reporting period is typically renewed.

The tables below analyse the Group's and Bank's principal non-derivative financial liabilities into relevant maturity groupings based on the remaining period at the end of the reporting period to the contractual maturity date. The amounts disclosed in the tables are the contractual undiscounted cash flows.

Group	**Less than 3 months**	**Between 3 months and 1 year**	**Between 1 year and 5 years**	**More than 5 years**	**Total**
At 31 December 2021	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Financial liabilities					
Amounts owed to banks	**1,224**	-	-	-	**1,224**
Amounts owed to customers	**667,887**	**66,930**	**196,949**	**70,328**	**1,002,094**
Total financial liabilities	**669,111**	**66,930**	**196,949**	**70,328**	**1,003,318**
At 31 December 2020					
Financial liabilities					
Amounts owed to banks	5,602	-	-	-	5,602
Amounts owed to customers	669,960	71,009	170,317	51,232	962,518
Total financial liabilities	675,562	71,009	170,317	51,232	968,120

Bank	**Less than 3 months**	**Between 3 months and 1 year**	**Between 1 year and 5 years**	**More than 5 years**	**Total**
At 31 December 2021	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Financial liabilities					
Amounts owed to banks	**1,224**	**-**	**-**	**-**	**1,224**
Amounts owed to customers	**668,907**	**67,133**	**196,949**	**70,328**	**1,003,317**
Total financial liabilities	**670,131**	**67,133**	**196,949**	**70,328**	**1,004,541**
At 31 December 2020					
Financial liabilities					
Amounts owed to banks	5,602	-	-	-	5,602
Amounts owed to customers	675,330	73,012	170,317	51,232	969,891
Total financial liabilities	680,932	73,012	170,317	51,232	975,493

2 Financial risk management *(continued)*

2.6 Operational risk

Operational risk is the risk of losses due to:

- deficient or erroneous internal procedures;
- human or system errors;
- external events, including legal events;
- internal and external fraud;
- employment practices and workplace safety;
- clients, products and business practices;
- damage to physical assets;
- business disruption and system failures; and
- execution, delivery and process management.

Operational risk is thus often associated with specific and one-off events, such as failure to observe business or working procedures, defects or breakdowns of the technical infrastructure, criminal acts, fire and storm damage or litigation. Operational risks are, thus, non-financial risks. Operational risk management relies on a framework of policies implemented by the different operational functions and which implementation is overseen by the Risk Management Function.

A financial measurement of this risk is arrived at by the Group for the purpose of allocating risk capital using the Basic Indicator Approach under the European Union Directive on Capital Requirements (CRD) rules. The capital requirement for operational risk under this method was calculated at €4,107,000 (2020: €3,997,000).

In 2021, the COVID-19 pandemic situation was constantly monitored and when COVID-19 cases started to rise, the pandemic business contingency plan was triggered. Where possible, employees were asked to work remotely, and the remaining staff were working on a rotation basis and dispersed to allow sufficient social distance. Contingency sites and equipment were tested regularly. The Executive Committee maintained regular meetings to analyse the situation and provide direction accordingly. No major disruption to the business was experienced.

2.7 Capital risk management

The Group's objectives when managing capital, which is a broader concept than the 'equity' on the consolidated statement of financial position, are:

- to comply with the capital requirements set by the MFSA with respect to the Bank's operations;
- to safeguard the Group's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- to maintain a strong capital base to support the development of its business.

Accordingly, the purpose of the Group's capital management is essentially that of ensuring efficient use of capital taking cognisance of the Group's risk appetite and profile as well as its objectives for business development. The Group is subject to externally imposed capital requirements only in respect of the Bank's activities as a credit institution. The Bank is a licensed financial services provider and must therefore comply with the capital requirements under the relevant laws and regulations.

The Bank's Executive Team and ALCO are responsible for managing the Bank's regulatory capital. The Bank aims to maintain a strong capital base to support the risks inherent in its business, investing in accordance with its strategy and meeting regulatory capital requirements at all times. Internal capital adequacy assessments are aligned with the regulatory and supervisory requirements and with the Bank's assessment of risk, including credit, market and operational risks.

The Bank manages its capital requirements based on internal targets, which are set above the prescribed minimum capital requirements, i.e. levels established within the Capital Requirement Regulation ('CRR') and the additional capital requirements established by the MFSA for supervisory purposes.

2 **Financial risk management** *(continued)*

The following is an analysis of the Bank's Capital Base in accordance with the CRD's requirements:

	2021	2020
	€ 000	€ 000
Common Equity Tier 1 (CET1) capital		
Share capital	**11,192**	11,044
Share premium	**18,530**	18,530
Revaluation and other reserves	**20,828**	17,076
Retained earnings	**81,452**	74,692
	132,002	121,342
Adjustments:		
Final dividend (note 36)	**(873)**	(861)
Depositor Compensation Scheme	**(2,959)**	(2,925)
Intangible assets	**(122)**	(246)
Other regulatory adjustments	**2,097**	2,483
Total CET1 capital	**130,145**	119,793
Total own funds	**130,145**	119,793

Minimum capital requirements are computed for credit, market and operational risks. The Banking Act, 1994 requires a bank to maintain a ratio of total regulatory capital to risk-weighted assets and instruments (the Capital requirements ratio) at or above the prescribed minimum of 8%.

The Bank is compliant with the CRD IV capital requirements and in addition to the prescribed minimum, Banking Rule BR/15: 'Capital Buffers of Credit Institutions authorised under the Banking Act 1994' requires Banks to hold additional buffers, namely the 'capital conservation buffer' and the 'countercyclical buffer'. Automatic restrictions on capital distributions apply if the Bank's CET1 capital falls below the level of its CRD IV combined buffer.

The Bank is required to maintain a capital conservation buffer of 2.5% and the institution-specific countercyclical buffer as determined by Article 140 (1) of Directive 2013/36/EU which is composed of CET1 capital. These buffers were phased in over the period from 1 January 2016 to 31 December 2020.

CRD IV contemplates a countercyclical buffer in line with Basel III, in the form of an institution-specific countercyclical buffer and the application of increased requirements to address macro-prudential or systemic risk. This is expected to be set in the range of 0-2.5% of relevant credit exposure risk-weighted assets, whereby the rate shall consist of the weighted average of the 'countercyclical buffer' rates that apply in the jurisdiction where the relevant exposures are located. Given that the local group's exposures are all contained within Malta, this buffer was set at 0%.

In June 2021, the Bank received from the MFSA a SREP Decision letter, whereby in addition to the regulatory requirements stated above, the Bank is expected to maintain a Pillar 2 Requirement (P2R) of 3.25% to be held in excess of the minimum own funds requirement and to be maintained at all times in accordance with Article 104a of the EU's Capital Requirements Directive (CRD V). In addition, a Pillar 2 Guidance (P2G) of 1% and made up entirely of CET 1 Capital is to be held over and above the Overall Capital Requirement (OCR) of 13.75%.

During the financial years ended 31 December 2021 and 31 December 2020, the bank has met all external capital requirements at all times.

The Capital requirements ratio expresses Own funds as a proportion of risk-weighted assets and off-balance sheet instruments in relation to Credit Risk together with notional risk-weighted assets in respect of Operational Risk and Market Risk.

2 **Financial risk management** *(continued)*

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of – and reflecting an estimate of credit, market and other risks associated with – each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet instruments, with some adjustments to reflect the more contingent nature of the potential losses. Risk-weighted assets are measured using the 'Standardised Approach' for credit risk with risk-weights being assigned to assets and off-balance sheet instruments according to their asset class and credit risk mitigation. For the determination of credit assessments, independent rating agencies are nominated as required.

Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 (i.e. the reciprocal of the minimum capital ratio of 8%) and adding the resulting figures to the sum of risk-weighted assets for credit risk.

2.8 Fair values of financial assets and liabilities

2.8.1 Financial instruments measured at fair value

The Group's financial instruments which are carried at fair value include the Group's financial assets measured at FVOCI (note 6). The Group is required to disclose fair value measurements by level of the following fair value measurement hierarchy for financial instruments that are measured in the statement of financial position at fair value:

- Quoted prices (unadjusted) in active markets for identical assets (Level 1).
- Inputs other than quoted prices included within Level 1 that are observable for the asset either directly i.e. as prices, or indirectly i.e. derived from prices (Level 2).
- Inputs for the asset that are not based on observable market data i.e. unobservable inputs (Level 3).

The IFRS 7 hierarchy of valuation techniques is based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions.

The Bank considers only relevant and observable market prices in its valuations. Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations.

The fair value of the Bank's financial assets measured at FVOCI, which are principally traded in active markets, is mainly based on quoted market prices. Hence, as at 31 December 2021 and 2020, the principal financial instruments that are measured at fair value, consisting of the investments measured at FVOCI, were valued using principally Level 1 inputs.

No transfers of financial instruments between different levels of the fair value hierarchy have occurred during the financial years ended 31 December 2021 and 2020.

2.8.2 Financial instruments not measured at fair value

Loans and advances to banks and customers

These categories of assets are presented net of impairment allowances to reflect the estimated recoverable amounts. As at 31 December 2021, the Group's aggregate carrying amount in this respect was €721,172,000 (2020: €718,114,000). The loans and advances to customers, which are principally subject to floating interest rates, are measured at the amount of €545,126,000 (2020: €512,930,000). This carrying value approximates to fair value in view of the fact that these loans and advances are repriceable at the Group's discretion. The loans and advances to banks, comprising term placements maturing within one month from the end of the reporting period, are carried at the amount of €42,255,000 (2020: €49,726,000). Rates on advances reflect current market rates, and the Directors consider the carrying amounts to be a reasonable estimate of their fair value principally in view of the relatively short periods to repricing or maturity from the end of the reporting periods. The current market interest rates utilised for fair value estimation, which reflect essentially the respective instruments' contractual interest rates, are deemed observable and accordingly these fair value estimates have been categorised as Level 2.

Trade and other receivables

This category principally represents short-term trade receivables arising from postal operations in respect of which the carrying amount is a reasonable approximation of its fair value.

2 **Financial risk management** *(continued)*

Amounts owed to banks and customers

These categories of financial liabilities are carried at amortised cost and amount to €978,367,000 as at 31 December 2021 (2020: €946,712,000), 15.7% (2020: 14.2%) of this liability is non-interest bearing, 52.7% (2020: 57.0%) of the liability has a contractual repricing term of three months or less, 6.8% (2020: 7.4%) reprices between three months and one year, 18.7% (2020: 16.8%) reprices between one year and five years while 6.1% (2020: 4.7%) is repriceable after more than five years. Accordingly, in view of their profile, the fair value of these financial liabilities is not deemed to be significantly different from their carrying amounts. This applies to variable rate deposits in view of the short periods to repricing, but also applies to liabilities subject to fixed interest rates, based on discounting future contractual cash flows at current market interest rates, taking into account the short periods to maturity. The current market interest rates utilised for discounting purposes, which were almost equivalent to the respective instruments' contractual interest rates, are deemed observable and accordingly these fair value estimates have been categorised as Level 2.

Other financial instruments

The fair values of certain other financial assets, including balances with the Central Bank of Malta and accrued income, are considered to approximate their respective carrying values due to their short-term nature.

3 **Accounting estimates and judgements**

3.1 Critical accounting estimates and judgements in applying the Group's accounting policies

Estimates and judgements are continually evaluated and based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. These estimates and assumptions present a risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. The Group's management also makes judgements, apart from those involving estimations, in the process of applying the entity's accounting policies that may have a significant effect on the amounts recognised in the financial statements.

3.2 Measurement of the Expected Credit Losses

The measurement of the Expected Credit Loss allowance for financial assets measured at amortised cost and FVOCI is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour. Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is further detailed in note 2.

A number of significant judgements are required in measurement of Expected Credit Loss, such as:

- Determining criteria for significant increase in credit risk;
- Choosing appropriate models and assumptions for the measurement of ECL; and
- Establishing the number and relative weightings of forward-looking scenarios and associated ECL.

As previously explained, the level of uncertainly in the estimation of the Bank's expected credit loss allowances has increased in the financial years ended 31 December 2021 and 2020 as a result of the economic effects of the outbreak of the COVID-19 pandemic.

Detailed information about the judgements and estimates made by the Bank in the above areas is set out in note 2.

3.3 Assessment of estimates and judgements

In the opinion of the Directors, the accounting estimates and judgements made in the course of preparing these consolidated financial statements, which have been highlighted above, are not difficult, subjective or complex to a degree which would warrant their description as critical in terms of the requirements of IAS 1.

3 **Accounting estimates and judgements** *(continued)*

However, the Directors would like to draw attention to these accounting judgements that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In this respect these primarily comprise assumptions and estimates relating to the calculation of impairment allowances in respect of loans and advances to customers (see notes 2.3, 8 and 31).

The COVID-19 pandemic and the economic distress it created has elevated the level of estimation uncertainty and judgement, especially in light of the inability to track observable historical trends which can be reflected in ECL modelling that could accurately represent the financial implications brought about by the pandemic. Hence, the level of subjectivity underlying the ECL model parameters, including how these react to forward-looking economic conditions remains high.

The exercise of judgement in making estimations requires the use of assumptions that are highly subjective and very sensitive to the risk factors, detailed in note 2.3.4. In addition, many of the factors have a high degree of interdependency and there is no single factor to which loan impairment allowances as a whole is sensitive.

A key judgement in the context of the COVID-19 pandemic is whether the heightened level of macroeconomic uncertainty and its effects are more likely to be temporary or prolonged. The shape of recovery is also a significant uncertainty. This in turn increases significantly the level of subjectivity around the estimation of credit loss allowances in respect of loans and advances to customers. Although the effective implementation of vaccination roll-out programmes has amongst other factors, led to an economic recovery during 2021, the level of subjectivity around the estimation of credit loss allowances remains significant, particularly due to successive waves of infections, the potential mutation of COVID-19 variants, the efficacy of such vaccines/boosters upon the emergence of new virus strains, and the unwinding of Government support schemes and regulatory relief measures.

In this regard, management applied a higher level of expert judgement in order to assess the impact of the pandemic on the Bank's level of defaults, including evaluating the impact of government support schemes and regulatory relief measures on both the incidence of default events and the severity of losses as described below.

The identification of customers experiencing significant increase in credit risk or credit impairment in the context of the elevated level of uncertainty is highly judgemental due to limitations in available credit information on customers. This is particularly relevant in those instances where customers have accepted payment deferrals and other relief designed to address short-term liquidity issues or have extended those deferrals. In response to such limitations, management used segmentation techniques for the purposes of identifying indicators of significant increase in credit risk within both corporate and retail portfolios.

As previously explained in view of the nature of the Bank's portfolio, where a relatively small number of loans comprise a significant proportion of the loan book value, during the past two years the Bank continued to apply an individual-debtor-focused credit management process.

In relation to retail portfolios, ECL models are generally reliant on the assumption that default emergence is directly impacted by delinquency related indicators since less information is available at asset level to enable the timely identification of a SICR or UTP events. In this respect, a set of criteria which considered the current level of income of the borrower, the economic sector in which the same borrower is employed and the LTV of the exposure were established to determine if borrowers which were granted a general payment moratorium (note 2.3.9) exhibited signs of SICR or UTP. With respect to borrowers who have not requested a moratorium, the Bank continued to apply rigorously its credit assessment and oversight processes, which include monitoring of arrears and exposure LTV.

Judgement was also required in determining whether corporate loans experienced a SICR or a UTP event. In this respect, as part of management's response to the COVID-19 pandemic, the Bank assessed all borrowers which were granted a general payment moratorium (note 2.3.9) within the corporate portfolio. As part of these credit assessments, judgement is exercised in evaluating all relevant information on indicators of impairment, particularly where factors indicate deterioration in the financial condition and outlook of borrowers affecting their ability to pay. The Bank also considered potential heightened credit risk factors emanating from exposures not subject to a general payment moratorium in the process of its ongoing credit review process and through focused economic concentration exposure.

For individually significant credit impaired loans, management determines the size of the allowance required based on a range of factors such as the realisable value of security, the viability of the customer's business model and the capacity to generate cash flow to service debt obligations, under different scenarios. Judgement is applied in estimating the expected future cash flows from each borrower and the time to recover these cash flows under the different scenarios as well as to attach probabilities to those scenarios.

3 **Accounting estimates and judgements** *(continued)*

The assumptions around forecasted recoveries from the sale of collateralised properties, including around valuation haircuts and time to recovery, are key drivers in the estimation of credit loss allowances in respect of individually assessed loans. The heightened level of uncertainty within the local property market, driven by the pandemic, increases the level of expert judgement required to predict with reasonable accuracy the recoverability of exposures through the sale of collateral, since the real impact of the pandemic will not be fully known until market conditions stabilise.

As previously explained, following the expiration of all general payment moratoria during 2021, a post- model mechanism was enhanced to estimate the impact of delayed emergence of default in view of government support measures which were still in force during the current financial year and also the potential economic impact of Malta's grey-listing by the FATF.

Specifically, the mechanism devised by management considers an overlay which increases the level of expected credit losses on performing (Stage 1) exposures within both the corporate and retail portfolios, which allowances would have otherwise being subjected to a higher decrease in expected credit losses, driven by the forecasted macroeconomic model inputs (note 2.3.4.4). The overlay, which is in the region of €3 million, is based on specific expert-based assumptions intended to account for expected losses which could arise on performing exposures, after taking cognisance of the prevailing level of uncertainty in respect of the duration and economic impact of the pandemic, the other developments referred to above, and the level of coverage of expected credit losses on Stage 1 exposures.

To reflect the volatile economic conditions associated with the COVID-19 pandemic, judgemental overlays were also applied by management in respect of individually significant credit-impaired loans in order to overcome limitations in respect of determining collateral valuations, and the uncertainty around the time to repossess properties held as collateral and to resell such properties in the open market.

The level of expert judgement required in selection of macroeconomic scenarios and the respective probability weights is exacerbated by the heightened level of uncertainty around predictions in respect of the potential impacts of epidemiological assumptions in relation to the pandemic, of the efficacy of vaccines/boosters upon the emergence of new virus strains, and of the effectiveness of government support schemes and regulatory relief measures together with the impacts of their unwinding, on key macroeconomic variables and, as a result on forward-looking PDs and LGDs. As alluded to earlier, there is an absence of an observable historical trend that can accurately represent the severity and speed of the economic impacts brought about by the pandemic. The complexities of government support schemes and their unwinding, regulatory guidance on the treatment of customer impacts (such as forbearance) and the unpredictable pathways of the pandemic taking cognisance of potential new virus strains, have never been modelled. Consequently, in some cases, the bank's IFRS 9 models generate outputs that appear overly sensitive when compared with other credit risk metrics and as a result, modelled assumptions and linkages between economic factors and credit losses may underestimate or overestimate ECL in these conditions.

In addition to the above, Malta's grey-listing by the FATF during the financial year ended 31 December 2021 has compounded the level of economic uncertainty within the local market. The estimated economic impact of the grey-listing remains difficult to gauge, since this is highly dependent on the speed at which Malta exits grey-listing, the effectiveness of national efforts to address the findings, as well as the response from foreign investors. Significant judgement is required in order to assess the potential impact of the FATF grey-listing on the local economy.

Accordingly, in view of the matters highlighted above, expert judgement was applied by management when determining the appropriateness of selected macroeconomic scenarios and their respective probability weights.

The model limitations have been addressed through the enhancements described in note 2.3.4.4. In view of the above, management considered the sensitivity of the ECL outcome to the macro-economic forecasts by recalculating the ECL under the different scenarios, applying a 100% weighting to each scenario. The effect of economic uncertainty on the ECL outcome is disclosed in the sensitivity analysis presented in note 2.3.4.4 within the section entitled 'Economic scenarios sensitivity analysis of ECL estimates'. The ECL calculated for the upside and downside scenarios should not be taken to represent the upper and lower limits of possible ECL outcomes as there is a high degree of estimation uncertainty in the numbers representing tail risk scenarios when assigned a 100% weighting.

4 Segmental information

The Group has two reporting segments, as described below, which are the Group's strategic business units and cash-generating units. The strategic business units offer different services and are managed separately because they require different technology and marketing strategies. For each of the strategic business units, the Board of Directors reviews internal management reports.

The following summary describes the operations in each of the Group's reportable segments:

- Banking services comprise the Group's banking services and other activities carried out as a licensed credit institution, an authorised currency dealer and financial intermediary. Stockbroking activities may also be carried out since the Bank is a member of the Malta Stock Exchange; and
- Postal services comprise the Group's postal services activities, being the sole licensed Universal Service Provider of postal services in Malta.

The Group's internal reporting to the Board of Directors and senior executives is analysed according to the below segments. Information about reportable segments:

	Banking services		Postal services		Total	
	2021	2020	**2021**	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000	**€ 000**	€ 000
Interest receivable	**25,586**	24,749	**139**	149	**25,725**	24,898
Interest expense	**(6,115)**	(5,964)	**(54)**	(62)	**(6,169)**	(6,026)
Postal sales and other revenue	**180**	626	**37,190**	33,519	**37,370**	34,145
Net fee and commission income	**4,126**	3,623	**1,085**	1,116	**5,211**	4,739
Other operating income/(expense)	**902**	2,653	**25**	(67)	**927**	2,586
Segment operating income	**24,679**	25,687	**38,385**	34,655	**63,064**	60,342
Depreciation and amortisation	**(917)**	(772)	**(1,802)**	(1,495)	**(2,719)**	(2,267)
Credit impairment reversals/(losses)	**1,464**	(3,946)	**(2)**	(27)	**1,462**	(3,973)
Employee compensation and benefits	**(8,195)**	(7,646)	**(16,165)**	(15,112)	**(24,360)**	(22,758)
Other costs	**(6,557)**	(5,732)	**(17,849)**	(15,089)	**(24,406)**	(20,821)
Operating profit	**10,474**	7,591	**2,567**	2,932	**13,041**	10,523
Share of loss of investment accounted for using the equity method, net of tax	**(185)**	-	**(217)**	(151)	**(402)**	(151)
Profit before taxation	**10,289**	7,591	**2,350**	2,781	**12,639**	10,372
Income tax expense	**(3,809)**	(2,213)	**(951)**	(1,017)	**(4,760)**	(3,230)
Profit for the year	**6,480**	5,378	**1,399**	1,764	**7,879**	7,142
Segment total assets	**1,123,219**	1,084,409	**52,172**	46,546	**1,175,391**	1,130,955
Capital expenditure during the year	**3,728**	6,610	**3,374**	2,327	**7,102**	8,937
Segment total liabilities	**1,006,210**	977,815	**23,411**	19,378	**1,029,621**	997,193

There are no material inter-segment transactions.

The Group mainly provides banking and postal services within the local market and economic sectors. From a customers' perspective, during 2021 MaltaPost p.l.c. generated 53.4% (2020: 48.4%) of its revenue internationally.

The Group's reliance on any single customer is not considered significant for disclosure purposes.

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

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Balances with Central Bank of Malta	**71,805**	68,417	**71,805**	68,417
Malta Government treasury bills	**47,590**	93,655	**47,590**	93,655
Cash in hand	**6,884**	7,615	**6,157**	6,576
	126,279	169,687	**125,552**	168,648

The balances with the Central Bank of Malta include a reserve deposit amounting to €50,104,000 (2020: €36,216,000) held in terms of Regulation (EC) No.1745/2003 of the European Central Bank. The average reserve deposit balance held for the relevant maintenance period amounted to €7,396,000 (2020: €7,068,000).

At 31 December 2021, the Bank had pledged a deposit with the Central Bank of Malta amounting to €2,139,000 (2020: €2,809,000) in favour of the Depositor Compensation Scheme to comply with local regulatory requirements.

As at 31 December 2021 and 2020, the credit loss allowance on balances with Central Bank of Malta and Malta Government treasury bills was insignificant.

6 Investments

Financial investments measured at FVOCI include the following:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Debt and other fixed income instruments	**218,080**	152,182	**215,179**	148,621
Equity instruments	**9,421**	9,242	**9,421**	9,242
	227,501	161,424	**224,600**	157,863

Debt and other fixed income instruments measured at FVOCI are analysed as follows:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Issued by public bodies:				
- local government	**168,145**	104,389	**166,483**	102,310
- foreign government	**8,679**	6,468	**8,679**	6,468
Issued by public issuers:				
- local banks	**13,020**	12,738	**12,440**	12,170
- local corporates	**5,714**	5,334	**5,055**	4,420
- foreign banks	**14,169**	12,949	**14,169**	12,949
- foreign corporates	**8,353**	10,304	**8,353**	10,304
	218,080	152,182	**215,179**	148,621

As at 31 December 2021, the credit loss allowance measured in accordance with IFRS 9 expected loss model was €464,000 (2020: €808,000).

6 **Investments** *(continued)*

At 31 December 2021, the Bank held Malta Government Stocks investments measured at FVOCI pledged with the Central Bank of Malta, with a carrying amount of €10,575,000 (2020: €9,874,000), in terms of Directive No.8 (Chapter 204 of the Central Bank of Malta Act) as security for a facility that was not utilised during the reporting period.

The debt securities held by the Group are listed on the Malta Stock Exchange, a regulated market in Malta, or on other recognised exchanges.

Equity instruments measured at FVOCI consist of equities listed on the Malta Stock Exchange, except for investments with a carrying amount of €366,000 (2020: €342,000) which are measured at cost in view of the absence of a reliable fair valuation of these investments.

The movement in debt and other fixed income financial investments measured at FVOCI is summarised as follows:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
At 1 January	**152,182**	100,945	**148,621**	97,020
Amortisation	**(1,103)**	(807)	**(1,101)**	(807)
Acquisitions	**75,271**	67,862	**75,271**	67,814
Redemptions/disposals	**(6,819)**	(13,566)	**(6,219)**	(13,335)
Fair value movement	**(2,711)**	(1,659)	**(2,653)**	(1,529)
Other movements	**1,260**	(542)	**1,260**	(542)
At 31 December	**218,080**	152,182	**215,179**	148,622

The movement in equity financial investments measured at FVOCI is summarised as follows:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
At 1 January	**9,242**	10,786	**9,242**	10,786
Acquisitions	**-**	51	**-**	51
Redemptions/disposals	**-**	(1,501)	**-**	(1,501)
Fair value movement	**149**	(14)	**149**	(14)
Other movements	**30**	(80)	**30**	(80)
At 31 December	**9,421**	9,242	**9,421**	9,242

The disclosure requirements emanating from IFRS 13 in respect of equity investments measured at FVOCI were not deemed necessary by the directors taking cognisance of the immateriality of the carrying amount of these equity investments as at 31 December 2021 and 2020.

7 **Loans and advances to banks**

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Repayable on call and at short notice	**59,253**	77,062	**55,398**	75,218
Term loans and advances	**19,026**	19,923	**13,026**	18,423
	78,279	96,985	**68,424**	93,641

8 Loans and advances to customers

	Group 2021 € 000	Group 2020 € 000	Bank 2021 € 000	Bank 2020 € 000
Repayable on call and at short notice	**97,898**	102,543	**97,900**	102,546
Term loans and advances	**570,617**	544,500	**570,617**	544,500
Gross loans and advances to customers	**668,515**	647,043	**668,517**	647,046
Credit loss allowances	**(25,622)**	(25,914)	**(25,622)**	(25,914)
Net loans and advances to customers	**642,893**	621,129	**642,895**	621,132
Credit loss allowances				
Stage 1	**5,187**	6,200	**5,187**	6,200
Stage 2	**3,361**	2,799	**3,361**	2,799
Stage 3	**17,074**	16,915	**17,074**	16,915
	25,622	25,914	**25,622**	25,914

Assets acquired in settlement of debt amounting to €661,000 (2020: €134,000) are presented as assets classified as held for sale.

9 Investment in subsidiaries

Name of company	Country of incorporation	Nature of business	Equity interest 2021 %	Equity interest 2020 %	Carrying amount 2021 € 000	Carrying amount 2020 € 000
Redbox Limited	Malta	Holding Company	**100**	100	**15,732**	15,732
Lombard Capital Asset Management Ltd	Malta	Asset management	**100**	-	**125**	-
Lombard Select SICAV p.l.c.	Malta	Asset management	**100**	-	**21**	-

At 31 December 2021, Redbox Limited held 71.5% (2020: 71.5%) of the equity share capital and voting rights of MaltaPost p.l.c., a listed company incorporated and operating in Malta, comprising the Group's postal services reportable segment (see note 4). The remaining 28.5% (2020: 28.5%) is held by the general public.

The profit or loss allocated to non-controlling interests of MaltaPost p.l.c. during the financial year under review, accumulated non-controlling interests of the subsidiary at the end of the reporting period and dividends paid to non-controlling interests are presented within the Group's statement of changes in equity. Financial information about the assets, liabilities, revenues, profit or loss, total comprehensive income and cash flows of the subsidiary are disclosed within the annual report and financial statements of MaltaPost p.l.c., which are publicly available in view of the company's listed status. Financial information about the subsidiary is also disclosed within note 4 to these financial statements dealing with segmental information. The non-controlling interests of this subsidiary are not deemed material to the reporting entity with respect to the Bank's consolidated financial statements for the purpose of disclosures in terms of the requirements of IFRS 12 "Disclosure of interests in other entities".

The end of the reporting period of the audited financial statements of MaltaPost p.l.c. and its associate IVALIFE Insurance Limited that have been utilised in the preparation of these consolidated financial statements is 30 September 2021, since the financial statements prepared as of this date constitute the most recent audited financial statements of the respective companies.

9 **Investment in subsidaries** *(continued)*

Acquisition of controlling stake in subsidiaries

Ciantar Brothers Limited

On 26 April 2021, MaltaPost p.l.c. entered into a share purchase agreement with the shareholders of Ciantar Brothers Limited (CBL), a limited liability company registered in Malta, with registration number C 577 and registered office at 22, Warehouse il-Moll tal-Pont, Marsa MRS1400, for the purchase of 100% of the entity's issued share capital for a cash consideration of €140,000. The transfer of shares was effected on 6 May 2021. The purchase consideration was deemed equivalent to the fair value of the 100% equity holding in CBL and accordingly of the identifiable assets and liabilities of CBL as at date of acquisition, which principally comprised intangible assets.

CBL did not operate during the twelve-month period to 30 September 2021. CBL is principally engaged in leasing warehouse space, a service offering that is ancillary to services currently provided by MaltaPost p.l.c. This acquisition is expected to give rise to synergies within the Group. The impact of this acquisition on the Bank's consolidated financial statements for the year ended 31 December 2021 is considered insignificant.

PostaInsure Agency Limited

On 5 November 2020, MaltaPost p.l.c. entered into a share purchase agreement with PostaInsure Agency Limited (PostaInsure), formerly Untours Insurance Agents Limited, a limited liability company registered in Malta under the Companies Act (Cap.386), with registration number C 5655 and registered office at 4, Old Bakery Street, Valletta, for the purchase of 49% of the issued share capital for a consideration of €275,000. The transfer of shares was effected on 9 December 2020, at which date MaltaPost p.l.c. also acquired control over the entity in view of its rights to appoint 60% of the members of PostaInsure's Board of Directors.

The purchase consideration was deemed equivalent to the fair value of the 49% equity holding in PostaInsure.

The assets and liabilities recognised as a result of the acquisition are as follows:

	Fair Value € 000
Property, plant and equipment	4
Deferred tax	103
Trade and other receivables	439
Current tax receivable	5
Cash and cash equivalents	1,108
Trade and other payables	(996)
Net identifiable assets acquired	**662**
Less: non-controlling interest	**(387)**
Net assets acquired	**275**

Non-controlling interests have been measured at the related proportion of the net identifiable assets at acquisition.

Net cash inflow arising from acquisition of subsidiary is as follows:

	€ 000
Cash consideration	(275)
Balances acquired	
Cash and cash equivalents	1,108
	833

9 **Investment in subsidaries** *(continued)*

PostaInsure is principally engaged in providing general insurance services, a service offering that is ancillary to services currently provided by MaltaPost p.l.c. This acquisition is expected to give rise to synergies within the Group. The impact of this acquisition on the Bank's consolidated financial statements for the years ended 31 December 2020 and 2021 is considered insignificant.

Lombard Select SICAV p.l.c. and Lombard Capital Asset Management Limited

In February 2021, the Bank established two wholly-owned subsidiaries, namely Lombard Select SICAV p.l.c. and Lombard Capital Asset Management Limited. The impact of these additional investments on the Group's financial results and financial position as reflected in the financial statements for the current financial year is insignificant, as by 31 December 2021 the entities had not yet started operating.

Lombard Select SICAV p.l.c. will be a Retail Collective Investment Scheme in terms of applicable law on undertakings for collective investment in transferable securities. Lombard Capital Asset Management Limited will be a UCITS management company which will primarily provide investment management services to collective investment schemes, carry on such other investment services business in terms of its licence and provide any ancillary services.

10 **Investment in associates**

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
At 1 January	**1,932**	1,684	**1,645**	1,645
Additions	**1,476**	399	**-**	-
Share of results	**(402)**	(151)	**-**	-
At 31 December	**3,006**	1,932	**1,645**	1,645
At 31 December				
Cost	**3,520**	2,044	**1,645**	1,645
Share of results	**(514)**	(112)	**-**	-
Carrying amount	**3,006**	1,932	**1,645**	1,645

The Group's associates at 31 December 2021 and 2020 are shown below:

Name of company	**Country of incorporation**	**Nature of business**	**Equity interest**		**Carrying amount**	
			2021	2020	**2021**	2020
			%	%	**€ 000**	€ 000
Gozo Hotels Company Limited	Malta	Accommodation	**33.3**	33.3	**1,499**	1,684
IVALIFE Insurance Limited	Malta	Insurance	**25.0**	25.0	**1,507**	248

MaltaPost p.l.c. controls 25% of the share capital (and holds an equivalent amount of voting rights) of IVALIFE Insurance Limited, an unlisted company which was incorporated in Malta towards the end of 2019 and commenced operations in 2021. The company was established to provide Class I and Class III long term business of insurance within Malta with a registered office at 'Gaba Buildings', Level 2, Naxxar Road, Iklin, Malta. During 2021 financial year, MaltaPost p.l.c. further injected capital amounting to €1,476,000 in its associate IVALIFE Insurance Limited. The Group's 25% share of the losses registered by the associate during the current financial year, amounting to €368,000, was reflected within the Group's 2021 financial results.

The associate's capital and reserves as at 30 September 2021 stood at €6,029,000 (2020: €897,735) and the entity registered a loss for the year amounting to €861,000 (2020: €602,265).

10 **Investment in associates** *(continued)*

In previous financial years the exposure with Gozo Hotels Company Limited with a carrying amount of €1,645,000 had been recognised as an investment in associate on the basis that the Bank controls 33.3% of the shares (and holds an equivalent amount of voting rights). The Group is deemed to have significant influence over the investee in accordance with the requirements of IAS 28 'Investments in Associates'. The Group's share of losses registered by the entity during the current year, amounting to €146,000, was reflected within the Group's 2021 financial result in respect of this investment.

Gozo Hotels Company Limited is an unlisted company incorporated and operating in Malta. Its principal activity is the operation of the Hotel Calypso in Marsalforn, Gozo, and its registered address is 'Calypso', Ghar Qawqla Street, Zebbug, Gozo.

The associate's capital and reserves as at 31 December 2020 stood at €4,496,254 (2019: €5,067,967) and the entity registered a loss for the year amounting to €571,713 (2019: €88,434).

These associates are not considered material for the reporting entity, with respect to the Bank's consolidated financial statements, as at 31 December 2021 for the purposes of disclosures in terms of the requirements of IFRS 12 "Disclosure of interests in other entities".

11 **Intangible assets**

	Group				Bank
	Goodwill € 000	**Computer software € 000**	**Other intangible assets € 000**	**Total € 000**	**Computer software € 000**
At 1 January 2020					
Cost	857	6,363	-	7,220	3,388
Accumulated amortisation	-	(5,220)	-	(5,220)	(2,989)
Net book amount	857	1,143	-	2,000	399
Year ended 31 December 2020					
At 1 January 2020	857	1,143	-	2,000	399
Additions	-	617	-	617	30
Disposal	-	(490)	-	(490)	-
Amortisation for the year	-	(567)	-	(567)	(183)
Amortisation release of disposal	-	490	-	490	-
At 31 December 2020	857	1,193	-	2,050	246
At 31 December 2020					
Cost	857	6,490	-	7,347	3,418
Accumulated amortisation	-	(5,297)	-	(5,297)	(3,172)
Net book amount	857	1,193	-	2,050	246
Year ended 31 December 2021					
At 1 January 2021	**857**	**1,193**	**-**	**2,050**	**246**
Additions	**-**	**635**	**-**	**635**	**3**
Amortisation of subsidiary	**-**	**-**	**140**	**140**	**-**
Amortisation for the year	**-**	**(662)**	**(18)**	**(680)**	**(127)**
At 31 December 2021	**857**	**1,166**	**122**	**2,145**	**122**
At 31 December 2021					
Cost	**857**	**7,125**	**140**	**8,122**	**3,422**
Accumulated amortisation	**-**	**(5,959)**	**(18)**	**(5,977)**	**(3,300)**
Net book amount	**857**	**1,166**	**122**	**2,145**	**122**

11 **Intangible assets** *(continued)*

11.1 *Impairment test for the cash-generating unit to which goodwill has been allocated*

The recognised goodwill represents payments made by the Group in anticipation of future economic benefits from assets that are not capable of being individually identified and separately recognised. As at 31 December 2021 and 2020 the recognised goodwill amounted to €857,000 and related to the acquisition of MaltaPost p.l.c.

In applying the requirements of IAS 36, 'Impairment of assets', in relation to goodwill arising in business combinations, the Directors carried out an impairment test at the end of the reporting period to obtain comfort that the recoverable amount of the cash-generating unit to which goodwill has been allocated is at least equal to its carrying amount.

The recoverable amount of the cash-generating unit is based on fair value less costs to sell.

This calculation takes into account the market capitalisation of MaltaPost p.l.c. based on the quoted price of its equity on the Malta Stock Exchange at a price per share of €1.22 as at 31 December 2021 (2020: €1.33). On this basis, the recoverable amount of the cash-generating unit is higher than its carrying amount.

12 **Property, plant and equipment**

Group	**Land and buildings € 000**	**Computer equipment € 000**	**Other € 000**	**Total € 000**
Year ended 31 December 2020				
At 1 January 2020	38,712	760	3,876	43,348
Additions	7,602	367	1,051	9,020
Disposals	(2)	(950)	(966)	(1,918)
Depreciation charge for the year	(450)	(368)	(622)	(1,440)
Depreciation released on disposals	2	950	966	1,918
At 31 December 2020	45,864	759	4,305	50,928
At 31 December 2020				
Cost or valuation	48,189	4,035	12,900	65,124
Accumulated depreciation	(2,325)	(3,276)	(8,595)	(14,196)
Net book amount	45,864	759	4,305	50,928
Year ended 31 December 2021				
At 1 January 2021	**45,864**	**759**	**4,305**	**50,928**
Revaluation surplus arising during the year:				
Effect on cost or valuation	**7,998**	**-**	**-**	**7,998**
Effect on accumulated depreciation	**479**	**-**	**-**	**479**
Additions	**6,779**	**393**	**691**	**7,863**
Acquisition of subsidiary	**-**	**-**	**116**	**116**
Disposals	**-**	**(20)**	**(8)**	**(28)**
Depreciation charge for the year	**(848)**	**(371)**	**(818)**	**(2,037)**
Depreciation released on disposals	**-**	**19**	**8**	**27**
At 31 December 2021	**60,272**	**780**	**4,294**	**65,346**
At 31 December 2021				
Cost or valuation	**62,958**	**4,407**	**13,703**	**81,068**
Accumulated depreciation	**(2,686)**	**(3,627)**	**(9,409)**	**(15,722)**
Net book amount	**60,272**	**780**	**4,294**	**65,346**

12 **Property, plant and equipment** *(continued)*

Bank	**Land and buildings € 000**	**Computer equipment € 000**	**Other € 000**	**Total € 000**
Year ended 31 December 2020				
At 1 January 2020	22,735	456	345	23,536
Additions	7,036	266	207	7,509
Disposals	-	(7)	(67)	(74)
Depreciation charge for the year	(292)	(201)	(106)	(599)
Depreciation released on disposals	-	7	67	74
At 31 December 2020	29,479	521	446	30,446
At 31 December 2020				
Cost or valuation	30,767	2,431	2,756	35,954
Accumulated depreciation	(1,288)	(1,910)	(2,310)	(5,508)
Net book amount	29,479	521	446	30,446
Year ended 31 December 2021				
At 1 January 2021	**29,479**	**521**	**446**	**30,446**
Revaluation surplus arising during the year:				
Effect on cost or valuation	**6,513**	**-**	**-**	**6,513**
Effect on accumulated depreciation	**330**	**-**	**-**	**330**
Additions	**4,635**	**289**	**171**	**5,095**
Disposals	**-**	**(11)**	**(8)**	**(19)**
Depreciation charge for the year	**(441)**	**(232)**	**(126)**	**(799)**
Depreciation released on disposals	**-**	**11**	**8**	**19**
At 31 December 2021	**40,516**	**578**	**491**	**41,585**
At 31 December 2021				
Cost or valuation	**41,910**	**2,709**	**2,919**	**47,538**
Accumulated depreciation	**(1,394)**	**(2,131)**	**(2,428)**	**(5,953)**
Net book amount	**40,516**	**578**	**491**	**41,585**

Land and buildings presented in the tables above include improvements to leasehold properties as follows:

	Group		**Bank**	
	2021 € 000	2020 € 000	**2021 € 000**	2020 € 000
At 1 January	**2,318**	2,357	**1,578**	1,632
Additions	**17**	120	**-**	-
Depreciation charge for the year	**(214)**	(159)	**(49)**	(54)
At 31 December	**2,121**	2,318	**1,529**	1,578

Property, plant and equipment of the Group and the Bank includes right-of-use assets of €4,613,000 (2020: €3,759,000) and €3,141,000 (2020: €2,026,000) respectively, as disclosed in note 13.

12 **Property, plant and equipment** *(continued)*

12.1 Fair valuation of land and buildings

The Bank's land and buildings were revalued on 25 May 2021 while the subsidiary's land and buildings were revalued on 30 September 2021, by an independent firm of property valuers having appropriate recognised professional qualifications and experience in the location and category of the property being valued. The Directors have reviewed the carrying amounts of the Group's properties, on the basis of the valuations carried out by the independent property valuers.

Valuations were made on the basis of open market value taking cognisance of the specific location of the properties, the size of the sites, the availability of similar properties in the area, and whenever possible, having regard to recent market transactions for similar properties in the same location. During 2021, the carrying values of the properties, classified within property, plant and equipment, have been adjusted to the valuations and the net resultant adjustment comprised an increase of €8,478,000 in the carrying values for the Group and an increase of €6,844,000 in the carrying values for the Bank, to reflect the property's estimated open market value on an individual asset level. This increase was recognised in other comprehensive income in the property revaluation reserve.

The revaluation surplus net of applicable deferred income taxes is accordingly shown in 'other reserves' in shareholders' equity (note 19).

The Group is required to analyse non-financial assets carried at fair value by level of the fair value hierarchy within which the recurring fair value measurements are categorised in their entirety (Level 1, 2 or 3). The different levels of the fair value hierarchy have been defined as fair value measurements using:

- Quoted prices (unadjusted) in active markets for identical assets (Level 1);
- Inputs other than quoted prices included within Level 1 that are observable for the asset, either directly (i.e. as prices) or indirectly (i.e. derived from prices) (Level 2);
- Inputs for the asset that are not based on observable market data (i.e. unobservable inputs) (Level 3).

The Bank's land and buildings comprise various offices and operational premises, including the Bank's head office. The subsidiary's land and buildings, within property, plant and equipment, comprises the head office, mail delivery hubs and retail outlets. All the Group's recurring property fair value measurements use significant unobservable inputs and are accordingly categorised within Level 3 of the fair valuation hierarchy.

The Group's policy is to recognise transfers into and out of fair value hierarchy levels as of the beginning of the reporting period. There were no transfers between different levels of the fair value hierarchy during the years ended 31 December 2021 and 2020.

A reconciliation from the opening balance to the closing balance of land and buildings for recurring fair value measurements categorised within Level 3 of the value hierarchy, is reflected in the table above. The principal movements reflect changes in fair value, additions and depreciation charge for the years ended 31 December 2021 and 2020.

For all Group properties, their current use equates to the highest and best use.

12.2 Valuation processes

The valuations of the properties are performed on a periodic basis taking into consideration the valuation reports prepared by independent and qualified valuers. These reports are based on both:

- information provided by the Bank such as current terms and conditions of lease agreements. This information is derived from the Bank's systems and is subject to the Bank's overall control environment; and
- assumptions and valuation models used by the valuers – the assumptions are typically market related, such as rental yields, discount rates and sales prices. These are based on professional judgement and market observation.

The information provided to the valuers – and the assumptions and the valuation models used by the valuers – are reviewed by management.

When management considers that the valuation report is appropriate, the valuation report is considered by the Audit & Risk Committee as part of its monitoring responsibility for effective financial reporting.

12.3 Valuation techniques

The Level 3 fair valuation of the Bank's property was determined using discounted cash flow (DCF) projections based on significant unobservable inputs. These inputs include estimated rental values per square metre, estimated growth rate in rental values and the discount rate applied.

The external valuations of the subsidiary's Level 3 property have been performed using an adjusted sales comparison approach for the land component and the replacement cost approach for the buildings component.

In view of a limited number of similar sales in the local market, the valuations have predominately been performed using unobservable inputs. The significant input to the adjusted sales comparison approach is generally a sales price per square metre related to transactions in comparable properties located in proximity to the subsidiary's property, with significant adjustments for differences in size, age, exact location and condition of the property. The significant input to the replacement cost approach is the estimated development costs per square metre.

12.4 Information about fair value measurements using significant unobservable inputs (Level 3)

			Range of significant unobservable inputs		
				Weighted	
Description by class based on highest and best use	**Fair value**	**Valuation technique**	**Rental value €/sqm**	**Growth rate %**	**Discount rate %**
Current use as Bank's offices and operational premises	€26.4 million	Discounted cash flow approach	370	2	5

Description by class based on highest and best use	**Fair value**	**Valuation technique**	**Significant unobservable input**	**Range of unobservable inputs €**
Current use as subsidiary's office premises, retail outlets and mail delivery hubs	€17.8 million	Adjusted sales comparison approach	Sales price per square metre	1,200 - 4,400

The higher the rental value or the growth rate, the higher the resultant fair value. Conversely, the lower the discount rate, the higher the resultant fair value.

The higher the sales price per square metre or the development costs per square metre, the higher the resultant fair valuation.

12.5 Historical cost of land and buildings

If the land and buildings were stated on the historical cost basis, the carrying amounts would be as follows:

	Group		**Bank**	
	2021 € 000	2020 € 000	**2021 € 000**	2020 € 000
Cost	**37,105**	31,871	**23,581**	20,316
Accumulated depreciation	**(2,788)**	(2,450)	**(2,263)**	(2,000)
Net book amount at 31 December	**34,317**	29,421	**21,318**	18,316

13 Leases

The Group leases various locations for offsite ATMs, offices and branches as well as low value items such as IT equipment. Rental contracts are typically made for fixed periods but may have extension options. Extension and termination options are included in a number of property leases across the Group. These are used to maximise operational flexibility in terms of managing the assets used in the Group's operations. The majority of extension and termination options held are exercisable only by the Group and not by the respective lessor. Most extension options in property and motor vehicle leases have been included in the lease liability as the lease term reflects the exercise of such options.

Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants other than the security interests in the leased assets that are held by the lessor. Leased assets may not be used as security for borrowing purposes.

Leases are recognised as a right-of-use asset within 'Property, plant and equipment' (note 12) and a corresponding liability at the date at which the leased asset is available for use by the Group within 'Other liabilities' (note 23).

	Group			**Bank**
	Buildings	**Other**	**Total**	**Buildings**
	€ 000	**€ 000**	**€ 000**	**€ 000**
Year ended 31 December 2020				
At 1 January 2020	2,891	313	3,204	1,239
Additions	970	2	972	930
Depreciation charge for the year	(360)	(57)	(417)	(143)
At 31 December 2020	3,501	258	3,759	2,026
At 31 December 2020				
Cost or valuation	3,900	315	4,215	2,219
Accumulated depreciation	(399)	(57)	(456)	(193)
Net book amount	3,501	258	3,759	2,026
Year ended 31 December 2021				
At 1 January 2021	**3,501**	**258**	**3,759**	**2,026**
Additions	**1,396**	**-**	**1,396**	**1,370**
Depreciation charge for the year	**(480)**	**(61)**	**(541)**	**(255)**
At 31 December 2021	**4,417**	**197**	**4,614**	**3,141**
At 31 December 2021				
Cost or valuation	**5,290**	**315**	**5,605**	**3,582**
Accumulated depreciation	**(873)**	**(118)**	**(991)**	**(441)**
Net book amount	**4,417**	**197**	**4,614**	**3,141**

13 **Leases** *(continued)*

The Group and the Bank's lease liabilities are presented below:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Lease liabilities				
Current	**366**	352	**104**	97
Non-current	**4,015**	3,484	**2,781**	1,999
	4,381	3,836	**2,885**	2,096

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Lease liabilities				
At beginning of year	**3,836**	3,269	**2,096**	1,261
Additions	**945**	929	**920**	929
Payments	**(523)**	(480)	**(203)**	(152)
Interest charge	**123**	118	**72**	58
At end of year	**4,381**	3,836	**2,885**	2,096

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
The income statement reflects the following amounts relating to leases:				
Depreciation charge of right-of-use assets	**541**	417	**255**	143
Interest expense	**123**	118	**72**	58
Expense relating to short-term leases (included in administrative expenses)	**473**	565	**83**	194
Expense relating to leases of low-value assets that are not shown above as short-term leases (included in administrative expenses)	**293**	265	**50**	44

The total cash payments for leases, included short-term and low-value leases, in 2021 was €1,227,000 (2020: €1,244,000) for the Group and €318,000 (2020: €285,000) for the Bank.

There were no expenses relating to variable lease payments which were not included in the measurement of lease liabilities.

In 2021 and 2020 no income was earned from subleasing of right-of-use assets and no gains or losses were made from sale and leaseback transactions.

14 Deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

Group	Assets 2021 € 000	Liabilities 2021 € 000	Net 2021 € 000	Assets 2020 € 000	Liabilities 2020 € 000	Net 2020 € 000
Differences between depreciation and capital allowances	**86**	**(117)**	**(31)**	95	(105)	(10)
Provisions for liabilities and charges	**441**	**-**	**441**	633	-	633
Impairment allowances	**9,252**	**-**	**9,252**	9,389	-	9,389
Revaluation of property	**-**	**(4,099)**	**(4,099)**	-	(2,661)	(2,661)
Fair value movements on investments	**-**	**(2,628)**	**(2,628)**	-	(3,682)	(3,682)
	9,779	**(6,844)**	**2,935**	10,117	(6,448)	3,669

Bank	Assets 2021 € 000	Liabilities 2021 € 000	Net 2021 € 000	Assets 2020 € 000	Liabilities 2020 € 000	Net 2020 € 000
Differences between depreciation and capital allowances	**-**	**(117)**	**(117)**	-	(106)	(106)
Provisions for liabilities and charges	**128**	**-**	**128**	316	-	316
Impairment allowances	**9,155**	**-**	**9,155**	9,353	-	9,353
Revaluation of property	**-**	**(2,800)**	**(2,800)**	-	(1,633)	(1,633)
Fair value movements on investments	**-**	**(2,628)**	**(2,628)**	-	(3,682)	(3,682)
	9,283	**(5,545)**	**3,738**	9,669	(5,421)	4,248

Movement in deferred tax assets and liabilities relate to:

Group

	At 1 January 2020 € 000	Recognised in profit or loss € 000	Recognised in other comprehensive income € 000	**At 31 December 2020 € 000**	**Recognised in profit or loss € 000**	**Recognised in other comprehensive income € 000**	**Aquisition of subsidaries € 000**	**At 31 December 2021 € 000**
Differences between depreciation and capital allowances	22	(32)	-	**(10)**	**(64)**	**-**	**42**	**(32)**
Provisions for liabilities and charges	796	(116)	(47)	**633**	**(192)**	**-**	**-**	**441**
Credit loss allowances	8,874	515	-	**9,389**	**(198)**	**-**	**61**	**9,252**
Revaluation of property	(2,661)	-	-	**(2,661)**	**-**	**(1,438)**	**-**	**(4,099)**
Fair value movements on investments	(4,062)	-	380	**(3,682)**	**-**	**1,055**	**-**	**(2,628)**
	2,969	367	333	**3,669**	**(454)**	**(383)**	**103**	**2,935**

14 Deferred tax assets and liabilities *(continued)*

Bank

	At 1 January 2020 € 000	Recognised in profit or loss € 000	Recognised in other comprehensive income € 000	**At 31 December 2020 € 000**	**Recognised in profit or loss € 000**	**Recognised in other comprehensive income € 000**	**Recognised on acquisition € 000**	**At 31 December 2021 € 000**
Differences between depreciation and capital allowances	(109)	3	-	**(106)**	**(13)**	**-**	**-**	**(119)**
Provisions for liabilities and charges	411	(95)	-	**316**	**(187)**	**-**	**-**	**129**
Credit loss allowances	8,847	506	-	**9,353**	**(199)**	**-**	**-**	**9,154**
Revaluation of property	(1,633)	-	-	**(1,633)**	**-**	**(1,166)**	**-**	**(2,799)**
Fair value movements on investments	(4,062)	-	380	**(3,682)**	**-**	**1,055**	**-**	**(2,627)**
	3,454	414	380	**4,248**	**(399)**	**(111)**	**-**	**3,738**

The recognised deferred tax assets and liabilities are expected to be recovered or settled principally after more than twelve months from the end of the reporting period. The deferred tax liabilities reflected in other comprehensive income relate principally to the revaluation of property, plant and equipment and the fair valuation of investments measured at FVOCI (note 34).

15 Inventories

	Group		**Bank**	
	2021 € 000	2020 € 000	**2021 € 000**	2020 € 000
Postal supplies and materials	**288**	282	**-**	-
Merchandise	**411**	437	**-**	-
Stocks for resale	**567**	509	**567**	509
Other stock items	**58**	46	**58**	46
	1,324	1,274	**625**	555

16 Trade and other receivables

	Group		**Bank**	
	2021 € 000	2020 € 000	**2021 € 000**	2020 € 000
Trade receivables - net of expected credit loss allowances	**5,004**	3,409	**-**	-
Others	**5,783**	5,727	**1,606**	1,761
	10,787	9,136	**1,606**	1,761

16 **Trade and other receivables** *(continued)*

The Expected Credit Loss allowances in respect of trade receivables are analysed as follows:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Loss allowance as at 1 January	**104**	77	**-**	-
Acquisition of subsidiary	**172**	-	**-**	-
Net charge recognised in profit or loss during the year	**1**	27	**-**	-
Loss allowance as at 31 December	**277**	104	**-**	-

17 **Accrued income and other assets**

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Accrued income	**1,946**	2,204	**1,912**	2,164
Prepayments	**1,171**	1,054	**581**	494
Other assets	**1,053**	1,079	**1,053**	1,079
	4,170	4,337	**3,546**	3,737

18 **Share capital**

Bank	**2021**		2020	
	No. of shares 000s	**€ 000**	No. of shares 000s	€ 000
Authorised				
Ordinary shares of 25 cent each	**80,000**	**20,000**	80,000	20,000
Issued				
Ordinary shares of 25 cent each	**44,767**	**11,192**	44,178	11,044

By virtue of a resolution dated 28 May 2021, the shareholders of the Bank approved the allotment of 589,047 ordinary shares of 25 cents each as a bonus issue of one (1) share for every (75) shares held by shareholders on the Company's Register of Shareholders as at close of business on 23 June 2021, and thereby increased the issued and fully paid share capital to 44,766,961 shares of 25 cent each, resulting in a paid up share capital of €11,191,740.

19 Reserves

These reserves are non-distributable.

19.1 Share premium

The share premium arises on premium attributable to the scrip issue of ordinary shares. Utilisation of the share premium account is governed by the requirements of Article 114 within the Companies' Act, Chapter 386 of the Laws of Malta.

19.2 Revaluation and other reserves

The Group and the Bank had the following reserves as at end of the reporting period:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Property revaluation reserve	**13,041**	6,383	**10,122**	4,444
Investment revaluation reserve	**5,179**	7,181	**4,845**	6,805
Reserve for General Banking Risks	**2,903**	2,903	**2,903**	2,903
Other reserve	**2,545**	2,511	**2,958**	2,924
	23,668	18,978	**20,828**	17,076

The property revaluation reserve relates to the fair valuation of the land and buildings component of property, plant and equipment, and the balance represents the cumulative net increase in fair value of such property, net of related deferred tax.

The investment revaluation reserve represents the cumulative net change in fair values of financial assets measured at FVOCI held by the Group and by the Bank, net of related deferred tax impacts.

Banking Rule BR 09 'Measures addressing credit risks arising from the assessment of the quality of asset portfolios of credit institutions authorised under the Banking Act 1994', issued by the MFSA, requires banks in Malta to hold additional reserves for general banking risks in respect of non-performing loans. This reserve is required to be funded from planned dividends.

The other reserve represents amounts set aside by the Bank from its retained earnings in relation to the Depositor Compensation Scheme reflecting the carrying amount of assets pledged in favour of the Scheme to comply with local regulatory requirements.

20 Amounts owed to banks

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Term deposits with agreed maturity dates or periods of notice	**23**	23	**23**	23
Repayable on demand	**1,201**	5,579	**1,201**	5,579
	1,224	5,602	**1,224**	5,602

21 Amounts owed to customers

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Term deposits with agreed maturity dates	**358,094**	317,534	**358,294**	321,634
Repayable on demand	**619,049**	623,576	**620,071**	626,844
	977,143	941,110	**978,365**	948,478

22 Provisions for liabilities and other charges

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Obligation to Government	**1,678**	1,728	**-**	-
Legal	**366**	616	**366**	615
Other Expected Credit Losses on off-balance sheet items	**69**	288	**69**	288
	2,113	2,632	**435**	903

These provisions are predominantly non-current in nature.

Group	**2021**				2020			
	Obligation to Government	**Legal**	**Expected Credit Loss allowance**	**Total**	Obligation to Government	Legal	Expected Credit Loss allowance	Total
	€ 000	**€ 000**	**€ 000**	**€ 000**	€ 000	€ 000	€ 000	€ 000
At 1 January	**1,728**	**616**	**288**	**2,632**	2,009	1,186	41	3,236
Exchange differences recognised in profit or loss	**-**	**-**	**-**	**-**	-	(37)	-	(37)
Actuarial gains - recognised in other comprehensive income	**-**	**-**	**-**	**-**	(133)	-	-	(133)
Charge/(reversal) - recognised in profit or loss	**115**	**(250)**	**-**	**(135)**	35	80	-	115
Crystallised obligations	**(165)**	**-**	**-**	**(165)**	(183)	(613)	-	(796)
Change in ECL provision on off-balance sheet items	**-**	**-**	**(219)**	**(219)**	-	-	247	247
At 31 December	**1,678**	**366**	**69**	**2,113**	1,728	616	288	2,632

The obligation to Government arises in terms of Article 8A of the Pensions Ordinance (Chapter 93 of the Laws of Malta), covering former Government employees who opted to become full-time employees of MaltaPost p.l.c., and who continued to be entitled to pension benefits which go beyond the National Insurance Scheme. The pension benefits scheme is a final salary defined benefit plan and is unfunded.

Obligation to Government recognised in the statement of financial position is derived as follows:

	2021	2020
	€ 000	€ 000
Present value of unfunded obligations	**3,988**	3,873
Crystallised obligations	**(1,611)**	(1,446)
Fair value of obligations to be reimbursed by Government	**(699)**	(699)
	1,678	1,728

The amounts recognised in other comprehensive income are as follows:

	2021	2020
	€ 000	€ 000
Net actuarial gains		
- attributable to financial assumptions	**-**	133
	-	133

22 Provisions for liabilities and other charges *(continued)*

In computing the provision, the Group used a weighted average discount rate of 1.46% (2020: 1.41%). Assumptions regarding future mortality experience are based on published mortality tables in Malta, which translate into an average life expectancy of 83 (2020: 83) depending on age and gender of the beneficiaries.

These factors are deemed to be the main assumptions used in the computation of the liability. The sensitivity of the obligation to changes in these assumptions is considered immaterial for disclosure purposes.

Bank

		2021			2020	
	Legal	**Expected Credit Loss allowance**	**Total**	Legal	Expected Credit Loss allowance	Total
	€ 000	**€ 000**	**€ 000**	€ 000	€ 000	€ 000
At 1 January	**616**	**287**	**903**	1,132	41	1,173
Exchange differences recognised in profit or loss	**-**	**-**	**-**	18	-	18
Reversal/(charge) - recognised in profit or loss	**(250)**	**-**	**(250)**	79	-	79
Crystallised obligations	**-**	**-**	**-**	(613)	-	(613)
Change in ECL provision on off-balance sheet items	**-**	**(218)**	**(218)**	-	246	246
At 31 December	**366**	**69**	**435**	616	287	903

In addition, the Bank is also a defendant in legal actions by other customers as a result of which the Directors are of the opinion that no liability will be incurred.

23 Other liabilities

	Group		**Bank**	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Trade payables	**7,762**	5,697	**-**	-
Bills payable	**3,248**	5,169	**3,248**	5,169
Cash Collateral	**969**	1,253	**969**	1,253
Lease liabilities	**4,381**	3,836	**2,885**	2,096
Other payables	**14,289**	13,710	**7,670**	10,324
	30,649	29,665	**14,772**	18,842

24 Accruals and deferred income

	Group		**Bank**	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Accrued interest	**5,674**	5,125	**5,674**	5,126
Other	**5,165**	5,767	**1,597**	1,317
	10,839	10,892	**7,271**	6,443

25 Commitments and contingent liabilities

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Contingent liabilities				
Guarantee obligations incurred on behalf of third parties	**9,155**	8,549	**9,320**	8,681
Documentary credits	**4,040**	2,302	**4,040**	2,302
	13,195	10,851	**13,360**	10,983
Commitments				
Credit facilities and other commitments to lend	**195,264**	197,180	**196,372**	198,288
Capital commitments	**584**	3,690	**41**	1,929
	195,848	200,870	**196,413**	200,217

Credit facilities and other commitments to lend funds to customers are granted at prevailing market interest rates at drawdown date.

Capital commitments as at 31 December 2021 and 2020 mainly relate to the acquisition of property, plant and equipment.

Total future minimum lease net payments under non-cancellable property operating leases, with a lease term of less than 12 months, are as follows:

	2021	2020
	€ 000	€ 000
Current		
Within 1 year	**608**	572

Specific lease agreements include an option to renew the lease after the original term but the amounts presented in the table above do not reflect payments subsequent to renewal.

The Group is also committed to pay a licence fee of 1.50% (2020: 1.50%) of its total gross revenue from postal services within the scope of the universal services.

26 Net interest income

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Interest income				
On loans and advances to banks	**(5)**	230	**(42)**	199
On loans and advances to customers	**23,826**	22,984	**23,826**	22,984
On balances with Central Bank of Malta	**42**	54	**42**	54
On Malta Government treasury bills	**(412)**	(469)	**(412)**	(469)
	23,451	22,799	**23,414**	22,768
On debt and other fixed income instruments	**3,377**	2,906	**3,275**	2,788
Net amortisation of premiums and discounts	**(1,103)**	(807)	**(1,101)**	(805)
	2,274	2,099	**2,174**	1,983
Total interest income	**25,725**	24,898	**25,588**	24,751
Interest expense				
On amounts owed to customers	**(6,046)**	(5,908)	**(6,048)**	(5,910)
On leases	**(123)**	(118)	**(72)**	(58)
Total interest expense	**(6,169)**	(6,026)	**(6,120)**	(5,968)
Net interest income	**19,556**	18,872	**19,468**	18,783

27 Net fee and commission income

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Fee and commission income				
Retail banking customer fees	**3,007**	2,754	**3,007**	2,754
Brokerage	**53**	81	**53**	81
Other	**2,364**	2,165	**1,281**	1,052
Total fee and commission income	**5,424**	5,000	**4,341**	3,887
Fee and commission expense				
Inter-bank transaction fees	**(198)**	(247)	**(198)**	(247)
Other	**(15)**	(14)	**(15)**	(14)
Total fee and commission expense	**(213)**	(261)	**(213)**	(261)
Net fee and commission income	**5,211**	4,739	**4,128**	3,626

28 Postal sales and other revenues

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Stamps, parcel post and postal stationery including income from foreign inbound mail	**32,552**	29,436	**-**	-
Collectibles and philatelic sales	**882**	1,026	**518**	786
Other	**3,937**	3,683	**-**	-
	37,371	34,145	**518**	786

29 Dividend income

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Subsidiary undertaking	**-**	-	**1,657**	1,657
Equity shares measured at FVOCI	**80**	105	**81**	105
	80	105	**1,738**	1,762

30 Net trading income

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Gains on foreign exchange activities	**615**	539	**590**	607

31 Employee compensation and benefits

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Staff costs				
Wages, salaries and allowances	**22,756**	21,229	**7,772**	7,254
Social security costs	**1,604**	1,529	**423**	392
	24,360	22,758	**8,195**	7,646

	Group		Bank	
	2021	2020	**2021**	2020
Average number of employees				
Executives and senior managerial	**44**	45	**36**	37
Other managerial, supervisory and clerical	**468**	237	**160**	148
Others	**496**	631	**7**	8
	1,008	913	**203**	193

32 Credit impairment losses

Credit impairment losses during 2021 were as follows:

	Group			Bank		
	Write-downs € 000	Reversals of write-downs € 000	Total € 000	Write-downs € 000	Reversals of write-downs € 000	Total € 000
Trade receivables						
Stage 3	(2)	-	(2)	-	-	-
Total trade receivables	(2)	-	(2)	-	-	-
Loans and advances to customers						
Stage 1	-	1,013	1,013	-	1,013	1,013
Stage 2	(562)	-	(562)	(562)	-	(562)
Stage 3	-	453	453	-	453	453
Total loans and advances to customers	(562)	1,466	904	(562)	1,466	904
Financial investments measured at FVOCI						
Stage 1	-	344	344	-	344	344
Total financial investments measured at FVOCI	-	344	344	-	344	344
Off-balance sheet items						
Stage 1	-	228	228	-	228	228
Stage 2	(11)	-	(11)	(11)	-	(11)
Stage 3	-	1	1	-	1	1
Total off-balance sheet items	(11)	229	218	(11)	229	218
Credit impairment losses	(575)	2,039	1,464	(573)	2,039	1,466

32 Credit impairment losses *(continued)*

Credit impairment losses during 2020 were as follows:

	Group			Bank		
	Write-downs € 000	Reversals of write-downs € 000	Total € 000	Write-downs € 000	Reversals of write-downs € 000	Total € 000
Trade receivables						
Stage 3	(27)	-	(27)	-	-	-
Total trade receivables	(27)	-	(27)	-	-	-
Loans and advances to customers						
Stage 1	(2,368)	-	(2,368)	(2,368)	-	(2,368)
Stage 2	(1,453)	-	(1,453)	(1,453)	-	(1,453)
Stage 3	-	747	747	-	747	747
Total loans and advances to customers	(3,821)	747	(3,074)	(3,821)	747	(3,074)
Financial investments measured at FVOCI						
Stage 1	(625)	-	(625)	(625)	-	(625)
Total financial investments measured at FVOCI	(625)	-	(625)	(625)	-	(625)
Off-balance sheet items						
Stage 1	(245)	-	(245)	(245)	-	(245)
Stage 3	(2)	-	(2)	(2)	-	(2)
Total off-balance sheet items	(247)	-	(247)	(247)	-	(247)
Credit impairment losses	(4,720)	747	(3,973)	(4,693)	747	(3,946)

33 Profit before taxation

Profit before taxation is stated after charging and crediting the following:

	Group		Bank	
	2021 € 000	2020 € 000	**2021 € 000**	2020 € 000
After charging				
Directors' emoluments				
- fees	**93**	73	**69**	49
- other emoluments	**392**	393	**388**	389
After crediting				
Net income from investment services	**380**	222	**380**	222

33 Profit before taxation *(continued)*

Other operating costs are analysed as follows:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Foreign outbound mail	**11,269**	8,901	**-**	-
Utilities and insurance	**1,430**	1,164	**1,031**	747
IT support and telecommunication costs	**459**	470	**282**	278
Repairs and maintenance	**2,256**	2,095	**937**	869
Operating lease rental charges	**1,223**	1,127	**615**	554
Other administrative expenses	**7,907**	6,949	**4,264**	3,721
Total other operating costs	**24,544**	20,706	**7,129**	6,169

Other administrative expenses mainly comprise professional expenses, subcontracted services and other services or expense items which are incurred in the course of the operations of the Group and the Bank.

Fees charged by the parent company auditor for services rendered during the financial years ended 31 December 2021 and 2020 relate to the following:

	Audit	Other assurance/ advisory services	Tax compliance services
	€ 000	**€ 000**	**€ 000**
Bank			
2021	**90**	**-**	**4**
2020	98	-	5
Subsidiary companies			
2021	**71**	**38**	**5**
2020	29	18	5

During the current year fees amounting to €75,800 (2020: €1,200) have been charged to the Bank by connected undertakings of the Bank's auditor, in respect of regulatory advisory services and compliance services.

During the current year fees amounting to €23,500 (2020: nil) have been charged to the subsidiary companies by connected undertakings of the subsidiaries' auditor, in respect of regulatory advisory services and tax advisory and compliance services.

34 Income tax expense

Recognised in profit or loss:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Current taxation				
Current tax expense	**4,305**	3,597	**3,990**	3,206
Deferred taxation				
Deferred tax charge/(income) (note 14)	**454**	(367)	**399**	(414)
	4,759	3,230	**4,389**	2,792

The tax on the profit before income tax differs from the theoretical amount that would arise using the tax rate applicable as follows:

	Group		Bank	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Profit before tax	**12,638**	10,372	**12,193**	9,251
Tax on profit at 35%	**4,507**	3,630	**4,267**	3,238
Tax effect of:				
Income not subject to tax	**(24)**	(23)	**(10)**	(23)
Expenses non-deductible for tax purposes	**236**	156	**208**	134
Income taxed at different tax rates	**(31)**	(454)	**(1)**	(419)
Share of results of associate	**76**	53	**-**	-
Other differences	**(5)**	(132)	**(75)**	(138)
	4,759	3,230	**4,389**	2,792

The tax impacts, which are entirely attributable to deferred taxation, relating to components of other comprehensive income and accordingly presented directly in equity are as follows:

Group	**2021**			2020		
	Before tax	**Tax credit /(charge)**	**Net of tax**	Before tax	Tax credit/ (charge)	Net of tax
	€ 000	**€ 000**	**€ 000**	€ 000	€ 000	€ 000
Fair valuation of land and buildings	**8,486**	**(1,438)**	**7,048**	-	-	-
Fair valuation of financial assets measured at FVOCI:						
- Net changes in fair value	**(2,562)**	**876**	**(1,686)**	(170)	15	(155)
- Reclassification adjustments to profit or loss on disposal	**(168)**	**58**	**(110)**	(167)	59	(108)
- Net movement attributable to change in credit risk	**(344)**	**121**	**(223)**	625	(219)	406
Remeasurements of defined benefit obligations	**-**	**-**	**-**	133	(47)	86
Other	**-**	**-**	**-**	18	-	18
	5,412	**(383)**	**5,029**	439	(192)	247

34 **Income tax expense** *(continued)*

Bank	**2021**			2020		
	Before tax	**Tax credit /(charge)**	**Net of tax**	Before tax	Tax credit/ (charge)	Net of tax
	€ 000	**€ 000**	**€ 000**	€ 000	€ 000	€ 000
Fair valuation of land and buildings	**6,844**	**(1,166)**	**5,678**	-	-	-
Fair valuation of financial assets measured at FVOCI:						
- Net changes in fair value	**(2,504)**	**876**	**(1,628)**	(42)	15	(27)
- Reclassification adjustments to profit or loss upon disposal	**(168)**	**59**	**(109)**	(167)	59	(108)
- Net changes attributable to change in credit risk	**(343)**	**120**	**(223)**	625	(219)	406
	3,829	**(111)**	**3,718**	416	(145)	271

35 **Earnings per share**

Earnings per share is based on the net profit for the year divided by the weighted average number of ordinary shares in issue during the year.

	Group	
	2021	2020 Restated
Net profit attributable to equity holders of the Bank (€ 000)	**7,481**	6,640
Number of ordinary shares in issue	**44,484,541**	44,484,541
Earnings per share (€ cent)	**16c8**	14c9

The comparative information in the table above has been restated to reflect the bonus issue effected during the current financial year and the impact on the number of shares in issue, referred to in note 18, retrospectively.

The Bank has no instruments or arrangements which give rise to dilutive potential ordinary shares, and accordingly diluted earnings per share is equivalent to basic earnings per share.

36 **Dividends**

	2021	2020
Dividends declared and paid by the Bank (€ 000)	**862**	-
€ per share – gross	**3c0**	-

On 27 July 2020, the European Central Bank ('ECB') issued a Recommendation on dividend distributions during the COVID-19 pandemic and repealing Recommendation ECB/2020/19 (ECB/2020/35), which inter-alia recommended that no dividends be paid out by credit institutions until 1 January 2021 and that no irrevocable commitment to pay out dividends be undertaken by credit institutions for the financial years 2019 and 2020.

On the basis of this, during August 2020 the Board of Directors resolved to withdraw its recommendation of 23 March 2020 for the payment of a final gross dividend of 7 cent per nominal 25 cent share (net dividend of 4.55 cent for a total amount of €2,010,095) for the twelve months ended 31 December 2019.

36 **Dividends** *(continued)*

On 15 December 2020, the ECB issued another Recommendation on dividend distributions during the COVID-19 pandemic repealing Recommendation ECB/2020/35 (ECB/2020/62), which encourages prudence on the part of credit institutions when deciding on or paying out dividends. In this respect, the ECB generally considers distributions exceeding the lower of 15% of accumulated profit for the financial years ended 31 December 2019 and 2020 and 20 basis points in terms of the Common Equity Tier 1 ratio to lack prudence. On the basis of this, a gross dividend of 3 cent per nominal 25 cent share (net dividend of 1.95 cent for a total amount of €861,469) for the twelve months ended 31 December 2020 was paid during the current financial year.

On 23 July 2021, the ECB issued another Recommendation repealing Recommendation ECB/2020/62 (ECB/2021/31) with effect from 30 September 2021.

The Board has resolved that a gross dividend of 3 cent per nominal 25 cent share (net dividend of 1.95 cent for a total amount of €872,956) in respect of the financial year ended 31 December 2021 is being proposed. The final dividend will be paid to shareholders who are on the Bank's register of shareholders at 26 April 2022 subject to approval by the Annual General Meeting scheduled for 26 May 2022. This dividend will be reflected as an appropriation of retained earnings during the financial year ending 31 December 2022.

37 **Cash and cash equivalents**

Cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

	Group		**Bank**	
	2021	2020	**2021**	2020
	€ 000	€ 000	**€ 000**	€ 000
Malta Government treasury bills (note 5)	**26,029**	93,655	**26,029**	93,655
Loans and advances to banks (notes 5 and 7)	**134,548**	114,437	**130,694**	112,594
Cash (note 5)	**6,885**	7,615	**6,157**	6,576
Amounts owed to banks (note 20)	**(1,202)**	(5,580)	**(1,202)**	(5,580)
Cash and cash equivalents	**166,260**	210,127	**161,678**	207,245

38 **Related parties**

38.1 Identity of related parties

The Bank considers that it has a related party relationship with the National Department and Social Fund (as from 10th August 2018), its associated companies, the Bank's Directors and Chief Officers (deemed to be key management personnel, which category comprises Chief Executive Officer, Chief Officer – Credit, Chief Operations Officer, Chief Financial Officer, Chief Information Officer) and other related parties, principally entities controlled by key management personnel.

The Government of Malta is also considered to be a related party, through its control over the National Development and Social Fund. Nevertheless, in its Company Announcement dated 10 August 2018, the Bank reported that the NDSF had reaffirmed that:

Quote

- it does not intend to increase its holdings in the Bank;
- it shall not act in concert with any other shareholders;
- it will seek to reduce its shareholding in the Bank in an orderly manner, at the right market conditions and by agreement with the regulatory authorities;
- it has no intention of exerting any influence on the operations of the Bank; and
- this acquisition will not result in a change in control of the Bank.

38 **Related parties** *(continued)*

Unquote

The Group's exposure with the Government of Malta arises through its investment in Government debt securities and treasury bills which are disclosed in note 6 and other obligations disclosed in note 22.

Related party transactions with government owned/controlled entities were carried out on an arm's length basis and on normal commercial terms.

38.2 Transaction arrangements and agreements involving key management personnel and entities controlled by the latter

	2021	2020
	€ 000	€ 000
Income statement		
Interest payable	**5**	5
Interest receivables	**400**	311
Administrative expenses	**950**	916

	2021	2020
	€ 000	€ 000
Statement of financial position		
Loans and advances to customers	**11,123**	9,674
Trade and other receivables	**10**	13
Amounts owed to customers	**1,970**	1,416
Accruals and deferred income	**2**	3
Contingent liabilities	**9**	7
Commitments	**1,512**	1,945

	Loans and advances 2021 € 000	**Commitments 2021 € 000**	Loans and advances 2020 € 000	Commitments 2020 € 000
At 1 January	**9,674**	**(1,952)**	6,678	(4,428)
Additions	**3,396**	**(273)**	4,015	(301)
Reductions/ repayments	**(1,946)**	**704**	(1,019)	2,777
At 31 December	**11,123**	**(1,521)**	9,674	(1,952)

The above banking facilities are part of long-term commercial relationships and were made in the ordinary course of business on substantially the same terms, including rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

38.3 Compensation to key management personnel

Directors' remuneration and salaries to executive officers amounts to €549,402 (2020: €514,548).

38 **Related parties** *(continued)*

38.4 Transactions with other related parties

38.4.1 Subsidiaries

Information relating to transactions undertaken by the Bank with its subsidiary companies during the year:

	2021	2020
	€ 000	€ 000
Income statement		
Fee and commission income	**1**	2
Postal sales and other income	**24**	1
Other operating income	**56**	369
Interest payable	**2**	2
Administrative expenses	**540**	162
Statement of financial position		
Loans and advances to customers	**2**	2
Trade and other receivables	**83**	366
Amounts owed to customers	**1,222**	7,369
Accruals and deferred income	**37**	69
Contingent liabilities	**165**	132
Commitments	**1,108**	1,108

During the year, Redbox Limited received gross dividends from MaltaPost p.l.c. amounting to €1,657,000 (2020: €1,657,000).

38.4.2 Associates

Information relating to transactions undertaken by the Bank with its associates during the year:

	2021	2020
	€ 000	€ 000
Income statement		
Interest receivable and similar income	**19**	19
Statement of financial position		
Loans and advances to customers	**1,900**	1,900
Investment in associate	**1,645**	1,645
Prepayments and accrued income	**470**	450

39 **Investor compensation scheme**

In accordance with the requirements of the Investor Compensation Scheme Regulations, 2003 issued under the Investment Services Act, 1994 (Chapter 370 of the Laws of Malta) licence holders are required to transfer a variable contribution to an Investor Compensation Scheme Reserve and place the equivalent amount with a bank, pledged in favour of the Scheme. Alternatively licence holders can elect to pay the amount of variable contribution directly to the Scheme. Lombard Bank Malta p.l.c. has elected to pay the amount of the variable contribution directly to the Scheme.

40 **Statutory information**

Lombard Bank Malta p.l.c. is a limited liability company domiciled and incorporated in Malta.

41 **Events subsequent to the reporting period**

Subsequent to the reporting date, an armed conflict between Russia and Ukraine commenced as a result of which economic sanctions were imposed by the EU, the US and other countries on Russia and Belarus as well as a number of Russian and Belarussian individuals. The war and related sanctions are expected to contribute to global economic dislocation, including potentially, disruption of energy supplies, higher inflation and additional credit and market risks.

The Group performed an initial assessment of the effects the current situation may have on its business. This considered impacts on the valuation of its investments, that were deemed immaterial, as well as the effect on the Group's processes and on its borrowers' business models and supply chains. The Group has virtually no direct exposure to assets in Russia, Belarus or Ukraine and concluded that there should not be material effects on the Group or its businesses. The Group will ensure compliance with any applicable sanctions and will continue to follow closely the developing situation and any potential effects on its customers and operations.

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

1 Risk management

1.1 Overview of risk disclosures

The Additional Regulatory Disclosures seek to increase public disclosure with respect to a bank's capital structure and adequacy as well as its risk management policies and practices. These disclosures have been prepared by the Bank in accordance with the Pillar III quantitative and qualitative disclosure requirements as governed by Banking Rule BR/07: Publication of Annual Report and Audited Financial Statements of Credit Institutions authorised under the Banking Act, 1994, issued by the Malta Financial Services Authority. These disclosures are published by the Bank on an annual basis as part of the Annual Report. The rule follows the disclosure requirements of Directive 2013/36/EU (Capital Requirements Directive) and EU Regulation No. 575/2013 (Capital Requirements Regulation) of the European Parliament and of the Council of 26 June 2013.

Consistent with the requirements of banking regulations, these disclosures are not subject to an external audit, except to the extent that any disclosures are equivalent to those made in the Financial Statements which have been prepared in accordance with the requirements of International Financial Reporting Standards ('IFRS') as adopted by the EU. The Bank is satisfied that internal verification procedures ensure that these Additional Regulatory Disclosures are presented fairly.

1.2 Risk Management Framework

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework.

To enhance its risk oversight efforts, the Board of Directors established an Audit & Risk Committee with a mandate to supervise and monitor *inter alia*, the Bank's compliance with its risk management policies and procedures, review any financial information, statements and disclosures to be issued and the adequacy of the Bank's risk management framework, including its risk appetite statement and strategy.

The Bank has also established the Assets & Liabilities Committee (ALCO) and the Credit Committee that are responsible for developing the Bank's risk management policies in their specific areas.

The Bank also has an independent Risk Management function as the Bank's second line of defence and independent of operations which also reports directly to the ARC and is represented during meetings of the above-mentioned committees. It is responsible for ensuring that the Bank's Risk Management Policy, Risk Appetite Statement and any other guidelines support the Bank's objectives. It is also responsible for further identifying any unmitigated risks and for formulating suitable action plans for their treatment. The function monitors the high-level principles that guide staff in its day-to-day management of risk through oversight of policies, limits, procedures, processes and systems as well as by using methods and tools for risk measuring, monitoring, controlling and reporting.

The Bank considers risk management a core competency that helps produce consistently high returns for its various stakeholders. The Bank's business involves taking on risks in a targeted manner and managing them professionally. The Bank aims to manage all major types of risk by applying methods that meet best practice. The Bank considers it important to have a clear distribution of responsibilities within risk management. One of the main tasks of the Bank's executive management is to set the framework for this area. The core functions of the Bank's risk management are to identify all key risks for the Bank, measure these risks, manage the risk positions and determine capital allocations. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and best market practice.

An understanding of risk-taking and transparency in risk-taking are key elements in the Bank's business strategy and thus in its ambition to be a strong financial institution. The Bank's internal risk management processes support this objective.

Risk management within the Bank is mainly carried out on a unified basis, using an integrated and global framework. This framework is based on local and international guidelines, such as the Basel III Accord and corresponding Directives and Regulations of the European Union, including technical standards, as well as on contemporary international banking practices guided by the Basel Committee on Banking Supervision.

The Bank has adopted the Standardised Approach and the Basic Method with respect to the calculation of capital requirements and management of credit and foreign exchange risk respectively, as well as the Basic Indicator Approach with respect to operational risk.

1 **Risk management** *(continued)*

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Board deems the risk management framework adopted by the Bank to be adequate and gives assurance to the Bank's stakeholders that the risk management systems are appropriate in relation to the Bank's risk profile and strategy.

The Bank's different operational functions, on an entity-wide basis, are primarily responsible for risk management procedures and activities in their respective areas. All the operational functions have a primary role in risk management at Bank-wide level. The Risk Management Function provides oversight, independently from operations. The Bank's risk management is implemented and handled properly by the operational functions. The Bank's Internal Audit Function, through verification, ensures that effective risk management procedures and activities are adequately designed and operating as prescribed.

1.3 Board and Senior Management Committees

The Bank's Board of Directors is responsible for ensuring that adequate processes and procedures exist to ensure effective internal control systems for the Bank. These internal control systems ensure that decision-making capability and the accuracy of the reporting and financial results are maintained at a high level at all times. The Board assumes responsibility for:

- setting business objectives, goals and the general strategic direction for Management with a view to maximise value;
- selecting and appointing the Chief Executive Officer who is entrusted with the day-to-day operations of the Bank;
- management of the Bank's operations, as well as appointment of members of Management;
- ensuring that significant business risks are identified and appropriately managed; and
- setting the highest business standards and code for ethical behaviour, and monitoring performance in this respect.

In deciding how best to discharge its responsibilities, the Board upholds a policy of clear demarcation between its role and responsibilities and those of Management. It has defined the level of authority that it retains over strategy formulation and policy determination, and delegated authority and vested accountability for the Bank's day-to-day business in the Assets & Liabilities Committee and Credit Committee and, for the Bank's day-to-day operations, in an Executive Team comprising the Chief Executive Officer and Chief Officers. The Audit & Risk Committee reviews the processes and procedures to ensure the effectiveness of the Bank's system of internal control, as well as the implementation of the Board's risk strategy by Management. The Audit & Risk Committee is supported by the Internal Audit, Risk Management and Compliance functions.

The ALCO monitors the Bank's financial performance, considers investment policy and overseas counterparty limits. Membership of this Committee is made up of a number of Chief Officers and Senior Managers including managers from Finance and Treasury Departments. The Chief Executive Officer is Chairman of ALCO and retains primary responsibility for asset and liability management. The ALCO oversees risk management practices in relation to asset and liability management.

The Credit Committee considers the development of general lending principles and oversees risk management practices in lending operations. The Credit Committee is chaired by the Chief Executive Officer and is composed of other Chief Officers as well as other Senior Officers.

The Audit & Risk Committee assists the Board in fulfilling its supervisory and monitoring responsibility by reviewing the financial statements and disclosures, the system of internal control established by management as well as the external and internal audit processes. The Audit & Risk Committee is also responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank.

The Bank's independent Internal Audit Department reviews the adequacy and proper operation of internal controls in individual areas of operation and reports its findings to the Audit & Risk Committee. The Internal Audit Function carries out both regular and ad-hoc reviews of risk management controls and procedures, in both cases reporting its findings.

The Bank has an appropriate organisational structure for planning, executing, controlling and monitoring business operations in order to achieve the Bank's objectives.

1 **Risk management** *(continued)*

Authority to operate the Bank and its subsidiaries is delegated to the Chief Executive Officer within the limits set by the Board. The Board is ultimately responsible for the Bank's system of internal control 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 provide only reasonable, and not absolute, assurance against material misstatement or loss.

The Bank is committed to the highest standards of business conduct and seeks to maintain these standards across all of its operations. Bank policies and procedures are in place for the reporting and resolution of fraudulent activities.

1.4 Key risk components

The Bank's Board of Directors is empowered to set out the overall risk policies and limits for all material risk types. The Board also decides on the general principles for managing and monitoring risks.

To ensure coherence between the Bank's strategic considerations regarding risk-taking and day-to-day decisions, from time to time, the Bank establishes its risk appetite as a strategic tool. Risk appetite is the maximum risk that the Bank is willing to assume to meet business targets. The Bank's risk appetite is set in a process based on a thorough analysis of its current risk profile. The Bank identifies a number of key risk components and for each determines a target that represents the Bank's views on the component in question.

In terms of the Capital Requirements Regulation (CRR), an 'exposure' is the amount at risk arising from the reporting credit institution's assets and off-balance sheet instruments. Consistent with this, an exposure would include the amount at risk arising from the Bank's:

- claims on a customer including actual and potential claims which would arise from the drawing down in full of undrawn advised facilities, which the Bank has committed itself to provide;
- contingent liabilities arising in the normal course of business, and those contingent liabilities which would arise from the drawing down in full of undrawn advised facilities which the Bank has committed itself to provide; and
- other on and off-balance sheet financial assets and commitments.

The Bank is exposed to a number of risks, which it manages at different organisational levels.

The main categories of risk are:

- *Credit risk:* Credit risk stems from the possible non-prompt repayment or non-payment of existing and contingent obligations by the Bank's counterparties, resulting in the loss of equity and profit. It comprises the risk that deterioration in the financial condition of a borrower will cause the asset value to decrease or be extinguished. Country risk and Settlement risk are included in this category. Country risk refers to the risk of losses arising from economic or political changes that affect the country from which the asset originates. Settlement risk refers to the risk of losses through failure of the counterparty to settle outstanding dues on the settlement date owing to bankruptcy or other causes.

- *Market risk:* Risk of losses arising from unfavourable changes in the level and volatility of interest rates, foreign exchange rates or investment prices.

- *Liquidity risk:* Liquidity risk may be divided into two sub-categories:

  - Market (product) liquidity risk: Risk of losses arising from difficulty in accessing a product or market at the required time, price and volume.
  - Funding liquidity risk: Risk of losses arising from a timing mismatch between investing, placements and fund raising activities resulting in obligations missing the settlement date or satisfied at higher than normal rates.

- *Operational risk:* Risk of loss resulting from the lack of skilful management or good governance within the Bank and the inadequacy of internal control, which might involve internal operations, staff, systems or external occurrences that in turn affect the income and capital funds of financial institutions. The Bank has adopted an operational risk management framework and procedures, which provide for the identification, assessment, management, monitoring and reporting of the Bank's operational risks.

1 **Risk management** *(continued)*

1.5 Risk statement by the Board of Directors

The Bank's business model throughout the years has been that of retaining a stable deposit base and granting credit principally to the commercial real estate sector, particularly because the Board strongly believes that despite the increased capital requirements introduced by the CRR, an active commercial real estate market is a fundamental source of employment and economic growth in Malta. Nonetheless, the Bank is conscious of the risks involved in commercial real estate lending, and thus ensures it prices loans by reference to underlying risks. In this respect, the Bank's return on assets, expressed as a percentage of profit after tax to average total assets, for the reporting period ended 31 December 2021 amounts to 0.7%.

In this respect, the loan loss coverage ratio, calculated as provisions for impairment on non-performing exposures to total non-performing exposures, which as at 31 December 2021, amounted to 33.0% differs from that experienced within the sector, which generally tends to fluctuate between 50% to 55%. This clearly illustrates the robustness of the Bank's risk management practices particularly in respect of credit risk.

2 **Credit risk**

2.1 Introduction to Credit risk

Credit risk is the risk of suffering financial loss, should any of the Bank's customers, clients or market counterparties fail to fulfil their contractual obligations to the Bank. Credit risk arises mainly from commercial and consumer loans and advances and loan commitments arising from such lending activities, but can also arise from credit enhancement provided, such as financial guarantees, letters of credit, endorsements and acceptances.

Credit risk constitutes the Bank's largest risk in view of its significant lending and securities portfolios, which are monitored in several ways. The Bank is fully aware of such risk and places great importance on its effective management.

The Bank allocates considerable resources in ensuring the ongoing compliance with approved credit limits and to monitor its credit portfolio. In particular, the Bank has a fixed reporting cycle to ensure that the relevant management bodies, including the Board of Directors and the Executive Team, are kept informed on an ongoing basis of developments in the credit portfolio, non-performing loans and other relevant information.

2.2 Credit risk management

The Board of Directors has delegated the responsibility for the monitoring of management of credit risk to the Credit Committee. The granting of a credit facility is based on the Bank's insight into the customer's financial position, which is reviewed regularly to assess whether the basis for the granting of credit has changed. Furthermore, the customer must be able to demonstrate a reasonable ability to repay the debt. Approval limits are graded starting from authorised staff members and leading up to the Credit Committee and the Board of Directors depending on the size and the particular risk attached to the loan. Facilities are generally adequately secured either by property and/or guarantees and are reviewed periodically by Management both in terms of the exposure to the Bank and to ensure that security is still valid.

The Bank's Credit Department is responsible for undertaking and managing credit risk in relation to the entity's lending activities; covering all the stages in the lending cycle comprising credit proposal, loan approval, effecting advances, credit and collateral monitoring, processing repayments and credit recovery procedures. The Bank manages, limits and controls concentrations of credit risk arising from loans and advances wherever they are identified – in particular, to individual customers and groups, and to industry sectors. Such risks are monitored on a revolving basis and subject to frequent review, as considered necessary. The exposure to any one borrower is further restricted by sub-limits covering on and off-balance sheet exposures. Actual exposures against limits are monitored at end of day on a daily basis and on a real-time basis too. As highlighted previously, the Bank's reporting framework with respect to lending credit risk is comprehensive with regular reporting by the Credit Department to the Board, Credit Committee and Executive Team on adherence to limits, activity levels, performance measures and specific credit risk events.

2 **Credit risk** *(continued)*

In order to minimise the credit risk undertaken, counterparty credit limits may be defined, which consider a counterparty's creditworthiness, the value of collateral and guarantees which can reduce the overall credit risk exposure, as well as the type and the duration of the credit facility. In order to examine a counterparty's creditworthiness, the following are considered: country risk, quantitative and qualitative characteristics, as well as the industry sector in which the counterparty operates. The Bank has set limits of authority and has segregated duties so as to maintain impartiality and independence during the approval process and control for new and existing credit facilities.

The Bank's maximum exposure amount to credit risk before taking account of any collateral held or other credit enhancements can be classified in the following categories:

- Financial assets recognised on-balance sheet comprising principally balances with Central Bank of Malta, Malta Government treasury bills, cheques in course of collection, financial assets measured at FVOCI as well as loans and advances to banks and customers. The maximum exposure of these financial assets to credit risk equals their carrying amount.
- Guarantee obligations incurred on behalf of third parties. The maximum exposure to credit risk is the full amount that the Bank would have to pay if the guarantees are called upon.
- Loan commitments and other credit related commitments that are irrevocable over the life of the respective facilities. The maximum exposure to credit risk is the full amount of the committed facilities.

The Bank's credit risk exposure amounts reflect the maximum exposure to credit risk before collateral held or other credit enhancements in accordance with the regulatory information submitted to the MFSA and are as follows:

	2021	2021
		Year end
	Average value	Exposure value
	€ 000	€ 000
Central governments or central banks	**306,072**	**298,887**
Public sector industries	**538**	**545**
Multilateral development banks	**3,432**	**3,453**
International organisations	**878**	**896**
Institutions	**107,104**	**98,663**
Corporates	**74,084**	**69,557**
Retail	**19,911**	**18,177**
Secured by mortgages on immovable property	**423,599**	**449,337**
Exposures in default	**37,108**	**26,865**
Exposures associated with particularly high risk	**115,167**	**112,833**
Equity	**22,022**	**22,481**
Other items	**52,732**	**54,710**
	1,162,647	**1,156,404**

The exposures set out in the table above are based on the sum of on-balance sheet exposures and off-balance sheet exposures adjusted for the credit conversion factors stipulated in Article 166(10) of the CRR.

2 **Credit risk** *(continued)*

The following is an analysis of the Bank's exposure to credit risk split by on-balance sheet assets and off-balance sheet instruments:

	2021
	€ 000
On-balance sheet assets	**1,139,614**
Other adjustments	**(4,748)**
Off-balance sheet instruments	**(21,538)**
	1,156,404

As set out in the Financial Statements under 'Accounting estimates and judgements', the measurement of the Expected Credit Loss allowance for financial assets measured at amortised cost and Fair Value through Other Comprehensive Income (FVOCI) is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour. The COVID-19 pandemic gave rise to levels of uncertainty that required increased use of estimation and judgement since 31 December 2020, especially in relation to effects that the pandemic will be having on the local and international economy. Judgement in this context, to name a few, would include assumptions as to duration of the pandemic, change in collateral value, central support to business, availability of medical facilities and solutions and level of response to central authority directives. The situation is still highly fluid and there is little to no visibility on the extent of the impact on the economy by the end of 2021. Stressed probabilities of default (PDs) used in the sectorial macroeconomic variables were adjusted to reflect the forecasted severe Central Bank of Malta forecasts. However, at the reporting date the asset quality of the Bank's financial assets remains sound and there is no evidence of an increase in credit risk. The Bank will continue to closely monitor its exposures in the light of developments so as to align the Expected Credit Loss accordingly.

On 25 March 2021 the European Banking Authority (EBA) issued guidance 'Statement on the application of the prudential framework regarding Default, Forbearance and IFRS9 in light of COVID-19 measures' clarifying that the application of moratoria or deferral of payments, aimed at addressing the adverse systemic economic impact of the COVID-19 pandemic, should not by itself act as a trigger to conclude that a significant increase in credit risk occurred. Credit institutions are, however, still obliged to assess the credit quality of exposures benefitting from these measures and identifying any situation of unlikeliness to pay of the borrower.

On 13 April 2021 the Central Bank of Malta issued Directive 18 (in terms of Legal Notice 142) specifying parameters for granting of COVID-19 measures and other Government guaranteed assistance. Following the outbreak of the pandemic the Bank contacted its borrowing customers offering assistance. The Bank set aside €12.5 million as assistance for working capital requirements at favourable terms to its commercial customers. The Bank also considered requests for loan repayment moratoria on a case-by- case basis and also in line with the parameters laid down in CBM Directive 18. Since May 2021 the Bank is also offering working capital loans under the MDB COVID-19 Guarantee Scheme. With regard to retail borrowers, particularly Home Loan customers, the Bank offered a moratorium on up to 80% of loan repayment for a twelve-month period. This initiative was introduced by the Bank before the coming into force of CBM Directive 18 on loan repayment moratoria.

As at 31 December 2021, there were no outstanding gross loans and advances subject to general payment moratoria as established within Directive No. 18 and the EBA guidelines.

2 **Credit risk** *(continued)*

The gross carrying amount of the loans and advances to customers for which moratorium was offered or granted is analysed below:

	Number of obligors	Total	Of which: legislative moratoria	Of which: expired
		€ 000	€ 000	€ 000
At 31 December 2021				
Loans and advances for which moratorium was offered	98	72,150	-	-
Loans and advances subject to moratorium (granted)	96	71,873	71,873	71,873
of which: Households		13,363	13,363	13,363
of which: Collateralised by residential immovable property		12,184	12,184	12,184
of which: Non-financial corporations		30,793	30,793	30,793
of which: Small and Medium-sized Enterprises		13,030	13,030	13,030
of which: Collateralised by commercial immovable property		26,429	26,429	26,429

The gross carrying amount of newly originated loans and advances subject to public guarantee schemes are analysed below:

	Total	Of which: forborne	Of which: gaurantees received	Inflows to non-performing exposures
	€ 000	€ 000	€ 000	€ 000
At 31 December 2021				
Newly originated loans and advances subject to public guarantee	10,956	3,452	4,930	-
of which: Households	-	-	-	-
of which: Collateralised by residential immovable property	-	-	-	-
of which: Non-financial corporations	10,491	3,452	4,721	-
of which: Small and Medium-sized Enterprises	2,360	-	-	-
of which: Collateralised by commercial immovable property	228	-	-	-

2 **Credit risk** *(continued)*

2.3 Concentration risk

Concentration risk arises as a result of the concentration of exposures within the same category, whether the category relates to geographical location, industry sector or counterparty type.

As at 31 December 2021, no loans and advances to customers were deemed to be prohibited large exposures, prior to any eligible exemptions, in accordance with the requirements of Part Four of the CRR, Large Exposures. A limited number of customers account for a certain percentage of the Bank's loans and advances.

Credit risk attributable to concentration of investments is not considered by the Directors to be significant in view of the credit standing of the issuers.

The following tables analyse the concentration of credit risk by geographical region, industry sector and residual maturity at the end of the reporting period.

2.3.1 Credit risk exposures analysed by geographical region

The Bank monitors concentration of credit risk by geographical region. The following table summarises the country of risk by exposure class:

	Total	**Malta**	**Eurozone**	**Other European countries**	**Other**
At 31 December 2021	**€ 000**	**€ 000**	**€ 000**	**€ 000**	**€ 000**
Central governments or central banks	**298,887**	**291,117**	**-**	**1,612**	**6,158**
Public Sector entities	**545**	**-**	**545**	**-**	**-**
Multilateral Development Banks	**3,453**	**-**	**1,499**	**-**	**1,954**
International Organisations	**896**	**-**	**896**	**-**	**-**
Institutions	**98,663**	**13,259**	**52,779**	**29,574**	**3,051**
Corporates	**69,557**	**68,003**	**930**	**624**	**-**
Retail	**18,177**	**18,177**	**-**	**-**	**-**
Secured by mortgages on immovable property	**449,337**	**449,337**	**-**	**-**	**-**
Exposures in default	**26,865**	**26,865**	**-**	**-**	**-**
Items associated with particularly high risk	**112,833**	**112,833**	**-**	**-**	**-**
Equity	**22,481**	**21,608**	**-**	**-**	**873**
Other items	**54,710**	**54,710**	**-**	**-**	**-**
	1,156,404	**1,055,909**	**56,649**	**31,810**	**12,036**

2 **Credit risk** *(continued)*

2.3.2 Credit risk exposures analysed by industry sector

The following are the exposure amounts split by exposure class according to the respective industry concentration:

At 31 December 2021	**Total € 000**	**Manufacturing € 000**	**Tourism € 000**	**Trade € 000**	**Property and construction € 000**	**Personal, professional and home loans € 000**	**Financial institutions € 000**	**Other sectors € 000**
Central governments or central banks	**298,887**	**-**	**-**	**-**	**-**	**-**	**298,887**	**-**
Public Sector entities	**545**	**-**	**-**	**-**	**-**	**-**	**545**	**-**
Multilateral Development Banks	**3,453**	**-**	**-**	**-**	**-**	**-**	**3,453**	**-**
International Organisations	**896**	**-**	**-**	**-**	**-**	**-**	**896**	**-**
Institutions	**98,663**	**-**	**-**	**-**	**-**	**-**	**98,472**	**191**
Corporates	**69,557**	**4,123**	**5,526**	**21,641**	**5,393**	**805**	**25,876**	**6,193**
of which: SME	**7,053**	**2**	**-**	**3,118**	**29**	**56**	**3,832**	**16**
Retail	**18,177**	**3,401**	**3,751**	**188**	**749**	**8,445**	**14**	**1,629**
of which: SME	**8,611**	**3,350**	**3,722**	**123**	**554**	**754**	**12**	**96**
Secured by mortgages on immovable property	**449,337**	**1,573**	**46,782**	**15,241**	**130,036**	**146,399**	**97,645**	**11,661**
of which: SME	**66,279**	**-**	**2,783**	**3,190**	**31,913**	**6,286**	**17,609**	**4,498**
Exposures in default	**26,865**	**141**	**1,104**	**3,768**	**13,018**	**2,942**	**5,133**	**759**
of which: SME	**14,132**	**138**	**-**	**3,545**	**10,400**	**-**	**1**	**48**
Items associated with particularly high risk	**112,833**	**332**	**1,046**	**757**	**91,068**	**3,363**	**7,962**	**8,305**
of which: SME	**29,109**	**68**	**816**	**-**	**28,221**	**4**	**-**	**-**
Equity	**22,481**	**259**	**1,645**	**-**	**-**	**-**	**2,287**	**18,290**
Other items	**54,710**	**-**	**459**	**-**	**41,179**	**-**	**7,107**	**5,965**
	1,156,404	**9,829**	**60,313**	**41,595**	**281,443**	**161,954**	**548,277**	**52,993**

2 **Credit risk** *(continued)*

2.3.3 Credit risk exposures analysed by residual maturity

The residual maturity breakdown by exposure class at the end of the reporting period was as follows:

At 31 December 2021	Total € 000	Less than 1 year € 000	Over 1 but less than 5 years € 000	Over 5 years € 000
Central governments or central banks	**298,887**	**128,175**	**74,015**	**96,697**
Public sector entities	**545**	**-**	**545**	**-**
Multilateral Development Banks	**3,453**	**-**	**2,868**	**585**
International Organisations	**896**	**896**	**-**	**-**
Institutions	**98,663**	**69,838**	**7,336**	**21,489**
Corporates	**69,557**	**29,609**	**16,939**	**23,009**
Retail exposures	**18,177**	**8,502**	**3,027**	**6,648**
Secured by mortgages on immovable property	**449,337**	**120,138**	**39,550**	**289,649**
Exposures in default	**26,865**	**19,193**	**4,738**	**2,934**
Exposures associated with particularly high risk	**112,833**	**54,439**	**56,306**	**2,088**
Equity exposures	**22,481**	**22,481**	**-**	**-**
Other items	**54,710**	**54,710**	**-**	**-**
	1,156,404	**507,981**	**205,324**	**443,099**

2.3.4 Counterparty banks' risk

The Bank runs the risk of loss of funds due to the possible delay in the repayment of existing and future obligations by counterparty banks.

Within its daily operations, the Bank transacts with banks and other financial institutions. By conducting these transactions, the Bank is running the risk of losing funds due to the possible delays in the repayment to the Bank of the existing and future obligations of the counterparty banks. The Bank primarily places short-term funds with pre-approved banks subject to the limits in place and subject to the respective institutions' credit rating being within controlled parameters. The positions are checked against the limits in real time and at end of day on a daily basis.

2.3.5 Country risk

The Bank runs the risk of loss of funds due to the possible political, economic and other events in a particular country where funds have been placed or invested with several counterparties. Countries are assessed according to their size, economic data and prospects and their credit ratings from international rating agencies. Existing country credit risk exposures are monitored and reviewed periodically. The Bank's assets are predominantly in Malta. The Bank's exposures to other countries are mainly limited to bank balances and money market placements with a total carrying amount of €93,639,000 (2020: €115,673,000) at the end of the reporting period.

2.4 Use of External Credit Assessment Institutions

In calculating its risk-weighted exposure amounts, the Bank uses an External Credit Assessment Institution (ECAI) for Central governments, Institutions, Corporates and Items associated with particularly high risk for which a credit assessment is available. The credit quality of such exposures is determined by reference to external credit ratings applicable to issuers or counterparties. The Bank maps the external ratings to the credit quality steps prescribed in the CRR as required by CEBS publication *'Standardised Approach: Mapping of ECAIs' credit assessments to credit quality steps'*.

2 **Credit risk** *(continued)*

The following are the exposure values for which an ECAI is used:

At 31 December 2021	Credit quality step	Central governments or central banks € 000	Public Sector entities € 000	Multilateral Development Banks € 000	International organisations € 000	Institutions € 000	Total € 000
AAA to AA-	1	5,749	545	2,680	896	2,540	12,410
A+ to A-	2	291,656	-	773	-	60,937	353,366
BBB+ to BBB-	3	1,482	-	-	-	30,906	32,388
BB+ to BB-	4	-	-	-	-	-	-
B+ to B-	5	-	-	-	-	-	-
CCC+ and below	6	-	-	-	-	4,280	4,280
		298,887	545	3,453	896	98,663	402,444

2.5 Credit quality of the Bank's lending portfolio

The Bank manages the credit quality of its loans and advances to customers by using internal risk grades, which provide a progressively increasing risk profile ranging from 'P1' (best quality, less risky) to 'NP'. These risk grades are an essential tool for the Bank to identify both non-performing exposures and better-performing customers. The internal risk grades used by the Bank are as follows:

- Performing: Internal grade 'P1';
- Under performing: Internal grades 'P2' and 'P3'; and
- Non-performing: Internal grade 'NP'.

P1

The Bank's loans and advances to customers which are categorised as 'P1' are principally debts in respect of which the payment of interest and/or capital is not overdue by 30 days and with no recent history of customer default. Management does not expect any losses from non-performance by these customers.

P2

Loans and advances which attract a 'P2' grading are those which are receiving the close attention of the Bank's Management and are being reviewed periodically in order to determine whether such advances should be reclassified to either 'P1' or 'P3' classification. Credit facilities that attract this category include those where the payment of interest and/or capital becomes overdue by 30 days and over but not exceeding 60 days.

P3

Loans and advances which attract a 'P3' grading are those having the weaknesses inherent in those loans and advances classified as 'P2' with the added characteristics that repayment is inadequately protected by the current sound worth and paying capacity of the borrower. Loans and advances so graded have a well-defined weakness or weaknesses that could jeopardise the repayment of the debt. They are characterised by the distinct possibility that the Bank will sustain some loss if the deficiencies are not corrected. Credit facilities that attract this category include those where the payment of interest and/or capital becomes overdue by 60 days and over but not exceeding 90 days.

NP

Loans and advances which attract a 'NP' grading are those facilities where the Bank deems the recoverability of principal to be remote as a result of worsening conditions of loans and advances classified as 'P3'. Credit facilities that attract this category include those where the payment of interest and/or capital becomes overdue by more than 90 days. These loans and advances are generally past due by more than 90 days and comprise those exposures which are deemed by the Bank as credit-impaired (see definition in note 2.3.10).

2 **Credit risk** *(continued)*

The following table provides a detailed analysis of the credit quality of the Bank's lending portfolio.

	2021
	€ 000
Gross loans and advances to customers	
Performing (*'Stage 1' assets*)	**504,477**
Under-performing (*'Stage 2' assets*)	**112,283**
Non-performing (*'Stage 3' assets*)	**51,757**
	668,517

2.5.1 Credit-impaired loans and advances to customers

Credit-impaired loans and advances are advances which are either more than 90 days past due, or for which the Bank determines as probable that it will be unable to collect all principal and interest due according to the contractual terms of the loans and advances agreement(s). The Bank's credit-impaired loans and advances mainly relate to a number of independent customers which are not meeting repayment obligations or deemed by the Bank as unlikely to pay their obligations to the Bank without recourse by the Bank to realising the collateral.

2.5.2 Past due but not credit-impaired loans

Past due but not credit-impaired loans include loans and advances where contractual interest or principal payments are past due. Credit losses that may arise are covered through the Bank's assessment of Expected Credit Loss allowances.

Loans and advances to customers are analysed into credit-impaired, past due and other exposures as follows:

	2021
	€ 000
Gross loans and advances to customers	
Credit-impaired	**51,757**
Past due but not credit-impaired	**4,983**
Neither past due nor credit-impaired	**611,777**
	668,517

The table below analyses the impaired and the past due but not impaired gross loans and advances to customers by industry sector.

At 31 December 2021	**Impaired** € 000	**Past due but not Impaired** € 000
Manufacturing	**446**	**303**
Tourism	**2,483**	**51**
Trade	**3,923**	**205**
Property and construction	**35,785**	**1,075**
Personal, professional and home loans	**3,185**	**983**
Financial institutions	**5,173**	**2,250**
Other sectors	**762**	**116**
	51,757	**4,983**

The majority of the impaired and past due but not impaired loans and advances to customers were concentrated within Malta.

2 **Credit risk** *(continued)*

2.5.3 Collateral

The Bank holds collateral against exposures in the form of hypothecs over property, other registered securities over assets and guarantees. The nature and level of collateral required depends on a number of factors, including, but not limited to, the amount of the exposure, the type of facility provided, the term of the facility, the amount of the counterparty's contribution and an evaluation of the level of the credit risk or Probability of Default involved. Collateral is an important mitigant of credit risk. Nevertheless, it is the Bank's policy to establish that facilities are within the customer's capacity to repay rather than to over rely on security. In certain cases, depending on the customer's standing and the type of product, facilities may be unsecured. The Bank applies various measures to reduce the risk on individual transactions, including collateral in the form of physical assets and guarantees.

The principal collateral types used as credit risk mitigants are mortgages on residential properties and commercial real estate. For regulatory purposes, none of the Bank's collateral in the form of commercial real estate qualifies as eligible collateral, as these properties fail to meet the conditions of Article 126(2) of the CRR.

Out of the €642.9million exposures arising from the Bank's lending, €435.7million are secured by mortgages on immovable property, while €108.3million are secured by mortgages on immovable property but are classified within the high risk exposures since these are associated with speculative immovable property financing. From the €435.7million exposures secured by mortgages on immovable property, €128.8million qualify as fully and completely secured by mortgages on residential immovable property, and accordingly attract a risk-weight of 35%.

2.5.4 Loss allowances

The Bank assesses on a forward-looking basis the Expected Credit Losses associated with its loans and advances portfolio. The Bank recognises a loss allowances for such losses at each reporting date.

Expected Credit Losses	**Total € 000**	**Manufacturing € 000**	**Tourism € 000**	**Trade € 000**	**Property and construction € 000**	**Personal, professional and home loans € 000**	**Financial institutions € 000**	**Other sectors € 000**
At 1 January 2021	**25,914**	**599**	**1,771**	**1,718**	**15,775**	**1,269**	**3,560**	**1,222**
Additions	**4,394**	**15**	**267**	**355**	**2,336**	**560**	**844**	**17**
Reversals	**(4,686)**	**(80)**	**(152)**	**(791)**	**(618)**	**(983)**	**(938)**	**(1,124)**
At 31 December 2021	**25,622**	**534**	**1,886**	**1,282**	**17,493**	**846**	**3,466**	**115**

2.5.5 Write-off policy

The Bank writes off loan or advance balances (and any related allowances for impairment losses) when it determines that these are uncollectible. This decision is reached after considering information such as the occurrence of significant changes in the borrower's financial position, such that the borrower can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure.

3 Market risk

The Bank takes on exposure to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices.

Accordingly, market risk for the Bank consists of three elements:

- Interest rate risk, which is the risk of losses because of changes in interest rates;
- Exchange rate risk, which is the risk of losses on the Bank's positions in foreign currency because of changes in exchange rates; and
- Equity price risk, which is the risk of losses because of changes in investment prices.

3.1 Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or at different amounts. The Bank accepts deposits from customers at both fixed and floating rates and for varying maturity periods. This risk is managed through the matching of the interest resetting on repricing dates on assets and liabilities as much as it is practicable. The Bank monitors on a continuous basis the level of mismatch of interest rate repricing taking cognisance of the terms of the Bank's principal assets, comprising loans and advances to customers, that are repriceable at the Bank's discretion. Accordingly, the Bank is in a position to manage the interest rate terms of its financial assets and simultaneously modify the interest terms of its liabilities. The Bank seeks to manage its net interest spread, taking cognisance of the cost of capital, by investing funds in a portfolio of loans and advances and securities with a longer tenure than the funding liabilities (therefore normally giving rise to a negative maturity gap position) through the effective management of shorter term deposit liabilities with a view to securing steady base deposits with differing terms over the medium to longer term.

Interest rate risk is managed principally through monitoring interest rate gaps and by having pre-approved limits for repricing bands which are set by ALCO. ALCO is the monitoring body for compliance with these limits and is assisted by Treasury through its day-to-day operational activities. 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 interest rate movements.

Accordingly, the Bank's ALCO is primarily responsible for the interest rate risk management process and for monitoring actively the interest rate risk measures utilised by the Bank. Reporting of interest rate risk measures exposures vis-à-vis limits flows to the ALCO and Board on a regular systematic basis. The Bank's independent Risk Management Function provides oversight in respect of the interest rate risk management process ensuring that it is designed in an appropriate manner and is functioning properly.

The Bank's repricing gaps at 31 December 2021 are disclosed in the tables within note 2.4.1 to the financial statements. The measures applied for the monitoring of the fair value sensitivity of the fixed rate instruments and the cash flow sensitivity for variable rate instruments are disclosed within notes 2.4.3 and 2.4.4 to the financial statements.

3.2 Currency risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. Foreign exchange risk is the risk to earnings and value caused by a change in foreign exchange rates. Foreign exchange risk arises when financial assets or liabilities are denominated in currencies which are different from the Bank's functional currency.

The Bank manages this risk principally by ensuring that its foreign currency denominated liabilities are matched with corresponding assets in the same currency.

Accordingly, foreign currency liabilities are utilised to fund assets denominated in the same foreign currency thereby matching asset and liability positions as much as is practicable. This mechanism is reflected in the figures reported in the table below which presents this matching process.

The Bank's foreign exchange risks are managed actively and monitored by the Treasury Function, which process ensures that the Bank maintains its exposure to foreign currencies within prescribed limits set by the Bank's ALCO. ALCO sets limits

3 **Market risk** *(continued)*

on the level of exposure by currency and in aggregate for both overnight and intra-day positions which are monitored on a real-time basis. Reporting of exposures vis-à-vis limits flows to the ALCO and Board on a regular systematic basis. The Bank's independent Risk Management Function is responsible for assuring that the foreign exchange risk management process is designed in an appropriate manner and is functioning effectively.

The Bank enters into forward foreign currency exchange contracts with customers in the normal course of its business. Generally, it is the Bank's policy to cover these contracts by other forward positions. As a result, the Bank is not open to any significant exchange risk in respect of derivative contracts. The Bank also takes a deposit margin of the nominal value from the customer thereby reducing its credit risk should the client default. The Bank had no open forward foreign currency contracts at the end of the reporting period.

The following table summarises the Bank's net exchange position by currency taking into account the Bank's financial assets and liabilities as well as off-balance sheet instruments exposing the Bank to foreign exchange risk.

Bank **At 31 December 2021**	**Total** **€ 000**	**EUR** **€ 000**	**GBP** **€ 000**	**USD** **€ 000**	**Other** **€ 000**
Financial assets					
Balances with Central Bank of Malta, treasury bills and cash	**125,552**	**105,379**	**11,080**	**9,081**	**12**
Investments measured at FVOCI	**224,600**	**206,753**	**6,668**	**11,179**	**-**
Loans and advances to banks	**68,424**	**12,237**	**20,354**	**32,482**	**3,351**
Loans and advances to customers	**642,895**	**639,445**	**3,118**	**302**	**30**
Other assets	**4,048**	**3,913**	**59**	**76**	**-**
Total financial assets	**1,065,519**	**967,727**	**41,279**	**53,120**	**3,393**
Financial liabilities					
Amounts owed to banks	**1,224**	**1,224**	**-**	**-**	**-**
Amounts owed to customers	**978,365**	**882,951**	**40,232**	**51,809**	**3,373**
Other liabilities	**22,043**	**19,742**	**995**	**1,244**	**62**
Total financial liabilities	**1,001,632**	**903,917**	**41,227**	**53,053**	**3,435**
Net currency exposure in financial assets/liabilities		**63,810**	**52**	**67**	**(42)**
Commitments and contingent liabilities	**209,663**	**207,790**	**1,195**	**678**	**-**

3.3 Equity price risk

The exposure of the Bank to this risk is not significant given the low holdings of equity instruments by the Bank, which are not deemed material in the context of the Bank's statement of financial position. Such holdings are limited to locally quoted equity instruments issued by local well-known corporate issuers. Frequent management reviews are carried out to obtain comfort on the high quality of the portfolio.

4 Liquidity risk

4.1 Management of liquidity risk

Liquidity risk is defined as the risk of losses due to:

- the Bank's funding costs increasing disproportionately;
- lack of funding preventing the Bank from establishing new business; and
- lack of funding ultimately preventing the Bank from meeting its obligations.

Liquidity risk may result from an inability to sell a financial asset quickly at close to its fair value. The Bank is exposed to daily calls on its available cash resources from overnight deposits, current and call deposits, maturing term deposits, loan drawdowns and guarantees.

The objective of the Bank's liquidity and funding management is to ensure that all foreseeable funding commitments and deposit withdrawals can be met when due. It is the Bank's objective to maintain a diversified and stable funding base with the objective of enabling the Bank to respond quickly and smoothly to unforeseen liquidity requirements.

The Bank manages this risk by ensuring that its assets and liabilities are matched in terms of maturities as much as is practicable. However, the Bank ought to manage its net interest spread by investing funds in a portfolio of assets with a longer term than the liabilities funding them. To mitigate exposures arising in this respect, the Bank holds significant liquid assets in the form of Malta Government treasury bills, money market placements and other short-term instruments for managing liquidity risk to support payment obligations and contingent funding in a stressed market environment.

The Bank maintains internal liquidity buffers established by ALCO made up of cash and financial assets which are also eligible for collateral against borrowing from the European Central Bank. In order to ensure that maturing funds are always available to meet unexpected demand for cash, the Board sets parameters within which maturities of assets and liabilities may be mismatched in line with the stance referred to previously. Unmatched positions potentially enhance profitability, but also increase risks. The Bank's ALCO focuses on the entity's management process with respect to market and funding liquidity risks. ALCO maintains ongoing oversight of forecast and actual cash flows, by monitoring the availability of funds to meet commitments associated with financial instruments. ALCO is supported by the Bank's Executive Team and Treasury Function in this respect, at operational level. ALCO monitors the Bank's Liquidity Gap analysis on a monthly basis. The Bank's liquidity management process comprises management of day-to-day funding, by monitoring future cash flows to ensure that requirements can be met and that funds are replenished as they mature or are borrowed by customers. This implies a structured ongoing analysis of the contractual maturity of the financial liabilities and the expected collection date of the financial assets. The Bank's liquidity management focuses on maintaining a portfolio of highly marketable assets, subject to pre-established limits, that can easily be liquidated in case of any unforeseen interruption to cash flow; and monitoring the liquidity ratios of the Bank against internal and regulatory requirements. In this respect, the Bank's advances-to-deposit ratio of 65.7% at the end of the reporting period reflects management's prudent stance in the context of liquidity management. Also, the Liquidity Coverage ratio at 31 December 2021 is 225.3%, which is significantly higher than the prudential parameters set by Regulation.

Reporting of measures of liquidity risk and liquidity ratios vis-à-vis internal limits flows to the ALCO and Board on a regular basis. The Bank's Risk Management Function provides oversight in respect of the liquidity risk management process ensuring that it is functioning effectively.

The Bank also monitors the level and type of undrawn lending commitments and the impact of contingent liabilities such as guarantees as part of the liquidity management process previously referred to.

As at 31 December 2021, the Bank had outstanding guarantees on behalf of third parties amounting to €9,320,000 (2020: €8,681,000), which are cancellable upon the request of the third parties. The Bank's liquidity exposures arising from these commitments and contingencies are expected to expire principally within a period of twelve months from the end of the reporting period.

4.2 Asset Encumbrance

The disclosure on asset encumbrance is a requirement introduced in Banking Rule BR/07 transposing the provisions of the EBA Guidelines on Disclosure of Encumbered and Unencumbered Assets (EBA/GL/2014/03).

4 **Liquidity risk** *(continued)*

The objective of this disclosure is to facilitate an understanding of available and unrestricted assets that could be used to support potential future funding and collateral needs. An asset is defined as encumbered if it has been pledged as collateral against an existing liability, and as a result is no longer available to the Bank to secure funding, satisfy collateral needs or be sold to reduce the funding requirement.

The disclosure is not designed to identify assets which would be available to meet the claims of creditors or to predict assets that would be available to creditors in the event of a resolution or bankruptcy.

In accordance with the EBA 'Guidelines on Disclosure of Encumbered and Unencumbered Assets', the amounts disclosed in the table below represent median values, being the rolling quarterly amounts over the previous 12 months.

	Carrying amount of encumbered assets € 000	Fair value of encumbered assets € 000	Carrying amount of unencumbered assets € 000	Fair value of unencumbered assets € 000
At 31 December 2021				
Assets of the reporting institution	**13,007**	**13,007**	**1,137,854**	**1,137,854**
Loans on demand	**2,122**	**2,122**	**96,299**	**96,299**
Equity instruments	**-**	**-**	**8,676**	**8,676**
Debt securities	**10,064**	**10,064**	**262,877**	**262,877**
Loans and advances	**-**	**-**	**689,204**	**689,204**
Other assets	**820**	**820**	**80,798**	**80,798**

The Bank does not encumber any of the collateral received. Moreover, as at 31 December 2021, the Bank did not have any outstanding liabilities associated with encumbered assets and collateral received.

The Bank undertakes encumbrance by pledging debt securities against the provision of credit lines by the Central Bank of Malta and in favour of the Depositor Compensation Scheme.

5 **Operational risk**

Operational risk is the risk of loss resulting from the lack of skilful management or good governance within the Bank and the inadequacy of internal control, which might involve internal operations, staff, systems or external occurrences that in turn affect the income and capital funds of financial institutions. The Bank has adopted an operational risk management framework and procedures, which provide for the identification, assessment, management, monitoring and reporting of the Bank's operational risks. Operational risk is also addressed through proper insurance cover.

Operational risk management relies on a framework of policies and procedures implemented by the different operational functions within the Bank through transaction processing and business execution. Regular reporting of operational risk events to the Board of Directors is carried out as required. The implementation of such policies and procedures by the Bank's operational functions is overseen by the Risk Management Function.

The Bank currently uses the Basic Indicator Approach to assess the operational risk capital requirements and accordingly allocates 15% of average gross income for a three year period in accordance with regulatory requirements. The operational risk capital regulatory requirement as at 31 December 2021 amounted to €4,107,000.

6 Capital risk management

The Bank is a licensed credit institution and must therefore comply with the capital requirements under the relevant capital requirements within laws and regulations. Maltese law and regulations on capital adequacy are naturally based on EU capital requirements.

The prudent and efficient management of capital remains one of the Bank's top priorities. The Bank must have sufficient capital to comply with regulatory capital requirements. The purpose of the Bank's capital management is to ensure an efficient use of capital in relation to risk appetite as well as business development. Capital management is managed primarily through the capital planning process that determines the optimal amount and mix of capital that should be held by the Bank, subject to regulatory limits.

Capital adequacy and the use of regulatory capital are monitored regularly by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee, European Union Regulations and Directives, as implemented by the MFSA for supervisory purposes. The Bank's capital management is based on the regulatory requirements established within the CRR and by local regulations which are modelled on the requisites of the CRD rules.

The Bank's Executive Team and ALCO are predominately responsible for the Bank's capital risk management process. Capital adequacy ratios together with the level and quality of Own funds are reported on a regular basis to the Board and the ALCO by the Finance Function.

6.1 Own funds

Own funds represent the Bank's available capital and reserves for the purposes of capital adequacy. Capital adequacy is a measure of the financial strength of a bank, expressed as a ratio of its capital to its assets. The Bank adopts 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. During the year ended 31 December 2021, the Bank complied with all of the externally imposed capital requirements to which it was subject.

In July 2013, the European Banking Authority (EBA) issued its final draft Implementing Technical Standards (ITS) on Own funds disclosures. The disclosure requirements of these technical standards have been integrated within the Bank's disclosures set out below.

The Bank's capital base comprises Common Equity Tier 1 (CET1) capital, which includes the following items:

- ordinary share capital;
- share premium;
- retained earnings;
- revaluation and other reserves; and
- other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes including deductions relating to amounts pledged in favour of the Depositor Compensation Scheme.

(a) Share capital

The Bank's share capital as at 31 December 2021 is analysed as follows:

	2021	
	No. of shares 000s	**€ 000**
Authorised		
Ordinary shares of 25 cent each	**80,000**	**20,000**
Issued		
Ordinary shares of 25 cent each	**44,767**	**11,192**

The holders of 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. All shares rank equally with regard to the Bank's residual assets.

6 **Capital risk management** *(continued)*

The following table describes the terms and conditions of the ordinary share capital issued by the Bank.

Capital Instruments	**Ordinary share capital and share premium**
Unique Identifier	MT0000040106
Governing law(s) of the instrument	Maltese Law
Regulatory treatment	
Transitional CRR rules	Common Equity Tier 1
Post-transitional CRR rules	Common Equity Tier 1
Eligible at solo/(sub-)consolidated/solo &(sub-) consolidated	Solo
Amount recognised in regulatory capital	€11,191,740
Nominal amount of instrument	€11,191,740
Nominal amounts of each share	€0.25
Accounting classification	Share capital
Issuer call subject to prior supervisory approval	No
Position in subordination hierarchy in liquidation	Subordinated to creditors and depositors
Non-compliant transitioned features	No

(b) Share premium

The share premium represents the amounts at which ordinary shares were issued in excess of their nominal value, normally arising as a result of rights issues approved by the shareholders during the Annual General Meetings. The amount is not distributable by way of dividend to shareholders.

(c) Retained earnings

The retained earnings represent earnings not paid out as dividends.

Retained earnings form part of Own funds only if those profits have been verified by the Bank's independent external auditor. 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.

On 27 July 2020, the European Central Bank ('ECB') issued a Recommendation on dividend distributions during the COVID-19 pandemic and repealing Recommendation ECB/2020/19 (ECB/2020/35), which inter alia recommended that no dividends be paid out by credit institutions until 1 January 2021 and that no irrevocable commitment to pay out dividends be undertaken by credit institutions for the financial years 2019 and 2020.

On the basis of this, during August 2020 the Board of Directors resolved to withdraw its recommendation of 23 March 2020 for the payment of a final gross dividend of 7 cent per nominal 25 cent share (net dividend of 4.55 cent for a total amount of €2,010,095) for the twelve months ended 31 December 2019.

On 15 December 2020, the ECB issued another Recommendation on dividend distributions during the COVID-19 pandemic repealing Recommendation ECB/2020/35 (ECB/2020/62), which encourages prudence on the part of credit institutions when deciding on or paying out dividends. In this respect, the ECB generally considers distributions exceeding the lower of 15% of accumulated profit for the financial years ended 31 December 2019 and 2020 and 20 basis points in terms of the Common Equity Tier 1 ratio to lack prudence. On the basis of this, a gross dividend of 3 cent per nominal 25 cent share (net dividend of 1.95 cent for a total amount of €861,469) for the twelve months ended 31 December 2020 was paid during the current financial year.

On 23 July 2021, the ECB issued another Recommendation repealing Recommendation ECB/2020/62 (ECB/2021/31) with effect from 30 September 2021. A gross dividend of 3 cent per nominal 25 cent share (net dividend of 1.95 cent for a total amount of €872,956) in respect of the financial year ended 31 December 2021 is being proposed. The final dividend will be paid to shareholders who are on the Bank's register of shareholders at 26 April 2022 subject to approval by the Annual General Meeting scheduled for 26 May 2022.

6 **Capital risk management** *(continued)*

(d) Reserve for General Banking Risks

Banking Rule BR/09 'Measures addressing credit risks arising from the assessment of the quality of asset portfolios of credit institutions authorised under the Banking Act 1994', issued by the MFSA, requires banks in Malta to hold additional reserves for general banking risks in respect of non-performing loans. This reserve is required to be funded from planned dividends. As at the reporting date, this reserve amounted to €2,903,000 (representing 100% of the total estimated amount). The amount has not changed during the year under review.

(e) Property revaluation reserve

This represents the surplus arising on the revaluation of the Bank's freehold property net of related deferred tax effects. The revaluation reserve is not available for distribution.

(f) Investment revaluation reserve

This represents the cumulative net change in fair values of assets measured at FVOCI held by the Bank, net of related deferred tax effects.

The Bank's Own funds and capital ratio calculations are set out below:

At 31 December 2021	**€ 000**
Common Equity Tier 1 (CET1) capital	
Common Equity Tier 1 (CET1) capital: instruments and reserves	
Capital instruments and the related share premium accounts	**29,722**
Retained earnings	**80,579**
Accumulated other comprehensive income (and other reserves)	**14,966**
Reserve for General Banking Risks	**2,903**
CET1 capital before regulatory adjustments	**128,170**
Common Equity Tier 1 (CET1) capital: regulatory adjustments	
Intangible assets	**(122)**
Other regulatory adjustments	**2,097**
Total regulatory adjustments to CET1	**1,975**
CET1 capital	**130,145**
Total risk-weighted assets	**805,762**
Capital ratios	
CET1 capital	**16.15%**
Tier 1 capital	**16.15%**
Total capital	**16.15%**
Institution specific buffer requirement	**7.00%**
of which: capital conservation buffer requirement	**2.50%**
CET1 available to meet buffers in excess of the CRR 4.5% minimum requirement	**11.65%**
CET1 available to meet buffers	**9.15%**
	€ 000
Items not deducted from own funds in accordance with Article 48 of CRR	**3,737**

6 **Capital risk management** *(continued)*

6.2 Capital requirements

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital, though in some cases the regulatory requirements do not reflect differing risk profiles, subject to the overall level of capital to support a particular operation or activity not falling below the minimum required for regulatory purposes. The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation.

Although maximisation of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Bank to particular operations or activities, it is not the sole basis used for decision-making. Account is also taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Bank's long-term strategic objectives. The Bank's policies in respect of capital management and allocation are reviewed regularly by the Board of Directors.

The Pillar I minimum capital requirements are calculated for credit, market and operational risks. During the year, the Bank continued to use the Standardised Approach for credit risk, the Basic Method for foreign exchange risk and the Basic Indicator Approach for operational risk in order to calculate the Pillar I minimum capital requirements. For credit risk, under the Standardised Approach, risk weights are determined according to the asset class, credit risk mitigation and external credit ratings - or by using the applicable regulatory risk weights for unrated exposures. Capital charge for foreign exchange risk using the Basic Method is calculated at 8% of the higher of the sum of all the net short positions and the sum of all the net long positions in each foreign currency. The Basic Indicator Approach requires that the Bank allocates capital for operational risk by taking 15% of the average gross income of the preceding three years.

The Total Capital Ratio is calculated using the definition of regulatory capital and risk-weighted assets. As required by the CRR, the minimum level of the Capital Requirements Ratio stands at 8%. The Capital Requirements Ratio expresses Own funds as a proportion of risk-weighted assets and off-balance sheet instruments for credit risk purposes, together with notional risk-weighted assets in respect of operational risk and market risk. Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 (i.e. the reciprocal of the minimum capital ratio of 8%) and adding the resulting figures to the sum of risk-weighted assets for credit risk.

The Bank's policy is to maintain a strong 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.

The Bank fully implemented the CRD IV capital requirements with effect from January 2020. Although it is not yet certain whether the Bank will be required to maintain an additional countercyclical capital buffer as required by the CRR, given that the Bank's exposures are mainly contained within Malta, this buffer is expected to be marginal, since the deviation of Malta's credit-to-GDP ratio is not expected to be significant taking cognisance of its long-term trend.

Additionally, the Bank is required to maintain a capital conservation buffer of 2.5%, made up of CET1 capital, on the risk-weighted exposures of the Bank as from 1 January 2021. This buffer was phased in over the period from 1 January 2016 to 31 December 2021.

6 **Capital risk management** *(continued)*

The Bank's capital requirements and Total Capital Ratio computation are as follows:

At 31 December 2021	Exposure value € 000	Risk-weighted assets € 000	Capital required € 000
Central governments or central banks	**298,887**	**7,245**	**579**
Regional Government or Local Authorities	-	-	-
Public Sector Entities	**545**	**109**	**9**
Multilateral Development Banks	**3,453**	**386**	**31**
International Organisations	**896**	-	-
Institutions	**98,663**	**28,051**	**2,244**
Corporates	**69,557**	**69,058**	**5,524**
Retail	**18,177**	**13,633**	**1,091**
Secured by mortgage on immovable property	**449,337**	**356,749**	**28,540**
Exposures in default	**26,865**	**40,298**	**3,224**
Items associated with particularly high risk	**112,833**	**169,249**	**13,540**
Covered Bonds	-	-	-
Claim on Institutions and Corporate with a short-term credit assessment	-	-	-
Claims in the form of CIU	-	-	-
Equity	**22,481**	**22,481**	**1,798**
Other items	**54,710**	**47,121**	**3,770**
Credit risk	**1,156,404**	**754,380**	**60,350**
Foreign exchange risk		**45**	**4**
Operational risk		**51,337**	**4,107**
Total capital required		**805,762**	**64,461**
Own funds			
Common Equity Tier 1 capital			**130,145**
Total own funds			**130,145**
Total capital ratio			**16.15%**

6.3 Other disclosures on own funds

The Bank has opted for the transitional arrangements laid down in Regulation (EU) 575/2013 Article 473a to mitigate the impact of IFRS9 on own funds. Under Regulation (EU) 2017/2395, during the transitional period ending 31 December 2023, the Bank would have had the option to add back a proportion of:

- the Day 1 impact as a result of the introduction of IFRS 9, being the difference between IFRS 9 Expected Credit Losses ('ECLs') on 1 January 2018 and IAS 39 provisions determined at 31 December 2017; and
- on difference in the IFRS 9 ECLs determined at reporting date and the ECLs determined on 'day 1' of the introduction of IFRS 9 (being 1 January 2018 for the Bank) for 'Stage 1' (12-months ECLs) and 'Stage 2' (lifetime ECLs) assets.

The factors used to adjust the above ECLs declines across the transitional period starting at 100% during the financial year ended 31 December 2020 to 25% in the final transitional financial year ended 21 December 2024. The above treatment is in accordance with the requirements laid down in paragraph 2 and paragraph 4 of Regulation (EU) 2017/2395.

6 **Capital risk management** *(continued)*

In line with Section 2 of the EBA 'Guidelines on uniform disclosures under Article 473a of Regulation (EU) No 575/2013 as regards transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds', the Bank is required to disclose a comparison of the institutions' own funds, Common Equity Tier 1 capital, Tier 1 capital, risk-weighted assets, Common Equity Tier 1 capital ratio, Tier 1 capital ratio, total capital ratio and leverage ratio with and without the application of transitional arrangements for IFRS 9 or analogous ECLs.

The comparison of Bank's own funds and capital and leverage ratios with and without the application of transitional arrangements for IFRS 9 or analogous ECLs, and with and without the application of the temporary treatment in accordance with Article 468 of the CRR is presented below:

At 31 December 2021	**€ 000**
Available capital	
CET1 capital	**130,145**
CET1 capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**127,956**
Tier1 capital	**130,145**
Tier 1 capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**127,956**
Total capital	**130,145**
Total capital as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**127,956**
Risk-weighted assets	
Total risk-weighted assets	**805,762**
Total risk-weighted assets as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**805,811**
Capital Ratios	
CET1 (as a percentage of risk exposure amount)	**16.15%**
CET1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**15.88%**
Tier 1 (as a percentage of risk exposure amount)	**16.15%**
Tier 1 (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**15.88%**
Total capital (as a percentage of risk exposure amount)	**16.15%**
Total capital (as a percentage of risk exposure amount) as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**15.88%**
	€ 000
Leverage ratio	
Leverage ratio total exposure measure	**1,173,187**
Leverage ratio	**11.09%**
Leverage ratio as if IFRS 9 or analogous ECLs transitional arrangements had not been applied	**10.90%**

6.4 Internal Capital Adequacy Assessment Process (ICAAP)

The Bank considers the Internal Capital Adequacy Assessment Process (ICAAP) embedded in Pillar II as a tool that ensures the proper measurement of material risks and capital and allows for better capital management and improvements in risk management. Therefore, it facilitates a better alignment between material risks and regulatory capital in order to have better capital deployment and improvements in the risk management and mitigation techniques adopted by the Bank. The ICAAP as required by the MFSA Banking Rule BR/12: The Supervisory Review Process of Credit Institutions authorised under the Banking Act, 1994, is performed on an annual basis.

6 Capital risk management *(continued)*

Therefore, ICAAP is a process that the Bank utilises to ensure that:

- there is adequate identification, measurement, aggregation and monitoring of the Bank's risks;
- adequate internal capital is held by the institution in relation to its risk profile; and
- the Bank uses sound risk management systems and there is the intention to develop them further.

The Board and the Bank's Executive Team take overall responsibility for the conceptual design and technical details of the ICAAP document. Apart from the responsibility for the conceptual design, the Board discussed, approved, endorsed and delivered the yearly ICAAP submission. The Bank's independent Risk Management Function is involved in the ICAAP with a view to ensuring that the process reflects and takes cognisance of the Bank's risk management activities and processes.

The ICAAP is an ongoing process which starts with defining risk strategy followed by identifying, quantifying and aggregating risks, determining risk-bearing ability, allocating capital, establishing limits and ongoing risk monitoring. The individual elements of the process are performed with varying regularity. All the activities described are examined at least once a year to ensure that they are up to date, adequate and also adjusted to current underlying conditions when necessary.

The process involves a quantitative assessment of individual types of risk and an assessment of the existing methods and systems for monitoring and managing risk (qualitative assessment). The risk assessment concept is based on a scoring procedure, thus providing a comprehensive overview of the risk situation of the Bank.

The basis for the quantitative implementation of the ICAAP is the risk-bearing capacity calculation which demonstrates that adequate capital is in place at all times to provide sufficient cover for risks that have been entered into and which also ensures such cover is available for the future. The Bank's ICAAP is based upon a 'Pillar I Plus' approach whereby the Pillar I capital requirement for credit, market and operational requirements are supplemented by the capital allocation for other material risks not fully addressed within Pillar I. The risks considered for ICAAP include concentration, liquidity, reputational and strategic risks, interest rate risk in the banking book, and risks arising from the macroeconomic environment.

The Bank's ICAAP contains three year projections as well as the capital plan, and the Board monitors that there are adequate capital resources to support the corporate goals contained within the Bank's plan and the associated risks.

The Bank also covers Pillar II capital requirements through stress testing processes to forecast the Bank's projected capital requirements and resources in a range of stress scenarios. This enables the Bank to guarantee that it can meet its minimum regulatory capital requirements in a stressed environment. The results of the ICAAP once again show that the Bank maintains a comfortable level of excess capital and substantial liquidity that ensured the flexibility and resources needed to achieve the long-term strategic objectives of the Bank, even in situations of market stress.

7 Leverage

The leverage ratio is a regulatory and supervisory tool intended to provide a transparent and non-risk based measurement of an institution to supplement the risk-based capital requirements.

The leverage ratio is calculated on the end of year capital position as a proportion of total exposures. Capital is defined as Tier 1 capital in line with Article 25 of the CRR, while total exposure relates to the total on- and off-balance sheet exposures less the deductions applied to Tier 1 capital.

During 2016, the European Commission published a Proposal to amend Regulation 575/2013 (CRR), which included the introduction of a 3% leverage ratio as a binding Pillar I requirement by 2018. The Bank complies with a 3% leverage ratio based on fully-transitioned Basel III standards.

7 **Leverage** *(continued)*

The following table represents the Bank's estimated leverage ratio determined in accordance with the requirements stipulated by Implementing Regulation EU 2016/200.

	2021 € 000
Tier 1 capital	**130,145**
Leverage ratio total exposure measure	**1,173,187**
Leverage ratio	**11.09%**

The table shown hereunder represents the amounts making up the leverage ratio exposure

	2021 € 000
On-balance sheet exposures (excluding derivatives and SFTs)	
On-balance sheet items (excluding derivatives and SFTs, but including collateral)	**1,135,080**
Asset amounts deducted in determining Tier 1 capital	**(213)**
On-balance sheet exposures (excluding derivatives and SFTs)	**1,134,867**
Off-balance sheet exposures	
Off-balance sheet exposures at gross notional amount	**209,733**
Adjustments for conversion to credit equivalent amounts	**(171,412)**
Off-balance sheet exposures	**38,321**

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

	2021 €000
Total assets as per published financial statements	**1,139,614**
Adjustment for off-balance sheet items	**38,321**
Other adjustments:	**(4,748)**
Leverage ratio total exposure measure	**1,173,187**

7 **Leverage** *(continued)*

The table below shows the different on-balance sheet exposures in relation to the calculation of the leverage ratio.

	2021 € 000
Total on-balance sheet exposures (excluding derivatives and SFTs), of which:	
Exposures treated as sovereigns	**298,887**
Public sector entities	**545**
Multilateral Development Banks	**3,453**
International Organisations	**896**
Institutions	**98,318**
Secured by mortgages on immovable property	**435,737**
Retail	**16,038**
Corporate	**64,156**
Exposures in default	**26,865**
Other exposures	**189,972**
	1,134,867

The leverage ratio is a regulatory and supervisory instrument used by the Regulator to limit the build-up of excessive leverage. The leverage ratio at 31 December 2021 stood at 11.1%

The Bank is currently not at risk in curtailing excessive leverage since the growth in CET1 capital of 8.5% was greater than the 3.3% increase in the Bank's total exposure measure. As a result, the Leverage ratio is expected to remain well above the mandatory requirement. Board limits to the leverage ratio are set and reviewed annually and the ratio is monitored at every Audit & Risk Committee to ensure that it remains above the tolerance limit set by the Board of Directors. This limit supports the Bank's attitude towards finding a suitable balance between risk and returns provided to shareholders.

8 **Remuneration policy**

Information on the Bank's remuneration policy and practices is disclosed in the Remuneration Report within the Annual Report located on page 23.

9 **Other Directorships**

In terms of Article 91 of Directive 2013/36/EU (CRD IV), directors of an institution that is significant in terms of its size, internal organisation and the nature, scope and complexity of its activities shall not hold more than one of the following combinations of directorships at the same time:

(a) one executive directorship with two non-executive directorships;
(b) four non-executive directorships.

According to the 'Guide to banking supervision' issued by the European Central Bank in November 2014, a credit institution will be considered significant if any one of the following conditions is met:

- the total value of its assets exceeds €30 billion or – unless the total value of its assets is below €5 billion – exceeds 20% of national GDP;
- it is one of the three most significant credit institutions established in a Member State;
- it is a recipient of direct assistance from the European Stability Mechanism; or
- the total value of its assets exceeds €5 billion and the ratio of its cross-border assets/liabilities in more than one other participating Member State to its total assets/liabilities is above 20%.

Lombard Bank Malta p.l.c. does not meet any of the above criteria, and therefore is currently not considered significant by banking supervisors. Accordingly, the Bank is exempt from the requirements of Article 91 of CRD IV.

9 **Other Directorships** *(continued)*

The Bank is not disclosing the number of directorships held by the members of the Bank's Board of Directors on the basis of materiality in terms of Article 432 of the CRR.

10 **Recruitment and Diversity policy**

The Bank is aware that a vigorous and professional approach to recruitment and selection of prospective staff members within the Bank helps it to attract and appoint those individuals having the necessary skills and attributes compatible with achieving the Bank's overall objectives. Thus, the Bank ensures that appointments at all levels are based on each individual's knowledge, skills, expertise and merit, as required by laws, rules, regulations, etc. and in line with policy.

The Bank undertakes a rigorous selection process for all prospective staff members bearing in mind the key activities, tasks and skills required. As part of the selection process, multiple interviews are conducted, during which the individual's knowledge, experience, skills and competence are evaluated against those of other individual.

The Bank continues to promote diversity with no discrimination as to gender, race, family, disability, sexual orientation, identity or preference, etc.

Bearing its objectives in mind, the Bank, particularly by virtue of the Board appointed Suitabilities & Evaluations Committee, endeavours to have a Board of Directors composed of members possessing diverse skills and expertise that allow the Board to create value for shareholders by ensuring that the specific risks pursued by the Bank as well as risks that are intrinsic to banking business are appropriately managed and mitigated within the Bank's risk appetite.

Five Year Summary
Statements of Financial Position
As at 31 December

Group

	2021	2020	2019	2018	2017
	€ 000	€ 000	€ 000	€ 000	€ 000
Assets					
Balances with Central Bank of Malta, treasury bills and cash	**126,279**	169,687	182,348	128,726	215,133
Cheques in course of collection	**530**	666	1,214	1,422	1,755
Investments	**227,501**	161,424	111,731	100,070	75,895
Loans and advances to banks	**78,279**	96,985	121,060	140,581	97,048
Loans and advances to customers	**642,893**	621,129	552,043	511,124	428,611
Investment in associates	**3,006**	1,932	1,684	1,684	1,575
Intangible assets	**2,145**	2,050	2,000	1,701	1,648
Property, plant and equipment	**65,346**	50,928	43,348	38,554	31,753
Assets classified as held for sale	**661**	134	134	778	822
Current tax assets	**2,691**	1,156	193	865	1,557
Deferred tax assets	**9,779**	10,117	9,801	9,221	8,980
Inventories	**1,324**	1,274	1,468	1,360	1,164
Trade and other receivables	**10,787**	9,136	5,625	5,010	8,826
Accrued income and other assets	**4,170**	4,337	9,648	8,973	7,979
Total assets	**1,175,391**	1,130,955	1,042,297	950,069	882,746
Equity and liabilities					
Equity					
Share capital	**11,192**	11,044	11,044	11,044	11,044
Share premium	**18,530**	18,530	18,530	18,530	18,530
Property revaluation reserve	**13,040**	6,383	6,384	6,384	2,420
Investment revaluation reserve	**5,180**	7,181	7,978	4,975	4,113
Reserve for General Banking Risks	**2,903**	2,903	2,903	2,903	2,903
Other reserves	**2,545**	2,510	2,567	3,094	3,226
Retained earnings	**83,910**	77,470	69,722	61,380	53,904
Equity attributable to equity holders of the Bank	**137,300**	126,021	119,128	108,310	96,140
Non-controlling interests	**8,470**	7,741	7,674	7,525	6,734
Total equity	**145,770**	133,762	126,802	115,835	102,874
Liabilities					
Amounts owed to banks	**1,224**	5,602	5,871	854	5,362
Amounts owed to customers	**977,143**	941,110	864,993	788,044	733,151
Provisions for liabilities and other charges	**2,113**	2,632	3,236	3,135	3,177
Current tax liabilities	**809**	844	1,128	-	229
Deferred tax liabilities	**6,844**	6,448	6,832	5,264	3,914
Other liabilities	**30,649**	29,665	21,949	27,138	23,217
Accruals and deferred income	**10,839**	10,892	11,486	9,799	10,822
Total liabilities	**1,029,621**	997,193	915,495	834,234	779,872
Total equity and liabilities	**1,175,391**	1,130,955	1,042,297	950,069	882,746
Memorandum items					
Contingent liabilities	**13,195**	10,851	11,671	14,148	9,078
Commitments	**195,848**	200,870	225,826	202,384	247,737

Five Year Summary
Income Statements
For the Year Ended 31 December 2021

Group

	2021	2020	2019	2018	2017
	€ 000	€ 000	€ 000	€ 000	€ 000
Interest receivable and similar income	**25,725**	24,898	25,285	23,188	21,426
Interest expense	**(6,169)**	(6,026)	(5,605)	(5,677)	(5,992)
Net interest income	**19,556**	18,872	19,680	17,511	15,434
Other operating income	**43,856**	41,731	40,474	45,609	42,747
Other operating charges	**(51,836)**	(46,107)	(44,311)	(49,225)	(46,372)
Credit impairment losses	**1,464**	(3,973)	(549)	(234)	(2,835)
Share of (loss)/profit of investment accounted for using equity method	**(402)**	(151)	-	109	(106)
Profit before taxation	**12,638**	10,372	15,294	13,770	8,868
Income tax expense	**(4,759)**	(3,230)	(5,424)	(4,831)	(3,165)
Profit for the year	**7,879**	7,142	9,870	8,939	5,703
Attributable to:					
Equity holders of the Bank	**7,481**	6,640	9,320	8,447	5,129
Non-controlling interests	**398**	502	550	492	574
Profit for the year	**7,879**	7,142	9,870	8,939	5,703

Five Year Summary
Statements of Cash Flows
For the Year Ended 31 December

Group

	2021	2020	2019	2018	2017
	€ 000	€ 000	€ 000	€ 000	€ 000
Net cash flows generated from/(used in) operating activities	**31,636**	14,475	53,125	(30,882)	(27,882)
Cash flows from investing activities					
Dividends received	**81**	105	211	369	326
Interest received from investments	**3,012**	2,198	2,325	2,011	2,196
Proceeds on maturity/disposal of investments	**6,760**	16,468	8,163	4,406	3,285
Purchase of investments	**(75,270)**	(67,862)	(15,905)	(27,850)	(905)
Purchase of property, plant and equipment	**(7,601)**	(8,942)	(3,345)	(2,921)	(2,943)
Proceeds from disposal of property, plant and equipment	**-**	18	-	-	-
Acquisition of non-controlling interests	**-**	-	-	-	(429)
Purchase of investment in associate	**(1,500)**	(399)	-	-	-
Net cash inflow arising from acquisition of subsidiary	**833**	-	-	-	-
Net cash flows (used in)/from investing activities	**(73,685)**	(58,414)	(8,551)	(23,985)	1,530
Cash flows from financing activities					
Dividends paid to equity holders of the Bank	**(862)**	-	(1,436)	(1,149)	(1,149)
Dividends paid to non-controlling interests	**(429)**	(427)	(429)	(427)	(244)
Payment from lease liability	**(527)**	(409)	-	-	-
Net cash flows used in financing activities	**(1,818)**	(836)	(1,865)	(1,576)	(1,393)

Report on the audit of the financial statements

Our opinion

In our opinion:

- The Group financial statements and Parent Company financial statements (the "financial statements") give a true and fair view of the Group and the Bank's financial position of Lombard Bank Malta p.l.c. as at 31 December 2021, and of the Group's and the Bank's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU; and
- The financial statements have been prepared in accordance with the requirements of the Maltese Companies Act (Cap. 386) and the Maltese Banking Act (Cap. 371).

Our opinion is consistent with our additional report to the Audit & Risk Committee.

What we have audited

Lombard Bank Malta p.l.c.'s financial statements, comprise:

- the Consolidated and Parent Company statements of financial position as at 31 December 2021;
- the Consolidated and Parent Company income statements and statements of comprehensive income for the year then ended;
- the Consolidated and Parent Company statements of changes in equity for the year then ended;
- the Consolidated and Parent Company statements of cash flows for the year then ended; and
- the notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements section of our report*.

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

Independence

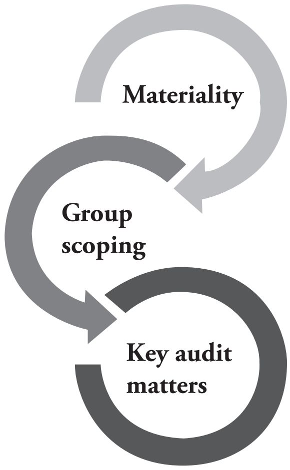
We are independent of the Group and the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code) together with the ethical requirements of the Accountancy Profession (Code of Ethics for Warrant Holders) Directive issued in terms of the Accountancy Profession Act (Cap. 281) that are relevant to our audit of the financial statements in Malta. We have fulfilled our other ethical responsibilities in accordance with these Codes.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Bank and its subsidiaries are in accordance with the applicable law and regulations in Malta and that we have not provided non-audit services that are prohibited under Article 18A of the Accountancy Profession Act (Cap. 281).

The non-audit services that we have provided to the Bank and its subsidiaries, in the period from 1 January 2021 to 31 December 2021, are disclosed in note 33 to the financial statements.

Our audit approach

Overview



Overall group materiality: €642,000, which represents approximately 5% of 3 years average profit before tax.

The audit procedures carried out covered all the components within the Group namely Lombard Bank Malta p.l.c. (the parent company) and its subsidiaries Redbox Limited, MaltaPost p.l.c., Tanseana Limited, Lombard Select SICAV p.l.c. and Lombard Capital Asset Management Limited which are all based in Malta.

Credit loss allowances in respect of loans and advances to customers of Lombard Bank Malta p.l.c.

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where the directors made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall group materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Overall group materiality	€642,000
How we determined it	Approximately 5% of 3 years average profit before tax
Rationale for the materiality benchmark applied	We chose profit before tax as the benchmark because, in our view, it is the benchmark against which the performance of the Group is most commonly measured by users, and is a generally accepted benchmark. We chose an average of 3 years as it was determined more appropriate in view of the fluctuations in results during the current year. We chose 5% which is within the range of quantitative materiality thresholds that we consider acceptable.

We agreed with the Audit & Risk Committee that we would report to them misstatements identified during our audit above €64,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the Key audit matter
Credit loss allowances in respect of loans and advances to customers of Lombard Bank Malta p.l.c. Credit loss allowances in respect of loans and advances to customers represent management's best estimate of Expected Credit Losses ('ECLs') within the loan portfolios at the balance sheet date. The development of the models designed to estimate ECLs on loans measured at amortised cost in accordance with the requirements of IFRS 9 requires a considerable level of judgement since the determination of ECLs is subject to a high degree of estimation uncertainty. The outbreak of the COVID-19 pandemic has exacerbated the level of uncertainty around the calculation of ECLs, giving rise to heightened subjectivity in the determination of model assumptions used to estimate key model risk parameters and hence necessitating a higher level of expert judgement. Credit loss allowances relating to all loans and advances in the Bank's portfolios are determined at an instrument level. In general, the Bank calculates ECLs by multiplying three main components: probability of default (PD), loss given default (LGD) and exposure at default (EAD): i. Probability of default ("PD"): the likelihood of a borrower defaulting on its financial obligation either over the next 12 months or over the remaining lifetime of the obligation. ii. Loss given default ("LGD"): the expected losses taking into account, among other attributes, the mitigating effect of collateral value (if any) at the time it is expected to be realised and the time value of money. The LGD modelling methodology utilises historical experience, which might result in limitations in its reliability to appropriately estimate ECLs especially during periods characterised by unprecedented economic conditions such as those currently experienced as a result of the COVID-19 pandemic. iii. Exposure at default ("EAD"): the expected exposure in the event of a default (including any expected drawdowns of committed facilities). The Bank also applies overlays based on expert judgement where management's view is that the calculated ECLs based on	During our audit of the financial statements for the year ended 31 December 2021, we continued to focus on the key drivers of the estimation of ECL. Apart from assessing the continuing appropriateness of management assumptions, updates to key parameters and model enhancements, largely driven by the outbreak of the COVID-19 pandemic, were evaluated and tested. Discussions with the Audit & Risk Committee and management were held on: - inputs, assumptions and adjustments to ECL, in particular changes to risk factors and other inputs within the Bank's models, in respect of which we provided updates on the results of our testing procedures; - the application of forward economic scenarios, including the severity and magnitude of modelled downside scenarios, particularly in the context of the potential future impacts of the COVID-19 pandemic; - considerations around post-model adjustments, mainly in response to the impact of COVID-19 and Malta's grey-listing, and the estimation uncertainty involved in determining ECLs on the basis of historical experience; and - individually significant loan impairments. With respect to the ECL models utilised by the Bank, the continued appropriateness of the modelling policies and methodologies used was independently assessed by reference to the requirements of IFRS 9. *ECL calculation for non-defaulted loan exposures and a number of defaulted loans which are not individually significant* We understood and critically assessed the models used for ECL estimation for the Bank's loan portfolio. Since modelling assumptions and parameters are based on historic data, we assessed whether historic experience was representative of current circumstances and of the recent losses incurred within the portfolios. The appropriateness of management's judgements was also independently considered in respect of calculation methodologies, calibration of PDs and LGDs, segmentation and

Key audit matter	How our audit addressed the Key audit matter
these key inputs do not fully capture the risks within the Bank's loan portfolios. For non-defaulted (Stage 1 and 2) loans and a number of defaulted (Stage 3) loans which are not individually significant, the Bank uses internally developed statistical models. For non-defaulted (Stages 1 and 2) exposures, PDs are estimated using historical model development data based on the Bank's own experience as available at the reporting date. For exposures secured by immovable properties, LGDs are driven by the adjusted loan-to-value ratio of the individual facilities and takes into account other assumptions, including market value haircut (which includes costs to sell), time to sell and the impact of discounting the collateral from the date of realisation back to the date of default. The maximum period considered when measuring ECLs is the maximum contractual period over which the Bank is exposed to credit risk. For individually significant defaulted (Stage 3) exposures, discounted cash flow models are utilised in order to estimate ECLs. Internal credit risk management practices are used to determine when a default has occurred, considering quantitative and qualitative factors where appropriate. Judgement is required to determine when a default has occurred and then to estimate the expected future cash flows related to defaulted (Stage 3) exposures which are dependent on parameters or assumptions such as the valuation of collateral (including forced sale discounts and assumed realisation period) or forecasted operating cash flows. The Bank is required to assess multiple scenarios in this respect, which scenarios will have probabilities attached. The local impact of the pandemic has been mitigated by a number of government programmes and measures, including general payment moratoria which have given rise to the deferral of payments of capital and/or interest over time periods that potentially extended until the end of the current financial reporting period. This factor has increased the level of uncertainty around judgements made in determining the timing of defaults and in respect of staging. For the purposes of avoiding the cliff edge effect on ECLs upon expiry of the moratoria, the Bank reassessed the internal credit risk ratings of all exposures with approved moratoria on the basis of quantitative and qualitative characteristics to enable the identification of significant increase in credit risk (SICR) or Unlikeliness-to-Pay (UTP) events as early as possible. Under IFRS 9, the Bank is required to formulate and incorporate multiple forward-looking economic conditions, reflecting	selection of macro-economic variables. Model calculations were also tested independently. Substantive procedures were performed as follows: - Performed an overall assessment of the ECL provision levels by stage to determine if they were reasonable considering the Bank's portfolio, risk profile, credit risk management practices and the macro-economic environment. - Tested a sample of loans to independently review the borrower's financial performance and ability to meet loan repayments and assess the appropriateness of the credit rating assigned by management, taking into consideration the impact of COVID-19 on the repayment capabilities of the sampled borrowers. - Challenged the criteria used to allocate an asset to stage 1, 2 or 3 in accordance with IFRS 9 and tested a sample of assets in stage 1, 2 and 3 to verify that they were allocated to the appropriate stage. - Tested the completeness and accuracy of the critical data extracted from the underlying systems, that is utilised within the models for the purposes of the year end ECL calculation. - Risk based testing of models, including a review of the continuing appropriateness of model assumptions. We tested the assumptions, inputs and formulas used in ECL models on a sample basis. This included assessing the appropriateness of model design and formulas used, and recalculating PDs, LGDs and EADs on a sample basis, through the involvement of subject matter experts. - We assessed the reasonableness of modelled PDs through a comparison of historically predicted and observed default rates, taking into consideration the potential postponement in timing of defaults due to government support programmes and measures, and the adequacy of modelled LGDs in light of the potential impact of the pandemic and Malta's grey-listing by the FATF on local property prices. - We also assessed the reasonableness of market value haircuts and time to sell assumptions used as inputs to modelled LGDs, in light of the potential impact of the pandemic and Malta's grey-listing on local property prices. Additionally, we assessed the appropriateness of the post model overlay intended to address early identification of SICR or UTP events in respect of those exposures to which the bank extended general payment moratoria or which benefitted from Government support schemes or measures. - Tested the multiple macroeconomic scenarios and variables using our experts to assess their reasonableness. We assessed the appropriateness of changes effected to factor the impact of the pandemic, including the recalibration of probability

Key audit matter	How our audit addressed the Key audit matter

management's view of potential future economic variables and environments, into the ECL estimates. A number of macro-economic scenarios based on the selected macro-economic variables are considered to capture non-linearity across credit portfolios. The complexity attributable to this factor requires management to develop multiple macro-economic scenarios involving the use of significant judgements.

The outbreak of COVID-19 and the government support and relief measures adopted to mitigate it have significantly impacted macroeconomic factors such as the gross domestic product (GDP), increasing the uncertainty around judgements made in determining the severity and likelihood of macroeconomic forecasts across the different economic scenarios used in ECL models. Overly sensitive ECL modelled outcomes can be observed when current conditions fall outside the range of historical experience. The level of uncertainty has been exacerbated by Malta's inclusion in the list of jurisdictions under increased monitoring, referred to as the grey-list, by the Financial Action Task Force ('FATF') during the year ended 31 December 2021. This gave rise to an elevated level of uncertainty in respect of judgements made in determining macroeconomic forecasts underlying the different economic scenarios used in ECL models. The Bank has applied overlays based on expert judgement to reflect risks that are not fully captured by the ECL models.

Data used in the impairment calculation is sourced from a number of systems, including systems that are not necessarily used for the preparation of accounting records. The ECL models are based on a general-purpose application which requires extensive manual handling of data. This increases risk around the accuracy and completeness of data used to determine assumptions and to operate the ECL models. In some cases, data is unavailable and reasonable alternatives have been applied to allow calculations to be performed.

Since the estimation of ECLs is subjective in nature and inherently judgemental, the Bank's application of the IFRS 9 impairment requirements is deemed to be an area of focus, especially in the context of COVID-19, which has an unprecedented impact on the economy and has significantly increased the level of estimation uncertainty around the calculation of credit loss allowances.

We focused on credit loss allowances due to the subjective nature of specific data inputs into the calculation and the subjective judgements involved in both timing of recognition of impairment and the estimation of the size of any such impairment.

weights. We assessed whether the severity of the forecasted macroeconomic variables was appropriate in view of the pandemic and the high level of uncertainty surrounding the economic conditions. We challenged the correlation and impact of the macroeconomic factors on the ECL.

Our testing of models and model assumptions did not highlight material differences.

Based on the evidence obtained, we found that the model assumptions, data used within the models and overlays are reasonable.

ECL calculation for defaulted individually significant loan exposures

For defaulted exposures within the loan portfolio, the appropriateness of the methodology and policy used to calculate ECLs was independently assessed. We understood and evaluated the processes for identifying default events within loan portfolios, as well as the impairment assessment process.

Substantive procedures were performed in respect of identification of defaults as follows:

- Assessed critically the criteria used by management for identifying borrowers whose financial performance is expected to be particularly impacted by COVID-19 and for determining whether a UTP/default event had occurred by testing a sample of loans with characteristics that might imply a default event had occurred (for example a customer experiencing financial difficulty or material sector disruption) to challenge whether default events had actually occurred and to assess whether default events had been identified by management in a timely manner.
- Selected a sample of performing loans, including from within those sectors that we consider to have been significantly impacted by the pandemic, which had not been identified by management as potentially defaulted, to form our own judgement as to whether that was appropriate and to further challenge whether all relevant events had been identified by management.

Substantive procedures were performed on defaulted exposures in respect of the estimation of the amounts of the respective ECL provisions, as follows:

- Reviewed the credit files of a selected sample of loans to understand the latest developments at the level of the borrower and the basis of measuring the ECL provisions and considered whether key judgements were appropriate taking

Key audit matter	How our audit addressed the Key audit matter
Accordingly, summarising the key areas relevant to the bank's measurement of ECLs would include: - Allocation of assets to stage 1, 2, or 3 using criteria in accordance with IFRS 9; - Accounting interpretations and modelling assumptions used to build the models that calculate the ECL; - Completeness and accuracy of data used to calculate the ECL; - Inputs and assumptions used to estimate the impact of multiple macroeconomic scenarios; and - Measurements of individually assessed provisions including the assessment of multiple scenarios. Relevant references in the Annual Financial Report and Financial Statements: - Accounting policy: note 1.7 - Credit risk management: note 2.3; - Accounting estimates and judgements: note 3.2;	- Note on Credit impairment losses: note 32; and - Note on Loans and advances to customers: note 8.cognisance of the pandemic. - Challenged the severity of scenarios being applied for these exposures, together with their respective probability weights by forming an independent view of the recoverability of the selected loan exposures under different scenarios, assigning probabilities independently and comparing the outcomes to that of the Bank. - Tested key inputs to and reperformed the impairment calculation used to derive expected cash flows under different scenarios. - Assessed the appropriateness of a sample of property valuations securing impaired loans through the use of experts. In the case of some impairment provisions, we formed a different view from that of management, but in our view the differences were within a reasonable range of outcomes.

How we tailored our group audit scope

The Group is composed of six components: Lombard Bank Malta p.l.c. (the parent company), and its subsidiaries Redbox Limited, MaltaPost p.l.c., Tanseana Limited, Lombard Select SICAV p.l.c. and Lombard Capital Asset Management Limited. MaltaPost p.l.c. has been determined to be a financially significant entity. We tailored the scope of our audit in order to perform sufficient work on all components to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates, and local statutory requirements.

The Group audit team performed all of this work by applying the Group overall materiality, together with additional procedures performed on the consolidation. This gave us sufficient appropriate audit evidence for our opinion on the Group financial statements as a whole.

Other information

The directors are responsible for the other information. The other information comprises all of the information in the Annual Financial Report (but does not include the financial statements and our auditor's report thereon).

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except as explicitly stated within the *Report on other legal and regulatory requirements*.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors and those charged with governance for the financial statements

The directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Maltese Companies Act (Cap. 386) and the Maltese Banking Act (Cap. 371), and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Group's and the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or the Bank or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's and the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's and the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's or the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Group's or the Bank's ability to continue as a going concern. In particular, it is difficult to evaluate all of the potential implications that COVID-19 will have on the Group's and the Bank's operations, assets and liabilities, and the disruption to their business and the overall economy.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on compliance with the requirements of the European Single Electronic Format Regulatory Technical Standard (the "ESEF RTS"), by reference to Capital Markets Rule 5.55.6

We have undertaken a reasonable assurance engagement in accordance with the requirements of Directive 6 issued by the Accountancy Board in terms of the Accountancy Profession Act (Cap. 281) - the Accountancy Profession (European Single Electronic Format) Assurance Directive (the "ESEF Directive 6") on the Annual Financial Report of Lombard Bank Malta p.l.c. for the year ended 31 December 2021, entirely prepared in a single electronic reporting format.

RESPONSIBILITIES OF THE DIRECTORS

The directors are responsible for the preparation of the Annual Financial Report, including the consolidated financial statements and the relevant mark-up requirements therein, by reference to Capital Markets Rule 5.56A, in accordance with the requirements of the ESEF RTS.

OUR RESPONSIBILITIES

Our responsibility is to obtain reasonable assurance about whether the Annual Financial Report, including the consolidated financial statements and the relevant electronic tagging therein, complies in all material respects with the ESEF RTS based on the evidence we have obtained. We conducted our reasonable assurance engagement in accordance with the requirements of ESEF Directive 6.

OUR PROCEDURES INCLUDED:

- Obtaining an understanding of the entity's financial reporting process, including the preparation of the Annual Financial Report, in accordance with the requirements of the ESEF RTS.
- Obtaining the Annual Financial Report and performing validations to determine whether the Annual Financial Report has been prepared in accordance with the requirements of the technical specifications of the ESEF RTS.
- Examining the information in the Annual Financial Report to determine whether all the required taggings therein have been applied and whether, in all material respects, they are in accordance with the requirements of the ESEF RTS.

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

OPINION

In our opinion, the Annual Financial Report for the year ended 31 December 2021 has been prepared, in all material respects, in accordance with the requirements of the ESEF RTS.

OTHER REPORTING REQUIREMENTS

The *Annual Financial Report and Financial Statements 2021* contains other areas required by legislation or regulation on which we are required to report. The Directors are responsible for these other areas.

The table below sets out these areas presented within the Annual Financial Report, our related responsibilities and reporting, in addition to our responsibilities and reporting reflected in the *Other information* section of our report. Except as outlined in the table, we have not provided an audit opinion or any form of assurance.

Area of the *Annual Report and Financial Statements 2021* and the related Directors' responsibilities	Our responsibilities	Our reporting
Directors' report (on pages 8 to 16) The Maltese Companies Act (Cap. 386) requires the directors to prepare a Directors' report, which includes the contents required by Article 177 of the Act and the Sixth Schedule to the Act.	We are required to consider whether the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements. We are also required to express an opinion as to whether the Directors' report has been prepared in accordance with the applicable legal requirements. In addition, we are required to state whether, in the light of the knowledge and understanding of the Company and its environment obtained in the course of our audit, we have identified any material misstatements in the Directors' report, and if so to give an indication of the nature of any such misstatements. With respect to the information required by paragraphs 8 and 11 of the sixth schedule to the Act, our responsability is limited to ensuring that such information has been provided.	In our opinion: - the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and - the Directors' report has been prepared in accordance with the Maltese Companies Act (Cap. 386). We have nothing to report to you in respect of the other responsibilities, as explicitly stated within the *Other information section*.
Statement of Compliance with the Principles of Good Corporate Governance (on pages 17 to 22) The Capital Market Rules issued by the Malta Financial Services Authority require the directors to prepare and include in the Annual Financial Report a Statement of Compliance with the Code of Principles of Good Corporate Governance within Appendix 5.1 to Chapter 5 of the Capital Market Rules. The Statement's required minimum contents are determined by reference to Capital Market Rule 5.97. The Statement provides explanations as to how the Company has complied with the provisions of the Code, presenting the extent to which the Company has adopted the Code and the effective measures that the Board has taken to ensure compliance throughout the accounting period with those Principles.	We are required to report on the Statement of Compliance by expressing an opinion as to whether, in light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we have identified any material misstatements with respect to the information referred to in Capital Market Rules 5.97.4 and 5.97.5, giving an indication of the nature of any such misstatements. We are also required to assess whether the Statement of Compliance includes all the other information required to be presented as per Capital Market Rule 5.97. We are not required to, and we do not, consider whether the Board's statements on internal control included in the Statement of Compliance cover all risks and controls, or form an opinion on the effectiveness of the Company's corporate governance procedures or its risk and control procedures.	In our opinion, the Statement of Compliance has been properly prepared in accordance with the requirements of the Capital Market Rules issued by the Financial Services Authority. We have nothing to report to you in respect of the other responsibilities, as explicitly stated within the *Other information section*.

<table>
<tr><th>Area of the Annual Report and Financial Statements 2021 and the related Directors' responsibilities</th><th>Our responsibilities</th><th>Our reporting</th></tr>
<tr><td>Remuneration report

The Capital Market Rules issued by the Financial Services Authority require the directors to prepare a Remuneration report, including the contents listed in Appendix 12.1 to Chapter 12 of the Capital Market Rules.</td><td>We are required to consider whether the information that should be provided within the Remuneration report, as required in terms of Appendix 12.1 to Chapter 12 of the Capital Market Rules, has been included.</td><td>In our opinion, the Remuneration report has been properly prepared in accordance with the requirements of the Capital Market Rules issued by the Financial Services Authority.</td></tr>
<tr><td></td><td>Other matters prescribed by the Maltese Banking Act (Cap. 371)

In terms of the requirements of the Maltese Banking Act (Cap. 371), we are also required to report whether:

- 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 of those books;
- the bank's financial statements are in agreement with the books of account;
- in our opinion, and to the best of our knowledge and according to the explanations given to us, the financial statements give the information required by any law which may from time to time be in force in the manner so required.</td><td>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 of those books;
- the bank's financial statements are in agreement with the books of account; and
- to the best of our knowledge and according to the explanations given to us, the financial statements give the information required by any law in force in the manner so required.</td></tr>
<tr><td></td><td>Other matters on which we are required to report by exception

We also have responsibilities under the Maltese Companies Act (Cap. 386) to report to you if, in our opinion, adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us.

We also have responsibilities under the Capital Market Rules to review the statement made by the directors that the business is a going concern together with supporting assumptions or qualifications as necessary.</td><td>We have nothing to report to you in respect of these responsibilities.</td></tr>
</table>

Other matter – use of this report

Our report, including the opinions, has been prepared for and only for the Bank's shareholders as a body in accordance with Article 179 of the Maltese Companies Act (Cap. 386) and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior written consent.

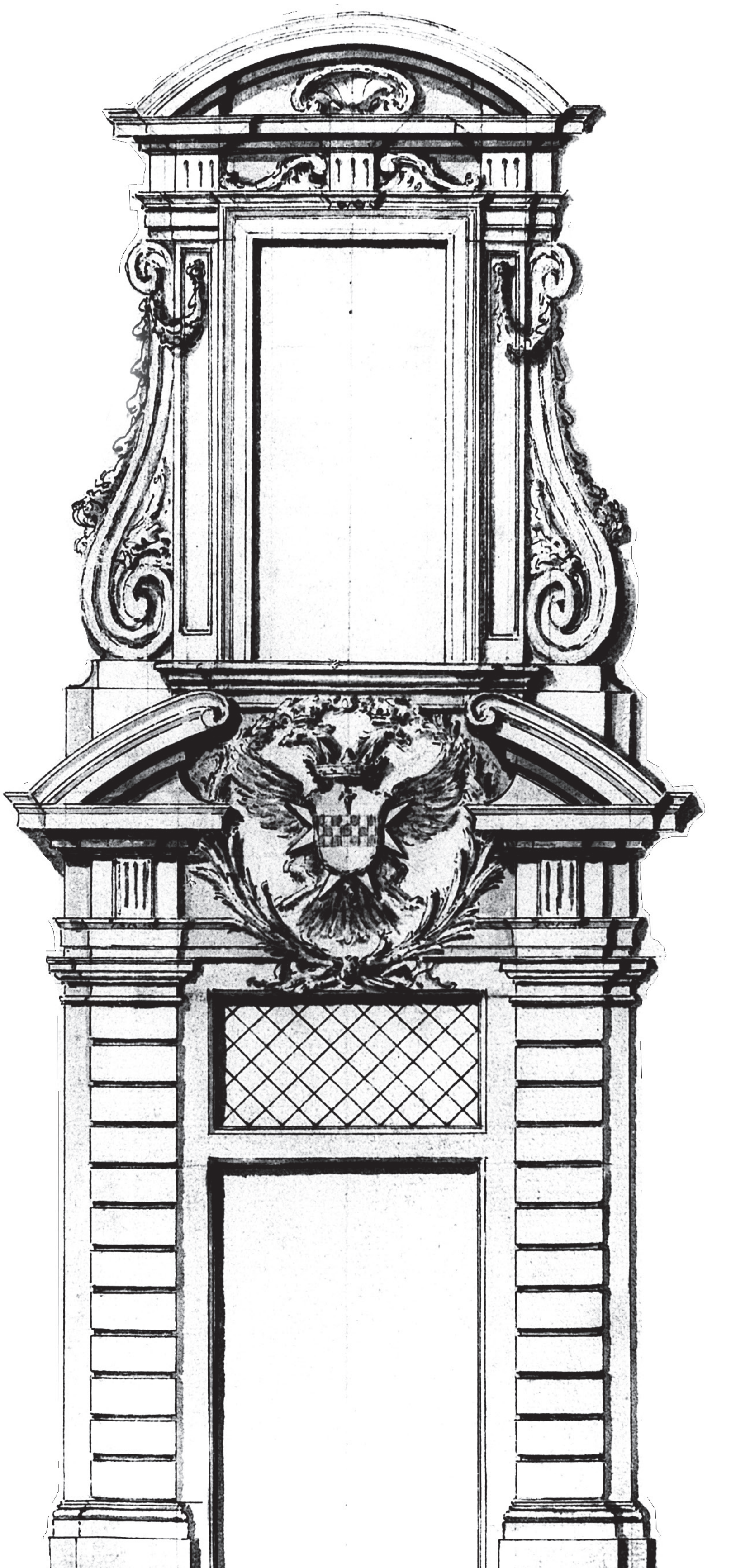
Appointment

We were first appointed as auditors of the Bank on 10 April 2010. Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 12 years.

PricewaterhouseCoopers
78, Mill Street
Zone 5, Central Business District
Qormi
Malta

Fabio Axisa
Partner

20 April 2022



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