Habib Bank AG Zurich

Habib Bank Zurich plc

Annual Report 2018


Canada
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UAE
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Contents

Corporate Information

Board of Directors

Mr Muhammad H. Habib (Chairman)	Non-Executive Director
Mr Carey Leonard	Independent Non-Executive Director
Mr Gerald Arthur Gregory	Independent Non-Executive Director
Mr Anjum Iqbal	Non-Executive Director
Mr Rajat Garg	Non-Executive Director
Mr Satyajeet Roy (CEO)	Executive Director
Mr Masum Billah (COO)*	Executive Director

Board Committees

Risk Committee		Audit & Compliance Committee	
Mr Carey Leonard	Chairman	Mr Gerald Arthur Gregory	Chairman
Mr Gerald Arthur Gregory	Member	Mr Carey Leonard	Member
Mr Anjum Iqbal	Member	Mr Anjum Iqbal	Member
Mr Rajat Garg	Member	Mr Rajat Garg	Member

Management Committees

Executive Committee (EXCO)
Asset and Liability Committee (ALCO)
Audit, Risk and Compliance Committee (ARCC)
Country Credit Committee (CCC)
Operations and Technology Committee (OTCO)
Human Resource Committee (HRC)

Company Secretary

Taylor Wessing
5 New Street Square
London EC4A 3TW

Registered Office

Habib Bank Zurich plc
Habib House
42 Moorgate
London EC2R 6JJ

Auditors

KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London E14 5GL

Legal Advisors

Saleem Malik
40 Eagle Lane
Snaresbrook
London E11 1PF

* Subject to regulatory authorisation

Chairman's Message

On behalf of the Board of Directors ("the Board") of Habib Bank Zurich plc, I am delighted to introduce this year's Annual Report and Financial Statements.

By the Grace of God, 2018 was another successful year with continued growth across the business. In what has been an environment challenged by political and economic uncertainties, the Bank increased its customer deposits and loan portfolio, and recorded balance sheet growth of 5%. The annual performance includes higher yields on interest and investment income, and a reduction in the non-performing book thereby reflecting a robust and controlled framework.

The key attributes of this performance were a well-articulated strategy, organic growth and personalised relationship management. When the market appeared to be moving towards remote service delivery, we maintained a balance between evolving preferences and a high-contact relationship model, which enabled a better understanding of the needs of our customers and garnered agility in our decision making to protect their best interests.

The UK is going through a major change due to its impending exit from the European Union (EU). This has led to economic uncertainty, which is expected to continue into 2020. We take market risk seriously and while we do not have any direct exposure to the EU, we will continue to monitor ongoing developments to mitigate any potential risk to the Bank and its customers.

We also feel that cyber security and operational resilience are a major concern for the financial services industry. The wider business community has faced these threats on an increasing scale in recent times. To address this, we strive to stay vigilant and abreast of technological and cyber security advancements and continue to invest in operational infrastructure to protect the interests of our customer and to ensure seamless service to them.

The Board's responsibility to provide strong, effective governance and to maintain an appropriate balance of skill and experience is of paramount importance. I believe that with the broad cumulative experience of the members, the Board is well placed to provide effective guidance in the delivery of its strategy.

During the year the Board worked closely with the CEO and the Executive team to ensure that the Bank remains aligned with its business strategy, regulatory expectations and best practices. The Board is reassured that the Executive Management team remains focused on good governance and organisational culture; having robust controls; closely monitoring the customer journey; and staying on course in the areas of strength, strategy and a strong operational infrastructure.

The UK and the banking sector continue to face an uncertain environment with ongoing challenges around Brexit, weaker economic growth, a slowdown in the housing market, an ever-changing regulatory landscape and technological innovation.

Based on our target market, focused strategy and proven business model, we firmly believe that there is a continued demand in the market for our services. Consistent with our operational capabilities, the small and medium-sized enterprise ("SME") segment, especially the South Asian diaspora, provides a significant opportunity for growth in the UK. As a Bank driven by a business model with customer experience as a strong focus, built on a robust governance and control framework and backed by shareholders' long-term view of the UK franchise, we are confident of meeting the challenges of economic uncertainty and continuing to deliver the Board's primary objectives of maintaining financial soundness, profitability and achieving sustainable growth with low risk.

I am also pleased to confirm that the Bank will be offering its Islamic Banking proposition 'Sirat' in 2019. This project is aligned to our customer-centric approach and aims to meet the expectations of our target market. The Habib Bank AG Zurich Group offers Islamic banking products and services in three other global locations and the UK will be the latest addition for further diversification and growth.

I would like to thank our customers for their support and patronage during our journey and hope for their continued support in the future.

I would also like to thank our Board of Directors, the Executive Management team and all the employees of the Bank for their consistent hard work and dedication.

Muhammad H. Habib
Chairman

Strategic Report

The Directors are pleased to present the Strategic Report for the year ended 31 December 2018 for Habib Bank Zurich plc (the "Bank"). The Strategic Report is a part of the Bank's Annual Report and Financial Statements.

Overview

The purpose of the Strategic Report is to provide stakeholders with a fair review of the Bank's strategic objective, business performance in the current challenging environment and the Bank's position at the end of the reporting period. This report includes a description of the key risks associated with the Bank's business and an analysis of its overall business and financial performance and major developments during the reporting period.

Principal activity

The Bank offers standard commercial, SME and retail products combined with personalised relationship management. Service is delivered through the branch managers, specialist lending relationship managers, selected intermediaries and personal bankers for deposit mobilisation. The customer takes comfort in continuity with a relationship manager and quick turnaround on their requests as well as continued access to the decision makers at the Bank.

The products offered to its customers include retail banking, saving accounts and deposits, commercial lending, trade finance, internet deposits, cash management and treasury services. The Bank is in the process of launching an Islamic Window facility to offer selected Shariah-compliant banking products.

Strategy and objectives

The Bank's strategy is built on providing banking services to SMEs and affluent individuals. The brand value is grounded in 'Service with security'. Accordingly, the Bank is focused on its niche to deliver excellent service to its customers.

The Bank's primary customer base is family-owned and managed businesses with a focus on South Asian communities. These traditionally mercantile communities are known for their business and entrepreneurial traits. The key attribute of this segment is generational continuation and expansion of their business interests across generations. We feel proud in serving second and third and sometimes fourth generational customers, which is a reflection of our strong bonding with our customer base.

The Bank's target market in the UK is frequently geared towards property investments, trading activities, services and small-scale manufacturing. Our customers' banking needs are centred on conventional commercial banking products.

The Bank differentiates itself from the competition based on its relationship management model, which offers customised solutions according to customers' individual needs as opposed to the 'one size fits all' packaged product and distant customer assistance model of most high-street banks for the SME segment. The Bank is a niche player focused on commercial banking, having a natural fit with the family owned and managed enterprises of South Asian origin. This is a substantial and growing segment, which provides an opportunity for the Bank to build a sustainable business model.

Business model

The Bank's business model is built on delivering high-quality products and services and taking a long-term view on building customer relationships. The model is geared towards focusing on selected segments to deliver their strategic objectives.

The Bank's core value of 'Service with security' has led to a natural longevity in customer relationships, which are cross-generational and cross-border, strengthening the Bank's reputation as a businessman's bank. Owing to its history from the Indian subcontinent, and based on the intrinsic value of the Bank as a family-owned conservative financial institution, customers identify the brand with security and trust.

The Bank offers product lines through a conveniently located network of eight branches in London, Manchester, Leicester and Birmingham. It also offers fixed-term bonds accessible directly through the web-based channel.

The Bank offers two main services – real estate finance and commercial banking. The Bank also offers regular cash management, trade finance and retail banking in line with customer needs. The Bank's product offering is comprised of buy-to-let finance, commercial loans, working capital finance, current accounts, savings accounts, notice accounts, fixed term deposits and treasury services.

In 2018, the Bank introduced another client acquisition channel by on-boarding selected intermediaries a well-established distribution network in the UK. The Bank has a dedicated team of relationship managers for managing this channel. This enables intermediaries to offer their clients our lending products and services, while maintaining full control of their personal client relationships.

Products offered through intermediaries comprise commercial lending, residential and commercial buy-to-let and mixed use buy-to-let mortgages, and are designed to be flexible and collaborative so that the Bank can adopt the most appropriate strategy for intermediaries and their clients.

Business review

2018 has been another year of robust financial performance for the Bank despite uncertainties around Brexit throughout the year. The Bank delivered balance sheet growth and successfully exceeded its profit targets set for the year 2018. The continued political and economic uncertainties owing to the outlook for the UK in 2019 are being keenly monitored through the Bank's committees. The Bank has no direct impact from Brexit as the majority of its business is domestic with no presence in the EU. However, a disorderly Brexit impacting the Bank's business through factors such as increase in competition, rising cost of funds and pressure on property prices cannot be ruled out. These risks are monitored at respective Board and Management Committee level.

The Bank continued to focus on maintaining a sustainable business model through proactive risk management, effective liquidity and capital management and meeting the requirements of the changing regulatory environment.

The highlight of the year was fresh loan disbursements of £121 million, which was 20% higher than in 2017. There was an increase in the proportion of disbursements to new businesses in 2018 which demonstrate the Bank's strong position among its peers and strength of its relationship team. The Bank continues to focus and grow responsible lending to broaden the customer base in line with its long-term strategy.

There was a substantial reduction in non-performing loans (NPLs), which decreased by £18 million either through settlement or moving to the performing category. This has been achieved by relentlessly working with customers in achieving a desired outcome that is most suitable to both parties.

The Bank was also steadfast on the continuous improvement of its customers service level and to further upscale the standard of culture and ethics within the organisation. The Bank remained focused on providing high levels of services to customers by meeting their business needs and financial objectives with consistency. This was enhanced through feedback received from customer surveys and the interaction of relationship managers with customers.

The main segments of the Bank's lending portfolio, comprising real estate and commercial lending, have shown sustained growth during the year. The Bank successfully maintained profitability momentum by increasing its lending book with high collateralised loans and placed great emphasis on the retention of existing clients.

The Bank has adopted International Financial Reporting Standard (IFRS) 9 "Financial Instruments" from 1 January 2018. The project led by the Habib Bank AG Zurich ("the Parent Bank") was completed with input and challenge from internal committees and external consultants. The approach taken by the Bank in developing expected credit loss ("ECL") models were proportionate to its size within the UK financial market, its relative lack of complexity as well as minimal volatility in its credit losses over the past five years.

The implementation of IFRS 9 resulted in a net decrease of £0.8 million in CET1 capital due to increase in impairment provision that was offset by the transitional relief of £0.3 million for the purpose of regulatory capital.

The UK has been a strong centre for Islamic Banking over a number of years with growing demand. The Bank sees the introduction of Islamic Banking as a natural fit within its product suite as alternate Islamic financing solutions are available for conventional real estate commercial and residential financing. The Parent Bank offers Islamic Banking through its branches and subsidiaries in other jurisdictions, which the Bank plans to offer to its UK customers. This would allow the Bank to benefit from group experience during the project implementation process.

Financial review

The Bank operating results for 2018 reflects sustained revenue growth despite growing pressure on net interest margins. Competition among banks to retain existing or to attract new customers and higher interest rate expectation from depositors has put additional pressure on margins.

The net operating income of the Bank increased by 3% in 2018 (£18.25 million compared to £17.73 million in 2017). Increases in the lending book and placement of funds in higher-yield debt securities resulted in improved interest income as compared to 2017. The Bank earned a net profit after taxation of £3.6 million in 2018 (2017: £4.40 million). The reduction in net profit was due to the receipt of a one-off insurance claim of £1.5 million in 2017.

The financial highlights for the 2018 are provided below:

Profit and Loss Analysis

	2018 (£)	2017 (£)
Operating Profit		
Net interest income	16,247,943	15,782,250
Net fee and Commission income	1,275,618	1,344,209
Net other income	605,791	598,977
Net operating income	**18,129,352**	**17,725,436**
Total operating expenses	(14,699,438)	(14,438,905)
Operating profit before impairment losses on loans and advances and tax expenses	**3,429,914**	**3,286,531**
Reversal of losses on loans and advances	925,714	178, 880
Receipt of insurance claim	-	1,526,105
Reversal / (impairment) losses on loans and advances	925,714	1,704,985
Profit before tax	**4,355,628**	**4,991,516**
Taxation	(767,549)	(590,937)
Profit after Tax	**3,588,079**	**4,400,579**

Total interest income of £16.3 million (2017: £15.8 million) includes the interest received from loans, return from the investment portfolio and interest on placement with banks. The 4% increase in interest income during 2018 was driven by disbursement of new loans of £121 million and recovery of interest income on settlement of NPLs. The disbursement during 2018 was the highest ever in the history of the Bank, reflecting its continued focus towards a strategy of new customers' loan origination and expanding business activities with existing customers.

Operating expenditure mainly represents staff and other operating expenses incurred during the year for the Bank's operations. The Bank managed its expenses cautiously and kept good control to look for efficiencies wherever possible. Overall increase in operating expenditure for the year 2018 was 2% as compared to 2017.

There were no unusual items in the operating expenses.

Balance sheet analysis

	2018 (£)	2017 (£)
Assets		
Loans and advances to customers	398,976,852	380,433,726
Balances with banks	125,741,023	125,260,531
Financial investments	103,384,856	90,906,053
Other	7,802,459	8,347,776
Total assets	**635,905,190**	**604,948,086**
Liabilities and equity		
Due to customers	523,493,393	496,852,369
Due to banks	17,398,649	15,865,126
Others	4,680,475	4,714,542
Subordinated liabilities	20,103,671	20,083,974
Tier 1 capital / equity	70,229,002	67,432,075
Total liabilities and equity	**635,905,190**	**604,948,086**

The growth of balance sheet volumes reflects the Bank's continued progress towards its strategic plans. Both deposits and advances grew over the 2017 position despite economic uncertainties due to Brexit. The impact of £121 million of customer disbursements was to an extent reduced by the early settlement of some of its existing regular loans during the year due to various factors such as the sale of property or refinancing. The Bank also successfully increasing earning assets by £29 million to £389 million as at 31 December 2018 (2017: £360 million), reducing the portfolio of NPLs by £18 million during 2018.

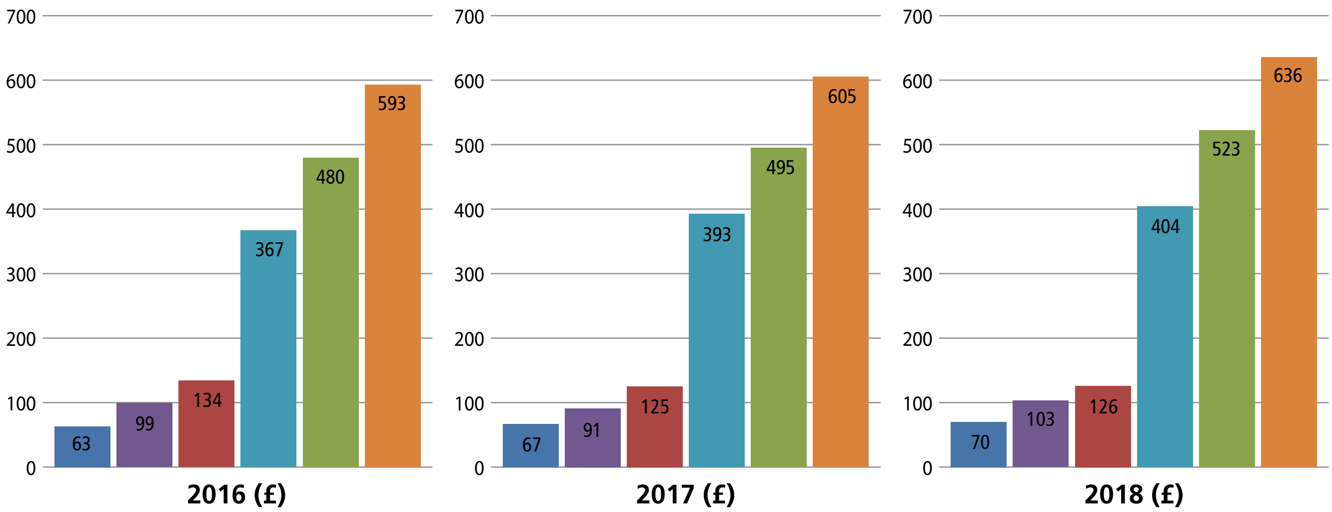
Investment income increased by 37% during 2018, which reflects the diversification of its investment portfolio in higher-yielding assets, in particular US dollar corporate bonds. The majority of the Bank's investment is in corporate bonds with a credit rating of A or above by the top three global credit rating agencies, which reflects its cautious approach.

Customer deposit growth of 5% mainly came through an increase in relationship-based deposits, a hallmark of the Bank's customer base.

The following chart provides the key performance of the bank for the last three years.

Assets and liabilities

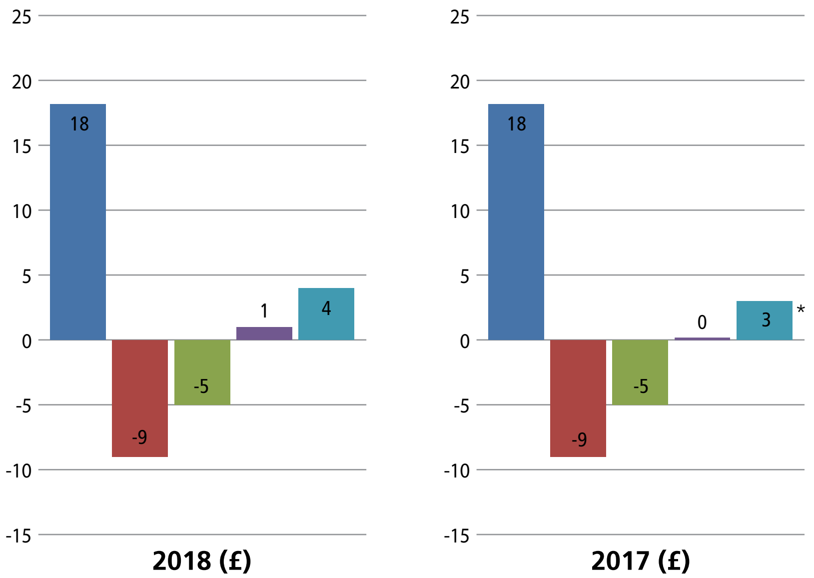
FINANCIAL HIGHLIGHTS



KEY

- Equity
- Balances with banks
- Due to customers
- Financial investments
- Gross loans and advances to customers
- Total Assets

Profit and loss



KEY

- Net operating income
- Staff cost
- Other operating expenses
- Depreciation and amortisation
- Profit before tax (PBT)

*2017 PBT excludes receipt of insurance claim

Capital structure

The Bank has a strong capital base with net equity of £70 million and a five-year subordinated loan of £20 million to support long-term asset growth and cover risks inherent to the business. Such strength in capital allows the Bank to deploy funds in areas that provide sustainable returns in line with the set objectives.

The regulatory capital base differs slightly from the amount reported above due to the different treatment of certain reserves. The Bank's regulatory capital and risk-weighted assets as at 31 December 2018 are summarised below:

		£ in million
Description	**2018**	**2017**
Share capital – Tier 1	60.00	60.00
Retained earnings – Tier 1	10.23	7.43
Subordinated loan – Tier 2	20.35	20.00
Risk weighted assets	387.18	359.94

The capital adequacy ratio as of 31 December 2018 was 23.30% (2017: 24.3%), which was in surplus of the regulatory requirements and internal management buffer.

The Bank's total capital requirement (TCR) is calculated as follows:

		£ in million
	2018	**2017**
Risk weighted assets (£ million)	387.18	359.94
Total capital requirement - TCR (£ million)	53.510	42.08
Capital		
Share capital - Tier 1 (£ million)	60.00	60.00
Retained earnings	10.23	7.43
Subordinated liabilities - Tier 2 (£ million)	20.35	20.00
	90.58	87.43
Excess capital over requirement (£ million)	**37.07**	**45.35**

Other key regulatory ratios

The Bank maintained sufficient high-quality liquid assets ("HQLA") against the net cash outflows over a 30-day horizon on a daily basis. The Bank maintains its liquidity coverage ratio ("LCR") above the regulatory threshold at all times as set out by the Prudential Regulation Authority ("PRA"). The Bank maintained LCR of 198% as at 31 December 2018 (2017: 236%) as compared to a 100% regulatory threshold. Reduction in LCR was mainly due to the increase in investments in financial institutions debt securities to earn better yields, which are not eligible to be included in the liquidity buffer calculation.

The Bank's leverage ratio as of 31 December 2018 was 10.11% (2017: 9.92%) as against the regulatory threshold of 3%.

Customer related contingent liabilities largely comprise trade finance business including letters of credit and guarantees and undrawn commitments.

Key performance indicators ("KPIs")

The Bank uses KPIs to measure and quantify the financial performance and progress against the strategic objectives. Keeping in view the Bank's business activities capital adequacy, liquidity monitoring and operations and technology risks have been considered more important by the Directors than to other risks.

The Bank continues to monitor these KPIs along with others to identify and monitor trends in the performance of the strategies employed.

Capital adequacy measures the Bank's capital strength, expressed as a ratio of total capital to risk-weighted assets. By having a mix of high-quality assets and capital free of deductions, the Bank maintained a capital adequacy ratio above the required regulatory requirement. The available capital resources of £90.18 million are considered sufficient with a view to support the business over a five-year period, which is demonstrated through the individual capital adequacy and assessment process ("ICAAP").

The ICAAP document summarises and demonstrates to the Board and to senior management that the Bank has adequate financial and capital resources to support its business and the risks attached to its business plan and model. The ICAAP also demonstrates the adequacy of non-financial resources (in the form of people, systems, policies and procedures) to manage the adequacy of these financial resources on an ongoing basis.

The ICAAP document also summarises the results of the Board's assessment of the amounts, types and distribution of capital that it considers adequate to cover the level and nature of the risks to which the Bank is or might be exposed based on five-year financial projections.

The Assets & Liabilities Committee ("ALCO") performs a detailed assessment of the assumptions and overall conclusions of the ICAAP on an annual basis in order to confirm that they remain essentially valid. The Executive Committee ("EXCO") reviews the ICAAP document to ensure that it's aligned with the overall business strategy and takes into account emerging risks owing to changing market conditions. Following this, the Board Risk Committee ("BRC") considers the ICAAP, challenges the appropriateness of the assumptions used and the resulting capital requirements and capital adequacy. The Board is ultimately responsible for the Bank's capital arrangements.

The Bank maintains a liquid balance sheet in the form of HQLA and placements with banks with a tenor of up to 12 months. The customer deposit base is sticky and stable with a mix of relationship-based retail depositors and business owners. The Bank's liquidity risk is managed by the Treasury function with oversight from ALCO and BRC.

An assessment of liquidity needs, known as the internal liquidity adequacy assessment process ("ILAAP"), is undertaken at least annually and is presented to ALCO, EXCO and the Board Risk Committee for review, challenge and approval by the Board of Directors. The ILAAP describes how liquidity risks are assessed, controlled, monitored, mitigated and reported and helps management to determine what might be required to maintain liquidity assuming certain stressed conditions. In addition, reverse stress testing is also performed at least annually.

Operation and technology risks have emerged as a major risk for the banking sector in the past few years on the risk matrix. This refers to the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. To mitigate the risk, the Bank has put in place a robust risk event reporting process alongside self-assessment of an internal control system ("ICS") and risk control self-assessment ("RCSA") process. The Operations and Technology Committee ("OTCO") is responsible for monitoring of the risk with oversight from BRC. All operational risk events are analysed in detail in OTCO with appropriate controls measures put in place through root cause analysis. The operational risk profile of the Bank remains stable.

The Bank's core banking system is managed by the Parent Bank under a defined service level agreement ("SLA"). The Parent Bank has made substantial investments in IT infrastructure, cyber control and process improvement given the significant emphasis on the pace of evolution in the industry and continued exposure to the risk of cyber crime

Principal risks and mitigation plan

The Bank's approach to risk management is built on the principle of low to medium risk appetite over its investment return horizon, which is medium to long term. In order to achieve this, the Bank's business strategy is built on:

- A clearly defined target market (selected customer and industry segments).
- Conventional products and service offerings.
- Robust governance and control frameworks.

The key elements of the Bank's risk management framework are as follows:

- Governance at the Board and Management level.
- Risk oversight.
- Risk management controls.
- The Bank's risk management strategy and risk appetite are aligned with its motto 'Service with security', core values and strategic intent of delivering sustainable growth.

The Bank's risk appetite is articulated in the Risk Appetite Statements set by the Board of Directors. The Bank takes a conservative view on the inherent risks and has zero tolerance for financial crime, compliance and regulatory risks. All risk types are measured and monitored through identification, measurement, mitigation and escalation processes from management to the Board level.

The table overleaf highlights the key risks that the Bank is exposed to and provides details of the measures taken to mitigate these risks.

Risk type	Tolerance and mitigation
Credit risk	The Bank's mitigation of credit risk is based on a combination of focused strategy, defined target market, secured lending and quality of underwriting, ongoing monitoring and pre-set thresholds for single party exposure, industry concentration and type of collateral. The Bank has a well-defined and articulated credit risk management framework ("CRMF"), which comprises its credit risk appetite, credit policies, terms of reference of management and board level committees, target market analysis, collateral management, credit monitoring and other credit related policies. The Board Risk Committee ("BRC").has oversight responsibilities of the CRMF. The Country Credit Committee ("CCC") and Board Risk Committee review and approve credit exposures based on delegated authorities. The Bank adopted IFRS 9 from January 2018, as a result of which the CRMF has been updated by taking into consideration changes in the classification and measurement of financial assets and calculation of credit losses from an incurred loss basis to an expected credit loss basis. The Bank has followed a general approach in designing ECL methodologies, which are commensurate with its size, complexity, structure, economic significance and profile of exposure. The approach taken is considered proportionate in the context of the size of the Bank within the UK financial market, its relative lack of complexity as well as minimal volatility in its credit losses over the past five years. The Bank has put in place detailed policies and guidance for the credit team to deal with impact of IFRS 9.
Concentration risk	The Bank has an articulated concentration risk appetite. This is monitored by taking into consideration single name risk, industry, product, portfolio and geographical basis at CCC, ALCO and BRC level.
Operational risk	The Bank manages operational risk through articulated risk appetite and ongoing monitoring with oversight at management and board level committees. The Bank has a fully operational risk assurance function, which monitors various operational risks. The Bank sets various tolerance trigger points in accordance with regulation and guidance from the UK Financial Conduct Authority ("FCA") and Prudential Regulation Authority ("PRA"). In the event of these tolerances being breached, reporting to the Operations and Technology Committee ("OTCO") is made. OTCO reviews the breaches and considers whether further escalation to Audit, Risk and Compliance Committee ("ARCC") and Executive Committee is required. Reporting is made together with confirmation of remediation plans.
Financial crime risk	The Bank has in place a robust anti-money laundering ("AML") governance process supported by three lines of defence. The Board Audit and Compliance Committee is primarily responsible for oversight of financial crime risk supported by the Executive Committee of the Bank. A compliance dashboard, which incorporates risk events and regulatory updates, is reviewed and reported to the committees for oversight. The Bank has a zero tolerance for financial crime and is vigilant to identify, report and take appropriate action to mitigate the inherent risk associated with financial crime. Risk identification and mitigation is undertaken through risk assessment, effective implementation of customers due diligence requirements and ongoing account and transaction monitoring process. The Bank has comprehensive AML policies and procedures in place, which are reviewed and updated regularly. The Bank provides continuous training to its staff in the areas of AML and compliance.

Conduct risk	The Bank is a service-orientated institution and therefore managing customer outcomes is central to the Bank's philosophy, business strategy and operations. The Bank has in place robust controls, adequate skill sets and appropriate decision- making arrangements to deliver its objectives of understanding customer needs, ensuring fair treatment and pro-actively preventing poor outcomes for its customers. The Bank has an articulated conduct risk appetite, which is driven by best customer outcome. The Audit, Risk and Compliance Committee and Board Audit and Compliance Committee monitor business performance against the risk appetite at management and board level respectively. The Bank has implemented the requirements under a senior managers and Certification Regime, assigning prescribed responsibilities and application of certification and conduct regime requirements. The Bank arranged adequate training for its employees, including senior management and members of the board, to ensure awareness and assist in implementing the requirements. Staff members meeting the certification requirements are identified through a robust process and undergo relevant training on an ongoing basis.
Capital risk	The Bank's capital structure has been built up to support the business over a long-term horizon and meet regulatory requirements. These include capital resources to cover Pillar 1, Pillar 2, Capital Requirement Directives ("CRD") Buffers and PRA Buffer. The Bank also maintains internal capital buffers over and above the minimum regulatory capital requirement. ALCO and Executive Committee monitor adequacy of capital with oversight from the Board Risk Committee.
Liquidity and funding risk	The Bank manages the maturities of its assets and liabilities and its cash flows on a daily basis. The Bank maintains substantial liquidity in a Bank of England Reserve account, high quality liquid assets and in short-term deposits. The Bank has early warning indicators in place, which are monitored at operational and management committee levels. The Bank's customer deposit base is stable and considered sticky based on long-term relationships. The Bank's depositor base mainly comprises relationship-based retail and SME deposits. The Bank also offers six- and 12- month fixed-rate web-based deposits, which are mainly a rate-driven source of funding.
Interest rate risk	Interest rate risk at the Bank is well managed and contained under oversight from ALCO and BRC. The Bank has no significant or complex long-term interest rate positions. The Bank is part of a group-wide implementation plan to further strengthen and more effectively monitor interest rate risk in the banking book ("IRRBB"), which will be completed during 2019.
Foreign exchange risk	As the Bank does not maintain a trading book, it has significantly low foreign exchange exposure risk. The foreign exchange exposures are managed by the treasury front office with defined levels of maximum allowable net open position in a single currency.

Emerging risks

The Bank continuously updates its enterprise risk management framework in line with any change in profile of existing risks and emerging risks. These could be due to a change in the business environment, introduction of new products or regulatory expectations.

The Bank considers the following as emerging risks:

Risk type	Tolerance and mitigation
Brexit uncertainty	The Bank's business is mainly concentrated in the UK with no presence in the EU. Keeping in view the uncertainties related to the outcome of a deal with the EU, the Bank continues to monitor ongoing developments to assess the impact on its business activities and future plans. The Bank considers the uncertain political environment may impact market dynamics and sentiment. As the Bank operates in the UK, the core risk is considered a deterioration in the UK economy that could impact the Bank's business in the form of less lending opportunities as investors will be cautious to make investments in the UK, margin compression due to competition among banks and an increase in operating cost due to higher inflation. Management prudently monitors the developments and their potential impact on Bank's overall performance and risks in various committees including ALCO, BRC and the Board.
Cyber risk	The Bank recognises risk associated with cyber threats and is constantly taking proactive measures to strengthen its operating environment to provide a secure banking experience to internal as well as external stakeholders. The Bank takes risks associated with cyber security extremely seriously and is constantly engaged in not only improving and strengthening its transactional gateways but also its internal operating environment.
Non-compliance with General Data Protection Regulations ("GDPR")	The new data protection regulation which came in to effect from May 2018 strengthens the data protection for individuals in the EU. The Bank has implemented the regulations under oversight from the Board. The Bank monitors compliance with GDPR through a committee comprising of key management personal.

The notes to the financial statements and Pillar 3 Disclosures provide further information about most of these risks; the committees that have the relevant responsibility for these risks; and the policies to manage the key risks. The Directors are confident that the current risk management structure is sufficient for identification, monitoring and management of significant financial risks to the business.

Employee remuneration policy

The Bank's remuneration policy is in line with market practice and is weighted towards a performance-based compensation plan. The Bank does not have an incentivised compensation scheme for its staff. However, all staff members are included under a performance-based bonus scheme, which is paid out once a year.

The Bank's objectives, organisation structure and HR policies are integrated for best results. This works within an effective control framework and customer focus in order to implement the Bank's business strategy.

Performance is reviewed annually against pre-defined measures and efforts are recognised through a combination of monetary and non-monetary benefits. The performance management framework is managed through the Bank's HR and senior executive teams. The Board is responsible for annual reviews to determine the remuneration of senior management with Senior Management Function ("SMF") roles.

Annual performance is a self-assessment process where employees assess their own performance against their job profile. This is evaluated and agreed on with a line manager through a documented feedback process. Compliance also provides its input on adherence to certification regime staff and their required competencies.

Future outlook

The Bank's overall results for 2018 were quite strong with reasonable growth in lending, deposits and operating profit. The Bank exceeded its profit target despite a challenging and evolving economic and regulatory environment. The Bank is confident of maintaining and continuing the same performance momentum from 2018 and committed to the targets set for 2019 despite more challenging market conditions due to Brexit uncertainties and the weaker global economic outlook. The Bank is focused on following the strategic plan that is drawn up to achieve future growth, including meeting annual targets and monitoring progress against the projections.

The Bank entered 2019 with another positive start. The Bank recognises and appreciates that the future is changing rapidly and business success will depend on successfully aligning and implementing the business model to provide the service required for meeting customer needs effectively. The Bank is confident to execute the business plan, follow the strategy and have the right resources to meet the ever-changing requirements of a rapidly evolving market. The Directors are not aware, at the date of this report, of any likely major changes to the Bank's activities in the next year and expect the Bank to continue as a going concern for the foreseeable future.

Hence, the future emphasis will be on enhancing customer relationships, improving operational efficiency, technological enhancement and upgrading business capabilities. The Bank intends to do this through a strong and robust control process through the three lines of defence model and strong EXCO / Senior Management team and continuing Board oversight.

Approved by the Board and signed on its behalf by:

Kamran Qazi
Chief Financial Officer

Directors' Report

On behalf of the Board of Directors of Habib Bank Zurich plc ("the Bank"), I am pleased to present the Directors Report on the Financial Statements of the Bank for the year ended 31 December 2018. The Bank is registered in England and Wales with number 08864609 and is authorised by the PRA and regulated by the FCA and PRA. The Bank is a wholly owned subsidiary of Habib Bank AG Zurich.

Results

The Bank posted a profit after taxation of £3.59 million (2017: £4.40 million). The Bank's focus remains on developing its core business activities real estate finance and commercial banking services. The Bank also benefited from an increase in US dollar Libor rates through investments in floating rate bonds.

The UK's vibrant SME sector offers tremendous business opportunities for the Bank to grow its market share. Despite economic and political uncertainties, which impacts investors' confidence, the Bank was able to grow its lending business, which reflects the strength of its relationship-based banking. The Bank has financial and operational capacity in place to expand its business activities and also explore new opportunities.

Share capital and dividend

The Directors recommended a final dividend of £0.0299 per ordinary share for the year 2018 (2017: Nil).

The share capital of the bank remained unchanged at £60 million, which is divided into 60 million ordinary shares of £1 each.

Board of Directors

The following directors have been appointed to serve on the Board of the Bank:

Mr Muhammad H. Habib	Non-Executive Director (NED) Chairman
Mr Carey Leonard	Independent NED
Mr Gerald Arthur Gregory	Independent NED
Mr Anjum Iqbal	Non-Executive Director
Mr Rajat Garg	Non-Executive Director
Mr Satyajeet Roy	CEO / Executive Director
Mr Masum Billah*	COO / Executive Director – appointed on 12 December 2018

The Bank's Board membership represents a suitable mix of experience and knowledge relevant to the services offered.

Board meetings are held at least four times a year and additional meetings can be held at any time to discuss urgent issues.

* Subject to regulatory authorisation

Directors' representation

In the case of each of the persons who are Directors at the time the report is approved, so far as the director is aware, there is no relevant audit information of which the Bank's auditor is unaware, and the director has taken all the steps that he ought to have taken as a director in order to make himself aware of any relevant audit information and to establish that the Bank's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Independent Auditor

KPMG LLP has expressed an unqualified opinion on the 2018 financial statements.

KPMG LLP has expressed its willingness to continue in office as Auditors and a resolution to reappoint the firm will be considered at the forthcoming annual general meeting.

Senior Management and Certification Regime

The Bank has established adequate documented processes over monitoring and governance of the Senior Management and Certification Regime ("SM&CR"), including the certified population. This includes adequate governance and oversight exercised by the Board, updating management responsibility and related business activities, and training staff in particular with Senior Management Function ("SMF") roles, as well as assessing the fitness and propriety of SM&CR staff.

Going concern

The Bank's operating model is simple, offering core lending and deposits products to its customers, who have a strong loyalty to the franchise. This is the bedrock of the value proposition for the Bank. Service is delivered through dedicated branch and relationship managers. The customer takes comfort in continuity with a relationship manager and quick turnaround on their requests as well as access to the decision makers at the Bank. The expertise of the Bank in understanding and dealing with SME customers and business owners has positioned the Bank very strongly among its peer banks. This has enabled longevity of customers relationships spreading over two to three generations.

The Bank has prepared these financial statements taking into account that it operates on a self-sufficient basis with minimum dependency on Habib Bank AG Zurich (the "Parent Bank"). The Bank also expects to grow its lending book in line with its strategy and improve its credit quality, which provides a steady stream of interest income from customers. In addition to net interest income the Bank has a flow of revenue from fees and commissions. In line with the Bank's strategy, there will also be an expected increase in flow of income from investments, which is likely to grow over the next two to three years.

The Bank has a sound governance structure in place, which comprises the Board of Directors, Committees of the Directors and Management Committees covering all key risk areas such as credit risk, liquidity risk, anti-money laundering, compliance risk and operational risk. The capital base of the Bank is sound with more than the required capital invested by the Parent Bank. The Bank's liquidity position is also very strong with more than adequate liquid assets to cover a stress over a 90-day survivability period.

The Bank made profits after tax of £3.59 million (2017: £4.4 million) during the year. The Bank is expected to gradually increase its profitability in future years. To this respect the Bank has prepared five years of financial projections based on conservative assumptions.

Based on the above, the Directors are confident that the Bank has adequate resources to continue and grow the franchise for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

Post-balance sheet events

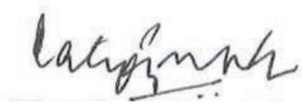
There have been no reportable events subsequent to the balance sheet date.

Acknowledgement

The Board of Directors takes the opportunity to express its gratitude to all stakeholders for their continued support.

The Board of Directors also records its appreciation to the EXCO and staff for their efforts, dedication, commitment and teamwork during 2018.

Approved by the Board and signed on its behalf by



Satyajeet Roy
Chief Executive Officer

Trafalgar Square and Big Ben, London

Directors' Responsibilities Statement

The Directors are responsible for preparing the Strategic Report, Directors' Report and the financial statements in accordance with the applicable law and regulations.

Company law requires the Directors to prepare the Bank's financial statements for each financial year. Under that law they have elected to prepare the Bank's financial statements in accordance with IFRS, as adopted by the EU and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Bank and of its profit or loss for that period. In preparing the Bank's financial statements, the Directors are required to:

- Select suitable accounting policies and then apply them consistently.
- Make judgements and estimates that are reasonable and prudent.
- State whether they have been prepared in accordance with IFRSs' as adopted by the EU.
- Prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Bank will continue in business.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Bank's transactions and disclose with reasonable accuracy at any time the financial position of the Bank and enable it to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as is reasonably open to them to safeguard the assets of the Bank and to prevent and detect fraud and other irregularities.

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Bank's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Satyajeet Roy
Chief Executive Officer

Corporate Governance Report

The Board of Directors

The Board of Directors ("the Board") is committed to follow best practice in Corporate Governance. The Financial Reporting Council updated the UK Corporate Governance Code ("the Code") in April 2016 and while the Code does not apply directly to the Bank, the Board agrees with and supports its general principles. This report sets out how the Bank has regard to the principles of the Code.

Board profile

Board of Directors
From left to right: Carey Leonard, Gerald Arthur Gregory, Rajat Garg, Muhammad H. Habib, Satyajeet Roy, Anjum Iqbal.

Muhammad H. Habib

Chairman

Roles & Committees	Chairman & Non-Executive Director
Skills & Experience	Muhammad H. Habib became a member of the General Management in 1992 (Habib Bank AG Zurich Group, Switzerland). He was appointed as the President & Chief Executive Officer of Habib Bank AG Zurich Group, in 2011. His banking journey, spanning over 37 years, started in 1981 from Dubai, UAE where he went through extensive trainings and manager level positions, in all aspects of banking over the next 11 years. After entering General Management in 1992, his remit and responsibilities took him across Africa, UK, North America and Switzerland. Under his leadership, the Group ventured into newer geographies, inclusive of but not limited to South Africa (1995) and Canada (2001). During this period, he was elevated to the rank of Joint President in 1996. He is currently a member of the General Management and President of Habib Bank AG Zurich Group.
Principal external appointments	· Chairman, Habib Canadian Bank, Canada · Director, Habib Metropolitan Bank, Pakistan · Chairman, HBZ Bank Limited, South Africa · Vice Chairman, Gefan Finanz AG Zug, Switzerland · Member Board of Trustees, Habib University Foundation · Member Board of Trustees, Habib Public School, Karachi (Pakistan) · Member Global Advisory Board, Babson College

Carey Leonard

Independent
Non-Executive Director

Roles & Committees	· Independent Non-Executive Director · Chair of the Board Risk Committee · Member of the Board Audit and Compliance Committee
Skills and experience	Carey Leonard has over 45 years of banking experience in Asia, the Middle East, Africa and the UK. He has strong commercial banking disciplines in the areas of governance, strategy, business development, wholesale banking and risk management.
Principal external appointments	· Independent Non-Executive Director and Chair of Board Credit Committee and Member of the Board Audit and Risk Committee Diamond Bank (UK) Plc · Trustee and Treasurer to the Council, Malvern College · Governor and Chairman of the Commercial Committee, The Downs Malvern Preparatory School
Former appointments	Standard Chartered Bank · Regional Head, Special Assets Management Africa · Chief Executive Officer, South Africa · Managing Director and CEO, Nigeria · Chief Executive Officer, Sri Lanka · Member of Business Leadership Team

Gerald Arthur Gregory

Independent
Non-Executive Director

Roles & Committees	· Independent Non-Executive Director · Chair of the Board Audit and Compliance Committee · Member of the Board Risk Committee
Skills and experience	Gerald Gregory brings extensive experience both in practice and in independent non-executive functions. His experience covers treasury, lending, strategy, marketing and risk management.
Principal external appointments	· Deputy Chairman and Independent Non-Executive Director, Chair of Risk Committee and member of Audit Committee, Gatehouse Bank Plc · Chairman and Independent Non-Executive Director, Chair of Remuneration Committee, member of Audit committee and Risk Committee, Northern Bank Limited (t/a Danske Bank)
Former appointments	· Managing Director, Britannia Capital Investment Group · Executive Director, Britannia Building Society · Sales and Marketing Director, Britannia Building Society

Anjum Iqbal

Non-Executive Director

Roles & Committees	· Member of the Board Risk Committee · Member of the Board Audit and Compliance Committee
Skills and experience	Anjum Iqbal has extensive management experience in various part of the world in corporate and commercial banking. He has worked in several regions including Latin America, Europe, the Middle East, Africa and South Asia.
Principal external appointments	· Member of General Management and Regional CEO (Developing markets), Habib Bank AG Zurich (Switzerland) · Non-Executive Director and member of Board Audit Committee, Board Risk Committee, HBZ Bank Ltd (South Africa) · Chair of Risk and Compliance Committee, Chair of Board IT Committee, member of Board Audit Committee and Board Credit Committee, Habib Metropolitan Bank (Pakistan)
Former appointments	Habib Bank AG Zurich, UK · Chief Executive Officer Habib Metropolitan Bank, Pakistan · President and Chief Executive Officer Citigroup · Managing Director Commercial Banking Group (EMEA) · Strategy and Business Development Head · CEO Africa Division · Regional CEO, Turkey and Central Asia

Rajat Garg

Non-Executive Director

Roles & Committees	· Member of the Board Risk Committee · Member of the Board Audit & Compliance Committee
Skills and experience	Rajat Garg possesses over 28 years of experience in senior banking positions across Asia, Europe and Middle East. His professional background includes extensive experience in managing commercial banking and wealth management business.
Principal external appointments	· Member of General Management and Regional CEO (Developed markets), Habib Bank AG Zurich (Switzerland) · Non-Executive Director, HBZ Bank (Hong Kong) Ltd · Non-Executive Director, Habib Canadian Bank
Former appointments	Citigroup · Head of Retail Banking and Wealth Management, EMEA · Country Business Manager, Turkey · Cards Business Manager, Saudi Arabia · Regional CFO - Asia Pacific Cards, Singapore · NRI Wealth Management Head, Singapore · Financial Controller and Business Planning Head, India

Satyajeet Roy

Chief Executive Officer

Roles & Committees	· Executive Director · Chief Executive Officer
Skills and experience	Satyajeet Roy is a seasoned executive with over 25 years of international banking experience across the Middle East, UK, Europe & India spread over Commercial, SME and Retail segments. He brings cross-functional experience covering business strategy, risk, audit and operations.
Principal external appointments	none
Former appointments	Commercial Bank International, UAE · Head of Business Banking Citigroup · Head of Commercial Banking for UAE & Bahrain · Head of Business Development, Business Banking, EMEA (London UK) · Audit and Risk Review, Lead Auditor, EMEA

Masum Billah

Chief Operations Officer

Roles & Committees	· Executive Director * · Chief Operations Officer
Skills and experience	Masum Billah has over 20 years of experience in financial services spread across operations, technology, operational risk, business development, compliance and risk management. During his various roles he has been based in Bangladesh and UK with coverage for Europe, Middle East and Africa markets.
Principal external appointments	none
Former appointments	Bank of America Merrill Lynch (London, UK) · Director, GTS EMEA Compliance Citigroup · Senior Compliance Officer, TTS EMEA Compliance (London, UK) · Risk and Control Programs Lead, TTS Global Operations (London, UK) · EMEA Trade Deal Facilitation and FI Training Head (London, UK) · Head of Operations and Technology (Dhaka, Bangladesh)

* Subject to regulatory authorisation

Executive Committee

Satyajeet Roy	CEO and Executive Director
Kamran Qazi	Chief Financial Officer
Syed Kausar Kazmi	Head of Commercial Banking
Nadia Saleem	Head of Compliance and MLRO
Masum Billah	Chief Operations Officer
Parmod Garg	Head of Credit
Waqar Haider	Head of Governance and Risk Control and Board Secretary
Monika Poznar	Head of Human Resources

Executive Committee
From left to right: Parmod Garg, Syed Kausar Kazmi, Satyajeet Roy, Nadia Saleem, Monika Poznar, Masum Billah, Kamran Qazi and Waqar Haider.

LEADERSHIP

The role of the Board

The primary role of the Board is to set the overall strategy for the Bank and to protect and enhance its long-term strategic value. The Board ensures that the business of the Bank is conducted in an efficient and effective manner to promote the success of the Bank within an established framework of effective systems of internal control, robust risk management process and compliance with regulatory requirements. The Board also ensures that good corporate governance policies and practices are implemented within the Bank. In the course of discharging its responsibilities, the Board acts in good faith, with due diligence and care, and in the best interests of the Bank and its shareholders.

The primary responsibilities, which the Board undertakes in this respect, are to:

- Consider changes to the structure, size and composition of the Board and board committees and approve terms of reference.
- Define, oversee and be accountable for the implementation of governance arrangements that ensure effective and prudent management of the Bank, including the segregation of duties in the organisation and the prevention of conflicts of interest.
- Set the Bank's strategic objectives and goals and reviewing the performance of the executive team.
- Review and approve the risk appetite statements of the Bank.
- Establish and maintain a framework for the overall sound and proper internal control and risk management processes.
- Review and challenge the business performance of the Bank, set the budget and financial forecasts, and ensure that the business of the Bank is managed to balance risk and reward.
- Ensure that adequate succession planning arrangements are in place related to senior management so as to maintain an appropriate balance of skills and experience within the Bank.

The responsibilities of the Board are clearly set out in its Terms of Reference ("TORs"), which is reviewed and approved annually by the members of the Board. The schedule of Board meetings along with recurring items is approved in advance with the permission of the Chairman and circulated to all members.

Division of responsibilities

The responsibilities of the Board members are set out in the Board TORs, which are aligned with a respective statement of responsibilities prepared under the senior management regime for each Board member. The Chairman is responsible for leading the development of and monitoring the effective implementation of policies and procedures for the induction, training and professional development of all members of the Board.

The Chairman sets the Board's agenda primarily focusing on strategy, performance, value creation and accountability and ensures that adequate time is available for discussion on all agenda items, in particular strategic issues. Along with other Board members, the Chairman is also the responsibility for leading the development of the Bank's culture as a whole.

The two appointed independent non-executive directors ("INEDs") support the Board in the oversight functions on the basis of requisite skill sets and experience needed for effectively performing their respective SMF roles.

Collectively and individually the INEDs provides adequate challenge to other members of the Board and the senior management team in the course of discharging their oversight responsibilities as board members.

The non-executive directors ("NEDs") along with INEDs are responsible for setting the Bank's strategic objectives and goals and reviewing the performance of the executive team. They approve and keep an oversight of the Bank's strategy and business plan prepared by the executive team. They also review and challenge the business performance of the Bank, approve the budget and financial forecasts, and ensure that the business of the bank is managed to balance risk and reward. They also scrutinise the delivery of the strategy within the risk and control framework set by the Board and satisfy themselves on the integrity of financial reporting.

The Chief Executive Officer ("Executive Director") is responsible for managing the Bank's business on a day-to-day basis on behalf of the Board. The business is managed within the strategy, risk appetite and control frameworks set and overseen by the Board. The Executive Director has specific management responsibilities for which he is accountable to the Board, such as executing the business plan, delivering planned results, managing risk, systems and the control framework, and delivering timely and accurate information to the Board.

EFFECTIVENESS

The composition of the Board

The size of the Board is aligned with the overall governance structure required for the effective oversight of the business, risk and control framework; operational, regulatory and compliance; and financial performance of the Bank. The composition of the Board has been established to ensure the availability of a pool of resource with relevant knowledge and experience to manage the strategic objective of the Bank.

The Board comprises six directors – the Chairman, two INEDs, two NEDs and one Executive Director. The relevant knowledge of Board members and diversity of their experience allows all directors to actively and effectively participate in the meetings.

The Board considers Carey Leonard and Gerald Arthur Gregory to be independent within the meaning of the UK Corporate Governance Code. They do not perform any executive or other role or have any relationship with the Bank that, in the Board's view, would affect their objectivity and judgement in performing their respective function.

Appointment to the board

Appointments to the Board are made by carrying out a formal and rigorous process of evaluating candidates by the Board members, selected on the skills and experience required for their particular appointment. The Bank usually uses an external executive search firm for shortlisting candidates.

Commitment

The Bank has a balanced combination of non-executive, independent non-executive and executive directors keeping in view the complexity and nature of the Bank's operations. All directors in accordance with their terms of appointment are required to allocate sufficient time to the Bank to discharge their responsibilities effectively and efficiently.

Development

The Bank provides a detailed overview of the business to all directors on their joining of the Board. The process includes a formal presentation conducted by senior executive management covering their respective areas including but not limited to strategy and risk management, business development, credit, AML and compliance, operations, treasury and finance and information technology. There is also continuous interaction between executive management and the Board members, which allows the new directors to gain further knowledge and insight about Bank's business.

All directors are required to complete in-house online courses, which comprehensively cover areas such as AML, information security, fraud prevention, anti-bribery and corruption, whistleblowing, complaints, data protection. In addition, directors are also provided face-to-face training related to emerging risks to keep them abreast of new challenges within financial services.

Information and support

The Chairman ensures that the Board members receive accurate, timely and clear information for effective decision-making processes and applies sufficient challenge to major proposals. The Directors keep close liaison with the executive management of the Bank for a better understanding of the business operations of the Bank. Furthermore, the Board has independent access to senior management and the Board Secretary at all times.

The Board Secretary ensures timely and accurate information flows within the Board and its committees and between senior management and the NEDs. Senior management of the Bank present information related to all key areas, such as risk management, credit, compliance, operations, finance and audit to the Board through its committees.

Evaluation

Each Board member undergoes an annual evaluation process by completing a self-assessment questionnaire, which is discussed with the Chairman of the Board. The assessment aims to assess the performance evaluation of each member by recognising strengths and addressing weaknesses.

To assess the overall performance of the Board, each member also completes a questionnaire on board effectiveness, which includes areas of strategic goals and objectives, governance, risk management, quality of information and leadership.

Re-election

In accordance with the provisions in the Articles of Association, all directors who have been appointed by the Board must stand for re-election every three years.

ACCOUNTABILITY

Board committees

To help carry out its responsibilities, the Board has also established the following committees with terms of reference setting out matters relevant to the committees' composition, responsibilities and administration.

Board Risk Committee

Membership

Carey Leonard	Chairman
Gerald Arthur Gregory	Member
Anjum Iqbal	Member
Rajat Garg	Member

Board Audit and Compliance Committee

Membership

Gerald Arthur Gregory	Chairman
Carey Leonard	Member
Anjum Iqbal	Member
Rajat Garg	Member

Board Risk Committee

Primary responsibilities are to:

- Review the overall approach of the Bank to risk, its management and reporting line framework to ensure the effective application of the risk management framework.
- Assess and regularly review the three lines of defence model implemented by the Bank for its effectiveness.
- Provide assurance on the Bank-wide risk management framework and monitor the overall risk profile of the Bank through effective control processes.
- Annually review the Risk Appetite Statement and consider the adequacy of risk limits and returns.
- Set guidelines for maintaining risk control parameters for all types of risk across the business, including policies, control standards, underwriting standards, risk exposure limits or other control levers.
- Receive information on any material breaches of risk limits, policies or procedures and agree proposed action as soon as practically possible.
- Consider and make recommendations to the Board regarding the appointment, removal and resignation of employees with SMF responsibilities under the Senior Management Regime (SMR) with the exception of Directors.
- Consider and make recommendations to the Board regarding the remuneration including increment and bonus of employees with SMF responsibilities with the exception of Directors.

Board Audit and Compliance Committee

An independent Audit and Compliance Committee is responsible for challenging executive management and the Bank's internal and external auditors as part of a good governance process. Primary responsibilities are:

- Review key internal control policies, processes and procedures and assess the effectiveness of those keeping in view the size, nature and complexities of Bank's operations.
- Review the effectiveness of the Bank's internal audit in the context of the Bank's overall risk management system.
- Review and assess independence of internal audit function.
- Make recommendations on the internal and external auditors' appointment, reappointment and removal.
- Review and monitor the independence of the external auditors.
- Discuss the financial statements and the quality of the underlying accounting processes with the member of management responsible for accounting and finance.
- Review and approve the non-audit services policy in respect of the external auditors.
- Review and approve accounting policies and changes therein.
- Review policies to ensure the Bank's ongoing compliance with relevant legal and regulatory requirements.
- Ensure that its recommendations to combat money laundering, terrorist financing and financial crime risks are incorporated into the Bank's ongoing procedures and monitoring infrastructure.
- Oversight of adequacy of processes put in place by the management to manage Conduct Risk
- Oversight of the adequacy of the training and competency framework required fulfilling the Bank's obligations under the SMR and the Certification Regime.
- Review and ensure the implementation and compliance of EU audit legislation in liaison with external auditors.

Board meetings

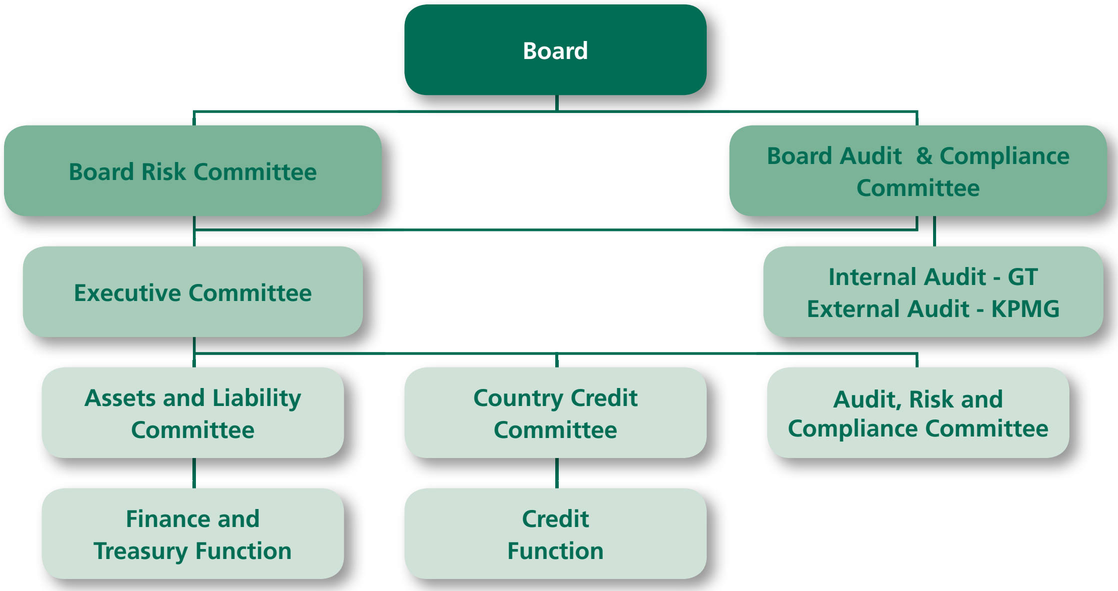
The Board meets regularly at least four times a year at quarterly intervals and holds additional meetings as and when the Board thinks appropriate. Four Board meetings were held during 2018. The agenda, together with Board papers, are sent in full to the directors not less than five business days before the intended date of the Board meeting. The Board Secretary prepared minutes of Board meetings, with details of decisions reached.

At each regular Board meeting, the executive management of the Bank made presentations to the Board on various aspects, including business performance, financial performance, corporate governance and outlook. Throughout 2018, Directors of the Bank also participated in the consideration and approval of matters of the Bank by way of written resolutions circulated to them. Supporting written materials were provided in the circulation and the Board Secretary when required gave verbal briefings.

All Directors attended the Board and its committee meetings held during the year.

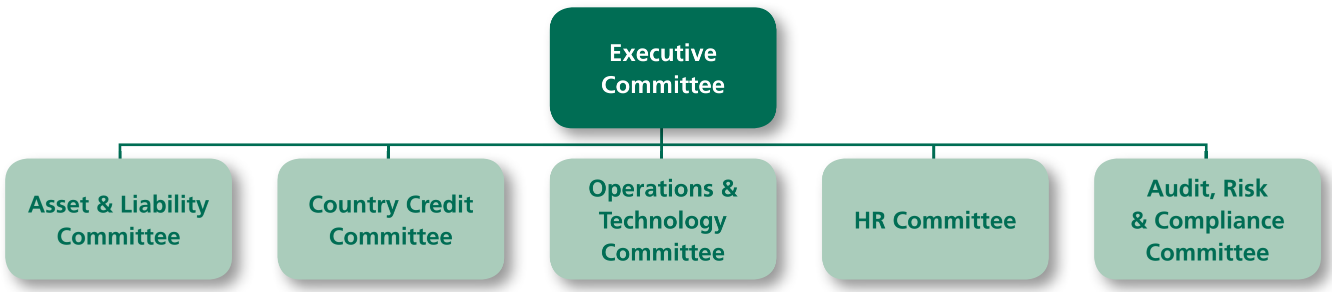
Interaction with management committees

There is a formal division of responsibilities matrix, which identifies the responsibilities of the Board and those of the management through its respective committees. Management committees are responsible for oversight of various operational processes through which the strategy and objectives set by the Board are achieved. These are clearly defined and approved in terms of reference of each management committee.



The CEO and EXCO represent the principal forum for conducting the day-to-day business of the Bank. The terms of reference of EXCO is approved by the Board. EXCO is represented in the Board through the CEO. While retaining the ultimate responsibility for the actions taken, the CEO and EXCO at its discretion has delegated certain responsibilities to the following standing sub-committees:

- Asset and Liability Committee
- Audit Risk and Compliance Committee
- Country Credit Committee
- Operations and Technology Committee
- Human Resource Committee



The Chairman of the respective committee presents key matters arising from each of the above committees to EXCO, which are also reported to the Board or its committees through various management information presented in Board or its committee meetings.

Financial and business reporting

The Board has put in place appropriate checks and controls to ensure that financial and business information presented in the financial statements provides a balanced and fair assessment of the Bank's performance, business model and strategy.

Risk management and internal control

The Board reviews and approves the overall risk appetite of the Bank. The Board has established and maintained a framework for the overall sound and proper internal control and risk management processes. The Board regularly receive reports on, and reviews the effectiveness of, the risk and control processes to support the strategy and objectives.

REMUNERATION

The Board is responsible for the review and approval of the Bank's HR Policy including remuneration practices. The Board, on the recommendation of the Chief Executive Officer, approves the annual staff remuneration plan along with the total remuneration for senior executive staff.

The Bank's remuneration policy is in line with market practice and is weighted towards performance-based development. The Bank is fully cognisant of having a remuneration policy that is aligned with its long-term objectives and can provide support in the successful implementation of its business strategy. The remuneration policy has been developed while keeping in view the core values of the Bank, which has trust as its core supported by integrity, team work, respect, responsibility and commitment. Values are upheld continuously and embedded at all levels of the organisation.

The Bank recognises that robust performance assessment is essential for the sustained success and development of the Bank and its employees. The Bank's performance assessment creates a shared vision of the purpose and aims of the Bank and ensures that each employee understands how he or she makes their contribution.

Performance is reviewed annually against predefined measures and efforts are recognised through a combination of monetary and non-monetary benefits. The performance management framework is managed through the Bank's senior executive management.

The Bank's remunerations structure is not linked to any pre-defined business targets for front-end staff. Annual performance rewards are based on overall performance of the Bank and then of the employee based on overall achievement during the year. A key consideration given in evaluating the performance of employees is there overall conduct and compliance with relevant rules and competencies demonstrated during the year.

RELATIONS WITH SHAREHOLDERS

The Bank is a wholly owned subsidiary of Habib Bank AG Zurich ("the Parent Bank"). The Chairman discusses matters relating to governance and business strategy of the Bank with the other shareholders. He ensures that views of shareholders are shared with the Board.

Constructive use of annual general meeting

All members of the Board are encouraged to attend the annual general meeting of the Bank to be used as an opportunity to interact and communicate with the shareholders.

Independent auditor's report

to the members of Habib Bank Zurich plc

1. Our opinion is unmodified

We have audited the financial statements of Habib Bank Zurich plc ("the Bank") for the year ended 31 December 2018 which comprise the Income statement, Statement of Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity, Cash Flow Statement and the related notes, including the accounting policies in note 5.

In our opinion:

— give a true and fair view of the state of Bank's affairs as at 31 December 2018 and of its profit for the year then ended;

— have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union; and

— have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee. We were appointed as auditor by the directors for the period ended 31 December 2015. The period of total uninterrupted engagement is for the 4 financial years ended 31 December 2018. We have fulfilled our ethical responsibilities under, and we remain independent of the Bank in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

Overview

Materiality: Financial statement as a whole		£218k (2017: £250k)
		5% of profit before tax
		(2017: 5% of profit before tax)
Key audit matters		**vs 2017**
New matter	The impact of uncertainties due to the United Kingdom exiting the European Union on our audit	
Recurring risks	Provision for impairment on loans and advances	▲

2. Key audit matters: including our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

Key audit matter	The risk	Our response
The impact of uncertainties due to the United Kingdom exiting the European Union on our audit Refer to the Strategic report (page 5)	**Unprecedented levels of uncertainty** All audits assess and challenge the reasonableness of estimates, in particular as described in provision for impairment on loans and advances below, and related disclosures and the appropriateness of the going concern basis of preparation of the financial statements. All of these depend on assessments of the future economic environment and the Bank's future prospects and performance. Brexit is one of the most significant economic events for the UK and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes, with the full range of possible effects unknown.	We developed a standardised firm-wide approach to the consideration of the uncertainties arising from Brexit in planning and performing our audits. Our procedures included: — **Our Brexit knowledge** – We considered the directors' assessment of Brexit-related sources of risk for the Bank's business and financial resources compared with our own understanding of the risks. We considered the directors' plans to take action to mitigate the risks. — **Sensitivity analysis** – When addressing provision for impairment on loans and advances and other areas that depend on forecasts, we compared the directors' analysis to our assessment of the full range of reasonably possible scenarios resulting from Brexit uncertainty and, where forecast cash flows are required to be discounted, considered adjustments to discount rates for the level of remaining uncertainty. — **Assessing transparency** – As well as assessing individual disclosures as part of our procedures on provision for impairment on loans and advances we considered all of the Brexit related disclosures together, including those in the strategic report, comparing the overall picture against our understanding of the risks. **Our results** As reported under provision for impairment on loans and advances,we found the resulting estimates and related disclosures of sensitivity and disclosures in relation to going concern to be acceptable. However, no audit should be expected to predict the unknowable factors or all possible future implications for a Bank and this is particularly the case in relation to Brexit.

2. Key audit matters: including our assessment of risks of material misstatement (continued)

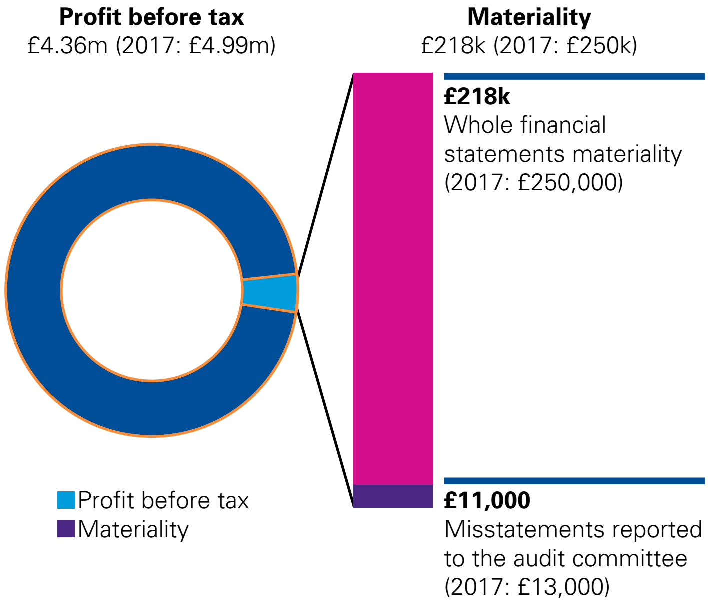
Key audit matter	The risk	Our response
Provision for impairment on loans £5.6m (1 Jan. 2018: £13.7m) (2017: £12.9m) Refer to note 5 (Accounting Policy), note 16 (Loans and advances to customers), 31 (Risk management)	From 1 January 2018, the Bank have adopted IFRS 9, resulting in an impairment charge being recognised when losses are expected rather than when they have been incurred and taking into account the expectation of economic scenarios. The status of each loan is also assessed to establish whether this is a 12 month expected loss calculation (for 'performing' loans) or a lifetime expected loss calculation (for underperforming / non-performing loans). Key judgements and estimates in respect of the timing and measurement of expected credit losses (ECL) include: — Allocation of assets to stage 1, 2, or 3 using criteria in accordance with the accounting standard; —Accounting interpretations and modelling assumptions used to build the models that calculate the ECL; —Inputs and assumptions used to estimate the impact of multiple economic scenarios; — Completeness and valuation of post model adjustments; — Measurements of individually assessed provisions including the assessment of multiple scenarios. The effect of these matters is that, as part of our risk assessment, we determined that the provision for impairment on loans and advances has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (note 5.3.1) discloses the sensitivity estimated by the Bank.	Our procedures included: — **Controls testing:** We tested the design and operating effectiveness of key controls across the processes relevant to the ECL. This included the allocation of assets into stages,model governance, data accuracy and completeness, credit monitoring, multiple economic scenarios, post model adjustments, individual provisions and production of journal entries and disclosures. — **Our financial risk modelling expertise:** We involved our own financial risk modelling specialist in evaluating the appropriateness of the Bank's IFRS9 impairment methodologies. This included challenging the reasonableness of management's assumptions, assessing the appropriateness of the model design and formulas used and recalculating the Probability of Default, Loss Given Default and Exposure at Default for a sample of models. — **Our economic scenario expertise:** We involved our own economic specialist to assist us in challenging and assessing the appropriateness of the Bank's methodology for determining the macro economic variables, economic scenarios used and the probability weightings applied to them. They also assessed key economic variables used which included agreeing the economic variables to external sources as well as the overall reasonableness of the economic forecast by comparing the Bank's forecast to our own modelled forecasts with a focus on commercial property and other lending portfolios. As part of this work we assessed the possible impact of economic uncertainty, including Brexit. — **Tests of detail:** We challenged the criteria used to allocate an asset to stage 1, 2 or 3 in accordance with IFRS 9; this included peer benchmarking to assess staging levels. We identified a sample of loans based on their risk characteristics and tested the appropriateness of their classification to stage 1, 2 and 3; We assessed the completeness and appropriateness of post model adjustments. Based on customer specific conditions, we considered the need for systemic adjustments. We assessed the appropriateness of the scenarios used and calculation of the overlay. — **Assessing transparency:** We assessed the adequacy of the Bank's disclosures in respect of the degree of estimation involved in arriving at the provision. **Our results** We found the resulting estimate of provision for impairment of loans and advances to customers to be acceptable (1 Jan 2018: result acceptable).

3. Our application of materiality and an overview of the scope of our audit

Materiality for the financial statements as a whole was set at £218k (2017: £250k), determined with reference to a benchmark of the Bank's profit before tax, of which it represents 5% (2017: 5%).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £11k (2017: £13k), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Our audit of the Bank was undertaken to the materiality level specified above and was all performed at the Bank's head office in London.



4. We have nothing to report on going concern

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Bank or to cease its operations, and as they have concluded that the Bank's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the Bank will continue in operation.

In our evaluation of the Directors' conclusions, we considered the inherent risks to the Bank's business model and analysed how those risks might affect the Bank's financial resources or ability to continue operations over the going concern period. The risks that we considered most likely to adversely affect the Bank's available financial resources over this period was the impact of Brexit on the Bank's liquidity and capital resources.

As these were risks that could potentially cast significant doubt on the Bank's ability to continue as a going concern, we considered sensitivities over the level of available financial resources indicated by the Bank's financial forecasts taking account of reasonably possible (but not unrealistic) adverse effects that could arise from these risks individually and collectively and evaluated the achievability of the actions the Directors consider they would take to improve the position should the risks materialise.

Based on this work, we are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least a year from the date of approval of the financial statements. We have nothing to report in these respects, and we did not identify going concern as a key audit matter.

5. We have nothing to report on the other information in the Annual Report

The directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion thereon.

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

— we have not identified material misstatements in the other information;

— in our opinion the information given in those reports are consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion

— adequate accounting records have not been kept by the Bank, or returns adequate for our audit have not been received from branches not visited by us; or

— the financial statements are not in agreement with the accounting records and returns; or — certain disclosures of directors' remuneration specified by law are not made; or —we have not received all the information and explanations we require for our audit. We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 22, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; 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 they either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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 other irregularities (see below), or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud, other irregularities or error and 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.

A fuller description of our responsibilities is provided on the FRC's website at:

www.frc.org.uk/auditorsresponsibilities

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the annual accounts from our general commercial and sector experience, through discussion with the directors and other management (as required by auditing standards), and from inspection of the Bank's regulatory correspondence and discussed with the directors and other management the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. The potential effect of these laws and regulations on the annual accounts varies considerably.

Firstly, the Bank is subject to laws and regulations that directly affect the annual accounts including financial reporting legislation including related companies legislation and taxation legislation, and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Bank is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the annual accounts, for instance through the imposition of fines or litigation or the loss of the Bank's licence to operate. We identified the following areas as those most likely to have such an effect: regulatory capital and liquidity, financial crime including money laundering, sanction list and market abuse regulations recognising the financial and regulated nature of the Bank's activities. Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and other management and inspection of regulatory correspondence, if any.

Through these procedures we became aware of actual or suspected non-compliance and considered the effect as part of our procedures on the related financial statement items. The actual or suspected non-compliance was not sufficiently significant to our audit to result in our response being identified as a key audit matter.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the annual accounts, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the annual accounts, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

8. The purpose of our audit work and to whom we owe our responsibilities

This report is made solely to the Bank's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's members, as a body, for our audit work, for this report, or for the opinions we have formed.

M Davidson

Michael Davidson (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL

18 April 2019

The Cube building behind Gas Street Basin, Birmingham

Income statement

For the year ended 31 December 2018

	Notes	2018 (£)	2017 (£)
Interest income calculated using effective interest method		20,978,947	19,955,827
Interest expense		(4,731,004)	(4,173,577)
Net interest income	6	**16,247,943**	**15,782,250**
Fee and commission income		1,580,706	1,650,925
Fee and commission expense		(305,088)	(306,716)
Net fee and commission income	7	**1,275,618**	**1,344,209**
Foreign exchange income		304,841	452,467
Fair value gain on derivative financial instruments		30,021	53,772
Gain / (loss) on sale of financial investments		-	57,649
Other income	8	270,929	1,561,194
Net other income		**605,791**	**2,125,082**
Staff costs	9	(9,307,350)	(8,901,621)
Depreciation	19	(521,992)	(540,781)
Administrative and general expenses	10	(4,870,096)	(4,996,503)
Operating expenses before credit impairment losses		**(14,699,438)**	**(14,438,905)**
Operating profit before credit impairment losses		**3,429,914**	**4,812,636**
Reversal of credit impairment losses	11 & 31.14	925,714	178,880
Profit before tax		**4,355,628**	**4,991,516**
Tax (charge)	12	(767,549)	(590,937)
Profit after tax		**3,588,079**	**4,400,579**

Profit for the financial year arises from continuing operations.

The accompanying notes on pages 47 to 110 form an integral part of the financial statements.

The Bank adopted IFRS 9 with effect from 1 January 2018. Due to the transition method applied, the comparative year amounts have not been restated.

Statement of Comprehensive Income

For the year ended 31 December 2018

	Notes	2018 (£)	2017 (£)
Profit after tax		**3,588,079**	**4,400,579**
Items that may be reclassified subsequently to income statement:			
Fair value through other comprehensive income reserve			
- Net losses from changes in fair value	17	(299,900)	-
- Deferred tax asset / (charge)	27	55,872	-
		(244,028)	-
Net losses transferred to P&L due to impairment		7,142	-
Available for sale reserve			
Fair value gain on available for sale investments	17	-	106,674
- Deferred tax asset charge	27	-	(17,536)
Other comprehensive income for the period net of tax		**(236,886)**	**89,138**
Total comprehensive income for the period attributable to equity holders		**3,351,193**	**4,489,717**

The accompanying notes on pages 47 to 110 form an integral part of the financial statements.

Statement of Financial Position

As at 31 December 2018

	Notes	2018 (£)	2017 (£)
Assets			
Cash in hand and with central bank	14	66,809,975	65,612,043
Due from banks	15	58,931,047	59,648,488
Loans and advances to customers at amortised cost	16	398,976,852	380,433,726
Financial investments	17	103,384,856	90,906,053
Derivative assets held for risk management	18	167,181	279,254
Property and equipment	19	5,785,948	6,005,261
Other assets	20	881,343	1,136,998
Deferred tax assets	13	967,988	926,263
Total assets		**635,905,190**	**604,948,086**
Liabilities and Equity			
Liabilities			
Due to banks at amortised cost	21	17,398,649	15,865,126
Due to customers at amortised cost	22	523,493,393	496,852,369
Derivative liabilities held for risk management	18	137,160	225,482
Accruals, deferred income and other liabilities	23	3,924,961	3,336,160
Current tax liabilities	24	650,581	773,000
Deferred tax liabilities	27	0	72,181
Subordinated liabilities	25	20,103,671	20,083,974
Total liabilities		**565,708,415**	**537,208,292**
Equity			
Called up share capital	26	60,000,000	60,000,000
Retained earnings		10,229,002	7,432,075
Fair value loss on financial assets at fair value through other comprehensive income	27	(32,227)	-
Available for sale reserves	27	-	307,719
Total equity		**70,196,775**	**67,739,794**
Total liabilities and equity		**635,905,190**	**604,948,086**

Signed on behalf of the Board of Directors

Chairman
(Muhammad H. Habib)

Director
(Satyajeet Roy)

The accompanying notes on pages 47 to 110 form an integral part of the financial statements.

The Bank adopted IFRS 9 with effect from 1 January 2018. Due to the transition method applied, the comparative year amounts have not been restated.

These financial statements were approved by the Board of Directors and authorised for issue on 18 April 2019.

Statement of Changes in Equity

For the year ended 31 December 2018

	Called up share capital £	Available for sale reserve £	Fair value through other comprehensive income reserve £	Retained earnings £	Total £
Balance as at 31 December 2017	**60,000,000**	**307,719**	**-**	**7,432,075**	**67,739,794**
Adjustment on initial application of IFRS 9					
- Change in accounting policy	-	(307,719)	307,719	(953,194)	**(953,194)**
- Deferred tax impact on change in accounting policy	-	-	-	162,042	**162,042**
	-	-	-	(791,152)	**(791,152)**
- Adjustment in fair value due to change in investment classification			(135,440)		**(135,440)**
- Deferred tax impact on fair value on change in investment classification			25,734		**25,734**
			(109,706)		**(109,706)**
Net losses transferred due to reclassification			6,646		**6,646**
Balance as at 1 January 2018	**60,000,000**	**-**	**204,659**	**6,640,923**	**66,845,582**
Profit after tax	-	-	-	3,588,079	**3,588,079**
Fair value through other comprehensive income (net losses during the year)	-	-	(299,900)	-	**(299,900)**
Deferred tax	-	-	55,872	-	**55,872**
			(244,028)		**(244,028)**
Net losses transferred to OCI due to impairment			7,142	-	**7,142**
Balance as at 31 December 2018	**60,000,000**	**-**	**(32,227)**	**10,229,002**	**70,196,775**

For the year ended 31 December 2017

	Called up Share Capital £	Available for Sale Reserve £	Retained earnings £	Total £
Balance as at 1 January 2017	**60,000,000**	**218,581**	**3,031,496**	**63,250,077**
Profit after tax	-	-	4,400,579	**4,400,579**
Available for sale (net gains during the year)	-	89,138	-	**89,138**
Balance as at 31 December 2017	**60,000,000**	**307,719**	**7,432,075**	**67,739,794**

The accompanying notes on pages 47 to 110 form an integral part of the financial statements.

The Bank adopted IFRS 9 with effect from 1 January 2018. Due to the transition method applied, the comparative year amounts have not been restated.

Cash Flow Statement

For the year ended 31 December 2018

	Notes	2018 (£)	2017 (£)
Cash flows from operating activities			
Profit before tax		4,355,628	4,991,516
Adjusted for:			
- (Reversal) / Impairment losses on loans and advances at amortised cost	11	(925,714)	(178,880)
- Gain / (loss) on sale of available for sale investments		-	(57,649)
- Depreciation	19	521,992	540,781
- Gain on sale of property and equipment		-	(526)
		3,951,906	**5,295,242**
Net (increase)/decrease in operating assets			
Loans and advances to banks at amortised cost		662,959	(17,415,810)
Loans and advances to customers at amortised cost		(18,508,983)	(29,859,562)
Derivative financial instruments for risk management		112,073	268,755
Other assets		618,268	973,676
Net increase/(decrease) in operating liabilities			
Due to banks at amortised cost		1,533,523	(9,053,664)
Due to customers at amortised cost		26,641,024	17,232,467
Derivative financial instruments for risk management		(88,322)	(277,441)
Accruals, deferred income and other liabilities		588,801	(1,063,626)
Current tax liabilities		(773,000)	(400,000)
Tax paid		(349,838)	(412,330)
Net cash inflow / (outflow) from operating activities		**14,388,411**	**(34,712,293)**
Cash flows from investing activities			
Purchase of property and equipment		(302,679)	(382,418)
Proceeds from sale of property and equipment		-	700
Purchase of financial investments		(38,136,525)	(44,415,898)
Maturity /sale of financial investments		25,229,028	52,813,490
Net cash (outflow) / inflow from investing activities		**(13,210,176)**	**8,015,874**
Cash flows from financing activities			
Subordinated liabilities		19,697	83,974
Net cash inflow from financing activities		**19,697**	**83,974**
Net increase / (decrease) in cash and cash equivalents		**1,197,932**	**(26,612,445)**
Cash and cash equivalents at the beginning of the year		65,612,043	92,224,488
Cash and cash equivalents at the end of the year		**66,809,975**	**65,612,043**

The accompanying notes on pages 47 to 110 form an integral part of the financial statements.

Notes to the Financial Statements

For the year ended 31 December 2018

1. The company and its operation

Habib Bank Zurich plc ("the Bank or HBZ UK") was incorporated in the United Kingdom on 28 January 2014 as a public limited company. The Bank is a wholly owned subsidiary of Habib Bank AG Zurich, Weinbergstrasse 59, PO Box 225, 8042 Zurich, Switzerland ("The Group). The Group's financial statements are available at www.habibbank.com.

2. Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS).

The functional currency of the Bank is Pound Sterling, which is also the presentational currency of these financial statements.

3. Basis of measurement

The financial statements have been prepared on a historical cost basis, except for the following material items:

Items	Measurement basis
Financial assets at FVOCI (applicable from 1 January 2018)	Fair value
Available-for-sale financial assets (applicable before 1 January 2018)	Fair value
Derivative financial instruments	FVTPL

4. 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 balance sheet composition, future projections of profitability, cash flows and capital resources.

The Directors have also considered the Bank's capital and liquidity plans, including stress tests in making such assessment based on growth projection as set out in long term strategic plan. Based on the assessment performed the Directors believes that the Bank has sufficient resources to continue its activities for the foreseeable future and to continue its expansion, and the Bank has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the PRA.

The Directors also considered ongoing developments related to Brexit and are of the view that any adverse outcome will not impact future viability of Bank's business.

Although the permissible measurement bases for financial assets - amortised cost, fair value through other comprehensive income and fair value though profit or loss - are similar to IAS 39, the criteria for classification into the appropriate measurement category are significantly different. IFRS 9 replaces the 'incurred loss' model in IAS 39 with an "Expected Credit Loss" (ECL) model, which means that a loss event will no longer need to occur before an impairment allowance is recognised.

5. Accounting Policies

5.1 Compliance with international Financial Standards

The financial statements of the Bank have been prepared in accordance with the Companies Act 2006 and with International Financial Reporting Standards ("IFRS") as adopted by the European Union. IFRS comprise accounting standards issued by the International Accounting Standards Board ("IASB"), as well as interpretations issued by the International Financial Reporting Interpretation Committee ("IFRIC").

This is the first set of the Bank's annual financial statements in which IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers have been applied.

Changes to significant accounting policies are described on Note 5.4.

5.2 Standards issued but not yet effective

New standards and amendments to standards have been issued by the International Accounting Standards Board, which are not yet effective for these financial statements. Out of these standards, IFRS 16 would be applicable to the Bank with effect from 1 January 2019. The key requirements are described below:

5.2.1 IFRS 16 Leases

IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use (ROU) asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low-value items. Lessor accounting remains a similar to the current standard - i.e. Lessors continue to classify leases as finance or operating leases.

IFRS 16 replaces existing leases guidance, including IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15 Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease.

The Bank will apply IFRS 16 initially on 1 January 2019, using a modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of the retained earnings as at 1 January 2019, with no restatement of comparative information.

Estimated impact of the adoption of IFRS 16

The Bank has completed an initial assessment of the potential impact on its financial statements but has not yet completed its detailed assessments. The actual impact of applying IFRS 16 on the financial statements in the period of initial application will depend on future economic condition, the development of the Bank's lease portfolio, the Bank's assessments of whether it will exercise any lease renewal option and the extent to which the Bank chooses to use practical expedients and recognition exemptions.

The Bank will recognise new assets and liabilities for its operating leases of branch and office premises. The nature of expenses related to these leases will now change because IFRS 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities. Future lease liability also includes impact of dilapidation cost to be incurred on termination of respective lease agreements.

The expected impact of adopting IFRS 16 is an increase in assets of £2.4, an increase in liabilities of £2.4 with no material impact on retained earnings. This impact assessment has been estimated under an interim control environment.

5.2.2 Other standards

The following amended standards are not expected to have a significant impact on the Bank's financial statements:

- Annual improvement to IFRS Standards 2015-2017 Cycle – various standards
- Long-term interests in associates and Joint Ventures (Amendments to IAS 28)
- Plan Amendment, Curtailment or Settlement (Amendment to IAS 19)
- IFRIC 23 Uncertainty over Income Tax Treatments
- Amendments to Reference to Conceptual Framework in IFRS Standards
- IFRS 17 Insurance Contracts

5.3 Critical accounting estimates and judgements

The preparation of the Bank's financial statements in accordance with IFRS requires management to make judgements, estimates and assumptions that affect the application of the Bank's and the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures. Actual results may differ from estimates.

Estimates and assumptions predominantly relate to ECL modelling, impairment of loans and advances and the determination of useful lives and residual values for property and equipment.

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

5.3.1 Judgement

Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the financial statements is included in the following notes:

- Note 5.5.3: classification of financial assets: assessment of business model within which the assets are held and assessment of whether the contractual terms of the financial assets are SPPI on the principal amount outstanding.

- Note 31.8: establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL.

In determining the amount of the impairment loss, the Bank is required to exercise a degree of judgement.

The accuracy of the provision would therefore be affected by unexpected changes to these assumptions.

The table below shows the estimated ECL impact on key principal portfolios for both a positive growth (Upward scenario) and a downturn (Downward scenario) of macroeconomic variables used by the Bank in estimating the Estimated Credit Loss (Loss).

The inputs have been modelled by replacing the Baseline macroeconomic variables with the Downside and Upside movement re-calibrating the PDs and LGDs.

	Impact on ECL
Improvement in Debt to GDP Ratio and unemployment rate 5%	6% decrease
Improvement in Debt to GDP Ratio and unemployment rate 10%	11% decrease
Improvement in Debt to GDP Ratio and unemployment rate 20%	22% decrease
Deterioration in Debt to GDP Ratio and unemployment rate 5%	6% increase
Deterioration in Debt to GDP Ratio and unemployment rate 10%	12% increase
Deterioration in Debt to GDP Ratio and unemployment rate 20%	24% increase

- Effective interest rate: Bank makes assumptions around the expected lives of mortgages and the collateral support to calculate the effective interest rate for specific customer. Management regularly reviews these assumptions and compares with actual results.
- Tax position: Recognition and measurement of deferred tax assets is based on business profit forecasts. Details on the recognition of deferred tax assets is provided in Note 13.
- Fair value of derivatives and financial assets: The Bank measures Fair Value through Other Comprehensive Income (FVOCI) at fair value using market prices and Derivative financial instruments based on observable market data. Note 30 provide the determination criteria of the fair value of financial instruments with significant unobservable inputs.
- Note 5.5.8 provides the recognition and measurement of provision and contingencies.

5.3.2 Assumptions and estimation uncertainties:

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ended 31 December 2018 is included in the following notes.

Impairment of financial instruments at Note 5.5.3 Page 55 explains determining inputs into the ECL measurement model, including incorporation of forward-looking information

These estimates and assumptions are explained in the notes below.

5.4 Changes in accounting policies

The Bank has initially adopted IFRS 9 and IFRS 15 from 1 January 2018.

Due to the transition method applied, the comparative year amounts have not been restated.

The adoption of IFRS 15 did not materially impacted the timing or amount of fee and commission income from contracts with customers and the related assets and liabilities recognised by the Bank as the basis of recognition of fee and commission income applied to previous accounting period was in line with the requirements of IFRS 15. Accordingly, the impact on the comparative information is limited to new disclosure requirements.

The effect of initially applying these standards is mainly attributed to the following:

- An increase in impairment losses recognised on financial assets and
- Additional disclosures related to IFRS 9

Except for the changes below, the Bank has consistently applied the accounting policies as set out on Note 5.5 to all periods presented in these financial statements.

5.4.1 IFRS 9 Financial Instruments

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement. The requirements of IFRS 9 represent a significant change from IAS 39. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities and covers three main areas:

i) Classification and measurement;
ii) Impairment; and
iii) Hedge accounting.

Although the permissible measurement bases for financial assets - amortised cost, fair value through other comprehensive income and fair value though profit or loss - are similar to IAS 39, the criteria for classification into the appropriate measurement category are significantly different. The classification of financial assets will be based on the objectives of the Bank's business model and the contractual cash flow characteristics of the instruments. The classification of financial liabilities is essentially unchanged from the treatment under IAS 39.

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an "Expected Credit Loss" (ECL) model, which means that a loss event will no longer need to occur before an impairment allowance is recognised. Impairment provisions on all financial assets are recognised based on either 12 month expected losses or lifetime expected losses. This will result in the acceleration of the recognition of impairment provisions and will lead to the reflection of more procyclical impairment charges in the income statement. However, whilst IFRS 9 represents a significant change compared to IAS 39, the quantum of impairment losses recorded against any one loan over the life of the loan will not change as IFRS 9 alters only the timing of recognition of impairment losses.

Implementation and governance of IFRS 9

The Bank implemented the requirements of IFRS 9 with the help of a group wide project. The most significant impact from IFRS 9 for the Bank is in relation to the Impairment part of the standard. Habib Bank AG Zurich (the Parent bank) led the project with input and challenge from external consultants and internal project steering committee. Model development for expected loss calculations under IFRS 9 were completed in last quarter of 2017 for financial assets and off-balance sheet items within the scope of IFRS 9.

The Bank has followed a general approach in designing ECL methodologies, which are commensurate with its size, complexity, structure, economic significance and profile of exposure. The approach taken is considered proportionate in the context of the size of the Bank within the UK financial market, its relative lack of complexity as well as minimal volatility in its credit losses over the past five years.

The assessments have been made by the Bank on the basis of the facts and circumstances that existed at the date of initial application for the determination of the business model within which a financial asset is held.

Transition

IFRS 9 is effective from 1 January 2018 and the Bank has adopted it from the date of transition.

The Bank has adopted consequential amendments to IFRS 7 Financial Instruments Disclosures that are applied to 2018 disclosures. Comparative periods generally have not been restated as the Bank used the exemption not to restate comparative periods. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

As a result of adoption of IFRS 9, the Bank has adopted consequential amendments to IAS 1 *Presentation of Financial Statements*, which require separate presentation in the statement of profit and loss and OCI of interest revenue calculated using the effective interest rate method.

Additionally, the Bank has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures about 2018, but have not been applied to the comparative information. The following table sets out the allocation of impairment on financial assets due to adoption of IFRS 9 as at 1 January 2018:

	Amount in £
Impairment on portfolio as at 1 Jan 2018 – Adoption of IFRS 9	
Due from banks	82,910
Loans and advances to customers	2,062,085
Financial investments	8,199
	2,153,194
Reversal of collective provision	(1,200,000)
Net impairment to charge in equity	953,194
Less: Deferred tax asset recognized	(162,042)
	791,152

Classification of financial assets and financial liabilities

IFRS 9 contains three principle classification categories for financial assets: measured at amortised cost (AC), fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the previous IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

IFRS 9 largely retains the existing requirements of IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

- The amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- The remaining amount of change in the fair value is presented in profit or loss.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, refer to the notes below.

5.4.2 FRS 15 Revenue from Contracts with Customers- Applicable after 1 January 2018

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.

The Bank initially applied IFRS 15 on 1 January 2018 without any practical expedients. The impact of transitioning to IFRS 15 did not materially change the basis of recognition of fee and commission in 2018 in comparison to the accounting policies applied in the previous accounting.

5.5 Significant accounting policies

As a result of adoption of IFRS 9 effective 01 January 2018 the Bank has presented relevant significant accounting policies separately for the year 2017 and 2018 as the 2017 financial statements were prepared on the basis of IAS 39 Financial Instruments: "Recognition and Measurement".

The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarised on Note 5.4.1 above.

Revenue recognition

5.5.1 Interest income and expense

Applicable after 1 January 2018

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 under stage 1 and stage 2 ; or
- The net amount (gross carrying amount less provisions held) under stage 3; or
- The amortised cost of the financial liability

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Bank estimates the future cash flows considering all contractual terms of the financial

Applicable before 1 January 2018

The Bank applies IAS 39 Financial Instruments: Recognition and Measurement.

Interest income on loans and advances at amortised cost, available for sale debt investments, and interest expense on financial liabilities held at amortised cost, are calculated using the effective interest method, which allocates interest, and direct and incremental fees and costs, over the expected lives of the assets and liabilities.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument, to the net carrying amount of the financial asset or financial liability. The effective interest method requires the Bank to estimate future cash flows, to which it uses its experience of instruments, but does not the assets' future credit losses.

The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability 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 allowance (or impairment allowance before 1 January 2018).

The 'gross carrying of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

customers' behaviour and considers all contractual terms of the financial instrument to estimate its expected lives. Due to the large number of products and types (both assets and liabilities), in the normal course of business there are no individual estimates that are material to the results or financial position.

The Bank continues to accrue interest on impaired loans using the effective interest rate method. The interest is also considered as part of the cash flows when assessing for impairment.

5.5.2 Non-interest income: Fee and commission income

The Bank adopted IFRS 15 Revenue from Contracts with Customers effective 01 January 2018. As stated in Note 5.4.2 above the timing or amount of the Bank's fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15 as the basis of recognition of fee and commission income applied to previous accounting period was in line with the requirements of IFRS 15.

The Bank provided banking services to personal and business customers, including account management, foreign currency transactions and servicing fees.

Fee and commission income is accounted for depending on the services to which the income relates:

- Revenue from account services and servicing fees is recognised over time as the services are provided.
- Commitment fees form an integral part of the effective interest rate of a financial instrument. These are recognised as an adjustment to the effective interest rate and recorded in interest income; and
- Loan termination represents fee paid by customers on early repayment of loans is recognised at the time loan is settled by the customer.
- Fees for ongoing account management are charged to the customer's account as per schedule of fee and charges. The Bank sets the rates separately for personal and business banking customers in each jurisdiction on monthly basis.
- Revenue earned on the execution of a significant act is recognised in fee income when the act is completed including trade finance income;
- Transaction-based fees for interchange and foreign currency transactions are charges to the customer's account when the transaction takes place.
- Bank provides locker services to the customers, the fee of which is charged upfront on annual basis and amortised monthly.
- Other fees charged to the customer's account when the transaction takes place

5.5.3 Financial assets and liabilities

Applicable after 1 January 2018

IFRS 9 is effective from 1 January 2018 and the Bank has adopted it from that date.

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items

The Bank initially recognises loan and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated.

Business model assessment

The Bank has considered the business model objective for each category of financial assets. For all loans and advances to banks and customers, the objective is to collect the contractual cash flows. The Bank maintains financial investments in (i) held to collect and (ii) held to collect and sell. For financial investments held to collect, the objective is to collect the contractual cash flows while for the financial investments held to collect and sell, the objective is to collect the contractual cash flows and sell the assets.

The Bank makes an assessment of the objectives of a business model in which as asset is held at a portfolio level as it best reflects the way the business is managed and information is provided to management.

Assessment whether contractual cash flows are solely payment of principal and interest (SPPI Test)

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 of the time value of money and for the credit risk associated with the principal amount during a particular period of time and for basic lending risk and costs, as well as profit margin.

The Bank has made an assessment of the cash flow characteristics (SPPI test) of financial assets and concluded that loans and advances to banks and customers will continue to be recognized at amortized cost and financial investments at fair value through other comprehensive income and at amortised cost.

In assessing whether the contractual cash flows are SPPI, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains

Applicable before 1 January 2018

The Bank applies IAS 39 Financial Instruments: Recognition and Measurement for recognition, classification and measurement, and de-recognition of financial assets and financial liabilities and the impairment of financial assets.

a contractual term that could change the timing or amount of contractual cash flows that it would not meet its condition.

As a result of the assessments made, the Bank does not consider there is any material impact to the classification and measurement of its financial assets and liabilities.

Based on Bank's assessment it does not hold any financial assets, which fail to meet the SPPI test.

Classification

On initial recognition, a financial asset classified is measured at: amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL).

Financial Assets

As required by IFRS 9 classification and measurement of financial assets is based on the Bank's business model for managing the asset and the asset's contractual cash flow characteristics.

Amortised Cost

A financial asset is measured at amortised cost if it meets both the following conditions and is not designated as FVTPL

- The asset is held with the business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified basis to cash flows that are SPPI.

Fair value through other comprehensive income (FVOCI)

A debt instrument is measured at FVOCI only if it meets both the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is achieve by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial assets give rise on specific dates to cash flows that are SPPI.

Fair value through profit and loss (FVTPL)

- All other financial assets are classified as measured at FVTPL.

Classification

Financial assets

The Bank classifies its financial assets in the following categories:

- Financial assets at fair value through profit or loss;
- Loans and advances to customers;
- Held to maturity investments; and
- Available for sale financial assets.

Management determines the classification of financial assets at initial recognition

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss comprise financial assets that are held for trading, and those designated by management as being at fair value through profit or loss on initial recognition.

Financial assets are classified as held for trading if they are acquired principally for the purposes of generating a profit from short-term fluctuations in price or dealers' margin, or form part of a portfolio of similar assets for which there is evidence of a recent actual pattern of short-term profit-taking, or are derivatives (not designated into a qualifying hedge relationship).

Loans and advances to customers

Loans and advances to customers are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and which are not classified upon initial recognition as available for sale or at fair value through profit and loss.

Loans and advances to customers are initially recognised at fair value including direct and incremental transaction costs and are subsequently measured at amortised cost, using the effective interest rate method, less any impairment losses.

Held to maturity investments

Held to maturity investments are non-derivative financial assets including debt securities with fixed or determinable payments that the management has the positive intention and ability to hold to maturity.

Held to maturity assets are initially recognised at fair value including direct and incremental transaction costs and are subsequently measured at amortised cost, using the effective interest rate method, less any impairment losses.

Available for sale financial assets

Available for sale assets are non-derivative financial assets including debt securities that are designated as available for sale on initial recognition or are not classified into any of the other categories described above.

Available for sale assets are initially recognised at fair value including direct and incremental transaction costs. They are subsequently held at fair value. Gains and losses arising from changes in fair value are included as a separate component of shareholders' equity in other comprehensive income (OCI), until sale or impairment, when the cumulative gain or loss is transferred to the income statement. Interest determined using the effective interest method, impairment losses, and translation differences on monetary assets and dividends received where the right to receive payment is established are recognised in the income statement.

Financial liabilities

All financial liabilities are measured at amortised cost, except for financial liabilities at fair value through profit or loss. Such liabilities include derivatives (other than derivatives that are financial guarantee contracts or are designated and effective hedging instruments), other liabilities held for trading, and liabilities that an entity designates to be measured at fair value through profit or loss.

Financial liabilities

Management determines the classification of all financial liabilities at initial recognition.

The Bank will classify its financial liabilities as financial liabilities designated at fair value through profit or loss if they are acquired principally for the purposes of generating a profit from short-term fluctuations in price or dealers margin, or form part of a portfolio of similar liabilities for which there is evidence of a recent actual pattern of short-term profit-taking, or they are derivatives (not designated into a qualifying hedge relationship).

The Bank classifies its financial liabilities as other financial liabilities as at balance sheet date. Other financial liabilities are measured at amortised cost, using the effective interest rate method.

Financial liabilities may be designated at fair value through profit or loss only if such a designation (a) eliminates

	or significantly reduces a measurement or recognition inconsistency; (b) applies to a group of financial assets, financial liabilities, or both that the Bank manages and evaluates on a fair value basis; or (c) relates to an instrument that contains an embedded derivative which is not evidently closely related to the host contract. Financial liabilities at fair value through profit or loss are recognised initially at fair value, with transaction costs recognised in the income statement. Subsequently, gains and losses arising from changes in fair value are recognised as they arise in the income statement.
Derecognition *Financial Assets* The Bank derecognise 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 flows in a transaction in which substantially all 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 new asset obtained less any liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss. *Financial Liabilities* The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.	**Derecognition** *Financial assets* Financial assets are derecognised when the right to receive cash flows from the assets has expired; or when the Bank has transferred its contractual right to receive the cash flows of the financial assets, and substantially all the risks and rewards of ownership; or where control is not retained. *Financial liabilities* Financial liabilities are derecognised when they are extinguished, that is when all obligations are discharged, cancelled or have expired.
Modification *Financial Assets* If the terms of a financial asset were modified, then the Bank evaluated whether the cash flows of the modified assets were substantially different. If the cash flows were substantially different, then the contractual rights to cash flows from the original financial asset were deemed to have expired. In this case, the original financial asset was derecognised and a new financial asset	**Modification** *Financial Assets* If the terms of a financial asset were modified, then the Bank evaluated whether the cash flows of the modified assets were substantially different. If the cash flows were substantially different, then the contractual rights to cash flows from the original financial asset were deemed to have expired. In this case, the original financial asset was derecognised and a new financial asset was recognised at fair value.

was recognised at fair value plus any eligible transaction cost. 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 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.

If cash flows are modified when borrower is in financial difficulties, then 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 Bank plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place.

Financial Liabilities

The Bank derecognises a financial liability when its terms were modified and the cash flows of the modified liability were substantially different. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss.

Impairment of financial assets

ECL are probability-weighted estimates of credit losses. They are measured as follows:

Financial assets that are not credit impaired at the reporting date: at the present value of all cash shortfalls i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive.

Financial assets that are credit-impaired at the reporting date: at the difference between the gross carrying amount and the present value of the future cash flows.

IFRS 9 Impairment applies to financial instruments that are not measured at fair value through profit and loss (FVTPL). Financial assets falling within the scope of impairment are provided for by calculating their Expected Credit Loss (ECL). This requires considerable judgement regarding how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

If the terms of a financial asset were modified because of financial difficulties of the borrower and the asset was not derecognised, then impairment of the asset was measured using the pre-modification interest rate.

Financial Liabilities

The Bank derecognises a financial liability when its terms were modified and the cash flows of the modified liability were substantially different. In this case, a new financial liability on the modified terms was recognised at fair value.

Impairment of financial assets

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a portfolio of financial assets not carried at fair value through the profit or loss is impaired.

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

If there is objective evidence that an impairment loss on a financial asset or group of financial assets classified as held to maturity or Loans and advances to customers has been incurred, the amount of impairment loss is measured as the difference between the asset or group of assets carrying amount and the present value of estimated future cash flows from the asset or group of assets discounted at the effective interest rate determined on initial recognition.

Estimated Credit Loss (ECL)

ECL is an estimate of present value of cash shortfalls over the life of the financial instrument, and is computed as a product of probability of default (PD), loss given default (LGD) and exposure at default (EAD). The present value of cash shortfalls is calculated by taking into account the time value of money and forward-looking information.

Probability of default (PD)

The PD represents the expected point-in-time probability of a default over the next 12 months and remaining lifetime of the financial instrument, respectively, based on conditions existing at the balance sheet date and future economic conditions that affect credit risk.

Loss given default (LGD)

The LGD represents the expected loss conditional on default, taking into account the mitigating effect of collateral, its expected value when realized, and the time value of money.

Exposure at default (EAD)

The EAD represents the expected exposure at default, taking into account the repayment of principal and interest from the balance sheet date to the default event together with any expected drawdown of a facility.

Measurement of ECL

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluation of a range of possible outcomes that incorporates forecasts of future economic conditions. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions.

In determining ECLs, the Bank has considered two economic scenarios for selected macroeconomic variables, (i) government debt to GDP and (ii) unemployment rate and weighted these according to their likely occurrence. The scenarios include a baseline scenario, based on the current economic environment, an upturn scenario and a downturn scenario. Scenario forecasts were weighted by the scenario's probability of occurrence in order to arrive at the probability-weighted macroeconomic impact over the 5 year forecast horizon.

Individual Impairment

The individual component of the total allowance for impairment applies to financial assets evaluated individually for impairment, and found to be individually impaired, and is based on management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a debtor's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function.

The values of collateral taken into consideration are assessed by professional valuers. The Bank applies an appropriate haircut to collateral values when using them for the purpose of calculating individual impairment. Haircuts applied to collateral values are based on sale of similar properties under distressed conditions.

Impairment losses are recognised in the income statement and the carrying amount of the financial assets or group of financial assets are reduced by establishing an allowance for impairment losses.

If, in a subsequent period, the amount of the impairment loss reduces and the reduction can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the income statement.

When an asset is uncollectable, it is written off against the related provision for impairment. Such assets are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are credited to the income statement.

Allowances for impairment represent management's estimate of losses incurred at the balance sheet date. Impairments are calculated on an individual basis using discounted expected future cash flows. Subjective judgements are made in this process. Changes in these estimates could result in a change in allowances and have a direct impact on the impairment charge.

For all reversals of impairments, it is noted that the decrease in the impairment loss related objectively to an event occurring after the initial impairment was recognised. None

The estimation and application of this forward-looking information will require significant judgement and be subject to appropriate internal governance and scrutiny.

Loss allowance for ECL are presented in the statement of financial position as follows:

Financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;

Loan commitments, off balance sheet items and financial guarantees: generally, as a provision;

Where a financial instrument includes both a drawn and an undrawn component / off balance sheet items, and the Bank cannot identify the ECL on the loan commitment component separately for those on the drawn components: the Bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and

Debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and recognised in the fair value reserves.

Significant increase in credit risk (SICR)

A critical element to the implementation of IFRS 9 Impairment is determining whether there has been a significant increase in risk of a credit exposure since origination to classify the assets into one of three stages as set out below.

The Bank considers 30 days past due (DPD), marking the status of a loan as non-performing, a rating downgrade, restructure tag, or cross product defaults as being strong indicators of a significant increase in credit risk of an account. Hence, staging rules have been determined based on these criteria, as explained below:

Impairment is measured as either 12 months ECL, or Lifetime ECL depending on the change in credit risk associated with the financial instrument. The approach allocates financial instruments into three stages:

of the reversals of impairments has caused the assets to have a carrying value higher than its amortised cost if the impairment had never been recognised.

All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances that are not individually significant are collectively assessed for impairment.

Collective impairment

A collective component of the total allowance is established for:

Groups of homogenous loans that are not considered individually significant; and

Group of assets that are individually significant but were not found to be individual impaired (loss ‘incurred but not reported’ or IBNR)

The IBNR allowance is based on historical loss rates, adjusted to reflect the current economic conditions affecting the portfolio. It also reflects assumptions made about the loss emergence period. The factors that may influence the loss emergence period include economic and market information, customer behaviour, portfolio management information, credit management process and collection experience.

In assessing the collective loss allowance, management considers factors such as credit quality, portfolio size, concentrations and economic factors. To estimate the required allowance, assumptions are made to define how inherent losses are modelled and to determine the required input parameters, based on historical experience and current economic conditions.

Available-for-sale financial assets

Available-for-sale financial assets are assessed at each balance sheet date for objective evidence of impairment. In assessing objective evidence of impairment at the reporting date, the Bank considers all available evidence, including observable data or information about events specifically relating to the securities, which may result in a shortfall in the recovery of future cash flows.

Objective evidence that the financial investments are impaired includes:

Staging Criteria

Stage 1 - 12 month ECL
The Bank assesses ECLs on exposures where there has not been a significant increase in credit risk since initial recognition and that were not credit impaired upon origination.

Stage2 - Lifetime ECL
The Bank assesses ECLs on exposures where there has been a significant increase in credit risk since initial recognition but are not credit impaired. Bank recognizes a lifetime ECL (i.e. reflecting the remaining lifetime of the financial asset).

Stage3 - Lifetime ECL
The Bank identifies ECLs on those exposures that are assessed as credit impaired based on whether one or more events that have a negative impact on the estimated future cash flows of that asset have occurred. For exposures that have become credit impaired, a lifetime ECL is recognized as a specific provision, and interest revenue is calculated by applying the effective interest rate to the amortised cost (net of provision) rather than the gross carrying amount.

Write off

Loan and debt securities are written off (either partially or in full) where there is no reasonable expectation of recovering a financial asset in entirely or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or source of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Recoveries of amount previously written off are included in 'impairment loss on financial instruments' in the statement of profit or loss or OCI.

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

Significant financial difficulty of a borrower or issuer;
Default or delinquency by a borrower;
The restructuring of a loan or advance by the group on terms that the group would not consider otherwise;
Indications that a borrower or issuer will enter bankruptcy;
The disappearance of an active market for a security; or
Observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

When a decline in the fair value of an available for sale financial asset has been recognised in Other Comprehensive Income (OCI) and there is objective evidence of impairment, the cumulative loss, being the difference between the asset's acquisition cost and its current fair value, less any impairment loss on that asset previously recognised in the income statement, is removed from equity and recognised in the income statement. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases, and the increase can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed. The amount of the reversal is recognised in the income statement to the extent of the increase in fair value.

Hedge accounting

IFRS 9 also incorporates new hedge accounting rules that intend to align hedge accounting with risk management practices. There is also an accounting policy choice to defer the adoption of IFRS 9 hedge accounting and to continue with IAS 39 hedge accounting. As the Bank does not currently adopt hedge accounting, this part of the standard does not currently impact the Bank.

Salford Quays skyline, Manchester

5.5.4 Derivative financial instruments

All derivative instruments are held at fair value through profit or loss. Derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative. Derivative assets and liabilities arising from different transactions are only offset, if they meet the offsetting criteria under IAS 32.

5.5.5 Employee benefits

Short-term employee benefits, such as salaries, paid absences and other benefits, are accounted for on an accrual basis over the period which employees have provided services in the year. Bonuses are recognised to the extent that the Bank has a present obligation to its employees that can be measured reliably. All expenses related to employee benefits are recognised in the income statement in staff costs, which is included within operating expenses.

The Bank provides a defined contribution pension scheme for its staff. For this scheme, the Bank recognizes contributions due in respect of the accounting period in the income statement. Any contributions unpaid at the balance sheet date are included as a liability.

5.5.6 Cash and cash equivalents

Cash and cash equivalents represent Cash in bank in current account and balances held with the central bank.

For the purpose of the cash flow statement, cash and cash equivalents include highly liquid financial assets that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in their fair value.

Such financial assets are normally those with less than three months' maturity from the date of acquisition, and include cash and balances at central banks, loans and advances to banks and FVOCI investments.

5.5.7 Property and equipment

Property and equipment are initially recognised at acquisition cost, including any costs directly attributable to bringing the assets to the location and condition necessary for it to be capable of operating in the manner intended by the Bank's management.

Property and equipment are subsequently measured using the cost model at cost less accumulated depreciation and impairment losses, if any. The Bank adheres to IAS 36, Impairment of Assets which, seeks to ensure that property and equipment assets are not carried at more than their recoverable amount (i.e. the higher of fair value less costs of disposal and value in use).

At the end of each reporting period, the Bank assesses whether there is any indication that a property and equipment may be impaired (i.e. its carrying amount may be higher than its recoverable amount). If there is an indication that a property and equipment may be impaired, then the asset's recoverable amount is calculated [IAS 36.9].

Depreciation is provided on a straight line basis over estimated useful lives as follows:

Freehold improvements	25 Years
Leasehold improvements	Over the remaining period of the lease
Motor vehicles	5 years
Furniture, fixture and fittings	3 - 7 years
Computer hardware	4 years
Buildings	40 years

The assets' useful lives are reviewed, and adjusted if appropriate, at the reporting date. Gains or losses arising on the disposal of property and equipment are determined as the difference between the disposal proceeds and the carrying amount of the assets and are recognised in profit or loss within other operating income.

5.5.8 Provisions and contingent liabilities

Provisions are recognised when it is probable that an outflow of economic benefits will be required to settle a current legal or constructive obligation as a result of past events, and a reliable estimate can be made of the amount of the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are disclosed in the financial statements unless the probability of an outflow of resources is remote.

Contingent assets are not recognised. Contingent assets are disclosed in the financial statements when an inflow of economic benefits is probable.

5.5.9 Taxes

Income tax on the profit or loss for the year comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

Current tax is the tax expected to be payable on the taxable profit for the year, calculated using tax rates enacted or substantively enacted by the balance sheet date, and any adjustment to tax payable in respect of previous year.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the balance sheet and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax asset is recognised based on availability of future taxable profit against which carry-forward tax losses can be used. Future profits are based on financial projections prepared based on some key assumptions, which may vary in future due to internal and external factors such as projected growth, economic outlook, interest rates.

Deferred tax is determined using tax rates and legislation enacted, or substantively enacted, by the balance sheet date and is expected to apply when the deferred tax asset is realised or the deferred tax liability is settled.

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously.

5.5.10 Foreign currency translation

Transactions in foreign currencies are initially recorded at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into the functional currency at the rate of exchange ruling at the reporting date.

5.5.11 Segment Reporting

The Bank undertakes commercial banking, which is carried on mainly within the United Kingdom and all other services are ancillary to commercial banking activities. The management information system and reporting to Board is also aligned to this business model.

The Bank currently manages its business activities on a centralised basis; as a result the revenue and costs are not attributable to any one operating and geographic segment. No revenue transaction with a single external customer or counterparty amounted to 10% of total revenue for the year.

5.5.12 Accounting for operating leases

The Bank applies IAS 17 Leases, for operating leases. An operating lease is a lease where substantially all of the risks and rewards of the leased assets remain with the lessor. Where the Bank is the lessor, lease income is recognised on a straight-line basis over the period of the lease unless another systematic basis is more appropriate. Where the Bank is the lessee, rentals payable are recognised as an expense in the income statement on a straight-line basis over the lease term unless another systematic basis is more appropriate.

6. Net interest income

	2018 £	2017 £
Interest income calculated using the effective interest method		
Funds held with central bank	405,918	168,727
Due from banks	1,155,875	855,029
Loans and advances to customers	17,881,127	17,851,656
Negative interest on deposits (6.1)	58,355	-
Financial investments – FVOCI (2017: AFS)	1,082,231	1,080,415
Financial investments – Amortised cost	395,441	-
	1,477,672	1,080,415
Total interest Income	**20,978,947**	**19,955,827**
Interest expense		
Due to banks	(28,640)	(249)
Due to customers	(4,299,421)	(3,817,499)
Subordinated liabilities	(402,943)	(355,829)
Total interest Expense	**(4,731,004)**	**(4,173,577)**
Net Interest Income	**16,247,943**	**15,782,250**

Interest income against loans and advances to customers included total of £213,965 (2017: £1,012,542) relating to impaired financial assets and has been considered as part of the cash flows when assessing for individual impairment provisions.

6.1 This includes the interest charged by the Bank on the deposits maintained in the currencies of Euro and Swiss Franc.

7. Net fee and commission income

	2018 £	2017 £
Fee and commission income		
Loan termination fee	291,083	177,486
Customer transaction fees	366,408	431,319
Trade Finance	375,946	498,134
Other fees and commission on banking and credit products	547,269	543,986
Total fee and commission income	**1,580,706**	**1,650,925**
Fee and commission expense		
Bank charges	(253,428)	(194,759)
Commission on internet deposits	(11,664)	(25,465)
Other fees and commission	(39,996)	(86,492)
Total fee and commission expense	**(305,088)**	**(306,716)**
Net fee and commission income	**1,275,618**	**1,344,209**

7.1 Disaggregation of fee and commission income

In the above table, fee and commission income with customers in the scope of IFRS 15 is disaggregated by major type of services.

The following table provides information about receivables and contract liabilities from contacts with customers:

	2018 £	2017 £
Receivables included in other assets	31,400	55,000
Deferred income included in other liabilities	593,054	542,708

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

8. Other income - net

	2018 £	2017 £
Receipt of insurance claim – Note 8.1	-	1,526,105
Rental income – Note 8.2	267,341	267,901
Other	3,588	(232,812)
Total other income	**270,929**	**1,561,194**

8.1 During the year 2017 the Bank received insurance proceeds relating to a claim settled with a customer in previous years.

8.2 Rent receivables under operating leases are recognised in the income statement on a straight-line basis over the period of the leases. The future minimum lease payments under operating leases are:

	2018 £	2017 £
Less than one year	267,521	267,521
Later than one year but less than five years	91,169	358,690
	358,690	**626,211**

9. Staff costs, including Directors' emoluments

	2018 £	2017 £
Salaries and allowances	(7,344,142)	(7,117,423)
Social security costs	(1,441,981)	(1,273,645)
Pension costs - defined contribution plan	(521,227)	(510,553)
Total staff costs	**(9,307,350)**	**(8,901,621)**
Average number of employees	142	137
Directors emoluments		
- Total emoluments of Directors	£573,234	£580,550
- Salary and benefits paid to the highest paid Director	£427,601	£451,725

The emoluments of Directors disclosed above include salary and social security cost. Pension contribution included in Directors emoluments is £24,000 (2017: £24,000).

The Parent bank paid emoluments of other Non-Executive directors' and has not recharged the Bank specifically for their services.

Key management personnel:

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Bank.

The key management personnel are the members of the Bank's Executive Committee together with its Directors. The table below details, on an aggregated basis, key management personnel compensation:

	2018 £	2017 £
Salaries and other short-term benefits	1,176,085	1,119,568
Post-employment benefits	69,306	71,147
Total staff costs	**1,245,391**	**1,190,715**
Loans outstanding	165,628	174,017
No of persons	2	2

The loans are on secured basis and expected to be settled in cash. The loan attracted interest rate of 3%. No provisions have been recognised in respect of loans given to key management personnel.

	2018 £	2017 £
Deposits placed - £	32,334	73,688
No of persons - Nos	4	5

10. Other operating expenses

		2018 £	2017 £
Premises running costs		(1,868,901)	(1,747,764)
Legal and Professional charges		(304,511)	(425,572)
Auditors remuneration	10.1	(125,000)	(110,000)
IT and communication costs		(406,281)	(605,569)
Branches operation charges		(587,319)	(551,026)
Group direct expenses		(1,309,629)	(1,030,597)
Travelling and conveyance		(187,045)	(120,312)
Marketing and advertisement		(2,001)	(278,765)
Miscellaneous		(79,409)	(126,898)
Total other operating expenses		**(4,870,096)**	**(4,996,503)**

10.1 Auditors remuneration

Statutory audit fee	(125,000)	(100,000)
Audit related assurance services	-	(5,000)
Non- audit services	-	(5,000)
Tax compliance services	-	-
Total Auditors remuneration	**(125,000)**	**(110,000)**

11. Reversal of Credit Impairment Losses

	2018 £	2017 £
Loans and advances to customers		
Charged during the year		
- ECL Stage 1	191,625	-
- ECL Stage 2	283,930	-
- ECL Stage 3	962,221	-
- As per IAS 39	-	2,283,638
	(1,437,776)	(2,283,638)
Recovered / settled during the year		
- ECL Stage 1	842,992	-
- ECL Stage 2	427,364	-
- ECL Stage 3	1,154,758	-
- As per IAS 39	-	2,462,518
	2,425,114	2,462,518
	987,338	178,880
Financial investments		
- ECL Stage 1	(7,142)	-
Due from banks		
- ECL Stage 1	(54,482)	-
(Reversal) / Impairment losses on financial assets	**925,714**	**178,880**

12. Taxation

	2018 £	2017 £
Corporate tax:		
Current year	(650,580)	(773,000)
Prior year	12,773	51,821
	(637,807)	(721,179)
Deferred tax:		
Current year	(129,742)	130,242
	(767,549)	**(590,937)**

		2018 £		2017 £
Tax reconciliation				
Profit before tax		4,355,628		4,991,516
Expected tax charge	(19.00)%	(827,569)	(19.25)%	(960,867)
Permanent disallowable expenses	(0.20)%	(8,733)	(2.11)%	(105,191)
Deferred tax not recognized	(0.81)%	(35,382)	1.04%	52,122
Deferred tax on losses not previously recognized	2.00%	87,072	7.44%	371,178
Impact of rate differences	0.1%	4,290		-
Prior year adjustment	0.29%	12,773	1.04%	51,821
Total tax charge	(17.62)%	**(767,549)**	(11.84)%	**(590,937)**

The corporation tax rate from 01 April 2017 to 31 March 2020 is set at 19%. A reduction in UK corporate tax rate to 17% (effective from 1 April 2020) was substantively enacted on 6 September 2016.

13. Deferred tax assets

Deferred taxes are calculated on temporary differences under the liability method using the tax rates expected to apply when the liability is settled or the asset is realised.

Deferred tax assets mainly relate to carry forward losses. The amount of carry forward losses available as at 31 December 2018 was £21.9 million (2017: £22.5 million) on which estimated amount of deferred tax not recognised amounted to £ 3.7 million (2017: £3.8 million). The Bank only account for deferred tax on the basis of future profits for a foreseeable period not exceeding four years. The Bank is of the view that assumptions used for preparing cash flow projections beyond such period are subject to significant change.

The table below shows the deferred tax assets including the movement in the deferred tax account during the year:

2018 £	Tax losses carried forward	IFRS 9 transitional arrangement	FV Loss on FVOCI investments	Total
Opening balance as at 01 January 2018	926,263	-	-	926,263
Charged to Equity (Note 27)	-	162,042	9,425	171,467
Charged to P&L	(115,919)	(13,821)	-	(129,742)
Balance as at 31 December 2018	**810,344**	**148,221**	**9,425**	**967,988**

2017 £	Tax losses carried forward	Total
Opening balance as at 01 January 2017	796,020	796,020
Charged to P&L	130,243	130,243
Closing balance as at 31 December 2017	**926,263**	**926,263**

14. Cash in hand and with central bank

		2018 £	2017 £
Balance with central bank	Note 14.1	65,846,887	64,625,164
Cash in hand		963,088	986,879
Total cash in hand and with central bank		**66,809,975**	**65,612,043**

14.1 This includes an amount of £3 million (2017: £3 million) held as a settlement cap for Image Clearing System

15. Due from banks

	2018 £	2017 £
Money market placements	43,499,129	44,107,794
Cash in current accounts	15,541,674	15,252,324
Bankers acceptances	27,635	118,370
Cash in margin accounts*	-	170,000
	59,068,438	**59,648,488**
Estimated credit loss (ECL – Stage 1)	(137,391)	-
Total due from banks	**58,931,047**	**59,648,488**

*This represents cash held with counterparty in accordance with collateral requirement under Credit Support Annex (CSA) agreements.

16. Loans and advances to customers at amortised cost

	2018 £	2017 £
Commercial loans	362,162,231	342,141,656
Overdraft	30,751,552	41,037,436
Discounted bills & trade finance loans	11,212,160	9,640,372
Other loans including staff loans	434,274	490,760
Gross loans and advances to customers	**404,560,217**	**393,310,224**
Less: Provision for impairment	(5,583,365)	(12,876,498)
Net loans and advances to customers	**398,976,852**	**380,433,726**

16.1 Provision for impairment

	2018 £	2017 £
Balance brought forward from previous year	12,876,498	16,860,868
Impairment on portfolio as at 1 Jan 2018 – Adoption of IFRS 9	862,085	-
Balance at the beginning of the year	13,738,583	16,860,868
Impairment charged to profit and loss	1,437,776	2,283,638
Reversals during the period	(2,425,114)	(2,462,518)
Net impairment charged to P&L	(987,338)	(178,880)
Write off	(7,167,880)	(3,805,490)
Total provision for impairment*	**5,583,365**	**12,876,498**

17. Financial investments

	FVOCI - debt instruments	Amortised cost - debt instruments	Total 2018	Total 2017
Cost at the beginning of the year	90,526,153	-	**90,526,153**	**98,866,096**
Change of classification due to amortised cost	(35,152,233)	35,152,233	**-**	**-**
	55,373,920	**35,152,233**	**90,526,153**	**98,866,096**
Movement during the year				
- Purchase	38,136,524	-	**38,136,524**	**44,415,898**
- Redemption / Sale	(25,229,028)	-	**(25,229,028)**	**(52,813,490)**
- Other movement	246,856	(238,656)	**8,200**	**57,649**
	13,154,352	(238,656)	**12,915,696**	**(8,339,943)**
Cost at the closing of the year	68,528,272	34,913,577	**103,441,849**	**90,526,153**
FV gain at the beginning of the year	379,900	-	**379,900**	**273,226**
Movement in FV due to change in classification	(135,440)	-	**(135,440)**	**-**
FV movement during the year	(299,900)	-	**(299,900)**	**106,674**
FV (loss) / gain at the end of the year	(55,440)	-	**(55,440)**	**379,900**
	68,472,832	34,913,577	**103,386,409**	**90,906,053**
Estimated credit loss	-	(1,553)	**(1,553)**	**-**
	68,472,832	**34,912,024**	**103,384,856**	**90,906,053**

17.1 As at 31 December 2018 all financial investments were free of any encumbrance.

* At 1 January 2018, the Bank designated certain investments as financial assets at amortised cost. In 2017, these investments were classified as available-for-sale and measured at fair value. The investment classification was changed on of adoption of IFRS as these investments are expected to be held till maturity as held to collect basis. The related FV reserve movement was adjusted in statement of changes in equity.

The financial assets designated at amortised cost at 1 January 2018 valued £35,287,673 carried ECL of £1,478 as at that date.

** This includes exposures to sovereigns and central banks.

18. Derivative financial instruments

The Bank transacts derivatives to manage and hedge its own risk and that of its customers.

The Bank uses derivatives for hedging purposes for an economic perspective in the management of its own asset and liability portfolios. This enables the Bank to mitigate the market risk, which would otherwise arise from structural imbalances.

Forward foreign exchange currency contracts are Over the Counter agreements to deliver, or take delivery of, a specified amount of an asset or financial instrument based on a specific rate applied against the underlying asset or financial instrument, at a specific date.

Derivatives are measured at their fair value, which is calculated as the present value of the future expected net contracted cash flows at market related rates as of the balance sheet date.

The fair values and notional amounts of derivative instruments are as follows:

	2018 £	2017 £
Sales	20,199,852	22,725,777
Purchase	19,953,150	23,209,613
Fair value asset	167,181	279,254
Fair value liability	137,160	225,482

19. Property and equipment

	Land	Freehold and leasehold improvements	Property and other equipment	Furniture, fixture and fittings	Motor vehicles	Total
Cost						
As at 1 January 2018	1,050,000	10,630,538	1,750,084	1,862,305	106,102	15,399,029
Additions	-	155,462	88,222	58,995	-	302,679
As at 31 December 2018	**1,050,000**	**10,786,000**	**1,838,306**	**1,921,300**	**106,102**	**15,701,708**
Accumulated Depreciation						
As at 1 January 2018	-	6,275,080	1,391,860	1,620,726	106,102	9,393,768
Depreciation	-	356,641	98,844	66,507	-	521,992
As at 31 December 2018	**-**	**6,631,721**	**1,490,704**	**1,687,233**	**106,102**	**9,915,760**
Net book value as at 31 December 2018	**1,050,000**	**4,154,279**	**347,602**	**234,067**	**-**	**5,785,948**
Net book value as at 31 December 2017	**1,050,000**	**4,355,458**	**358,224**	**241,579**	**-**	**6,005,261**

	Land	Freehold and leasehold improvements	Property and other equipment	Furniture, fixture and fittings	Motor vehicles	Total
Cost						
As at 1 January 2017	1,050,000	10,555,195	1,473,834	1,842,125	106,102	15,027,256
Additions	-	75,343	276,250	30,825	-	382,418
Disposals	-	-	-	(10,645)	-	(10,645)
As at 31 December 2017	**1,050,000**	**10,630,538**	**1,750,084**	**1,862,305**	**106,102**	**15,399,029**
Accumulated Depreciation						
As at 1 January 2017	-	5,884,546	1,308,684	1,564,126	106,102	8,863,458
Depreciation	-	390,534	83,176	67,071	-	540,781
Disposals	-	-	-	(10,471)	-	(10,471)
As at 31 December 2017	**-**	**6,275,080**	**1,391,860**	**1,620,726**	**106,102**	**9,393,768**
Net book value as at 31 December 2017	**1,050,000**	**4,355,458**	**358,224**	**241,579**	**-**	**6,005,261**

20. Other assets

	2018 £	2017 £
Corporation tax	362,611	464,151
Prepayments	289,257	268,998
Receivable from Parent bank	-	116,596
Value added tax refundable	80,836	71,938
Customer transaction fee receivable	31,400	55,000
Other	117,239	160,315
Total other assets	**881,343**	**1,136,998**

21. Due to banks at amortised cost

Due to Parent bank (Habib Bank AG Zurich, Switzerland)	10,869,263	10,053,569
Due to associates (fellow subsidiaries)	5,979,886	3,899,561
Other deposits	207,907	1,911,996
Margin held	341,593	-
Total due to banks	**17,398,649**	**15,865,126**

22. Due to customers at amortised cost

	2018 £	2017 £
Time deposits	341,945,411	304,047,648
Current and demand accounts	180,954,155	192,137,162
Margin accounts	20,000	56,457
Call deposits	573,827	611,102
Total due to customers	**523,493,393**	**496,852,369**

23. Accrual, deferred income and other liabilities

Bills payable	1,326,101	971,921
Staff costs payable	812,015	570,989
Accrued expenses	800,620	798,935
Deferred income	593,054	491,375
Other	393,171	502,940
Total accrual, deferred income and other liabilities	**3,924,961**	**3,336,160**

24. Current tax liabilities

Provision for corporation tax	650,581	773,000
Total current tax liabilities	**650,581**	**773,000**

25. Subordinated liabilities

The Parent bank, Habib Bank AG Zurich, issued a subordinated loan of £20m in 2016, providing Tier 2 capital to the Bank. The loan carries interest at a rate of 6-month Libor plus 125 bps per annum to be paid semi-annually.

The initial term of the loan is five years. The term of loan can be extended for one additional year on each anniversary with the mutual consent of both lender and borrower after the expiry of the initial term.

Subordinated liabilities are measured at amortised cost using the effective interest method under IFRS 9.

26. Share capital

	2018 £	2017 £
Called up and fully paid		
60 million authorised and fully paid ordinary shares of £1 each (2017: 60 million ordinary shares of £1 each)	60,000,000	60,000,000
	60,000,000	**60,000,000**

27. Fair value loss on financial assets at fair value through other comprehensive income (2017: Available for sale reserves)

	2018 £	2017 £
Fair value movement		
FV gain at the beginning of the year	379,900	273,226
Movement in FV due to change in classification	(135,440)	-
FV movement during the year	(299,900)	106,674
FV (loss) / gain at the end of the year	(55,440)	379,900
Deferred tax movement		
Deferred tax liability at the beginning of the year	(72,181)	(54,645)
Liability reversed due to change in investment classification	25,734	-
Net movement during the year	55,872	(17,536)
Deferred tax asset / (liability)	9,425	(72,181)
	(46,015)	307,719
Net losses of FVOCI transferred due to impairment		
- Transferred on initial application of IFRS 9	6,646	-
- FV loss during the year	7,142	-
	13,788	-
	(32,227)	**307,719**

28. Contingent liabilities and commitments

The Bank enters into transactions, which exposes it to tax, legal and business risks in the ordinary course of business. Provisions are made for known liabilities, which are expected to materialise. Contingent obligations and banking commitments, which the Bank has entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities.

	2018 £	2017 £
Direct credit substitutes		
- Guarantees	6,084,342	7,124,160
Trade related contingent liabilities		
- Letters of credit	454,545	2,130,139
- Acceptances	96,234	357,033
Unused credit facilities	19,461,681	19,073,798

Unused credit facilities refer to commitments to make loans and revolving credits.

Commitments generally have fixed expiry dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements. The potential credit loss is less than the total commitments since most commitments to extend credit are contingent upon customers maintaining specific standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

29. Related party disclosure

Details of transactions between the Bank and related parties are summarized below.

	2018 £	2017 £
Banking transactions:		
- Interest earned from Parent bank	29,649	157
- Interest and expenses paid to Parent bank *	1,722,524	1,386,426
- Transactions with parent bank and fellow subsidiaries	11,726,946	8,035,912
Outstanding balance:		
- Due to Parent bank including subordinated loan	30,972,934	30,035,943
- Due to fellow subsidiaries	5,979,886	3,899,561
- Due from related parties	11,418,906	2,709,276

The Bank's related parties include Parent bank and fellow subsidiaries.

*Interest and expenses represents interest of £412,895 (2017: £355,829) charged on borrowings and allocation of group expenses of £1,309,629 (2017: £1,030,597).

The transactions arose from the ordinary course of business and on the same terms and conditions as for comparable transactions with third party counterparties.

Key management personnel information is disclosed in note 9.

30. Fair value of financial instruments

30.1 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. It is a measure as at a specific date and may be significantly different from the amount, which will actually be paid or received on maturity or settlement date. Fair values of financial assets and liabilities measured at fair value are determined on the basis of their gross exposures. The carrying amount of the financial instruments is a reasonable approximation of fair values as illustrated in the table below.

30.2 Valuation of financial assets and liabilities

Assets and liabilities carried at fair value or for which fair values are disclosed has been classified into three levels based on significance and observability of inputs to determine the fair values.

Level 1 fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 predominantly comprise debt securities where observable prices are available in the market.

Level 2 This category comprises forward currency contracts, valued using external exchange rates.

Level 3 portfolios are those where the valuation technique includes input not based on observable data and the unobservable inputs have a significant effect on the instruments' valuation. Where the fair value cannot be reliably determined for an investment, the instrument is measured at cost.

The Bank had no level 3 financial instruments.

30.3 Financial instruments carried at fair value and basis of valuation

				Amount in £
	2018 Level 1	2018 Level 2	2018 Level 3	2018 Total
Financial investments				
- Fair value through other comprehensive income	**68,472,832**	**-**	**-**	**68,472,832**
Derivative financial instruments-assets	**-**	**167,181**	**-**	**167,181**
Total financial assets carried at fair value	**68,472,832**	**167,181**	**-**	**68,640,013**
Derivative financial instruments-liabilities	**-**	**137,160**	**-**	**137,160**
Total financial liabilities carried at fair value	**-**	**137,160**	**-**	**137,160**

				Amount in £
	2017 Level 1	2017 Level 2	2017 Level 3	2017 Total
Financial investments				
- Available for sale	**90,906,053**	**-**	**-**	**90,906,053**
Derivative financial instruments-assets	**-**	**279,254**	**-**	**279,254**
Total financial assets carried at fair value	**90,906,053**	**279,254**	**-**	**91,185,307**
Derivative financial instruments-liabilities	**-**	**225,482**	**-**	**225,482**
Total financial liabilities carried at fair value	**-**	**225,482**	**-**	**225,482**

30.4 Financial instruments not measured at fair value

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

Amount in £

	Level 1 2018	Level 2 2018	Level 3 2018	Total fair value 2018	Total carrying amount 2018
Assets					
Cash in hand and with central bank	66,809,975	-	-	66,794,215	**66,809,975**
Due from banks	-	-	58,931,047	58,931,047	**58,931,047**
Loans and advances to customers	-	-	377,180,777	377,180,777	**398,976,852**
Financial investments	32,511,735	-	-	32,511,735	**34,912,024**
Liabilities					
Due to banks	-	-	17,398,649	17,398,649	**17,398,649**
Due to customers	-	-	-	520,057,404	**523,493,393**
Subordinated liabilities	-	-	19,164,406	19,164,406	**20,103,671**

Amount in £

	Level 1 2017	Level 2 2017	Level 3 2017	Total fair value 2017	Total carrying amount 2017
Assets					
Cash in hand and with central bank	65,612,043	-	-	65,612,043	**65,612,043**
Due from banks	-	-	59,648,488	59,648,488	**59,648,488**
Loans and advances to customers	-	-	349,141,844	349,141,844	**380,433,726**
Liabilities					
Due to banks	-	-	15,856,126	15,856,126	**15,856,126**
Due to customers	-	-	495,565,249	495,565,249	**496,852,369**
Subordinated liabilities	-	-	18,987,986	18,987,986	**20,083,974**

The fair value of cash in hand and with central bank, due from banks and due to banks approximate to their carrying amount due to their short-dated nature of less than 1 year maturity.

The fair value of loans and advances to customers, due to customers and subordinated liabilities is estimated using valuation models, such as discounted cash flow techniques. Inputs into the valuation techniques include interest rates and outstanding maturities.

The fair value of other financial instruments is estimated using valuation models, such as discounted cash flow techniques. Input into the valuation techniques includes expected lifetime credit losses, interest rates and outstanding maturities.

31. Risk management

The Bank has an overall risk management framework set out in line with its risk appetite, documented within a set of risk management policies approved by the Board. Risk appetite defines the types and amounts of risk that the Bank is willing to take in pursuit of its business strategy. This is reviewed regularly and provides qualitative statements and quantitative measures to assist with the monitoring of various risk types. This process is underpinned by disclosure of risk exposures to Board, its committees and the senior management.

The Bank's approach to Risk Management is built on the principle of low to medium risk appetite and Investment return horizon, which is medium to long term. In order to achieve this, the Bank offers conventional products where the focus is on personalised customer service.

The Bank maintains an internal controls system, with clear responsibilities for risk management, applying governance model, which enables oversight and management of risks. These specific responsibilities include:

- Review and determine the risk appetite of the Bank;
- Identify and evaluate the principal risks to the Bank's Business model and the achievement of its strategic objectives, including risks that could threaten its capital or liquidity;
- Review of the risk management and internal control systems and satisfy itself that they are functioning effectively and corrective action is being taken where necessary;
- Capital, liquidity and earnings are protected by the effective controlling of the risk exposures across all material risk types and businesses;
- Ensure that an appropriate risk culture is instilled in the Bank; and
- A strong ethical and risk culture is maintained so that risk awareness is embedded into all activities.

31.1 Board Committees

The Board of Directors has established Committees of the Board for effective oversight of business strategy and key risks. To implement an effective governance process the Board established "Board Risk Committee" (BRC) and "Board Audit and Compliance Committee" (BACC).

The Board Risk Committee (BRC) oversees and challenges the risk management function to ensure that governance arrangements, risk framework and systems and controls are evaluated and managed properly. BRC periodically review the risk framework to evaluate its adequacy and appropriateness under the prevailing business environment and in light of major changes in internal or external factors. It provides assurance on the Bank-wide risk framework and monitors the overall risk profile of bank through effective control processes. BRC annually review the Risk Appetite Statement and consider the adequacy of risk limits and returns.

The independent internal audit function reports into BACC and conduct reviews of all key risk areas including the risk management framework. Reports are presented to BACC and the Board.

31.2 Management responsibilities

At an operational level the Risk Management Framework is managed through a management committee structure with delegated authorities from the Board. The Executive Committee presides over the committees and is responsible for implementing Bank's strategic objectives and managing the business with adequate controls within the risk appetite of the Bank.

The management of the Bank through committee structure allows for Enterprise Wide Risk Management through the consideration of different aspects and challenge at decision-making levels. Significant and relevant decisions and issues at other committees are escalated to EXCO for information and consideration as appropriate. This structure ensures that management of the Bank's operations, strategic decision-making and risk management are undertaken on a consultative basis at committee level by experienced functional and business personnel.

The ALCO is the committee responsible to review and recommend to the EXCO the capital and liquidity related matters. The EXCO reviews and further recommend the same to the BRC and Board for its consideration, review and approval.

31.3 Credit risk

Credit Risk is defined as loss of principal or a loss of a financial reward stemming from a borrower's failure to repay a loan or otherwise meet a contractual obligation resulting in financial loss to the Bank. It is also measured in terms of credit losses or provisions charged to the profit and loss account. Qualitative information also used to assess issues related to the effectiveness of the risk appetite.

The Bank manages its credit risk through documented Credit Risk Management Framework ("CRMF"), which is part of the overall Risk management framework. CRMF serves as a collection of tools, processes and methodologies that support the Bank in identifying, assessing, monitoring and controlling the credit risk.

The CRMF also provides a sound basis for more informed risk-based decision-making across the business areas. The CRMF includes the credit risk appetite, which defines the bank's target customer segment, industries and products, risk acceptance. CRMF reflects regulatory requirements and guidelines in the UK while also referencing the overall credit risk framework and guidelines of the Group.

Through CRMF the Board ensure that the Bank has a clear and measurable statement of its credit risk appetite against which the strategy to achieve the credit related aspects of its business plan can be actively assessed. In order to measure its achievements against this goal, the Board and management of the Bank are provided with robust, well calibrated and sufficiently granular management information so that they can provide an effective challenge to management's actions.

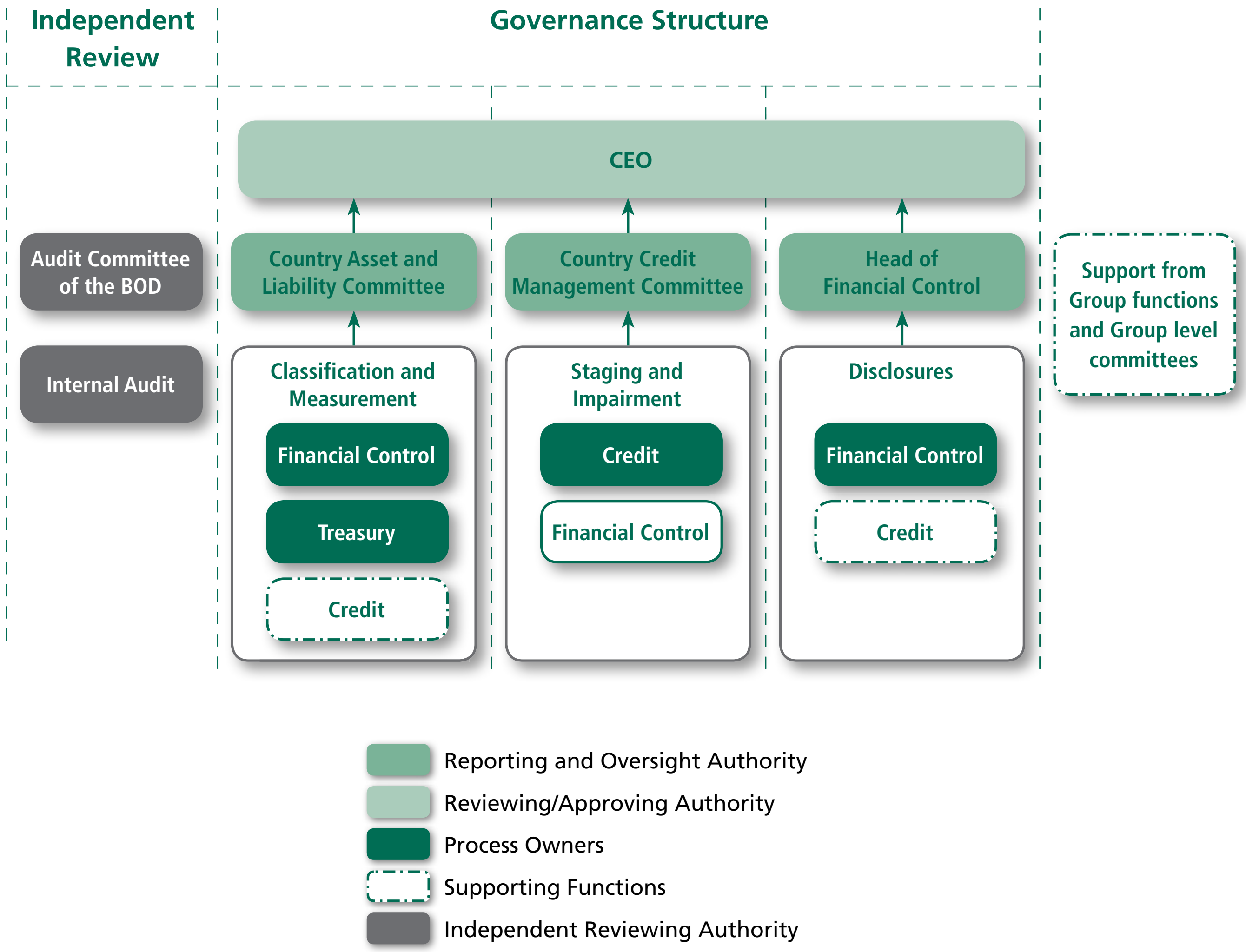
31.4 IFRS 9 Adoption

The Bank implemented IFRs 9 from 01 January 2018 by implementing suitably developed models with the assistance of external consultants. Details in respect of changes business model, classification and measurement and impairment are explained in Notes 5.4 and 5.5.3 above. In this section the Bank has provided changes made in governance and risk management on adoption of IFRS 9.

Post implementation of IFRS 9, the Bank established principles for ongoing IFRS 9 governance to ensure effective oversight of IFRS 9 processes. IFRS 9 governance structure incorporates Credit, Risk and Finance departments as central support functions for each component of IFRS 9, defines clear process owners and reviewing functions and utilises the three lines of defence to ensure an effective framework.

Governance Structure outlined below are the three lines of defence for the four key IFRS 9 processes, classification and measurement, staging, impairment and disclosures,:

- The process owners i.e. Credit, Financial Control and Treasury form the first line of defence
- The reviewing/approving functions i.e. Chief Executive Officer, Head of Financial Control, Country Credit Management Committee and Country Asset and Liability Committee form the second line of defence
- The independent review functions i.e. Internal Audit and the Audit Committee of the BOD form the third line of defence



The Bank has also put in place appropriate control to cover credit risk model governance risk. The objective was to set out the governance for the development, validation / review, deployment and maintenance of the credit risk related models. The implemented controls put in place framework for governance along the different stages of the model lifecycle.

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The purpose of these controls is to set out in particular the principles and requirements for effective governance of the Bank's Expected Credit Loss (ECL) models and methodologies used for estimating the respective risk components. The main statistical models in scope of these controls include the following:

- credit risk rating model for rating of obligors belonging to the Corporate / SME portfolios
- probability of default ("PD") models (and /or methodologies)
- loss given default ("LGD") models (and /or methodologies)
- exposure at default ("EAD") models (and /or methodologies)
- credit conversion factor ("CCF") models (and /or methodologies), and
- macroeconomic models.

For the purpose calculating ECL Bank has developed models for types of financial assets

- Customer Lending – separate models for property lending and other lending
- Investments and Financial Institutions

31.5 Probability of Default – model methodology

The Bank collects performance and default information about its credit risk exposures analysed by type of product and borrower or region as well as by credit risk grading. For some portfolios, information from external credit reference agencies is also used.

The Bank employs statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

Probability of Default is one of the three risk components needed to estimate ECL under IFRS 9. PD is defined as probability that a borrower will be unable to meet his/her debt obligations over a stipulated time period. IFRS 9 requires PD to be a Point in Time ("PiT") as opposed to a Through the Cycle (TTC) estimate, implying that the PD associated with each internal rating grade should reflect current economic conditions rather than the long-term average.

For ECL calculation, Bank segregates 'Loans and advances to customers' in two categories i.e. lending secured against property and other lending.

The methodology used to estimate the IFRS 9 calibrated PD for the Bank's Other Lending portfolio involves developing a macroeconomic model incorporating relevant macroeconomic variables for the portfolio to estimate the forward-looking default rates for a period of 5 years ranging from 2018-2022. The default rates obtained from the macroeconomic model are further calibrated for each rating grade based on the portfolio distribution.

The portfolio distribution across the internal rating grades for the Other Lending portfolio was obtained for a given reporting date. Based on the Bank's mapping of the internal rating scale with the S&P scale, the mid-point PDs were assigned to each rating grade. Further to estimating the calibrated PD for the current year for each rating grade, in order to make the calibrated PD forward looking, the S&P rating migration was used to obtain the calibrated PD curves for each rating grade from 2018-2022.

The PD was computed for the Property Lending portfolio using flow rate analysis, where migration matrices were built to track the historical performance of customers into default status over a twelve-month performance period in order to arrive at the default rate.

While developing the model, an 'ever default' definition was employed in order to capture all accounts obtaining default status over a twelve-month period, regardless of whether the customer ceased to be in default at the end of the period. The default rate obtained from this calculation is considered to be a point-in-time estimate of the PD.

31.6 Loss Given Default – model methodology

The LGD for the Other Lending portfolio is computed at an account level and leverages the Basel F-IRB LGD. The main drivers of Basel F-IRB LGD framework are seniority of the facility, facility type (secured / unsecured), security (collateral type) and security coverage of the facility (level of collateralization). The LGD computed using the Basel LGD framework is adjusted using a beta-regression. The methodology utilizes macroeconomic data and facility level collateral coverage to predict LGD estimates based on Basel LGD estimates. The adjustment is performed to reflect potential dependency on macroeconomic factors and to remove the element of conservatism (floors) included in the Basel LGD estimates.

As the Bank's Property Lending exposures essentially follow the 'Held to Collect' business model, a workout LGD approach to measurement was adopted to estimate potential losses. This approach involves use of contracts which have defaulted over a period of time to calculate internal recovery and loss cash flows to compute the 'Net Present Value' (NPV) of the loss as percentage of the EAD.

The final loss on the exposure was arrived at by adding the loss estimates for the cure, restructure and recovery nodes, weighted by the probability of the account flowing into either of the three nodes. This was divided by the Exposure at Default to derive the LGD %. The final LGD takes into account the cost of recovery and also includes a discount rate to discount the recovered amounts to the point of default.

31.7 Exposure at Default

For amortizing facilities, cash flows are used to determine the principal outstanding as of a given reporting date, while for non-amortizing facilities, such as bonds where only coupon payments are made periodically (with the principal falling due on the bond's maturity date), the principal outstanding will remain unchanged on each reporting date. Since the Bank has a low amortising portfolio 100% EAD as on the reporting date is representative of the expected exposure at default.

31.8 Determining whether credit risk has increased significantly (Significate increase in credit risk – SICR)

The Bank assesses whether credit risk has increased significantly since initial recognition at each reporting date. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower, and the geographical region. What is considered significant differs for different types of lending, in particular between wholesale and retail. As a general indicator, credit risk of a particular exposure is deemed to have increased significantly since initial recognition if, based on the Bank's quantitative modelling.

The credit risk may also be deemed to have increased significantly since initial recognition based on qualitative factors linked to the Bank's credit risk management processes that may not otherwise be fully reflected in its quantitative analysis on a timely basis. This will be the case for exposures that meet certain heightened risk criteria, such as placement on a watch list. Such qualitative factors are based on its expert judgment and relevant historical experiences.

As a backstop, the Bank considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

31.9 Curing policy

If there is evidence that there is no longer a significant increase in credit risk relative to initial recognition, then the loss allowance on an instrument returns to being measured as 12-month ECL. Some qualitative indicators of an increase in credit risk, such as delinquency or forbearance, may be indicative of an increased risk of default that persists after the indicator itself has ceased to exist. In these cases, the Bank determines a probation period during which the financial asset is required to demonstrate good behaviour to provide evidence that its credit risk has declined sufficiently. When contractual terms of a loan have been modified, evidence that the criteria for recognising lifetime ECL are no longer met includes a history of up-to-date payment performance against the modified contractual terms.

Under IFRS 9, exposures transferred into Stage 2 and Stage 3 are deemed to be significantly riskier than those falling within Stage 1. Hence the Bank seeks objective evidence of an improvement in customer credit worthiness prior to relegating a Stage 2 or Stage 3 account back to Stage 1.

The Bank follows a three-month time period or payment of three consecutive instalments for movements from Stage 3 to Stage 2 and three-month time period or payment of three consecutive instalments for movement from Stage 2 to Stage 1, implying that once the triggers for movement to Stage 2 or Stage 3 cease to exist, the exposure would still remain in Stage 2/Stage 3 for the duration of the cool-off period. Once the cool-off period is over, the exposure may be transferred out of Stage 2/Stage 3. The table below illustrates the minimum requirements for backward movement across stages. The Bank may choose to adopt a stricter cool off period in line with updates to its credit policy.

Movement	Time Period	Instalments
Stage 2 to Stage 1	3 months	3
Stage 3 to Stage 2	3 months	3

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- the criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- the criteria do not align with the point in time when an asset becomes 30 days past due;
- the average time between the identification of a significant increase in credit risk and default appears reasonable;
- exposures are not generally transferred directly from 12-month ECL measurement to credit- impaired; and
- there is no unwarranted volatility in loss allowance from transfers between 12-month PD (Stage 1) and lifetime PD (Stage 2).

31.10 Definition of default

The classification is consistent with the 90 DPD definition of default adopted by the Bank for the portfolio and the 30 & 90 DPD rebuttable presumptions provided under IFRS 9 for classification of financial instruments into Stage 2 and Stage 3.

In order to maintain a default definition consistent with both regulatory guidelines and the Bank's business practices for management of credit risk, an exposure has been considered non-performing if:

- The account is 90 or more days overdue on contractual payments; or
- Based on observed payment delays or early warning indicators detected as a result of the Country Credit function's portfolio monitoring activities, the account has been tagged as Default. The management taken such decision when the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held). Further, it is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to borrower's inability to pay its credit obligations.

While developing the model, an 'ever default' definition has been employed by the Bank in order to capture all accounts obtaining default status over a twelve-month period, regardless of whether the account ceases to be in default at the end of the period.

31.11 Impairment

IFRS 9 Impairment applies to financial instruments that are not measured at fair value through profit and loss (FVTPL). Financial assets falling within the scope of impairment are provided for by calculating their Expected Credit Loss (ECL). This requires considerable judgement regarding how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. ECL is an estimate of present value of cash shortfalls over the life of the financial instrument, and is computed as a product of probability of default (PD), loss given default (LGD) and exposure at default (EAD). The present value of cash shortfalls is calculated by taking into account the time value of money and forward-looking information.

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluation of a range of possible outcomes that incorporates forecasts of future economic conditions. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions.

In determining ECLs, the Bank has considered three economic scenarios for selected macroeconomic variables, (i) government debt to GDP and (ii) unemployment rate and weighted these according to their likely occurrence. The scenarios include a baseline scenario, based on the current economic environment, an upturn scenario and a downturn scenario. Scenario forecasts were weighted by the scenario's probability of occurrence in order to arrive at the probability-weighted macroeconomic impact over the 5 year forecast horizon.

31.12 Incorporation of forward-looking information

The estimation and application of forward-looking information requires significant judgement and are subject to appropriate internal governance and scrutiny. The Bank incorporates forward-looking information into both the assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and the measurement of ECL.

The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses.

In order to comply with the requirements of IFRS 9, the ECL estimates must be forward looking. Hence, a macroeconomic adjustment was applied to the Point in Time PD estimates for each segment.
The macroeconomic model built for Lending products contains the following exogenous variables capable of explaining the Property Lending default rates:

- Unemployment Rate
- Debt to GDP Ratio

On account of low data points, the macroeconomic model forecasts the raw default rates based on the assumption that the macroeconomic cycle repeats itself every five years.

Base, Upturn and Downturn scenario forecasts for the exogenous macroeconomic variable (i.e. Unemployment Rate) were multiplied with their respective scenario probabilities in order to arrive at a probability weighted forecast value for each year.

31.13 Modified financial assets and forbearance

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

When the terms of a financial asset are modified and the modification does not result in de-recognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

When modification results in de-recognition, a new loan is recognised and allocated to Stage 1 (assuming it is not credit-impaired at that time).

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities) 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 extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. The Group Credit Committee regularly reviews reports on forbearance activities.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired. A customer needs to demonstrate consistently good payment behaviour over a period of time before the exposure is no longer considered to be credit-impaired/in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to Stage 1.

The Bank renegotiates loans to customers in financial difficulties through processes referred to as forbearance activities to maximise collective opportunities and minimise risk of default. Under the forbearance process, loans to customers who face financial difficulties in maintaining the repayments are reviewed and analysed to assess the nature and extent of these difficulties. All such customers are either currently in default or there is a high risk of default. There is clear evidence that the customer has made all efforts to meets its financial obligation under the original contractual obligations.

All such situations are discussed and approved as per the credit sanction process by the Country Credit Committee. The Bank accommodates the forbearance situations by deferring the principal repayments, providing an Interest moratorium, converting the overdraft into an amortising loan, or by using a letter of credit to finance trade finance rather than an Overdraft.

All customers assessed under a forbearance process with revised repayment terms are kept under a close monitoring process. Once the circumstances leading to a forbearance process related to a loan no longer exists, and customers demonstrate continuous repayment history, the loan is no longer considered as forborne.

During the year, loans amounting to £4 million (2017: £13 million) were considered as forborne of which £3 million (2017: £10 million) were classified as impaired. A provision of £0.2 million (2017: £2.6 million) was made against forborne loans.

31.14 Loss allowance

The following tables show reconciliations from the opening to the closing balances of the loss allowance by class of financial instrument. Comparative amounts for 2017 represent allowance account for credit losses and reflect measurement basis under IAS39.

Amount in £

Due from banks at amortised cost	2018 Stage 1	2018 Stage 2	2018 Stage 3	2018 TOTAL	2017 TOTAL
Balances at the beginning of the year	**82,910**	**-**	**-**	**82,910**	**-**
New provisions	34,944	-	-	34,944	-
Increased provisions	19,537	-	-	19,537	-
Uncollectable recovered / settled	-	-	-	-	-
Net measurement of loss allowance	**54,481**	**-**	**-**	**54,481**	**-**
Transferred to 12 month's ECL Stage 1	-	-	-	-	-
Transferred to lifetime ECL stage 2 Credit not impaired	-	-	-	-	-
Transferred to lifetime ECL stage 3 Credit impaired	-	-	-	-	-
Balances at the closing of the year	**137,391**	**-**	**-**	**137,391**	**-**

Loans and advances to customers at amortised cost	2018 Stage 1	2018 Stage 2	2018 Stage 3	2018 TOTAL	Amount in £ 2017 TOTAL
Balances at the beginning of the year	**1,419,576**	**642,509**	**11,676,498**	**13,738,583**	**16,860,868**
New provisions	191,625	-	-	191,625	285,287
Increased provisions	-	283,930	962,221	1,246,151	1,998,351
Recovered / settled / reduced	(842,992)	(427,364)	(1,154,758)	(2,425,114)	(2,462,518)
Net measurement of loss allowance	**(651,367)**	**(143,434)**	**(192,537)**	**(987,338)**	**(178,880)**
Transferred to 12 month's ECL Stage 1	325,278	(275,756)	(49,522)	-	-
Transferred to lifetime ECL stage 2 Credit not impaired	(36,942)	324,568	(287,626)	-	-
Transferred to lifetime ECL stage 3 Credit impaired	-	(89,842)	89,842	-	-
Uncollectable written off	-	-	(7,167,880)	(7,167,880)	(3,805,490)
Balances at the closing of the year	**1,056,545**	**458,045**	**4,068,775**	**5,583,365**	**12,876,498**

The contractual amounts outstanding on financial assets that were written off during the year ended 31 December 2018 are subject to enforcement activity.

Financial investments	2018 Stage 1	2018 Stage 2	2018 Stage 3	2018 TOTAL	Amount in £ 2017 TOTAL
Balances at the beginning of the year	**8,199**	**-**	**-**	**8,199**	**-**
New provisions	1,637	-	-	1,637	-
Increased provisions	5,505	-	-	5,505	-
Uncollectable recovered / settled	-	-	-	-	-
Net measurement of loss allowance	**7,142**	**-**	**-**	**7,142**	**-**
Transferred to 12 month's ECL Stage 1	-	-	-	-	-
Transferred to lifetime ECL stage 2 Credit not impaired	-	-	-	-	-
Transferred to lifetime ECL stage 3 Credit impaired	-	-	-	-	-
Impairment of FVOCI investment shown under OCI	(13,788)	-	-	(13,788)	-
Balances at the closing of the year	**1,553**	**-**	**-**	**1,553**	**-**

The following table provides reconciliation between:

- Amounts shown in above tables reconciling of opening and closing balances of loss allowance per class of financial instrument; and
- The impairment losses on financial instruments' line item in the statement of profit and loss.

Amount in £

	Due from banks at amortised cost	Loans and advances to customers at amortised cost	Financial investments	Total
New provisions	(34,944)	(191,625)	(1,637)	(228,206)
Increased provisions	(19,538)	(1,246,151)	(5,505)	(1,271,194)
Uncollectable recovered / settled	-	2,425,114	-	2,425,114
Total	**(54,482)**	**987,338**	**(7,142)**	**925,714**

31.15 Credit quality analysis

The following table set out information about the credit quality of financial assets measured at amortised cost and FVOCI debt investments (2018) and available-for-sale debt assets (2017). Unless specifically identified, for financial assets, the amounts in the table represent the gross carrying amounts.

Amount in £

	2018 Stage 1	2018 Stage 2	2018 Stage 3	2018 TOTAL	2017 TOTAL
Cash in hand and with central bank	66,809,975	-	-	66,809,975	65,612,043
Due from banks	59,068,438	-	-	59,068,438	59,648,488
Loans and advances to customers	369,903,047	19,736,600	14,920,570	404,560,217	393,310,224
Financial investments - amortised cost	34,913,577	-	-	34,913,577	90,906,053
Financial investments - FVOCI debt instruments	68,472,832	-	-	68,472,832	-
	103,386,409	-	-	103,386,409	90,906,053
	599,167,869	19,736,600	14,920,570	633,825,039	609,476,808
Loss allowance	(1,099,244)	(458,045)	(4,165,020)	(5,722,309)	(12,876,498)
	598,068,625	**19,278,555**	**10,755,550**	**628,102,730**	**596,600,310**

The following table provides information about the credit quality of financial assets outstanding as at the balance sheet date in terms of regular, past due and impaired.

Amount in £

2018	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Total
Current & past due up to 1 month	66,809,975	59,068,438	401,207,424	103,386,409	167,181	630,639,430
Past due 1 to 3 months	-	-	1,340,185	-	-	1,340,185
Past due over 3 months	-	-	2,012,608	-	-	2,012,608
Gross exposure	66,809,975	59,068,438	404,560,217	103,386,409	167,181	633,992,223
Less: impairment	-	(137,391)	(5,583,365)	(1,553)	-	(5,722,309)
Net exposure	**66,809,975**	**58,931,047**	**398,976,852**	**103,384,856**	**167,181**	**628,269,914**

Amount in £

2017	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Total
Neither past due or impaired	65,612,043	59,648,488	333,522,170	90,906,053	279,254	549,968,008
Past due but not impaired	-	-	26,818,756	-	-	26,818,756
Past due or impaired	-	-	32,969,298	-	-	32,969,298
Gross exposure	**65,612,043**	**59,648,488**	**393,310,224**	**90,906,053**	**279,254**	**609,756,062**
Less: Individual impairment	-	-	(11,676,498)	-	-	(11,676,498)
Collective impairment	-	-	(1,200,000)	-	-	(1,200,000)
Net exposure	**65,612,043**	**59,648,488**	**380,433,726**	**90,906,053**	**279,254**	**596,879,564**

The following table sets out information about the overdue status of loans and advances to customers in Stage 1, 2 and 3:

Age bracket	2018 Stage 1	2018 Stage 2	2018 Stage 3	2018 Total	2017 Total
< 30 days	23,489,991	1,797,643	3,231,445	28,519,079	19,904,815
> 30 days to 60 days	-	370,105	160,491	530,596	12,142,878
> 60 days to 90 days	-	809,589	-	809,589	-
> 90 days to 180 days	-	-	-	0	4,826
> 180 days	-	-	2,012,608	2,012,608	5,380,844
Total overdue	**23,489,991**	**2,977,337**	**5,404,544**	**31,871,872**	**37,433,363**
Not overdue	346,413,056	16,759,263	9,516,026	372,688,345	355,876,861
Gross loans and advances to customers	369,903,047	19,736,600	14,920,570	404,560,217	393,310,224
Less: Impairment allowance	(1,056,545)	(458,045)	(4,068,775)	(5,583,365)	(12,876,498)
Net loans and advances to customers	**368,846,502**	**19,278,555**	**10,851,795**	**398,976,852**	**380,433,726**

31.16 Credit Risk Ratings

For the purpose of credit risk ratings, the Bank segregates its loans and advances portfolio into two categories namely, Property Sector lending and Other Lending (primarily comprising of commercial lending). Property sector lending covers major portion of the total lending portfolio. The Bank follows a program based lending approach for property sector lending with clearly defined Risk Acceptance Criteria (RAC) for this segment rather than a credit risk rating methodology.

The Bank recognises loans and advances as past due when the customer does not meet its contractual payment obligations.

The Bank regards a loan and advance or a debt security as impaired if there is objective evidence that a loss event has an impact on future estimated cash flows from the asset.

The following table sets out the credit quality of non-trading Financial assets split by external rating, where applicable:

Amount in £

2018	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
AAA to AA-	65,846,901	14,254,664	-	77,350,797	-	-	157,452,363
A+ to A--		201,670	-	26,034,059	30,946	3,754,117	30,020,792
BBB+ to B--		32,443,913	-	-	135,947	7,855,175	40,435,035
Unrated	963,074	12,030,800	398,976,852	-	288	34,458,107	446,429,120
	66,809,975	**58,931,047**	**398,976,852**	**103,384,856**	**167,181**	**46,067,399**	**674,337,310**

The above numbers represent the carrying values of the financial assets.

Amount in £

2017	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
AAA to AA-	64,625,164	84,427	-	79,515,452	-	-	144,225,043
A+ to A-	-	184,122	-	11,390,601	-	-	11,574,723
BBB+ to B--		56,593,632	-	-	7,748	11,587,107	68,188,487
Unrated	986,879	2,786,307	380,433,726	-	271,506	40,222,464	424,700,882
	65,612,043	**59,648,488**	**380,433,726**	**90,906,053**	**279,254**	**51,809,571**	**648,689,135**

The following table shows as analysis of counterparty credit exposures arising from derivative transactions. Derivative transactions of the Bank are fully collateralised by cash.

Amount in GBP	Total Notional amount	Total Fair value	Over-the-counter Other bilateral collateralized Notional amount	Over-the-counter Other bilateral collateralized Fair value
2018				
Derivative assets	**20,199,852**	**167,181**	**20,199,852**	**167,181**
Derivative liabilities	**19,953,150**	**(137,160)**	**19,953,150**	**(137,160)**
2017				
Derivative assets	22,725,777	279,254	22,725,777	279,254
Derivative liabilities	23,209,613	(225,482)	23,209,613	(225,482)

31.17 Concentration of Risk

Concentration arises when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar features that would cause their ability to meet contractual obligations to be affected by changes in economic, political or other conditions. The Country Credit Committee primarily manages concentration risk. The Bank Assets and Liabilities Committee also monitor credit concentration. All material exposures are reported to the Board Risk Committee, which escalates material concerns to Board of Directors.

Concentration of financial assets and credit related contingent liabilities:

Amount in £

2018	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
Supernationals	65,846,901	-	-	58,920,213	-	-	124,767,114
Financial Institutions	-	58,931,047	-	44,464,643	166,893	11,778,484	115,341,067
Industrial & commercial	-	-	335,788,938	-	288	33,373,755	369,162,981
Individual	-	-	63,187,914	-	-	915,160	64,103,074
Other	963,074	-	-	-	-	-	963,074
	66,809,975	**58,931,047**	**398,976,852**	**103,384,856**	**167,181**	**46,067,399**	**674,337,310**

Amount in £

2017	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
Supernationals	64,625,164	-	-	79,515,452	-	-	144,140,616
Financial Institutions	-	59,648,488	-	11,390,601	7,749	12,281,379	83,328,217
Industrial & commercial	-	-	311,360,830	-	271,505	37,475,611	349,107,946
Individual	-	-	69,072,896	-	-	2,052,581	71,125,477
Other	986,879	-	-	-	-	-	986,879
	65,612,043	**59,648,488**	**380,433,726**	**90,906,053**	**279,254**	**51,809,571**	**648,689,135**

Supernationals include investment made by the Bank in high rated bonds issued by sovereigns and multilateral development banks.

Geographical concentration of financial assets and credit related contingent liabilities:

2018	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Amount in £ Total
UK	66,809,975	25,730,227	369,426,479	7,535,071	125,660	38,259,903	**507,887,315**
Europe excl UK	-	7,846,212	4,425,255	66,926,536	41,521	4,698,077	**83,937,601**
Asia	-	14,250,843	5,181,752	11,263,892	-	33,672	**30,730,159**
North America	-	240,250	14,386,164	3,000,495	-	-	**17,626,909**
Africa	-	9,738,744	5,557,202	-	-	3,075,747	**18,371,693**
USA	-	1,124,771	-	10,160,894	-	-	**11,285,665**
Australia	-	-	-	4,497,968	-	-	**4,497,968**
	66,809,975	**58,931,047**	**398,976,852**	**103,384,856**	**167,181**	**46,067,399**	**674,337,310**

2017	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Amount in £ Total
UK	65,612,043	22,942,761	338,135,504	4,617,614	271,697	36,949,924	**468,529,543**
Europe	-	2,671,362	6,259,896	71,398,992	7,557	11,553,839	**91,891,646**
USA	-	24,336,714	13,463,736	-	-	23,214	**37,823,664**
Africa	-	203,112	17,676,963	-	-	220,370	**18,100,445**
Asia	-	9,193,114	4,897,627	-	-	3,062,224	**17,152,965**
North America	-	255,381	-	14,889,447	-	-	**15,144,828**
Australia	-	46,044	-	-	-	-	**46,044**
	65,612,043	**59,648,488**	**380,433,726**	**90,906,053**	**279,254**	**51,809,571**	**648,689,135**

The Bank held cash and cash equivalents of £65.8 million as at 31 December 2018 (2017: £64.6 million) with central bank that is rated at least AA- to AA+ as per approved external credit rating agencies.

31.18 Collateral Management

Collateral Risk is mitigated through the use of readily marketable collateral, avoidance of collateral with high volatility and use of haircuts as per approved Bank's policy.

Collateral values are assessed by professional valuers. The Bank uses a panel of valuers selected through a robust due diligence process. Residential or commercial collateral values used by the Bank are based on vacant possession values, which provides fair degree of conservativeness to the values used for calculating LTV. The Bank generally performs valuation of properties every five years.

Key threat arising along with controls & mitigations in place are tabulated below:

Collateral Risk	Controls & Mitigation in Place
Risk arising from reduction in collateral values	• Generally acceptable collateral - Cash, Residential & Commercial Property, Bank Guarantees, Shares & Bonds & life insurance with surrender value. • Lien is marked against cash taken as collateral • Charge is recorded in Bank's name in land registry relating to residential and commercial properties taken as collateral. • Other collateral like Bank Debenture, Stocks, Receivables, Personal Guarantees also available but discounted for lending and provision decisions. • Well defined haircuts for all collateral with Property haircuts arrived at on the basis of type of property, location and market conditions • Property Stress tests conducted every six months
Risk arising from inadequate perfection of Security for Customer Borrowing	• Credit Administration unit centralised • Standardisation of documents and processes for Risk mitigation • Duly reviewed & approved panel of solicitors & valuation firms

The Bank accepts collateral subject to legal review and appropriate documentation in accordance with the Credit Risk Management Policy. The Credit Department keeps a comprehensive record of collateral received and is responsible for regular updates to the valuation of the underlying collateral. The documentation entered into with the obligor specifies the Bank's rights and ability to liquidate the collateral, if required. The Country Credit Committee is responsible for decisions regarding liquidation or appropriation of collateral based on recommendations from the Head of Credit and advice from the Legal Department.

The carrying amount of financial assets recorded in the balance sheet, net of any allowances for losses, represents the Bank's maximum exposure to credit risk without taking account of any collateral obtained. The fair value of collateral and security enhancements held against loans or advances to customers is shown below:

Collateral Type	2018 Collateral Value	2018 Advances	2017 Collateral Value	Amount in £ 2017 Advances
Commercial real estate	585,575,250	282,820,268	558,914,497	268,904,249
Residential real estate	217,983,934	98,448,301	224,692,811	95,359,453
Cash collateral	30,929,290	20,144,691	36,840,896	24,420,145
Other collateral	-	-	2,331,453	1,049,011
Guarantees	-	-	300,000	280,878
Unsecured	-	3,146,957	-	3,296,488
Total	**834,488,474**	**404,560,217**	**823,079,657**	**393,310,224**

The Bank doesn't hold collateral against any of the financial asset other than loans and advances to the customers.

The following table stratifies credit exposures from mortgage loans and advances to customers by ranges of loan-to-value (LTV) ratio. LTV is calculated as the ratio of gross amount of the loan – to the value of the collateral. The value of the collateral for mortgage loans is based on the collateral value at origination updated based on changes in valuation. For credit-impaired loans the value of collateral is based on the most recent appraisals and taking into account any reduction in values as a result of forced sales.

Loans and Advances

							Amount in £
	2018	2018	2018	2018	2017	2017	2017
LTV Bracket	Stage 1	Stage 2	Stage 3	Total	Regular	Non-performing	Total
Less than 50%	102,314,604	13,293,970	2,026,786	117,635,360	122,674,836	5,042,898	127,717,734
51-70%	219,439,682	2,336,351	3,798,174	225,574,207	185,697,866	6,650,740	192,348,606
71-90%	38,091,484	-	477,119	38,568,603	14,001,372	-	14,001,372
91-100%	1,453,958	-	-	1,453,958	17,524,281	492,945	18,017,226
More than 100%	8,603,319	4,106,279	8,618,491	21,328,089	20,005,011	21,220,275	41,225,286
Grand Total	**369,903,047**	**19,736,600**	**14,920,570**	**404,560,217**	**359,903,366**	**33,406,858**	**393,310,224**

31.19 Market risk

Market risk refers to the risk to an institution resulting from movements in market prices, in particular, changes in interest rates, foreign exchange rates, and equity and commodity prices.

Market risk is the potential for loss of earnings or economic value due to adverse changes in financial markets. Banks involved in proprietary trading are exposed to market risk due to change in interest or foreign exchange rates.

31.20 Interest Rate Risk Management

Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair value of financial instruments. Interest rate risk at the Bank is well managed and contained and the Bank has no significant long term or complex interest rate positions. The Bank seeks to minimize the negative impact on net interest income of adverse movement in interest rates.

The Bank uses its own base rate for pricing of products, which can be changed with 30 days' notice to the customers. Therefore any significant fluctuation in interest rate is unlikely to have a material impact on the Bank as it can re-price its lending and customer deposit books. The Bank is exposed to interest rate risk on its fixed rate investment portfolio maintained to meet the Liquidity Coverage Ratio (LCR) requirement. However, this is only limited to a portion, which is monitored in ALCO.

Customers' deposits are mostly short tenors (<1year) and priced in accordance with market conditions and the Bank's cost of funds. Hence the interest rate risk on the same is limited.

The following table provides a summary of the interest rate re-pricing profile of the Bank's financial assets and liabilities. Items have been allocated to time bands by reference to the earlier of the next interest rate reset date and the contractual maturity date.

Amount in £

2018	Within 3 months	<3 to 6 months	<6 months to 1 year	<1 to 2 years	<2 to 3 years	< 3 to 4 years	<4 to 5 years	No specific re-pricing	Total
Assets									
Cash in hand & with central bank	65,846,901	-	-	-	-	-	-	963,074	66,809,975
Due from banks	37,921,953	5,524,593	-	-	-	-	-	15,484,501	58,931,047
Loans & advances to customers	1,470,259	397,066,558	-	70,070	28,500	-	341,465	-	398,976,852
Financial investments									0
- fair value through other comprehensive income	63,725,316	-	-	2,659,984	1,569,210	518,332	-	-	68,472,832
- Amortised cost	-					27,438,337	7,473,687		34,912,024
Derivative financial instruments	129,963	37,218	-	-	-	-	-	-	167,181
Total assets	**169,094,392**	**402,628,369**	**0**	**2,730,054**	**1,597,710**	**27,956,659**	**7,815,152**	**16,447,575**	**628,269,911**
Liabilities									
Due to banks	17,398,649	-	-	-	-	-	-	-	17,398,649
Due to customers	168,044,151	94,080,227	80,124,060	270,800	-	-	-	180,974,155	523,493,393
Derivative financial instruments	108,004	29,156	-	-					137,160
Subordinated liabilities	-	-	-	-	20,103,671	-			20,103,671
Total Liabilities	**185,550,804**	**94,109,383**	**80,124,060**	**270,800**	**20,103,671**	**0**	**0**	**180,974,155**	**561,132,873**
Net Gap (Assets - Liabilities)	**(16,456,412)**	**308,518,986**	**(80,124,060)**	**2,459,254**	**(18,505,961)**	**27,956,659**	**7,815,152**	**(164,526,580)**	**67,137,038**

Amount in £

2017	Within 3 months	<3 to 6 months	<6 months to 1 year	<1 to 2 years	<2 to 3 years	< 4 to 5 years	> 5 years	No specific re-pricing	Total
Assets									
Cash in hand & with central bank	64,625,164	-	-	-	-	-	-	986,879	65,612,043
Due from banks	59,083,868	564,620	-	-	-	-	-	-	59,648,488
Loans & advances to customers	1,236,575	378,592,405	597,739	-	7,007	-	-	-	380,433,726
Financial investments									-
Available for sale	35,613,279	-	19,481,491	-	-	28,319,204	7,492,079	-	90,906,053
Derivative financial instruments	212,970	66,284	-	-	-	-	-	-	279,254
Total assets	**160,771,856**	**379,223,309**	**20,079,230**	**-**	**7,007**	**28,319,204**	**7,492,079**	**986,879**	**596,879,564**
Liabilities									
Due to banks	15,865,126	-	-	-	-	-	-	-	15,865,126
Due to customers	147,480,897	74,398,432	82,734,421	45,000	-	-	-	192,193,619	496,852,369
Derivative financial instruments	176,975	48,507	-	-					225,482
Subordinated liabilities	-	-	-	-		20,083,974	-	-	20,083,974
Total Liabilities	**163,522,998**	**74,446,939**	**82,734,421**	**45,000**	**-**	**20,083,974**	**-**	**192,193,619**	**533,026,951**
Net Gap (Assets - Liabilities)	**(2,751,142)**	**304,776,370**	**(62,655,191)**	**(45,000)**	**7,007**	**8,235,230**	**7,492,079**	**(191,206,740)**	**63,852,613**

Interest Rate Sensitivity Analysis

The sensitivity to the income statement to various interest risk variables is considered on daily basis. An analysis of sensitivity to an increase or decrease in market interest rates, assuming no asymmetrical movement in yield curves and a constant financial position, is as follows at the financial year end.

	2018 Impact on P&L £	2017 Impact on P&L £
25bps increase in interest rate	68,869	18,910)
25bps decrease in interest rate	(86,249)	(55,360)
50bps increase in interest rate	137,738	37,821
50bps decrease in interest rate	(198,566)	(113,889)

31.21 Foreign Currency (FX) Risk Management

Foreign Exchange risk – is the risk that the Bank will suffer a loss as a result of an adverse movement in exchange rates.

The Bank has identified FX its risk component of its market risk that could lead to losses considering the nature of Bank's business. As the Bank is not running a trading book it is not exposed to FX risk to a large extent.

The Bank has developed various management reports to measure and manage foreign exchange risk. The Bank's open foreign exchange positions are monitored intraday. The foreign exchange exposures are managed by the treasury front office with a maximum allowable net open position ("NOP") of £1m with a maximum amount of £250,000 in a single currency. The Bank considers this an acceptable risk exposure. Client transactions are generally executed on a matched basis reducing the risk of losses. The Bank's does not engage in proprietary trading. This eliminates the likelihood of FX losses.

Key Risk Indicators exceeding tolerance are reviewed in the CCC & ALCO & reported to the Audit Risk and Compliance Committee (ARCC) together with remedial action plans.

The Bank's net open position (NOP) as at 31 December 2018 was £40,147 (2017: 26,738)

Currency	2018 (£)	2017 (£)
USD	10,539	20,240
EUR	(9,074)	(40,687)
PKR	9,838	20,241
ZAR	(6,822)	(7,254)
CAD	620	5,767
INR	24,486	23,207
Others	10,560	5,224

31.22 Liquidity Risk Management

The Bank's liquidity risk is clearly articulated in its "Liquidity Risk Management Policy" (LRMP) approved by the Board of Directors. The Bank maintains adequate liquidity levels all the time to cover its short and medium term liquidity risks over an appropriate set of time horizons for both BAU and stressed conditions. The Bank keeps a liquid asset buffer of High Quality Liquid Assets as required by European Union (EU) regulations. The Bank also maintains substantial liquidity in the Bank of England Reserve account and in short term deposits to meets its liquidity requirements.

Liquidity risk is the risk that the Bank is unable to meet its obligations as they fall due and in the currency in which they are due. Typically this arises from a mismatch in the cash flows arising from assets, liabilities and contingencies. To limit this risk, the Bank manages the maturities of its assets and liabilities and its cash flows on a daily basis.

The Bank has put in place strategies, policies, processes and systems that enable it to identify measure, manage and monitor liquidity risk over an appropriate set of time horizons, including intraday, so as to ensure that it maintains adequate levels of liquidity buffers. The Bank's liquidity policy is based on maintaining sufficient liquid resources to ensure there is no significant risk that its liabilities cannot be met as they fall due.

The Board oversees liquidity risks. The risks identified in the Bank's risk profiles are all at a level, which are in line with the current business operations and the Business Plan. The Bank has a clearly defined liquidity risk appetite approved by the Board. This forms the basis of its liquidity risk policy as well as systems and controls around the management of liquidity adequacy. The Bank will continue to review and update its liquidity risk management framework based on feedback from PRA experience and from developments in market and industry best practices.

In order to achieve the above, the Bank has identified several risk factors, which form components of the Bank's overall liquidity risk profile. These include but are not limited to:

- Wholesale secured and unsecured funding risk
- Retail funding risk
- Intra-day liquidity risk
- Intra-group liquidity risk
- Cross-currency liquidity risk
- Off-balance sheet liquidity risk
- Franchise viability risk
- Marketable assets risk
- Non-marketable assets risk
- Funding concentration risk

The Treasury Department is responsible for the day-to-day management of funding and liquidity with particular attention to the level of mismatch between assets and liabilities as well as currency exposure. The Finance Department provides daily monitoring reports against the regulatory and MI requirements, with a clear escalation process for reporting adverse outcomes. The ALCO coordinates and provides direct oversight on the whole process of liquidity risk management in accordance with their terms of reference approved by the Board.

The Bank has the following liquidity profile that analyses assets and liabilities into relevant maturity buckets based on the remaining period to contractual maturity. The maturity profile is the representative of its contractual undiscounted cash flows.

Amount in £

2018	Carrying amount	Gross nominal inflow/ (outflow)	Within 1 month	1 - 3 months	3 months - 1 year	1 - 5 years	>5 years
Financial asset by type							
Non-derivative assets							
Cash in hand & with central bank	66,809,975	66,851,919	66,851,919	-	-	-	-
Due from banks	58,931,047	59,044,540	40,423,546	13,060,901	5,560,093	-	-
Loans & advances to customers	398,976,852	476,976,221	48,749,158	6,946,491	17,169,673	68,433,977	335,676,922
Financial investments							
- fair value through other comprehensive income	68,472,832	68,580,979	1,576,431	-	12,082,061	54,922,487	-
- Amortised cost	34,912,024	35,547,952	-	-	-	35,547,952	-
	628,102,730	**707,001,611**	**157,601,054**	**20,007,392**	**34,811,827**	**158,904,416**	**335,676,922**
Derivative assets							
Risk management	167,181						
Outflow		9,510,433	2,415,487	5,396,582	1,698,364	-	-
Inflow	-	(9,314,946)	(2,371,419)	(5,295,192)	(1,648,335)	-	-
	167,181	**195,487**	**44,068**	**101,390**	**50,029**	**-**	**-**
Financial liability by type							
Non-derivative liabilities							
Due to banks	17,398,649	(17,381,208)	(17,381,208)	-	-	-	-
Due to customers	523,493,393	(526,953,998)	(280,165,890)	(70,299,907)	(176,207,042)	(281,159)	-
Subordinated liabilities	20,103,671	(20,319,786)	-	-	-	(20,319,786)	
	560,995,713	**(564,654,992)**	**(297,547,098)**	**(70,299,907)**	**(176,207,042)**	**(20,600,945)**	**0**
Derivative liabilities							
Risk management	137,160	0	-	-	-	0	0
Outflow	-	10,635,401	5,235,035	3,743,401	1,656,965	-	-
Inflow	-	(10,884,906)	(5,367,267)	(3,819,275)	(1,698,364)	-	-
	137,160	**(249,505)**	**(132,232)**	**(75,874)**	**(41,399)**	**-**	**-**

Amount in £

2017	Carrying amount	Gross nominal inflow/ (outflow)	Within 1 month	1 - 3 months	3 months - 1 year	1 - 5 years	>5 years
Financial asset by type							
Non-derivative assets							
Cash in hand & with central bank	65,612,043	65,639,480	65,639,480	-	-	-	-
Due from banks	59,648,488	59,959,782	32,994,138	26,389,416	576,228	-	-
Loans & advances to customers	380,433,726	424,842,683	42,278,118	7,730,488	21,360,472	71,952,268	281,521,337
Financial investments							
- Available for sale	90,906,053	91,672,029	3,722,859	-	20,458,184	53,820,092	13,670,894
	596,600,310	**642,113,974**	**144,634,595**	**34,119,904**	**42,394,884**	**125,772,360**	**295,192,231**
Derivative assets							
Risk management	279,254						
Outflow		12,661,562	2,651,577	4,887,832	5,122,153	-	-
Inflow	-	(12,409,172)	(2,585,360)	(4,754,305)	(5,069,507)	-	-
	279,254	**252,390**	**66,217**	**133,527**	**52,646**	**0**	**0**
Financial liability by type							
Non-derivative liabilities							
Due to banks	15,865,126	(15,847,692)	(15,847,692)	-	-	-	-
Due to customers	496,852,369	(499,779,103)	(265,155,096)	(75,570,447)	(159,008,560)	(45,000)	-
Subordinated liabilities	20,083,974	(20,263,726)	-	-	-	(20,263,726)	
	532,801,469	**(535,890,521)**	**(281,002,788)**	**(75,570,447)**	**(159,008,560)**	**(20,308,726)**	**0**
Derivative liabilities							
Risk management	225,482	-	-	-	-	-	0
Outflow	-	10,360,308	2,453,510	4,757,717	3,149,081	-	-
Inflow	-	(10,316,614)	(2,266,926)	(4,865,531)	(3,184,157)	-	-
	225,482	**43,694**	**186,584**	**(107,814)**	**(35,076)**	**0**	**0**

The Bank has disclosed a contractual maturity analysis for its financial instruments. This includes a maturity analysis for financial assets that it holds as part of its managing liquidity risk - e.g. financial assets that are expected to generate cash inflows to meet cash outflows on financial liabilities - because the Bank considers that such information is necessary to enable financial statement users to evaluate the nature and extent of its liquidity risk.

Exposure to Liquidity risk

The key measure used by the Bank for managing liquidity risk is the ratio of high quality liquid assets (HQLA) to deposits from customers and short term funding. For this purpose HQLA divided by deposits from customers and banks. Bank also considers the liquidity coverage ratio (LCR) being another strong tool for liquidity Risk. Details of the reported ratios at the reporting date and during the reporting period were as follows:

	2018 Liquidity coverage (£)	2018 HQLA to deposits (£)	2017 Liquidity coverage (£)	2017 HQLA to deposits (£)
As at 31 December	198%	23%	241%	28%
Average for the period	267%	25%	282%	29%
Maximum for the period	345%	28%	365%	36%
Minimum for the period	198%	22%	225%	23%

31.23 Financial assets and financial liabilities

- Classification of financial assets and financial liabilities

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

31-December-2018	Mandatorily at FVPTL	FVOCI - debt instruments	Amortised cost	Estimated credit loss	**Amount in £** Total carrying amount
Cash in hand and with central bank	-	-	66,809,975	-	66,809,975
Due from banks	-	-	59,068,438	(137,391)	58,931,047
Loans and advances to customers	-	-	404,560,217	(5,583,365)	398,976,852
Financial investments	-	68,472,832	34,913,577	(1,553)	103,384,856
Derivative assets held for risk management	167,181	-	-	-	167,181
Total financial assets	**167,181**	**68,472,832**	**565,352,207**	**(5,722,309)**	**628,269,911**
Due to banks	-	-	17,398,649	-	17,398,649
Due to customers	-	-	523,493,393	-	523,493,393
Derivative liabilities held for risk management	137,160	-	-	-	137,160
Current tax liabilities	-		650,581		650,581
Subordinated liabilities	-	-	20,103,671	-	20,103,671
Other liabilities	-		1,326,102		1,326,102
Total financial liabilities	**137,160**	**-**	**562,972,396**	**-**	**563,109,556**

31-December-2017	Designated As at FVPTL	Available-for-sale	Loans and receivables	Other amortised cost	Impairment loss	Amount in £ Total carrying amount
Cash in hand & with central bank	-	-	65,612,043		-	65,612,043
Due from banks	-	-	59,648,488		-	59,648,488
Loans & advances to customers	-	-	393,310,224		(12,876,498)	380,433,726
Financial investments	-	90,906,053	-		-	90,906,053
Derivative assets held for risk management	279,254	-	-		-	279,254
Other assets				160,314		160,314
Total financial assets	**279,254**	**90,906,053**	**518,570,755**	**160,314**	**(12,876,498)**	**597,039,878**
Due to banks	-	-	-	15,865,126	-	15,865,126
Due to customers	-	-	-	496,852,369	-	496,852,369
Derivative liabilities held for risk management	225,482	-	-	-	-	225,482
Current tax liabilities	-	-	-	773,000		773,000
Subordinated liabilities	-	-	-	20,083,974	-	20,083,974
Other liabilities	-	-	-	971,921		971,921
Total financial liabilities	**225,482**	**-**	**-**	**534,546,390**	**-**	**534,771,872**

- Classification of financial assets and financial liabilities on the date of initial application of IFRS 9

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Bank's financial assets and financial liabilities as at 1 January 2018.

	Original classification under IAS 39	New classifications under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Financial assets				
Cash in hand and with central bank	Loans and receivables	Amortised cost	65,612,043	65,612,043
Due from banks	Loans and receivables	Amortised cost	59,648,488	59,565,578
Loans and advances to customers	Loans and receivables	Amortised cost	380,433,726	379,571,641
Financial investments - Debt securities	Available for sale	Amortised cost	35,152,233	35,144,034
Financial investments - Debt securities	Available for sale	FVOCI	55,753,820	55,753,820
Derivative assets held for risk management	FVTPL	FVTPL (mandatory)	167,181	167,181
Total financial assets			**596,767,491**	**595,814,297**

	Original classification under IAS 39	New classifications under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Financial liabilities				
Due to banks	Amortised cost	Amortised cost	15,865,126	15,865,126
Due to customers	Amortised cost	Amortised cost	496,852,369	496,852,369
Derivative liabilities held for risk management	FVPTL	FVPTL (held-for-trading)	225,482	225,482
Subordinated liabilities	Amortised cost	Amortised cost	20,083,974	20,083,974
Total financial liabilities			**533,026,951**	**533,026,951**

The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018:

	IAS 39 carrying amount	Reclassification	Re-measurement	IFRS 9 carrying amount 01 Jan 2018
Financial assets				
Amortised cost				
- Loans and advances to banks	59,648,488	-	(82,910)	59,565,578
- Loans and advances to customers	380,433,726	-	(862,085)	379,571,641
Investment securities				
- Opening balance (available-for-sale)	90,906,053	(35,152,233)	-	55,753,820
- Transferred to Amortised cost	-	35,152,233	(8,199)	35,144,034
	90,906,053	-	(8,199)	90,897,854
	530,988,267	**-**	**(953,194)**	**530,035,073**

The Bank's accounting policies on the classification of financial instruments under IFRS 9 are set out in relevant notes. The application of these policies resulted in the reclassifications set out in the tables above and explained below.

- Before the adoption of IFRS 9, certain debt investments were designated as available for sale categories at their then fair values. On the adoption of IFRS 9, the carrying amount of those assets was adjusted to their amortised cost under IFRS 9 as on 1 January 2018.
- Before the adoption of IFRS 9, bank holds derivatives at FVPTL, these assets meet the criteria of mandatory measurement of FVPTL because the contractual cash flows are not SPPI on the principal outstanding.

31.24 Encumbered assets

Certain assets are pledged as collateral to secure liabilities under Credit Support Annex ("CSA") for derivative liabilities and as security deposits relating to FX forward transactions. The holders of these securities do not have the right to sell or re-pledge the asset except where specifically disclosed. The aggregate amount of collateral pledged under CSAs is nil as on 31 December 2018 (2017: £ 170,000).

31.25 Operational Risk Management

Operational Risk is the risk that the Bank triggers one or more of the below situations due to failed internal processes, people and systems – these can be internal or external to the Bank:

- Adversely impacts customers (customers are defined as customer of the Bank as well as internal "customers" such as colleagues with a dependency on particular output or service)
- Incurs losses e.g. operational losses (this includes temporary losses i.e. where recovery is made or is in progress of being made)
- Breaches in regulatory requirements or other policies and practices of the Bank

The Bank's operational processes exist to support the servicing of customers and to maintain compliance with relevant regulation. These imperatives will be robustly protected. The Bank will ensure that it remains compliant with the latter but its approaches to the former will vary according to priority and need. In terms of customer service the Bank will actively employ flexible approaches to maintaining and protecting delivery and to this end will incur reasonable costs as required.

The Bank adopts the Basic Indicator approach for calculating Operational Risk capital as set out in the CRR and consequently embarks on rigorous risk identification exercises to establish any Pillar 2 requirements for Operational Risk.

31.26 Capital Management and Risk

The primary objective of capital management is to maintain strong capital to support medium to long-term business growth. An effective capital management process provides resilience arising from both internal and external factors resulting in additional capital requirements. The Bank maintains strong capital ratios not only to support its business and maximise shareholders' value but also to maintain depositors' and market confidence. The Prudential Regulation Authority sets and monitors the capital requirement for the Bank.

The Bank's capital has been invested by the Parent bank to support long-term business growth of the Bank, which includes capital resources to meet Pillar 1, Pillar 2, CRD Buffers and PRA Buffer. The Bank also maintains an internal capital buffer over and above the minimum regulatory capital requirement. The Bank also takes into account changes in economic conditions; risk characteristics of its activities and regulatory requirement in managing its capital structure and make adjustments to it in the light of such changes. The bank has put in place processes and controls to monitor and manage its own funds and no breaches were reported to the PRA during the period.

The Bank's regulatory capital consists of the sum of the following elements:

- Common equity Tier 1 (CET 1) capital, which includes ordinary share capital and retained earnings, and
- Tier 2 capital which includes qualifying subordinated liabilities.

	2018 £	2017 £
Share capital	60,000,000	60,000,000
Retained earnings	10,229,002	7,432,075
Tier 1 capital	**70,229,002**	**67,432,075**
Subordinated liability	20,000,000	20,000,000
IFRS 9 (ECL) impact of regulatory capital	348,911	-
	20,348,911	20,000,000
Own funds	**90,577,913**	**87,432,075**

32. Ultimate Parent Company

The Bank is a wholly owned subsidiary undertaking of Habib Bank AG Zurich, which is the ultimate controlling parent, incorporated in Switzerland. The largest group in which the results of the company are consolidated is Habib Bank AG Zurich, Switzerland.

33. Significant Events after the Balance Sheet Date

A final dividend for 2018 of £0.0299 per ordinary share (a distribution of approximately £1.794 million) was declared by the Directors after 31 December 2018. These accounts were approved by the Board of Directors on 12 April 2019 and authorised for issue.

The Directors confirm that there have been no significant events since the reporting date what require to be disclosed.

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International Network

1 Switzerland	Habib Bank AG Zurich	1 Branch
2 United Kingdom	Habib Bank Zurich plc	8 Branches
3 United Arab Emirates	Habib Bank AG Zurich	8 Branches
4 Pakistan	Habib Metropolitan Bank Ltd	352 Branches
5 United Arab Emirates	HBZ Services FZ LLC	1 Branch
6 Kenya	Habib Bank AG Zurich	5 Branches
7 South Africa	HBZ Bank Ltd	10 Branches
8 Canada	Habib Canadian Bank	3 Branches
9 Hong Kong	Habib Bank Zurich (Hong Kong) Ltd	5 Branches
10 Pakistan	Habib Bank AG Zurich	Representative Office
11 Hong Kong	Habib Bank AG Zurich	Representative Office
12 Bangladesh	Habib Bank AG Zurich	Representative Office

Habib Bank AG Zurich is the trading name of Habib Bank Zurich plc.
Registered office: Habib House, 42 Moorgate, London EC2R 6JJ.
Registered in England and Wales: Company registered number: 08864609.

Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority
and the Prudential Regulation Authority under registration number 627671.
Habib Bank Zurich plc is covered by the Financial Services Compensation Scheme.