Annual Report and Financial Statements 2022

izola Bank

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Annual Report 2022

Company Registration Number: C 16343

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Readers are reminded that the official statutory Annual Report and Financial Statements 2022, authorised for issue by the Board of Directors, is in European Single Electronic Format (ESEF) and is published on our website at: https://www.izolabank.com/mt-en/who-we-are/investor-information/annual-reports-financial-statements

A copy of the Independent auditor's report issued on the official statutory Annual Report and Financial Statements 2022 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 (the ESEF RTS), by reference to Capital Markets Rule 5.55.6.

izola Bank

2022 will surely be remembered for the unexpected resurgence of an unstable geopolitical and macroeconomic climate due to the Russian invasion of Ukraine, supply chain disruptions and rising interest rates as Central Banks attempted to rein in inflation after over a decade of very loose monetary policy.

From the Bank's perspective, we continued the implementation of our growth and diversification strategy, which resulted in a year-on-year growth in operating income of 16%. Furthermore, I would like to mention the issuance of our subordinated bond, which was very well received by the investor community. I would like once again to express our thanks for this clear show of confidence in the Bank.

In early 2022, a new business line was introduced when the Bank launched its residential mortgage product to the retail market in Malta. Subsequently, the Board also considered complementary investment opportunities to accelerate the level of growth in this business line and introduce further diversification, always within a conservative risk profile. In this respect, the Board decided to commence the origination of a portfolio of Dutch NHG (government-guaranteed) mortgages in 2023 whilst continuing to build our local offering. During 2022, we continued the multi-year comprehensive overhaul of our technology platforms, successfully replacing our core factoring software and introducing significant upgrades to our AML/CFT systems and data capabilities.

Looking ahead, the Bank will continue to pursue growth opportunities to further diversify its asset base. The Board acknowledges the need to focus on being agile and responsive enough to meet new demands in a rapidly changing economic environment and continue offering and developing sustainable products, services and solutions through innovation and digitalisation that fully respect the environment around us.

Bank Performance

During the year ended 31 December 2022, the Bank managed to generate growth in its revenue streams, increasing its net interest income by 24% over 2022 levels. Net interest income, which is by far the primary indicator of business performance, grew by €1,484,302 compared to the previous year. This increase resulted in an overall 16% improvement in operating income.

However, the financial year 2022 was also characterised by several exceptional charges, which ultimately resulted in the Bank registering a marginal loss after tax for the year of €284,219. These exceptional charges included one-time costs related to the exchange offer accompanying our subordinated bond issue and a change in IFRS9 provisioning models, resulting in higher Expected Credit Loss (ECL) charges. The Bank also recognised accelerated depreciation on various IT systems that are being replaced as part of the digital transformation programme. Finally, increases in Depositor Compensation Scheme (DCS) contributions due to changes in relevant legislation also contributed to these extraordinary charges.

The Bank's total assets increased by 4.6% to €421,489,265, mainly driven by growth in the lending and factoring portfolios. Factored receivables increased by €23.3 million, or 25% on the prior year, whilst lending increased by €29.0 million, or 22%, compared to 2021. The investment portfolio decreased by €25.7m compared to December 2021, mainly driven by the liquidation of treasury assets to partially fund new business and fair value adjustments due to increased yields.

As of 31 December 2022, the Bank remained well capitalised, with the Capital Adequacy Ratio (CAR) and Core Equity Tier 1 (CET1) Ratio standing at 22.12% and 13.35% respectively, well within the capital requirements established following the Supervisory Review and Evaluation Process (SREP) by the Malta Financial Services Authority (MFSA). The downward movement in the Bank's CET1 ratio was mainly a result of adverse movements on highly rated sovereign bonds classified as hold-to-collect-and-sell (HTC&S), which, following the increase in term market yield curves, impacted revaluation reserves negatively, resulting in a negative fair value reserve net of deferred tax amounting to €10.3 million.

In Financial Year 2022, the Board has decided to initiate a new business line, as the Bank launched its mortgage product offering to the retail market in Malta. In addition, by the date the financial statements were authorised for issue, the Bank signed a term sheet submitted by a leading market provider in order to originate a €100 million portfolio of Dutch mortgages. In this respect, tighter management of liquidity buffers was deemed even more important in light of the launch of the mortgage business line, first locally in 2022, followed by the Netherlands in 2023. In support of this significant development, the Bank is adjusting its funding profile by shifting towards shorter term deposits to fund its mortgage portfolio in order to manage its net interest margin.

Going forward, this portfolio of high-quality liquid assets would be specifically allocated solely to raise funding through ECB operations in order to address the above-mentioned liquidity gaps, attributable to the mortgage business line in particular following the origination of the Dutch mortgage business. Accordingly, management is considering reclassifying its sovereign bond portfolio out of the fair value through other comprehensive income (FVOCI) category into the amortised cost category in 2023, since the financial instruments would be held within a business model where the objective is to hold financial assets to collect contractual cash flows.

The Bank's Liquidity Cover Ratio (LCR) of 725% is significantly above European banking sector norms and results from the Bank's stable, predominantly retail funding base with a high percentage of fixed-term rather than demand deposit funding.

Regulatory Environment

In 2022 the Bank continued strengthening the compliance and risk management functions and remained committed to monitoring all relevant regulatory developments to ensure full compliance with its legal and regulatory obligations. This hard work and commitment were reflected in, amongst others, the outcome of the recent Financial Intelligence Analysis Unit's report on the Bank's internal AML/CFT processes and systems and the periodic Supervisory Review and Evaluation Process (SREP) by the Malta Financial Services Authority.

The Board

The Board of Directors met nine times during the year under review. The corporate governance structure remains robust and is sustained through challenge and guidance to the management team, not only at Board meetings but also through the various Board Committees.

Having served on the Board as a non-executive director since 2000, I assumed the chairpersonship of the Bank in March 2022. On behalf of my fellow board members and the Van Marcke family, I would like to thank Ms Magdalena De Roeck for her twelve years of chairpersonship of the Bank. Her devotion and interest enabled the Bank to further develop as an independent, niche bank focusing on unburdening its customers via digitalisation with a human touch. She can indeed be very proud of her achievement.

After sixteen years of service as a non-executive director, Mr Joseph Caruana communicated his decision to retire and not to offer himself to be re-elected to the Board of Directors at the Annual General Meeting held in March 2022. Mr Caruana was very much appreciated for his vast banking and credit experience, which he gladly shared with his fellow members and management. It was with deep sadness that we received the news that he passed away in December 2022. I would also like to welcome Mr Alain Malschaert to the Board. Appointed in March 2022, I am confident that he will bring additional expertise and insight in the areas of credit risk management and overall governance from his prior years of work experience at a global, systemically important bank where, for over 10 years, he led the credit risk management function.

Solidarity with the community

The Bank strongly believes in taking an active role in society by investing in community-based organisations that directly address pressing issues within the country. Starting in 2017, the Bank partnered with Foodbank Lifeline Foundation, a registered NGO which provides short-term emergency food packs to people in desperate need, regardless of race, religion and gender, until they find a path to stability.

In 2022, Izola Bank continued its financial and practical support to meet the increasing demand for Foodbank Lifeline's services, which became even more relevant this year. We aim to continue helping Foodbank Lifeline not only ease hunger in Malta but also significantly reduce food waste and carbon emissions.

Looking ahead

Besides focusing on growing the retail mortgage portfolio, in 2023, the Bank will remain committed to nurturing its factoring operations, corporate lending activity, and deposit-raising capacity, mainly through our Izola Saver platform. Current economic and market conditions brought about by the factors highlighted in the first paragraph of this statement merit that we approach the future with restraint.

2023 will also be a milestone year when, after 29 years of operations from our various premises in East Street, Valletta, we will move to our new head office at Castille Square, Valletta. This will allow the Bank's staff to work together under one roof and provide more brand visibility due to the landmark location.

Uncertainty reared its head again in the first quarter of 2023 when the international banking sector was hit by the collapse of a few U.S. regional banks and the acquisition of Credit Suisse by UBS in Switzerland. These events led to heightened market turmoil; however, we can safely report that the Bank's operations were unaffected.

Conclusion

On behalf of the Board, I would like to thank our customers for their continued loyalty and support. Finally, I would like to thank the management team and all staff members for their hard work and unfaltering commitment to the Bank.

Ms. Caroline Van Marcke
Chairperson/Director
Izola Bank p.l.c.

26 April 2023

The directors have prepared this report for Izola Bank p.l.c. ("the Bank") in accordance with Article 177 of the Companies Act 1995 (Chapter 386, Laws of Malta) ("the Act") including the further provisions as set out in the sixth schedule of the Act, together with the financial statements of the Bank for the year ended 31 December 2022.

Board of directors

The directors who served throughout the year were as follows:

Members

Ms. Magdalena De Roeck (acted as Chairperson until 24 March 2022)
Ms. Caroline Van Marcke (appointed as Chairperson on 24 March 2022)
Mr. Simon Azzopardi
Mr. Joseph C. Caruana*
Mr. Francis Gouder
Mr. Alain Malschaert (appointed on 24 March 2022)
Mr. Andrew Mifsud
Mr. Guido Mizzi
Mr. Patrick H. Van Leynseele

* After sixteen years of service as non-executive director, Mr. Joseph Caruana communicated his decision to retire and not to offer himself to be re-nominated to the Board of directors at the Annual General Meeting held on 24 March 2022.

Company secretary

Mr. Calvin Bartolo

Principal activities

Izola Bank p.l.c. is registered in Malta as a public limited liability company under the Companies Act, 1995 (Chapter 386, Laws of Malta). The Bank is licensed by the Malta Financial Services Authority to carry out the business of banking in terms of the Banking Act, 1994 (Chapter 371, Laws of Malta).

The Bank is principally engaged in providing corporate banking and factoring services to resident and non-resident customers, including to related parties, with simple and easy to use savings products for both local and foreign individuals and businesses.

Operational Review

A review of the business of the Bank for the year ended 31 December 2022 and an indication of future developments are provided in the Chairperson's Statement, which can be found in the front section of this Annual Report.

Principal risks and uncertainties

The main risks that the Bank has identified are credit risk arising from changes in credit quality and the recoverability of loans and amounts due from Maltese and Belgian counterparties, concentration risk arising from an uneven distribution of counterparties and liquidity and interest rate risks which are inherent in the nature of the business of banking. Other risks which are closely monitored by management include foreign exchange risk and investment price risk, reputational risk, operational risk as well as cyber-security and business continuity risks.

Risk management policies have been established to identify and analyse the risks faced by the Bank, to set out appropriate risk limits and controls, and to monitor risks and adherence to limits. A detailed overview of these risks, together with the respective financial metrics are outlined in Note 4 of the Financial Statements.

Directors' responsibilities for the financial statements

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 Bank as at the end of each reporting period and of the profit or loss for that period. 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 Bank 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 Bank 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 2022 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.

Dividends and reserves

As disclosed in Note 28.1, the Bank declared a net interim dividend of €2,000,000 at the Annual General Meeting held on 24 March 2022. The Bank obtained all the necessary approvals on 25 October 2022 and paid the dividend through a bonus issue of new ordinary shares on 22 November 2022.

In the interest of preservation of capital and liquidity, the Directors are not proposing the payment of a final dividend.

Going concern pursuant to Capital Markets Rule 5.62

The financial statements are prepared on a going concern basis. The directors regard that pursuant to Capital Markets Rule 5.62, this is appropriate, after due consideration of the Bank's profitability, liquidity, the statement of financial position, capital adequacy and solvency. Specifically, the directors have prepared financial and capital plans for the next three years which show that the Bank is able to continue operating as a going concern for the foreseeable future.

Information pursuant to Capital Markets Rule 5.64

The Bank does not have any listed securities carrying voting rights.

Statement of the Directors pursuant to Capital Markets 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 2022, 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.

Information pursuant to Capital Markets Rule 5.70.1

The Bank provides a range of banking services to the Van Marcke Group, of which the Bank itself is a member. Ms. Magdalena de Roeck, Ms. Caroline Van Marcke and Mr. Patrick Van Leynseele are indirectly interested in this business relationship by virtue of their directorships of various companies within the Van Marcke Group.

Further details can be found within Note 32 of the Financial Statements.

Information pursuant to Capital Markets Rule 5.68

Pursuant to Capital Markets Rule 5.68, we, the undersigned, declare that to the best of our knowledge, the financial statements included in the Annual Report, and prepared in accordance with the requirements of International Financial Reporting Standards as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Bank, and that the Directors' Report includes a fair review of the development and performance of the business and position of the Bank, together with a description of the principal risks and uncertainties that it faces.

Auditors

PricewaterhouseCoopers have expressed their willingness to continue in office. A resolution proposing the re-appointment of PricewaterhouseCoopers as auditors of the Bank will be submitted at the forthcoming Annual General Meeting.

Signed on behalf of the Board of Directors on 26 April 2023 by Mr. Andrew Mifsud (Chief Executive Office/Director) and Mr. Francis Gouder (Director) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Financial Report.

Registered Address

53-58 East Street
Valletta
Malta
Tel: +356 2124 1258

Directors' Statement of Compliance
with the Code of Principles of Good Corporate Governance

Pursuant to Capital Markets Rule 5.97 as issued by the Malta Financial Services Authority, Izola Bank p.l.c. (the 'Bank') hereby includes a Statement of Compliance reporting on the extent to which the Bank has adopted the Code of Principles of Good Corporate Governance appended as Appendix 5.1 to the said Capital Markets Rules (the 'Principles') and the effective measures that the Bank has taken to ensure compliance with these Principles during the financial year under review.

Introduction

The adoption of the Principles is not mandatory, however the Board of Directors (the 'Board') of Izola Bank p.l.c. believes that the adoption of these Principles is in the best interest of the Bank and its shareholders.

The Bank applies all the provisions of the Code of Principles of Good Corporate Governance (the "Principles"), save where there exist circumstances that warrant non-adherence thereto, as outlined in Part Two to this Statement. During the financial year under review, the Bank did not apply any corporate governance practices beyond the provisions under national law.

PART ONE - Compliance with the Code

Principle 1: The Board

The Bank is headed by an effective Board and all directors exercise prudent controls which enable risk to be assessed and managed. The Board is composed of members who are honest and competent, making them fit and proper to conduct the business of the Bank. The directors are of the appropriate calibre, having the necessary experience to provide leadership, integrity, and judgement in directing the Bank. All directors are responsible for determining the Bank's strategic aims and its organisational structure. The directors regularly review management performance and ensure that the Bank has the appropriate mix of financial and human resources to meet its objectives. Every director is conversant with the statutory and regulatory requirements connected to the business of the Bank and regularly attends meetings of the Board. Directors are appointed by the shareholders during the Bank's Annual General Meeting for a period of one year.

The Board delegates specific responsibilities to the Audit and Risk Committee, the Remuneration and Nomination Committee, the Credit Committee, the Strategy Committee and the Asset and Liability Committee. Each Committee has its own terms of reference which are in turn approved by the Board.

Principle 2: Chairperson and Chief Executive Officer (CEO)

The Bank's current organisational structure incorporates the position of a CEO and that of a Chairperson, both of which are occupied by two different individuals. In line with the Board of Directors' terms of reference, there is a clear division of responsibilities between the running of the Board and the CEO's responsibility in managing the Bank's business. The separation of roles of the Chairperson and the CEO avoids concentration of authority and power in one individual.

The Chairperson is responsible to lead the Board and set out the agenda and ensures that the directors receive precise, timely and objective information so that they can take sound decisions and effectively monitor the performance of the Bank. During the Board meeting, the Chairperson encourages active engagement by all Board members and ensures that the opinions of all the directors are considered in the discussion of complex or contentious issues.

The CEO is responsible to drive and deliver performance within strategic goals and business plans agreed by the Board. He actively leads the senior management in the day-to-day running of the Bank and the execution of the agreed strategy. He takes decisions in all matters affecting the operations, performance, and strategy of the business, except for those matters reserved for the Board or specifically delegated by the Board to its Committees.

Principle 3: Composition of the Board

The Board considers that it is of sufficient size for the requirements of the business and its members possess the required diversity of knowledge and experience to properly execute their duties as directors. Each of the directors is skilful, competent, knowledgeable, and experienced to fulfil the role diligently. The CEO was appointed to the Board of Directors in 2019 and provides the Board with all necessary management and operational information.

During the year under review, the Board consisted of five independent Non-Executive Directors, two Non-Independent, Non-Executive Directors including the Chairperson (as set out in the Directors' Report) and one Executive Director, being the CEO. In determining the independence of its directors, the Board has referred to the principles relating to independence contained in the Code. Each independent non-executive director has made a declaration in writing to that effect in line with the requirements emanating from Code Provisions 3.4. All directors shall disclose their interests and external commitment, both ahead of their appointment and, where significant changes arise, during their tenue as directors. This ensures that directors' business interests and commitments do not give rise to potential conflicts of interest and allow them to devote the necessary time and attention to properly execute their duties on the Board.

Principle 4: Responsibilities of the Board

The Board's role and responsibility is to execute the four basic roles of corporate governance namely: accountability, monitoring, strategy formation and policy development.

The Board regularly reviews and evaluates corporate strategy, major operational and financial plans, risk policy and performance objectives, and monitors implementation and corporate performance within the parameters of all relevant laws, regulations, and codes of best business practice. The Board ensures that policies and procedures are in place to maintain the highest standards of corporate conduct, including compliance with laws, regulations, business and ethical standards by the Bank and its employees. Board members are provided with regular training and information sessions on topical matters such as developments in banking regulation and emerging trends in the business of banking.

The Board requires management to constantly monitor performance and report to its satisfaction, at least on a quarterly basis, fully and accurately on the key performance indicators ('KPI's'). Business risks and KPI's are benchmarked against industry norms so that the Bank's performance can be effectively evaluated.

The Board delegates specific responsibilities to the following Committees:

BOARD COMMITTEES

Audit and Risk Committee

The Audit and Risk Committee's Terms of Reference include the monitoring of the financial reporting process, the effectiveness of the Bank's internal control, internal audit and risk management systems, and the statutory audit of the Bank's annual financial statements. Given that the nature of Related Party Transactions does not change from year to year, the vetting and approving of Related Party Transactions is a matter dealt with by the Board.

The Audit and Risk Committee protects the interests of the Bank's shareholders and assists 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. It ensures that the Bank maintains a robust finance function responsible for accounting and financial data. This Committee has non-executive responsibility for oversight of, and advice to, the Board on matters relating to financial reporting. The Committee monitors the integrity of the Bank's financial statements, any formal announcements relating to the Bank's financial performance and reviews significant financial reporting judgements contained therein.

Principle 4: Responsibilities of the Board *(Continued)*

BOARD COMMITTEES *(Continued)*

Audit and Risk Committee *(Continued)*

The Committee approves the internal audit work plan, which will include assessment of controls relating to financial reporting and other risks as appropriate. The Audit and Risk Committee also has the responsibility to appoint the external auditors, review and monitor the external auditor's independence, and assess the effectiveness of the statutory audit process.

In terms of Capital Markets Rules 5.117, 5.118 and 5.119, the Audit and Risk Committee is composed of three non-executive directors. All three non-executive directors are considered independent since they are free from any business, family or other relationship with the Bank or its management that may create a conflict of interest such as to impair their judgement. The Chairman of the Audit and Risk Committee is appointed by the Board of Directors.

In terms of Capital Markets Rule 5.119, Mr Guido Mizzi is the director whom the Board considers as independent of the Bank and competent in accounting, given his extensive experience as a former managing partner of a local accountancy firm. Mr. Van Leynseele is a partner in a Brussels law firm and a member of the Bar in both Brussels and New York. Mr. Azzopardi has an extensive background in product development, predominantly in the financial services sector and technology-focused businesses.

All three directors have experience serving on various other boards and are considered competent to fulfil their responsibilities as members of the Audit and Risk Committee of the Bank. The Board thus considers that the committee members have the competence relevant to the banking sector.

	Meetings held: 6
Members	***Attended***
Mr. Guido Mizzi (Chairman)	6
Mr. Simon Azzopardi	6
Mr. Patrick H. Van Leynseele	6

Other Board members have a right to attend the meetings. The Audit and Risk Committee has direct access to the Head of Finance and Treasury, who is responsible for the preparation and integrity of financial statements, and a direct reporting line to the Head of Risk and Compliance, who is responsible for ensuring proper execution of the risk management and control framework. The Head of IT, who is responsible for the maintenance of internal controls in relation to Information and Communications Technology ('ICT'), attends meetings when ICT-related topics are discussed. Both the internal and external auditors are also invited to attend meetings on an ad-hoc basis. The Company Secretary acts as Secretary to the Committee.

Remuneration and Nomination Committee

In its nomination function, the Committee is primarily tasked with identifying and nominating new Board candidates for the approval of the Board. The Committee periodically assesses the structure, size, composition, and performance of the Board and makes recommendations to the Board regarding any changes. It is also tasked with reviewing the remuneration structure for the Bank's senior management and all staff, evaluating the impacts of remuneration considerations on its overall risk profile and corporate culture. This Committee is also responsible to periodically assess the skills, knowledge, and experience of individual directors, and of the Board collectively, and report on this to the Board.

The Remuneration and Nomination Committee is composed of three non-executive directors, two of whom are independent and meets at least once a year. The Remuneration and Nomination Committee is tasked with oversight of performance and remuneration practices, making proposals to the Board on the remuneration policy for directors and leading the process for Board appointments. The Committee also assesses the size, composition and performance of the Board and the individual and collective suitability of directors. The terms of reference of this Committee are in line with Code Provisions of 8.A.2 - 8.A.6 and 8.B.2 - 8.B.8. Further information on the Bank's remuneration practices is included within the Report of the Remuneration and Nomination Committee immediately following the Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance.

Principle 4: Responsibilities of the Board *(Continued)*

BOARD COMMITTEES *(Continued)*

Remuneration and Nomination Committee *(Continued)*

	Meetings held: 2
Members	***Attended***
Mr. Francis Gouder (Chairperson)	2
Ms. Caroline Van Marcke	2
Mr. Patrick H. Van Leynseele	2

The Company Secretary acts as Secretary to the Committee.

Credit Committee

The Credit Committee is composed of two independent non-executive directors and the CEO and operates within a Board-approved credit sanctioning limit. Proposals falling outside the Committee's limits are referred together with the Committee's recommendations to the Board for consideration and determination.

	Meetings held: 6
Members	***Attended***
Mr. Alain Malschaert (Chairman - appointed on 24th March 2022)	4
Mr. Joseph A. Caruana*	1
Mr. Francis Gouder	6
Mr. Andrew Mifsud	6

* After sixteen years of service as non-executive director, Mr. Joseph Caruana communicated his decision to retire and not to offer himself to be re-nominated to the Board of Directors at the Annual General Meeting held on 24 March 2022.

The Company Secretary acts as Secretary to the Committee. The Head of Credit regularly attends the meetings.

Strategy Committee

The Committee is responsible for making recommendations to the Board of Directors in respect of the Bank's business model and forward-looking strategy, taking into consideration the risks and opportunities related to various strategies. The Committee is also responsible for analysing the implementation of the business model and strategy or any changes thereto, including any potential ICT implications.

It is composed of three directors and meets at least once a year. The Bank's Senior Management team and other bank executives may be invited to attend meetings. The Company Secretary acts as Secretary to the Committee.

	Meetings held: 2
Members	***Attended***
Mr. Simon Azzopardi (Chairman)	2
Ms. Caroline Van Marcke	2
Mr. Andrew Mifsud	2

Principle 4: Responsibilities of the Board *(Continued)*

BOARD COMMITTEES *(Continued)*

Management Committee

Asset and Liability Management Committee (ALCO)

The ALCO meets at least quarterly to monitor the Bank's financial performance, and review and manage financial risks in accordance with Bank policies, namely: interest rate, liquidity and funding risk, solvency, market sector and country risk; and counterparty and foreign exchange risk. The ALCO reports to the Board on a quarterly basis.

The ALCO is chaired by the CEO and is also composed of the Head of Finance and Treasury, and the Senior Finance and Treasury Manager. The Company Secretary acts as Secretary to the Committee.

	Meetings held: 8
Members	***Attended***
Mr. Andrew Mifsud (Chairman)	8
Mr. Calvin Bartolo	8
Mr. Kurt Grima	8

Principle 5: Board Meetings

During the financial year ended 31 December 2022 the Board met eight times. Notice of the dates of forthcoming meetings together with all board papers were circulated well in advance to the directors so that they had ample opportunity to consider the information and prepare for the next scheduled Board meeting. After each Board meeting and before the next meeting, minutes that faithfully recorded attendance and decisions were prepared and circulated to all directors.

Attendance of the Board members during the financial year ended 31 December 2022 was as follows:

	Meetings held: 8
Members	***Attended***
Ms. Magdalena De Roeck (acted as Chairperson until 24 March 2022)	8
Ms. Caroline Van Marcke (appointed as Chairperson on 24 March 2022)	8
Mr. Simon Azzopardi	6
Mr. Joseph C. Caruana*	2
Mr. Francis Gouder	8
Mr. Alain Malschaert (appointed on 24 March 2022)	5
Mr. Andrew Mifsud	8
Mr. Guido Mizzi	8
Mr. Patrick H. Van Leynseele	6

* After sixteen years of service as non-executive director, Mr. Joseph Caruana communicated his decision to retire and not to offer himself to be re-nominated to the Board of Directors at the Annual General Meeting held on 24 March 2022.

Company Secretary
Calvin Bartolo

Principle 6: Information and Professional Development

All new directors are briefed in detail by the CEO and Company Secretary on the Bank's organisation and activities and their responsibilities as directors.

When they judge it necessary, all directors can access independent professional advice at the Bank's expense to enable them to discharge their responsibilities as directors. All directors also have access to the services of the Company Secretary for advice on all governance matters.

The Bank is committed to provide for the development and training of management and employees. The Board is updated at least annually with the latest staff development programme. In accordance with Code Provision 6, the Board is responsible for the appointment of the CEO whilst, in line with Code Provision 6.5, the CEO is responsible for the recruitment and appointment of senior management. Training of management and employees is a priority and, in this respect, access to internal and external training is provided by the Bank to management and employees. The Bank also has a system in place which monitors management and staff engagement. As part of succession planning and talent management, the Board and the CEO ensure that the Bank implements appropriate schemes to recruit, retain and motivate high quality staff members.

Principle 7: Evaluation of the Board's Performance

The Board has set up the Remuneration and Nomination Committee to periodically review and monitor the effectiveness of the Bank's Board suitability policy and to guide the execution of suitability assessments of directors. The Chairperson reports on the Committee's activities and submits recommendations on areas falling within its remit upon request of the Board of Directors. In line with its policies, the Bank performs a suitability assessment every 2 years, with the most recent one performed in May 2021.

The Committee may request information or reports from internal departments to facilitate discussions and decision-making. It may also provide guidance on how policies pertaining to performance, remuneration and training are to be communicated internally.

Principle 8: Committees

The Board established a Remuneration and Nomination Committee to oversee matters of remuneration and nomination in line with best practice. More detailed information regarding remuneration is presented in the Report of the Remuneration and Nomination Committee following the Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance.

Principle 9 and 10: Relations with Shareholders and with the Market and Institutional Shareholders

The Bank provides the market with regular, timely, accurate and detailed information in accordance with the requirements of the Capital Markets Rules by way of company announcements.

The Bank communicates with its shareholders through the Bank's Annual General Meeting as well as by way of the Annual Report and Financial Statements.

The Bank has an Internal Code of Dealing Policy to give guidance to the Bank's directors and employees on procedures to be followed when dealing in the Bank's securities and on the treatment of Inside Information in line with the provisions of the Prevention of Financial Markets Act and any related subsidiary legislation and regulations.

The Bank's shareholders are not custodians, banks, financial institutions, fund managers, stockbrokers, or investment managers and as a result, Principle 10 is not applicable.

Principle 11: Conflicts of Interest

The directors are always strongly aware of their responsibility to act in the interest of the Bank and its shareholders as a whole and of their obligation to avoid conflicts of interest. The latter may and do arise on specific matters. In such instances, the Bank ensures that such conflicts, actual or potential, are managed in the best interest of the Bank. Each director is required to disclose in full any matter where there is a potential or actual conflict of interest, whether such conflict arises from personal interests or the interests of the companies in which such person is a director or officer. Directors do not participate in a discussion concerning matters in which they have a conflict of interest unless the Board finds no objection to the presence of such director. In any event, the director shall refrain from voting on the matter.

On joining the Board, and regularly thereafter, the directors are informed of their obligations on dealing in securities of the Bank within the parameters of the law, including the Capital Markets Rules, and the directors follow the required procedures. Interests of directors are disclosed within Note 32 - Related Parties - to the accompanying Financial Statements.

Principle 12: Corporate Social Responsibility

Over the past 28 years, the Bank has transformed itself to be in a better position to deliver on its purpose: enabling purposeful growth. This value is at the heart of the Bank's CSR initiatives, as it continues to provide both tangible and immediate contributions to the community's welfare. The Bank's approach to CSR is through investing in community-based organisations that directly address pressing issues within the country – issues if left unattended would have dire consequences for people in need.

- ***Foodbank Lifeline Foundation***

  In 2018, the Bank became an official sponsor of Foodbank Lifeline Foundation Malta, a registered NGO, which provides short-term emergency food packs to people in desperate need, regardless of race and religion– till they find a path to stability. Over the course of this relationship, the Bank has increased its support, both financially and in practical terms to meet the increasing demand for Foodbank Lifeline's services – presently feeding thousands every year. Going beyond a one-time annual monetary donation, the Bank sought to support Foodbank Lifeline using a more hands on strategy through-out the year. The Bank has become a valued partner to the Foodbank, and a member of the Bank's staff also sits on the NGO's Board of Directors. The Bank and Foodbank Lifeline share a joint vision of hoping that one day there will be no need for a foodbank in Malta. Until that day comes, the Bank is committed to supporting the community and ensuring that where possible no one should suffer the indignity of hunger.

- ***Supporting Foodbank Foundation's Digital Presence***

  The Bank sponsors the design, development, hosting and maintenance of Foodbank Lifeline's website which includes a platform where Care Professionals can enter quick referrals online, where visitors can access information on how to help Foodbank Lifeline or catch up on the latest updates and where people in need can follow the steps required to obtain a referral. Maintaining a regular presence in the community is vital for Foodbank Lifeline. The Bank also sponsors the management of Foodbank Lifeline's social pages (Facebook, Instagram and LinkedIn), helping to oversee the day-to-day posts, comments and messages. The Bank has helped the foodbank gain an impressive 11,000 followers over the last 5 years. The Bank also injects funds and organises the promotion of various campaigns through-out the year helping to drive food and monetary donations.

- ***Reverse Advent Calendar Campaign***

  Held once a year in the run up to Christmas, the Reverse Advent Calendar Campaign is a way for the community to get involved in helping the less fortunate. It is the largest campaign run by the Bank and Foodbank Lifeline and is hugely popular with local schools, businesses, and families. The Bank oversees the entire campaign including the media productions, bookings, press coverage and the ongoing social channel management.

PART TWO – Non-Compliance with the Code

Principle 2 – Code Provision 2.3

The Chairperson of the Bank cannot be considered independent in accordance with the principles relating to independence contained in the Code.

Principle 4 – Code Provision 4.2.7

The Code Provision recommends that the Board should develop a succession policy for the future composition of the Board and particularly the executive component thereof, for which the Chairman should hold key responsibility. The Board does not have a succession policy in place for the future composition of the Board of Directors. This approach may be revised in the future in line with changes to the Bank's size and/or organisational structure.

Principle 6 – Code Provision 6.4.4

Code Provision 6.4.4 recommends the CEO to establish a succession plan for senior management. The Board does not have a succession policy in place for senior management. This approach may be revised in the future in line with changes to the Bank's size and/or organisational structure.

Principle 7 – Code Provision 7.3

Code Provision 7.3 recommends that the non-executive Directors are responsible for the evaluation of the Chairperson, taking into account the views of the executive directors. This evaluation has not been adopted to date but may be revised with future policy changes.

Capital Markets Rule 5.97.4

The information required by this Capital Markets Rule is found in the Directors' Report, within the Directors' Responsibilities section.

The Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance was approved by the Board of Directors on 26 April 2023.

Governance

The Bank's Remuneration and Nomination Committee comprises three non-executive directors and is tasked with the oversight of the Bank's remuneration and nomination practices. Information in respect of the functions, composition, and attendance to meetings of the Remuneration and Nomination Committee is disclosed within the Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance.

The Report of the Remuneration and Nomination Committee was approved by the Board of Directors at the Board meeting held on 27 July 2022.

Remuneration Policy

The aim of the Bank's Remuneration Policy is to increase transparency in remuneration matters, to support the business goals of the Bank by efficient remuneration structures, and to create common basic values and guidelines for the Bank when offering remuneration and benefits to the senior management team of the Bank.

There were no deviations from the procedure for the implementation of the Bank's Director's Remuneration Policy.

Remuneration Statement

Executive Management

Reference to senior management shall mean the CEO, the Head of Finance & Treasury, the Head of Operations, the Head of Credit, the Head of IT, the Head of Risk and Compliance, the Head of HR and the Head of Strategy & Value. The Board is of the opinion that the remuneration packages for senior management are in line with local market expectations and are at an appropriate level to attract and retain executives with the appropriate skills, qualities, and experience to ensure the effective management of the Bank.

The terms and conditions of employment of senior management are set out in the respective indefinite contracts of employment. Senior management are not entitled to share options or profit sharing. There are no supplementary pension or early retirement schemes in place and notice periods are as established by law. Senior management are eligible for an annual salary increase and discretionary performance bonus (not exceeding fixed remuneration) in line with the Bank's overall performance, individual performance and general market remuneration trends.

Non-cash benefits to which senior management are entitled comprise the use of a company car. Other benefits afforded to all staff members, including senior management, are personal accident, life, and health insurance cover.

Loans amounting to €782,327 were advanced to key management personnel as disclosed in Note 32.3 to the financial statements.

There have been no significant changes in the Bank's remuneration policy for senior management during the year under review. During 2022, the Bank continued offering all staff members, including senior management, subsidies on home loan interest rates and intends to start contributing to a personal pension scheme during 2023.

Total emoluments of senior management for the year ended 31 December 2022 are as follows:

Fixed Remuneration	Variable Remuneration	Share Options	Others
€661,758	€96,000	None	Non-cash benefits referred to immediately above

During the year under review, no special payments (sign-on and/or severance pay), payments exceeding €1 million or any payments subjects to deferral were made to key management personnel.

Directors

As of 31 December 2022, the Board was composed of 7 non-executive directors and one executive director.

The maximum annual aggregate emoluments that may be paid to the directors are approved by the shareholders in a General Meeting. This amount was fixed at an aggregate sum of €175,000 at the Annual General Meeting held on 24 March 2022.

None of the directors had service contracts with the Bank as at the end of the financial year.

Furthermore, none of the directors, in their capacity as a director of the Bank, are entitled to profit sharing, share options, pension benefits or any other remuneration.

In line with the Bank's Remuneration Policy, none of the Directors are eligible to receive variable remuneration in their function as Directors. In this respect, there is no formal provision for the reclamation of variable remuneration.

Total emoluments received by directors relative to their directorship of the Bank in respect of the financial year ended 31 December 2022 are disclosed in the table below:

Fixed Remuneration	Variable Remuneration	Share Options	Others
€145,000	None	None	None

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Readers are reminded that the official statutory Annual Report and Financial Statements 2022, authorised for issue by the Board of Directors, is in European Single Electronic Format (ESEF) and is published on our website at: https://www.izolabank.com/mt-en/who-we-are/investor-information/annual-reports-financial-statements

A copy of the Independent auditor's report issued on the official statutory Annual Report and Financial Statements 2022 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 (the ESEF RTS), by reference to Capital Markets Rule 5.55.6.

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Statement of Profit or Loss and Other Comprehensive Income

As at 31 December 2022

	Note	2022	2021
		€	€
Interest and similar income	5	**13,087,771**	10,704,557
Interest expense	5	**(5,412,645)**	(4,513,733)
Net interest income		**7,675,126**	6,190,824
Fee and commission income	6	**182,419**	119,866
Fee and commission expense	6	**(126,507)**	(130,061)
Net fee and commission income/(expense)		**55,912**	(10,195)
Net trading income	7	**15,789**	31,168
Net (losses)/gains on disposal of financial investments measured at FVOCI		**(7,299)**	442,395
Other operating income	8	**101,325**	97,746
Total operating income		**7,840,853**	6,751,938
Depreciation of property and equipment	19	**(149,201)**	(243,933)
Amortisation of intangible assets	20	**(863,548)**	(600,229)
Changes in expected credit losses and other credit impairment charges	9	**(919,147)**	(385,692)
Employee compensation and benefits	10.2	**(2,513,276)**	(2,103,290)
Other administrative expenses	10.4	**(3,783,487)**	(2,598,637)
(Loss)/profit before tax	10	**(387,806)**	820,157
Income tax credit/(expense)	11	**103,587**	(372,176)
(Loss)/profit for the year		**(284,219)**	447,981
Other comprehensive income			
Items that will not be reclassified to profit or loss			
Loss on property revaluation		**100,784**	-
Income taxes		**(15,118)**	-
		85,666	-
Items that are or may be reclassified subsequently to profit or loss			
Debt instruments measured at fair value through other comprehensive income:			
Net movement in fair value, before tax		**(14,923,822)**	(1,495,306)
- Income taxes		**5,223,338**	523,357
Movement in expected credit losses, before tax		**34,822**	11,860
- Income taxes		**(12,188)**	(4,151)
Net gains reclassified to profit or loss on disposal, before tax		**(7,299)**	(442,395)
- Income taxes		**2,555**	154,838
		(9,682,594)	(1,251,797)
Other comprehensive income for the year, net of tax		**(9,596,928)**	(1,251,797)
Total comprehensive income for the year, net of tax		**(9,881,147)**	(803,816)
Earnings per share	12	**0c49**	0c77

The accompanying notes on pages 8 to 94 are an integral part of these financial statements.

	Note	**2022**	2021
ASSETS		**€**	€
Balances with Central Bank of Malta and cash	14	**17,598,287**	16,193,768
Loans and advances to banks	15	**10,214,993**	25,420,282
Financial investments	16	**91,550,927**	117,280,712
Factored receivables	17	**118,363,724**	95,051,834
Loans and advances to customers	18	**160,329,282**	131,369,341
Property and equipment	19	**11,712,225**	12,565,395
Intangible assets	20	**1,975,593**	1,774,370
Current tax asset		**641,499**	793,029
Deferred tax asset	26	**5,920,924**	388,435
Other assets	21	**3,181,811**	1,971,720
Total assets		**421,489,265**	402,808,886
LIABILITIES			
Amounts owed to institutions	22	**40,000,000**	55,000,000
Amounts owed to banks	23	**275,815**	274,715
Amounts owed to customers	24	**335,660,870**	297,780,509
Debt securities in issue	25	**16,820,322**	11,940,167
Deferred tax liabilities	26	**436,414**	558,446
Accruals and other liabilities	27	**4,759,914**	3,975,122
Total liabilities		**397,953,335**	369,528,959
EQUITY			
Called up share capital	28	**29,000,000**	10,000,000
Capital contribution reserve	28	**32,675**	17,032,675
Property revaluation reserve	28	**2,977,302**	3,521,238
Fair value reserve	28	**(10,295,141)**	(612,547)
Depositor compensation scheme reserve	28	**831,860**	1,288,168
Reserve for general banking risks	28	**72,782**	45,091
Retained earnings	28	**916,452**	2,005,302
Total equity		**23,535,930**	33,279,927
Total liabilities and equity		**421,489,265**	402,808,886
Memorandum items			
Commitments	29	**185,068,135**	92,738,305

The accompanying notes on pages 8 to 94 are an integral part of these financial statements.

The financial statements on pages 2 to 94 were approved and authorised for issue by the Board of Directors on 26 April 2023. The financial statements were signed on behalf of the Bank's Board of Directors by Mr. Andrew Mifsud (Chief Executive Officer) and Mr. Francis Gouder (Director) as per the Directors' Declaration on ESEF Annual Financial Report submitted in conjunction with the Annual Report and Financial Statements 2022.

Statement of Changes in Equity

For the Year Ended 31 December 2022

	Notes	Share Capital	Property revaluation reserve	Fair value reserve	Depositor compensation scheme reserve	Capital contribution	Reserve for general banking risk	Retained earnings	Total
		€	€	€	€	€	€	€	€
Balance at 1 January 2022		10,000,000	3,521,238	(612,547)	1,288,168	17,032,675	45,091	2,005,302	33,279,927
Total comprehensive income									
Loss for the year		-	-	-	-	-	-	(284,219)	(284,219)
Other comprehensive income									
Gain arising on property revaluation, net of tax		-	85,666	-	-	-	-	-	85,666
Financial investments measured at fair value through other comprehensive income									
- Net movement in fair value, net of tax		-	-	(9,700,484)	-	-	-	-	(9,700,484)
- Movement in expected credit losses, net of tax		-	-	22,634	-	-	-	-	22,634
- Net gains reclassified to profit or loss on disposal, net of tax		-	-	(4,744)	-	-	-	-	(4,744)
Total other comprehensive income		-	85,666	(9,682,594)	-	-	-	-	(9,596,928)
Total comprehensive income for the year		-	85,666	(9,682,594)	-	-	-	(284,219)	(9,881,147)
Transfers within reserves									
Transfer of revaluation surplus on disposal of property, net of tax		-	(629,602)	-	-	-	-	629,602	-
Derecognition of deferred tax on fair value of property		-	-	-	-	-	-	137,150	137,150
Other transfers	28	-	-	-	(456,308)	-	27,691	428,617	-
Total transfers within reserves		-	(629,602)	-	(456,308)	-	27,691	1,195,369	137,150
Transactions with owners									
Contributions by owners	28	17,000,000	-	-	-	(17,000,000)	-	-	-
Issue of bonus shares	28	2,000,000	-	-	-	-	-	(2,000,000)	-
Total transactions with owners recognised directly in equity		19,000,000	-	-	-	(17,000,000)	-	(2,000,000)	-
Balance at 31 December 2022		29,000,000	2,977,302	(10,295,141)	831,860	32,675	72,782	916,452	23,535,930

The accompanying notes on pages 8 to 94 are an integral part of these financial statements.

	Notes	Share Capital	Property revaluation reserve	Fair value reserve	Depositor compensation scheme reserve	Capital contribution	Reserve for general banking risk	Retained earnings	Total
		€	€	€	€	€	€	€	€
Balance at 1 January 2021		10,000,000	3,521,238	639,250	1,707,717	17,032,675	3,860	1,179,003	34,083,743
Total comprehensive income									
Profit for the year		-	-	-	-	-	-	447,981	447,981
Other comprehensive income									
Financial investments measured at fair value through other comprehensive income									
- Net movement in fair value, net of tax		-	-	(971,949)	-	-	-	-	(971,949)
- Movement in expected credit losses, net of tax		-	-	7,709	-	-	-	-	7,709
- Net gains reclassified to profit or loss on disposal, net of tax		-	-	(287,557)	-	-	-	-	(287,557)
Total other comprehensive income		-	-	(1,251,797)	-	-	-	-	(1,251,797)
Total comprehensive income for the year		-	-	(1,251,797)	-	-	-	447,981	(803,816)
Transfers within reserves									
Other transfers	28	-	-	-	(419,549)	-	41,231	378,318	-
Total transfers within reserves		-	-	-	(419,549)	-	41,231	378,318	-
Balance at 31 December 2021		10,000,000	3,521,238	(612,547)	1,288,168	17,032,675	45,091	2,005,302	33,279,927

The accompanying notes on pages 8 to 94 are an integral part of these financial statements.

Statement of Cash Flows
For the Year Ended 31 December 2022

	Note	2022 €	2021 €
Cash used in operating activities	30	**(30,306,813)**	10,160,681
Income tax paid		**(63,667)**	(342,102)
Net cash (outflows)/inflows from operating activities		**(30,370,480)**	9,818,579
Cash flows from investing activities			
Payments to acquire property and equipment and intangible assets		**(2,478,688)**	(1,639,455)
Proceeds from disposal of property		**2,204,000**	-
Payments to acquire investments		**(40,740,036)**	(85,996,927)
Proceeds from disposal of investment securities		**51,362,776**	76,537,399
Interest received from financial investments		**1,612,389**	2,066,104
Net cash flows generated from/(used in) investing activities		**11,960,441**	(9,032,879)
Cash flows from financing activities			
Proceeds from issue of debt securities		**13,633,597**	-
Redemption of debt securities		**(8,814,000)**	-
Interest and premium paid on debt conversion		**(284,663)**	-
Interest paid on debt securities in issue		**(540,000)**	(540,000)
Net cash flows generated from/(used in) financing activities		**3,994,934**	(540,000)
Net (decrease)/increase in cash and cash equivalents		**(14,415,105)**	245,700
Cash and cash equivalents at beginning of year		**39,970,678**	39,724,978
Cash and cash equivalents at end of year	31	**25,555,573**	39,970,678

The accompanying notes on pages 8 to 94 are an integral part of these financial statements.

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izola Bank

1 Reporting entity

Izola Bank p.l.c. (the "Bank") is a public limited liability company domiciled and incorporated in Malta. The Bank is a credit institution licenced in Malta and is primarily involved in the provision of lending and factoring services to corporate and retail customers, as well as the raising of deposits from retail customers.

2 Basis of preparation

2.1 Statement of compliance with IFRSs as adopted by the European Union

These financial statements have been drawn up in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"), including interpretations issued by the IFRS Interpretations Committee ("IFRIC"), and as adopted by the European Union ("EU").

These financial statements have also been prepared and presented in accordance with the provisions of the Companies Act, 1995 (Chapter 386, Laws of Malta) and the Banking Act, 1994 (Chapter 371, Laws of Malta).

2.2 Basis of measurement

These financial statements have been prepared on a historical cost basis, except for:

- Financial investments measured at fair value through other comprehensive income ("FVOCI");
- Financial investments designated at FVOCI or at fair value through profit or loss ("FVTPL"); and
- Property within 'Property and equipment' measured at revalued amount.

2.3 Standards, interpretations and amendments to published standards effective in 2022

During the financial year ended 31 December 2022, the Bank adopted amendments to existing standards, specifically amendments to IFRS 3 Business Combinations; IAS 16 Property, Plant and Equipment; IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and Annual Improvements 2018-2020, that are mandatory for financial years starting on or after 1 January 2022.

The adoption of these revisions to the requirements of IFRSs as adopted by the EU did not result in significant changes to the Bank's accounting policies impacting the Bank's financial performance and position.

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

Certain new accounting standards and interpretations have been published, which are not mandatory for 31 December 2022 reporting periods and have not been early adopted by the Bank. The IASB has published a number of minor amendments to IFRSs that are effective from 1 January 2023, which have been endorsed by the EU, and other minor amendments to IFRSs that are effective from 1 January 2024, which have not yet been endorsed by the EU.

The changes resulting from the above standards, interpretations and amendments are not expected to have a material impact on the Bank in the current or future reporting periods and on foreseeable future transactions.

2.5 Functional and presentation currency

These financial statements are presented in Euro (€), which is the Bank's functional currency.

2 Basis of preparation *(continued)*

2.6 Use of judgements and estimates

The preparation of financial statements in conformity with IFRSs as adopted by the EU requires the use of certain accounting estimates. In this respect, management is required to exercise their judgement in the process of applying the Bank's accounting policies. This requires assumptions to estimate the carrying amount of assets and liabilities, as well as the recognition of income and expenses. Due to the inherent uncertainty and high level of subjectivity involved in making such judgements, actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

Information about critical accounting judgements, assumptions and estimation uncertainties as at 31 December 2022 is disclosed within Note 34 – Critical accounting estimates and judgements in applying the Bank's accounting policies, as well as within the following notes to the financial statements:

- Expected credit losses on factored receivables and loans and advances to customers: Note 4.3
- Valuation of financial instruments: Note 4.7
- Valuation of property within 'Property and equipment': Note 4.7 and Note 19

2.7 Going Concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the Bank has the resources to continue in business for the foreseeable future. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including future projections of profitability, cash flows, capital requirements and capital resources. These considerations include the application of stressed scenarios that reflect existing economic uncertainties triggered by the escalation of the military conflict between Russia and Ukraine, the ensuing inflationary pressures in the aftermath of the global Covid-19 pandemic, as well as considering potential impacts from other top and emerging risks, including exposure to interest rate hikes, drops in asset prices, and local jurisdiction risks, and the related impact on profitability, capital and liquidity.

3 Significant accounting policies

3.1 Financial assets

3.1.1 Recognition and initial measurement

The Bank 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 trade date, being the date on which the Bank commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Bank has transferred substantially all the risks and rewards of ownership.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue. Transaction costs of financial assets carried at FVTPL are expensed in profit or loss.

2 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.2 Classification and measurement

At initial recognition, the Bank classifies its financial assets in the following measurement categories:
- Financial assets measured at FVTPL;
- Financial assets measured at FVOCI; and
- Financial assets measured at amortised cost.

The classification of investments in debt instruments depends on the Bank's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether the Bank has made an irrevocable election at the time of initial recognition to account for the equity investment at FVOCI.

The Bank reclassifies debt instruments when and only when its business model for managing those assets changes.

Debt instruments

Subsequent measurement of debt instruments depends on the Bank's business model for managing the asset and the cash flow characteristics of the asset.

Business model assessment

The Bank performs an assessment of the objective of a business model in which an asset is held at a portfolio level since this is deemed to best reflect the way the business is managed and the monitoring of financial information by management.

The information considered in the performance of this assessment includes:
- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, management considers whether the 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 manner in which the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and its strategy for how those risks are managed;
- how managers of the business are compensated for business performance (e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected); and
- the frequency, volume, and timing of sales transacted in prior periods, the reasons for such sales and management's expectations in respect of future sales activity. Information about sales activity is not considered in isolation but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or financial assets that are managed and whose performance is evaluated on a fair value basis are measured at FVTPL since such assets are neither held with the objective to collect contractual cash flows nor held with the objective to collect contractual cash flows and sell financial assets.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.2 Classification and measurement (continued)

Assessment of whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin that is consistent with a basic lending arrangement.

In assessing whether the contractual cash flows are solely payments of principal and interest ("SPPI"), the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:
- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets; and
- variable interest rates and features that modify consideration of the time value of money.

In some cases, loans originated by the Bank that are secured by collateral limit the Bank's claim to cash flows from the underlying collateral (non-recourse loans). The Bank applies judgement in assessing whether non-recourse loans meet the SPPI criterion.

The Bank typically considers the following information when making this judgement:
- whether the contractual arrangement specifically defines the amounts and dates of the cash payments of the loan;
- the fair value of the collateral relative to the amount of the secured financial asset;
- the ability and willingness of the borrower to make contractual payments, notwithstanding a decline in the value of collateral;
- whether the borrower is an individual or a substantive operating entity or is a special-purpose entity;
- the Bank's risk of loss on the asset relative to a full-recourse loan;
- the extent to which the collateral represents all or a substantial portion of the borrower's assets; and
- whether the Bank will benefit from any upside from the underlying assets.

Financial assets measured at amortised cost

A debt instrument is measured at amortised cost if it meets both of the following conditions and is not designated at FVTPL:
- the financial asset is held within a business model where the objective is to hold financial assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

Interest income from these financial assets is recognised in 'Interest income' using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss. Impairment losses are presented as a separate line item in the statement of profit or loss.

The 'amortised cost' of a financial instrument is the amount at which the financial instrument is measured on 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 expected credit loss ("ECL") allowance.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.2 Classification and measurement (continued)

Such financial assets comprise primarily 'Balances with Central Bank of Malta', 'Loans and advances to banks', 'Factored receivables' and 'Loans and advances to customers'.

Financial assets measured at fair value through other comprehensive income

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated at FVTPL:
- the financial asset is held within a business model where the objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses, 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 profit or loss and recognised in 'Other operating income'. Interest income from these financial assets is recognised in 'Interest income' using the effective interest rate method. Foreign exchange gains and losses are presented in 'Other operating income', and impairment losses are presented as a separate line item in the statement of profit or loss.

Such financial assets comprise primarily debt securities measured at FVOCI and classified within 'Financial investments'.

Equity investments designated at fair value through other comprehensive income

The Bank subsequently measures all equity investments at fair value. On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an instrument-by-instrument basis and is irrevocable.

Where the Bank's management has elected to present fair value gains and losses on equity investments in OCI, there is no subsequent reclassification of fair value gains and losses to profit or loss following the derecognition of the investment. Dividends from such investments continue to be recognised in profit or loss as 'Other operating income' when the Bank's right to receive payments is established.

Such financial assets comprise primarily equity investments designated at FVOCI and classified within 'Financial investments'.

Financial assets measured at fair value through profit or loss

Debt instruments that do not meet the criteria for amortised cost or FVOCI are automatically classified and measured at FVTPL. The Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise. A gain or loss on a debt instrument that is subsequently measured at FVTPL is recognised in profit or loss and presented net within 'Other operating income' in the period in which it arises.

In addition, equity investments that are not designated at FVOCI at initial recognition are also classified and measured at FVTPL. Changes in the fair value of financial assets measured at FVTPL are recognised in 'Other operating income' in the statement of profit or loss as applicable.

Such financial assets comprise primarily equity investments designated at FVTPL at initial recognition and classified within 'Financial investments'.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.3 Derecognition

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

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI, is recognised in profit or loss.

Any cumulative gain/loss recognised in OCI in respect of equity investment securities designated at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognised as a separate asset or liability.

3.1.4 Modifications of terms

If the contractual terms of a financial asset are modified, the Bank evaluates whether the cash flows arising from the modified asset are substantially different than those arising from the original contractual terms of the asset. The Bank applies judgement in assessing whether a change in contractual terms (such as a change in interest rates or the remaining term of the loan) is substantial enough to represent an expiry of the original instrument by considering, among others:

- If the borrower is in financial difficulty, whether the modification merely reduced the contractual cash flows to amounts the borrower is expected to be able to pay;
- Whether any new terms that substantially affect the risk profile of the asset are introduced;
- Significant extensions to the term of the financial instrument when the borrower is not in financial difficulty;
- Significant changes to the interest rate;
- Changes in the currency in which the asset is denominated; and
- The insertion of collateral, other security or credit enhancements that significantly affect the associated credit risk.

If the cash flows are substantially different, the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised (Note 3.1.3) and a new financial asset is recognised at fair value plus any eligible transaction costs.

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 Bank 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 borrower being unable to make the originally agreed payments.

Any fees received as part of the modification are accounted for as follows:

- fees that are considered in determining the fair value of the new asset and fees that represent a reimbursement of eligible transaction costs are included in the initial measurement of the asset; and
- other fees are included in profit or loss as part of the gain or loss on derecognition.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.4 Modifications of terms (continued)

If the modification of a financial asset measured at amortised cost or FVOCI is not deemed to be substantial and therefore does not result in the derecognition of the financial asset, the Bank recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs or fees incurred and fees received in relation to the modification of contractual terms are reflected in an adjustment to the gross carrying amount of the modified financial asset and amortised over the remaining term of the modified financial asset. Modification gains or losses are presented within 'Interest income' in profit or loss.

If cash flows are modified in view of concessions granted to borrowers experiencing financial difficulties, the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. If the modification of the financial asset results in the forgiveness of cash flows, the Bank considers whether a portion of the asset should be written off before the modification takes place. This approach impacts the result of the quantitative assessment and means that the derecognition criteria are not usually met in such cases. Modification gains or losses arising as a result of renegotiations in response to financial difficulties experienced by a borrower are presented together with impairment losses in profit or loss.

3.1.5 Impairment

The Bank assesses on a forward-looking basis the expected credit losses ("ECL") associated with its debt instruments carried at amortised cost and FVOCI and with the exposure arising from loan commitments, including:
- Loans and advances to banks;
- Debt instruments classified within 'Financial investments';
- Factored receivables; and
- Loans and advances to customers.

The Bank recognises credit loss allowances in respect of the above portfolios of financial assets at each reporting date. No credit loss allowances are recognised in respect of equity investments.

The measurement of ECL reflects:
- 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.

The Bank measures credit loss allowances at an amount equal to lifetime ECL except for the following financial instruments, in respect of which credit loss allowances are measured as 12-month ECL:
- debt securities classified within 'Financial investments' that are determined to have low credit risk at the reporting date; and
- financial instruments that have not had a significant increase in credit risk ("SICR") since initial recognition.

Balances held with credit institutions in reputable jurisdictions classified within 'Loans and advances to banks' and debt securities classified within 'Financial investments' are considered to have low credit risk when the financial instrument is assigned an 'investment-grade' credit risk rating. The Bank does not apply the low credit risk exemption to any other financial instrument.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.5 Impairment (continued)

12-month ECLs are a portion of lifetime ECLs and represent the lifetime cash shortfalls that result from default events on a financial instrument that are possible within 12 months from reporting date. Financial instruments for which a 12-month ECL is recognised are referred to as 'Stage 1' financial instruments.

Lifetime ECLs are the ECLs that result from all possible default events over the expected life of the financial instrument. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as 'Stage 2' financial instruments.

Note 4.3 provides more detail in respect of the methodology applied for the measurement of credit loss allowances. 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;
- Undrawn loan commitments: generally, as a provision, measured as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive;
- Financial instruments having both a drawn and undrawn component, whereby the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Bank presents a combined credit loss allowance for both components as a deduction from the gross carrying amount of the drawn component;
- 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 represents their fair value. An amount equal to the allowance that would arise if the assets were measured at amortised cost is recognised in other comprehensive income as an accumulated impairment amount, with a corresponding charge to profit or loss; and
- Financial guarantee contracts: generally, as a provision, measured as the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Renegotiated financial assets

The Bank renegotiates loans and advances to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. This practice is not applied to exposures classified within 'Factored receivables'.

If the terms of a financial asset are renegotiated or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, an assessment is performed to determine whether the financial asset should be derecognised. The implications on the ECL calculation depend on whether the renegotiation leads to derecognition or otherwise, as follows:

- If the restructuring does not result in the derecognition of the existing asset, renegotiated loans are typically considered credit-impaired and accordingly classified as Stage 3 assets unless no unlikeliness-to-pay ("UTP") events are deemed to have occurred. Assets that are credit-impaired at the time of renegotiation remain in Stage 3 post renegotiation. The credit loss allowance in respect of such exposures is estimated by reference to the expected cash flows arising from the modified financial asset. When evidence suggests that the renegotiated loan is no longer credit-impaired, the asset is transferred out of Stage 3 based on an assessment of historical and forward-looking information and an evaluation of the credit risk over the expected life of the asset, including information about the circumstances that led to the renegotiation.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.5 Impairment (continued)

- If the restructuring results in derecognition of the existing asset, the restructured asset is considered a 'new' financial asset. Any new financial assets that arise following derecognition events as a result of substantial modification to the terms of the instrument are classified as Stage 1 assets, unless the new financial asset is credit-impaired on initial recognition, in which case it will be classified as a purchased or credit-impaired ("POCI") financial asset. A loss is booked in profit or loss (normally as a write-off) since the new instrument is recognised at fair value.

Other than originated credit-impaired loans, all other modified loans can be transferred out of Stage 3 if they no longer exhibit any evidence of being credit-impaired and, in the case of renegotiated loans, there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows over the minimum observation period, and there are no other indicators of impairment.

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt instruments classified within 'Financial investments' and measured at FVOCI are credit-impaired (referred to as 'Stage 3 financial assets'). A financial asset is classified as 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable information:
- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the default risk has reduced significantly and if there are no other impairment indicators. In addition, a loan that is overdue for 90 days or more is considered credit-impaired.

In assessing whether a financial investment is credit-impaired, the Bank considers the following factors:
- The market's assessment of creditworthiness as reflected in bond yields;
- The rating agencies' assessments of creditworthiness, if available;
- The issuer's ability to access the capital markets for new debt issuance;
- The probability of debt restructuring, resulting in holders suffering losses through voluntary or mandatory debt forgiveness; or
- In case of sovereign debt issuers, the international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

3 Significant accounting policies *(continued)*

3.1 Financial assets (continued)

3.1.5 Impairment (continued)

Write-off

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Bank 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-off. Indicators that there is no reasonable expectation of recovery include (i) the cessation of enforcement activity and (ii) instances where the Bank's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full. This assessment is performed at the individual asset level.

Recoveries of amounts previously written off are presented within 'Change in expected credit losses and other credit impairment charges' in profit or loss.

Financial assets that are written off could still be subject to enforcement activities to comply with the Bank's procedures for recovery of amounts due.

3.2 Financial liabilities

3.2.1 Initial recognition, classification and measurement

The Bank recognises a financial liability on the 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.

The Bank classifies its financial liabilities, other than financial guarantees and loan commitments, as subsequently measured at amortised cost. Financial liabilities measured at amortised cost principally comprise 'Amounts owed to institutions', 'Amounts owed to banks', 'Amounts owed to customers', 'Debt securities in issue', together with 'Accruals'.

3.2.2 Derecognition

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

In addition, the Bank derecognises a financial liability when its terms are modified, and the contractual cash flows of the modified liability are substantially different. 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. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss. Any costs or fees incurred are recognised as part of the gain or loss on the extinguishment.

3 Significant accounting policies *(continued)*

3.2 Financial liabilities (continued)

3.2.2 Derecognition (continued)

If the modification of a financial liability is not deemed to be substantial and therefore does not result in the derecognition of the original financial liability, the amortised cost of the financial liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

3.3 Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions, such as in the Bank's trading activity.

3.4 Fair value measurement

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

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

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

The best evidence of the fair value of a financial instrument on initial recognition is normally the transaction price - i.e. the fair value of the consideration given or received. If the Bank determines that the fair value on initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique for which any unobservable inputs are judged to be insignificant in relation to the measurement, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value on initial recognition and the transaction price.

Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

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

3 Significant accounting policies *(continued)*

3.4 Fair value measurement (continued)

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Bank on the basis of the net exposure to either market or credit risk are measured on the basis of a price that would be received to sell a net long position (or paid to transfer a net short position) for the particular risk exposure. Portfolio-level adjustments - e.g. bid-ask adjustment or credit risk adjustments that reflect the measurement on the basis of the net exposure - are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of a financial liability with a demand feature (e.g. a demand deposit) is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

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

3.5 Property and equipment

3.5.1 Recognition and measurement

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

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

Freehold property is subsequently measured at fair value based on periodic valuations by external independent valuers, less subsequent depreciation. A revaluation is carried out if there is an indication that the fair value of the property differs materially from the carrying amount as at the reporting date. 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.

Equipment is subsequently stated at historical cost less accumulated depreciation and impairment losses.

3.5.2 Revaluation surplus or deficit

Increases in the carrying amount arising on revaluation of property are credited to the Property revaluation reserve within equity. Decreases that offset previous increases of the same individual asset are recognised in the Property revaluation reserve in equity; all other decreases are expensed in profit or loss. Any subsequent increases are credited to profit or loss up to the amount previously debited, at which point such increases continue to be credited to the Property revaluation reserve. Upon disposal of the premises, the relevant portion of the revaluation reserve realised is released and transferred from the Property revaluation reserve to retained earnings.

Where parts of an item of property and equipment have different useful lives, these are accounted for as separate items of property and equipment.

3.5.3 Subsequent costs

The cost of replacing a component of an item of property and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits emanating from such component will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property and equipment are recognised in profit or loss as incurred.

3 Significant accounting policies *(continued)*

3.5 Property and equipment (continued)

3.5.4 Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment from the date they are available for use.

Land is not depreciated. Upon revaluation of property, accumulated depreciation is eliminated against the gross carrying amount of the asset.

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

Premises and improvements	10 – 100 years
Computer hardware	5 years
Motor vehicles	5 years
Other equipment	5 – 7 years

Items with an initial cost of less than €250 (including taxes) are expensed immediately.

3.5.5 Derecognition

Property and equipment are derecognised upon disposal or when no future economic benefits are expected from its use. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the year during which the asset is derecognised. The asset's residual value, useful life and method is reviewed, and adjusted if appropriate, at each financial year end.

3.6 Intangible assets - software

Software acquired by the Bank is stated at cost less accumulated amortisation and any accumulated impairment losses.

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

Software is amortised on a straight-line basis in profit or loss over its estimated useful life, from the date on which it is available for use. The estimated useful life of software for the current and comparative periods is three to fifteen years.

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

3.7 Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

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

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

3 Significant accounting policies *(continued)*

3.7 Impairment of non-financial assets (continued)

An impairment loss is recognised if the carrying amount of an asset or cash-generating unit ("CGU") exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss.

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

3.8 Share capital

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity net of any tax effects. The Bank presents basic earnings per share ("EPS") data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to the Bank's ordinary shareholders by the weighted average number of ordinary shares outstanding during the period.

3.9 Financial guarantees and loan commitments

'Financial guarantees' are contracts that require the Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to honour payment commitments when due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at below-market interest rates are initially measured at fair value. Subsequently, they are measured at the higher of the credit loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15. Loan commitments provided by the Bank are measured as the amount of the credit loss allowance.

Liabilities arising from financial guarantees and loan commitments are included within provisions.

3.10 Interest income and expense

Effective interest rate

Interest income and expense are recognised in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:
- the gross carrying amount of the financial asset; or
- the amortised cost of the financial liability.

When calculating the effective interest rate for financial instruments other than POCI financial assets, the Bank estimates future cash flows by reference to the contractual terms of the financial instrument, excluding expected credit losses. For POCI financial assets, a credit-adjusted effective interest rate is calculated by reference to estimated future cash flows also taking into consideration expected credit losses.

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

3 Significant accounting policies *(continued)*

3.10 Interest income and expense (continued)

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability. The effective interest rate is revised because of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest.

However, for financial assets that are classified as credit-impaired after initial recognition, interest income is calculated by applying the effective interest rate to the net carrying amount of the financial asset after deducting ECL. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

Presentation

Interest income calculated using the effective interest method presented in profit or loss includes:
- interest on financial assets measured at amortised cost; and
- interest on debt instruments measured at FVOCI.

Interest expense presented in profit or loss represents interest in respect of financial liabilities measured at amortised cost.

3.11 Fees and commission income and expense

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

Other fees and commission income, including account servicing fees, credit administration charges and similar fees, are recognised as the related services are performed. 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.

A contract with a customer that results in a recognised financial instrument may be partially in scope of IFRS 9 and partially in scope of IFRS 15. In such an event, the Bank first applies IFRS 9 to separate and measure the part of the contract that is in scope of IFRS 9 and then applies IFRS 15 to the residual.

Other fee and commission expense relates mainly to transaction and service fees, which are expensed as the services are received.

3.12 Other operating income

The line item primarily comprises realised gains on disposal of financial instruments measured at FVOCI; foreign exchange differences attributable to the translation of monetary assets and liabilities to the Bank’s functional currency at reporting date or foreign currency transactions; and fair value movements, interest income, dividend income and foreign exchange differences attributable to financial instruments measured at FVTPL.

3 Significant accounting policies *(continued)*

3.13 Dividend income

Dividend income is recognised when the right to receive income is established. Usually, this is the ex-dividend date for quoted equity investments. Dividends are presented in other operating income. Dividends on equity instruments designated as at FVOCI that clearly represent a recovery of part of the cost of the investment are presented in other comprehensive income.

3.14 Leases

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Bank uses the definition of a lease in IFRS 16.

The Bank does not have right-of-use over assets that span over a long term or that are of significant value.

Short term leases and leases of low-value assets

The Bank has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

3.15 Employee benefits

The Bank contributes towards the State pension defined contribution plan in accordance with local legislation and to which it has no commitment beyond the payment of fixed contributions. Obligations for contributions to the defined contribution plan are recognised as an expense in profit or loss as they fall due.

3.16 Income tax

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit or loss except to the extent that it relates to items recognised directly in equity, or in other comprehensive income.

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. The amount of current tax payable or receivable is the best estimate of the tax amount expected to be paid or received that reflects uncertainty related to income taxes, if any. It is measured using tax rates enacted or substantively enacted at the reporting date. Current tax also includes any tax arising from dividends. Current tax assets and liabilities are offset only if certain criteria are met.

Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Future taxable profits are determined based on the reversal of relevant taxable temporary differences. If the amount of taxable temporary differences is insufficient to recognise a deferred tax asset in full, then future taxable profits, adjusted for reversals of existing temporary differences, are considered, based on business plans. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Such reductions are reversed when the probability of future taxable profits improves.

Unrecognised deferred tax assets are reassessed at each reporting date and recognised to the extent that it has become probable that future taxable profits will be available against which they can be used. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date. Deferred tax assets and liabilities are only offset when they arise in the same tax reporting group and relate to income taxes levied by the same taxation authority, and when the Bank has a legal right to offset.

3 Significant accounting policies *(continued)*

3.17 Foreign currency transactions

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

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

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

Foreign currency differences arising on translation are generally recognised in profit or loss save for foreign currency differences arising from equity investments in respect of which an election has been made to present subsequent changes in fair value in other comprehensive income.

3.18 Cash and cash equivalents

Cash and cash equivalents comprise notes and coins in hand, unrestricted balances held with the Central Bank of Malta and highly liquid financial assets with original maturities of three months or less from the date of acquisition that are subject to an insignificant risk of changes in their fair value, and are used by the Bank in the management of its short-term commitments.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

3.19 Segment reporting

An operating segment is a component of the Bank that engages in business activities from which it may earn revenues and incur expenses, including revenue and expenses that relate to transactions with any of the Bank's other components, whose operating results are reviewed regularly by the Bank's Board of Directors (being the chief operating decision maker), to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

3.20 Dividend distribution

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

4. Financial risk management and review

4.1 Organisation

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Audit and Risk Committee and the Credit Committee with the responsibility for monitoring risk in their specified areas. Non-executive directors sit on these Committees whereas the Chief Executive Officer ("CEO") is either a member of, or otherwise attends, all Committees. The Committees report regularly to the Board of Directors on their activities. The Board has also established an Asset and Liability Management Committee ("ALCO") which is a management committee that reports to the Board of Directors on a quarterly basis.

Risk management policies have been established to identify and analyse the risks faced by the Bank, to set out appropriate risk limits and controls, and to monitor risks and adherence to limits. The risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank has developed appropriate risk management training for the needs of the relevant staff members.

4.2 Risk exposure

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

The main categories of risk are:
- *Credit risk;*
- *Market risk*;
- *Liquidity risk; and*
- *Operational risk.*

4.3 Credit risk

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

The Bank follows standards, policies and procedures established by the Bank's Board of Directors for the control and monitoring of credit risk. The Board of Directors has delegated the responsibility for the management of credit risk to the Credit Committee within a Board-approved credit sanctioning limit. The Bank's management reports to the Credit Committee and the Board of Directors in respect of their responsibility for the management and oversight of credit risk within the Bank's portfolios of financial instruments. The responsibilities comprise the following:
- Formulating credit policies in consultation with business units, in respect of collateral requirements, credit risk assessments, risk grading and reporting, legal procedures, and compliance with regulatory and statutory requirements.
- Establishing the authorisation structure for the approval and renewal of credit facilities. Authorisation limits are allocated to the CEO, the Head of Finance and Treasury, the Credit Committee or the Board of Directors, as appropriate.
- Reviewing and assessing credit risk: the Bank's Credit department assesses the level of credit risk exposure in respect of all credit exposures, both prior to origination as well as thereafter. In this respect, the Credit department performs credit risk reviews on a periodic basis to monitor the level of credit risk subsequent to origination date. Exposures in excess of designated limits are referred for approval to the Credit Committee or the Board of Directors, as necessary.
- Limiting concentrations of exposure to counterparties, geographies and industries (for lending exposures) and to issuers, credit rating bands, markets and countries (for financial investments).
- Developing and maintaining the Bank's risk gradings to categorise exposures according to the degree of default risk. The current risk grading framework consists of 5 grades reflecting varying degrees of default risk, as described in Note 4.3.4 of the financial statements. The responsibility for setting risk grades lies with the final approving executive or committee, as appropriate. Risk grades are subject to regular reviews by senior management.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

- Developing and maintaining the Bank's processes for measuring expected credit losses ("ECLs"), including:
  - The initial approval, regular validation and back-testing of the models used;
  - The identification of SICR and UTP events; and
  - The incorporation of forward-looking information in the ECL calculation.
- Reviewing compliance of departments with agreed exposure limits, including those for selected industries, country risk and product types. Regular reports on the credit quality of the Bank's portfolios are provided to the Credit Committee, which may require appropriate corrective action to be taken. These include reports containing estimates of ECL allowances.
- Providing advice, guidance and specialist skills to departments to promote best practice throughout the Bank in respect of the management of credit risk.

The Bank's principal exposure to credit risk arises from the 'Factored receivables' portfolio as well as the Bank's lending portfolio classified as 'Loans and advances to customers'. The former portfolio comprises two sub-portfolios, both of which represent factoring of receivables on a non-recourse basis: i) factoring of local bills of exchange (hereinafter referred to as the "Bills of exchange factoring" sub-portfolio) amounting to €76.7 million as at 31 December 2022 (2021: €66.6 million); and ii) factoring of invoices issued by local and foreign customers (hereinafter referred to as the "Invoice factoring" sub-portfolio) amounting to €42.6 million as at 31 December 2022 (2021: €29.3 million).

'Loans and advances to customers' comprises the sanctioning of term loans and advances and overdraft facilities to local corporate customers, amounting to €112.9 million as at 31 December 2022 (2021: €95.3 million), as well as term lending exposures provided to related parties on an arm's length basis, amounting to €42.2 million as at 31 December 2022 (2021: €36.4 million). These exposures to local and foreign corporate customers are managed in a similar manner for credit risk management purposes, and are hereinafter collectively referred to as the "Corporate lending" sub-portfolio.

During the financial year ended 31 December 2022, the Bank started to implement its strategy to further diversify its asset base through the introduction of a new lending product, namely retail mortgage lending. In this respect, 'Loans and advances to customers' also comprises drawn retail mortgage lending exposures amounting to €5.9 million as at 31 December 2022 (2021: nil). Given that retail mortgage lending exposures (hereinafter referred to as the "Retail mortgage lending" sub-portfolio) are managed in a different manner than corporate lending facilities, the Bank's credit risk management activities in respect of the former sub-portfolio are being described and presented separately from the latter.

The outbreak of the Covid-19 pandemic during the financial year ended 31 December 2020 has resulted in unprecedented economic conditions and heightened levels of economic uncertainty, impacting the business models, income levels and cash flow generation capacity of a significant portion of the Bank's customers throughout the financial years ended 31 December 2020 and 2021. The level of economic uncertainty induced by the pandemic has subsided during the financial year ended 31 December 2022.

Following the removal of Malta from the Financial Action Task Force ("FATF") grey list in June 2022, the local economic uncertainties brought about by such grey-listing have also subsided.

Notwithstanding the above, the level of economic uncertainty remains elevated as at 31 December 2022, mainly due to the combined impact of global supply chain disruptions experienced in the aftermath of the pandemic as well as the outbreak of the military conflict between Russia and Ukraine in February 2022. Due to this, Europe experienced significant inflationary pressures during the financial year ended 31 December 2022. In response to this, the European Central Bank ("ECB") has repeatedly announced increases in interest rates in a bid to contain inflation.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

As a result, the current macroeconomic conditions on the Bank's portfolios are subject to a heightened level of uncertainty. Locally, the level of economic uncertainty has been partially mitigated through the implementation of government support schemes aimed at subsidising energy prices. Nevertheless, material uncertainties in respect of the duration of the current inflationary economic environment, potential adjustments to ECB monetary policy in the form of further interest rate hikes, the market response to increases in interest rates, the ongoing ability of the Maltese government to maintain energy subsidies at current levels, and the potential implementation of fiscal policy instruments to curtail inflation remain elevated as at 31 December 2022.

In this respect, the Bank has continued to support its customers and adapted its credit risk management processes accordingly to enable the identification of deterioration in credit risk within its portfolios as early as possible and estimating credit loss allowances using the best possible judgement.

During the financial years ended 31 December 2020 and 2021, the Bank granted moratoria on capital and/or interest payments to customers and originated new loans to provide relief to customers experiencing liquidity pressures induced by the prevailing macroeconomic conditions. These moratoria have now matured and customers have reverted to pre-moratoria repayment schedules. In addition, the Bank continues to service facilities granted to support its corporate customers during the pandemic, which facilities are guaranteed under the Malta Development Bank Covid-19 Guarantee Scheme.

During 2022, the Bank continued to individually rate borrowers deemed mostly impacted by the heightened levels of economic uncertainty through individual credit risk assessments, on the basis of recently obtained management information and, where available, forecasts, enabling management to assess borrower-specific credit risk levels and identify SICR or UTP events.

In respect of the Bills of exchange factoring sub-portfolio, the Bank assesses credit risk at origination through a scorecard designed to assess the individual debtor's level of credit risk by reference to the debtor's net disposal income and employment status, amongst other factors featuring in the scorecard.

The macroeconomic uncertainties being experienced throughout Europe, particularly in respect of the current inflationary pressures and an increasing interest rate environment, induced an elevated level of uncertainty in respect of economic outlook. In this respect, the extent to which macroeconomic forecasts accurately reflect potential future developments in the general macroeconomic environment and the effects of monetary and fiscal policy instruments on markets remains uncertain. These factors necessitate heightened expert judgement to 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 4.3.2.4.

4.3.1 Credit risk measurement

Measurement of credit risk considers that an exposure varies with changes in market conditions, expected cash flows and the passage of time. The Bank's internal models measure expected credit losses by portfolio using probability of default ("PD"), exposure at default ("EAD") and loss given default ("LGD") parameters.

(a) Loans and advances to customers

The Bank uses internal credit risk grades (refer to Note 4.3.4) to reflect its assessment of the probability of default of individual counterparties or facilities. Internal credit risk gradings are based on payment behaviour, loan specific information and expert judgement of the Bank's Credit Committee.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.1 Credit risk measurement (continued)

For corporate lending exposures, information considered by the Bank when determining the internal credit risk grades includes the payment behaviour of the borrower, compliance with financial covenants, and other information impacting a corporate borrower's creditworthiness assessment, including historical information in respect of its financial performance and financial position as well as forecasted financial information. Management also takes into consideration non-financial indicators in the performance of credit risk assessments, such as the timeliness of the provision of financial information, the industry-specific outlook and the impact of general macroeconomic conditions on the borrower's financial performance.

The internal credit risk grades are calibrated such that they reflect the increased risk of default at each higher risk grade. The rating is determined at borrower level through the performance of a creditworthiness assessment of the borrower in each periodic review, performed at least annually.

For retail mortgage lending exposures, internal credit risk grades are determined on the basis of payment behaviour and days past due. Refer to Note 4.3.4 for the definition of the internal retail credit risk grades used by the Bank.

(b) Factored receivables

Unlike corporate exposures classified within 'Loans and advances to customers', bills of exchange factoring and invoice factoring facilities classified within 'Factored receivables' are not managed on a credit by credit basis due to the high volume of relatively low value and homogeneous exposures.

In respect of bills of exchange factoring facilities, the credit risk assessment after the date of initial recognition is based on the payment behaviour of debtors, which is monitored on an ongoing basis. The Bank therefore distinguishes between 'problematic' and 'non-problematic' exposures by reference to the number of overdue monthly bill payments at any given point in time.

In respect of invoice factoring facilities, the Bank performs its credit risk assessment at the debtor level by (i) monitoring the payment behaviour of any particular debtor by reference to the proportion of invoices which are past due at any given point in time; and (ii) determining PDs by reference to a credit score assigned to each debtor, which credit score is sourced from a third party external vendor and captures other information about the borrower which impacts their creditworthiness, such as financial performance and previous delinquency history.

(c) Other financial assets

Other financial assets include balances with the Central Bank of Malta, loans and advances to banks and financial investments. The Bank considers public credit ratings determined by external credit rating agencies to assess the probability of default of individual counterparties. Such public credit ratings are continuously monitored and updated, with the associated PD being determined by reference to realised default rates over the prior 12 months. In determining the probability of default of individual counterparties, the Bank distinguishes between investment-grade and sub-investment grade counterparties.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

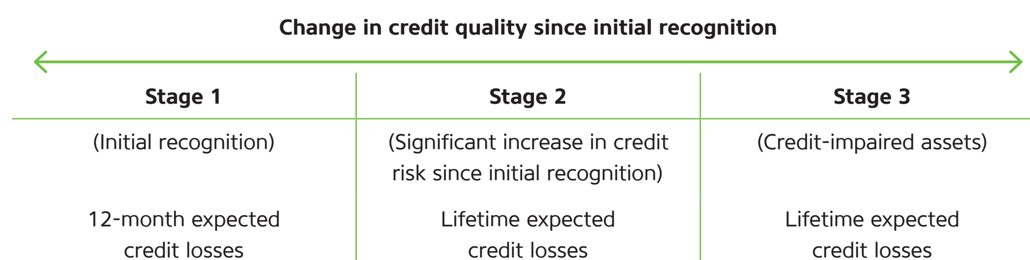
4.3.2 Expected credit loss measurement

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 upon initial recognition is classified in 'Stage 1'.
- 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. Refer to Note 4.3.2.1 for a description of how the Bank determines when a SICR has occurred.
- If the financial instrument becomes credit-impaired, the financial instrument is moved to 'Stage 3'. Refer to Note 4.3.2.2 for the Bank's definition of credit-impaired.
- 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 'Stage 2' or 'Stage 3' have their ECL measured based on expected credit losses on a lifetime basis. Refer to Note 4.3.2.3 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 forward-looking information is considered. Note 4.3.2.4 includes an explanation of how the Bank has incorporated forward looking information into ECL models.
- Purchased or originated credit-impaired financial assets are those financial assets that are credit-impaired upon initial recognition. The ECL in respect of POCI exposures is always measured on a lifetime basis ('Stage 3').

The expected credit loss requirements apply to financial assets measured at amortised cost and FVOCI, and certain loan commitments. At initial recognition, a credit loss allowance (or provision in the case of loan commitments) 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").

The Bank recognises credit 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 Bank considers a debt security to have low credit risk when it is considered 'investment-grade', as defined by external credit rating agencies. The following diagram summarises the impairment requirements under IFRS 9 (other than POCI financial assets):



4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.1 Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Bank's historical experience and expert credit assessment and including forward-looking information.

For Corporate lending exposures classified within 'Loans and advances to customers', the Bank primarily identifies whether a SICR has occurred since initial recognition by reference to the internal risk gradings determined on an individual borrower level. The Bank allocates each exposure to an internal credit risk grade based on financial and non-financial information which is deemed to be predictive of the risk of default. Amongst other things, reference is made to audited financial statements, management accounts, budgets and projections. Management applies expert credit judgement in assessing the level of credit risk attributable to specific borrowers. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different internal rating grade (refer to Note 4.3.4).

The Bank classifies non-defaulted exposures into 'Stage 2' when the borrower is classified within the 'Substandard' internal credit risk grade and / or forbearance measures have been granted to the borrower, unless additional UTP events have been identified.

As referred to previously, the macroeconomic conditions being experienced as a result of the global supply chain disruptions experienced in the aftermath of the pandemic, together with the escalation of the military conflict between Russia and Ukraine, resulting in widespread inflationary pressures and an increasing interest rate environment, 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 potential delays in default emergence as a result of the application of government support schemes which might veil longer term financial difficulties.

Corporate borrowers are assessed periodically for SICR and UTP events by reference to recently obtained management information, including forecasts. During 2022, more information became available in respect of the real impact of the developments referred to above on specific borrowers and industry sectors. This enabled management to better identify SICR events, resulting in migrations from stage 1 to 2, as per information presented in Note 4.3.5.

In relation to retail mortgage lending exposures classified within 'Loans and advances to customers' and 'Factored receivables', 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 addition, the Bank uses a backstop of 30 days past due to determine whether a significant increase in credit risk has occurred since origination in respect of loans and advances to customers as well as exposures classified within the bills of exchange factoring portfolio.

Due to the short-term nature of facilities within the invoice factoring portfolio, the Bank does not distinguish between exposures classified within Stage 1 or Stage 2 since the lifetime PD is deemed to be equivalent to the 12-month PD.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.1 Significant increase in credit risk (continued)

In the case of other financial assets (including loans and advances to banks and debt investment securities), the Bank applies the low credit risk simplification to exposures having an 'investment grade' public credit rating. In this respect, such exposures are not subject to the SICR assessment. Moving from 'investment-grade' to 'sub-investment grade' does not automatically trigger a SICR.

4.3.2.2 Definition of default and credit-impaired assets

The Bank'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.

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

The Bank determines that a financial instrument is credit-impaired or in default (and accordingly classified as Stage 3 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 Bank; and
- for corporate lending exposures classified within loans and advances to customers, whether there are other indicators that the borrower is unlikely to pay without realisation of collateral, such as an observed deterioration in the financial performance and / or financial position of the borrower; covenant breaches; and concessions granted to a borrower experiencing financial difficulties.

As described earlier, the staging determination in respect of retail mortgage lending exposures and factored receivables is based on payment behaviour, since these portfolios comprise exposures which are homogeneous and individually low in value.

The default definition is applied consistently when modelling PD, EAD and LGD parameters throughout the Bank's expected credit loss calculations.

Due to the elevated level of uncertainty induced by the current economic environment, as well as the potential delayed default emergence due to the implementation of government support schemes, the Bank performed borrower-level assessments in respect of corporate lending exposures classified within loans and advances to customers to determine whether the economic shock may transform into long-term borrower financial difficulties, thereby potentially requiring a downgrade of individual exposures to Stage 3 to reflect the level of change in credit risk.

An instrument is considered to have cured from defaulted status when it no longer meets any of the default criteria for a period of three consecutive months and, in case of forborne exposures, a period of 12 consecutive months.

The Bank considers other financial assets to be in default when a payment (including a coupon payment) becomes overdue by 1 day or more.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.3 Measurement of ECL

The key inputs into the measurement of ECL comprise the PD, LGD and EAD, with the term structure being determined in respect of each parameter.

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD.

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

Probability of default

The PD represents the likelihood of a borrower defaulting on its financial obligation (as defined in Note 4.3.2.2), either over the next 12 months (12-month PD) or over the remaining lifetime (lifetime PD) of the obligation.

Until 2021, the PD calculation for loans and advances to customers was based on a transition matrix approach. The main assumptions underlying the latter approach is that the PD does not depend on 'months on book' and that the future PD depends on current characteristics of the exposure or borrower.

In this respect, credit scores were assigned to individual borrowers on the basis of financial performance data, payment behaviour and country risk. Credit scores were then mapped to a rating scale, on the basis of which a PD was assigned to each borrower. The rating scale to PD matrices were calibrated based on historical default data observed in the market, where the data was sourced from external credit rating agencies.

During the financial year ended 31 December 2022, the Bank implemented a credit risk modelling solution developed by an external vendor to estimate PDs in respect of corporate lending exposures classified within loans and advances to customers, in view of the lack of internal history of defaults within this sub-portfolio.

In this respect, the Bank employs statistical models to analyse financial statement data collected in respect of each individual borrower and assign a credit score accordingly. Specifically, the Bank benchmarks the borrower's financial statements with those of an underlying model dataset comprising obligors which are comparable to the Bank's corporate borrowers in terms of size and industry. Borrower-specific credit scores are then mapped to a PD, which is first adjusted to capture country- and industry-specific credit risk characteristics and then assigned to each obligor. The credit score to PD matrices are calibrated based on historical default data observed in the market, where the data was sourced from publicly available information.

As described in Note 4.3.2, the determination of staging is based on a qualitative assessment performed at borrower level. In this respect, the estimation of 12-month or lifetime PDs in respect of any given borrower is determined by reference to assigned internal credit risk grades.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.3 Measurement of ECL (continued)

Lifetime PDs are estimated by applying a scalar to the 12-month PD. The scalar, which is based on historical observed data and is assumed to be the same across all assets within a portfolio, looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans.

For retail mortgage lending exposures, PDs are determined by reference to comparable portfolios at peer banks, given that the portfolio is still in its infancy and the Bank does not have any internally observable default data.

In the case of bills of exchange factoring facilities, the Bank's PDs are determined by reference to an internally developed statistical model based on a Markov chain approach. In this respect, 12-month transition matrices were derived from internal historical data. Default is considered to be an absorbing state, whereby if an exposure is defaulted, it subsequently remains in default for the purposes of estimation of PDs.

A seven-tier rating scale has been developed, designed to capture different potential states of delinquency, ranging from a 'current' status to a '360DPD+' status. Exposures classified within each of the seven-tier rating scales are assigned a PD determined on the basis of internal historical delinquency information. Each tier is then mapped to a relative stage, as described in Note 4.3.4. A cure rate is also applied, also estimated by reference to internal historical delinquency information in respect of this portfolio.

In the case of invoice factoring facilities, PDs are sourced from an external vendor. In this respect, a debtor-specific credit score is assigned by the external vendor based on borrower-specific information. PDs are then determined by reference to the debtor-specific credit score. Due to the short-term maturity profile of such exposures, no distinction is made between 12-month and lifetime PDs for the purposes of the ECL calculation.

For financial investments issued by corporates, the PD is estimated using the same methodology applied in respect of exposures classified within loans and advances to customers. In this respect, PDs are determined through the use of a credit risk modelling solution developed by an external vendor.

For sovereign debt securities, the Bank estimates PDs by reference to market data issued by external credit rating agencies. In this respect, the PDs used in the ECL calculation reflects historical default rates determined by external credit rating agencies for issuers assigned an external credit rating which is equivalent to the Bank's financial investments. If a counterparty or exposure migrates between external credit ratings, this will lead to a change in PD.

As described in further detail in Note 4.3.2.4, the 12-month and lifetime PDs estimated in respect of loans and advances to customers and bills of exchange factoring facilities also take into consideration forward-looking economic information.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.3 Measurement of ECL (continued)

Loss given default

The LGD represents the Bank's expectation of the extent of the loss on a defaulted exposure. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). The Bank estimates the LGD on the basis of historical recovery rates of claims against defaulted counterparties. The estimation of LGD considers the structure and seniority of the claim, together with the nature and recoverability / enforceability of collateral and associated recovery costs.

Loans and advances to customers are primarily secured by residential and / or commercial real estate, as well as cash pledges. In respect of the former, the LGD takes into consideration projected collateral values, historical discounts to market values to reflect a deduction in future proceeds due to costs to sell and potential loss in value in a forced sale scenario, and time to repossession. A key determinant for the LGD applied to exposures secured by real estate is the Loan-to-Value ratio of individual facilities, where the value of the property takes into account the expected recovery from the sale of the property.

Until 2021, a 100% LGD was assumed by the Bank for unsecured loans and advances to customers. Subsequent to the model change implemented during the financial year ended 31 December 2022, the Bank applies LGDs developed by an external vendor and determined by reference to the carrying amount of tangible assets recognised on the borrower's balance sheet. Expected recoveries from the sale of such assets are used to determine the expected loss and are modelled by reference to assumptions in relation to different haircuts to sale proceeds depending on asset type and the time value of money. The LGD determined through the use of statistical techniques by the external vendor also takes into consideration a correlation factor between PDs and LGDs, with higher LGDs being assigned to borrowers to whom a higher PD is determined by the model.

For bills of exchange factoring facilities, the LGD is determined by reference to the value of the motor vehicle being financed. Specifically, it is assumed that the original value of the motor vehicle is depreciated on a straight-line basis over its useful life. In addition, the LGD calculation also takes into consideration the collateral provided by the factoring clients, which comprises pledged cash held with the Bank to cover potential losses from factored bills of exchange.

In the case of invoice factoring facilities, the Bank purchases credit insurance from a foreign third party underwriter which provides insurance cover in respect of losses up to 95% of each eligible invoice. In this respect, the LGD applied to invoice factoring facilities is determined on this basis.

Exposure at default

EAD represents the expected exposure in the event of a default. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EAD reflects an estimation of potential future drawdowns permissible in terms of the contract, which are estimated based on historical observations and forward-looking expectations.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.3 Measurement of ECL

For loans and advances to customers, the Bank estimates the EAD by reference to the expected balance at default. In this respect, the EAD for term lending exposures (including retail mortgage exposures) takes into consideration the current exposure to the counterparty as well as future expected drawdowns of committed facilities, with different drawdown factors applied to partially drawn and fully unutilised facilities. For revolving exposures, the EAD is estimated by reference to the maximum potential exposure at default.

For bills of exchange factoring facilities, the Bank estimates the EAD by reference to the current exposure to the counterparty and potential changes to the exposure due to contractual repayments.

For invoice factoring facilities, the EAD is assumed to be equal to the gross carrying amount of the exposure at reporting date, since repayments from each facility are expected to be made in one instalment in line with the invoice credit terms.

Period over which ECL is measured

The Bank measures ECL considering the risk of default over the maximum contractual period over which it is exposed to credit risk (including any extension options), even if, for credit risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment.

However, for revolving facilities that include both a loan and an undrawn commitment component, the Bank measures ECL over a period longer than the maximum contractual period if the Bank's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Bank's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are managed on a collective basis. The Bank can cancel them with immediate effect, albeit this contractual right is not enforced in the normal day-to-day management unless the Bank becomes aware of an increase in credit risk at facility level. This longer period is estimated considering the credit risk management actions that the Bank expects to take, and that serve to mitigate ECL. These include a reduction in limits, cancellation of the facility and/or turning the outstanding balance into a loan with fixed repayment terms.

4.3.2.4 Forward-looking information incorporated in the ECL model

The calculation of ECL incorporates forward-looking information. The Bank 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 ECL may vary by portfolio. Expert judgement has been applied in the process.

The key drivers of credit risk and credit losses for each portfolio were determined on the basis of a statistical regression analysis of historical relationships between macroeconomic variables and market default data. These key macroeconomic variables determined in respect of each portfolio are disclosed below:

- Corporate lending exposures classified within loans and advances to customers: Until 2021, the Euro area real Gross Domestic Product ("GDP") and the Euro area Terms of Trade ("ToT") represented the key macroeconomic variables used to estimate ECL for such exposure. Subsequent to the model change, the Bank started estimating forward-looking ECL by reference to the GDP growth rate, unemployment rate, inflation rate, and interest rates, all specific to the local Maltese economy, reflecting the impact of general economic activity on the financial performance of corporate entities; and

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.4 Forward-looking information incorporated in the ECL model (continued)

- Bills of exchange factoring: the Euro area real GDP, which is deemed to be a good indicator of general economic activity.

Given the short-term nature of invoice factoring facilities, the impact of forward-looking information on the estimation of ECL in respect of these exposures is not deemed to be significant. Similarly, the impact of forward-looking information on the estimation of ECL in respect of retail mortgage lending exposures classified within loans and advances to customers is also deemed to be insignificant due to the fact that the portfolio is still in its infancy.

Three possible scenarios are considered to capture non-linearity across credit portfolios. The 'baseline' scenario represents the most-likely outcome. Macroeconomic forecasts in respect of these macroeconomic variables are sourced from an authoritative source on a semi-annual basis, providing the best estimate view of the economy over a forecasted time horizon.

Until 2021, the macroeconomic forecasts applied in the estimation of ECL for loans and advances to customers and bills of exchange factoring exposures were modelled over a five-year time horizon. After five years, to project the macroeconomic variables out for the full remaining lifetime of each financial instrument, a mean reversion approach was used, with the macroeconomic variables assumed to tend to a long-run average growth rate.

Subsequent to the implementation of the new model developed by an external vendor and used to estimate ECLs for corporate lending exposures classified within loans and advances to customers, macroeconomic forecasts are modelled over a 12-month time horizon. The macroeconomic modelling approach used to estimate ECL for bills of exchange factoring exposures remains unchanged.

In addition to the 'baseline' scenario, the Bank considers an 'upside' and a 'downside' macroeconomic scenario, which respectively represent a more optimistic and a more pessimistic outcome, reflecting economically plausible upside and downside scenarios. The relative paths for the macroeconomic variables in the 'upside' and 'downside' scenarios are determined through statistical variance analysis techniques applied to the 'baseline' scenario.

Each scenario is weighted by a probability of occurrence, determined by a combination of macroeconomic research and expert credit judgment, taking into account the range of possible outcomes each chosen scenario represents. The ECL under each scenario is multiplied by the appropriate scenario weighting to determine a probability-weighted ECL.

As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and, as a result, the actual outcomes may be significantly different to those projected. The level of uncertainty is exacerbated by the economic conditions being currently experienced in the aftermath of the pandemic and the escalation of the military conflict between Russia and Ukraine, with global supply chain disruptions triggering inflationary pressures across Europe and an ensuing monetary policy response from the ECB resulting in an increasing interest rate environment.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.4 Forward-looking information incorporated in the ECL model (continued)

The heightened level of macroeconomic uncertainty experienced in both global and local economies has had varying effects on different industry sectors. At the same time, measures designed to soften the extent of the damage to economic activity and the labour market were announced by the Maltese government in the form of subsidised energy prices.

The current financial year was characterised by strong economic growth as the global and local economies bounced back resulting in high growth rates. The base assumption is that the inflationary pressures and the increasing interest rate environment being experienced at a continental level will continue to prevail in the short-to-medium term. However, it is forecasted that the effect of inflationary pressures on local economic activity will be partially contained through the subsidization of energy prices by the Maltese government.

The unwinding of such government support schemes, as well as potential further increases in interest rates designed to contain existing inflationary pressures, represent significant uncertainties to be taken into consideration when forecasting potential economic paths over the short-to-medium term.

In view of the above, a significant judgement within the Bank's estimation of credit loss allowances relates to the determination of forward-looking scenarios reflecting potential future economic conditions under different scenarios and their impact on the ECL calculation. The Bank considers these forecasts to represent its best estimate of the possible outcomes.

The most significant year end assumptions used for the ECL estimate as at 31 December 2022 and 31 December 2021 are set out below.

	As at 31 December 2022		
	Projection for Malta in 2023		
	Baseline	**Upside**	**Downside**
GDP growth rate	**0.4**	**2.0**	**-4.0**
Unemployment rate	**7.1**	**6.0**	**8.0**
Inflation rate	**5.2**	**4.0**	**11.0**
Interest rates	**3.5**	**3.0**	**4.5**

	As at 31 December 2022		
	Euro area real GDP growth rate (%)		
	Baseline	**Upside**	**Downside**
2023	**0.5**	**3.1**	**-2.1**
2024	**1.8**	**4.4**	**-0.9**
2025	**1.9**	**4.6**	**-0.7**
2026	**1.7**	**4.4**	**-0.9**

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.2 Expected credit loss measurement (continued)

4.3.2.4 Forward-looking information incorporated in the ECL model (continued)

	As at 31 December 2021					
	Euro area real GDP growth rate (%)			Euro area Terms of Trade (%)		
	Baseline	Upside	Downside	Baseline	Upside	Downside
2022	3.10	6.34	-0.14	-1.60	-0.61	-2.60
2023	2.21	5.46	-1.03	-0.63	0.36	-1.62
2024	1.70	4.95	-1.54	-0.21	0.79	-1.20
2025	1.42	4.66	-1.83	-0.02	0.97	-1.01
2026	1.77	5.02	-1.47	-0.29	0.71	-1.28

The weightings assigned to the ‘baseline’, ‘upside’ and ‘downside’ scenarios are 50% (2021: 50%), 25% (2021: 25%) and 25% (2021: 25%) respectively.

Economic scenarios sensitivity analysis of ECL estimates

The outcome of the Bank’s credit loss allowances estimation process is sensitive to judgements and estimations made throughout the incorporation of forward-looking economic conditions. Management has assessed the sensitivity of ECLs by assigning a 100% weighting to the baseline, downside and upside scenarios respectively. The Bank’s credit loss allowances would increase by €445,864 (2021: €862,371) if these had to be estimated solely on the basis of the downside scenario and would reduce by €251,551 (2021: €232,781) if these had to be estimated solely on the basis of the upside scenario.

4.3.3 Maximum exposure to credit risk

The Bank’s maximum credit risk exposure to on and off-balance sheet financial instruments, before taking account of any collateral held or other credit enhancements, can be classified in the following categories:

- Financial assets recognised in the statement of financial position comprise balances with Central Bank of Malta, loans and advances to banks, financial investments, factored receivables, and loans and advances to customers. The maximum exposure to credit risk in respect of these financial assets equals their carrying amount.
- Commitments in respect of factored receivables, overdrafts, and credit cards - the maximum exposure to credit risk is the full amount of the committed facilities (Note 29).

The following table presents the maximum exposure to credit risk from on-balance sheet and off-balance sheet financial instruments before taking account of any collateral held or other credit enhancements.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.3 Maximum exposure to credit risk (continued)

	2022		2021	
	Gross carrying amount €	**Allowance For ECL €**	Gross carrying amount €	Allowance For ECL €
Credit risk exposure relating to on-balance sheet assets				
Subject to IFRS 9 impairment requirements				
Financial assets measured at amortised cost				
Balances with Central Bank of Malta	**17,598,287**	**-**	16,192,155	-
Loans and advances to banks	**10,214,993**	**-**	25,420,282	-
Factored receivables				
- Bills of exchange factoring	**76,657,356**	**(116,000)**	66,550,268	(15,000)
- Invoice factoring	**42,611,756**	**(789,388)**	29,277,379	(760,813)
Loans and advances to customers				
- Corporate lending	**155,255,795**	**(816,086)**	131,698,327	(328,986)
- Retail mortgages	**5,907,178**	**(17,605)**	-	-
Accrued income	**1,937,194**	**-**	1,335,715	-
Debt securities measured at FVOCI	**90,972,629**	**(46,682)**	96,730,990	(11,860)
Credit risk exposure	**401,155,188**	**(1,785,761)**	367,205,116	(1,116,659)
Credit risk exposure relating to off-balance sheet assets				
Undrawn commitments to lend	**185,068,135**	**-**	92,738,305	-
Credit risk exposure	**586,223,323**	**(1,785,761)**	459,943,421	(1,116,659)

Accrued income substantially arises from factored receivables and loans and advances to customers. Expected credit losses in respect of accrued income, which are not deemed material, have been allocated to factored receivables and loans and advances to customers. Similarly, expected credit losses in respect of undrawn commitments are also allocated to loans and advances to customers.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.3 Maximum exposure to credit risk (continued)

	2022 Fair value €	2021 Fair value €
Credit risk exposure relating to on-balance sheet assets not subject to IFRS 9 impairment requirements		
Equity investments designated at FVOCI	**30,275**	30,275
Equity investments measured at FVTPL	**548,023**	20,519,447
Credit risk exposure	**578,298**	20,549,722

4.3.4 Credit quality analysis

As described in Note 4.3, the Bank's internal credit risk grades are designed to highlight exposures which require closer management attention because of their greater probability of default and potential loss. The credit quality of the Bank's portfolios of financial instruments is assessed by reference to the Bank's standard credit rating system, as described below:

Credit quality classification	**Financial investments**	**Bills of exchange factoring**	**Invoice factoring / Retail mortgage lending**
Regular	BBB and above	Not past due	Not past due
Watch	BBB- to C	1 to 30 days past due	1 to 30 days past due
Substandard		31 to 90 days past due	31 to 90 days past due
Doubtful	Default	Past due by more than 90 days	Past due by more than 90 days
Loss		Amount partially or fully written off	Amount partially or fully written off

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.4 Credit quality analysis (continued)

The credit quality of loans and advances to customers is managed by the Bank's Credit department using internal credit ratings, defined as follows.

Credit quality classification	Risk attributes
Regular	A customer having no overdue interest and/or capital payments overdue or a recent history of default. Regular exposures are typically deemed to have minimal risk of future losses on the basis of strong financial position and performance.
Watch	A customer having interest and/or capital payments overdue by up to 30 days. 'Watch' exposures typically exhibit deteriorating financial position and performance and initial signs of financial difficulties.
Substandard	A customer having interest and/or capital payments overdue by more than 30 days and up to 90 days. 'Substandard' exposures typically exhibit a prolonged deterioration in financial position and performance which raises concerns in respect of potential debt service shortfalls.
Doubtful	A customer having interest and/or capital payments overdue by more than 90 days. 'Doubtful' exposures are considered to be defaulted on the basis of the identification of unlikeliness to pay events as defined in Note 3.1.5, whereby it becomes evident that the borrower will not be in a position to meet contractual repayments without resorting to the sale / repossession of collateral.
Loss	Amount partially or fully written off

The following tables summarise the credit loss allowances recognised as at 31 December 2022 and 2021 in respect of each class of financial instruments by stage distribution.

		Allowance for ECL			
2022	**Gross carrying amount**	**Stage 1**	**Stage 2**	**Stage 3**	**Net carrying amount**
	€	**€**	**€**	**€**	**€**
Loans and advances to customers measured at amortised cost					
- Corporate lending	**155,255,795**	**(705,052)**	**(22,202)**	**(88,832)**	**154,439,709**
- Retail mortgages	**5,907,178**	**(17,605)**	**-**	**-**	**5,889,573**
Factored receivables measured at amortised cost	**119,269,112**	**(170,168)**	**(51,391)**	**(683,829)**	**118,363,724**
ECL allowance per stage		**(892,825)**	**(73,593)**	**(772,661)**	

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.4 Credit quality analysis (continued)

2021	Gross carrying amount	Allowance for ECL Stage 1	Stage 2	Stage 3	Net carrying amount
	€	€	€	€	€
Loans and advances to customers measured at amortised cost					
- Corporate lending	131,698,327	(263,165)	(1,699)	(64,122)	131,369,341
Factored receivables measured at amortised cost	95,827,647	(93,303)	-	(682,510)	95,051,834
ECL allowance per stage		(356,468)	(1,699)	(746,632)	

2022	Fair value	Allowance for ECL Stage 1	Stage 2	Stage 3
	€	€	€	€
Debt securities measured at FVOCI	**90,972,629**	**(46,682)**	**-**	**-**

2021	Fair value	Allowance for ECL Stage 1	Stage 2	Stage 3
	€	€	€	€
Debt securities measured at FVOCI	96,730,990	(11,860)	-	-

The credit loss allowances in respect of balances with Central Bank of Malta and Loans and advances to banks are deemed insignificant.

The following tables present information in respect of the credit quality of financial assets measured at amortised cost and debt securities measured at FVOCI.

	As at 31 December 2022			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Loans and advances to banks measured at amortised cost				
Grade 1: Regular	**10,214,993**	**-**	**-**	**10,214,993**
Gross carrying amount	**10,214,993**	**-**	**-**	**10,214,993**
Allowance for ECL	**-**	**-**	**-**	**-**
Net carrying amount	**10,214,993**	**-**	**-**	**10,214,993**

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.4 Credit quality analysis (continued)

	As at 31 December 2021			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Loans and advances to banks measured at amortised cost				
Grade 1: Regular	25,420,282	-	-	25,420,282
Gross carrying amount	25,420,282	-	-	25,420,282
Allowance for ECL	-	-	-	-
Net carrying amount	25,420,282	-	-	25,420,282

	As at 31 December 2022			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Debt securities measured at FVOCI				
Grade 1: Regular	**90,972,629**	**-**	**-**	**90,972,629**
Fair value	**90,972,629**	**-**	**-**	**90,972,629**
Allowance for ECL	**(46,682)**	**-**	**-**	**(46,682)**

	As at 31 December 2021			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Debt securities measured at FVOCI				
Grade 1: Regular	96,730,990	-	-	96,730,990
Fair value	96,730,990	-	-	96,730,990
Allowance for ECL	(11,860)	-	-	(11,860)

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.4 Credit quality analysis (continued)

	As at 31 December 2022			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Loans and advances to customers measured at amortised cost				
Corporate Lending				
Grade 1: Regular	147,602,932	-	-	147,602,932
Grade 2: Watch	4,169,993	-	-	4,169,993
Grade 3: Substandard	-	1,481,010	-	1,481,010
Grade 4: Doubtful	-	-	1,984,580	1,984,580
Grade 5: Loss	-	-	17,280	17,280
Gross carrying amount	151,772,925	1,481,010	2,001,860	155,255,795
Allowance for ECL	(705,052)	(22,202)	(88,832)	(816,086)
Net carrying amount	151,067,873	1,458,808	1,913,028	154,439,709
Retail mortgages				
Grade 1: Regular	5,907,178	-	-	5,907,178
Gross carrying amount	5,907,178	-	-	5,907,178
Allowance for ECL	(17,605)	-	-	(17,605)
Net carrying amount	5,889,573	-	-	5,889,573
Total				
Grade 1: Regular	153,510,110	-	-	153,510,110
Grade 2: Watch	4,169,993	-	-	4,169,993
Grade 3: Substandard	-	1,481,010	-	1,481,010
Grade 4: Doubtful	-	-	1,984,580	1,984,580
Grade 5: Loss	-	-	17,280	17,280
Gross carrying amount	157,680,103	1,481,010	2,001,860	161,162,973
Allowance for ECL	(722,657)	(22,202)	(88,832)	(833,691)
Net carrying amount	156,957,446	1,458,808	1,913,028	160,329,282

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.4 Credit quality analysis (continued)

	As at 31 December 2021			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Loans and advances to customers measured at amortised cost				
Corporate Lending/Total				
Grade 1: Regular	122,115,721	-	-	122,115,721
Grade 2: Watch	4,936,292	-	-	4,936,292
Grade 3: Substandard	-	3,172,018	-	3,172,018
Grade 4: Doubtful	-	-	1,425,198	1,425,198
Grade 5: Loss	-	-	49,098	49,098
Gross carrying amount	127,052,013	3,172,018	1,474,296	131,698,327
Allowance for ECL	(263,165)	(1,699)	(64,122)	(328,986)
Net carrying amount	126,788,848	3,170,319	1,410,174	131,369,341

	As at 31 December 2022			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Factored receivables measured at amortised cost				
Grade 1: Regular	**60,159,527**	**-**	**-**	**60,159,527**
Grade 2: Watch	**10,165,247**	**-**	**-**	**10,165,247**
Grade 3: Substandard	**-**	**29,141,788**	**-**	**29,141,788**
Grade 4: Doubtful	**-**	**-**	**19,802,550**	**19,802,550**
Gross carrying amount	**70,324,774**	**29,141,788**	**19,802,550**	**119,269,112**
Allowance for ECL	**(170,168)**	**(51,391)**	**(683,829)**	**(905,388)**
Net Carrying amount	**70,154,606**	**29,090,397**	**19,118,721**	**118,363,724**

	As at 31 December 2021			
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Factored receivables measured at amortised cost				
Grade 1: Regular	36,598,774	-	-	36,598,774
Grade 2: Watch	18,928,174	-	-	18,928,174
Grade 3: Substandard	-	26,530,945	-	26,530,945
Grade 4: Doubtful	-	-	13,769,754	13,769,754
Gross carrying amount	55,526,948	26,530,945	13,769,754	95,827,647
Allowance for ECL	(93,303)	-	(682,510)	(775,813)
Net Carrying amount	55,433,645	26,530,945	13,087,244	95,051,834

The following tables present information in respect of the overdue status of the gross carrying amount of

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.4 Credit quality analysis (continued)

factored receivables and loans and advances to customers analysed by stage distribution.

	As at 31 December 2022				As at 31 December 2021			
	Stage 1 €	Stage 2 €	Stage 3 €	Total €	Stage 1 €	Stage 2 €	Stage 3 €	Total €
Factored receivables								
Current	**60,159,527**	**-**	**-**	**60,159,527**	36,598,774	-	-	36,598,774
Overdue < 30 days	**10,165,247**	**-**	**-**	**10,165,247**	18,928,174	-	-	18,928,174
Overdue > 30 days	**-**	**29,141,788**	**-**	**29,141,788**	-	26,530,945	-	26,530,945
Overdue > 90 days	**-**	**-**	**19,802,550**	**19,802,550**	-	-	13,769,754	13,769,754
Total	**70,324,774**	**29,141,788**	**19,802,550**	**119,269,112**	55,526,948	26,530,945	13,769,754	95,827,647
Loans and advances to customers								
Current	**157,680,103**	**1,481,010**	**-**	**159,161,113**	127,052,013	3,172,018	-	130,224,031
Overdue > 90 days	**-**	**-**	**2,001,860**	**2,001,860**	-	-	1,474,296	1,474,296
Total	**157,680,103**	**1,481,010**	**2,001,860**	**161,162,973**	127,052,013	3,172,018	1,474,296	131,698,327

4.3.5 Reconciliation of changes in gross carrying amount and allowances for ECL

The credit loss allowance recognised 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 during the period, and the consequent “step up” (or “step down”) between 12-month and Lifetime ECL;
- additional allowances for new financial instruments recognised during the period, as well as releases in respect of financial instruments derecognised during the period;
- impact on the measurement of ECL due to changes in PD, LGD or EAD during the period;
- impacts on the measurement of ECL due to changes made to models and assumptions; and
- write-offs of allowances related to assets that were written off during the period.

The allowance for ECL in respect of loans and advances to customers as at 31 December 2022 increased significantly compared to the prior year, resulting in an ECL charge for the financial year ended 31 December 2022 amounting to €504,705. This was primarily driven by the impact of the newly implemented model during the financial year ended 31 December 2022, which resulted in higher ECL coverage ratios in respect of loans and advances to customers. The increase in the allowance for ECL was also driven by the growth in the size of the lending portfolio, which increased by €29.5 million during the financial year ended 31 December 2022.

In addition, the reconciliation of ECL in respect of loans and advances to customers also shows downward migrations of borrowers from Stage 1 to Stage 2 and from Stage 2 to Stage 3, primarily reflecting observed credit deterioration in the aftermath of the Covid-19 pandemic.

The ECL charge in respect of loans and advances to customers for the financial year ended 31 December 2021 was not significant. Downward migrations within the corporate lending portfolio were effected to reflect cases where signs of financial difficulties became apparent. This resulted in a downward migration of certain corporate borrowers to Stage 2 or Stage 3 reflecting the identification of SICR or UTP events respectively. However, the ECL impact arising from such migrations was not significant in view of the high level of collateral available in respect of downgraded borrowers. In addition, write-offs amounting to €123,970 were effected

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.5 Reconciliation of changes in gross carrying amount and allowances for ECL (continued)

during the financial year ended 31 December 2021.

The allowance for ECL in respect of factored receivables as at 31 December 2022 increased compared to the prior year, resulting in an ECL charge for the financial year ended 31 December 2022 amounting to €129,575. This was primarily driven by the growth in the size of the factored receivables portfolio, which increased by €23.4 million during the financial year ended 31 December 2022.

Improvements to the Bank's ECL methodology during the financial year ended 31 December 2021 resulted in a downward migration of borrowers from Stage 1 to Stages 2 or 3 within the bills of exchange factoring portfolio. Notwithstanding that, the impact on the ECL in respect of these borrowers was immaterial due to the fact that, as described in more detail in section 4.3.2.3, the LGD calculation takes into consideration the cash collateral pledged by factoring clients to cover potential losses from factored bills of exchange.

Specifically in respect of the invoice factoring portfolio, the Bank reviewed long outstanding exposures as at 31 December 2022 in order to assess their recoverability, resulting in write-offs amounting to €235,513 (2021: €321,137).

The following tables provide a reconciliation of the gross carrying amount and credit loss allowances relating to loans and advances to customers and factored receivables. A full reconciliation of changes in expected credit losses and other credit impairment charges is presented in Note 9 of the financial statements.

	Stage 1		Stage 2		Stage 3		Total	
Loans and advances to customers	**Gross carrying amount €**	**Allowance for ECL €**	**Gross carrying amount €**	**Allowance for ECL €**	**Gross carrying amount €**	**Allowance for ECL €**	**Gross carrying amount €**	**Allowance for ECL €**
At 1 January 2022	**127,052,013**	**(263,165)**	**3,172,018**	**(1,699)**	**1,474,296**	**(64,122)**	**131,698,327**	**(328,986)**
New and further lending	**56,625,161**	**(344,828)**	**-**	**-**	**40,143**	**(40,143)**	**56,665,304**	**(384,971)**
Repayments and disposals	**(25,630,773)**	**62,505**	**(399,420)**	**500**	**(1,144,073)**	**26,190**	**(27,174,266)**	**89,195**
Transfers of financial instruments								
Stage 1 to Stage 2	**(366,298)**	**23,794**	**366,298**	**(23,794)**	**-**	**-**	**-**	**-**
Stage 1 to Stage 3	**-**	**-**	**(1,657,886)**	**1,177**	**1,657,886**	**(1,177)**	**-**	**-**
Net remeasurement of ECL arising from stage transfers and changes in risk parameters	**-**	**(200,963)**	**-**	**1,614**	**-**	**(35,972)**	**-**	**(235,321)**
Amounts written off	**-**	**-**	**-**	**-**	**(26,392)**	**26,392**	**(26,392)**	**26,392**
At 31 December 2022	**157,680,103**	**(722,657)**	**1,481,010**	**(22,202)**	**2,001,860**	**(88,832)**	**161,162,973**	**(833,691)**
Total income statement charge for the year								**(504,705)**

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.5 Reconciliation of changes in gross carrying amount and allowances for ECL (continued)

	Stage 1		Stage 2		Stage 3		Total	
Loans and advances to customers	**Gross carrying amount €**	**Allowance for ECL €**	**Gross carrying amount €**	**Allowance for ECL €**	**Gross carrying amount €**	**Allowance for ECL €**	**Gross carrying amount €**	**Allowance for ECL €**
At 1 January 2021	121,768,023	(212,190)	-	-	167,520	(167,520)	121,935,543	(379,710)
New and further lending*	37,709,028	(64,809)	1,622,414	-	97,692	(7,382)	39,429,134	(72,191)
Repayments and disposals	(29,168,664)	(642)	(373,716)	-	-	108,745	(29,542,380)	108,103
Transfers of financial instruments								
Stage 1 to Stage 2	(1,923,320)	1,159	1,923,320	(1,159)	-	-	-	-
Stage 1 to Stage 3	(1,333,054)	2,013	-	-	1,333,054	(2,013)	-	-
Net remeasurement of ECL arising from stage transfers and changes in risk parameters	-	11,304	-	(540)	-	(119,922)	-	(109,158)
Amounts written off	-	-	-	-	(123,970)	123,970	(123,970)	123,970
At 31 December 2021	127,052,013	(263,165)	3,172,018	(1,699)	1,474,296	(64,122)	131,698,327	(328,986)
Total income statement charge for the year								50,724

* *New and further lending classified within Stage 2 in the table above represents exposures originated under the terms of the MDB CGS during the financial year ended 31 December 2021 and subsequently migrated to Stage 2 on the basis of identified SICR events triggered by the sustained impact of the COVID-19 pandemic.*

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.5 Reconciliation of changes in gross carrying amount and allowances for ECL (continued)

	Stage 1		Stage 2		Stage 3		Total	
Factored receivables	Gross carrying amount €	Allowance for ECL €	Gross carrying amount €	Allowance for ECL €	Gross carrying amount €	Allowance for ECL €	Gross carrying amount €	Allowance for ECL €
At 1 January 2022	**55,526,948**	**(93,303)**	**26,530,945**	**-**	**13,769,754**	**(682,510)**	**95,827,647**	**(775,813)**
New and further lending*	**35,134,754**	**(86,734)**	**15,252,579**	**(24,628)**	**4,865,367**	**(484,346)**	**55,252,700**	**(595,708)**
Repayments and disposals	**(20,756,871)**	**32,337**	**(5,367,407)**	**18,203**	**(5,451,444)**	**336,503**	**(31,575,722)**	**387,043**
Transfers of financial instruments								
Stage 1 to Stage 2	**(5,699,245)**	**3,055**	**5,699,245**	**(3,055)**	**-**	**-**	**-**	**-**
Stage 1 to Stage 3	**(2,428,423)**	**1,259**	**-**	**-**	**2,428,423**	**(1,259)**	**-**	**-**
Stage 2 to Stage 1	**6,123,100**	**-**	**(6,123,100)**	**-**	**-**	**-**	**-**	**-**
Stage 2 to Stage 3	**-**	**-**	**(7,813,974)**	**-**	**7,813,974**	**-**	**-**	**-**
Stage 3 to Stage 1	**2,490,227**	**-**	**-**	**-**	**(2,490,227)**	**-**	**-**	**-**
Stage 3 to Stage 2	**-**	**-**	**963,500**	**-**	**(963,500)**	**-**	**-**	**-**
Net remeasurement of ECL arising from stage transfers and changes in risk parameters	**-**	**(26,782)**	**-**	**(41,911)**	**-**	**(22,014)**	**-**	**(90,707)**
Amounts written off	**(65,716)**	**-**	**-**	**-**	**(169,797)**	**169,797**	**(235,513)**	**169,797**
At 31 December 2022	**70,324,774**	**(170,168)**	**29,141,788**	**(51,391)**	**19,802,550**	**(683,829)**	**119,269,112**	**(905,388)**
Total income statement charge for the year								**(129,575)**

	Stage 1		Stage 2		Stage 3		Total	
Factored receivables	Gross carrying amount €	Allowance for ECL €	Gross carrying amount €	Allowance for ECL €	Gross carrying amount €	Allowance for ECL €	Gross carrying amount €	Allowance for ECL €
At 1 January 2021	98,950,941	(84,166)	134,426	-	871,727	(717,320)	99,957,094	(801,486)
New and further lending*	31,498,819	(33,920)	6,835,423	-	2,363,495	(89,067)	40,697,737	(112,987)
Repayments and disposals	(37,741,056)	9,596	(6,204,935)	-	(550,056)	360,636	(44,496,047)	370,232
Transfers of financial instruments								
Stage 1 to Stage 2	(25,766,031)	-	25,766,031	-	-	-	-	-
Stage 1 to Stage 3	(11,414,574)	4,078	-	-	11,414,574	(4,078)	-	-
Net remeasurement of ECL arising from stage transfers and changes in risk parameters	-	11,089	-	-	-	(562,667)	-	(551,578)
Amounts written off	(1,151)	20	-	-	(329,986)	329,986	(331,137)	320,006
At 31 December 2021	55,526,948	(93,303)	26,530,945	-	13,769,754	(682,510)	95,827,647	(775,813)
Total income statement charge for the year								(25,673)

** New and further lending classified within Stages 2 and 3 in the tables above represents exposures originated during the financial years ended 31 December 2022 and 31 December 2021, and migrated to Stages 2 and 3 on the basis of missed repayments.*

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.6 Renegotiation of financial instruments and forbearance

The contractual terms of a loan may be modified for several reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. Where terms have been modified, an existing exposure may be derecognised if the modification is deemed to be substantial, with the renegotiated instrument being recognised as a new instrument measured at the fair value as at the date of modification and allocated to Stage 1 (assuming it is not credit-impaired at that time).

When the terms of an instrument are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:
- the residual lifetime PD at the reporting date based on the modified terms; with
- the residual lifetime PD estimated based on data on initial recognition and the original contractual terms.

The Bank has aligned its policies with the European Securities and Markets Authority ("ESMA") Public Statement on the Treatment of Forbearance Practices in IFRS Financial Statements of Financial Institutions. Under certain circumstances, the Bank may renegotiate the terms and conditions of a loan in response to actual or perceived financial difficulties of a customer. Renegotiations of exposures to customers in financial difficulties (referred to as 'forbearance activities') are designed to maximise collection opportunities and minimise the risk of default. Under the Bank'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 maturity extensions, changes to the timing of interest payments, and amendments to the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. The Credit Committee regularly reviews reports on forbearance activities.

For financial assets modified as part of the Bank's forbearance policy, the Bank assesses whether the modification has improved or restored the Bank's ability to collect interest and principal and the probability of default in view of previous experience of similar forbearance activity. As part of this process, the Bank evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and may constitute evidence that an exposure is credit-impaired. A renegotiated loan is typically presented as credit-impaired when there has been a change in contractual cash flows as a result of a concession which the lender would otherwise not consider and it is probable that, without the concession, the borrower would be unable to meet contractual payment obligations in full. Accordingly, this will represent a significant concern regarding the borrower's ability to meet contractual payments, and the loan will be classified as credit-impaired, unless the concession granted is insignificant.

Renegotiated loans are classified as non-credit impaired where the renegotiation has resulted from significant concern about a borrower's ability to meet contractual payment terms but contractual cash flows are expected to be collected in full following the renegotiation and no other unlikely-to-pay indicators are evident.

In the event that a forborne exposure is deemed to be credit-impaired, the renegotiated loan will continue to be disclosed as credit-impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, and there are no other indicators of impairment. In this respect, a customer needs to demonstrate consistently good payment behaviour over a period before the exposure is no longer considered to be credit-impaired.

As at 31 December 2022 and 2021, there were no forborne exposures within the factored receivables portfolio. As at 31 December 2022, forborne loans and advances to customers comprised exposures with two borrowers (2021: one borrower), operating within the wholesale and retail trade industry. The carrying amount in respect of

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.6 Renegotiation of financial instruments and forbearance (continued)

these exposures, which are classified within Stage 3 as at 31 December 2022, is €1,219,230 (2021: €1,425,193). Credit loss allowances in respect of these exposures amount to €2,838 as at 31 December 2022 (2021: nil).

Interest income recognised during the financial year ended 31 December 2022 in respect of forborne exposures amounted to €136,576 (2021: €60,934).

The movement in the carrying amount of forborne loans and advances, before impairment allowances, is analysed below. Exposures eligible for a general payment moratorium are not considered to be forborne loans and are therefore not included in the table below.

	Forborne exposures	
	2022 **€**	2021 €
At 1 January	**1,425,193**	-
Loans to which forbearance measures have been extended during the year	**612,671**	1,368,266
(Decrease)/increase in exposure amount	**(818,634)**	56,927
At 31 December	**1,219,230**	1,425,193

Information on loans and advances subject to CBM compliant moratoria

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'). 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 financial difficulties prior to the pandemic.

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.

During the financial year ended 31 December 2022, extensions were made to one borrower operating within the wholesale and retail trade industry, which was subject to a general payment moratorium as at 31 December 2021. In addition, as at 31 December 2022, the Bank granted new moratoria to a borrower operating within the information technology industry as established within Directive No. 18 and the EBA Guidelines during the financial year ended 31 December 2022. In view of the forbearance allowance granted by the Bank, both exposures have been classified as 'doubtful' and treated as Stage 3 exposures in line with the credit policy of the Bank.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.7 Analysis of collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Bank has internal policies on the acceptability of specific classes of collateral or credit risk mitigation.

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

Loans and advances to customers

The Bank holds collateral against loans and advances to customers in the form of pledges over deposits held with the Bank, charges over real estate and corporate receivables. In response to the Covid-19 pandemic, the Bank provided support to its customers by offering loans originated in terms of the Malta Development Bank ("MDB") Covid-19 Guarantee Scheme ("CGS"). In this respect, up to 90% of such exposures are guaranteed by the Government of Malta, with the guarantee amount capped to 50% of all MDB CGS exposures originated by the Bank. The following is an analysis of the extendible value of the collateral (capped at the carrying amount of the loan) held by the Bank against exposures of loans and advances to customers:

	Carrying amounts	
	2022	2021
	€	€
Loans and advances to customers	**160,329,282**	131,369,341
Of which secured by:		
Real estate	**72,959,337**	31,590,896
Cash deposits held with the Bank	**36,757,690**	33,343,198
MDB CGS guarantee	**19,256,234**	25,815,046
Bills of exchange with recourse	**13,699,381**	9,872,005
Assignment of receivables	**5,018,618**	15,721,059
Pledges on life insurance policies	**462,572**	-
Total carrying amount secured by collateral	**148,153,832**	116,342,204
Residual unsecured exposure amounts	**12,175,450**	15,027,137
Allowance for ECL	**(833,691)**	(328,986)

During 2020, the Bank had confirmed its participation in the MDB CGS, 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 2022, gross loans subject to the MDB CGS amounted to €19,256,234 (2021: €25,815,046), of which a maximum of €9,628,117 (2021: €12,907,523) is considered guaranteed. As at 31 December 2022, gross loans originated under this scheme classified as Stage 1 and Stage 2 amounted to €16,364,488 (2021: €22,576,540) and €1,483,156 (2021: €3,135,998) respectively. As at 31 December 2022, loans originated under this scheme classified in Stage 3 amounted to €1,408,590 (2021: €102,508). The allowance for ECL in respect of the corresponding loans classified as Stage 1, Stage 2 and Stage 3 amounted to €17,116 (2021: €9,959), €22,202 (2021: €3,990) and €50,900 (2021: €32) respectively.

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.7 Analysis of collateral (continued)

Factored receivables

Factored receivables comprise bills of exchange and invoices factored on a no-recourse basis. The former sub-portfolio is secured by the motor vehicles being financed, with a pledge on cash deposits placed by factoring clients and held with the Bank also providing coverage on a first loss basis. The value of motor vehicles held as collateral in respect of factored bills of exchange as at 31 December 2022 and 2021, estimated by reference to the depreciated value of the motor vehicle to capture the loss in value through use, is presented in the table below.

	2022	2021
	€	€
Type of collateral		
Motor vehicles	**73,786,202**	66,535,568

Invoice factoring facilities are secured by credit insurance from a foreign third party underwriter providing insurance cover in respect of losses up to 95% of each eligible invoice.

Collateral held in respect of credit-impaired financial assets

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

	As at 31 December 2022			
	Gross carrying amount	**Allowance for ECL**	**Carrying amount**	**Extendible value of collateral held**
	€	**€**	**€**	**€**
Loans and advances to customers				
Overdrafts	**108,722**	**(39,134)**	**69,588**	**101,205**
Fixed term loans	**1,893,138**	**(49,698)**	**1,843,440**	**3,081,795**
Factored receivables				
Bills of exchange factoring	**16,698,406**	**-**	**16,698,406**	**15,373,954**
Invoice factoring	**3,104,144**	**(683,829)**	**2,420,315**	**-**
	21,804,410	**(772,661)**	**21,031,749**	**18,556,954**

	As at 31 December 2021			
	Gross carrying amount	**Allowance for ECL**	**Carrying amount**	**Extendible value of collateral held**
	€	**€**	**€**	**€**
Loans and advances to customers				
Overdrafts	74,740	(25,105)	49,635	103,982
Fixed term loans	1,399,556	(39,017)	1,360,539	2,982,018
Factored receivables				
Bills of exchange factoring	12,710,374	-	12,710,374	10,679,121
Invoice factoring	1,059,380	(682,510)	376,870	-
	15,244,050	(746,632)	14,497,418	13,765,121

The LTV ratio in respect of credit-impaired loans and advances to customers as at 31 December 2022 is

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.7 Analysis of collateral (continued)

63% (2021: 48%). As at 31 December 2022, credit-impaired loans and advances to customers comprise two exposures with a carrying amount of €1,219,714 classified as forborne stage 3 exposures and another two exposures with a carrying amount of €765,350 classified as non-forborne stage 3 exposures. These exposures are secured by commercial and residential real estate, with the exception of one forborne Stage 3 exposure which is secured by the MDB CGS guarantee and cash collateral. As at 31 December 2021, credit-impaired loans and advances to customers comprise one exposure with a carrying amount of €1,425,198 classified as a forborne stage 3 exposure, secured by commercial and residential real estate.

Credit-impaired invoice factoring facilities are secured by credit insurance cover procured from third party insurers up to 95% of credit losses in respect of each insured exposure.

No collateral is held in respect of financial investments and loans and advances to banks.

4.3.8 Write-off policy

The Bank writes off a loan, security and/or factored receivable balances (and any related credit loss allowances) when management determines that the loan, security and/or factored receivable is uncollectible. This determination is reached after considering information such as occurrence of significant changes in the borrower's/issuer's financial position such that the borrower/issuer can no longer pay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. During the current year, amounts receivable of €261,905 (2021: €445,107) were written off by the Bank.

4.3.9 Settlement risk

'Settlement risk' is the risk of loss due to the failure of an entity to honour its obligations to deliver cash, securities or other assets as contractually agreed. The Bank's activities do not expose it to significant settlement risk.

4.3.10 Industry concentration

The following table analyses the Bank's loans and advances to customers and factored receivables by business segment:

	2022		2021	
	€	**%**	€	%
Accommodation and food services	**2,520,656**	**1%**	2,596,576	1%
Construction and real estate activities	**53,811,039**	**19%**	43,408,653	19%
Households and individuals	**72,954,247**	**26%**	57,909,264	25%
Manufacturing	**12,127,295**	**4%**	10,387,443	5%
Services	**80,124,280**	**29%**	61,115,298	27%
Transportation	**8,578,125**	**3%**	8,349,363	4%
Wholesale and retail trade	**43,982,936**	**16%**	40,002,795	18%
Other Sectors	**4,594,428**	**2%**	2,651,783	1%
	278,693,006	**100%**	226,421,175	100%

The following table analyses the Bank's investment portfolio by business segment:

4. Financial risk management and review (continued)

4.3 Credit risk (continued)

4.3.10 Industry concentration (continued)

	2022		2021	
	€	**%**	€	%
Sovereign debt	**59,810,847**	**65%**	74,066,906	63%
Local corporate bonds:				
- Real estate	**12,828,010**	**14%**	5,508,875	5%
- Financial services	**5,324,241**	**6%**	2,446,950	2%
- Tourism	**3,828,382**	**4%**	4,005,194	3%
- Telecommunications	**3,641,946**	**4%**	4,169,766	4%
- Other	**5,539,203**	**6%**	6,533,299	6%
Equity investments	**578,298**	**1%**	20,549,722	17%
	91,550,927	**100%**	117,280,712	100%

4.3.11 Concentration risk

In addition to industry concentration mentioned in Note 4.3.10, the Bank monitors concentration of credit risk by counterparty and by geographic location. An analysis of credit risk concentration (net of credit loss allowances) is shown below.

	Loans and advances to customers		**Factored receivables**		**Loans and advances to banks**		**Financial investments**	
	2022	2021	**2022**	2021	**2022**	2021	**2022**	2021
	€	€	**€**	€	**€**	€	**€**	€
Carrying amount	**160,329,282**	131,369,341	**118,363,724**	95,051,834	**10,214,993**	25,420,282	**91,550,927**	117,280,712
Concentration by counterparty								
Corporates	**152,530,156**	130,180,000	**51,952,703**	36,673,177	**-**	-	**26,019,447**	20,217,134
Private individuals	**7,799,126**	1,189,341	**65,649,574**	57,559,639	**-**	-	**-**	-
Sovereign	**-**	-	**761,447**	819,018	**-**	-	**59,810,847**	74,066,906
Banks and financial services	**-**	-	**-**	-	**10,214,993**	25,420,282	**5,720,633**	22,996,672
Concentration by location								
Europe:								
- Malta	**116,514,907**	92,603,090	**82,660,500**	70,699,216	**4,913,366**	4,448,968	**89,526,389**	94,432,940
- Belgium	**35,874,194**	29,844,346	**31,201,798**	23,038,656	**5,221,415**	19,250,048	**30,275**	30,275
- France	**3,500,000**	3,500,000	**832,657**	757,115	**-**	-	**42,313**	20,519,447
- Other	**4,439,340**	4,376,378	**3,668,769**	556,847	**80,212**	1,721,266	**1,951,950**	2,298,050
USA	**841**	1,045,527	**-**	-	**-**	-	**-**	-

Concentration by location for loans and advances to customers and banks and investment securities is measured based on the location of the borrower or issuer of the security.

4.4 Market risk

4. Financial risk management and review (continued)

Market risk comprises the risk of losses in value caused by unexpected changes in market prices (interest rates, equity prices, foreign exchange rates and credit spreads) before the affected positions can be closed out or hedged.

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.
- Investment price risk, which is the risk of losses because of changes in investments prices.

4.4.1 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 re-price 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 dates on assets and liabilities. However, the Bank seeks to maximise the spread over the cost of capital by investing funds in a portfolio of securities and loans and receivables with a longer tenure than the liabilities (therefore carrying a negative maturity gap position) through the efficient management of shorter-term liabilities over the medium to longer term. The table below summarises re-pricing mismatches at reporting date together with the effective interest rates where applicable.

2022	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 €
Assets						
Balances with Central Bank of Malta	17,598,287	2.50%	17,598,287	-	-	-
Loans and advances to banks	10,214,993	0.30%	10,214,993	-	-	-
Financial investments:						
- Debt securities measured at FVOCI	90,972,629	1.84%	-	2,000,000	48,587,973	40,384,656
Factored receivables	118,363,724	5.96%	41,370,591	6,082,484	63,090,738	7,819,911
Loans and advances to customers	160,329,282	4.22%	92,543,392	38,784,583	28,755,057	246,250
Total assets	397,478,915		161,727,263	46,867,067	140,433,768	48,450,817
Liabilities						
Amounts owed to institutions	40,000,000	0.77%	40,000,000	-	-	-
Amounts owed to banks	275,815	0.00%	275,815	-	-	-
Amounts owed to customers	335,660,870	1.25%	134,800,316	103,102,902	78,312,950	19,444,702
Debt securities in issue	16,820,322	4.91%	-	-	3,174,653	13,645,669
Total liabilities	392,757,007		175,076,131	103,102,902	81,487,603	33,090,371
Interest repricing gap			(13,348,868)	(56,235,835)	58,946,165	15,360,446
Cumulative gap			(13,348,868)	(69,584,703)	(10,638,538)	4,721,908

4. Financial risk management and review (continued)

4.4 Market risk (continued)

4.4.1 Interest rate risk (continued)

2021	Carrying amount €	Average effective interest rate %	Less than 3 months €	Between 3 months and 1 year €	Between 1 year and 5 years €	More than 5 years €
Assets						
Balances with Central Bank of Malta	16,192,155	-0.50	16,192,155	-	-	-
Loans and advances to banks	25,420,282	-0.38	25,420,282	-	-	-
Financial investments:						
- Debt securities at FVOCI	96,730,990	1.63	-	-	26,290,338	70,440,652
Factored receivables	95,051,834	5.25	35,424,112	16,585,061	42,209,256	833,405
Loans and advances to customers	131,369,341	3.57	60,168,735	37,378,400	31,580,767	2,241,439
Total assets	364,764,602		137,205,284	53,963,461	100,080,361	73,515,496
Liabilities						
Amounts owed to institutions	55,000,000	-0.25	35,000,000	10,000,000	10,000,000	-
Amounts owed to banks	274,715	0.10	274,715	-	-	-
Amounts owed to customers	297,780,509	1.09	127,542,936	61,767,353	88,307,388	20,162,832
Debt securities in issue	11,940,167	4.52	-	-	11,940,167	-
Total liabilities	364,995,391		162,817,651	71,767,353	110,247,555	20,162,832
Interest repricing gap			(25,612,367)	(17,803,892)	(10,167,194)	53,352,664
Cumulative gap			(25,612,367)	(43,416,259)	(53,583,453)	(230,789)

4. Financial risk management and review (continued)

4.4 Market risk (continued)

4.4.1 Interest rate risk (continued)

4.4.1.1 Interest rate profile

The interest rate profile of the Bank's interest-bearing financial instruments as at 31 December 2022 and 2021 is presented below:

	2022		2021	
	€		€	
	Fixed	**Variable**	Fixed	Variable
Interest-earning assets				
Financial investments – debt securities	**90,972,629**	**-**	96,730,990	-
Factored receivables:				
- Invoice factoring	**41,822,368**	**-**	28,516,566	-
- Bills of exchange factoring	**76,541,356**	**-**	66,535,268	-
Loans and advances to customers				
- Corporate	**50,633,347**	**103,806,362**	75,772,648	55,596,693
- Retail	**-**	**5,889,573**	-	-
Balances with Central Bank of Malta and cash	**-**	**17,598,287**	-	16,192,155
Loans and advances to banks	**-**	**10,214,993**	-	25,420,282
	259,969,700	**137,509,215**	267,555,472	97,209,130
Interest-bearing liabilities				
Amounts owed to institutions	(40,000,000)	-	(55,000,000)	-
Amounts owed to customers	(260,658,694)	(75,002,176)	(229,305,887)	(68,474,622)
Debt securities in issue	(16,820,322)	-	(11,940,167)	-
Amounts owed to banks	-	(275,815)	-	(274,715)
	(317,479,016)	**(75,277,991)**	(296,246,054)	(68,749,337)

4.4.1.2 Fair value sensitivity analysis for fixed rate instruments

Financial instruments issued at fixed interest rates potentially expose the Bank to fair value interest rate risk. Balances with Central Bank of Malta, loans and advances to customers and to banks, amounts owed to Central Bank of Malta, customers and banks, and debt securities in issue are measured at amortised cost and are therefore not subject to fair value interest rate risk.

In this respect, the fair value sensitivity for fixed rate instruments is only performed in respect of debt financial investments measured at FVOCI. An increase of 250 basis points (2021: 50 basis points) in the yield to maturity of each respective debt security would lead to a decrease in value of debt financial investments measured at FVOCI amounting to €13,506,468 (2021: €2,835,263). Likewise, a decrease of 250 basis points (2021: 50 basis points) in interest rates would lead to an increase in value of debt financial investments measured at FVOCI amounting to €14,204,309 (2021: €2,835,263). Such increases or decreases in fair value would be recognised in other comprehensive income and in equity.

4. Financial risk management and review (continued)

4.4 Market risk (continued)

4.4.1 Interest rate risk (continued)

4.4.1.3 Cash flow sensitivity analysis for variable rate instruments

The Bank is exposed to cash flow interest rate risk principally in respect of financial assets and liabilities subject to variable interest rates. Taking cognisance of the nature of the Bank's financial assets and liabilities, a sensitivity analysis in respect of interest rate changes in relation to the Bank's variable rate financial assets is presented hereunder in line with the requirements emanating from IFRS 7.

The sensitivity of interest rate gaps to various interest rate scenarios is monitored by management. Standard scenarios that are considered on a quarterly basis include a 200-basis point (bp) parallel rise or fall in all the yield curves. An analysis of the Bank's sensitivity to an increase or decrease in market interest rates is presented below. This analysis assumes that all other variables, in particular exchange rates, remain constant.

	Impact on	
	Profit or loss	**Equity**
	€	**€**
2022		
+ 200 basis points	**(1,478,446)**	**(1,478,446)**
- 200 basis points	**1,478,446**	**1,478,446**
2021		
+ 50 basis points	(187,399)	(187,399)
- 50 basis points	187,399	187,399

4.4.2 Currency risk

Currency risk is the risk that the value of a financial instrument fluctuates due to changes in foreign exchange rates. The Bank holds and deals in foreign currency with the aim to service the foreign exchange buying and selling activity of its clients. The Bank does not speculate on its foreign exchange holdings. The Bank's foreign exchange exposure is mainly limited to the United States Dollar and Swiss Francs, originating from the Bank's corporate banking business. The Bank manages this risk by ensuring that its foreign currency denominated liabilities are matched to corresponding assets in the same currency.

Exposure to foreign currencies is maintained at minimum levels and within the prescribed limits set by the Bank's Board of Directors. In the scenario whereby all foreign currencies fluctuate upwards or downwards by 20% against the Euro, the carrying amounts of financial assets and liabilities would fluctuate upwards or downwards by €95,757 and €48,595 (2021: €115,807 and €46,042) respectively.

4. Financial risk management and review (continued)

4.4 Market risk (continued)

4.4.2 Currency risk (continued)

The following table provides an analysis of the financial assets and liabilities of the Bank into relevant currency groupings:

	2022			2021		
	Euro	Other currencies	Total	Euro	Other currencies	Total
	€	€	€	€	€	€
Financial assets						
Balances with Central Bank of Malta and cash	**17,598,287**	**-**	**17,598,287**	16,193,768	-	16,193,768
Loans and advances to banks	**9,743,873**	**471,120**	**10,214,993**	24,692,346	727,936	25,420,282
Financial investments:						
- Debt securities measured at FVOCI	**90,972,629**	**-**	**90,972,629**	96,730,990	-	96,730,990
Factored receivables	**118,356,423**	**7,301**	**118,363,724**	95,051,834	-	95,051,834
Loans and advances to customers	**160,328,441**	**841**	**160,329,282**	130,323,814	1,045,527	131,369,341
Other assets	**1,937,194**	**-**	**1,937,194**	1,335,715	-	1,335,715
	398,936,847	**479,262**	**399,416,109**	364,328,467	1,773,463	366,101,930
Financial liabilities						
Amounts owed to institutions	**40,000,000**	**-**	**40,000,000**	55,000,000	-	55,000,000
Amounts owed to banks	**275,815**	**-**	**275,815**	274,715	-	274,715
Amounts owed to customers	**335,417,698**	**243,172**	**335,660,870**	297,201,303	579,206	297,780,509
Debt securities in issue	**16,820,322**	**-**	**16,820,322**	11,940,167	-	11,940,167
Other liabilities	**4,759,914**	**-**	**4,759,914**	3,975,122	-	3,975,122
	397,273,749	**243,172**	**397,516,921**	368,391,307	579,206	368,970,513
Net currency position	**1,663,098**	**236,090**	**1,899,188**	(4,062,840)	1,194,257	(2,868,583)

As at 31 December 2022 and 2021, the Bank was not exposed to any significant currency risk in respect of off-balance sheet exposures. Balances under other currencies represent exposures predominantly to the US Dollar.

4.4.3 Investment price risk

The exposure of the Bank to this risk is not significant. Frequent management reviews are carried out to ensure high quality of the portfolio.

4. Financial risk management and review (continued)

4.5 Liquidity risk

Liquidity risk is the risk that the Bank's obligations to repay liabilities or fund new loans exceeds the Bank's ability to raise funds from either the liquidation of assets or the acceptance of new deposits. Liquidity risk arises primarily due to mismatches in the maturity profile of a bank's financial assets and liabilities, which exposes a bank to the risk that it might not be able to meet its liabilities as they become due or will have to do so at excessive cost. Liquidity risk may also be affected by the depth of the market in which the Bank operates.

Liquidity risk is divided into two categories:
- Market (product) liquidity risk: risk of losses arising from difficulties in accessing a product or market at the required time, price and volume.
- Funding liquidity risk: risk of losses arising from a timing mismatch in respect of the maturities of financial assets and liabilities, resulting in a risk that the Bank does not meet obligations when due or will have to raise funding at higher than normal rates.

The Bank's approach to managing liquidity risk is to ensure, as far as possible, that it always has sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation. The key elements of the Bank's liquidity strategy are as follows.

- Maintaining a diversified funding base consisting of customer deposits (both retail and corporate) and wholesale market deposits, whilst also maintaining contingency facilities.
- Carrying a portfolio of highly liquid assets, diversified by currency and maturity.
- Monitoring maturity mismatches, behavioural characteristics of the Bank's financial assets and financial liabilities, and the extent of asset encumbrance which might prevent financial assets from being used as collateral to obtain further funding.
- Stress testing of the Bank's liquidity position against various exposures and global, country-specific and Bank-specific events.

Liquidity policies and procedures are reviewed by internal audit. All liquidity policies are subject to review by the Asset and Liability Management Committee and the approval of the Board of Directors.

The Bank's liquidity and funding risk management framework employs two key measures to define, monitor and control the liquidity and funding risk:
- The Liquidity Coverage Ratio ("LCR"), which measures the Bank's level of High-Quality Liquid Assets ("HQLAs") against expected net cash outflows over a one-month period. This ratio is used to gauge the short-term resilience of the Bank's liquidity profile in terms of the requirements emanating from European Commission ('EC') Delegated Regulation 2015/61.
- The Net Stable Funding Ratio ("NSFR") is used to monitor the structural long-term funding position of the Bank. The NSFR requires institutions to maintain sufficient stable funding relative to required stable funding, and reflects a bank's long-term funding profile (funding with a term of more than a year). It is designed to complement the LCR.

4. Financial risk management and review (continued)

4.5 Liquidity risk (continued)

Details of the Bank's ratios at the reporting dates and during the reported periods are presented below:

	LCR		NSFR	
	2022	2021	**2022**	**2021**
As at 31 December	**725%**	1,320%	**134%**	164%
Average for the year	**1,584%**	2,525%	**161%**	163%
Maximum for the year	**3,081%**	3,634%	**179%**	166%
Minimum for the year	**454%**	1,090%	**134%**	158%

4.5.1 Contractual maturity ladder

The Bank also monitors the contractual maturity ladder, which provides insight into the extent to which the Bank relies on maturity transformation in respect of contractual cash flows. More precisely, the maturity ladder is used to determine the availability of liquid assets to meet liquidity gaps for diverse time horizons.

The following table provides an analysis of the financial assets and liabilities of the Bank into relevant remaining maturity groupings based on the ability of recovery or repayment:

At 31 December 2022	Less than 1 month €	Between 1 and 3 months €	Between 3 months and 1 year €	Between 1 and 5 years €	More than 5 years €	No maturity date €	Total €
Financial assets							
Balances with Central Bank of Malta	14,784,535	-	-	-	-	2,813,752	17,598,287
Loans and advances to banks	10,214,993	-	-	-	-	-	10,214,993
Financial investments:							
- Equity investments	-	-	-	-	-	578,298	578,298
- Debt securities	-	-	2,000,000	48,587,973	40,384,656	-	90,972,629
Factored receivables	25,008,507	16,362,084	6,082,484	63,090,738	7,819,911	-	118,363,724
Loans and advances to customers	16,981,755	8,611,573	38,614,529	65,947,309	30,174,116	-	160,329,282
Other assets	1,973,194	-	-	-	-	-	1,973,194
Total assets	68,962,984	24,973,657	46,697,013	177,626,020	78,378,683	3,392,050	400,030,407
Financial liabilities							
Amounts owed to institutions	10,000,000	30,000,000	-	-	-	-	40,000,000
Amounts owed to banks	275,815	-	-	-	-	-	275,815
Amounts owed to customers	89,702,291	42,492,871	104,342,245	79,658,759	19,464,704	-	335,660,870
Debt securities in issue	-	-	-	3,174,653	13,645,669	-	16,820,322
Other liabilities	4,759,914	-	-	-	-	-	4,759,914
Total liabilities	104,738,020	72,492,871	104,342,245	82,833,412	33,110,373	-	397,516,921
Liquidity gap	(35,775,036)	(47,519,214)	(57,645,232)	94,792,608	45,268,310	3,392,050	2,513,486
Cumulative gap	(35,775,036)	(83,294,250)	(140,939,482)	(46,146,874)	(878,564)	2,513,486	

4. Financial risk management and review (continued)

4.5.1 Contractual maturity ladder (continued)

At 31 December 2021	Less than 1 month €	Between 1 and 3 months €	Between 3 months and 1 year €	Between 1 and 5 years €	More than 5 years €	No maturity date €	Total €
Financial assets							
Balances with Central Bank of Malta	13,535,330	-	-	-	-	2,656,825	16,192,155
Loans and advances to banks	25,420,282	-	-	-	-	-	25,420,282
Financial investments:							
- Equity investments	-	-	-	-	-	20,549,722	20,549,722
- Debt securities	-	-	-	26,290,338	70,440,652	-	96,730,990
Factored receivables	20,220,035	15,204,077	16,585,061	42,209,256	833,405	-	95,051,834
Loans and advances to customers	9,513,793	9,734,192	22,602,524	72,081,834	17,436,998	-	131,369,341
Other assets	1,335,715	-	-	-	-	-	1,335,715
Total assets	70,025,155	24,938,269	39,187,585	140,581,428	88,711,055	23,206,547	386,650,039
Financial liabilities							
Amounts owed to institutions	-	35,000,000	10,000,000	10,000,000	-	-	55,000,000
Amounts owed to banks	274,715	-	-	-	-	-	274,715
Amounts owed to customers	80,933,275	43,496,995	61,998,441	91,153,354	20,198,444	-	297,780,509
Debt securities in issue	-	-	-	11,940,167	-	-	11,940,167
Other liabilities	3,975,122	-	-	-	-	-	3,975,122
Total liabilities	85,183,112	78,496,995	71,998,441	113,093,521	20,198,444	-	368,970,513
Liquidity gap	(15,157,957)	(53,558,726)	(32,810,856)	27,487,907	68,512,611	23,206,547	17,679,526
Cumulative gap	(15,157,957)	(68,716,683)	(101,527,539)	(74,039,632)	(5,527,021)	17,679,526	

Amounts owed to customers of €75,002,176 (2021: €68,449,774) as at 31 December 2022 are repayable on demand and included in the 'less than one month' bucket in the tables above. 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.

4.5.2 Cash flows payable by the Bank under financial liabilities by residual maturity

The table below shows a maturity analysis of undiscounted cash flows payable in respect of financial liabilities by residual contractual maturities of the instruments:

At 31 December 2022	Carrying amount €	Gross nominal outflow €	Repayable on demand €	Less than 3 months €	Between 3 months and 1 year €	Between 1 and 5 years €	More than 5 years €
Amounts owed to institutions	**40,000,000**	**(40,307,014)**	**-**	**(40,307,014)**	**-**	**-**	**-**
Amounts owed to banks	**275,815**	**(275,815)**	**(275,815)**	**-**	**-**	**-**	**-**
Amounts owed to customers	**335,660,870**	**(347,359,212)**	**(75,002,176)**	**(60,716,266)**	**(105,299,378)**	**(83,103,035)**	**(23,238,357)**
Debt securities in issue	**16,820,322**	**(24,616,110)**	**-**	**-**	**(843,370)**	**(6,272,740)**	**(17,500,000)**
Other liabilities	**4,759,914**	**(4,759,914)**	**-**	**(4,759,914)**	**-**	**-**	**-**
	397,516,921	**(417,318,065)**	**(75,277,991)**	**(105,783,194)**	**(106,142,748)**	**(89,375,775)**	**(40,738,357)**

4. Financial risk management and review (continued)

4.5 Liquidity risk (continued)

4.5.2 Cash flows payable by the Bank under financial liabilities by residual maturity (continued)

At 31 December 2021	Carrying amount €	Gross nominal outflow €	Repayable on demand €	Less than 3 months €	Between 3 months and 1 year €	Between 1 and 5 years €	More than 5 years €
Amounts owed to institutions	55,000,000	(54,857,843)	-	(34,911,062)	(9,974,589)	(9,972,192)	-
Amounts owed to banks	274,715	(274,715)	(274,715)	-	-	-	-
Amounts owed to customers	297,780,509	(307,149,714)	(68,449,774)	(51,560,478)	(70,239,049)	(95,166,586)	(21,733,827)
Debt securities in issue	11,940,167	(14,160,000)	-	-	(540,000)	(13,620,000)	-
Debt securities in issue	3,975,122	(3,975,122)	-	(3,975,122)	-	-	-
	368,970,513	(380,417,394)	(68,724,489)	(90,446,662)	(80,753,638)	(118,758,778)	(21,733,827)

4.6 Operational risk

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

Management of operational risk

The Bank's objective is to manage operational risk to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness. The Bank's operational risk management activities comprise actions to:

- Adopt policies, processes, and procedures to control and/or mitigate material operational risks.
- Identify and assess the operational risk inherent in all material products, activities, processes, and systems. Before new products, activities, processes, and systems are introduced or undertaken, the inherent operational risk is subject to adequate assessment.
- Monitor all potential operational risks and material exposures to losses.
- Monitor whether there is motive, means and opportunity within the overall control environment to commit fraudulent acts.
- Adopt contingency and business continuity plans to ensure the Bank's ability to operate on an ongoing basis and limit losses in the event of severe business disruption.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management. Periodic operational risk reports are submitted to the Bank's Audit and Risk Committee. A financial measurement of this risk is estimated by the Bank for the purpose of allocating risk capital using the Basic Indicator Approach under the Capital Requirements Directive rules. The capital requirement for operational risk under this method was calculated at €1,026,733 as at 31 December 2022 (2021: €960,383).

4. Financial risk management and review (continued)

4.7 Fair value measurement of financial instruments

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

(a) Valuation models

The Bank measures fair value using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements:

- Level 1: inputs that are quoted market prices (unadjusted) in active markets for identical instruments.
- Level 2: inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs that are not observable, and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Valuation techniques include net present value and discounted cash flow models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates.

Fair values reflect the credit risk of the instrument and include adjustments to take into account the credit risk of the counterparty as appropriate.

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

(b) Valuation framework

The Bank's financial assets measured at fair value comprise investments in Malta Government Stocks, corporate bonds listed on the Malta Stock Exchange, and collective investment schemes. Malta Government Stocks, corporate bonds and unquoted equity investments are classified as financial investments measured at FVOCI. Equity investments representing units in collective investment schemes are classified as financial investments measured at FVTPL. The Head of Finance and Treasury has overall responsibility for independently verifying the results of all fair value measurements.

(c) Financial instruments measured at fair value

The table below analyses financial instruments measured at fair value at the reporting date by fair value measurement categorisation within the fair value hierarchy. The amounts reflect the carrying amount recognised in the statement of financial position.

4. Financial risk management and review (continued)

4.7 Fair value measurement of financial instruments (continued)

	Level 1	Level 2	Level 3	Total
	€	€	€	€
31 December 2022				
Financial investments:				
- Debt securities	**88,972,629**	**-**	**2,000,000**	**90,972,629**
- Equity investments	**548,023**	**-**	**30,275**	**578,298**
	89,520,652	**-**	**2,030,275**	**91,550,927**
31 December 2021				
Financial investments:				
- Debt securities	96,730,990	-	-	96,730,990
- Equity investments	20,519,447	-	30,275	20,549,722
	117,250,437	-	30,275	117,280,712

Financial investments – Debt securities

This category of assets is carried at fair value, measured primarily by reference to quoted market prices as at 31 December 2022 and 2021.

Financial investments – Equity investments

The Bank has an interest in an open-ended investment fund as disclosed in Note 16.4, which is carried at fair value, determined by reference to the net asset value of the fund as at 31 December 2022 and 2021.

The Bank's exposure to unquoted equity investments is deemed immaterial as at 31 December 2022 and 2021.

No transfers of financial instruments between different levels of the fair value hierarchy have occurred during the financial years ended 31 December 2022 and 2021.

(d) Financial instruments not measured at fair value

Debt securities in issue

The fair value of the debt securities in issue as at 31 December 2022 amounted to €17,281,580 (2021: €12,360,000) whilst the carrying amount of these debt securities was €16,820,322 (2021: €11,940,167).

Balances with Central Bank of Malta, loans and advances to banks and factored receivables

These categories of assets are reported net of credit loss allowances to reflect the estimated recoverable amounts. Balances with Central Bank of Malta and loans and advances to banks re-price within 3 months, whilst factored receivables are relatively short-term in nature. The carrying amounts of these financial assets are therefore deemed to be a reasonable approximation of their fair value.

Loans and advances to customers

Loans and advances to customers are carried at amortised cost in the statement of financial position. The board considers the carrying amounts of these loans to be a reasonable estimate of their fair value in view of the relatively short periods to repricing or maturity from the end of the reporting periods.

4. Financial risk management and review (continued)

4.7 Fair value measurement of financial instruments (continued)

(d) Financial instruments not measured at fair value (continued)

Amounts owed to institutions

Amounts owed to institutions amounting to €40,000,000 (2021: €55,000,000) represent loans contracted in terms of the 'Eurosystem Monetary Policy Operations - Central Bank of Malta Directive No.8' and are carried at amortised cost. These amounts are secured by a pledge on a portion of the Bank's portfolio of investments in Malta Government Stocks as disclosed in Note 16.2. The fair value of these amounts is deemed to approximate the carrying amount in view of the short-term nature of the financial liability.

Amounts owed to customers

This category of liabilities is carried at amortised cost and amounts to €335,660,870 (2021: €297,780,509). The majority of the customer deposits reprice within one year or less and, in this respect, their carrying amount is deemed to be a reasonable approximation of their fair value.

Amounts owed to banks

This category of liabilities is carried at amortised cost and amounts to €275,815 (2021: €274,715). These liabilities are short-term in nature and, in this respect, their carrying amount is deemed to approximate their fair value.

Debt securities in issue

This category of liabilities is carried at amortised cost. The debt securities in issue with nominal value of €14.0 million and €3.2 million are quoted and the fair value has been determined by reference to the market price (Level 1), which was €100.00 and €103.00 respectively as at 31 December 2022 (2021: €103.00), resulting in a fair value of €14,000,000 and €3,281,580 (2021: €12,360,000).

(e) Non-financial instruments measured at fair value

The judgements and estimates made in determining the fair values of property classified within 'Property and equipment', which is recognised and measured at fair value in the statement of financial position are described hereunder.

The Bank engages external, independent and qualified valuers to determine the fair value of its properties at least every five years. At the end of each reporting period, the directors update their assessment of the fair value of each property, taking into account the most recent independent valuations and other market factors.

The Bank 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).

4. Financial risk management and review (continued)

4.7 Fair value measurement of financial instruments (continued)

(e) Non-financial instruments measured at fair value (continued)

The Bank's property, classified within 'Property and equipment', comprises the Bank's offices and other operational premises. All the recurring property fair value measurements at 31 December 2022 and 2021 use significant unobservable inputs and are accordingly categorised within Level 3 of the fair valuation hierarchy. The last independent valuation of these properties was performed as at 30 September 2022. During 2022, 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 €100,787 in the carrying values for the Bank. For all Bank properties, their current use equates to the highest and best use.

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 fair value hierarchy, is reflected in Note 19.1. The principal movements reflect changes in fair value, additions, disposals and depreciation charge for the years ended 31 December 2022 and 2021.

The external valuations of the Level 3 property have been performed using predominantly the traditional investment method of valuation based on the capitalised rentals approach. In view of the limited market information available, the valuations have been performed using unobservable inputs. In relation to the capitalised rentals approach, the significant unobservable inputs include:

- a capitalisation rate applied at 6% (2021: 6%) which is effectively the discount rate adjusted for anticipated growth; and
- the expected annual rental value ("ERV") taking into account the rental rate per square metre for comparable properties located in proximity to the Bank's property with adjustments for differences in the size, age, exact location and condition of the property. The assumed monthly rental rate per square metre is €23.24 (2021: €23.27).

Effectively, the capitalisation rate indicates the return the investor expects to receive through annual rental value.

4.8 Capital base

The Bank is a licensed credit institution and must therefore comply with the minimum capital requirements prescribed by the Capital Requirements Regulation. The Bank has adopted the Standardised Approach to calculate its capital requirements for credit risk and the Basic Indicator Approach for operational risk and foreign exchange risk in order to calculate the Pillar 1 minimum capital requirements

4.8.1 Capital management

The Bank is required to maintain sufficient capital to comply with regulatory capital requirements. The Bank's capital management processes ensure an efficient use of capital in relation to risk appetite as well as business development. The Bank's regulatory capital comprises Tier 1 capital and Tier 2 capital, which includes ordinary share capital, the capital contribution reserve, retained earnings, other reserves and subordinated debt. The Bank's regulatory capital also included Tier 2 capital

All financial instruments arising from the Bank's operations are categorised as banking book exposures, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and to exposures not recognised in the statement of financial position.

4. Financial risk management and review (continued)

4.8 Capital base (continued)

4.8.1 Capital management (continued)

In accordance with the common reporting framework (COREP) submissions, used by credit institutions for reporting to the supervisory authority under the Capital Requirements Directive (CRD), submitted by the Bank to the authority, the Bank has complied with all externally imposed capital requirements including the Common Equity Tier 1 ('CET1'), Tier 1 Capital ('T1'), Tier 2 Capital ('T2') and Capital Adequacy Ratio ('CAR') throughout the financial years ended 31 December 2022 and 2021. There have been no material changes in the Bank's management of capital during the respective financial years.

4.8.2 Calculation of minimum capital requirement and risk-weighted assets

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%.

On 18 May 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 3.50% 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 14%.

4. Financial risk management and review (continued)

4.8 Capital base (continued)

4.8.1 Capital management (continued)

The following is an analysis of the Bank's Capital Base in accordance with the CRD's requirements, as reported by the Bank in the COREP return:

	2022	2021
	€	€
Tier 1 capital		
Ordinary share capital	**29,000,000**	10,000,000
Capital contribution	**32,675**	17,032,675
Retained earnings	**916,452**	2,005,302
Property revaluation reserve	**2,977,302**	3,521,238
Fair value movement reserve	**(10,295,141)**	(612,547)
Other reserves	**72,782**	45,091
Deductions related to intangible assets	**(1,399,036)**	(1,774,370)
Total Tier 1 Capital	**21,305,034**	30,217,389
Subordinated debt	**14,000,000**	-
Total Tier 2 Capital	**14,000,000**	-
Total Own Funds	**35,305,034**	30,217,389

By reference to regulatory returns submitted to the MFSA in respect of the financial year ended 31 December 2022, as well as regulatory returns submitted to the MFSA up to the date of signing of these financial statements relating to reporting periods falling after 31 December 2022, the Bank is deemed to have met all minimum legal capital requirements until signing date.

Further information in respect of the Bank's capital ratios may be found in sections 3 and 4 of Appendix 1 - Pillar 3 disclosures as at 31 December 2022, which are subject to internal review by the Bank.

5 Net interest income

	Note	2022 €	2021 €
Interest income			
Factored receivables		**6,362,852**	4,989,116
Loans and advances to customers		**5,345,149**	4,567,305
Amounts owed to institutions		**28,194**	135,521
Financial investments measured at FVOCI		**1,738,480**	1,710,715
Amortisation of premium on financial investments measured at FVOCI	16.5	**(386,904)**	(698,100)
Total interest income		**13,087,771**	10,704,557
Interest expense			
On amounts owed to banks		**(290,730)**	(98,542)
On amounts owed to customers		**(4,197,297)**	(3,858,102)
On debt securities in issue		**(701,743)**	(540,000)
Amortisation of debt issuance costs	25	**(52,577)**	(17,089)
Loss on modification of debt securities	25	**(170,298)**	-
Total interest expense		**(5,412,645)**	(4,513,733)
Net interest income		**7,675,126**	6,190,824

6 Net fee and commission income

	2022 €	2021 €
Account maintenance and other bank charges	**182,419**	119,866
Fee and commission income	**182,419**	119,866
SWIFT and bank charges	**(126,507)**	(130,061)
Fee and commission expense	**(126,507)**	(130,061)
Net fee and commission income/(expense)	**55,912**	(10,195)

Performance obligations and revenue recognition policies

Fee and commission income from contracts with customers is measured based on the consideration specified in a contract with a customer. The Bank recognises revenue when it transfers control over a service to a customer.

The following table provides information about the nature and timing of the satisfaction of performance obligations in contracts

6. Net fee and commission income (continued)

with customers, including significant payment terms, and the related revenue recognition policies.

Type of service	Nature and timing of satisfaction of performance obligations, including significant payment terms	Revenue recognition under IFRS 15
Retail and corporate banking service	The Bank provides banking services to corporate customers, including the provision of credit facilities, foreign currency transactions, account maintenance and servicing fees. Transaction-based fees for foreign currency transactions and credit facilities are charged to the customer's account when the transaction takes place. Servicing fees are charged on a periodical basis and are based on fixed rates reviewed annually by the Bank. No fees are charged to the Bank's retail customer base.	Revenue from account maintenance and servicing fees is recognised over time as the services are provided. Revenue related to transactions is recognised at the point in time when the transaction takes place.

7. Net trading income

	2022	2021
	€	€
Net gains/(losses) on financial investments measured at FVTPL	**10,543**	(59,028)
Net gains from foreign exchange activities	**5,246**	90,196
	15,789	31,168

8. Other operating income

	2022	2021
	€	€
Other operating income	**101,325**	97,746

9. Changes in expected credit losses and other credit impairment charges

	2022	2021
	€	€
Changes in expected credit losses:		
Factored receivables	**(129,575)**	25,673
Loans and advances to customers	**(504,705)**	50,724
Debt financial investments measured at FVOCI	**(34,822)**	(11,860)
	(669,102)	64,537
Other credit impairment charges:		
Write-offs		
- Factored receivables	**(235,513)**	(330,006)
- Loans and advances to customers	**(26,392)**	(123,970)
Recoveries		
- Loans and advances to customers	**11,860**	3,747
	(250,045)	(450,229)
	(919,147)	(385,692)

10. Profit before tax

10.1 Profit before income tax is stated after fees, exclusive of VAT, charged by the Bank's statutory auditor in relation to the financial years ended 31 December 2022 and 2021 which comprise the following:

	2022	2021
	€	€
Auditors' remuneration – annual statutory audit	**90,000**	60,000
Other assurance services	**7,000**	4,500
Other non-assurance services	**2,000**	9,240

10.2 Personnel expenses incurred by the Bank during the respective financial years are analysed as follows:

	2022	2021
	€	€
Directors' fees	**145,000**	137,000
Staff costs:		
- wages, salaries and allowances	**2,222,340**	1,849,474
- defined contribution social security costs	**145,936**	116,816
	2,513,276	2,103,290

10. Profit before tax (continued)

10.3 The weekly average number of persons employed by the Bank during the respective financial years was as follows:

	2022	2021
Managerial	**8**	7
Supervisory and clerical	**57**	47
	65	54

10.4 Other expenses incurred by the Bank during the respective financial years are analysed as follows:

	2022 €	2021 €
Credit servicing fees	**508,534**	495,525
Depositor compensation scheme contributions	**395,931**	-
IT support and maintenance costs	**1,204,538**	1,351,039
Marketing expenses	**175,613**	129,374
Professional fees	**802,907**	457,408
Other expenses	**695,964**	165,291
	3,783,487	2,598,637

11. Income tax expense

11.1 Total income tax expense

	Note	2022 €	2021 €
Income Statement			
Current income tax – current year expense		**(215,197)**	(373,430)
Deferred tax credit	26	**318,784**	1,254
		103,587	(372,176)

11.2 The tax on profit and the result of accounting profit multiplied by the applicable tax rate in Malta of 35% are reconciled as follows:

	2022 €	2021 €
(Loss)/profit before income tax	**(387,806)**	820,157
Tax at the applicable tax rate of 35%	**135,732**	(287,055)
Tax effect of:		
- Non-deductible expenses	**(27,447)**	(106,298)
- Other differences	**(4,698)**	21,177
	103,587	(372,176)

12. Earnings per share

Earnings per share is calculated by dividing the profit or loss after tax attributable to ordinary shareholders of the Bank by the number of ordinary shares in issue and ranking equally for dividend during the year.

	Note	2022 €	2021 €
Income Statement			
Net profit attributable to equity holders of the Bank		**(284,219)**	447,981
Number of ordinary shares in issue	26	**58,000,000**	58,000,000
Earnings per share		**(0c49)**	0c77

The comparative information has been restated to reflect the bonus issue, share split and the capitalisation from the capital contribution reserve effected during the current financial year and the impact on the number of shares in issue, referred to in Note 28, retrospectively.

13. Classification of financial assets and financial liabilities

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments.

2022	Note	At FVTPL	FVOCI – debt instruments	FVOCI – equity instruments	Amortised cost	Total carrying amount
Balances with Central Bank of Malta and cash	14	-	-	-	**17,598,287**	**17,598,287**
Loans and advances to banks	15	-	-	-	**10,214,993**	**10,214,993**
Investment securities	16	**548,023**	**90,972,629**	**30,275**	-	**91,550,927**
Factored receivables	17	-	-	-	**118,363,724**	**118,363,724**
Loans and advances to customers	18	-	-	-	**160,329,282**	**160,329,282**
Other assets	29	-	-	-	**2,070,207**	**2,070,207**
Total financial assets		**548,023**	**90,972,629**	**30,275**	**308,576,493**	**400,127,420**
Amounts owed to institutions	22	-	-	-	**40,000,000**	**40,000,000**
Amounts owed to banks	23	-	-	-	**275,815**	**275,815**
Amounts owed to customers	24	-	-	-	**335,660,870**	**335,660,870**
Debt securities in issue	25	-	-	-	**16,820,322**	**16,820,322**
Other liabilities	27	-	-	-	**4,759,912**	**4,759,912**
Total financial liabilities		-	-	-	**397,516,919**	**397,516,919**

2021	Note	At FVTPL	FVOCI – debt instruments	FVOCI – equity instruments	Amortised cost	Total carrying amount
Balances with Central Bank of Malta and cash	14	-	-	-	16,193,768	16,193,768
Loans and advances to banks	15	-	-	-	25,420,282	25,420,282
Investment securities	16	20,519,447	96,730,990	30,275	-	117,280,712
Factored receivables	17	-	-	-	95,051,834	95,051,834
Loans and advances to customers	18	-	-	-	131,369,341	131,369,341
Other assets	21	-	-	-	1,335,715	1,335,715
Total financial assets		20,519,447	96,730,990	30,275	269,370,940	386,651,652
Amounts owed to institutions	22	-	-	-	55,000,000	55,000,000
Amounts owed to banks	23	-	-	-	274,715	274,715
Amounts owed to customers	24	-	-	-	297,780,509	297,780,509
Debt securities in issue	25	-	-	-	11,940,167	11,940,167
Other liabilities	27	-	-	-	3,975,122	3,975,122
Total financial liabilities		-	-	-	368,970,513	368,970,513

14. Balances with Central Bank of Malta and cash

	2022	2021
	€	€
Balances with Central Bank of Malta	**17,598,287**	16,192,155
Cash and items in transit	**-**	1,613
	17,598,287	16,193,768

Balances with the Central Bank of Malta comprise mandatory reserve deposits of €1,981,892 (2021: €1,368,657) and are not available for use in the Bank's day-to-day operations. During the current and prior years, the Bank has been compliant with the reserve deposit requirement. These balances also comprise an amount of €831,860 (2021: €1,288,168) pledged in favour of the Depositor Compensation Scheme. Credit loss allowances in respect of balances with the Central Bank of Malta are deemed to be negligible.

15. Loans and advances to banks

	2022	2021
	€	€
Repayable on call and at short notice	**10,214,993**	25,420,282

Credit loss allowances in respect of loans and advances to banks are deemed to be negligible.

16. Financial investments

16.1 Composition of investment portfolio

	2022	2021
	€	€
Debt securities measured at FVOCI	**90,972,629**	96,730,990
Equity investments designated at FVOCI	**30,275**	30,275
Equity investments measured at FVTPL	**548,023**	20,519,447
	91,550,927	117,280,712

16.2 Debt financial investments measured at FVOCI comprise:

	2022	2021
	€	€
Malta Government Stocks	**59,810,847**	74,066,906
Local corporate bonds listed on the Malta Stock Exchange	**31,161,782**	22,664,084
	90,972,629	96,730,990

At 31 December 2022, expected credit loss allowances in respect of debt securities measured at FVOCI amounted to €46,682 (2021: €11,860).

The Bank's holdings of debt financial investments measured at FVOCI represent securities quoted on the Malta Stock Exchange.

16. Financial investments (continued)

As at 31 December 2022, a portion of the Bank's investment in Malta Government Stocks with a fair value of €59,810,846 (2021: €58,128,816) was pledged in favour of the Central Bank of Malta as collateral held in respect of the Bank's participation in the ECB Pandemic Emergency Longer-Term Refinancing Operations ("PELTROs") amounting to €10,000,000 (2021: €55,000,000) and Targeted Longer-Term Refinancing Operations ("LTROs") amounting to €30,000,000 (2021: nil) as at that date.

16.3 Equity investments designated at FVOCI comprise:

	2022	2021
	€	€
Unquoted equity holding (Society for Worldwide Interbank Financial Telecommunications SCRL – SWIFT)	**30,275**	30,275

16.4 Equity investments measured at FVTPL comprise:

	2022	2021
	€	€
Collective investment schemes	**42,409**	20,519,447
Unrated financial investments	**505,614**	-
	548,023	20,519,447

Collective investment schemes represent holdings in investment-grade money market funds as part of the active liquidity management of the Bank. The position as of 31 December 2021 was liquidated during 2022 with the realized gains disclosed in the statement of profit or loss. Furthermore, the unrated financial investments disclosed above represent equity investments listed on the Malta Stock Exchange which are unrated by international credit rating agencies.

16.5 The table below summarises the movement in financial investments

	€
At 1 January 2022	**117,280,712**
Acquisitions	**40,740,036**
Redemptions and disposals	**(51,362,776)**
Amortisation of premium	**(386,904)**
Fair value movement	**(14,720,141)**
At 31 December 2022	**91,550,927**
At 1 January 2021	109,304,630
Acquisitions	85,996,927
Redemptions and disposals	(76,537,399)
Amortisation of premium	(698,100)
Fair value movement	(785,346)
At 31 December 2021	117,280,712

17. Factored receivables

	2022	2021
	€	€
Receivables factored on a non-recourse basis:		
- Invoice factoring	**42,611,756**	29,277,379
- Bills of exchange factoring	**76,657,356**	66,550,268
Allowance for ECL	**(905,388)**	(775,813)
	118,363,724	95,051,834

18. Loans and advances to customers

	Note	2022	2021
		€	€
Term loans and advances to third parties		**70,934,420**	61,091,191
Term loans and advances to related parties	32.3	**42,239,142**	36,442,579
Overdrafts		**47,989,411**	34,164,557
Allowance for ECL		**(833,691)**	(328,986)
		160,329,282	131,369,341

19. Property and equipment

19.1	Total	Premises and improvements	Computer hardware	Other equipment	Motor Vehicles
	€	€	€	€	€
Cost/revalued amount					
At 1 January 2021	13,931,521	12,415,047	739,224	106,624	670,626
Acquisitions	814,947	622,124	160,490	29,910	2,423
Premises revaluation	(31,610)	-	-	(31,610)	-
At 31 December 2021	14,714,858	13,037,171	899,714	104,924	673,049
At 1 January 2022	**14,714,858**	**13,037,171**	**899,714**	**104,924**	**673,049**
Acquisitions	**1,413,917**	**1,186,558**	**86,114**	**-**	**141,245**
Premises revaluation	**100,787**	**100,787**	**-**	**-**	**-**
Disposals	**(2,774,204)**	**(2,724,795)**	**-**	**-**	**(49,409)**
At 31 December 2022	**13,455,358**	**11,599,721**	**985,828**	**104,924**	**764,885**
Depreciation					
At 1 January 2021	1,937,072	651,107	598,623	90,695	596,647
Charge for the year	243,933	83,109	115,596	17,455	27,773
Depreciation released on disposals	(31,542)	-	-	(31,542)	-
At 31 December 2021	2,149,463	734,216	714,219	76,608	624,420
At 1 January 2022	**2,149,463**	**734,216**	**714,219**	**76,608**	**624,420**
Charge for the year	**149,201**	**77,820**	**49,781**	**5,998**	**15,602**
Depreciation released on revaluation/disposals	**(555,531)**	**(520,795)**	**-**		**(34,736)**
At 31 December 2022	**1,743,133**	**291,241**	**764,000**	**82,606**	**605,286**
Carrying amount					
At 1 January 2021	11,994,449	11,763,940	140,601	15,929	73,979
At 31 December 2021	12,565,395	12,302,955	185,495	28,316	48,629
At 31 December 2022	**11,712,225**	**11,308,480**	**221,828**	**22,318**	**159,599**

19.2 The carrying amount of premises and improvements that would have been included in the financial statements had these assets not been revalued (see Note 3.5) but had been carried at cost less depreciation would have been:

	2022	2021
	€	€
Cost	**8,372,372**	8,795,158
Accumulated depreciation	**(295,437)**	(430,678)
	8,076,935	8,364,480

19.3 As at 31 December 2022, commitments in respect of capital expenditure authorised and contracted for amounted to €666,000 (2021: €1,615,000). The bulk of this expenditure will be directed toward construction and refurbishment works at what will eventually become the Bank's main premises at Castille Square.

19. Property and equipment (continued)

19.4 Revaluation of premises

The Bank's premises are measured at revalued amount less accumulated depreciation. The revaluation amount is determined based on open market values provided periodically, at least every five years, by independent valuers. The Bank occupies almost the full complement of two adjacent and prestigious houses – Nos. 53 and 58 in East Street, Valletta, close to the 'Lower Barrakka' Gardens and with views of the Grand Harbour and the Three Cities. The buildings date back to the eighteenth century and are structurally sound and complete of finishes of a very high standard. In 2017, the Bank acquired new premises at 4, Castille Place, and as at 31 December 2022, was in the process of extensive improvements and refurbishment to the building.

Following an Extraordinary General Meeting held on 24 November 2022 and as disclosed in Company Announcements IZB103 and IZB104, during 2022, the Bank transferred to a related party, Barrakka Properties Limited, a private limited liability company registered under the laws of Malta, bearing company registration number C 102595 and having its registered office at 53/58 East Street, Valletta VLT 1251, Malta the following properties: , (i) Apartment 1 and Apartment 2 forming part of the block of buildings numbered 65 and situated in East Street Valletta, Malta and (ii) the properties numbered 66/67, 82, 83/84/94/95, 98/99 in East Street Valletta, Malta with a total net carrying amount of €2,204,000 for a cash consideration of €2,204,000.

Information in respect of the fair value measurement of the properties measured at revalued amount is disclosed in Note 4.7.

20. Intangible assets

	Computer software €
Cost	
At 1 January 2021	4,252,154
Acquisitions	824,508
At 31 December 2021	5,076,662
At 1 January 2022	**5,076,662**
Acquisitions	**1,064,771**
At 31 December 2022	**6,141,433**
Amortisation	
At 1 January 2021	2,702,063
Charge for the year	600,229
At 31 December 2021	3,302,292
At 1 January 2022	**3,302,292**
Charge for the year	**863,548**
At 31 December 2022	**4,165,840**
Carrying amount	
At 1 January 2021	1,550,091
At 31 December 2021	1,774,370
At 31 December 2022	**1,975,593**

As at 31 December 2022, commitments in respect of capital expenditure authorised and contracted for amounted to €1,179,000 (2021: €1,400,000). The bulk of this expenditure will be directed toward the procurement and development of the core banking system.

21. Other assets

	2022	2021
	€	€
Accrued interest	**1,437,194**	1,335,715
Prepayments	**1,244,617**	636,005
Other receivables	**500,000**	-
	3,181,811	1,971,720

22. Amounts owed to institutions

The Bank participates in the ECB LTROs and PELTROs. In this respect, a portion of the Malta Government Stocks held by the Bank as at 31 December 2022 and 2021 (see Note 16) were pledged in favour of the Central Bank of Malta as collateral in respect of the Bank's participation in the LTROs and PELTROs . As at 31 December 2022, LTROs amounted to €30,000,000 (2021: nil) and PELTROs amounted to €10,0000 (2021: €55,000,000).

23. Amounts owed to banks

	2022	2021
	€	€
Repayable on demand	**275,815**	274,715
	275,815	274,715

24. Amounts owed to customers

	2022	2021
	€	€
Repayable on demand	**75,002,176**	68,449,774
Term deposits	**260,658,694**	229,330,735
	335,660,870	297,780,509

25. Debt securities in issue

	2022	2021
	€	€
At 1 January	**11,940,167**	11,923,078
Debt securities issued	**14,000,000**	-
Debt securities converted to new securities	**(6,811,900)**	-
Redemption of debt securities	**(2,002,100)**	-
Issue costs incurred	**(528,720)**	-
Loss on modification of debt securities (Note 5)	**170,298**	-
Amortisation of debt issuance costs during the year (Note 5)	**52,577**	17,089
At 31 December 2022	**16,820,322**	11,940,167

Debt securities in issue as at 31 December 2021 represented unsecured debt securities with a nominal value of €12,000,000 issued on 30 June 2015 and redeemable on 30 June 2025. These debt securities, which are listed on the Malta Stock Exchange, are denominated in Euro and pay interest at a fixed rate of 4.5%. These debt securities constitute a general, direct, unconditional, and unsecured obligation of the Bank and shall at all times rank pari passu with other unsecured debt.

On 6 July 2022, the Bank announced the issue of €14,000,000 5% unsecured subordinated bonds maturing on 15 September 2032 with an early redemption option held by the Bank on 15 September 2027 and annually thereafter. These debt securities, which are listed on the Malta Stock Exchange, are denominated in Euro, pay interest at a fixed rate of 5% and are redeemable at par. The €14,000,000 5% unsecured subordinated bonds will, in the event of winding up of the Bank, be subordinated to the claims of depositors and all other creditors. As at 31 December 2022, the contractual amount due at maturity is of €14,000,000.

Holders of the €12,000,000 4.50% Unsecured Bond 2025 with a total nominal amount of €6,811,900 and a carrying value of €6.79 million subscribed to the unsecured subordinated bond issued in 2022 by surrendering bonds with a nominal amount of €6,811,900. This exchange did not result in derecognition and the loss on modification of €170,298 was recognised as an adjustment to the effective interest rate in profit or loss. Furthermore, the Bank purchased and cancelled an additional amount of bonds of €2,002,100 in nominal amount from the 4.5% Unsecured Bonds 2025 in accordance with the prospectus dated 18 May 2015.

The Bank has not had any defaults of interest or any other breaches with respect to these debt securities during the financial years ended 31 December 2022 and 2021.

26. Deferred tax assets and liabilities

The recognised deferred tax assets and liabilities are expected to be recovered or settled principally after more than 12 months from the end of the reporting period, and are attributable to the following:

	Assets 2022	**Liabilities 2022**	**Net 2022**	Assets 2021	Liabilities 2021	Net 2021
	€	**€**	**€**	€	€	€
Depreciation of property and equipment and amortisation of intangible assets	**-**	**(242,851)**	**(242,851)**	-	(329,988)	(329,988)
Revaluation of properties	**-**	**(436,414)**	**(436,414)**	-	(558,446)	(558,446)
Fair value changes on financial investments						
- measured at FVOCI	**5,543,538**	**-**	**5,543,538**	329,833	-	329,833
- measured at FVTPL	**-**	**(4,779)**	**(4,779)**	-	(2,240)	(2,240)
Allowance for ECL	**625,016**	**-**	**625,016**	390,830	-	390,830
	6,168,554	**(684,044)**	**5,484,510**	720,663	(890,674)	(170,011)

Deferred taxes are calculated on all temporary differences under the liability method and are measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled based on tax rates (and tax laws) that have been substantively enacted by the end of the reporting period.

The principal tax rate used is 35% (2021: 35%), with the exception of deferred taxation on the fair valuation of non-depreciable property, which is computed on the basis applicable to disposals of immovable property mainly giving rise to a tax effect of 10% of the transfer value (2021: 10%).

Movement in temporary differences relates to:

	At 1 January 2022	**Recognised in profit or loss**	**Recognised in OCI**	**Recognised directly in equity**	**At 31 December 2022**
	€	**€**	**€**	**€**	**€**
Depreciation of property and equipment and amortisation of intangible assets	**(329,988)**	**87,137**	**-**	**-**	**(242,851)**
Revaluation of properties	**(558,446)**	**-**	**(15,118)**	**137,150**	**(436,414)**
Fair value changes on financial investments					
- measured at FVOCI	**329,833**	**-**	**5,213,705**	**-**	**5,543,538**
- measured at FVTPL	**(2,240)**	**(2,539)**	**-**	**-**	**(4,779)**
Allowance for ECL	**390,830**	**234,186**	**-**	**-**	**625,016**
	(170,011)	**318,784**	**5,198,587**	**137,150**	**5,484,510**

	At 1 January 2021	**Recognised in profit or loss**	**Recognised in OCI**	**At 31 December 2021**
	€	**€**	**€**	**€**
Depreciation of property and equipment and amortisation of intangible assets	(359,958)	29,970	-	(329,988)
Revaluation of properties	(558,446)	-	-	(558,446)
Fair value changes on financial investments				
- measured at FVOCI	(344,211)	-	674,044	329,833
- measured at FVTPL	3,888	(6,128)	-	(2,240)
Allowance for ECL	413,418	(22,588)	-	390,830
	(845,309)	1,254	674,044	(170,011)

27. Accruals and other liabilities

	2022	2021
	€	€
Accrued interest payable	**3,744,225**	3,325,807
Other accrued expenses	**1,015,689**	649,315
	4,759,914	3,975,122

28. Share capital and reserves

28.1 Share capital

	2022		2021	
	No. of shares	**€**	No. of shares	€
Authorised				
Ordinary shares of €25 each	**-**	**-**	400,000	10,000,000
Ordinary shares of €0.50 each	**120,000,000**	**60,000,000**	-	-
Issued and fully paid up				
Ordinary shares of €25 each	**-**	**-**	400,000	10,000,000
Ordinary shares of €0.50 each	**58,000,000**	**29,000,000**	-	-

At 31 December 2022, the authorised and issued share capital comprised 120,000,000 and 58,000,000 ordinary shares of €0.50 each respectively, (2021 authorised and issued share capital: 400,000 ordinary shares of €25 each). 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 shareholders' meetings of the Bank.

During an Extraordinary General Meeting held on 27 July 2021, the Shareholders approved a resolution whereby the authorised share capital was re-designated from 400,000 ordinary shares at €25 each to 20,000,000 ordinary shares at €0.50 each. In addition, the authorised share capital was increased to 120,000,000 ordinary shares at €0.50 each. Through the same resolution, the Extraordinary General Meeting also approved an increase in issued share capital through the capitalisation of €17,000,000 out of the capital contribution reserve. In this respect, the Bank issued and allotted 34,000,000 ordinary shares of €0.50 each to IBL T Limited (C16322) and IBL I Limited (C16321), in the same proportion as the existing shareholding at the date of issuance, which shares were credited as fully paid-up shares.

Following Company Announcement IZB89, published on 27 July 2021, relating to the redenomination, reclassification and increase in share capital and the related changes to the Memorandum and Articles of Association, the Bank obtained all the necessary regulatory approvals and the shares have been reclassified and redenominated on 16 February 2022 and the additional shares have been issued with effect from 25 February 2022.

As communicated within Company Announcement IZB91, published on 21 March 2022, the Bank announced the payment of a net dividend of €2,000,000 to its shareholders. The Bank obtained all the necessary approvals on 25 October 2022 and paid the dividend through a bonus issue of new ordinary shares on 22 November 2022, resulting in an increase in issued share capital. In this respect, issued share capital as at 31 December 2022 amounted to €29,000,000.

28. Share capital and reserves (continued)

28.2 Capital contribution reserve

These amounts represent irrevocable and unconditional contributions by the shareholders and are interest free and repayable at the sole discretion of the Bank. As disclosed in Note 28.1, the Bank obtained regulatory approval for the conversion of €17,000,000 from its capital contribution reserve into fully paid-up ordinary share capital effective on 25 February 2022.

28.3 Property revaluation reserve

The property revaluation reserve represents the surplus arising on the revaluation of the Bank's premises, net of related deferred tax effects. This reserve is not available for distribution.

28.4 Fair value reserve

The fair value reserve comprises:
- the cumulative movement in the fair value of equity investments measured at FVOCI, net of deferred tax; and
- the cumulative movement in the fair value of debt securities measured at FVOCI net of deferred tax and allowances for ECL.

28.5 Depositor compensation scheme reserve

The depositor compensation scheme reserve represents amounts set aside by the Bank from its retained earnings. As at 31 December 2022, a total amount of €831,860 (2021: €1,288,168) was placed with the Central Bank of Malta and pledged in favour of the Depositor Compensation Scheme.

28.6 Reserve for general banking risks

Banking Rule 09 (BR09) requires the Bank to hold a Reserve for General Banking Risks, calculated as a percentage of non-performing loans. This reserve is required to be funded from planned dividends. In this respect, the reserve at the end of the year amounted to €72,782 (2021: €45,091).

28.7 Availability of reserves for distribution

	2022	2021
	€	€
Distributable	**916,452**	2,005,302
Non-distributable	**(6,380,522)**	21,274,625

28.8 Dividends

As disclosed in Note 28.1, the Bank declared a net interim dividend of €2,000,000 at the Annual General Meeting held on 24 March 2022. The Bank obtained all the necessary approvals on 25 October 2022 and paid the dividend through a bonus issue of new ordinary shares on 22 November 2022. No dividends are being declared in respect of the financial year ended 31 December 2022.

29. Commitments

	2022 €	2021 €
Unutilised factoring, overdraft facilities and credit card commitments	**185,068,135**	92,738,305

The Bank may unconditionally cancel undrawn factoring commitments at 31 December 2022 amounting to €137,794,135 (2021: €61,283,083) at its discretion.

30. Net cash from operating activities

	2022 €	2021 €
(Loss)/Profit for the year	**(284,219)**	447,981
Adjustments for:		
Depreciation of property and equipment	**149,201**	243,933
Amortisation of intangible assets	**863,548**	600,229
Income tax (credit)/expense	**(103,587)**	372,176
Allowance for ECL	**919,147**	385,692
Interest income on debt financial investments	**(1,738,480)**	(1,710,715)
Interest expense on debt securities in issue	**701,743**	540,000
Net unrealised (loss)/gain from financial investments measured at FVTPL	**(10,543)**	59,028
Realised gains/(losses) on disposal of financial investments	**7,299**	(442,395)
Amortisation of premiums and discounts on debt financial investments	**386,904**	698,100
Loss on modification of debt securities	**170,298**	-
Amortisation of debt issuance costs	**52,577**	17,089
	1,113,888	1,211,118
Movements in reserve deposit with Central Bank of Malta	**(613,235)**	(35,999)
Movements in loans and advances to customers	**(29,464,646)**	(9,762,784)
Movements in factored receivables	**(23,441,465)**	4,129,447
Movements in amounts owed to institutions	**(15,000,000)**	20,000,000
Movements in amounts owed to customers	**37,880,361**	(6,604,220)
Movements in accruals and deferred income	**(781,716)**	1,223,119
	(30,306,813)	10,160,681

31. Cash and cash equivalents

	2022	2021
	€	€
Cash	-	1,613
Balances with Central Bank of Malta	**15,616,395**	14,823,498
Loans and advances to banks with contractual maturity of three months or less	**10,214,993**	25,420,282
Amounts owed to banks	**(275,815)**	(274,715)
	25,555,573	39,970,678

Balances with the Central Bank of Malta exclude mandatory reserve deposits of €1,981,892 (2021: €1,368,657) which are not available for use in the Bank's day-to-day operations. Balances with the Central Bank of Malta also comprise an amount of €831,860 (2021: €1,288,168) pledged in favour of the Depositor Compensation Scheme.

32. Related parties

32.1 Identity of related parties, and parent and ultimate controlling party

Related parties of the Bank include the ultimate parent, all entities controlled by the ultimate parent, key management personnel, close family members of key management personnel and entities which are controlled or jointly controlled by key management personnel or their close family members.

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the Bank, being the directors and the Bank's executive management. Reference to executive management shall mean the CEO, the Head of Finance & Treasury, the Head of Strategy & Value, the Head of Operations, the Head of Credit, the Head of Information & Technology, the Head of Risk and Compliance and the Head of Human Resources.

The Bank's immediate parent is IBL T Limited, the registered office of which is 53-58, East Street, Valletta VLT 1251, Malta.

The financial results and assets and liabilities of the Bank are included in the consolidated financial statements of Carlenco Finance NV, with registration number 0755.471.533, the registered office of which is Lar Blok Z5, 8511 Kortrijk, Belgium.

Magdalena De Roeck and Caroline Van Marcke have an indirect beneficial interest in the shareholding of the Bank and have significant control in the ultimate parent.

32.2 Related party transactions

Interest, fees, and other income/expenses in respect of related parties, principally comprising entities within the Van Marcke Group, in the statement of profit or loss and other comprehensive income comprise:

	2022	2021
	€	€
Interest and similar income	**3,778,761**	1,572,688
Fee and commission income	**80,500**	86,645
Other operating income	**2,100**	65,492
Interest expense	**332,385**	374,943

32. Related parties (continued)

32.3 Related party balances

The statement of financial position includes outstanding transactions and balances with related parties, principally comprising entities within the Van Marcke Group, as follows:

	2022	2021
	€	€
Assets		
Loans and advances to customers	**42,239,142**	36,442,579
Prepayments and accrued income	**537,581**	508,679
Liabilities		
Amounts owed to customers	**42,133,209**	29,511,433
Debt securities issued to directors	**364,300**	290,000
Accruals	**5,743**	11,706

Loans and advances to customers include 6 (2021: 4) outstanding loans to key management personnel amounting to €250,000, €249,413, €14,253, €9,088, €232,995 and €26,578 (2021: €250,000, €97,699, €17,782 and €8,035). The two loans amounting to €250,000 and €232,995 (2021: €250,000) are secured against property in Malta, bear interest at 1.75% and 1% per annum respectively. Both loans are repayable after more than five years from the reporting date. The remaining amounts are unsecured and bear interest between 1.3% and 1.75% (2020: 1% and 1.75%) per annum and are repayable after more than five years.

32.4 Transactions with key management personnel

	2022	2021
	€	€
Directors' fees	**145,000**	137,000
Compensation to key management personnel – salaries	**757,758**	553,967

33. Operating segments

33.1 The segment reporting of the Bank is presented in terms of the following business segments, determined in accordance with the disclosure requirements in respect of reportable segments under IFRS 8 – Operating Segments:

Reportable segment	Description of activities
Factoring	Principally factoring of bills of exchange and invoices on a no-recourse basis
Lending	Principally lending to corporate clients and mortgages
Other	Principally treasury and other central functions

Revenues earned and expenses incurred in respect of each of the reportable business segments are presented in the table below. No reconciliation is required since there are no differences between the measurements of the reportable segments' profits or losses and the information disclosed in the statement of profit or loss and other comprehensive income.

	2022 Total €	**2022 Lending €**	**2022 Factoring €**	**2022 Other €**	2021 Total €	2021 Lending €	2021 Factoring €	2021 Other €
Interest and similar income								
Loans and advances to customers	**5,345,149**	**5,345,149**	**-**	**-**	4,567,305	4,567,305	-	-
Factored receivables	**6,362,852**	**-**	**6,362,852**	**-**	4,989,116	-	4,989,116	-
Amounts owed to institutions	**28,194**	**-**	**-**	**28,194**	135,521	-	-	135,521
Financial assets measured at FVOCI	**1,738,480**	**-**	**-**	**1,738,480**	1,710,715	-	-	1,710,715
Amortisation on financial assets measured at FVOCI	**(386,904)**	**-**	**-**	**(386,904)**	(698,100)	-	-	(698,100)
Total operating income	**13,087,771**	**5,345,149**	**6,362,852**	**1,379,770**	10,704,557	4,567,305	4,989,116	1,148,136
Interest expense								
Loans and advances to banks	**(290,730)**	**(117,100)**	**(86,450)**	**(87,180)**	(98,542)	(24,309)	(33,597)	(40,636)
Amounts owed to customers	**(4,197,297)**	**(1,690,585)**	**(1,248,081)**	**(1,258,631)**	(3,858,102)	(951,737)	(1,315,379)	(1,590,986)
Debt securities issued	**(701,743)**	**(282,647)**	**(208,666)**	**(210,430)**	(540,000)	(133,210)	(184,107)	(222,683)
Amortisation of debt issuance costs	**(52,577)**	**(21,177)**	**(15,634)**	**(15,766)**	(17,089)	(4,216)	(5,826)	(7,047)
Loss on modification of debt securities	**(170,298)**	**(68,592)**	**(50,639)**	**(51,067)**	-	-	-	-
Interest expense	**(5,412,645)**	**(2,180,101)**	**(1,609,470)**	**(1,623,074)**	(4,513,733)	(1,113,472)	(1,538,909)	(1,861,352)
Net interest income	**7,675,126**	**3,165,048**	**4,753,382**	**(243,304)**	6,190,824	3,453,833	3,450,207	(713,216)
Net fee and commission income/(expense)	**55,912**	**130,753**	**(61,504)**	**(13,337)**	(10,195)	59,248	(55,493)	(13,950)
Net trading income	**15,789**	**-**	**-**	**15,789**	31,168	-	-	31,168
Net (losses)/gains on disposal of financial investments measured at FVOCI	**(7,299)**	**-**	**-**	**(7,299)**	442,395	-	-	442,395
Other operating income	**101,325**	**-**	**-**	**101,325**	97,746	-	-	97,746
Operating profit/(loss)	**7,840,853**	**3,295,801**	**4,691,878**	**(146,826)**	6,751,938	3,513,081	3,394,714	(155,857)
Depreciation and amortisation	**(1,012,749)**	**(339,220)**	**(585,964)**	**(87,565)**	(844,162)	(369,264)	(302,889)	(172,009)
Changes in expected credit losses and other credit impairment charges	**(919,147)**	**(519,237)**	**(365,088)**	**(34,822)**	(385,692)	(28,153)	(345,679)	(11,860)
Employee compensation and benefits	**(2,513,276)**	**(542,271)**	**(1,481,981)**	**(489,024)**	(2,103,290)	(920,048)	(754,670)	(428,572)
Other administrative expenses	**(3,783,487)**	**(1,239,828)**	**(2,146,055)**	**(397,604)**	(2,598,637)	(1,136,728)	(932,403)	(529,506)
(Loss)/profit before tax	**(387,806)**	**655,245**	**112,790**	**(1,155,841)**	820,157	1,058,888	1,059,073	(1,297,804)

33. Operating segments (continued)

	2022 Total €	**2022 Lending €**	**2022 Factoring €**	**2022 Other €**
Assets				
Segment assets	**398,057,213**	**160,329,282**	**118,363,724**	**119,364,207**
Unallocated assets	**23,432,052**	**-**	**-**	**-**
Total Assets	**421,489,265**	**160,329,282**	**118,363,724**	**119,364,207**
Liabilities				
Segment liabilities	**392,757,007**	**158,194,468**	**116,787,689**	**117,774,850**
Unallocated liabilities	**5,196,328**	**-**	**-**	**-**
Total Liabilities	**397,953,335**	**158,194,468**	**116,787,689**	**117,774,850**

	2021 Total €	2021 Lending €	2021 Factoring €	2021 Other €
Assets				
Segment assets	385,315,937	95,051,834	131,369,341	158,894,762
Unallocated assets	17,492,949	-	-	-
Total Assets	402,808,886	95,051,834	131,369,341	158,894,762
Liabilities				
Segment liabilities	364,995,391	90,039,051	124,441,269	150,515,071
Unallocated liabilities	4,533,568	-	-	-
Total Liabilities	369,528,959	90,039,051	124,441,269	150,515,071

33.2 Geographical information

The Bank provides all its services from Malta. In presenting information on the basis of geographical segments, segment revenue is based on the geographical location of customers. Segment assets are based on the geographical location of the assets.

	2022 €	2021 €
Revenue		
Malta	**8,977,283**	7,525,207
Belgium	**4,402,722**	3,870,525
	13,380,005	11,395,732
Non-current assets		
Malta – tangible and intangible assets	**13,687,818**	14,339,765

Further geographical information about Loans and advances to customers, Factored receivables, Loans and advances to banks, and Financial investments is set out in Note 4.3.11.

The Bank's major customer is the Van Marcke Group of which it forms part. Belgium is the country of domicile of this Group.

Information about revenues, expenses, and balances as a result of transactions with the Group is set out in Note 32.

34. Critical accounting estimates and judgements

The preparation of financial statements in accordance with the requirements emanating from IFRSs as adopted by the EU requires the use of accounting estimates which, by definition, will seldom equal the actual results. Management also needs to exercise judgement in applying the Bank's accounting policies.

This note provides an overview of the areas that involved a higher degree of judgement or complexity, and of items which are more likely to be materially adjusted due to estimates and assumptions turning out to be wrong. Detailed information about these estimates and judgements is included in other notes together with information about the basis of calculation for affected line items in the financial statements.

Measurement of ECL in respect of loans and advances to customers and factored receivables

The estimation of credit loss allowances in respect of loans and advances to customers and factored receivables is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour.

A number of significant judgements are required in the measurement of ECL, including:

- The determination of criteria for the identification of significant increase in credit risk and unlikeliness-to-pay events;
- The choice of appropriate models and assumptions for the measurement of ECL; and
- The selection of forward-looking scenarios used in the estimation of credit loss allowances, including judgements and assumptions in relation to the number and severity of scenarios as well as the relative probability weights assigned to each scenario.

The measurement of the credit loss allowances is an area that requires the use of complex models and of statistical analyses of historical information, supplemented with significant management judgement, to assess whether current and future macroeconomic conditions are such that the level of ECL is likely to be greater or less than historical experience. The ECL models are reviewed regularly in light of differences between loss estimates and actual loss experience, although available information in respect of the Bank's historical loss experience since the initial adoption of IFRS 9 is still contained.

Notwithstanding the general economic recovery experienced during 2021 and 2022, with rapid economic growth registered as the global economy rebounded in the aftermath of the Covid-19 pandemic, together with Malta's removal from the FATF grey list in June 2022, the level of estimation uncertainty and judgement remains elevated due to the ensuing geopolitical and macroeconomic events occurring during the financial year ended 31 December 2022.

Specifically, the global supply chain disruptions experienced in the aftermath of the pandemic, together with the escalation of the military conflict between Russia and Ukraine in February 2022, have triggered significant inflationary pressures across Europe as well as a slowdown in global economic growth, resulting in a stagflationary economic environment. In response, the ECB has adjusted its monetary policy stance during the financial year ended 31 December 2022, which has been reflected through multiple incremental announced increases in interest rates in a bid to curtail inflation. In this respect, the current economic outlook is highly characterised by inflationary pressures and an increasing interest rate environment. In view of the induced level of economic uncertainty, the underlying models and their calibration, including how they react to forward-looking economic conditions, remain highly subjective and might not accurately represent the effects of these economic changes.

A detailed description of the inputs, assumptions and estimation techniques used in measuring ECL in respect of loans and advances to customers and factored receivables is disclosed in Note 4.3.2. The underlying risk factors have a high degree of interdependency and there is no single factor to which credit loss allowances as a whole is sensitive.

34. Critical accounting estimates and judgements (continued)

Significant judgement is required in establishing the number, severity and relative weightings of forward-looking economic scenarios in the context of the heightened level of macroeconomic uncertainty being experienced. The level of expert judgement required is exacerbated by the heightened level of uncertainty around predictions in respect of the potential impacts of assumptions in relation to inflation and interest rates, particularly the potential market response to further increases in interest rates, and of the effectiveness of government support schemes together with the impacts of their unwinding, on key macroeconomic variables and, as a result on forward-looking PDs. As alluded to earlier, there is an absence of an observable historical trend that can accurately represent the severity of the economic impacts brought about by the geopolitical tensions between Russia and Ukraine as well as the stagflationary and increasing interest rate environment being currently experienced. Moreover, the complexities of government support schemes and their unwinding, and the unpredictable pathways of the economic outlook taking cognisance of potential further changes to fiscal and monetary policies, have never been modelled. Consequently, in some cases, modelled assumptions and linkages between economic factors and credit losses may underestimate or overestimate ECL in these conditions.

The determination of economic forecasts in the current environment thus represents a significant source of uncertainty, which in turn significantly increases the level of subjectivity around the estimation of credit loss allowances in respect of loans and advances to customers and factored receivables.

In addition, the implementation of government support schemes, specifically the subsidisation of energy prices by the Maltese government, has partially mitigated the impact of inflationary pressures in the local economy. However, significant uncertainty exists in relation to the Maltese government’s continued ability to continue subsidising energy prices, especially if the current level of inflationary pressures remains sustained for a prolonged period of time. In this respect, the unwinding of government support schemes would have a significant impact on the local economy.

In this regard, management applied a higher level of expert judgement in order to assess the impact of the current macroeconomic environment on the Bank’s level of defaults, including evaluating the impact of government support schemes, and the unwinding of such measures, on both the incidence of default events and the severity of losses as described below.

The identification of customers experiencing a 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 the case of industry sectors which are benefiting significantly and are heavily reliant on energy price subsidies designed to curb the impact of inflationary pressures on local businesses, which might lead to delayed default emergence.

For loans and advances to customers, the Bank performs periodic credit assessments at borrower level by reference to recent historical management information and financial forecasts, where available. 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. In particular, corporate borrowers operating in industry sectors which are most likely to be impacted by inflationary pressures and an increasing interest rate environment, as well as being most reliant on the Maltese government’s subsidization of energy prices, were monitored closely in order to determine whether these economic shocks may transform into long-term financial difficulties.

In relation to factored receivables, 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 SICR or UTP events.

For credit-impaired loans and advances to customers, management estimates credit loss allowances by reference to the realisable value of security under different scenarios. Judgement is applied in estimating the forecasted recoveries from the sale of collateralised properties, including around valuation haircuts and time to recovery. The heightened level of uncertainty within the local property market, driven by the current inflationary pressures and the potential impact of an increasing interest rate environment, 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 these macroeconomic events will not be fully known until market conditions stabilise.

34. Critical accounting estimates and judgements (continued)

In view of the above, management considered the sensitivity of the ECL outcome to the macroeconomic forecasts by recalculating the ECL under the different scenarios, applying a 100% weighting to each scenario. The effect of economic uncertainty on ECL is disclosed in the sensitivity analysis presented in Note 4.3.2.4. 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.

35. Subsequent events

35.1 Notification of additional contributions payable to the Depositor Compensation Scheme

On 3 February 2023, the Depositor Compensation Scheme (the "Scheme") formally requested the Bank to settle the amount of €623,844 to cover its pro-rata share of the shortfall in the Scheme's available financial means as a result of the pay-out by the Scheme to Nemea Bank plc's eligible depositors.

The Bank paid the amount in full on 8 March 2023. The Bank has been notified that the amount is fully refundable, once the Scheme receives the amount of the shortfall from the Controller of Nemea Bank plc. Based on the information made available to the Bank as at the date of authorisation for issuance of these financial statements, it appears to be unlikely that the Controller would not refund the entire amount to the Scheme in the foreseeable future.

35.2 Reclassification of Malta Government Stock portfolio

During the financial year ending 31 December 2023, the Bank's management will continue to pursue potential investment opportunities to further diversify its asset base, in line with the growth and diversification strategy approved by the Bank's Board of Directors in the first quarter of 2022.

As part of this strategy, during the financial year ended 31 December 2022 management has initiated a new business line, as the Bank launched its mortgage product offering to the retail market in Malta. As at 31 December 2022, the carrying amount of drawn down retail mortgage exposures was €5.91 million, whereas undrawn commitments as at the same date amounted to €4.14 million. The development of this business line enables the Bank to diversify its asset portfolios and to limit the level of concentration risk to specific portfolios within its asset base.

During the financial year ending 31 December 2023, management is actively working towards the achievement of its growth target levels in line with the approved business plan for the next three financial periods.

In view of the above, management has considered different investment opportunities which should support the Bank in achieving higher levels of growth in its retail mortgage business line. In this respect, by the date the financial statements were authorised for issue, management had signed a term sheet submitted by a leading market provider in order to originate a €100 million portfolio of Dutch mortgages.

In support of this significant development, the Bank is adjusting its funding profile by shifting towards shorter term deposits to fund its mortgage portfolio in order to manage its net interest margin, given that the yields from a retail mortgage product are materially lower when compared to the yields from the Bank's other portfolios of financial assets. In this respect, liquidity gaps in the Bank's maturity profile are expected to arise as a result of the launch of longer-term mortgages and the raising of shorter-term deposits. These liquidity gaps are expected to widen with the introduction of its Dutch mortgage business, since the mismatch in maturity profiles of the Bank's asset and funding bases would be expected to become more pronounced. Management intends to address these liquidity gaps through the use of secured funding, specifically raising funding through ECB operations by pledging its portfolio of sovereign bonds to secure funded amounts.

35. Subsequent events (continued)

35.2 Reclassification of Malta Government Stock portfolio (continued)

As at 31 December 2022, the Bank's portfolio of sovereign bonds is measured at FVOCI in view of the fact it is deemed to be held within a business model where the objective is achieved by both collecting contractual cash flows and selling financial assets. Going forward, this portfolio of high-quality liquid assets would be specifically allocated solely to raise funding through ECB operations in order to address the above-mentioned liquidity gaps, attributable to the mortgage business line in particular following the origination of the Dutch mortgage business. Accordingly, management is considering reclassifying its sovereign bond portfolio out of the fair value through other comprehensive income (FVOCI) category into the amortised cost category in 2023, since the financial instruments would be held within a business model where the objective is to hold financial assets to collect contractual cash flows.

35.3 Assessment of emerging risks in relation to events occurring after year end

Many central banks have raised their benchmark interest rates at a significant and rapid pace over the past year. This significantly reduced the value of fixed rate investments and produced "unrealised losses" on the balance sheets of banks (either recognised in accumulated other comprehensive income for portfolios held at fair value through OCI, or unrecognised but disclosed for portfolios held at amortised cost).
These interest rate increases have also driven customers of banks to shift bank deposits to other products like money market funds in search of higher yields. This dynamic as well as customers' increased spending of cash accumulated during the pandemic has culminated in a loss of funding for many banks.

This combination of reduced values in investment portfolios and increased pressures from deposit outflows has led to challenges in managing liquidity risk, particularly as selling lower-yielding investments at a loss to cover deposit outflows erodes capital. The liquidity risk is heightened when the deposits are larger, concentrated or shorter-term and are not covered by a protected deposit guarantee scheme, which might give rise to an asset-liability mismatch. The recent events experienced in the global banking sector subsequent to 31 December 2022 demonstrate the potentially critical impact of increased deposit outflows surpassing existing liquidity buffers held in the form of cash and highly liquid investments that decline in value and highlight the need for all banks to continuously evaluate and adapt their liquidity risk and interest rate risk management practices.

In this respect, the Bank took cognisance of the ongoing developments occurring subsequent to the reporting date, particularly in view of the financial difficulties experienced by Silicon Valley Bank, Signature Bank and Credit Suisse Group AG, and performed an assessment to evaluate the Bank's ability to withstand liquidity pressures triggered by a potential deposit run.
The Bank holds a portfolio of financial investments measured at fair value through other comprehensive income, which instruments are predominantly listed and rated as 'investment grade' securities by external credit rating agencies. In this respect, the Bank's investment portfolio comprises sovereign bonds with a fair value of €59.8 million, out of which €19.8 million are unencumbered as at 31 December 2022, as well as local corporate bonds with a fair value of €31.2 million. In addition, the Bank also has unencumbered balances with the Central Bank of Malta amounting to €13.9 million as well as loans and advances to banks amounting to €10.2 million.

In this respect, the Bank deems that it holds sufficient high quality liquid assets to withstand pressures arising from a hypothetical stress on its liquidity, such as in a scenario with higher outflows in respect of deposits not covered by the Depositor Compensation Scheme. The Bank continues to report healthy levels of liquidity in its Liquidity Coverage Ratio up to 26 April 2023, well above both internal thresholds as well as minimum legal / regulatory requirements. In this respect, no material uncertainties to the use of the going concern assumption are deemed to arise.

Independent auditor's report

To the Shareholders of Izola Bank p.l.c.

Report on the audit of the financial statements

Our opinion

In our opinion:

- The financial statements give a true and fair view of the financial position of Izola Bank p.l.c. (the Bank) as at 31 December 2022, and of 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 Banking Act (Cap. 371) and the Maltese Companies Act (Cap. 386).

Our opinion is consistent with our additional report to the Audit Committee.

What we have audited

Izola Bank p.l.c.'s financial statements comprise:

- the statement of profit or loss and other comprehensive income for the year ended 31 December 2022;
- the statement of financial position as at 31 December 2022;
- the statement of changes in equity for the year then ended;
- the statement 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

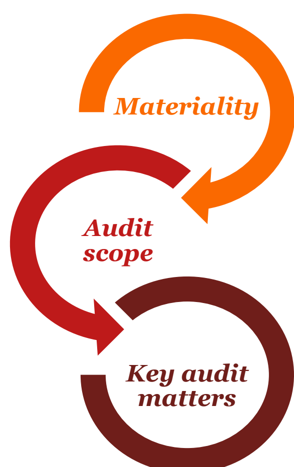
We are independent of the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code) together with the ethical requirements of the Accountancy Profession (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 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, in the period from 1 January 2022 to 31 December 2022, are disclosed in note 10.1 to the financial statements.

Our audit approach

Overview



- Overall materiality: €235,000, which represents 1% of net assets.

- Credit loss allowances in respect of loans and advances to customers and factored receivables

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the 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.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the financial statements as a whole, taking into account the structure of the Bank, the accounting processes and controls, and the industry in which the Bank operates.

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 financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the 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 materiality	€235,000
How we determined it	1% of net assets
Rationale for the materiality benchmark applied	We chose net assets as the benchmark because, in our view, the actual return payable to the equity holders of the Bank is heavily dependent on the adequacy of the Balance Sheet capitalisation in view of the regulatory restrictions in respect of dividend distributions. We also considered the fact that the principal users of the Bank's financial statements are the ultimate parent of the Bank and its bondholders. We chose 1% which is within the range of quantitative materiality thresholds that we consider acceptable.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above €23,500 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 and factored receivables Credit loss allowances in respect of loans and advances to customers and factored receivables represent management's best estimate of expected credit losses ('ECLs') within these portfolios at the balance sheet date. The Bank has two main portfolios: • Loans and advances to customers, comprising secured loans to local corporates as well as local residential mortgages, the latter representing a new product offering initiated by the Bank during the financial year ended 31 December 2022; and • Factored receivables, which comprise the factoring of bills of exchange issued to local debtors and the factoring of invoices payable by Maltese, Belgian,	During our audit of the financial statements for the year ended 31 December 2022, we focused on the key drivers of the estimation of ECL. In this respect, we evaluated and tested the appropriateness of management assumptions and key parameters. The revised ECL model used to estimate credit loss allowances in respect of loans and advances to customers represented a significant update to the methodology used by management to estimate ECLs. Accordingly, the underlying assumptions and key judgements around the amended model were reviewed, assessed and tested to evaluate the reasonableness of the modelled ECLs. Discussions with the Audit Committee and management included: • the policies and methodologies used by the bank in respect of the estimation of ECLs on loans and advances to customers and factored receivables;

French and Dutch debtors, both factored on a non-recourse basis.

The measurement of ECLs in respect of these portfolios, particularly for loans and advances to customers, requires a considerable level of judgement since the determination of ECLs is subject to a high degree of estimation uncertainty. In this respect, it is considered a key area of focus.

The development of the models designed to estimate ECLs on financial instruments measured at amortised cost in accordance with the requirements of IFRS 9 requires a considerable level of judgement. The prevailing macroeconomic environment during the financial year ended 31 December 2022, was highly characterised by global supply chain disruptions in the aftermath of the Covid-19 pandemic, the escalation of the military conflict between Russia and Ukraine, together with the ensuing inflationary pressures and the shift in ECB monetary policy resulting in an increasing interest rate environment. In this respect, the level of uncertainty around the calculation of ECLs has been exacerbated, 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.

In general, the bank calculates ECL by using the following key inputs: probability of default ('PD'), loss given default ('LGD') and exposure at default ('EAD'). The maximum period considered when measuring ECL is the maximum period over which the bank is exposed to credit risk.

Credit loss allowances relating to loans and advances to customers are determined at an instrument level. During the financial year ended 31 December 2022, the bank modified the model used to estimate ECL in respect of corporate exposures, which inherently required a significant level of judgement to be applied by management in the determination of key assumptions and calibration of key model parameters.

For non-defaulted (Stages 1 and 2) exposures, the bank uses an ECL model developed by an external vendor in which key risk parameters are estimated at a borrower level. Specifically, PDs are determined by reference to quantitative (financial statement information) model inputs,

- observations in respect of the key assumptions and judgements applied by management in the revised ECL model used to estimate credit loss allowances in respect of loans and advances to customers, together with the impact of the model change on ECLs;
- considerations in respect of the governance framework around the implementation of model changes;
- inputs, assumptions and adjustments to ECL, in particular the determination of 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 macroeconomic modelling, including the severity and magnitude of modelled scenarios, particularly in the context of the estimated impact of the prevailing macroeconomic conditions in the aftermath of the pandemic, highly characterised by inflationary pressures and an increasing interest rate environment; and
- individually significant loan impairments.

ECL calculation for non-defaulted loans and advances to customers and for all factored receivables

We understood and critically assessed the models used for ECL estimation in respect of loans and advances to customers and factored receivables. Since modelling assumptions and parameters are based on historic data, we assessed the impact of the unprecedented circumstances we are currently experiencing on the adequacy of key model parameters, since these are based on historical experience that is not necessarily reflective of the current level of credit risk within the portfolios.

The appropriateness of management's judgements was also independently considered in respect of calculation methodologies, calibration of PDs and LGDs, and selection of macroeconomic variables, especially in view of the revised model utilised to estimate ECLs in respect of loans and advances to customers.

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 macroeconomic environment.
- Tested a sample of exposures classified within loans and advances to customers to independently review the borrower's financial

which are used to generate a borrower-specific credit score. A set of key financial ratios, determined by reference to borrower-specific financial statement inputs, are estimated by the model and benchmarked against equivalent ratios relating to an underlying model dataset comprising obligors which are comparable to the Bank's corporate borrowers in terms of size and industry in order to determine a borrower-specific credit score. Credit scores are then mapped to a PD by reference to a credit score to PD matrix calibrated on the basis of historical market default data sourced from publicly available information. PDs are adjusted to capture country- and industry-specific credit risk characteristics and assigned to each borrower. PDs are then adjusted using statistical regression techniques to simulate the PD under multiple macroeconomic forecasts (conditional PiT PD).

For exposures classified within the newly launched residential mortgage portfolio, PDs are determined by reference to comparable portfolios at peer banks, in view of the lack of internal observable default data given that the portfolio is still in its infancy.

Loans and advances to customers are primarily secured by residential and / or commercial real estate, as well as cash pledges and government guarantees under the terms of the Malta Development Bank Covid-19 Guarantee Scheme ('MDB CGS').

The LGD used for loans and advances to customers secured by real estate is driven by the adjusted loan-to-value ('LTV') ratio of the individual facilities which takes into account a market value haircut (that includes costs to sell). No ECL is attributed to exposures (or parts thereof) which are cash secured, whereas losses in respect of exposures secured by the MDB CGS are assumed to be up to 90% covered by the government guarantee.

Following the model change implemented during the current financial year, LGDs for unsecured exposures are determined by reference to the carrying amount of tangible assets recognised on the borrower's balance sheet. Expected recoveries from the sale of such assets are modelled by reference to assumptions in relation to market value haircuts, taking into consideration asset type and the time value of money. The LGD for unsecured exposures, determined through the use of statistical

performance and ability to meet loan repayments and assess the appropriateness of the internal credit rating assigned by management, taking into consideration the impact of inflationary pressures and the increasing interest rate environment 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 assets in stage 1, 2 and 3 to verify that they were allocated to the appropriate stage.
- Tested the completeness and accuracy of key model data inputs utilised within the models for the purposes of the year end ECL calculation.
- Reviewed and assessed the appropriateness of model assumptions, inputs and formulas used in ECL models. This included assessing the appropriateness of model design, methodology and formulas used, specifically challenging the appropriateness of the methodology to derive PDs.
- Tested the segmentation applied in the ECL calculation to determine the PDs in respect of factored bills of exchange and factored invoice facilities.
- Reviewed a sample of property collateral valuations utilised to determine LGDs applied by the bank in respect of loans and advances to customers secured by real estate, using our valuation experts.
- For loans and advances to customers:
  - reviewed the appropriateness and reasonableness of the methodology and key assumptions applied by management in the newly implemented ECL model used to determine PDs and LGDs for corporate exposures;
  - tested the accuracy of model inputs to the calculation of PDs and unsecured LGDs, which principally comprise borrower-specific quantitative financial statement inputs, on a sample basis;
  - assessed the reasonableness of modelled ECLs by reference to ECL coverage rates determined by peer banks in respect of comparable portfolios;
  - tested the accuracy of the inputs to the LTV ratio calculation, which is a key input to the LGD determination, and assessed the reasonableness of market value haircuts applied to the LTV ratio; and

techniques by the external vendor, also takes into consideration a correlation factor between PDs and LGDs, with higher LGDs being assigned to borrowers for whom a higher PD is determined by the model.

For defaulted (Stage 3) loans and advances to customers, discounted cash flow models are utilised in order to estimate ECLs. Judgement is required to determine when a default has occurred and then to estimate the expected future cash flows related to that loan which are dependent on parameters or assumptions in respect of the valuation of collateral (including forced sale discounts). The bank is also required to assess multiple scenarios in this respect, which scenarios will have probabilities attached.

Credit loss allowances relating to all factored receivables (Stages 1, 2 and 3) are determined through the use of ECL models.

For non-defaulted factored bills of exchange, the Bank's PDs are determined by reference to a statistical model developed by an external vendor. Transition matrices were developed by reference to internal historical delinquency data. A portfolio segmentation approach was determined to categorise exposures sharing similar credit risk characteristics. In this respect, a multi-tier rating scale was developed, representing different states of delinquency, with a common PD being assigned to exposures classified within the same tier. The PD is adjusted by applying a cure rate estimated by reference to internal historical delinquency information.

For all factored bills of exchange, the LGD is determined by reference to the estimated value of the underlying asset, being the financed motor vehicle. Specifically, assumptions are made in respect of the expected value of the motor vehicle over its useful life. The LGD also takes into consideration cash collateral pledged by factoring clients to cover potential losses from factored bills of exchange.

For all invoice factoring facilities, PDs are sourced from an external vendor. Specifically, a debtor-specific credit score is assigned by the external vendor based on borrower-specific information. PDs are then determined by reference to the debtor-specific credit score. The LGD is in turn modelled by reference to the credit insurance cover purchased from a foreign third party underwriter which provides

  - performed procedures to assess the potential risks associated with unperfected collateral.

- For factored bills of exchange, assessed the reasonableness of the underlying assumptions and the accuracy of the calculations used in the estimation of LGD, specifically the assumptions in relation to the expected value of the underlying assets over the lifetime of the exposure.
- For factored invoice facilities, assessed the reasonableness of the assumption in relation to the determination of LGD by reference to the terms of the credit insurance arrangement with a third party underwriter.
- Performed a recalculation of the ECL for a sample of exposures across portfolios.
- Assessed the reasonableness of macroeconomic scenarios and variables used in the ECL calculation of loans and advances to customers and factored bills of exchange. We assessed whether the severity of the forecasted macroeconomic variables was appropriate in view of the high level of uncertainty surrounding the economic outlook as a result of the prevailing inflationary pressures and increasing interest rate environment.
- For a sample of invoice factoring facilities which were past due by more than 90 days as at 31 December 2022, performed procedures to assess the recoverability of such exposures.

Our testing of models and model assumptions did not highlight material differences.

Based on the evidence obtained, we found that the model assumptions and data used within the models are reasonable.

ECL calculation for defaulted loans and advances to customers

For defaulted loans and advances to customers, 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 the loan portfolio, as well as the impairment assessment processes.

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 was particularly impacted by the prevailing macroeconomic environment and for determining whether a UTP/default event had occurred by testing a sample of performing loans, including from

insurance cover in respect of losses up to 95% of each eligible invoice.

The bank's internal credit risk management framework designed to identify significant increase in credit risk ('SICR') or unlikeliness-to-pay ('UTP') events in respect of corporate loans and advances to customers is based on credit risk assessments performed at individual borrower level, taking into consideration quantitative and qualitative information. In this respect, staging of loans and advances to customers is determined by reference to internal credit risk gradings. Judgement is required to determine a) whether a SICR has occurred since initial recognition of the instrument; or b) when a default has occurred.

The local impact of the global inflationary pressures has been partially mitigated by government measures, specifically the subsidisation of energy prices across the local economy. These economic conditions have increased the level of uncertainty around judgements made in determining the timing of defaults and in respect of staging, particularly in relation to loans and advances to corporate customers. For the purposes of avoiding the cliff edge effect on ECLs upon the discontinuation of government subsidies, the Bank assesses the internal credit risk ratings of all loans and advances to corporate customers on an ongoing basis by reference to qualitative characteristics to enable the identification of SICR or UTP events as early as possible.

Factored receivables and exposures classified within the residential mortgage portfolio are not managed on a credit by credit basis due to the high volume of relatively low value and homogeneous exposures. In this respect, the bank's internal credit risk management framework designed to identify SICR or UTP events in respect of such exposures is primarily based on delinquency.

Under IFRS 9, the bank is also required to formulate and incorporate multiple forward-looking economic conditions, reflecting management's view of potential future economic variables and environments, into the ECL estimates. A number of macroeconomic scenarios based on the selected macroeconomic variables are considered to capture non-linearity across credit portfolios. The complexity attributable to this factor requires management

within those sectors that we consider to have been significantly impacted by current economic conditions, which had not been identified by management as potentially defaulted, to form our own judgement as to whether management's judgement was appropriate. Specifically, we challenged whether default events had actually occurred and assessed whether default events had been identified by management in a timely manner.

- Assessed the timeliness of the performance and review of the credit file review process.

Substantive procedures were performed on defaulted exposures in respect of the estimation of the size of the respective ECL provisions, as follows:

- Reviewed the credit files of loans and advances classified within stage 3 to understand the latest developments at the level of the borrower and the basis of measuring the ECL provisions and considered whether key judgements (such as market value haircuts used in the gone concern assessment) were appropriate given the borrowers' circumstances taking cognisance of the prevailing macroeconomic uncertainties.
- Challenged the appropriateness of the bank's methodology in respect of scenarios applied for the exposures referred to above, particularly in respect of the extent to which the bank considers multiple scenarios in determining the recoverability of stage 3 loans as well as the potential impact of the current economic conditions on the local property market, by forming an independent view of the recoverability of stage 3 loans under different scenarios.
- Tested key inputs and reperformed the impairment calculation used to derive expected cash flows under different scenarios.
- Assessed the appropriateness of property valuations securing impaired loans through our valuation experts.
- Tested the perfection of security in line with the bank's policy.

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.

to develop multiple macroeconomic scenarios involving the use of significant judgements. The bank utilises a methodology to generate the economic inputs applied within the ECL models in respect of loans and advances to customers and factored bills of exchange. Given the short-term nature of invoice factoring facilities, the impact of forward-looking information on the estimation of ECL in respect of these exposures is not deemed to be significant.

The prevailing macroeconomic conditions in the aftermath of the pandemic, including global supply chain disruptions and the escalation of the military conflict between Russia and Ukraine, which have triggered inflationary pressures and changes in ECB monetary policy resulting in an increasing interest rate environment, together with the government support measures adopted to mitigate inflationary pressures, have significantly impacted macroeconomic factors such as GDP and unemployment, 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.

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. This increases risk around completeness and accuracy of certain data used to create assumptions and operate the 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 the current unprecedented macroeconomic and geopolitical environment, which 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 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.

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 financial statements:

- Accounting policies: Note 3.1;
- Credit risk management: Note 4.3;
- Note on Changes in expected credit losses and other credit impairment charges: Note 9;
- Note on Factored receivables: Note 17
- Note on Loans and advances to customers: Note 18; and
- Critical accounting estimates and judgements: Note 34.

Other information

The directors are responsible for the other information. The other information comprises all of the information presented in the Annual Report and Financial Statements 2022 (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 Banking Act (Cap. 371) and the Maltese Companies Act (Cap. 386), 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 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 Bank or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing 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 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 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, future events or conditions may cause the Bank to cease to continue as a going concern.
- 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.

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 Izola Bank p.l.c. for the year ended 31 December 2022, 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 financial statements, 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 financial statements, 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 XHTML format.
- Examining whether the Annual Financial Report has been prepared in XHTML format.

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 2022 has been prepared in XHTML format in all material respects.

Other reporting requirements

The *Annual Report and Financial Statements 2022* 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 2022* and the related Directors' responsibilities	**Our responsibilities**	**Our reporting**
Directors' report 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 Bank 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.	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.
Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance The Capital Markets 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	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 Bank 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 Markets Rules 5.97.4 and 5.97.5, giving an indication of the nature of any such misstatements.	In our opinion, the Statement of Compliance has been properly prepared in accordance with the requirements of the Capital Markets Rules issued by the Malta Financial Services Authority. We have nothing to report to you in respect of the other responsibilities, as explicitly

Principles of Good Corporate Governance within Appendix 5.1 to Chapter 5 of the Capital Markets Rules. The Statement's required minimum contents are determined by reference to Capital Markets Rule 5.97. The Statement provides explanations as to how the Bank has complied with the provisions of the Code, presenting the extent to which the Bank 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 also required to assess whether the Statement of Compliance includes all the other information required to be presented as per Capital Markets 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 Bank's corporate governance procedures or its risk and control procedures.

stated within the *Other information* section.

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.

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.

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 Markets Rules to review the statement made by the directors that the business is a going concern together with supporting assumptions or qualifications as necessary.	We have nothing to report to you in respect of these responsibilities.

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 26 March 2021. Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 2 years.

PricewaterhouseCoopers
78, Mill Street
Zone 5, Central Business District
Qormi
Malta

Fabio Axisa
Partner

26 April 2023

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INTRODUCTION

Background to Pillar 3 disclosures

The objective of Basel III Pillar 3 is to improve market discipline through effective public disclosure and to complement requirements under Pillar 1 and Pillar 2. To that end, Pillar 3 introduces additional public disclosure requirements and represents an increase in the amount of information made publicly available by banks and investment firms regarding capital structure, capital adequacy, risk management and risk measurement.

Nature of Disclosures

This document serves as the Basel III Pillar 3 disclosures of Izola Bank p.l.c. in accordance with the Malta Financial Services Authority ('MFSA') Banking Rule 7 (BR07). Banking Rule BR/07 follows the disclosure requirements of Directive 2013/36/EU (Capital Requirements Directive — Pillar 1) and EU Regulation No 575/2013 (Capital Requirements Regulation — Pillar 2) of the European Parliament and of the Council of 26 June 2013.

The Annual Report of Izola Bank p.l.c. has been filed with the MFSA Registry of Companies and the MFSA Banking Unit. These Pillar 3 disclosures refer to the financial year ended 31st December 2022 and have been included in the Annual Report for 2022.

The Bank has in place a formal policy to comply with the disclosure requirements laid down in Banking Rule BR/07/2018. The Directors, after due consideration of the size and complexity of the Bank, do not feel it necessary to produce Pillar 3 disclosures more frequently than annually. Banking Rule BR/07 requirements are incorporated in this document if they are deemed relevant for the Bank.

As outlined in 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 International Financial Reporting Standards ('IFRS') as adopted by the EU. The Bank's management is responsible for the verification of these Pillar 3 disclosures. The Bank, through its internal verification process, is satisfied that these disclosures are presented fairly.

1 RISK MANAGEMENT OBJECTIVES AND POLICIES

The principal risks to which Izola Bank p.l.c. is exposed are business, credit concentration, operational and interest rate risk in the non-trading book. Counterparty risk is also recognised as important.

Business risk

Business risk is the risk that the Bank may not be able to carry out its business plan or its desired strategy and could therefore suffer losses if its income falls. This is a risk that every business faces. The two main contributors to the business risk arise from the Bank's dependence on the Group as its anchor client and the general business environment in Malta and Belgium. There are no specific mitigating factors though it is to be noted that the Group is itself diversified and has a large number of clients and suppliers which in turn helps to diversify the underlying risk.

1 RISK MANAGEMENT OBJECTIVES AND POLICIES *(continued)*

Concentration risk

Concentration risk arises as a result of the concentration of exposures within the same category, whether it is geographical location, product type, industry sector or counterparty type. These risks are managed through adherence to Board approved lending criteria.

The Bank recognizes that credit concentration risk is present in the Bank's factoring business in view of the fact that factored debtors are mainly active in the property, building and construction sector in Belgium and to the retail sector in Malta. Credit concentration risk is mitigated by a comprehensive credit insurance policy covering credit risks arising from the Bank's factoring exposures in Belgium and Malta. Furthermore, the diversification of the Bank's business model is also an important contributor towards reducing this risk.

The credit risk concentration to the factored receivables in Malta is mitigated through the dispersion of debtors combined with security over the underlying asset. Furthermore, the Bank retains insurance for credit risk on a major part of its invoice factoring business. As the Bank continues its growth path, concentration risk is reduced as each new product or business line launched reduces the overall scale of previous concentrations.

Operational risk

Operational risk is associated with the Bank's internal processes and systems and the potential for these not to function properly. Through implementing a robust internal control system, the Bank is able to mitigate many of the identified risks. The Bank also maintains third party insurance to cover certain risk events such as computer fraud and cybersecurity risk. Regular reporting on operational risk is made to the Audit and Risk Committee.

Interest rate risk in the banking book (IRRBB)

Market risk incorporates the loss of income which in the Bank's case would be as a result of changes to interest rates. Izola Bank p.l.c. limits this exposure to movements in interest rates by matching, as much as possible, its advances to deposits in the same maturity bands.

2 BOARD AND COMMITTEES STRUCTURE

The Bank's Board of Directors comprises seven non-executive directors and one executive director and meets at least quarterly throughout the year. In addition, the Board delegates specific responsibilities to the Remuneration and Nomination Committee, the Audit and Risk Committee, the Credit Committee, the Strategy Committee and the Asset and Liability Management Committee (ALCO).

Remuneration and Nomination Committee

Composition: *The Remuneration and Nomination Committee comprises three non-executive directors.*

Main Functions: The Remuneration and Nomination Committee is tasked with delving into the detail of oversight of remuneration and nomination practices.

Frequency: This Committee meets at least once a year.

Credit Committee

Composition: The Credit Committee is made up of two non-executive independent directors and the Chief Executive Officer.

Main Functions: The Credit Committee considers credit applications and keeps credit limits under review.

Frequency: The Committee meets at least four times a year.

2 BOARD AND COMMITTEES STRUCTURE *(continued)*

Audit and Risk Committee

Composition: The Audit and Risk Committee comprises three non-executive independent directors.

Main Functions: The primary purpose of the Audit and Risk Committee is to protect the interests of the Bank's shareholders and assist the directors in conducting their role effectively so that the Bank's decision-making capability, the accuracy of its reporting and financial results and the Bank's risk management processes are maintained at a high level at all times.

The Committee provides independent review, monitoring, and assessment of:
- the integrity of the annual financial statements
- the effectiveness of management's system of internal control
- the effectiveness of the Bank's risk management processes
- the Bank's compliance with applicable laws and regulations
- the Bank's ethical and business standards
- the appointment of the Bank's internal and external auditors

Frequency: The Committee meets at least four times a year.

Strategy Committee

Composition: This Committee is made up of two non-executive directors and the Chief Executive Officer.

Main Functions: The Committee is responsible for making recommendations to the Board of Directors on the Bank's business model and forward-looking strategy, taking into consideration the risks and opportunities related to various strategies. The Committee is also responsible for analysing the implementation of the business model and strategy or any changes thereof, including any potential ICT consequences.

Frequency: The Committee meets at least once a year.

Asset and Liability Management Committee (ALCO)

Composition: This Committee is made up of the Chief Executive Officer, the Head of Finance and Treasury and the Senior Finance and Treasury Manager.

Main Functions: The Asset and Liability Management Committee:
- monitors the Bank's financial performance, and reviews and manages financial risks in accordance with Bank policies;
- manages the Bank's balance sheet in respect of the adequate matching of assets and liabilities, asset mix, liabilities and balance sheet growth;
- formulates a forward-looking strategy for the Bank in terms of the mix of assets and liabilities given its expectations of the future and the potential consequences of interest rate movements, liquidity constraints, foreign exchange exposure and capital adequacy.

Frequency: The Committee meets at least four times a year.

3 OWN FUNDS

During the year ended 31 December 2022, the Bank complied with all the externally imposed capital requirements to which it was subject. The following table summarises the composition of the Bank's regulatory capital as reported to the MFSA as at 31 December 2022.

	2022 €
Common Equity Tier 1 (CET1) Capital: instruments and reserves	**22,704,070**
Paid up capital instruments	**29,032,675**
Retained Earnings	**916,452**
Accumulated other comprehensive income (and other reserves)	**(7,245,057)**
CET1 Capital before regulatory adjustments	**22,704,070**
Regulatory deductions and adjustments	
Deductions related to intangible assets	**(1,399,036)**
Tier 2 Capital	
Capital instruments and subordinated loans eligible as T2 Capital	**14,000,000**
Total Own Funds	**35,305,034**

Composition of Own Funds

i. Ordinary Shares: At 31 December 2022, the authorised share capital comprised 120,000,000 ordinary shares of €0.50 each. All shares in issue are fully paid up. 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 shareholders' meetings of the Bank.

ii. Accumulated other comprehensive income: this includes the balance available for distribution to the shareholders.

iii. Capital Contribution: this represents a contribution by the shareholders to the distributable reserves of the Bank.

iv. Fair value reserve: this represents fair value movements on investments classified at Fair Value through Other Comprehensive Income (FVOCI), net of tax.

v. Revaluation Reserve: this represents reserves arising from the revaluation of tangible fixed assets, net of tax.

4 CAPITAL ADEQUACY AND LIQUIDITY

4.1 Internal Capital Adequacy Assessment Process (ICAAP)

ICAAP Methodology

The Bank's latest ICAAP report is based on 31st December 2022 figures.

The Bank has chosen to base its ICAAP on the results of the Pillar 1 calculation with additional Pillar 2 risks – business risk, credit concentration and interest rate risk in the banking book – assessed separately through stress testing and added to Pillar 1. The Bank has also further analysed its operational risk exposure through stress testing in order to determine whether an additional Pillar 2 charge for operational risk may be necessary.

4 CAPITAL ADEQUACY AND LIQUIDITY *(continued)*

4.1 Internal Capital Adequacy Assessment Process (ICAAP) (continued)

The Bank's ICAAP also 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 plan.

In order to produce a capital plan, the Bank's ICAAP contains calculations of the capital resources requirement (effectively the minimum capital required) for each of the three years using the standardised approach for credit risk and the basic indicator approach for operational risk.

Under the standardised approach for credit risk, the Bank applies a risk weighted asset value to each of its exposure classes and provides 8% of that risk weighted asset value as the minimum capital requirement for credit risk.

Under the basic indicator approach for operational risk, the Bank calculates its average net income over the previous three years and provides 15% of that average net income as the minimum capital requirement for operational risk.

4.2 Credit Risk Capital Requirements by Standardised Approach Exposure Class

Capital Requirement by exposure class as at 31 December 2022

	Capital Requirement
	€
Central Government or Central Banks	-
Institutions	455,982
Retail	5,644,751
Corporates	1,575,472
Exposures secured by Mortgages on Immoveable Property	1,932,691
Items associated with particularly high risk	1,587,759
Equities & Collective Investment Undertakings (CIUs)	395,966
Other	128,768
Total	**11,721,389**

4.3 Market Risk Capital Requirement

The market risk capital requirement of the Bank is not significant, comprising a foreign exchange risk charge of €19,010.

4.4 Operational Risk Capital Requirement

The gross income registered by the Bank in 2022, 2021 and 2020 amounted to €7,840,853, €6,751,938 and €5,941,863 respectively. The operational risk capital requirement for 2022 amounted to €1,026,733.

4 CAPITAL ADEQUACY *(continued)*

4.5 Calculation of minimum capital requirement and risk-weighted assets

	Statement of financial position valuie 2022	Risk weighted exposure 2022	Captial requirement 2022	Statement of financial position valuie 2021	Risk weighted exposure 2021	Captial requirement 2021
	€	€	€	€	€	€
On balance sheet assets						
Balance with Central Bank of Malta and cash	**17,598,287**	**-**	**-**	16,193,768	-	-
Financial investments	**91,550,927**	**26,646,809**	**2,131,745**	117,280,712	25,453,264	2,036,261
Loans and advances to banks	**10,214,993**	**2,042,999**	**163,440**	25,420,282	5,084,056	406,725
Factored receivables	**118,363,724**	**69,192,297**	**5,535,384**	95,051,834	45,046,468	3,603,717
Loans and advances to customers	**160,329,282**	**33,694,541**	**2,695,563**	131,369,341	78,255,925	6,260,474
Property and equipment	**11,712,225**	**11,712,225**	**936,978**	12,565,395	13,044,225	1,043,538
Intangible assets	**1,975,593**	**-**	**-**	1,774,370	-	-
Prepayments and accrued income	**3,823,311**	**3,228,492**	**258,279**	2,764,749	2,776,609	222,129
	415,568,342	**146,517,363**	**11,721,389**	402,420,451	169,660,547	13,572,844
Off balance sheet items						
Commitments	**185,068,135**			92,738,305		
Credit risk capital requirement		**146,517,363**	**13,572,843**		169,660,547	13,572,844
Foreign exchange risk capital requirement		**237,626**	**19,010**		1,195,963	95,677
Operational risk capital requirement		**12,834,159**	**1,026,733**		11,970,399	957,632
Total capital requirement		**159,589,148**			182,826,909	
Total Tier 1 Capital	**21,305,033**			30,217,389		
Subordinated debt	**14,000,000**			-		
Total own funds	**35,305,033**			30,825,934		
CET 1 ratio			**13.35%**			16.5%
Capital adequacy ratio			**22.12%**			16.5%

4 CAPITAL ADEQUACY AND LIQUIDITY *(continued)*

4.6 Liquidity Coverage Ratio

The Liquidity Coverage Ratio (LCR) metric measures a bank's liquidity risk profile based on the stock of unencumbered high-quality liquid assets (HQLA) which can be easily converted in financial markets at no, or little loss of value, in relation to the estimated total net cash outflows over a 30-calendar day stress scenario.

The goal of this stress test is to ensure that the institution can meet its liquidity needs for a 30-day hypothetical financial stress scenario. The LCR is governed by the Liquidity Coverage Ratio Delegated Act (EU) 2015/61 which became a minimum regulatory standard from 1 October 2015. As of January 1, 2022, the minimum LCR regulatory limit required for banks is 100%.

The LCR ratio as at 31 December 2022 was 725% (2021: 1,320%). As at 31 December 2022 and 2021 and during the respective financial periods, the LCR ratio was within both the regulatory minimum and the risk appetite set by the Bank.

4.6 Leverage Ratio

The Leverage Ratio (LR) tool was designed by the Basel Committee on Banking Supervision (BCBS) as an easy and understandable metric to mitigate against risks of excessive leverage. This measure was introduced to serve as a complementary tool with other approaches to risk-based capital requirements, and the European Banking Authority (EBA) established, by Regulation (EU) No 1093/2010 of the European Parliament and of the Council, that the leverage ratio requirement should be calibrated at 3%.

The leverage ratio is calculated as the capital measure, which shall be the Tier 1 Capital according to Article 25 of the CRR, divided by the total exposure measure comprising of both on and off-balance sheet exposures, net of any deductions applied directly to Tier 1 Capital.

The leverage ratio as at 31 December 2022 was 5.6% (2021: 8.0%). As at 31 December 2022 and 2021 and during the respective financial periods, the leverage ratio was within both the regulatory minimum and the risk appetite set by the Bank.

5 CREDIT RISK

5.1 *Credit risk*

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to the financial instrument fails to meet its contractual obligations. For risk management reporting purposes, the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk).

The Bank follows standards, policies and procedures established by the Board of Directors for the control and monitoring of all risks. The Board of Directors has delegated the responsibility for the management of credit risk to the Credit Committee. The Bank's management is responsible for the oversight of the Bank's credit risk. The Bank's credit risk policies and procedures are reviewed regularly through internal audit.

5.2 *Definition of 'past due' and 'impaired' for accounting purposes*

Impaired factored receivables

These comprise factored receivables for which the Bank determines an expected credit loss based on the probability that it will be unable to collect all principal and interest due according to the contractual terms of the factored receivables agreements.

Allowance for impairment on factored receivables

	2022	2021
	€	€
Factored receivables – gross	**119,269,112**	95,827,647
12-month ECL	**221,559**	93,303
Lifetime ECL	**683,829**	682,510

Table 5.2 Neither past due nor impaired loans and securities

	2022	2021
	€	€
Loans and advances to customers	**157,680,103**	127,052,013
Loans and advances to banks	**10,214,993**	25,420,382
Investment securities	**91,550,927**	117,280,712
	259,446,023	269,753,107

5 CREDIT RISK *(Continued)*

5.3 Description of approaches and methods adopted for determining value adjustments and provisions

Allowances for impairment

The Bank establishes an allowance for expected credit losses that represents its estimate of expected losses in its factored receivables and loans & advances portfolios. The main components of this allowance are outlined in Note 4.4 of the financial statements.

	2022	2021
	€	€
Allowance for expected credit losses on factored receivables	**905,388**	775,813
Allowance for expected credit losses on loans and advances	**833,691**	328,986

Table 5.3 Total period end and average exposures after individual impairment and prior to credit risk mitigation by exposure class.

	Exposure as at 31/12/2022 € 000s	Average Exposure for period to 31/12/2022 € 000s
Central Government or Central Banks	85,985	90,234
Institutions	28,499	18,305
Retail	111,755	95,555
Corporates	82,522	89,876
Exposures secured by Mortgages on Immoveable Property	67,076	54,330
Items associated with particularly high risk	15,907	14,403
Equities & Collective Investment Undertakings (CIUs)	4,208	1,920
Other	19,616	17,997
Total	**415,568**	**382,620**

	Malta € 000s	Europe € 000s	Total € 000s
Central Government or Central Banks	84,447	1,538	85,985
Institutions	24,178	4,321	28,499
Retail	79,392	32,363	111,755
Corporates	38,424	44,098	82,522
Exposures secured by Mortgages on Immoveable Property	66,396	680	67,076
Items associated with particularly high risk	15,907		15,907
Equities & Collective Investment Undertakings (CIUs)	4,135	73	4,208
Other	19,033	583	19,616
Total	**331,912**	**83,656**	**415,568**

5 CREDIT RISK *(Continued)*

5.3 Description of approaches and methods adopted for determining value adjustments and provisions (continued)

Table 5.5 Distribution of the exposures by industry/counterparty type

	Central Government or Central Banks	Institutions	Corporates	Exposures secured by Mortgages on Immoveable Property	Equities & Collective Investment Under-takings (CIUs)	Retail	Items associated with particularly high risk	Other	Total
	€ 000s	€ 000s	€ 000s	€ 000s	€ 000s	€ 000s	€ 000s	€ 000s	€ 000s
Construction			1,024	9,687		16,077	1,889		28,677
Households and individuals				7,486		70,634			78,120
Monetary Financial Institutions	15,891	28,499			4,208				48,598
Manufacturing			6,975			7,832			14,807
Real estate, renting and business activities			1,899	12,716		2,967	6,448		24,030
Sovereigns	70,094								70,094
Wholesale and retail trade			21,332	9,889		7,254			38,475
Other sectors			51,292	27,298		6,991	7,570	19,616	112,767
Total	**85,985**	**28,499**	**82,522**	**67,076**	**4,208**	**111,755**	**15,907**	**19,616**	**415,568**

Table 5.6 Residual Maturity Breakdown of the exposures

	< 1 year	1 – 5 years	> 5 years	Total
	€ 000s	€ 000s	€ 000s	€ 000s
Central Government or Central Banks	24,779	23,011	38,195	85,985
Institutions	28,499			28,499
Retail	28,310	42,825	40,620	111,755
Corporates	36,709	28,933	16,880	82,522
Exposures secured by Mortgages on Immoveable Property	19,303	18,986	28,787	67,076
Items associated with particularly high risk	9,608	6,299		15,907
Equities & Collective Investment Undertakings (CIUs)	4,208			4,208
Other	311	19,305		19,616
Total	**151,727**	**139,359**	**124,482**	**415,568**

5 CREDIT RISK *(Continued)*

5.4 Past Due Exposures and Impaired Assets

Table 5.7 Impaired, past due exposures - provisions by industry sector

Standardised exposure classes	Expected Credit Losses € 000s	Charged to income statement in the year ended 31 December 2022 € 000s
Central Government or Central Banks		
Institutions		
Retail	116	101
Corporates	1,600	568
Items associated with particularly high risk		
Exposures secured by Mortgages on Immoveable Property	70	
Equities & Collective Investment Undertakings (CIUs)		
Other		
Total	**1,786**	**669**

Table 5.8 Impaired, past due exposures - provisions by geographic area

Standardised exposure classes	Expected Credit Losses € 000s	Charged to income statement in the year ended 31 December 2022 € 000s
Malta	996	640
Europe	790	29
Rest of the World		
Total	**1,786**	**669**

Table 5.9 Movement in allowances for impaired and past due exposures and provisions

	Individual & collective provisions € 000s
Opening balance	1,117
Expected credit loss increase	669
Closing balance	**1,786**
Amounts written off	262

6 STANDARDISED APPROACH TO CREDIT RISK

6.1 Exposure to Institutions

Fitch Rating Agency is the External Credit Assessment Institution (ECAI) used to rate exposures to institutions. The external ratings are mapped to the prescribed credit quality assessment scale that in turn produces standard risk weightings in line with Article 119 of the Credit Requirements Regulations (CRR).

The following table shows the exposure values before and after Credit Risk Mitigation associated with the credit quality step under the Standardised Approach.

Table 6.1 Institutions

Credit Quality Step	Risk Weight	Regulation - Ratings	Exposure	Exposure After CRM
			€ 000s	€ 000s
1	20%	Art. 121(3) - Fitch AAA	28,499	5,700

6.2 Exposure to Central Government and Central Bank

Exposures to central government and central bank denominated and funded in the domestic currency of the central government and central bank are assigned a risk weight of 0% in line with Article 114(4) of the CRR.

Table 6.2 Central Government and Central Bank

Credit Quality Step	Risk Weight	Regulation - Ratings	Exposure	Exposure After CRM
			€ 000s	€ 000s
1	0%	Art. 114(4)	85,985	

6.3 Exposure to Retail & Corporates (including SMEs)

A large part of corporate exposures has a 0% risk weighting as it is cash secured. A number of corporate exposures are secured by real estate and are allocated a 35% or 50% risk weighting. The rest are allocated a 75% or 100% risk weighting as they are unsecured with a portion subject to a reduction by virtue of the application of the SME support factor.

Table 6.3 Corporates

Credit Quality Step	Risk Weight	Banking Regulation	Exposure	Exposure After CRM
			€ 000s	€ 000s
1	0%	Art. 400(1) (g)	54,154	-
2	35%	Art. 125(1) (a)	16,992	2,997
3	50%	Art. 126(1) (a)	50,119	21,161
4	75%	Art. 123 (a) (b) (c)	111,755	70,559
5	100%	Art. 122 (2)	86,500	19,693

7 REMUNERATION POLICY

The Board has established a Remuneration Policy the aim of which is to increase transparency when offering remuneration and benefits to the Bank's staff. More details concerning remuneration are provided with the remuneration report as part of the Annual Report 2022.

8 CREDIT RISK MITIGATION

8.1 Collateral

Analysis of collateral is disclosed in Note 4.3.7 of the Annual Report 2022.

Table 8.1 Exposure value covered by eligible financial collateral

	€ 000s
Central Government or Central Banks	19,256
Corporates	109,291
Retail	19,607
Total	**148,154**

9. CONCLUSION

This disclosure document has been prepared in accordance with the requirements of Banking Rule 7 issued by the Malta Financial Services Authority (MFSA).

Statement of Profit or Loss and Other Comprehensive Income

	2022	2021	2020	2019	2018
	€	€	€	€	€
Interest receivable and similar income	**13,087,771**	10,704,557	10,575,188	10,158,455	8,081,029
Interest payable and similar charges	**(5,412,645)**	(4,513,733)	(5,011,314)	(3,972,954)	(2,627,953)
Net interest income	**7,675,126**	6,190,824	5,563,873	6,185,501	5,453,076
Fee and commission income	**55,912**	(10,195)	66,892	62,351	33,658
Net trading income	**15,789**	31,168	64,717	97,656	(197,123)
Net (losses)/gains on disposal of financial investments measured at FVOCI	**(7,299)**	442,395	172,944	25,000	450,896
Other operating income	**101,325**	97,746	73,437	88,330	64,378
Other operating charges	**(7,309,512)**	(5,546,089)	(5,164,175)	(3,873,224)	(3,497,085)
Net impairment gain/(losses)	**(919,147)**	(385,692)	(172,797)	(90,400)	(134,698)
(Loss)/Profit before tax	**(387,806)**	820,157	604,892	2,495,214	2,442,498
Income tax expense	**103,587**	(372,176)	(219,671)	(1,034,473)	(934,319)
(Loss)/Profit for the year	**284,219**	447,981	385,221	1,460,741	1,508,179
Other comprehensive income for the year, net of income tax	**(9,596,928)**	(1,251,797)	27,507	875,549	(245,292)
Total comprehensive income for the year	**(9,881,147)**	(803,816)	412,727	2,336,289	1,262,887
Earnings per share	0c49	0c77	96c	365c	377c

Appendix II – Five-Year Summary

Statement of Financial Position

	2022	2021	2020	2019	2018
	€	€	€	€	€
ASSETS					
Balances with Central Bank of Malta and cash	**17,598,287**	16,193,768	18,612,618	39,087,309	2,513,413
Investments	**91,550,927**	117,280,712	109,304,630	81,369,795	42,111,712
Loans and advances to banks	**10,214,993**	25,420,282	22,695,594	40,549,407	18,788,220
Factored receivables	**118,363,724**	95,051,834	99,155,608	105,412,199	86,260,140
Other loans and advances to customers	**160,329,282**	131,369,341	121,555,833	86,522,549	74,286,614
Property and equipment	**11,712,225**	12,565,395	11,994,449	11,618,961	10,264,853
Intangible assets	**1,975,593**	1,774,370	1,550,091	1,633,259	1,653,214
Other assets	**3,181,811**	1,971,720	3,603,758	1,576,048	1,275,436
Deferred tax asset	**5,920,924**	388,435	-	-	-
Current tax asset	**641,499**	793,029	824,359	562,378	-
Total assets	**421,489,265**	402,808,886	389,296,940	368,331,905	237,153,602
LIABILITIES					
Balance owed to Central Bank of Malta	**40,000,000**	55,000,000	35,000,000	-	13,000,000
Deposits from banks	**275,815**	274,715	250,576	250,322	250,068
Deposits from customers	**335,660,870**	297,780,509	304,384,729	319,737,813	177,157,086
Debt securities in issue	**16,820,322**	11,940,167	11,923,078	11,905,989	11,888,899
Deferred tax liabilities	**436,414**	558,446	845,309	777,023	560,484
Current tax payable	**-**	-	-	-	802,074
Accruals	**4,759,914**	3,975,122	2,809,505	1,989,742	1,410,264
Total liabilities	**397,953,335**	369,528,959	355,213,197	334,660,889	205,068,875
EQUITY					
Called up share capital	**29,000,000**	10,000,000	10,000,000	10,000,000	10,000,000
Property revaluation reserve	**2,977,302**	3,521,238	3,521,238	3,696,144	2,629,651
Fair value reserve	**(10,295,141)**	(612,547)	639,250	436,837	627,781
Depositor compensation scheme reserve	**831,860**	1,288,168	1,707,717	628,571	409,640
Reserve for general banking risk	**72,782**	45,091	3,860	3,860	6,470
Capital contribution	**32,675**	17,032,675	17,032,675	17,032,675	16,032,675
Retained earnings	**916,452**	2,005,302	1,179,003	1,872,929	2,378,510
Total equity attributable to equity holders of the Bank	**23,535,930**	33,279,927	34,083,743	33,671,016	32,084,727
Total liabilities and equity	**421,489,265**	402,808,886	389,296,940	368,331,905	237,153,602
Memorandum items commitments	**185,068,135**	92,738,305	96,000,451	71,868,667	88,918,753

Statement of Cash Flows

	2022	2021	2020	2019	2018
	€	€	€	€	€
Net cash from operating activities	**(30,370,480)**	9,818,579	(8,670,571)	99,049,941	(17,094,321)
Cash flows from investing activities					
Payments to acquire property, equipment and intangible assets	**(2,478,688)**	(1,639,455)	(1,022,615)	(683,999)	(559,531)
Proceeds from disposal of property	**2,204,000**				
Payments to acquire investments	**(40,740,036)**	(85,996,927)	(89,109,086)	(50,641,277)	(9,412,713)
Proceeds from disposals of investments	**51,362,776**	76,537,399	59,299,332	10,672,792	24,129,036
Interest received from financial investments	**1,612,389**	2,066,104	1,529,179	1,227,372	949,252
Dividend received	**-**	-	-	-	199,411
Payments on investments which are traded but not yet acquired	**-**	-	(1,500,000)	-	-
Net cash used in investing activities	**11,960,441**	(9,032,879)	(29,118,187)	(39,425,112)	15,305,456
Cash flows from financing activities					
Proceeds from issue of debt securities	**13,633,597**	-	-	-	-
Redemption of debt securities	**(8,814,000)**	-	-	-	-
Dividends paid to shareholders	**-**	-	-	(1,750,000)	(2,150,000)
Net capital contribution received	**-**	-	-	1,000,000	3,500,000
Interest and premium paid on debt conversion	**(284,663)**	-	-	-	-
Interest paid on debt securities	**(540,000)**	(540,000)	(540,000)	(540,000)	(540,000)
Net cash from / (used in) financing activities	**(3,994,934)**	(540,000)	(540,000)	(1,290,000)	810,000
Net movement in cash and cash equivalents	**25,555,573**	245,700	(38,328,758)	58,334,829	(978,865)

Accounting Ratios

	2022	2021	2020	2019	2018
	%	%	%	%	%
Net interest income and other operating income to total asset	**1.86**	1.68	1.53	1.75	2.45
Operating expenses to total assets	**1.91**	1.47	1.37	1.08	1.42
Profit before tax to total assets	**(0.09)**	0.20	0.16	0.68	1.03
Pre-tax return on capital employed	**(1.29)**	2.82	2.14	8.63	8.60
Profit after tax to equity	**(1.21)**	1.35	1.13	4.34	4.70

Directors' interest in the share capital of the Bank or in any related company as at 31 December 2022

No director has a direct beneficial or non-beneficial interest in the share capital of the Bank.

Magdalena De Roeck and Caroline Van Marcke have an indirect beneficial interest in the shareholding of the Bank through their indirect shareholding in Carlenco Finance NV, a company registered in Belgium with registration number 0755.471.533.

Furthermore, Magdalena De Roeck and Caroline Van Marcke are also directors of IBL I Limited and IBL T Limited and other companies forming part of the Group.

Shareholders holding 5% or more of the Share Capital as at 31st December 2021

IBL I Limited	Ordinary	135	100% Paid up	€0.50
IBL T Limited	Ordinary	53,999,865	100% Paid up	€0.50

As at date of publication of the annual report, no changes were effected to the shareholding structure.

izola Bank

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