FCM Bank Limited

Annual Report and Financial Statements 31 December 2023

Company Registration Number: C 50343

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Directors' report

The Directors present their report and the audited financial statements of FCM Bank Limited ('the Bank') for the year ended 31 December 2023.

Principal activities

The Bank is licensed as a credit institution under the Maltese Banking Act (Cap. 371).

Performance Review

During the year under review, the Bank generated operating income of €12,544,031 (2022: €7,981,378) resulting in a profit before tax of €4,100,985 (2022: €2,500,681) and profit after tax of €2,374,029 (2022: €1,963,695). The improvement in the overall performance of the Bank was largely driven by the increase in interest income as a result of growth of its corporate lending business and increase in the interest rates. The Bank remained liquid and well capitalised as it focussed its efforts on developing its business.

During the year, the Bank continued to concentrate on its corporate lending business and its investment portfolio of fixed income securities. During 2023, loans and advances to customers increased by €132,722,902 (2022: €71,207,430), bringing the total loans and advances to customers as at the financial year end to €341,683,843 (2022: €208,960,941). The Bank's customer deposits increased by €140,250,347 during the year (2022: increased by €122,635,893), bringing total deposits up to €404,335,641 (2022: €264,085,294).

The Bank evaluates the achievement of its objectives or otherwise through the use of financial and non-financial measures. The Bank measures its Liquidity Risk with a minimum regulatory ratio at 30% as per BR/05/2007 Liquidity Requirements Of Credit Institutions Authorised Under The Banking Act 1994, and its Liquidity Coverage Ratio with a minimum of 100% as per Delegated Regulation (EU) 2015/61 supplementing Regulation (EU) No 575/2013 with a minimum of 100%. In both cases, the Bank's ratios were higher.

During financial year ended 31 December 2023, the socioeconomic impact of the Covid-19 pandemic subsided, with a significant rebound in economic growth registered during 2022 and 2023, restoring the local economy to pre-Covid levels. The economic growth registered was a result of a recovery in the tourism sector in the aftermath of the Covid-19 pandemic as well as an increase in private consumption.

Notwithstanding the above, the level of economic uncertainty remained elevated during 2023, primarily driven by increased inflation rate in the European Union. Inflation has risen substantially in both the euro area and in the US since the reopening of economies across the world after the COVID-19 pandemic, with a significant acceleration in prices following Russia's invasion of Ukraine in February 2022. The one key factor driving inflation dynamics has been energy costs, as well as widespread supply chain disruptions experienced as the world economy recovers from the impacts of the pandemic.

Considering economic and financial data and assessment of the inflation outlook, after July 2022, the ECB increased its fixed interest rate almost monthly. As of December 2023, the rate was 4.5 percent, the highest since the global financial crisis in 2007 and 2008.

As a result, economic uncertainty continued to prevail especially in view of the increasing interest rate environment and inflationary pressures, partially mitigated by government support measures. Inflation in Malta reached 5.6% in 2023, despite energy prices being kept at 2020 levels by government intervention. However, increased rates attracted more deposits from local market as well as from online platforms. Due to the higher cost of funding and market pressure the Bank increased its Base Rate to mitigate the negative impact of increased ECB rates.

Directors' report - continued

Key performance indicators

The Board of Directors tracks the Bank's progress in implementing its strategy with a range of financial measures or key performance indicators ('KPIs'). Progress is assessed by comparison with the Bank's budgets and historical performance. The financial KPIs tracked by the Board of the Bank are presented in the following table.

	2023 **€**	2022 €
Profit before tax for the year	**4,100,985**	2,500,681
Profit for the year	**2,374,029**	1,963,695
Total own funds	**75,375,649**	51,744,020
Capital adequacy ratio	**17%**	17%
Leverage ratio	**14%**	15%

Principal risks and uncertainties

The Board has designed a solid risk management framework and set a prudent risk appetite for the Bank. The Bank's risk management approach depends on the interaction of a number of key components from risk identification through to assessment, quantification and mitigation. This ensures that the Bank's strategy is consistent with its risk appetite and that optimal risk-return decisions are taken within appropriate structures. The ultimate responsibility for risk management rests with the Directors who have identified the following principal risks and uncertainties facing the Bank:

People risk

In spite of its small size and growth in staff numbers, the Bank is exposed to people risk arising principally from the loss of, or dependency on, key employees. The Bank is committed to be more focused on succession planning. The Bank mitigates the risk of single dependency through ensuring continuity in the absence of any individual. During the year the number of staff has doubled and within each team additional employees have been onboarded to be in line with business, regulatory, and operational requirements.

Strategy risk

During 2023 and 2022, the Bank registered substantial growth in its corporate lending business. This growth was in line with its strategic objectives and business plan. Total drawdowns were somewhat below the annual budget however the Bank retained its position in the Maltese market. The Bank is well capitalised and has in place a clearly defined capital strategy. This strategy is supported by regular capital injections by the main shareholder.

Reputational risk

The Bank's reputation is, of course, of vital importance to its continued progress and is essential in attracting business, since any damage to its good standing would negatively impact the trust that customers require to do business with a financial institution. The Bank is fully focused on developing and maintaining its good name.

Business risk management

Business risk is the risk of losses due to failed or inadequate strategy execution, marketing and sales practices, distribution channels, pricing, handling of customer complaints or late reaction to changes in the business environment. The Bank has a strong governance framework to mitigate this risk. The Risk Committee has been meeting on a regular basis and each potential risk has been assessed and evaluated.

Directors' report - continued

Financial risk management

Note 2 to the financial statements provides details in connection with the Bank's use of financial instruments, its financial risk management objectives and policies and the financial risks to which it is exposed.

Result and dividends

The results for the year ended 31 December 2023 are shown in the statement of profit or loss and other comprehensive income on pages 17 and 18. The profit before tax was €4,100,985 (2022: €2,500,681). The profit after tax for the year was €2,374,029 (2022: €1,963,695). As at 31 December 2023, the retained earnings of the Bank amounted to €2,863,483 (2022: €3,545,705).

In view of the above results, the Board of Directors will be recommending the payment of a dividend of €1,400,000 for the year 2023. Furthermore, the outlook for 2024 appears to be positive and in the course of this year, the Board of Directors will consider the payment of interim dividends if the profits of the Company justify such payments.

Shareholder's contribution

The Bank has been growing its asset base significantly, and this was supported by shareholder's capital contributions. By virtue of a resolution dated 27 March 2023, the shareholders of the Bank resolved to, subject to approval of MFSA, convert Perpetual Capital notes instrument amounting to €2,000,000 to issued share capital. Upon approval of MFSA, by virtue of resolution dated 9 May 2023, the Bank increased its issued share capital by €2,000,000 divided into 2,000,000 ordinary shares of a nominal value of €1.00 each from €39,750,000 (divided into 39,750,000 ordinary shares of a nominal value of €1.00 each) to €41,750,000 (divided into 41,750,000 ordinary shares of a nominal value of €1.00 each). Accordingly, the Bank reclassified this amount from 'Perpetual capital notes' to Share capital' (Note 14).

By virtue of a resolution dated and effective 30 March 2023, the Bank increased further its issued share capital by €4,500,000 divided into 4,500,000 ordinary shares of a nominal value of €1.00 each from €41,750,000 (divided into 41,750,000 ordinary shares of a nominal value of €1.00 each) to €46,250,000 (divided into 46,250,000 ordinary shares of a nominal value of €1.00 each).

By virtue of a resolution dated and effective 17 July 2023, the Bank increased further its issued share capital by €6,000,000 divided into 6,000,000 ordinary shares of a nominal value of €1.00 each from €46,250,000 (divided into 46,250,000 ordinary shares of a nominal value of €1.00 each) to €52,250,000 (divided into 52,250,000 ordinary shares of a nominal value of €1.00 each).

Future business developments

The Bank will continue to focus on the development of its product portfolio in line with its strategy and business plan and intends to continue growing its corporate lending business. The Directors believe that the present outlook is positive and strongly believe that in the foreseeable future this main income stream should be pursued further.

Directors

The Directors who served throughout the year were as follows:

John Soler
Petr Cumba
Ondrej Korecky
Martin Farsky – resigned on 30 November 2023
Michael Borg Costanzi
Lino Casapinta
Dusan Benda
Jiri Voda

Directors' report - continued

Statement of Directors' responsibilities for the financial statements

The Directors are required by the Maltese Banking Act (Cap. 371) and the Maltese Companies Act (Cap. 386) to prepare financial statements that give a true and fair view of the state of affairs of the Bank as at the end of the financial year and of the profit or loss of the Bank for that year in accordance with the requirements of International Financial Reporting Standards, as adopted by the European Union.

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

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

The financial statements of the Bank for the year ended 31 December 2023 are included in the Annual Report 2023, which is published in hard-copy printed form and is available on the Bank's website. The Directors are responsible for the maintenance and integrity of the Annual Report on the website in view of their responsibility for the controls over, and the security of, the website. Access to information published on the Bank's website is available in other countries and jurisdictions, where legislation governing the preparation and dissemination of financial statements may differ from requirements or practice in Malta.

The Directors are also responsible for designing, implementing, and maintaining internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and that comply with the Maltese Banking Act (Cap. 371) and the Maltese Companies Act (Cap. 386). They are also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditors

PricewaterhouseCoopers have indicated their willingness to continue in office and a resolution for their re-appointment will be proposed at the Annual General Meeting.

Approved by the Board of Directors on the 2 April 2024 and signed on its behalf by:

John Soler **Director**	Michael Borg Costanzi **Director**

Registered Office:
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Tower Street, Swatar
Birkirkara, BKR 4013
Malta

Independent auditor's report

To the Shareholders of FCM Bank Limited

Report on the audit of the financial statements

Our opinion

In our opinion:

- The financial statements give a true and fair view of the financial position of FCM Bank Limited (the Bank) as at 31 December 2023, and of the Bank's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU; and
- The financial statements have been prepared in accordance with the requirements of the Maltese Banking Act (Cap. 371) and Maltese Companies Act (Cap. 386).

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

What we have audited

FCM Bank Limited's financial statements, set out on pages 16 to 80, comprise:

- the statement of financial position as at 31 December 2023;
- the income statement and statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, comprising material accounting policy information and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

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

Independence

We are independent of the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code) together with the ethical requirements of the Accountancy Profession (Code of Ethics for Warrant Holders) Directive issued in terms of the Accountancy Profession Act (Cap. 281) that are relevant to our audit of the financial statements in Malta. We have fulfilled our other ethical responsibilities in accordance with these Codes.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Bank are in accordance with the applicable law and regulations in Malta and that we have not provided non-audit services that are prohibited under Article 18A of the Accountancy Profession Act (Cap. 281).

The non-audit services that we have provided to the Bank, in the period from 1 January 2023 to 31 December 2023, are disclosed in the Note 28 to the financial statements.

Our audit approach

Overview

Materiality	• Overall materiality: €5,116,000, which represents 1% of total assets. • Specific materiality solely for financial line items in the income statement: €205,000, which represents 5% of profit before tax.
Key audit matter	• Credit loss allowances in respect of loans and advances to customers

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we considered where the directors made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

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

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Independent auditor's report - continued

To the Shareholders of FCM Bank Limited

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Overall materiality	€5,116,000
How we determined it	Approximately 1% of total assets
Rationale for the materiality benchmark applied	We chose total assets as the benchmark because, in our view, the assets held are considered as the key driver of the business and the determinant of the Bank's value and is a generally accepted benchmark. We chose 1% which is within the range of quantitative materiality thresholds that we consider acceptable.
We have applied a specific materiality of €205,000 solely for the financial statement line items in the Income Statement, since the engagement team deemed that misstatements in those line items of a lower amount than overall materiality might reasonably influence stakeholders.	

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above €153,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	How our audit addressed the Key audit matter
Credit loss allowances in respect of loans and advances to customers Credit loss allowances in respect of loans and advances to customers represent management's best estimate of expected credit losses ('ECLs') within the loan portfolio at the balance sheet date. The development of the models designed to estimate ECLs on the Bank's loans to customers, measured at amortised cost in accordance with the requirements of IFRS 9, requires a considerable level of judgement since the determination of ECLs is subject to a high degree of estimation uncertainty. All loans and advances to customers are considered individually significant. As as result, credit loss allowances relating to all non-defaulted loans and advances to customers are determined at instrument level through the use of an ECL model. Through its ECL model, the Bank calculates ECLs by multiplying three main components: probability of default (PD), loss given default (LGD) and exposure at default (EAD) i. Probability of default ("PD"): the likelihood of a borrower defaulting on its financial obligation either over the next 12 months or over the remaining lifetime of the obligation. ii. Loss given default ("LGD"): the expected losses taking into account, among other attributes, the mitigating effect of collateral value (if any) at the time it is expected to be realised and the time value of money. Exposure at default ("EAD"): the expected exposure in the event of a default (including any expected drawdowns of committed facilities).	During our audit of the financial statements for the year ended 31 December 2023, we continued to focus on the key drivers of the estimation of ECLs. Since modelling assumptions and parameters are based on peer data, we independently assessed the appropriateness of management's judgements in respect of the calibration of PDs. We also assessed the reasonableness of the PDs under multiple scenarios and the LGDs generated by the model. The appropriateness of the modelling methodology and the key parameters used within the ECL calculations were discussed extensively with management. Discussions with management and the audit committee also included staging classification of individual borrowers and assumptions in the determination of ECLs for impaired loan. Our audit procedures in respect of credit loss allowances attributable to loans and advances to customers of the Bank included: • Ensuring that the granting of facilities was performed in accordance with the approval criteria of the Bank; testing of controls implemented by management over the monitoring of arrears, and of controls ensuring the necessary follow up actions on past due loans are satisfactorily resolved. We tested the design and operating effectiveness of these controls and determined that we could rely on these controls for the purposes of our audit.

Independent auditor's report *- continued*

To the Shareholders of FCM Bank Limited

Key audit matter	How our audit addressed the Key audit matter
Within the ECL model for non-defaulted (Stages 1 and 2) exposures, in the absence of sufficient internal historical default data, the Bank's starting point PDs are derived by reference to published peer data for similar portfolios which might result in limitations in appropriately estimating ECLs. For exposures secured by immovable properties, LGDs are driven by the loan-to-value ratio of the individual facilities taking into account other assumptions including market value haircut (which includes costs to sell), time to sell and the impact of discounting the collateral from the date of realisation back to the date of default. The maximum period considered when measuring ECLs is the maximum contractual period over which the Bank is exposed to credit risk. Under IFRS 9, the Bank is also required to formulate and incorporate multiple forward-looking economic conditions, reflecting management's view of potential future economic variables and environments, into the ECL estimates. The complexity attributable to this factor requires management to apply significant judgements within the ECL estimates to meet the measurement requirements of IFRS 9. Data used in the impairment calculation is manually compiled. The ECL model is based on a general-purpose application which requires extensive manual handling of data. This increases risk around the accuracy and completeness of data used to determine assumptions and to operate the ECL model. In some cases, data is unavailable and reasonable alternatives have been applied to allow calculations to be performed.	• Testing of a sample of exposures to independently review the borrower's financial performance and ability to meet loan repayments and assess the appropriateness of the stage classification assigned by management. • Assessing the reasonableness of the starting point PD derived by reference to peer data as well as the modelling methodology applied to determine life-time PDs. • Testing the completeness and accuracy of the critical data utilised within the models for the year-end ECL calculations, including agreeing the terms of the exposures to supporting documentation. • Reviewing, on a sample basis, property collateral valuations utilised to determine LGDs applied by the Bank within ECL calculations. • Challenging the application of certain parameters considered in the LGD estimations such as the time to realise the collateral and costs associated with such process. • Assessing whether the severity in respect of modelled scenarios was appropriate in view of the surrounding economic conditions. • Testing independently the model calculations. • Reviewing the credit files of defaulted loans to understand the latest developments at the level of the borrower and the basis of measuring the ECL provisions and considering whether key judgements were appropriate given the borrowers' circumstances.

Key audit matter	How our audit addressed the Key audit matter
Judgement is also required to determine when an increase in credit risk or a default has occurred and as a result, allocate the appropriate stage classification. Staging is determined based on a combination of criteria including days past due criteria, the regular monitoring of the performance of borrowers against forecasts, as well as strategic developments affecting the borrowers' future payment capabilities. For defaulted (Stage 3) exposures, discounted cash flow models are utilised to estimate ECL. Judgment is required to estimate future cash flows under multiple scenarios, which are highly dependent on assumptions in respect of realising the collateral. Since the estimation of ECLs is subjective in nature and inherently judgemental, the Bank's application of the IFRS 9 impairment requirements is deemed to be an area of focus. We focused on credit loss allowances due to the subjective nature of specific data inputs into the calculation and the subjective judgements involved in both timing of recognition of impairment and the estimation of the size of any such impairment. Relevant references in the Annual Report and Financial Statements: - Accounting policy: Note 1.3; - Credit risk management: Note 2.1.1; - Critical accounting estimates, and judgements in applying accounting policies: Note 3; - Note on Loans and advances to customers: Note 8; and - Note on Changes in expected credit losses and other credit impairment charges: Note 26.	• Determining different scenarios in respect of defaulted exposures and their respective probability weights independently, and formed our view (based on detailed loan and customer information in the credit file) on the recoverability of the selected defaulted exposures. Based on the evidence obtained, we found the model assumptions, data used within the models and model calculations to be reasonable. In the case of some ECL allowances, we formed a different view from that of management, but in our view the differences were within a reasonable range of outcomes.

Independent auditor's report - continued

To the Shareholders of FCM Bank Limited

Other information

The directors are responsible for the other information. The other information comprises the Directors' report and the Five-Year Summary (but does not include the financial statements and our auditor's report thereon).

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon except as explicitly stated within the *Report on other legal and regulatory requirements*.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors and those charged with governance for the financial statements

The directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Maltese Banking Act (Cap. 371) and the Maltese Companies Act (Cap. 386), and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Independent auditor's report - continued

To the Shareholders of FCM Bank Limited

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Independent auditor's report - *continued*

To the Shareholders of FCM Bank Limited

Report on other legal and regulatory requirements

The *Annual Report and Financial Statements 2023* contains other areas required by legislation or regulation on which we are required to report. The Directors are responsible for these other areas.

The table below sets out these areas presented within the Annual Report, our related responsibilities and reporting, in addition to our responsibilities and reporting reflected in the *Other information* section of our report. Except as outlined in the table, we have not provided an audit opinion or any form of assurance.

Area of the Annual Report and Financial Statements 2023 and the related Directors' responsibilities	**Our responsibilities**	**Our reporting**
Directors' report (on pages 1 to 4) The Maltese Companies Act (Cap. 386) requires the directors to prepare a Directors' report, which includes the contents required by Article 177 of the Act and the Sixth Schedule to the Act.	We are required to consider whether the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements. We are also required to express an opinion as to whether the Directors' report has been prepared in accordance with the applicable legal requirements.	In our opinion: • the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and • the Directors' report has been prepared in accordance with the Maltese Companies Act (Cap. 386).
	In addition, we are required to state whether, in the light of the knowledge and understanding of the Bank and its environment obtained in the course of our audit, we have identified any material misstatements in the Directors' report, and if so to give an indication of the nature of any such misstatements.	We have nothing to report to you in respect of the other responsibilities, as explicitly stated within the *Other information* section.

Independent auditor's report - *continued*

To the Shareholders of FCM Bank Limited

Area of the Annual Report and Financial Statements 2023 and the related Directors' responsibilities	**Our responsibilities**	**Our reporting**
	Other matters prescribed by the Maltese Banking Act (Cap. 371) In terms of the requirements of the Maltese Banking Act (Cap. 371), we are also required to report whether: • we have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our audit; • proper books of account have been kept by the bank, so far as appears from our examination of those books; • the bank's financial statements are in agreement with the books of account; • in our opinion, and to the best of our knowledge and according to the explanations given to us, the financial statements give the information required by any law which may from time to time be in force in the manner so required.	In our opinion: • we have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purpose of our audit; • proper books of account have been kept by the bank, so far as appears from our examination of those books; • the bank's financial statements are in agreement with the books of account; and • to the best of our knowledge and according to the explanations given to us, the financial statements give the information required by any law in force in the manner so required.
	Other matters on which we are required to report by exception We also have responsibilities under the Maltese Companies Act (Cap. 386) to report to you if, in our opinion:adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us.	We have nothing to report to you in respect of these responsibilities.

Independent auditor's report - *continued*

To the Shareholders of FCM Bank Limited

Other matter – use of this report

Our report, including the opinions, has been prepared for and only for the Bank's shareholders as a body in accordance with Article 179 of the Maltese Companies Act (Cap. 386) and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior written consent.

Appointment

We were first appointed as auditors of the Bank on 29 May 2018. Our appointment has been renewed annually by shareholder resolution representing a total period of uninterrupted engagement appointment of 6 years.

Norbert Paul Vella
Principal

For and on behalf of
PricewaterhouseCoopers
78, Mill Street
Zone 5, Central Business District
Qormi
Malta

2 April 2024

Statement of financial position

		As at 31 December	
		2023	**2022**
	Notes	**€**	**€**
ASSETS			
Balances with central banks	4	**50,869,548**	34,777,253
Loans and advances to banks	5	**10,227,227**	2,044,281
Financial investments	6	**94,895,743**	93,009,685
Derivative financial instruments	7	**116,891**	-
Loans and advances to customers	8	**341,683,843**	208,960,941
Prepayments and other assets	9	**11,562,475**	6,555,810
Property and equipment	10	**318,548**	588,626
Intangible assets	11	**96,259**	1,616,125
Deferred tax assets	12	**2,172,539**	3,362,978
Total assets		**511,943,073**	350,915,699
EQUITY			
Share capital	13	**52,250,000**	35,750,000
Perpetual capital notes	14	**17,492,939**	15,500,000
Fair value reserve	15	**(1,184,275)**	(1,137,509)
Retained earnings		**2,863,483**	3,545,705
Total equity		**71,422,147**	53,658,196
LIABILITIES			
Amounts owed to banks and other institutions	17	**25,400,000**	27,428,369
Amounts owed to customers	18	**404,335,641**	264,085,294
Other liabilities	19	**5,931,701**	5,743,840
Subordinated liabilities	20	**4,853,584**	-
Total liabilities		**440,520,926**	297,257,503
Total equity and liabilities		**511,943,073**	350,915,699
MEMORANDUM ITEMS			
Commitments	21	**146,166,162**	110,191,071

The notes on pages 21 to 80 are an integral part of these financial statements.

The financial statements on pages 16 to 80 were authorised for issue by the board on 2 April 2024 and were signed on its behalf by:

John Soler
Director

Michael Borg Costanzi
Director

Income statement

		Year ended 31 December	
		2023	2022
	Notes	€	€
Interest income	22	**23,864,435**	10,820,404
Interest expense	23	**(12,272,624)**	(3,609,214)
Net interest income		**11,591,811**	7,211,190
Fee income	24	**879,988**	490,942
Fee expense	24	**(201,050)**	(78,431)
Net fee income		**678,938**	412,511
Net income from financial instruments held for trading or managed on a fair value basis	25	**74,968**	235,991
Realised gains on disposal of debt instruments measured at FVOCI		**164,681**	69,498
Other income		**33,633**	52,188
Operating income		**12,544,031**	7,981,378
Changes in expected credit losses and other credit impairment charges	26	**(520,632)**	(303,600)
Employee compensation and benefits	27	**(3,809,790)**	(2,338,749)
Administrative expenses	28	**(4,112,624)**	(2,838,348)
Profit before tax		**4,100,985**	2,500,681
Tax expense	29	**(1,726,956)**	(536,986)
Profit for the year		**2,374,029**	1,963,695

The notes on pages 21 to 80 are an integral part of these financial statements.

Statement of comprehensive income

		Year ended 31 December	
		2023	**2022**
	Note	**€**	**€**
Profit for the year		**2,374,029**	1,963,695
Other comprehensive income			
Items that may be subsequently reclassified to profit or loss			
Fair valuation of debt instruments measured at FVOCI:			
- Net changes in fair value arising during the year, before tax	6	**92,733**	(1,737,260)
- Reclassification adjustments: net amounts reclassified to profit or loss, before tax		**(164,681)**	(69,498)
- Income tax relating to components of other comprehensive income		**25,182**	632,963
Other comprehensive income for the year, net of tax		**(46,766)**	(1,173,795)
Total comprehensive income for the year, net of tax		**2,327,263**	789,900

The notes on pages 21 to 80 are an integral part of these financial statements.

Statement of changes in equity

	Notes	Share capital	Perpetual capital notes	Fair value reserve	Retained earnings	Total equity
		€	€	€	€	€
Total equity as at 1 January 2022		28,750,000	15,500,000	36,286	2,153,840	46,440,126
Comprehensive income						
Profit for the year		-	-	-	1,963,695	1,963,695
Other comprehensive income						
Fair valuation of financial investments measured at FVOCI:						
- net changes in fair value arising during the year, net of tax		-	-	(1,128,621)	-	(1,128,621)
- net amounts reclassified to profit or loss upon disposal, net of tax		-	-	(45,174)	-	(45,174)
Total comprehensive income		-	-	(1,173,795)	1,963,695	789,900
Transactions with owners						
Contributions by owners						
Issue of share capital	13	7,000,000	-	-	-	7,000,000
Distributions to owners						
Interest paid on perpetual capital note	14	-	-	-	(571,830)	(571,830)
Total transactions with owners		7,000,000 -		-	(571,830)	6,428,170
Balance at 31 December 2022		35,750,000	15,500,000	(1,137,509)	3,545,705	53,658,196
Total equity as at 1 January 2023		**35,750,000**	**15,500,000**	**(1,137,509)**	**3,545,705**	**53,658,196**
Comprehensive income						
Profit for the year		**-**	**-**	**-**	**2,374,029**	**2,374,029**
Other comprehensive income						
Fair valuation of financial investments measured at FVOCI:						
- net changes in fair value arising during the year, net of tax		**-**	**-**	**60,277**	**-**	**60,277**
- net amounts reclassified profit or loss upon disposal, net of tax		**-**	**-**	**(107,043)**	**-**	**(107,043)**
Total comprehensive income		**-**	**-**	**(46,766)**	**2,374,029**	**2,327,263**
Transactions with owners						
Contributions by owners						
Issue of share capital	13	**16,500,000**	**(2,000,000)**	**-**	**-**	**14,500,000**
Issue of perpetual capital notes	14	**-**	**3,992,939**	**-**	**-**	**3,992,939**
Distributions to owners						
Interest paid on perpetual capital notes	14	**-**	**-**	**-**	**(1,096,251)**	**(1,096,251)**
Dividend paid	14	**-**	**-**	**-**	**(1,960,000)**	**(1,960,000)**
Total transactions with owners		**16,500,000**	**1,992,939**	**-**	**(3,056,251)**	**15,436,688**
Balance at 31 December 2023		**52,250,000**	**17,492,939**	**(1,184,275)**	**2,863,483**	**71,422,147**

The notes on pages 21 to 80 are an integral part of these financial statements.

Statement of cash flows

	Notes	As at 31 December 2023 €	 2022 €
Cash flows from operating activities			
Interest and fee income received		**23,732,656**	10,494,875
Other income		**182,589**	429,379
Interest and fee expense paid		**(10,271,101)**	(3,472,251)
Cash payments to employees and suppliers		**(8,221,873)**	(7,080,830)
Cash flows generated from operating activities before changes in operating assets and liabilities		**5,422,271**	371,173
Changes in operating assets and liabilities			
Net increase in balances with central banks		**(15,322,472)**	(1,093,136)
Net increase in loans and advances to customers		**(132,889,724)**	(71,333,803)
Net (increase)/decrease in other assets		**(1,990,500)**	1,924,911
Net increase in amounts owed to customers		**140,250,347**	122,635,893
Net decrease in amounts owed to banks and other institutions		**(2,028,369)**	(25,205,270)
Net cash (used in)/generated from operating activities		**(6,558,447)**	27,299,768
Cash flows from investing activities			
Purchase of financial investments	6	**(22,987,405)**	(16,852,578)
Proceeds from sale and redemption of financial investments	6	**19,988,443**	7,560,253
Purchase of property and equipment	9	**(130,542)**	(195,534)
Proceeds from disposal of property and equipment	9	**54,820**	-
Purchase of intangible assets	10	**(33,725)**	(463,446)
Net cash used in investing activities		**(3,108,409)**	(9,951,305)
Cash flows from financing activities			
Proceeds from issue of share capital	13	**10,500,000**	7,000,000
Proceeds from issue of perpetual capital notes	14	**3,992,939**	-
Interest paid on perpetual capital notes		**(1,096,251)**	(571,830)
Dividend paid	16	**(1,960,000)**	-
Proceeds from issue of subordinated liabilities		**5,080,383**	-
Other proceeds from parent company	19	**2,100,000**	4,000,000
Net cash generated from financing activities		**18,617,071**	10,428,170
Net movement in cash and cash equivalents		**8,950,215**	27,776,633
Cash and cash equivalents at beginning of year		**34,660,204**	6,883,571
Cash and cash equivalents at end of year	30	**43,610,419**	34,660,204

The notes on pages 21 to 80 are an integral part of these financial statements.

Notes to the financial statements

1. Summary of material accounting policies

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

1.1 Basis of preparation

The Bank's financial statements have been prepared in accordance with the requirements of International Financial Reporting Standards (IFRSs) as adopted by the EU and with the requirements of the Banking Act (Cap. 371) and the Maltese Companies Act (Cap. 386). These financial statements are prepared under the historical cost convention, as modified by the fair valuation of certain financial assets measured at fair value through profit or loss, including derivative financial instruments, and financial assets measured at fair value through other comprehensive income.

The preparation of financial statements in conformity with IFRSs as adopted by the EU requires the use of certain accounting estimates. It also requires the directors to exercise their judgment in the process of applying the Bank's accounting policies (see Note 3 - Critical accounting estimates, and judgments in applying accounting policies).

Appropriateness of going concern assumption

During 2023, financial markets were driven by concerns over high inflation, heightened interest rate risk environment, and recession risks, against the backdrop of the Russia-Ukraine war and geopolitical developments brought about by the conflict in the Middle East. Throughout the year, several major central banks tightened their monetary policies at a faster pace than previously anticipated in order to counter rising inflation. As a result, bond markets sold off sharply and bond yields rose to multi-year highs, which resulted in substantial losses in securities portfolios held by banks. The closure of several reputable banks during the first quarter of 2023 gave rise to apprehensions about the resilience of the banking sector at a global level. The loss of confidence by the public poses the risk of triggering excessive customer deposits withdrawals which can surpass the available liquidity of the banks.

At the date of authorisation for issue of these financial statements, despite the unfavourable macroeconomic environment, the Bank's fundamentals remained strong. Both deposits and lending increased, signalling continued customer confidence. The Bank's Board of directors also takes cognisance of the Bank's ability to continue generating positive operating cash flows in the context of estimated growth in revenues and activity levels.

Accordingly, the Bank's Board of directors has a reasonable expectation that the Bank will continue in operational existence for the foreseeable future and the Board's view is that there appears to be no material uncertainty that may cast significant doubt on the Bank's ability to continue operating as a going concern as at the date of authorisation for issue of these financial statements. In making this assessment, a wide range of information was taken into consideration, including both present and future conditions.

Standards, interpretations and amendments to published standards effective in 2023

In 2023, the Bank adopted new standards, amendments and interpretations to existing standards that are mandatory for the Bank's accounting period beginning on 1 January 2023. The adoption of these revisions to the requirements of IFRSs as adopted by the EU did not result in substantial changes to the Bank's accounting policies.

1. Summary of material accounting policies - continued

1.1 Basis of preparation - continued

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

Certain new amendments to existing standards which are mandatory for accounting periods beginning on or after 1 January 2024 have been published by the date of authorisation for issue of these financial statements. The Bank has not early adopted these amendments and the Bank's directors are of the opinion that, there are no amendments that will have a possible significant impact on the Bank's financial statements in the period of initial application.

1.2 Foreign currency transactions and balances

a) Functional and presentation currency

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

b) Transactions and balances

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

Equity items that have not been recognised in the income statement, such as the Bank's perpetual capital notes, are translated at the historical rate with no impact on the amount of total equity.

1.3 Financial assets

i. Initial recognition and measurement

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

On initial recognition the Bank classifies its financial assets in the following measurement categories: (a) amortised cost; (b) fair value through profit or loss (FVPL); or (c) fair value through other comprehensive income (FVOCI). The classification varies depending on whether the financial asset is a debt, equity or derivative financial instrument, taking into account the business model for managing the financial assets and the contractual terms of the cash flows.

At initial recognition, an expected credit loss (ECL) allowance is recognised for financial assets measured at amortised cost and investments in debt instruments measured at fair value through other comprehensive income (FVOCI), which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

1. **Summary of material accounting policies** - continued

1.3 Financial assets - continued

i. Initial recognition and measurement - continued

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

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

ii. Classification and subsequent measurement

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

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

The classification requirements for debt and equity investments are described below.

Debt instruments

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

Classification and subsequent measurement of debt instruments depend on:

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

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

- Amortised cost: The amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance. Assets that are held for the collection of contractual cash flows where those cash flows represent solely payments of principal and interest (SPPI), and that are not designated at FVPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any ECL allowance recognised and measured as described in Note 2.1.1.1. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

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

1. Summary of material accounting policies - continued

1.3 Financial assets - continued

Debt instruments - continued

- FVPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVPL. The Bank does not classify any of its debt instruments within this category.

The Bank reclassifies debt instruments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change.

Business Model Assessment

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

The information that is considered in such assessment includes:

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

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

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

1. Summary of material accounting policies - continued

1.3 Financial assets - continued

Cash flows that represent solely payments of principal and interest

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

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

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

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

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective i.e. instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Equity securities are classified in the FVPL category. Movements in fair value are recognised in profit or loss within 'Net income from financial instruments held for trading or managed on a fair value basis'.

1. Summary of material accounting policies - continued

1.3 Financial assets - continued

Modification of loans and advances to customers

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

The Bank renegotiates loans and advances to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. 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, revision of interest rate and changing the timing of interest payments. Both retail and corporate loans are subject to the forbearance policy.

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

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

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

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, and the Bank recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss.

The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets).

Impairment of financial assets

The Bank assesses on a forward-looking basis the ECLs associated with loans and advances to banks and customers, its debt instruments carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Bank recognises a loss allowance for such losses at each reporting date.

1. Summary of material accounting policies - continued

1.3 Financial assets - continued

Impairment of financial assets - continued

The measurement of ECLs reflects:

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

Note 2.1.1.1 provides more detail of how the expected credit loss allowance is measured.

ECL allowances are presented in the statement of financial position as follows:

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

Derecognition of financial assets

Financial assets, or a portion thereof, are derecognised when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either (i) the Bank transfers substantially all the risks and rewards of ownership, or (ii) the Bank neither transfers nor retains substantially all the risks and rewards of ownership and the Bank has not retained control.

Write-off

Financial assets (and the related credit loss allowances) are written off, either partially or in full, when there is no realistic prospect of recovery.

1.4 Offsetting financial instruments

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

1. Summary of material accounting policies - continued

1.5 Derivative financial instruments

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

The Bank principally uses currency swaps as a hedge of foreign exchange risk, and interest rate swaps as a hedge of interest rate risk, thereby entering into commitments to exchange one set of cash flows for another. All the Bank's derivative transactions provide effective economic hedges under the Bank's risk management policies. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in profit or loss.

The Bank deploys no hedging strategies that achieve hedge accounting in terms of IFRS 9.

1.6 Property and equipment

All property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

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

Depreciation is calculated using the straight-line method to allocate the cost of the assets to their residual values over their estimated useful lives, as follows:

Motor vehicles, furniture and fittings	5 years
Computer hardware	3-10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 1.9).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised in profit or loss.

1.7 Intangible assets

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use specific software. These costs are amortised over their estimated useful lives of five to ten years. Costs associated with maintaining computer software programme are recognised as an expense as incurred.

At the end of each reporting period, intangible assets are reviewed for indications of impairment or changes in estimated future economic benefits. If such indications exist, the intangible assets are analysed to assess whether their carrying amount is fully recoverable (Note 1.9).

1. Summary of material accounting policies - continued

1.7 Intangible assets - continued

As part of its arrangements, the Bank receives access to the application software managed and hosted by a third part supplier over the contract term in exchange for payment. The Bank does not obtain a right to direct the use of the software as this right remains with the supplier. Accordingly, the Bank does not have rights to the software that would create an asset for the Bank at contract commencement. The access to the software is a service that the Bank receives over the contract term. Fees paid in exchange for these services are recognised as expense as the services are received.

The Bank may enter into contracts with third parties to deliver configuration and customisation costs in the supplier's application software to which the Bank receives access. Costs associated with these are recognised as expense when the Bank receives the configuration or customisation services. In assessing when to recognise the costs as an expense, the Bank determines when the supplier performs the configuration or customisation services in accordance with the contract to deliver those services.

1.8 Leases

The Bank leases property used as office space and car spaces. In accordance with the practical expedients permitted by the standard, the Bank has elected not to separate lease and any associated non-lease components in respect of property leases, and instead accounts for these as a single lease component.

At the inception of a contract, the Bank assesses if the contract is or contains lease components that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

Lease liabilities arising from such contracts are measured at the present value of the remaining lease payments, discounted using the Bank's incremental borrowing rate, which is the rate that the Bank would have to pay to borrow the funds necessary to obtain an asset of a similar value in a similar economic environment with similar terms and conditions. Lease payments to be made under reasonably certain extension options are also included in the measurement of the liability. Lease payments are allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease term so as to produce a constant period rate of interest on the remaining balance of the liability.

The Bank measures the associated right-of-use assets at an amount equal to the lease liability at the date at which the leased asset is made available for use. The right-of-use assets are subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term.

The Bank elects not to recognise a right-of-use asset and a lease liability for short-term leases. Short-term leases are leases with a lease term of 12 months or less from the commencement date. Instead, payments associated with these short-term leases, are recognised as an expense in profit or loss on a straight-line basis over the term of the lease. If a lease for which the short-term lease exemption has been applied is subsequently modified or the lease term is changed, it is accounted for as a new lease.

1. Summary of material accounting policies - continued

1.9 Impairment of non-financial assets

Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units). The impairment test can also be performed on a single asset when the fair value less cost to sell or the value in use can be determined reliably.

1.10 Current and deferred tax

The tax expense for the period comprises current and deferred tax. Tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively. The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period.

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

Deferred tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities.

1.11 Perpetual capital notes

Perpetual capital notes are undated and subordinated obligations. Coupon payments on perpetual capital notes may be cancellable at the Bank's discretion and are accounted for through equity.

1.12 Financial liabilities

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

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

1.13 Contingent liabilities

A contingent liability is (a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the Bank; or (b) a present obligation that arises from past events but is not recognised because: (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability. Contingent liabilities are not recognised but are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

1. Summary of material accounting policies - continued

1.14 Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised within 'Interest income' and 'Interest expense' in profit or loss using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses.

The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

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

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

1.15 Fee income and expense

Fee income and expense that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate and treated as part of interest income and expense.

Other fee income is recognised as the related services are performed. Fee expense relate mainly to transaction and service fees which are expensed as the services are received.

1.16 Net income from financial instruments held for trading or managed on a fair value basis

Net income from financial instruments held for trading or managed on a fair value basis relate to income from foreign exchange transactions and balances, net income from derivatives, such as cross currency swaps, forward exchange contracts and interest rate swaps, as well as all gains and losses from changes in fair value on all financial assets measured at FVPL. These are recognised as income in the period in which they are earned.

1.17 Cash and cash equivalents

Cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition and deposits held at call with banks.

1.18 Dividend distribution

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

2. Financial risk management

2.1 Financial risk factors

Preamble

The Bank's activities expose it to a variety of financial risks and these activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. The Bank's aim is to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Bank's financial performance.

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The risk function of the Bank, which is headed by the Chief Risk Officer, is responsible for the monitoring of risk. The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Bank is exposed to financial risks, categorised as follows:

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

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

- Liquidity risk: Liquidity risk arises from:
  - Market (product) liquidity risk: risk of losses arising from the inability to easily offset or eliminate a position without significantly affecting the market price because of inadequate market depth or market disruption; and
  - Funding liquidity risk: risk of losses arising from a timing mismatch between investing, placements and fund raising activities resulting in obligations missing the settlement date or satisfied at higher than normal rates.

2.1.1 Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations in a timely manner and arises principally from the Bank's loans and advances to banks and customers.

Credit risk management

The measurement of credit exposure for risk management purposes considers that an exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties.

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk - continued

(a) Loans and advances to customers

The Bank's principal credit risk arises on loans and advances to customers. To manage this risk, the Bank compiles and updates due diligence reports through which the Bank primarily evaluates the capacity of customers to repay loans from sources other than collateral. The evaluation includes a review of the client's borrowings and repayments history and a financial analysis to assess profitability, liquidity, and debt capacity using both historical and projected financial information where necessary. The value of the collateral in place is also evaluated.

The Bank's approach when granting credit facilities is based on the customer's capacity to repay rather than placing primary reliance on credit risk mitigants. Notwithstanding, as part of the Bank's credit risk mitigation techniques, the Bank holds collateral against loans and advances to customers, which nature and level generally depends on the amount of the exposure, the type of facility provided, the term of the facility and the level of credit risk involved.

In addition, loan approval limits are in place to effectively manage credit risk. These limits are currently allocated among the Bank's Management Credit Committee, which includes the CEO, CCO, CRO, and Head of Credit and Corporate Banking, and the Board of Directors. The Credit Committee is tasked with approving facilities within defined limits. For credit facilities exceeding these limits, the Credit Committee evaluates them and makes recommendations to the Chairman of the Board and the Chairman of the Audit Committee based on exposure limits as defined within the Bank's Credit Policy. Moreover, approval authority is reserved for the Board, following recommendations from the Audit Committee, regarding the consideration of related party lending.

Exposure to credit risk is managed through regular analysis of the ability of counterparties and potential counterparties to meet interest and capital repayment obligations. Credit review procedures are conducted at a minimum of once a year, with the frequency of reviews typically adjusted based on the performance of the counterparty.

During the financial year ended 31 December 2023, the Bank's business model faced significant pressure due to the interest rate environment, prompting a comprehensive reassessment of credit exposures and the potential adverse impact stemming from increased interest costs.

This uncertainty has contributed to increased credit risk in respect of a proportion of the Bank's customers' business models, income levels or cash flow generation. In this respect, management continues to assess in an enhanced manner, borrower-specific credit risk levels to identify SICR or unlikeliness to pay ('UTP') events. The Bank monitors closely exposures through updating credit risk assessments. Exposures deemed mostly impacted and in respect of which a SICR has been observed triggered more frequent monitoring.

Where appropriate, the Bank also enhanced its credit risk mitigation techniques in order to manage the heightened level of credit risk by requesting additional collateral in respect of specific exposures.

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk - continued

(b) Other financial assets

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

In addition, in respect of unrated debt securities, the Bank compiles and updates due diligence reports through which the Bank primarily evaluates the capacity of the counterparty to repay the debt. The evaluation includes a financial analysis to assess the counterparty's profitability, liquidity, and debt capacity.

2.1.1.1 Expected credit losses

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

- A financial instrument that is not credit-impaired on initial recognition is classified as 'Stage 1' and has its credit risk continuously monitored by the Bank. At initial recognition, an impairment allowance (or provision) is required for ECLs resulting from default events that are possible within the next 12 months ('12-month ECLs').
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. An allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL').
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. An allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL').

A pervasive concept in measuring ECL in accordance with IFRS 9 is that ECL should consider forward looking information as described further below.

Significant increase in credit risk

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

The Bank primarily identifies whether a SICR has occurred based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. These factors vary depending on the nature of the exposure and the type of borrower. Exposures are subject to ongoing monitoring.

Monitoring typically involves use of the following data:

- Information obtained during periodic review of customer files – e.g. audited financial statements, management accounts, budgets and projections. Examples of areas of particular focus are; gross profit margins, financial leverage ratios, debt service coverage, compliance with contractual conditions, quality of management and senior management changes.

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk - continued

2.1.1.1 Expected credit losses - continued

- Data from credit reference agencies, press articles.
- Actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities.
- Utilisation of the granted limit.
- Requests for and granting of modifications to financial assets e.g. forbearance.
- Existing and forecast changes in business, financial and economic conditions.

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

In the case of financial assets other than loans and advances to customers, which primarily include balances with the Central Bank of Malta, loans and advances to banks and externally rated investments in debt securities, the Bank applies the low credit risk simplification to all its exposures considered 'investment-grade', as rated by external rating agencies such as Standard & Poor's and Moody's. This consideration is made in the light of the fact that all obligors within these categories are considered by the Bank to have a strong capacity to meet their obligations, and that adverse changes in economic conditions should not reduce their ability to fulfil obligations.

The Bank assumes that the credit risk on these financial assets has not increased significantly since initial recognition if the financial instrument is determined to have low credit risk within the meaning of paragraph 5.5.10 of IFRS 9, at the reporting date. Moving from 'investment-grade' to 'non-investment grade' does not automatically mean that there has been a SICR. If, on the other hand, these financial assets suffer a significant increase in credit risk, the financial instrument will be re-classified as a Stage 2 exposure. This will impact the measurement of the loss allowance, moving from a 12-month ECL assumption to a lifetime ECL assumption.

In respect of unrated debt securities, to determine whether credit risk has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cause or effect including both quantitative and qualitative information, and by applying experience credit judgement.

Definition of default and credit impaired

The Bank determines that a financial instrument is credit-impaired (or in default and accordingly Stage 3 for IFRS 9 purposes) when:

- Contractual payments of either principal or interest are past due by more than 90 days for any material credit obligation to the Bank.
- The counterparty is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as the realisation of collateral.
- There are indicators that the borrower is unlikely to pay in the absence of a concession granted due to reasons related to the borrower's financial condition.

If unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure exceeds 90 days past due.

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.1 Expected credit losses - continued

Measurement of ECL

The ECL is measured on either a 12-month ('12M') or lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired.

(a) Loans and advances to customers

The ECL from loans and advances to customers is determined by projecting the probability of default ('PD'), loss given default ('LGD') and exposure at default ('EAD') for each individual exposure. These three components are multiplied together to calculate the ECL.

The PD represents the likelihood of a borrower defaulting on its financial obligation (as per "Definition of default and credit-impaired assets" above), either over the next 12 months, or over the remaining lifetime of the obligation. The 12-month PD is developed by utlising publicly available peer data for portfolios similar to those of the Bank as a starting point, and is scaled to a Lifetime PD by considering probability weighted forward looking macroeconomic information as explained in further detail below.

LGD represents the Bank's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. It is expressed as a percentage loss per unit of exposure at the time of default. The LGD is determined based on factors which impact the recoveries made post default. This is primarily based on projected collateral values, discounts to values, time to repossession and recovery costs observed. The Bank also considers forward looking macroeconomic information to estimate the extent of loss on a defaulted exposure under different forward looking scenarios.

The EAD is based on the amounts the Bank expects to be owed at the time of default.

The 12-month ECL is calculated by multiplying the 12-month PD, LGD and EAD. Lifetime ECL is calculated on a similar basis for the residual life of the exposure. The ECL is then discounted back to the reporting date. The discount rate used in the ECL calculation is the original effective interest rate or an approximation thereof.

The Bank reflects forward-looking macroeconomic information into the calculation of ECL by incorporating the effects of two scenarios, representative of forecast economic conditions, sufficient to calculate unbiased expected losses. They represent a most likely outcome (the 'Baseline' scenario), and a less likely scenario, referred to as the 'Downside' scenario, weighted by an appropriate probability of occurrence, determined on the basis of scenarios and respective probability weights judgmentally set by management. In this respect, the Bank assigns a probability of occurrence of 70% (2022: 70%) to the 'Baseline' scenario and a probability of occurrence of 30% (2022: 30%) to the 'Downside' scenario.

More specifically, the Bank applies forward-looking economic scenarios into the calculation of ECL by incorporating the effect of macroeconomic variables into the estimation of the term structure of the PD. In order to model the impact of the macroeconomic scenarios on the 12M PD and Lifetime PD, the Bank determines a proxy default rate that best represents the credit performance of the Bank's portfolio. Consequently, the Bank determines, through a historical analysis, which macroeconomic variables correlate best to the proxy default rate. The macro-economic variable with the strongest correlation with the proxy default rate is Malta GDP growth . The Bank applies forward-looking macroeconomic information to forecast the change in the proxy default rate to construct PD curves under different macroeconomic scenarios

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.1 Expected credit losses - continued

(a) Loans and advances to customers - continued

With respect to the LGD, the Bank considered the impact of worsening property values under the 'Downside' scenarios.

The Bank considers a 'Baseline' scenario which assumes strong private consumption growth and a gradual recovery in private investment, alongside positive contributions from net exports. The projections for Malta GDP growth under the 'Baseline' scenario is obtained from data published by the Central Bank of Malta. For the 'Downside' scenario, the Bank assumes that both the Maltese and Czech economies are significantly impacted by a market deterioration. The Bank utilises statistical methods to infer the downside scenario based on a time series analysis of Malta GDP growth.

The macroeconomic scenarios and likelihoods of occurrence are subject to a high degree of uncertainty and therefore, the actual outcomes may be significantly different to those projected. As a result, management assessed and considered the sensitivity of the ECL outcome against the forward-looking economic conditions as part of the ECL governance process.

In this respect, as at 31 December 2023, the sensitivity of the ECL outcome to the economic forecasts was assessed by recalculating the ECL under the Downside scenario described above for the loan portfolio, applying a 100% weighting. If the ECL outcome was estimated solely on the basis of the Downside scenario, the credit loss allowances in respect of the loan portfolio would increase by €474,267 (2022: €290,304).

(b) Balances with central banks, loans and advances to banks and financial investments

In the absence of sufficient internal historical default data, in order to estimate its PDs, the Bank makes reference to external information published by Moody's. More specifically, in the case of rated counterparties or issuers, the Bank assigns a PD to each of its exposures on the basis of the external credit rating of the counterparty or issuer, by reference to Moody's default rates.

If a counterparty or exposure migrates between external credit ratings, then this will lead to a change in the associated PD. In the case of unrated loans and advances to banks and unrated debt securities, the Bank calibrates unrated counterparties to Moody's default rates by reference to external ratings of comparable financial assets. The Bank assigns a 1-year default rate to all exposures deemed to have low credit risk, and for very short-term financial assets, the 1-year default rate is scaled down to estimate a PD over a one or two day horizon, dependable on the said exposure. This is consistent within the meaning of paragraph 5.5.10 of IFRS 9, at the reporting date.

EAD is based on the amounts the Bank expects to be owed at the time of default, over the next 12 months ('12 EAD') or over the remaining lifetime ('Lifetime EAD').

LGD represents the Bank's expectation of the extent of loss on a defaulted exposure. In estimating LGD, the Bank assumes a LGD of 75% in the case of unsecured subordinated exposures and a LGD of 45% in the case of senior unsecured exposures, including sovereigns, financial institutions and corporates.

The ECL is calculated as a factor of the 12-month PD, LGD and EAD.

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.2 Maximum exposure to credit risk

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

	2023		2022	
	Gross carrying amount/ Fair value	**ECL Allowance**	Gross carrying amount/ Fair value	ECL Allowance
	€	**€**	€	€
Credit risk exposure relating to on-balance sheet assets				
Subject to IFRS 9 impairment allowance				
Financial assets measured at FVOCI				
Debt securities	**21,431,638**	**(9,854)**	10,377,155	(11,146)
Financial assets measured at amortised cost:				
Balances with the Central Banks	**50,869,548**	**-**	34,779,807	(2,554)
Loans and advances to banks	**10,227,227**	**-**	2,044,281	-
Loans and advances to customers	**342,326,746**	**(642,903)**	209,437,022	(476,081)
Debt securities	**72,701,796**	**(413,572)**	82,857,073	(224,543)
Accrued interest receivable	**1,254,644**	**-**	652,629	-
Not subject to IFRS 9 impairment allowance				
Financial assets measured at FVPL				
Derivative financial instruments	**116,891**	**-**	-	-
Credit risk exposure	**498,928,490**	**(1,066,329)**	340,147,967	(714,324)
Credit risk exposure relating to off-balance sheet instruments				
Undrawn commitments to lend	**146,166,162**	**-**	110,191,071	-

Financial assets in the form derivative financial instruments are subject to credit risk, but not subject to impairment rules in accordance with IFRS 9. These instruments are held at fair value through profit or loss and therefore any movements in the fair value of these assets are immediately recorded in profit or loss.

Accrued income substantially arises from loans and advances to customers. Expected credit losses in respect of accrued income, which are not deemed material, have been allocated to loans and advances to customers. Similarly, ECL arising on undrawn commitments to lend have been allocated to loans and advances to customers.

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.3 Credit concentration risk

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

Credit concentration risk by industry sector

The following table analysis the Bank's financial investments, at their gross carrying amount or fair value, by industry sector:

	2023 **€**	2022 €
Governments	**13,238,676**	4,905,813
Corporate		
Financial services	**11,140,082**	11,456,347
Gaming	**-**	4,228,607
Industrial	**6,369,444**	6,024,577
Transportation and automobile	**14,754,000**	15,695,868
Construction and real estate	**10,682,396**	10,789,992
Engineering	**11,434,483**	11,551,941
Retail trade	**4,344,401**	4,450,955
Manufacturing	**8,658,459**	10,412,852
Telecommunications	**6,215,092**	6,241,811
Other sectors	**7,296,401**	7,475,465
	94,133,434	93,234,228

The industry sector analysis of the Bank's loans and advances to customers, at their gross carrying amount, is described in the following table:

	2023 **€**	2022 €
Financial services	**18,875,145**	21,394,105
Households and individuals	**28,383,779**	24,201,683
Construction and real estate	**216,455,642**	114,415,324
Wholesale and retail	**8,192,507**	3,644,383
Hotels and accommodation	**18,950,916**	16,486,226
Other sectors	**51,468,757**	29,295,301
	342,326,746	209,437,022

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.3 Credit concentration risk - continued

Credit concentration risk by industry sector - continued

The Bank's undrawn commitments to lend in respect of loans and advances to customers are analysed in the table below by industry.

	2023 €	2022 €
Households and individuals	**7,802,324**	2,322,763
Construction and real estate	**113,767,592**	93,618,630
Wholesale and retail	**3,823,000**	3,700,000
Hotels and accommodation	**2,809,142**	1,174,642
Other sectors	**17,964,104**	9,375,036
	146,166,162	110,191,071

Credit concentration risk by name

A significant concentration of credit risk arises due to the limited number of customers to which the Bank has extended lending. As at 31 December 2023, 12 (2022: 9) customers, with a total value of €102,907,328 (2022: €57,839,947) were deemed to be large exposures as defined in the Capital Requirements Regulations (CRR). The allowance for ECL in respect of such large exposures amounted to €95,605 (2022: €64,872).

Credit concentration risk by geographical region

The tables below describe the Bank's exposure to credit concentration by geographical region, gross of ECL, or fair value.

As illustrated in the table, the majority of the Bank's exposures are in Malta in view of the Bank's operations being conducted in Malta, followed by the Czech Republic attributable to the fact that the Bank forms part of a group that operates in the Czech Republic.

	2023 €	2022 €
Financial investments		
Malta	**1,517,792**	1,402,135
Germany	**13,365,063**	15,068,316
Czech Republic	**31,537,087**	36,929,200
Netherlands	**8,840,927**	9,574,611
France	**10,274,616**	10,277,082
Austria	**7,397,657**	4,268,368
Romania	**7,196,708**	7,282,080
Poland	**2,962,976**	2,598,080
United States	**5,258,202**	-
Other	**5,782,406**	5,834,356
	94,133,434	93,234,228

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.3 Credit concentration risk - continued

Credit concentration risk by geographical region - continued

	2023 **€**	2022 €
Loans and advances to banks		
Malta	**1,629,609**	113,017
Netherlands	**2,572,781**	1,249,843
Czech Republic	**4,773,079**	246,937
Other	**1,251,758**	434,484
	10,227,227	2,044,281

	2023 **€**	2022 €
Loans and advances to customers		
Malta	**266,142,323**	177,965,419
Czech Republic	**76,184,423**	31,471,603
	342,326,746	209,437,022

	2023 **€**	2022 €
Undrawn commitments to lend		
Malta	**127,744,759**	101,516,114
Czech Republic	**18,421,403**	8,674,957
	146,166,162	110,191,071

	2023 **€**	2022 €
Derivative financial instruments		
Netherlands	**116,891**	-

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.4 Information on credit quality of balances with banks and debt securities

The Bank uses external ratings to highlight exposures which require closer management attention.

The following table presents an analysis of the Bank's financial investments, which comprise of debt securities, by rating agency based on Moody's ratings.

	2023		2022	
	FVOCI	**Amortised cost**	FVOCI	Amortised cost
	€	**€**	€	€
AAA	**5,258,202**	**-**	-	-
AA1	**3,074,701**	**-**	-	-
AA3	**273,445**	**-**	261,925	-
A2	**1,494,660**	**-**	433,800	-
A3	**1,769,854**	**-**	-	-
Baa2	**3,660,357**	**3,033,580**	5,034,455	10,822,892
Baa3	**3,744,976**	**20,624,776**	-	4,210,088
Ba1	**-**	**13,196,054**	947,400	16,280,527
Ba2	**-**	**1,505,885**	1,472,580	19,378,909
Ba3	**-**	**3,235,226**	-	-
Caa3	**-**	**1,930,580**	-	-
B1	**-**	**-**	-	1,928,885
Unrated	**2,155,443**	**29,175,695**	2,226,995	30,235,772
	21,431,638	**72,701,796**	10,377,155	82,857,073

As at 31 December 2023 and 2022, the Republic of Malta and accordingly the Central Bank of Malta had a credit rating of A-, A2 and A+ from the three international credit rating agencies S&P, Moody's and Fitch respectively.

Meanwhile, as at 31 December 2023 credit ratings in respect of placements with counterparty banks range between A2 and Baa3 (2022: A1 and Baa2).

As at 31 December 2023 and 2022, all balances with banks were classified as Stage 1.

In respect of unrated debt securities, the Bank compiles and updates due diligence reports through which the Bank primarily evaluates the capacity of the counterparty to repay the debt. The evaluation includes a financial analysis to assess the counterparty's profitability, liquidity, and debt capacity. To determine whether credit risk has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cause or effect including both quantitative and qualitative information, and by applying experience credit judgement. The Bank calibrates unrated counterparties to Moody's default rates by reference to external ratings of comparable financial assets.

The following tables set out information on the credit quality of financial investments measured at amortised cost and financial investments measured at FVOCI. The credit quality of the financial assets is determined by credit ratings applicable to issuers or counterparties. In respect of debt securities which are not externally rated, the Bank calibrates unrated counterparties to Moody's default rates by reference to external ratings of comparable financial assets. Explanation of the terms 12-month ECL, lifetime ECL and credit impaired are included in Note 2.1.1.1.

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.4 Information on credit quality of balances with banks and debt securities - continued

		2023	
	Stage 1 12-month €	**Stage 2 Lifetime ECL €**	**Total €**
Financial investments measured at FVOCI			
Gross carrying amount – fair value	**21,431,638**	**-**	**21,431,638**
Financial investments measured at amortised cost:			
Gross carrying amount	**70,771,216**	**1,930,580**	**72,701,796**
Loss allowance	**(64,330)**	**(349,242)**	**(413,572)**
	70,706,886	**1,581,338**	**72,288,224**

		2022	
	Stage 1 12-month ECL €	Stage 2 Lifetime ECL €	Total €
Financial investments measured at FVOCI			
Gross carrying amount – fair value	10,377,155	-	10,377,155
Financial investments measured at amortised cost:			
Gross carrying amount	80,928,188	1,928,885	82,857,073
Loss allowance	(89,135)	(135,408)	(224,543)
	80,839,053	1,793,477	82,632,530

As at 31 December 2023, the expected credit loss allowances in respect of financial investments measured at FVOCI classified as Stage 1 amounted to €9,854 (2022: €11,146).

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.5 Information on credit quality of loans and advances to customers

The following table presents the distribution, by stage, of the gross carrying amount of loans and advances to customers to which the impairment requirements in IFRS 9 are applied, and the associated ECL as at 31 December 2023 and as at 31 December 2023.

		2023		
	Stage 1	**Stage 2**	**Stage 3**	
	12-month ECL	**Lifetime ECL**	**Lifetime ECL**	**Total**
	€	**€**	**€**	**€**
Gross carrying amount	**329,333,238**	**9,863,816**	**3,129,692**	**342,326,746**
Loss allowance	**(428,345)**	**(60,789)**	**(153,769)**	**(642,903)**
	328,904,893	**9,803,027**	**2,975,923**	**341,683,843**

		2022		
	Stage 1	Stage 2	Stage 3	
	12-month ECL	Lifetime ECL	Lifetime ECL	Total
	€	€	€	€
Gross carrying amount	206,815,194	1,829,971	791,857	209,437,022
Loss allowance	(311,769)	(34,798)	(129,514)	(476,081)
	206,503,425	1,795,173	662,343	208,960,941

The Bank assesses and individually rates those borrowers that request moratoria or emergency funding to support their short-term liquidity constraints. These exposures are assessed periodically for SICR and UTP events through individual credit risk assessments, on the basis of recently obtained management information, including forecasts. Exposures in respect of which SICR has been observed are attributed higher ECL, requiring closer and more frequent monitoring on a monthly or quarterly basis (depending on the extent of credit risk deterioration) to facilitate timely identification of further deterioration in financial condition.

2.1.1.6 Modification of financial assets

The contractual terms of a loan may be revised for a number of reasons, including changes in market conditions, customer retention and other factors that are not related to the credit quality of a customer. Forbearance measures comprise concessions made on the contractual terms of a loan in response to a customer's financial difficulties.

The following table shows the gross carrying amounts of loans subject to forbearance measures by stage.

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.6 Modification of financial assets - continued

		2023		
	Stage 1	**Stage 2**	**Stage 3**	**Total**
	€	**€**	**€**	**€**
Gross carrying amount	**-**	**1,286,740**	**2,183,259**	**3,469,999**
Loss allowance	**-**	**-**	**(147,894)**	**(147,894)**

		2022		
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Gross carrying amount	1,598,872	1,747,200	791,857	4,137,929
Loss allowance	-	(33,608)	(129,514)	(163,122)

	2023	2022
	€	€
Total renegotiated loans and advances to customers as a percentage of total gross loans and advances to customers	**1.0%**	2.0%
Interest income recognised in respect of forborne/renegotiated assets	**270,315**	178,916
Movement in forbearance activity during the year:		
At 1 January	**4,137,929**	2,625,496
Loans renegotiated without derecognition	**1,286,740**	989,042
Additional drawings in relation to currently forborne loans	**33,998**	571,136
Repayments	**(1,988,668)**	(47,745)
At 31 December	**3,469,999**	4,137,929

Applications for new general payment moratoria or for extensions of general payment moratoria received after 31 March 2021, or extending beyond the maximum duration prescribed by Directive No. 18, are considered to be forbearance measures and are classified as renegotiated loans and included in the table above.

In this respect, outstanding gross loans and advances classified as renegotiated loans as a result of extensions of general payment moratoria beyond the terms prescribed by Directive No. 18 amounted to €3,469,999 as at 31 December 2023 (2022: €4,137,929). The allowance for ECL in respect of such exposures amounted to €147,894 (2022: €163,122), the large majority of which is attributable to Stage 2.

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk - continued

2.1.1.6 Modification of financial assets - continued

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

The following table shows the gross carrying amounts of loans subject to the Malta Development Bank COVID-19 Guarantee Scheme by stage.

		2023		
	Stage 1	**Stage 2**	**Stage 3**	**Total**
	€	**€**	**€**	**€**
Gross carrying amount	**10,563,044**	**44,410**	**317,860**	**10,925,314**
Loss allowance	**(24,195)**	**(158)**	**-**	**(24,353)**

		2022		
	Stage 1	Stage 2	Stage 3	Total
	€	€	€	€
Gross carrying amount	15,784,922	-	-	15,784,922
Loss allowance	(49,502)	-	-	(49,502)

Out of the total gross carrying amounts above, a maximum amount of €9,770,000 (2022: €10,370,000) is considered guaranteed by the Government of Malta.

2.1.1.7 Loss allowances

Reconciliation of the gross carrying amount analysed by 12-month and lifetime ECL provisions

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

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) in credit risk or becoming credit impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period;
- Impact on the measurement of ECL due to changes in PD, LGD or EAD in the period, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions; and
- Foreign exchange retranslations for assets denominated in foreign currencies and other movements.

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.7 Loss allowances - continued

The following table explains the changes in the gross carrying amount and loss allowances in respect of loans and advances to customers between the beginning and the end of the annual period. The increase in ECL during the year is primarily attributable to remeasurement of ECL arising from stage transfers and changes in risk parameters.

	2023							
	Stage 1		Stage 2		Stage 3		Total	
	Gross carrying amount €	Expected credit losses €	Gross carrying amount €	Expected credit losses €	Gross carrying amount €	Expecte credit losses €	Gross carrying amount €	Expected credit losses €
Loans and advances to customers at amortised cost								
At 1 January 2023	206,815,194	(311,769)	1,829,971	(34,798)	791,857	(129,514)	209,437,022	(476,081)
New and further lending	188,449,096	(270,940)	877,725	(3,929)	90,243	(945)	189,417,064	(275,814)
Repayments	(54,065,496)	100,305	(2,153,571)	2,199	(308,273)	126,145	(56,527,339)	228,649
Transfers of financial instruments								
Stage 1 to Stage 2	(10,942,477)	13,953	10,942,477	(13,953)	-	-	-	-
Stage 1 to Stage 3	(923,079)	3,449	-	-	923,079	(3,449)	-	-
Stage 2 to Stage 3	-	-	(1,632,786)	33,318	1,632,786	(33,318)	-	-
Net remeasurement of ECL arising from stage transfers and changes in risk parameters	-	36,657	-	(43,626)	-	(112,688)	-	(119,657)
At 31 December 2023	329,333,238	(428,345)	9,863,816	(60,789)	3,129,692	(153,769)	342,326,746	(642,903)
Total net income statement charge for the year								(166,822)

2. **Financial risk management** - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.7 Loss allowances – continued

	2022							
	Stage 1		**Stage 2**		**Stage 3**		**Total**	
	Gross carrying amount €	**Expected credit losses €**	**Gross carrying amount €**	**Expected credit losses €**	**Gross carrying amount €**	**Expecte credit losses €**	**Gross carrying amount €**	**Expected credit losses €**
Loans and advances to customers at amortised cost								
At 1 January 2022	134,511,323	(256,640)	3,591,895	(93,067)	-	-	138,103,218	(349,707)
New and further lending	120,560,778	(153,065)	1,558,353	(33,389)	-	-	122,119,131	(186,453)
Repayments	(48,168,724)	134,716	(2,616,603)	41,452	-	-	(50,785,327)	176,168
Transfers of financial instruments								
Stage 1 to Stage 2	(88,183)	221	88,183	(221)	-	-	-	-
Stage 2 to Stage 3	-	-	(791,857)	51,615	791,857	(51,615)	-	-
Net remeasurement of ECL arising from stage transfers and changes in risk parameters	-	(37,001)	-	(1,188)	-	(77,899)	-	(116,088)
At 31 December 2022	**206,815,194**	**(311,769)**	**1,829,971**	**(34,798)**	**791,857**	**(129,514)**	**209,437,022**	**(476,081)**
Total net income statement charge for the year								**(126,374)**

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.8 Collateral

The amount and type of collateral required depends on the amount of the exposure, the type of facility provided, the term of the facility and the level of credit risk involved. The main types of collateral obtained include charges over real estate properties, mortgages over residential properties and cash.

Management assesses the market value of collateral as part of the loan origination process. This assessment is reviewed periodically through ongoing credit file reviews, and in the case of real estate financing, upon the completion of agreed upon stages. The Bank requests additional collateral in accordance with the underlying agreement when necessary.

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

Loans granted as part of the Malta Development Bank COVID-19 Guarantee Scheme (Note 2.1.1.6) are secured by a Government guarantee which guarantees up to 90% of each individual exposure, subject to a 50% portfolio capping. These guarantees are included within 'Other collateral' in the tables below.

The 'extendible value' of the collateral is the lower of the fair value of a pledged asset for lending purposes and the gross carrying amount of the secured loans. Since, in the table below, collateral is capped at the gross carrying amount, the 'residual exposure' represents the unsecured portion of the Bank's loans and advances to customers.

The following is an analysis of the extendible value of the collateral and other credit enhancements held by the Bank against exposures of loans and advances to customers.

	2023	2022
	€	€
Performing – Stage 1		
Total maximum exposure relating to on-balance sheet assets	**329,333,238**	206,815,194
Extendible value of collateral		
Secured by cash	**445,000**	565,000
Residential and commercial property	**306,747,318**	180,575,943
Other collateral	**10,921,251**	13,491,934
Total extendible value of collateral	**318,113,569**	194,632,877
Residual exposure	**11,219,669**	12,182,316
Loss allowance	**(428,345)**	(311,769)

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.8 Collateral - continued

	2023	2022
	€	€
Underperforming – Stage 2		
Total maximum exposure relating to on-balance sheet assets	**9,863,816**	1,829,971
Extendible value of collateral		
Residential and commercial property	**9,819,406**	1,829,971
Commercial immovable property	**39,969**	-
Total extendible value of collateral	**9,859,375**	1,829,971
Residual exposure	**4,441**	-
Loss allowance	**(60,789)**	(34,798)
Nonperforming – Stage 3		
Total maximum exposure relating to on-balance sheet assets	**3,129,692**	791,857
Extendible value of collateral		
Secured by cash	**46,500**	43,380
Residential and commercial property	**2,811,832**	730,000
Other collateral	**271,360**	
Total extendible value of collateral	**3,129,692**	773,380
Residual exposure	**-**	18,477
Loss allowance	**(153,769)**	(129,514)

As at 31 December 2023, loans with a value of €317,294,679 (2022: €181,229,030) were fully collateralised and loans with value of €2,702,538 (2022: €2,123,253) were fully uncollateralised.

2.1.1.9 Offsetting financial assets and financial liabilities

The Bank is eligible to present certain financial assets and financial liabilities on a net basis in the statement of financial position in accordance with the Bank's policy described in Note 1.4 'Offsetting financial instruments'.

As at 31 December 2023, investment securities with a carrying value of €26,718,442 (2022:€41,429,299) were pledged in favour of amounts owed to financial institutions of €17,000,000 (2022: €27,428,369). These assets and liabilities were not offset in the statement of financial position.

During 2023, the Bank also entered in a pledge receivables agreement with a related party whereby the Bank pledged loans and advances to customers with a carrying amount of €10,921,180 (2022: nil) in favour of amounts owed to banks amounting to €8,400,000 (2022: nil). These assets and liabilities were not offset in the statement of financial position as the Bank does not have any currently legally enforceable right to settle on a net basis or to realise the asset and settle the liability simultaneously.

The Bank has an International Swaps and Derivatives Association ('ISDA') Master Agreement in place for transactions with a counterparty bank. It provides the contractual framework within which dealing activity across a full range of Over-the-Counter products is conducted, and contractually binds both parties to apply close-out netting across all outstanding transactions per currency.

2. Financial risk management - continued

2.1 Financial risk factors - continued

2.1.1 Credit risk – continued

2.1.1.9 Offsetting financial assets and financial liabilities – continued

Derivative financial assets and derivative financial liabilities are offset as a netting agreement is in place with the counterparty in order to set-off the liabilities against the assets received. There is a legal right to settle, or otherwise eliminate, the amount due by applying the amount receivable from the same counterparty against it. As at 31 December 2023, the Bank's derivative assets subject to master-netting agreements have a fair value of €116,891 (2022: nil). There are no derivative liabilities that can be offset against derivative assets.

The Bank also pledged collateral in the form of cash for transactions under the ISDA Master Agreement amounting to €1,120,000 (Note 9). Pledges are generally conducted under terms that are usual and customary for standard contracts and transactions of this nature. The rights of set off relating to such collateral are enforceable only on the occurrence of future credit events.

As at 31 December 2023, the Bank also placed a deposit with the Czech National Bank amounting to €12,133,959 for which treasury bills issued by the Government of the Czech Republic with the same value have been pledged in the Bank's favour. The pledged instrument is not recognised in the Bank's statement of financial position since the Czech National Bank has retained substantially all the risks and rewards of ownership of these instruments.

As at 31 December 2023, the Bank has also made advances to a related party amounting to €4,869,107 which are expected to be setoff at the end of foreseeable years against the fulfilment of services from the same related party.

2.1.2 Market risk

The Bank is primarily exposed to foreign exchange risk and interest rate risk.

Foreign exchange risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. Foreign exchange risk is the risk to earnings and value caused by a change in foreign exchange rates. Foreign exchange risk arises when financial assets or liabilities are denominated in currencies that are different from the Bank's functional currency.

The Bank manages its currency risk on an ongoing basis by ensuring that foreign currency liabilities are utilised to fund assets denominated in the same foreign currency thereby matching asset and liability positions as much as is practicable. When it is not possible to match the asset and liability currency positions, the Bank hedges its open foreign exchange exposures by entering into forward foreign exchange contracts or currency swaps.

2. **Financial risk management** - continued

2.1 Financial risk factors – continued

2.1.2 Market risk - continued

Foreign exchange risk - continued

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

	EUR	**CZK**	**Other**	
	currency	**currency**	**currencies**	**Total**
	€	**€**	**€**	**€**
As at 31 December 2023				
Financial assets				
Balances with central banks	37,677,815	13,191,733	-	50,869,548
Loans and advances to banks	3,503,635	6,511,313	212,279	10,227,227
Loans and advances to customers	333,831,223	8,495,523	-	342,326,746
Financial investments	64,371,112	24,230,675	6,707,528	95,309,315
Accrued interest receivable	640,621	395,934	218,089	1,254,644
	440,024,406	**52,825,178**	**7,137,896**	**499,987,480**
Financial liabilities				
Amounts owed to customers	367,090,661	37,209,018	35,962	404,335,641
Amounts owed to banks and other institutions	25,400,000	-	-	25,400,000
Accrued interest payable	2,895,221	-	600	2,895,821
Other accrued expenses	156,467	52,029	-	208,496
Subordinated liabilities	-	4,853,584	-	4,853,584
	395,542,349	**42,114,631**	**36,562**	**437,693,542**
Net on-balance sheet financial position		10,710,547	7,101,334	
Notional of derivative financial instruments		1,201,007	(6,172,654)	
Residual exposure		**11,911,554**	**928,680**	

	EUR	**CZK**	**Other**	
	currency	**currency**	**currencies**	**Total**
	€	**€**	**€**	**€**
As at 31 December 2022				
Financial assets				
Balances with central banks	34,779,807	-	-	34,779,807
Loans and advances to banks	1,225,179	564,330	254,772	2,044,281
Loans and advances to customers	209,405,044	31,978	-	209,437,022
Financial investments	64,497,547	28,422,407	314,274	93,234,228
Accrued interest receivable	392,793	257,452	2,384	652,629
	310,300,370	**29,276,167**	**571,430**	**340,147,967**
Financial liabilities				
Amounts owed to customers	259,828,761	4,073,790	182,743	264,085,294
Amounts owed to banks and other institutions	10,000,000	17,428,369	-	27,428,369
Accrued interest payable	552,045	127,761	13,443	693,249
	270,380,806	**21,629,920**	**196,186**	**292,206,912**
Net on-balance sheet financial position		**7,646,247**	**375,244**	

2. **Financial risk management** - continued

2.1 Financial risk factors – continued

2.1.2 Market risk - continued

Foreign exchange risk - continued

Accordingly, as at 31 December 2023, under the scenario that the euro appreciates by 20% against all currencies, the effect would be a loss of €3,562,376 (2022: €1,602,857) in the carrying amount of the financial instruments. Should the euro depreciate against all currencies by 20%, the effect would be a gain of €3,562,376 (2022: €1,602,857) in the carrying amount of the financial instruments. The impact would be recognised in profit or loss.

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the value of a financial instrument will fluctuate because of changes in market interest rates.

Interest rate risk is principally managed through monitoring, on a continuous basis, the level of mismatch of interest rate repricing, taking cognisance of the terms of the Bank's principal assets, loans and advances to customers, of which the majority are repriceable at the Bank's discretion and by hedging any undesired unmatched interest rate risk arising in the balance sheet by entering into interest rate swap with a related party bank. The Bank also invests in highly liquid quality assets, namely listed government and corporate debt securities, for the purpose of mitigating exposures to fluctuations in interest rates.

The following tables summarise the Bank's exposures to interest rate risk. These analyse the Bank's interest-bearing financial instruments at their gross carrying amounts or fair value, categorised by the earlier of contractual repricing or maturity dates.

	Less than three months	**Within one year but over three months**	**Within five years but over one year**	**More than five years**	**Gross carrying amount/ Fair value**
	€	**€**	**€**	**€**	**€**
As at 31 December 2023					
Financial assets					
Balances with central banks	50,869,548	-	-	-	50,869,548
Loans and advances to banks	10,227,227	-	-	-	10,227,227
Loans and advances to customers	285,102,788	9,955,567	39,683,710	7,584,681	342,326,746
Financial investments	30,762,725	-	46,121,660	17,249,049	94,133,434
	376,962,288	**9,955,567**	**85,805,370**	**24,833,730**	**497,556,955**
Financial liabilities					
Amounts owed to customers	347,564,926	55,456,870	1,313,845	-	404,335,641
Amounts owed to banks and other institutions	25,400,000	-	-	-	25,400,000
Subordinated liabilities	4,853,584	-	-	-	4,853,584
	377,818,510	**55,456,870**	**1,313,845**	**-**	**434,589,225**
Interest repricing gap	**(856,222)**	**(45,501,303)**	**84,491,525**	**24,833,730**	

2. Financial risk management - continued

2.1 Financial risk factors – continued

2.1.2 Market risk - continued

Interest rate risk - continued

	Less than three months	Within one year but over three months	Within five years but over one year	More than five years	Gross carrying amount/ Fair value
	€	€	€	€	€
As at 31 December 2022					
Financial assets					
Balances with central banks	34,779,807	-	-	-	34,779,807
Loans and advances to banks	2,044,281	-	-	-	2,044,281
Loans and advances to customers	177,933,442	10,010,241	20,612,103	881,236	209,437,022
Financial investments	26,654,320	-	28,856,150	37,723,758	93,234,228
	241,411,850	**10,010,241**	**49,468,253**	**38,604,994**	**339,495,338**
Financial liabilities					
Amounts owed to customers	137,853,324	120,983,271	5,248,699	-	264,085,294
Amounts owed to banks and other institutions	27,428,369	-	-	-	27,428,369
	165,281,693	120,983,271	5,248,699	-	291,513,663
Interest repricing gap	76,130,157	(110,973,030)	44,219,554	38,604,994	

The table below analyses interest-bearing assets and liabilities at their gross carrying amounts or fair value, into those that have a fixed rate and a variable rate.

	2023		2022	
	Variable	**Fixed**	Variable	Fixed
	€	**€**	€	€
Financial assets				
Balances with central banks	**38,735,589**	**12,133,959**	34,779,807	-
Loans and advances to banks	**10,227,227**	**-**	2,044,281	-
Loans and advances to customers	**285,102,787**	**57,223,959**	177,933,441	31,503,581
Financial investments	**29,466,823**	**64,666,611**	27,473,413	65,760,815
	363,532,426	**134,024,529**	242,230,942	97,264,395
Financial liabilities				
Amounts owed to customers	**96,027,905**	**308,307,736**	64,257,580	199,827,714
Amounts owed to banks and other institutions	**17,000,000**	**8,400,000**	10,000,000	17,428,369
Subordinated liabilities	**4,853,584**	**-**	-	-
	117,881,489	**316,707,736**	74,257,580	217,256,083
Exposure	**245,650,937**	**(182,683,207)**	167,973,362	(119,991,688)

2. **Financial risk management** - continued

2.1 Financial risk factors – continued

2.1.2 Market risk - continued

Fair value sensitivity for fixed rate instruments

Financial instruments issued at fixed rates potentially expose the Bank to fair value interest rate risk. Loans and advances to banks and customers and amounts owed to institutions and customers are measured at amortised cost and are therefore not subject to fair value interest rate risk.

As at 31 December 2023 and 2022, the Bank's instruments that are fair valued and which are subject to fair value interest rate risk comprise the Bank's investments in debt securities measured at FVOCI. The Bank has investments in debt securities measured at FVOCI that are subject to fixed interest rates. The estimated impact of an immediate 100 basis point increase in yields as at 31 December 2023 amounts to a loss of €929,824 (2022: loss of €302,598).

Cash flow sensitivity for variable rate instruments

The Bank is also exposed to cash flow interest rate risk principally in respect of financial assets and liabilities which are subject to floating interest rates.

At the end of the reporting period, if interest rates had increased by 1% (assuming a parallel shift of 100 basis points in yields) with all other variables held constant, in particular foreign currency rates, the post-tax result for the year would increase by €1,622,197 (2022: increase of €1,270,358). Taking cognisance of the current low interest rate environment, the Bank does not expect interest rates to decrease by a further 100 basis points. Accordingly, the disclosure relating to an assumed decrease in interest rates by a 100 basis points is not deemed necessary.

2.1.3 Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfil commitments.

The Bank manages this risk, by maintaining a strong base of shareholders' capital considering the stage of its operations. The Bank manages its asset base with liquidity in mind and monitors future cash flows and changes in available liquidity on a regular basis.

The Bank maintains sufficient cash and, where possible, financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs. The Bank is exposed to calls on its available cash resources from maturing term deposits and withdrawals from savings, from contractual commitments arising on loans and advances to customers, and other cash outflows. The Assets and Liabilities Committee ensures that funds are always available to meet the expected demand for cash. In addition, the Bank manages its risk to a shortage of funds by monitoring forecast and actual cash flows, by monitoring the availability of raising funds to meet commitments associated with financial instruments and by holding financial assets which are expected to generate cash inflows that will be available to meet cash outflows on liabilities.

2. **Financial risk management** - continued

2.1 Financial risk factors – continued

2.1.3 Liquidity risk - continued

All liquidity policies and procedures are subject to review and approval by the Board of Directors.

The Bank uses key liquidity measures to monitor its liquidity risk, namely the ratio of liquid assets to deposit liabilities, the Liquidity Coverage Ratio ('LCR'), the Net Stable Funding Ratio ('NSFR') and an internal cash flow model, which is a minimum buffer of liquid assets set based on expected gross outflows.

(i) Liquidity Coverage Ratio

The LCR metric is designed to promote the short-term resilience of a bank's liquidity profile, and became a minimum regulatory standard from 1 October 2015, under European Commission ('EC') Delegated Regulation 2015/61. It aims to ensure that a bank has sufficient unencumbered high-quality liquid assets ('HQLA') to meet its liquidity needs in a 30-calendar-day liquidity stress scenario. HQLA consist of cash or assets that can be converted into cash at little or no loss of value in markets.

During the years ended 31 December 2023 and 2022 the LCR was above the regulatory minimum requirement.

(ii) Net stable funding ratio

The NSFR requires institutions to maintain sufficient stable funding relative to required stable funding, and reflects a bank's long-term funding profile (funding with a term of more than a year). It is designed to complement the LCR.

The Bank calculated the NSFR in line with the provisions of the amendments to Regulation (EU) No.575/2013, known as the Capital Requirements Regulation ('CRR II'), which became effective as from 28 June 2021. During the years ended 31 December 2023 and 2022 the NSFR was above the regulatory minimum requirement.

2. Financial risk management - continued

2.1 Financial risk factors – continued

2.1.3 Liquidity risk - continued

The following table discloses the gross carrying amount or fair value of financial assets and liabilities at the end of the reporting period by the remaining period to maturity.

	On demand or less than three months	Within one year but over three months	Within five years but over one year	More than five years	No maturity	Gross carrying amount/ Fair value
	€	€	€	€	€	€
As at 31 December 2023						
Financial assets						
Balances with central banks	45,517,151	-	-	-	5,352,397	50,869,548
Loans and advances to banks	10,227,227	-	-	-	-	10,227,227
Loans and advances to customers	7,901,027	24,325,483	159,490,553	150,609,683	-	342,326,746
Financial investments	1,295,903	6,757,496	59,162,707	26,917,328	-	94,133,434
Other assets	5,130,949	4,110,759	-	-	1,923,824	11,165,532
	70,072,257	**35,193,738**	**218,653,260**	**177,527,011**	**7,276,221**	**508,722,487**
Financial liabilities						
Amounts owed to customers	347,564,926	55,456,870	1,313,845	-	-	404,335,641
Amounts owed to institutions	25,400,000	-	-	-	-	25,400,000
Other liabilities	3,831,701	-	-	-	2,100,000	5,931,701
Subordinated liabilities	-	-	-	4,853,584	-	4,853,584
	376,796,627	**55,456,870**	**1,313,845**	**4,853,584**	**2,100,000**	**440,520,926**
Maturity gap	**(306,724,370)**	**(20,263,132)**	**217,339,415**	**172,673,427**		
Cumulative gap	**(306,724,370)**	**(326,987,502)**	**(109,648,087)**	**63,025,340**		

The balances with no maturity comprise reserve deposits relating to the Minimum Reserve Requirement amounting to €5,352,397 (2022: €2,163,884), balances pledged in favour of the Depositor Compensation Scheme amounting to €803,824 (2022: €429,781) and cash collateral held by a counterparty bank in relation to the Bank's cross currency swaps agreement with the counterparty bank with an indefinite term amounting to €1,120,000 (2022: nil) which will be due from the counterparty bank upon mutual termination of the agreement.

Other liabilities include a contribution received from the parent company, which as explained in Note 19, is earmarked to increase the Bank's share capital.

2. Financial risk management - continued

2.1 Financial risk factors – continued

2.1.3 Liquidity risk – continued

	On demand or less than three months	Within one year but over three months	Within five years but over one year	More than five years	No maturity	Gross carrying amount/ Fair value
	€	€	€	€	€	€
As at 31 December 2022						
Financial assets						
Balances with central banks	32,615,923	-	-	-	2,163,884	34,779,807
Loans and advances to banks	2,044,281	-	-	-	-	2,044,281
Loans and advances to customers	2,186,118	15,230,290	96,149,495	95,871,119	-	209,437,022
Financial investments	4,564,182	58,412,636	-	30,257,410	-	93,234,228
Other assets	681,313	2,302,590	-	-	429,781	3,413,684
	42,091,817	75,945,516	96,149,495	126,128,529	2,593,665	342,909,022
Financial liabilities						
Amounts owed to customers	137,853,324	120,983,271	5,248,699	-	-	264,085,294
Amounts owed to institutions	27,428,369	-	-	-	-	27,428,369
Other liabilities	1,743,840	-	-	-	4,000,000	5,743,840
	167,025,533	120,983,271	5,248,699	-	4,000,000	297,257,503
Maturity gap	(124,933,716)	(45,037,755)	90,900,796	126,128,529		
Cumulative gap	(124,933,716)	(169,971,471)	(79,070,675)	47,057,854		

As of 31 December 2023, unencumbered financial investments measured at FVOCI with a carrying amount of €14,924,762 (2022: €4,144,831) and unencumbered financial investments measured at amortised cost with a carrying amount of €52,490,230 (2022: €47,660,098) are able to be disposed within one month.

Meanwhile, as at 31 December 2023, debt securities measured at FVOCI with a carrying amount of €6,506,876 (2022: €6,232,324) and debt instruments measured at amortised cost with a carying amount of €20,211,566 (2022: €35,196,975) have been pledged in favour of financial institutions.

Similarly, as at 31 December 2023, loans and advances to customers with a carrying amount of €10,921,180 (2022: nil) have been pledged in favour of amounts owed to banks amounting to €8,400,000 (2022: nil).

2. Financial risk management - continued

2.1 Financial risk factors – continued

2.1.3 Liquidity risk – continued

The following table analyses the Bank's principal undiscounted cash flows payable under non-derivative financial liabilities into relevant maturity groupings based on the remaining period at the end of the reporting period to the contractual maturity date.

	On demand or less than three months	Within one year but over three months	Within five years but over one year	More than five years	Total
	€	€	€	€	€
As at 31 December 2023					
Financial liabilities					
Amounts owed to customers	349,131,566	56,532,874	1,344,790	-	407,009,230
Amounts owed to institutions	25,654,314	-	-	-	25,654,314
Other liabilities	3,831,701	-	-	-	3,831,701
Subordinated liabilities	97,537	294,754	1,565,948	6,613,534	8,571,773
	378,715,118	**56,827,628**	**2,910,738**	**6,613,534**	**445,067,018**
As at 31 December 2022					
Financial liabilities					
Amounts owed to customers	138,191,936	121,497,346	5,349,406	-	265,038,688
Amounts owed to institutions	27,639,785	-	-	-	27,639,785
Other liabilities	1,743,840	-	-	-	1,743,840
	167,575,561	**121,497,346**	**5,349,406**	**-**	**294,422,313**

The Bank had derivative financial instruments as at 31 December 2023.

As at 31 December 2023, the contractual undiscounted cash inflows and outflows attributable to the Bank's derivative transactions, which were all due in less than three months, amount to €7,482,517 and €7,378,111 respectively, and which result in a net inflow of €104,406.

2.2 Operational risk

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

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

2. Financial risk management - continued

2.2 Operational risk - continued

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

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

2.3 Capital risk management

The Bank's objectives when managing capital, which is a broader concept than 'equity' as disclosed in the statement of financial position, are:

- to comply with the capital requirements set by the MFSA;
- to safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- to maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored on an ongoing basis by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee and the European Union Directives and Regulations, as implemented by the MFSA for supervisory purposes.

The Bank is subject to maintain a ratio of total regulatory capital to risk-weighted assets ('Capital adequacy ratio') of 15.5% which constitutes the following: (a) a minimum own funds requirement of 8% (6% of which needs to be composed of T1 capital), (b) an additional P2R of 4% (c) combined buffer requirements of 2.5%, and (d) a P2G of 1% which is entirely made up of CET1 capital. The Bank has processes to ensure that the minimum regulatory requirements in relation to own funds are met at all times.

During the financial years ended 31 December 2023 and 31 December 2022, the Bank has met all external capital requirements at all times.

2. Financial risk management - continued

2.3 Capital risk management - continued

The minimum capital requirements are calculated for credit, market and operational risks. During the year, the Bank utilised the Standardised Approach for credit risk, the Basic Indicator Approach for operational risk and the Basic Method for foreign exchange risk in order to calculate the Pillar 1 minimum capital requirements. For credit risk, under the standardised approach, risk weights are determined according to credit ratings provided by internationally recognised credit agencies such as Fitch or their equivalents and by using the applicable regulatory risk weights for unrated exposures. The Basic Indicator Approach requires that the Bank allocates capital for operational risk by taking 15% of the average gross income, while the Basic Method requires the Bank to allocate 8% of its overall net foreign exchange position to calculate the capital requirement for foreign exchange risk.

The Bank calculates the own funds in line with the provisions discussed above. During the years ended and as at 31 December 2023 and 2022, the Bank has met at all times all capital requirements was above the regulatory minimum requirement.

2.4 Fair value of financial instruments

Financial instruments measured at fair value

IFRS 13 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions.

Fair values are consequently determined according to the following hierarchy:

- *Level 1 – quoted market price:* financial instruments with quoted prices for identical instruments in active markets.
- *Level 2 – valuation technique using observable inputs:* financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.
- *Level 3 – valuation technique with significant unobservable inputs:* financial instruments valued using models where one or more significant inputs are unobservable.

The following table analysis financial instruments recorded at fair value by level of the fair value hierarchy:

	Level 1	**Level 2**	**Total**
	€	**€**	**€**
At 31 December 2023			
Financial assets			
Financial investments measured at FVOCI			
Debt securities	21,431,638	-	21,431,638
Financial investments measured at FVPL			
Equity securities	1,175,881	-	1,175,881
Derivative financial instruments	-	116,891	116,891
Total financial assets	**22,607,519**	**116,891**	**22,724,410**

2. Financial risk management - continued

2.4 Fair value of financial instruments - continued

Financial instruments measured at fair value - continued

	Level 1	Level 2	Total
	€	€	€
At 31 December 2022			
Financial assets			
Financial investments measured at FVOCI			
Debt securities	10,377,155	-	10,377,155
Derivative financial instruments	-	-	-
Total financial assets	10,377,155	-	10,377,155

As at 31 December 2023 and 2022 the Bank's debt securities measured at FVOCI and equity securities measured at FVPL were all deemed to be categorised as Level 1 assets. The fair value of financial instruments traded in active markets (i.e. Level 1) is based on quoted market prices at the end of the reporting period. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Bank is the current bid price.

Level 2 instruments comprise derivatives held for risk management that are fair valued based on valuation models with the key methodology utilised comprising the calculation of the net present value of a series of expected cash flows, taking into account the different terms of each specific contract/instrument (discounted cash flow approach). These models use as their basis independently sourced market parameters including, for example, interest rate yield curves. Market parameters are either directly observable or are implied from observable instrument prices.

Financial instruments not measured at fair value

As at 31 December 2023, financial investments measured at amortised cost carried in the statement of financial position at €72,288,224 (2022: €82,632,530) have a fair value of €65,254,288 (2022: €69,643,171). The fair value of such instruments reflects the closing bid price quoted in an active market.

Loans and advances to banks and customers and amounts owed to banks, other institutions and customers are carried at amortised cost in the statement of financial position. The directors consider the carrying amounts of loans and advances to banks and customers to be a reasonable estimate of their fair value principally in view of the relatively short periods to repricing or maturity from the end of the reporting periods.

3. Critical accounting estimates, and judgments in applying accounting policies

Significant estimates and judgements

Estimates and judgements are continually evaluated based on historical experience and other factors including expectations of future events that are believed to be reasonable under the current circumstances.

The Bank makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. These estimates and assumptions present a risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. The Bank's management also makes judgements, apart from those involving estimations, in the process of applying the entity's accounting policies that may have a significant effect on the amounts recognised in the financial statements.

In the opinion of the directors, other than for estimates relating to expected credit losses in respect of the Bank's loans and advances to customers, the accounting estimates and judgments made in the course of preparing these financial statements are not difficult, subjective or complex to a degree which would warrant their description as critical in terms of the requirements of IAS 1.

Accordingly, the directors believe there are no areas involving a higher degree of judgement that would have a significant effect on the amounts recognised in the financial statements, and there are no key assumptions and other key sources of estimation uncertainty relating to estimates that require subjective or complex judgments, other than for estimates relating to expected credit losses in respect of the Bank's loans and advances to customers.

The measurement of the expected credit loss allowance for loans and advances to customers is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour. In this respect, a number of significant judgements are made by management. These include (i) determining whether a SICR or UTP event has occurred; (ii) choosing appropriate assumptions at borrower level for the measurement of ECLs; and (iii) determining appropriate forward-looking macroeconomic variables under different scenarios and prescribing an associated probability weighting for each scenario.

The level of expert judgement required is currently exacerbated by the heightened level of estimation uncertainty around predictions in respect of forward-looking scenarios, particularly the impact of geopolitical developments brought about by the continuing conflict between Russian and Ukraine, as well as the heightened inflation and interest rate risk environment.

In view of the level of estimation uncertainty involved, the directors considered the sensitivity of the ECL outcome to the macro-economic forecasts by recalculating the ECL under the different scenarios, applying a 100% weighting to each scenario, the effect of which is disclosed in Note 2.1.1.1.

4. Balances with central banks

	2023 €	2022 €
Gross carrying amount		
Term deposit	**12,133,959**	-
Minimum reserve requirement with the Central Bank of Malta	**4,294,623**	2,163,884
Minimum reserve requirement with the Czech National Bank	**1,057,774**	-
Other balances with Central Bank of Malta	**33,383,192**	32,615,923
	50,869,548	34,779,807
Expected credit loss allowances	**-**	(2,554)
Net carrying amount	**50,869,548**	34,777,253

The term deposit with the Czech National Bank (CNB) is charged interest at a fixed rate of 6.74%. This deposit was secured by a pledge in the form of treasury bills issued by the Government of the Czech Republic in favour of the Bank.

Other balances with the Central Bank of Malta are charged interest at the deposit facility rate set by the European Central Bank ('ECB'), which as at 31 December 2023 was set at 4.50% (2022: 2.00%).

5. Loans and advances to banks

	2023 €	2022 €
Gross and net carrying amount		
Repayable on call and at short notice	**10,227,227**	2,044,281

Loans and advances to banks as at 31 December 2023 include €4,822,731 (2022: €296,593) receivable from a related party bank.

6. Financial investments

The Bank's financial investments consist of listed debt and other fixed income securities which are measured at FVOCI and listed equity securities which are measured at FVPL. The Bank's financial investments are analysed as follows:

	2023 €	2022 €
Debt instruments measured at FVOCI issued by:		
Local government	**469,200**	433,800
Local entities	**1,048,592**	968,335
Foreign governments	**8,606,348**	261,925
Foreign entities	**11,307,498**	8,713,095
	21,431,638	10,377,155

6. Financial investments - continued

The Bank's financial investments consist of listed debt and other fixed income securities which are measured at FVOCI and listed equity securities which are measured at FVPL. The Bank's financial investments are analysed as follows:

	2023	2022
	€	€
Equity instruments measured at FVPL issued by:		
Foreign entities	**1,175,881**	-
	1,175,881	-
Debt instruments measured at amortised cost issued by:		
Foreign governments	**4,163,128**	4,210,088
Foreign entities	**68,538,668**	78,646,985
	72,701,796	82,857,073
Expected credit loss allowances	**(413,572)**	(224,543)
Net carrying amount	**72,288,224**	82,632,530
Total debt and equity instruments	**94,895,743**	93,009,685

The movement in the carrying amount of financial investments is summarised as follows:

	2023	2022
	€	€
Debt instruments measured at FVOCI		
At 1 January	**10,377,155**	15,476,833
Additions	**17,339,976**	-
Disposals	**(6,346,025)**	(3,398,742)
Amortisation of premium/discount	**19,566**	(74,597)
Changes in fair value	**92,733**	(1,737,260)
Foreign exchange movement	**(51,767)**	110,921
At 31 December	**21,431,638**	10,377,155
Equity instruments measured at FVPL		
At 1 January	-	-
Additions	**2,647,429**	-
Disposals	**(1,728,163)**	-
Changes in fair value	**256,615**	-
At 31 December	**1,175,881**	-
Debt instruments measured at amortised cost		
At 1 January	**82,632,530**	69,378,654
Additions	**3,000,000**	16,852,578
Redemption/Maturity	**(12,082,882)**	(4,161,508)
Amortisation of premium/discount	**(517,357)**	70,209
Movements in credit loss allowances	**(189,029)**	(168,458)
Foreign exchange momvement	**(555,038)**	661,055
At 31 December	**72,288,224**	82,632,530

6. Financial investments - continued

As at 31 December 2023, the expected credit loss allowances in respect of financial investments measured at FVOCI amounted to €9,854 (2022: €11,146).

Investment securities with a nominal value of €25,590,000 (2022: €16,390,000) and carrying amount of €26,718,442 (2022: €16,886,662) have been pledged in favour of the Central Bank of Malta for the purpose of accessing the European Central Bank's open market operations and against which the Bank has drawn €17,000,000 (2022: €10,000,000).

In addition, as at 31 December 2022, investment securities with a nominal value of €23,950,940 and carrying amount of €24,542,637 had been pledged as financial collateral in respect of amounts owed to a related party bank amounting to €17,428,369. As at 31 December 2023, no investment securities have been pledged as financial collateral in respect of amounts owed to a related party bank amounting to €8,400,000 (Note 17).

7. Derivative financial instruments

	2023 **€**	2022 €
Derivative assets		
Cross currency swaps	**116,891**	-

During 2023, the Bank entered into cross currency swaps with a counterparty bank to hedge the foreign currency exposures arising out of loans and advances to customers and financial investments. As part of its agreement, the Bank has provided a security in the form of cash collateral in favour of the counterparty bank amounting to €1,120,000 (Note 9).

The derivative financial instruments held at 31 December 2023 relate to a forward purchase of CZK 29,680,800 against EUR maturing within one year from the end of the reporting period at the contractual rate of 24.734 and a forward sale of USD 6,826,813 against EUR at the average contractual rate of 1.0874.

During 2021, the Bank had a pay fixed receive floating interest rate swap contract with a related party with a notional amount of €10,000,000. During 2022, the Bank and the related party agreed to terminate the derivative contract, which resulted in a gain of €310,047 (Note 25).

8. Loans and advances to customers

	2023 **€**	2022 €
Gross carrying amount		
Term loans and advances	**334,425,719**	207,069,915
Repayable on call and at short notice	**7,901,027**	2,367,107
	342,326,746	209,437,022
Expected credit loss allowances	**(642,903)**	(476,081)
Net carrying amount	**341,683,843**	208,960,941

8. Loans and advances to customers - continued

Loans and advances to customers at 31 December 2023 include gross credit exposures to related parties amounting to €10,000,000 (2022: €10,000,000) and €4,375,000 (2022: €4,375,000), subject to an interest rate of 4.89% (2022: 3.2%) per annum and 6.50% (2022: 4.79%) per annum, respectively. These loans are unsecured and due on 31 May 2024 (2022: 31 May 2023) and 19 December 2029, respectively.

Loans and advances to customers with a carrying amount of €10,921,180 (2022: nil) have been pledged in favour of amounts owed to banks amounting to €8,400,000 (2022: nil) (Note 17).

9. Prepayments and other assets

	2023 **€**	2022 €
Amounts due from immediate parent company	**622,924**	599,338
Amounts due from ultimate parent company	**529,820**	529,820
Amounts due from group undertakings	**91,492**	85,236
Amounts due from related parties	**6,155,530**	923,064
Prepayments to a related party	**-**	2,773,864
Accrued interest income	**1,254,644**	652,629
Other assets	**2,511,123**	623,597
Other prepayments	**396,942**	368,262
	11,562,475	6,555,810

Amounts due from the immediate parent company, ultimate parent company, group undertakings and related parties are unsecured, non-interest bearing and repayable on demand. The directors deem that ECLs in respect of these balances are immaterial on the basis of their short-term nature and the low credit risk that the counterparties present.

On 1 January 2019, the Bank entered into an agreement with a related party for the services to be received by the Bank in relation to maintenance and support services in connection with the Bank's IT system for a period of 5 years. In 2022, the Bank entered into an amendment to this agreement, and also made prepayments amounting to €2,962,471 in relation to the above services. The terms of the services were extended by 9 years effective 1 June 2022. As at 31 December 2022, the balance of this prepayment amounted to €2,773,864. In 2023, the Bank amended the service agreement with the same related party and extended the services covered by the agreement to include hosting and operational support of data centres, document management systems, and internet digital banking channels.

On 1 January 2023, the Bank made further advances of €719,204 to the same related party and on the same day entered into an agreement to transfer assets to the same related party computer hardware with a carrying amount of €184,920 (Note 10), licences and capitalised system development cost with a carrying amount of €1,436,943 (Note 11). As part of the same agreement, the receivables in respect of the transferred assets, prepayments and other advances were converted into an advance subject to interest rate of EURIBOR + 1.5% per annum. The advance is expected to be settled through the provision of services by the related party under the amended service agreement. During 2023, the Bank has offset amounts due to the related party arising from the said agreement amounting to €245,824 against the Bank's advances to the related party. As at 31 December 2023, the advances amounted to €4,869,107 and are included in the above table within 'Amounts due from related parties'.

9. Prepayments and other assets -continued

As at 31 December 2023, other assets also include a balance of €803,824 (2022: €429,781) that has been placed under the Depositor Compensation Scheme ('DCS') account representing the Bank's payment commitment in terms of the Depositor Compensation Scheme Regulations (Subsidiary Legislation, 371.09) of the Laws of Malta. This also includes cash collateral held by a counterparty bank in relation to the Bank's cross currency swaps agreement amounting to €1,120,000 (2022: nil).

10. Property and equipment

	Motor vehicles	Furniture & fittings	Computer hardware	Total
	€	€	€	€
At 1 January 2022				
Cost	125,100	212,819	422,422	760,341
Accumulated depreciation	(15,476)	(113,728)	(112,758)	(241,962)
Net book amount	109,624	99,091	309,664	518,379
Year ended 31 December 2022				
Opening net book amount	109,624	99,091	309,664	518,379
Additions	91,610	66,791	37,133	195,534
Depreciation charge	(35,032)	(29,356)	(60,899)	(125,287)
Closing net book amount	166,202	136,526	285,898	588,626
At 31 December 2022				
Cost	216,710	279,610	459,555	955,875
Accumulated depreciation	(50,508)	(143,084)	(173,657)	(367,249)
Net book amount	166,202	136,526	285,898	588,626
Year ended 31 December 2023				
Opening net book amount	166,202	136,526	285,898	588,626
Additions	72,000	24,860	33,682	130,542
Disposal	(90,750)	-	(196,025)	(286,775)
Depreciation charge	(74,547)	(16,131)	(55,586)	(146,264)
Release of depreciation on disposals	21,314	-	11,105	32,419
Closing net book amount	**94,219**	**145,255**	**79,074**	**318,548**
At 31 December 2023				
Cost	197,960	304,470	297,212	799,642
Accumulated depreciation	(103,741)	(159,215)	(218,138)	(481,094)
Net book amount	**94,219**	**145,255**	**79,074**	**318,548**

During 2023, the Bank disposed one of its motor vehicles with a carrying amount of €69,436 which resulted in a loss of €14,616.

During 2023, the Bank entered into a contract to transfer assets related to licences and implementation of a core banking system to a related party of which €184,920 relates to computer hardware.

11. Intangible assets

	Computer software €
At 1 January 2022	
Cost	1,887,300
Accumulated amortisation	(578,227)
Net book amount	1,309,073
Year ended 31 December 2022	
Opening net book amount	1,309,073
Additions	463,446
Amortisation charge	(156,394)
Closing net book amount	1,616,125
At 31 December 2022	
Cost	2,350,746
Accumulated amortisation	(734,621)
Net book amount	**1,616,125**
Year ended 31 December 2023	
Opening net book amount	1,616,125
Additions	33,725
Disposals	(1,482,076)
Amortisation charge	(116,648)
Release of amortisation of disposals	45,133
Closing net book amount	**96,259**
At 31 December 2023	
Cost	902,395
Accumulated depreciation	(806,136)
Net book amount	**96,259**

During 2023, the Bank entered into a contract to transfer computer software with a total carrying amount of €1,436,943 to a related party.

12. Deferred tax assets

The movements in deferred tax assets during the year were as follows:

	2023 **€**	2022 €
At beginning of year	**3,362,978**	3,267,001
Recognised in profit or loss		
- Utilisation of unabsorbed tax losses	**(1,215,621)**	(536,986)
Recognised in other comprehensive income		
- Net changes in fair value arising during the year	**(32,456)**	608,639
- Reclassification adjustments: net amounts reclassified to profit or loss	**57,638**	24,324
At end of year	**2,172,539**	3,362,978

12. Deferred tax assets - continued

The year-end balance represents temporary differences attributable to:

	2023	2022
	€	€
Assets		
Unabsorbed tax losses	**1,532,448**	2,748,069
Fair valuation of financial investments measured at FVOCI	**640,091**	614,909
	2,172,539	3,362,978

The major part of the recognised deferred tax assets are expected to be recovered after more than twelve months from the end of the reporting period.

Deferred tax assets are recognised for unabsorbed tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. The directors believe that the Bank is well placed to manage its business risks successfully and have a reasonable expectation that the deferred tax asset will crystallise in the foreseeable future. In assessing whether the deferred tax asset should be recognised, the directors have taken into account the business plan and commitments made by the shareholder. The directors will continue to monitor the position on an ongoing basis.

13. Share capital

	2023		2022	
	No. of shares	**€**	No. of shares	€
Authorised				
Ordinary shares at €1 each	**75,000,000**	**75,000,000**	50,000,000	50,000,000
Issued and fully paid up				
Ordinary shares at €1 each	**52,250,000**	**52,250,000**	35,750,000	35,750,000

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at general meetings of the Bank. All shares rank equally with regards to the Bank's residual assets.

During 2022, by virtue of a resolutions dated 26 May 2022 and 31 August 2022, the Bank increased its issued share capital by €4,000,000 and €3,000,000 divided into 4,000,000 and 3,000,000 ordinary shares of a nominal value of €1.00 each, respectively. The issued share capital was thereby increased from €28,750,000 (divided into 28,750,000 ordinary shares of a nominal value of €1.00 each) to €35,750,000 (divided into 35,750,000 ordinary shares of a nominal value of €1.00 each).

By virtue of a resolution dated 30 November 2022, the Bank resolved to increase further its issued share capital by €4,000,000 divided into 4,000,000 ordinary shares of a nominal value of €1.00 each from €35,750,000 (divided into 35,750,000 ordinary shares of a nominal value of €1.00 each) to €39,750,000 (divided into 39,750,000 ordinary shares of a nominal value of €1.00 each). As at 31 December 2023, the transaction was subject to regulatory approval. Accordingly, the amount received from the parent company in respect of this transaction is included in 'Other liabilities' as at 31 December 2022 (Note 19). This was reclassified to 'Share capital' upon approval in 2023.

By virtue of resolution dated 27 March 2023, the shareholders of the Bank resolved to, subject to approval of MFSA, convert Perpetual Capital notes instrument amounting to €2,000,000 to issued share capital. Upon approval of MFSA, by virtue of resolution dated 9 May 2023, the Bank increased its issued share capital by €2,000,000 divided into 2,000,000 ordinary shares of a nominal value of €1.00 each from €39,750,000 (divided into 39,750,000 ordinary shares of a nominal value of €1.00 each) to €41,750,000 (divided into 41,750,000 ordinary shares of a nominal value of €1.00 each).

13. Share capital - continued

By virtue of a resolution dated and effective 30 March 2023, the Bank increased further its issued share capital by €4,500,000 divided into 4,500,000 ordinary shares of a nominal value of €1.00 each from €41,750,000 (divided into 41,750,000 ordinary shares of a nominal value of €1.00 each) to €46,250,000 (divided into 46,250,000 ordinary shares of a nominal value of €1.00 each).

By virtue of a shareholder's resolution dated 19 June 2023, the shareholders resolved to increase the authorised share capital of the Bank from 50,000,000 ordinary shares of €1.00 each to 75,000,000 ordinary shares of €1.00 each.

By virtue of a resolution dated and effective 17 July 2023 , the Bank increased further its issued share capital by €6,000,000 divided into 6,000,000 ordinary shares of a nominal value of €1.00 each from €46,250,000 (divided into 46,250,000 ordinary shares of a nominal value of €1.00 each) to €52,250,000 (divided into 52,250,000 ordinary shares of a nominal value of €1.00 each).

14. Perpetual capital notes

	2023 **€**	2022 €
At beginning of year	**15,500,000**	15,500,000
Conversion into share capital	**(2,000,000)**	-
Issue of new perpetual capital notes	**3,992,939**	-
At end of year	**17,492,939**	15,500,000

Analysed as follows:

	2023 **€**	2022 €
2W repo rate + 0.25bp Capital investment bonds	**11,992,939**	8,000,000
3.78% Temporary write-down notes	**5,500,000**	5,500,000
3.78% Investment capital contribution	**-**	2,000,000
	17,492,939	15,500,000

During 2022, by virtue of a resolution dated 6 October 2022, the Bank redenominated Temporary write-down notes held by a shareholder of €8,000,000 to their equivalents of CZK 196,000,000 and modified the terms and conditions of the instrument and renamed it as Capital investment bonds which was approved by the shareholder on the same day.

By virtue of a resolution dated 2 February 2023, the Bank issued Capital investment bonds amounting to euro equivalent of €3,992,939. These notes are subject to floating rate which as at 31 December 2023 was 7.25% and which resets every quarter end.

By virtue of a resolution dated 5 May 2023, the Bank converted Investment capital contribution of €2,000,000 into 2,000,000 Ordinary shares of €1 each.

14. Perpetual capital notes – continued

Perpetual capital notes denominated in CZK are translated using the historical rate.

All interest payments on perpetual capital notes are cancellable at the discretion of the Bank.

These capital instruments qualify as Additional Tier 1 instruments in accordance with the requirements of Articles 51 to 54 of the Regulation (EU) No. 575/2013 and are categorised as equity within the Bank's Statement of Financial Position under the requirements of IFRSs as adopted by the EU.

15. Fair value reserve

The fair value reserve reflects the effects of the fair value measurement of financial instruments classified as at fair value through other comprehensive income, net of deferred taxes. In respect of debt securities measured at FVOCI, any gains or losses are not recognised in profit or loss until the debt security has been disposed of.

16. Dividend

By virtue of resolution dated 1 September 2023, the Bank's shareholders resolved to approve the declaration of dividend amounting to €1,960,000, net of tax, distributed to shareholders in respect of the financial year ended 31 December 2022.

17. Amounts owed to banks and other institutions

	2023	2022
	€	€
Amounts owed to banks	**8,400,000**	17,428,369
Amounts owed to other institutions	**17,000,000**	10,000,000
	25,400,000	27,428,369

During the height of the COVID-19 pandemic in 2020, the Governing Council of the European Central Bank (ECB) decided to conduct a series of longer-term refinancing operations, called pandemic emergency longer-term refinancing operations ('PELTROs'). The Bank participated in such funding and as at 31 December 2022, the Bank borrowed a total of €10,000,000, which matured in 2023. In 2023, the Bank borrowed additional funds of €17,000,000 from longer-term refinancing operation ('LTROs') which will mature in 2024.

As at 31 December 2023, amounts owed to banks relate to pledge agreements entered into with a related party bank which were secured by a pledge over the Bank's loans and advances to customers (Note 8). As at 31 December 2022, amounts owed to banks relate to fixed short term repurchase agreements entered into with a related party bank which were secured by a pledge over the Bank's investments in debt instruments (Note 6).

18. Amounts owed to customers

	2023	2022
	€	€
Term deposits	**300,279,204**	199,589,139
Repayable on call and at short notice	**104,056,437**	64,496,155
	404,335,641	264,085,294

19. Other liabilities

	2023	2022
	€	€
Accrued interest expense	**2,895,821**	693,249
Other accrued expenses	**208,496**	42,138
Other liabilities	**2,827,384**	5,008,453
	5,931,701	5,743,840

By virtue of a resolution dated 30 November 2022, the Bank resolved to increase its issued share capital by €4,000,000 divided into 4,000,000 ordinary shares of a nominal value of €1.00 each (Note 13). As at 31 December 2022, the transaction was subject to regulatory approval. Accordingly, the amount received from the parent company in respect of this transaction is included in 'Other liabilities' in the table above and under financing activities in the statement of cash flows.

By virtue of a resolution dated 12 December 2023, the Bank resolved to increase its issued share capital by €2,100,000 divided into 2,100,000 ordinary shares of a nominal value of €1.00 each (Note 13). As at 31 December 2023, the transaction was subject to regulatory approval. Accordingly, the amount received from the parent company in respect of this transaction is included in 'Other liabilities' in the table above and under financing activities in the statement of cash flows.

20. Subordinated liabilities

On 27 April 2023, the Bank has offered CZK 240,000,000 unsecured subordinated bonds with a maturity date of 30 June 2033 at a floating rate linked to 2W repo rates announced by Czech National Bank at the quarter end plus 0.95bp. As at 31 December 2023, the interest rate was 7.95%. Out of the offered amount, the Bank issued CZK 120,000,000 to related parties. The subordinated liabilities will, in the event of the voluntary or involuntary liquidation or bankruptcy of the Bank, be subordinated to the claims of depositors and other creditors.

Subordinated liabilities are translated using the prevailing foreign exchange rate at year end. As at 31 December 2023, subordinated liabilities amounted to €4,853,589.

21. Commitments

	2023	2022
	€	€
Undrawn credit facilities	**146,166,162**	110,191,071

As part of its business activities, the Bank enters into various contractual commitments to extend credit. 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 unused commitments since most commitments to extend credit are contingent upon customers meeting specific conditions.

22. Interest income

	2023	2022
	€	€
On balances with banks and other institutions	**2,531,813**	155,622
On financial investments measured at FVOCI	**789,611**	652,800
On financial investments measured at amortised cost	**3,676,936**	2,954,965
On loans and advances to customers	**16,656,418**	7,057,017
On advances to a related party	**209,658**	-
	23,864,435	10,820,404

Interest income on loans and advances to customers include interest income in respect of loans and advances to related parties amounting to €713,825 (2022: €525,162).

23. Interest expense

	2023	2022
	€	€
On balances with central banks	**-**	17,257
On amounts owed to customers	**11,463,043**	1,823,214
On amounts owed to banks and other institutions	**543,055**	1,768,743
On subordinated liabilities	**266,526**	-
	12,272,624	3,609,214

Interest expense on amounts owed to banks amounting to €425,883 (2022: €1,732,993) arise in respect of transactions with related parties as disclosed in Note 17.

24. Net fee income

	2023	2022
	€	€
Fee income		
Credit related fees	**877,498**	475,914
Other fees	**2,490**	15,028
	879,988	490,942
Fee expense		
Credit related fees	**38,380**	22,200
Correspondent bank charges	**75,068**	38,236
Other fees	**87,602**	17,995
	201,050	78,431
Net fee income	**678,938**	412,511

25. Net income from financial instruments held for trading or managed on a fair value basis

	2023 €	2022 €
Net changes in fair value of equity instruments	**256,615**	-
Net income from foreign exchange transactions and balances	**(144,627)**	70,598
Net fair value losses on foreign exchange derivative contracts	**(29,300)**	-
Net interest expense on derivative financial instruments	**(8,147)**	(144,654)
Gain on disposal of equity instruments	**427**	-
Net gains on terminated derivative transactions	**-**	310,047
	74,968	235,991

Net interest expense on derivative financial instruments and net gains on terminated derivatives arise in respect of transactions with related parties as disclosed in Note 7.

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

	2023 €	2022 €
Increase/(decrease) in expected credit losses on:		
- Balances with central banks	**(2,554)**	-
- Loans and advances to banks	**-**	(222)
- Loans and advances to customers	**166,822**	126,373
- Financial investments measured at amortised cost	**189,029**	168,458
- Financial investments measured at FVOCI	**(1,292)**	8,991
Other credit impairment charges	**168,627**	-
	520,632	303,600

27. Employee compensation and benefits

	2023 €	2022 €
Wages and salaries	**3,595,845**	2,257,528
Social security costs	**213,945**	81,221
	3,809,790	2,338,749

The average number of persons employed by the Bank throughout the financial years 2023 and 2022 was as follows:

	2023	2022
Managerial	**22**	22
Other	**49**	41
	71	63

28. Administrative expenses

	2023	2022
	€	€
IT support	**951,173**	628,899
Regulatory expenses	**1,138,317**	458,970
Short-term lease payments	**364,452**	315,836
Legal and professional fees	**569,188**	391,688
Depreciation of property and equipment (Note 10)	**146,264**	125,287
Amortisation of intangible assets (Note 11)	**116,648**	156,394
Directors' fees	**219,675**	138,347
Loss on disposal of property and equipment (Note 10)	**14,616**	-
Other administrative expenses	**592,291**	622,927
	4,112,624	2,838,348

Other administrative expenses mainly comprise of marketing costs, telecommunication costs, and other services or expense items that are incurred in the course of the Bank's operations.

The Bank has a lease agreement in place with a related party to lease property used as office space and car spaces. The lease contract is a perpetual contract made for fixed periods of 1 year such that it is automatically renewable annually but has a termination option. The termination option held is exercisable by both the Bank and by the respective lessor without permission from the other party by giving 6 months' notice in writing. The lease term is therefore deemed to be the earliest point in time at which both parties can exit the contract and the related contractual obligations, being 6 months. In addition, during 2023 and 2022, the Bank entered into lease agreements with third parties to lease apartments for its employees' use with terms of less than one year.

Accordingly, these leases qualify and are accounted for as a short-term lease. The lease payments are recognised on a straight-line basis as an expense in profit or loss over the term of the lease.

Fees charged by the auditor for services excluding of VAT rendered during the financial year relate to the following:

	2023	2022
	€	€
Annual statutory audit	**135,000**	90,000
Other non-audit assurance services	**14,500**	4,500
Tax compliance and advisory services	**2,350**	2,350
Other non-audit services	**20,000**	45,000
	171,850	141,850

29. Tax expense

Tax expense consists of the following:

	2023 €	2022 €
Final tax on interest income on financial investments	**511,335**	-
Deferred tax	**1,215,621**	536,986
	1,726,956	536,986

The tax on the Bank's profit before tax, which relates to final tax on interest income on financial investments and deferred tax expense, differs from the theoretical amount that would arise using the effective tax rate applicable to the Bank as follows:

	2023 €	2022 €
Profit before tax	**4,100,985**	2,500,681
Tax at the applicable rate of 35%	**1,435,345**	875,238
Tax effect of:		
Expenses not deductible for tax purposes	**284,954**	112,782
Income not taxable for tax purposes	**(139,600)**	-
Utilisation of capital allowances in respect of which no deferred tax was recognised	**(186,111)**	(451,034)
Withholding tax suffered abroad	**332,368**	-
Tax expense	**1,726,956**	536,986

30. Cash and cash equivalents

Cash and cash equivalents comprise balances with contractual maturities of not more than three months for the purposes of the statement of cash flows and which form an integral part of the Bank's cash management.

	2023 €	2022 €
Statement of cash flows		
Balances with central banks	**33,383,192**	32,615,923
Loans and advances to banks	**10,227,227**	2,044,281
Cash and cash equivalents	**43,610,419**	34,660,204
Statement of financial position		
Balances with central banks	**50,869,548**	34,777,253
Loans and advances to banks	**10,227,227**	2,044,281
Adjustments for:		
Term deposit with the Central Bank of Czech Republic	**(12,133,959)**	-
Reserve Deposit Requirement	**(5,352,397)**	(2,163,884)
Expected credit loss allowances	**-**	2,554
Cash and cash equivalents	**43,610,419**	34,660,204

31. Related parties

Identification of related parties

The immediate parent company of the Bank is SAB Europe Holding Ltd., a company incorporated and registered in Malta, the registered address of which is Suite 3, Tower Business Centre, Tower Street, Swatar, Malta, while the ultimate parent company of the Bank is SAB Financial Group a.s., headquartered in Czech Republic. The ultimate controlling party of the Bank is Mr Radomir Lapcik, being the sole shareholder of SAB Financial Group a.s. All entities which are ultimately controlled by or under significant influence of SAB Financial Group a.s. or Mr Radomir Lapcik are considered to be related parties.

Key management personnel of the Bank, being the Bank's directors, who have the authority and responsibility for planning, directing and controlling the activities of the Bank, close family members of key management personnel and entities which are controlled or jointly controlled by key management personnel or their close family members are also considered to be related parties.

The following tables show the total amount of transactions entered into with related parties during the year and balances held with related parties as at the end of the financial year.

Transactions and balances with the Bank's immediate parent company

	2023	2022
	€	€
Assets		
Prepayments and other assets	**622,924**	599,338
Liabilities		
Other liabilities	**2,100,000**	4,000,000

Transactions with the Bank's immediate parent company in respect of issued share capital during 2023 and 2022 are explained in Note 13.

Transactions and balances with the Bank's ultimate parent company

	2023	2022
	€	€
Assets		
Prepayments and other assets	**529,820**	529,820
Liabilities		
Subordinated liabilities	**1,941,434**	-
Income statement		
Interest expense	**106,786**	-

31. Related parties - continued

Transactions and balances with other related parties ultimately controlled by or under significant influence of SAB Financial Group a.s. or Mr. Radomir Lapcik.

	2023	2022
	€	€
Assets		
Loans and advances to banks	**4,822,731**	296,593
Loans and advances to customers	**14,375,000**	14,375,000
Prepayments and other assets	**6,247,022**	3,782,164
Liabilities		
Amounts owed to banks and other institutions	**8,400,000**	17,428,370
Subordinated liabilities	**2,912,150**	-
Other liabilities	**88,006**	-
Income statement		
Interest income	**923,483**	525,162
Interest expense	**585,623**	1,732,993
Net income from financial instruments held for trading or managed on a fair value basis	**8,147**	165,393
Administrative expenses	**610,390**	168,720

Transactions with other related parties in respect of perpetual capital notes issued by the Bank during 2022 and 2023 are explained in Note 14. The interest paid on perpetual capital notes amounted to €1,096,251 (2022: €571,830).

During 2022, the Bank made prepayments of €2,962,471 to a related party in accordance with amendments to an agreement entered into with the related party for implementation of the core banking system. As at 31 December 2022, the balance of this prepayment amounted to €2,773,864.

During 2023, the Bank entered into an agreement with the same related party to transfer to the same related party asset items relating to computer hardware, licences and capitalised cost in relation to the implementation of a core banking system with a total carrying amount of €1,621,863 (Notes 10 and 11). The Bank also amended its service agreement with the related party into a 3-year contract covering extended IT outsourcing services. The receivables in respect of the transferred assets and the prepayments were converted into an advance. As at 31 December 2023, total advances made to the related party in respect of this agreement amounted to €4,869,107 (Note 9).

Transactions with the Bank's key management personnel

	2023	2022
	€	€
Income statement		
Directors' fees	**219,675**	138,347

32. Contingent liabilities

The Bank has contingent liabilities related to possible future contributions to the DCS. The DCS provides compensation, up to certain limits, to eligible customers of credit institutions that are unable, or likely to be unable, to pay claims against them. The DCS may impose a further contribution on the Bank to the extent the contributions to date are not sufficient to cover the compensation due to customers in any future possible collapse. The ultimate contribution to the industry as a result of a collapse cannot be estimated reliably. It is dependent on various uncertain factors including the potential recovery of assets by the DCS, changes in the level of protected products (including deposits and investments) and the population of DCS members at the time. As at 31 December 2023, deposits placed directly in the DCS' account amounted to €803,824 (2022: €429,781) (Note 9). The Bank discloses the identical amount as contingent liability to reflect the possibility that this amount becomes payable.

33. Statutory information

FCM Bank Limited is a limited liability company and is incorporated in Malta.

The immediate parent company of the Bank is SAB Europe Holding Ltd., a company incorporated and registered in Malta, the registered address of which is Suite 3, Tower Business Centre, Tower Street, Swatar, Malta.

The ultimate parent company of the Bank is SAB Financial Group a.s. which is incorporated and registered in Czech Republic, the registered address of which is Senovážné náměstí 1375/19 110 00 Praha 1, Czech Republic.

Five-Year Summary

Statement of comprehensive income

	Year ended	Year ended	Year ended	Year ended	Year ended
	31 December	31 December	31 December	31 December	31 December
	2023	2022	2021	2020	2019
			Restated		
			€	€	€
Interest income	**23,555,637**	10,820,404	4,788,773	1,487,441	497,027
Interest expense	**(12,272,624)**	(3,609,214)	(1,259,213)	(779,199)	(934,511)
Net interest income/(expense)	**11,591,811**	7,211,190	3,529,560	708,242	(437,484)
Fee income	**879,988**	490,942	113,936	47,569	175,764
Fee expense	**(201,050)**	(78,431)	(105,802)	(76,234)	(134,013)
Net fee income/(expense)	**678,938**	412,511	8,134	(28,665)	41,751
Net income from financial Instruments held for trading or managed on a fair value basis	**74,968**	235,991	(100,388)	-	-
Realised gain on disposal of financial investments at FVOCI	**164,681**	69,498	668,915	80,640	1,445,501
Other income	**33,633**	52,188	12,762	1,932,852	903,840
Operating income	**12,544,031**	7,981,378	4,118,983	2,693,069	1,953,608
Changes in expected credit losses	**(520,632)**	(303,600)	(142,712)	(174,670)	(85,915)
Employee compensation and benefits	**(3,809,790)**	(2,338,749)	(1,888,614)	(1,198,088)	(827,011)
Administrative expenses	**(4,112,624)**	(2,838,348)	(1,886,758)	(1,315,615)	(1,336,845)
Profit/(loss) before tax	**4,100,985**	2,500,681	200,899	4,696	(296,163)
Tax (expense)/income	**(1,726,956)**	(536,986)	1,599,997	400,229	381,055
Profit for the year	**2,374,029**	1,963,695	1,800,896	404,925	84,892
Other comprehensive income					
Fair valuation of financial investments measured at FVOCI					
- net changes in fair value during the year, before tax	**92,733**	(1,737,260)	301,044	381,395	121,456
- Net amounts reclassified to profit or loss, before tax	**(164,681)**	(69,498)	(668,915)	(80,640)	-
- Income tax relating to components of other comprehensive income	**25,182**	632,963	128,755	(105,264)	(41,545)
Other comprehensive income/ (loss) for the year, net of tax	**(46,766)**	(1,173,795)	(239,116)	195,491	79,911
Total comprehensive income for the year, net of tax	**2,327,263**	789,900	1,561,780	600,416	164,803

Five-year summary - continued

Statement of financial position

	2023	2022	2021 Restated	2020	2019
	€	**€**	€	€	€
Assets					
Cash and balances with central banks	**50,869,548**	34,777,253	4,589,358	19,378,296	13,317,530
Loans and advances to banks	**10,227,227**	2,044,281	3,362,185	3,106,276	8,104,291
Loans and advances to customers	**341,683,843**	208,960,941	137,753,511	43,918,435	17,564,550
Financial investments	**94,895,743**	93,009,685	84,855,487	43,766,208	4,471,393
Derivative financial instruments	**116,891**	-	2,171,859	756,057	124,328
Property and equipment	**318,548**	588,626	518,379	63,547	68,449
Intangible assets	**96,259**	1,616,125	1,309,073	190,285	250,161
Deferred tax assets	**2,172,539**	3,362,978	3,267,001	1,538,249	1,243,284
Prepayment and other assets	**11,562,475**	6,555,810	3,159,922	2,311,802	911,730
Total assets	**511,943,073**	350,915,699	240,986,775	115,029,155	46,055,716
Equity					
Share capital	**52,250,000**	35,750,000	28,750,000	20,250,000	20,250,000
Perpetual Capital Notes	**17,492,939**	15,500,000	15,500,000	-	-
Fair value reserve	**(1,184,275)**	(1,137,509)	36,286	275,402	79,911
Retained earnings/(Accumulated losses)	**2,863,483**	3,545,705	2,153,840	479,302	(8,825,623)
Total equity	**71,422,147**	53,658,196	46,440,126	21,004,704	11,504,288
Liabilities					
Amounts owed to banks and other institutions	**25,400,000**	27,428,369	52,633,639	10,000,000	34,138,102
Amounts owed to customers	**404,335,641**	264,085,294	141,449,401	83,546,776	-
Derivative financial instruments	**-**	-	11,793	-	-
Other liabilities	**5,931,701**	5,743,840	451,816	477,675	413,326
Subordinated liabilities	**4,853,584**				
Total liabilities	**440,520,926**	297,257,503	194,546,649	94,024,451	34,551,428
Total liabilities and equity	**511,943,073**	350,915,699	240,986,775	115,029,155	46,055,716

Additional Regulatory Disclosures

31 December 2023

1. Risk management

1.1 Overview of risk disclosures

These Additional Regulatory Disclosures (‘ARDs’) have been prepared by the Bank in accordance with the Pillar 3 quantitative and qualitative disclosure requirements as governed by Banking Rule 07: Publication of Annual report and Audited Financial Statements of Credit Institutions BR/07/2014 authorised under the Maltese Banking Act, (Cap. 371), issued by the Malta Financial Services Authority. These disclosures are published by the Bank on an annual basis as part of the Annual Report.

As per banking regulations, these disclosures are not subject to an external audit, except to the extent that any disclosures are equivalent to those made in the Financial Statements, which have been prepared in accordance with the requirements of International Financial Reporting Standards (‘IFRS’) as adopted by the EU. The Bank is satisfied that internal verification procedures ensure that these ARDs are presented fairly.

These ARDs should be read in conjunction with the Financial Statements and Notes to the Financial Statements.

1.2 Risk management framework

The Board of Directors has the overall responsibility for the establishment and oversight of the Bank’s risk management framework. The Bank has in place a Credit and Risk Committee that is responsible for developing and monitoring the Bank’s risk management policies in its specific areas. The aim of risk management is to create value for shareholders by supporting the Bank in achieving its goals and objectives, and ultimately ensuring that the risks are commensurate with the rewards.

The Bank has formed both the Assets & Liabilities Committee (ALCO) and the Credit Committee, which are entrusted with the task of formulating the Bank's risk management policies in their respective domains.

The Bank has also established an independent Risk Management function as the Bank’s second line of defence, which operates independently of the Bank’s operations. This function reports directly to the Risk Committee and is represented during meetings of these committees. Its responsibility is to ensure that the Bank’s Risk Management Policy, Risk Appetite Statement, and any other guidelines are supportive of the Bank’s objectives. Furthermore, it seeks to identify any unmitigated risks and formulates suitable action plans for their treatment. By providing oversight of policies, limits, procedures, processes, and systems, as well as using risk measurement, monitoring, controlling, and reporting tools and methods, the function monitors the high-level principles that guide staff in their daily management of risk.

The Bank considers risk management a core competency that helps produce consistently high returns for its various stakeholders. The Bank’s business involves taking on risks in a targeted manner and managing them professionally. The Bank aims to manage all major types of risk by applying methods that meet best practice. The Bank considers it important to have a clear distribution of responsibilities within risk management. One of the main tasks of the Bank’s executive management is to set the framework for this area. The core functions of the Bank’s risk management are to identify all key risks for the Bank, measure these risks, manage the risk positions and determine capital allocations. The Bank regularly reviews its risk management policies and systems to reflect changes in markets, products and best market practice.

1.3 Key risk components

The Bank’s Board of Directors is empowered to set out the overall risk policies and limits for all material risk types. The Board also decides on the general principles for managing and monitoring risks.

1. Risk management - continued

1.3 Key risk components - continued

To ensure coherence between the Bank's strategic considerations regarding risk-taking and day-to-day decisions, from time to time, the Bank establishes risk appetite as a strategic tool. Risk appetite is the maximum risk that the Bank is willing to assume to meet business targets. The Bank's risk appetite is set in a process based on a thorough analysis of its current risk profile. The Bank identifies a number of key risk components and for each, determines a target that represents the Bank's perception of the component in question.

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

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

Market risk: Market risk is the risk of reductions in earnings and/or asset values arising from unexpected changes in financial prices, including interest rates, exchange rates and equity prices. It is managed by a variety of different techniques.

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

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

2. Credit risk

Credit risk is the risk of suffering financial loss, should any of the Bank's customers, clients or market counterparties fail to fulfil their contractual obligations to the Bank. Credit risk arises from deposits with other banks and on its securities portfolio.

The Credit Committee and Board of Directors are responsible for approving all credit facilities, acquisitions of securities and placements of deposits with banks. In accordance with policies set by the Board, decisions are based on the Bank's insight into the counterparty's financial position which is regularly monitored and reported to the Board.

In order to minimise the credit risk undertaken, counterparty credit limits are defined, which consider a counterparty's creditworthiness. In order to examine a counterparty's creditworthiness, country risk, quantitative and qualitative characteristics, as well as the industry sector in which the counterparty operates are considered.

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

2. Credit risk - continued

Country risk

The Bank runs the risk of loss of funds due to the possible political, economic and other events in a particular country where funds have been placed or invested with several counterparties. Countries are assessed according to their size, economic data and prospects and their credit ratings from international rating agencies. Existing country credit risk exposures are monitored and reviewed periodically.

Exposures analysed by location

	Europe EUR	**Total EUR**
Central Government	50,869,548	50,869,548
Institutions	10,227,227	10,227,227
Corporates	436,460,180	436,460,180
Other assets	11,165,532	11,165,532
	508,722,487	**508,722,487**

Exposures analysed by residual maturity

	On demand or less than three months	**Within one year but over three months**	**Within five years but over one year**	**More than five years**	**No maturity**	**Gross carrying amount/ Fair value**
	€	**€**	**€**	**€**	**€**	**€**
As at 31 December 2023						
Financial assets						
Balances with Central Bank of Malta	45,517,151	-	-	-	5,352,397	50,869,548
Loans and advances to banks	10,227,227	-	-	-	-	10,227,227
Loans and advances to customers	7,901,027	24,325,483	159,490,553	150,609,683	-	342,326,746
Financial investments	1,295,903	6,757,496	59,162,707	26,917,328	-	94,133,434
Other assets	5,130,949	4,110,759	-	-	1,923,824	11,165,532
	70,072,257	**35,193,738**	**218,653,260**	**177,527,01**	**7,276,221**	**508,722,487**

	On demand or less than three months	Within one year but over three months	Within five years but over one year	More than five years	No maturity	Gross carrying amount/ Fair value
	€	€	€	€	€	€
As at 31 December 2022						
Financial assets						
Balances with Central Bank of Malta	32,615,923	-	-	-	2,163,884	34,779,807
Loans and advances to banks	2,044,281	-	-	-	-	2,044,281
Loans and advances to customers	2,186,118	15,230,290	96,149,495	95,871,119	-	209,437,022
Financial investments	4,564,182	58,412,636	-	30,257,410	-	93,234,228
Derivative financial instruments	681,313	2,302,590	-	-	429,781	3,413,684
Other assets	32,615,923	-	-	-	2,163,884	34,779,807
	42,091,817	**75,945,516**	**96,149,495**	**126,128,529**	**2,593,665**	**342,909,022**

2. Credit risk - continued

Asset quality

The Bank assigns risk weights to the credit risk of its assets in accordance with the rating assigned by Fitch, Moody's and S&P, all of which are MFSA eligible External Credit Assessment Institutions (ECAIs), in accordance with article 3.9 of Appendix 2 – Section 1.4 Credit Risk Standardised Approach – BR 04.

The credit quality of the securities as determined by the nominated ECAIs is as follows:

	2023	2022
	€	€
AAA	5,258,202	-
AA	273,445	261,925
AA+	3,074,701	-
A	1,494,660	433,800
A-	1,769,854	-
BBB+	-	-
BBB	6,693,937	15,857,347
BBB-	24,369,752	4,210,088
BB-	3,235,226	-
BB+	13,196,054	17,227,927
BB	1,505,885	20,851,489
B+	-	1,928,885
CCC	1,930,580	-
Unrated	31,331,138	32,462,767
	94,133,434	**93,234,228**

3. Market risk

The Bank assumes exposure to market risk, which refers to the possibility that the fair value or future cash flows of a financial instrument may vary due to fluctuations in market prices. Market risks emerge from open positions in interest rate, currency, and equity products, all of which are subject to overall and specific market movements, as well as changes in the level of market rate or price volatility, including but not limited to interest rates, credit spreads, foreign exchange rates, and equity prices.

The Bank does not operate a Trading Book and hence this is limited to the following risks:

- Interest rate risk, which is the risk of losses through changes in interest rates;
- Currency risk, which is the risk of losses on the Bank's positions in foreign currency through changes in exchange rates; and
- Price risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

3.1 Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or at different amounts. The Bank places deposits with Banks at both fixed and floating rates and for varying maturity periods. This risk is managed through the matching of the interest resetting dates on assets and liabilities as much as it is practicable. However, the Bank seeks to manage its net interest spread, after considering the cost of capital by investing funds in a **3.**

3. **Market risk** - continued

3.1 **Interest rate risk** – continued

portfolio of securities with a longer tenure than the liabilities (therefore carrying a negative maturity gap position).

At the end of the reporting period the interest rate profile of the Bank's interest bearing financial instruments is as follows:

	2023		2022	
	Variable	**Fixed**	Variable	Fixed
	€	**€**	€	€
As at 31 December 2023				
Financial assets				
Balances with Central Bank of Malta	**38,735,589**	**12,133,959**	34,779,807	-
Loans and advances to banks	**10,227,227**	**-**	2,044,281	-
Loans and advances to customers	**285,102,787**	**57,223,959**	177,933,441	31,503,580
Financial investments	**29,466,823**	**64,666,611**	27,473,413	65,760,815
	363,532,426	**134,024,529**	**242,230,942**	**97,264,395**
Financial liabilities				
Amounts owed to customers	96,027,905	308,307,736	64,257,580	199,827,714
Amounts owed to banks and other institutions	17,000,000	8,400,000	10,000,000	17,428,369
Subordinated liabilities	4,853,584	-	-	-
	117,881,489	**316,707,736**	**74,257,580**	**217,256,083**
Exposure	**245,650,937**	**(182,683,207)**	**167,973,362**	**(119,991,688)**

The following table sets out the gross carrying amount, or fair value, by reference to the earlier of the next contractual interest rate repricing date and maturity:

	Less than three months	**Within one year but over three months**	**Within five years but over one year**	**More than five years**	**Gross carrying amount/ Fair value**
	€	**€**	**€**	**€**	**€**
As at 31 December 2023					
Financial assets					
Balances with Central Bank of Malta	50,869,54	-	-	-	50,869,548
Loans and advances to banks	10,227,22	-	-	-	10,227,227
Loans and advances to customers	285,102,7	9,955,567	39,683,71	7,584,681	342,326,746
Financial investments	30,762,72	-	46,121,66	17,249,04	94,133,434
	76,962,288	**9,955,567**	**85,805,37**	**24,833,73**	**497,556,955**
Financial liabilities					
Amounts owed to customers	347,564,9	55,456,870	1,313,845	-	404,335,641
Amounts owed to banks and other	25,400,00	-	-	-	25,400,000
Subordinated liabilities	4,853,584	-	-	-	4,853,584
	77,818,510	**55,456,870**	**1,313,845**	**-**	**434,589,225**
Interest repricing gap	**(856,222)**	**(45,501,303)**	**84,491,52**	**24,833,730**	

3. **Market risk** - continued

3.1 **Interest rate risk** - continued

	On demand or less than three months	**Within one year but over three months**	**Within five years but over one year**	**More than five years**	**Gross carrying amount/ Fair value**
	€	**€**	**€**	**€**	**€**
As at 31 December 2022					
Financial assets					
Balances with Central Bank of Malta	34,779,807	-	-	-	34,779,807
Loans and advances to banks	2,044,281	-	-	-	2,044,281
Loans and advances to customers	177,933,442	10,010,241	20,612,103	881,236	209,437,022
Financial investments	26,654,320	-	28,856,150	37,723,758	93,234,228
	241,411,850	**10,010,241**	**49,468,253**	**38,604,994**	**339,495,338**
Financial liabilities					
Amounts owed to customers	137,853,324	120,983,271	5,248,699	-	264,085,294
Amounts owed to institutions	27,428,369	-	-	-	27,428,369
	165,281,693	**120,983,271**	**5,248,699**	**-**	**291,513,663**
Interest repricing gap	76,130,156	(110,973,030)	44,219,554	38,604,994	

3.2 Currency risk

Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Board of Directors sets limits on the level of exposure by currency and in total.

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. Foreign exchange risk is the risk to earnings and value caused by a change in foreign exchange rates. Foreign exchange risk arises when financial assets or liabilities are denominated in currencies that are different from the Bank's functional currency.

The Bank manages its currency risk on an ongoing basis by ensuring that foreign currency liabilities are utilised to fund assets denominated in the same foreign currency thereby matching asset and liability positions as much as is practicable. When it is not possible to match the asset and liability currency positions, the Bank hedges its open foreign exchange exposures by entering into forward foreign exchange contracts or currency swaps.

3. **Market risk** - continued

3.2 **Currency risk** - continued

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

	EUR currency	CZK currency	Other currency	Total
	€	€	€	€
As at 31 December 2023				
Financial assets				
Balances with Central Bank of Malta	37,677,815	13,191,733	-	50,869,548
Loans and advances to banks	3,503,635	6,511,313	212,279	10,227,227
Loans and advances to customers	333,831,223	8,495,523	-	342,326,746
Financial investments	64,371,112	24,230,675	6,707,528	95,309,315
Accrued interest receivable	640,621	395,934	218,089	1,254,644
	440,024,406	**52,825,178**	**7,137,896**	**499,987,480**
Financial liabilities				
Amounts owed to customers	367,090,661	37,209,018	35,962	404,335,641
Amounts owed to institutions	25,400,000	-	-	25,400,000
Accrued interest payable	2,895,221	-	600	2,895,821
Subordinated liabilities	156,467	52,029	-	208,496
	395,542,349	**42,114,631**	**36,562**	**437,693,542**
Net on-balance sheet financial position		10,710,547	7,101,334	
Notional of derivative financial instruments		1,201,007	(6,172,654)	
Residual exposure		**11,911,554**	**928,680**	

	EUR currency	CZK currency	GBP currency	Total
	€	€	€	€
As at 31 December 2022				
Financial assets				
Balances with Central Bank of Malta	34,779,807	-	-	34,779,807
Loans and advances to banks	1,225,179	564,330	254,772	2,044,281
Loans and advances to customers	209,405,044	31,978	-	209,437,022
Financial investments	64,497,547	28,422,407	314,274	93,234,228
Accrued interest receivable	392,793	257,452	2,384	652,629
	310,300,370	**29,276,167**	**571,430**	**340,147,967**
Financial liabilities				
Amounts owed to customers	259,828,761	4,073,790	182,743	264,085,294
Amounts owed to institutions	10,000,000	17,428,369	-	27,428,369
Accrued interest payable	552,045	127,761	13,443	693,249
	270,380,806	**21,629,920**	**196,186**	**292,206,912**
Net on-balance sheet financial position		**7,646,247**	**375,244**	

4. Liquidity risk

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfil commitments.

The risk of liquidity arises when the Bank is unable to sell a financial asset swiftly at a value close to its fair value. The Bank is susceptible to daily requests on its available cash resources from loan drawdowns, maturing term deposits, overnight deposits, current and call deposits, and guarantees.

The Bank's goal for liquidity and funding management is to guarantee that all anticipated funding commitments and deposit withdrawals are met on time. It aims to maintain a diversified and stable funding base that allows it to react rapidly and smoothly to unforeseen liquidity demands.

The Bank manages this risk by matching its assets and liabilities with respect to maturities as much as possible. Nevertheless, the Bank must manage its net interest spread by investing funds in a portfolio of assets with longer terms than the liabilities funding them.

The Bank manages this risk, by maintaining a strong base of shareholders' capital considering the stages of its operations. To mitigate exposures arising in this respect, the Bank arranged a credit line with another Credit Institution and pledging its loan portfolio as collateral. This credit line remains unused, contributing to a well-balanced and robust liquidity position.

The Bank maintains internal liquidity buffers established by ALCO, which consist of cash and financial assets eligible for collateral against borrowing from the European Central Bank. The Board sets parameters to ensure that maturing funds are always available to meet unexpected cash demand, allowing for a certain degree of asset and liability mismatch in line with the previously mentioned stance. Although unmatched positions may enhance profitability, they also increase risks. ALCO focuses on managing the entity's market and funding liquidity risks, with ongoing oversight of forecast and actual cash flows and monitoring of fund availability to meet financial instrument commitments. The Bank's Executive Team and Treasury Function provide operational support to ALCO in this regard.

ALCO conducts a monthly review of the Bank's Liquidity Gap analysis. The Bank's liquidity management process involves monitoring future cash flows to ensure that funding needs can be met on a daily basis, and that funds are replenished as they mature or are borrowed by customers. This process requires a structured and ongoing analysis of the contractual maturity of financial liabilities and the expected collection date of financial assets.

All liquidity policies and procedures are subject to review and approval by the Board of Directors.

The Bank uses a number of key liquidity measures to monitor its liquidity risk, namely the ratio of liquid assets to deposit liabilities, the maturity ladder which comprises projected cash flows, the Liquidity Coverage Ratio ('LCR'), the Net Stable Funding Ratio ('NSFR') and a CALL report which is a six monthly forecast based on projections and contains information on the Bank's financial health.

As at 31 December 2023, the Bank's liquidity ratios were above the regulatory liquidity ratios,

4. **Liquidity risk** - continued

The following table discloses financial assets and liabilities at the end of the reporting period by remaining period to maturity.

	On demand or less than three months	Within one year but over three months	Within five years but over one year	More than five years	No maturity	Gross carrying amount/ Fair value
	€	€	€	€	€	€
As at 31 December 2023						
Financial assets						
Balances with Central Bank of Malta	45,517,151	-	-	-	5,352,397	50,869,548
Loans and advances to banks	10,227,227	-	-	-	-	10,227,227
Loans and advances to customers	7,901,027	24,325,483	159,490,553	150,609,683	-	342,326,746
Financial investments	1,295,903	6,757,496	59,162,707	26,917,328	-	94,133,434
Other assets	5,130,949	4,110,759	-	-	1,923,824	11,165,532
	70,072,257	**35,193,738**	**218,653,260**	**177,527,011**	**7,276,221**	**508,722,487**
Financial liabilities						
Amounts owed to customers	347,564,926	55,456,870	1,313,845	-	-	404,335,641
Amounts owed to institutions	25,400,000	-	-	-	-	25,400,000
Other liabilities	3,831,700	-	-	-	2,100,000	5,931,701
Subordinated liabilities	-	-	-	4,853,584	-	4,853,584
	376,796,626	**55,456,870**	**1,313,845**	**4,853,584**	**2,100,000**	**440,520,926**
Maturity gap	**(306,724,370**	**(20,263,132)**	**217,339,415**	**172,673,427**		
Cumulative gap	**(306,724,370**	**(326,987,502)**	**(109,648,087**	**63,025,340**		

4. Liquidity risk - continued

	On demand or less than three months	Within one year but over three months	Within five years but over one year	More than five years	No maturity	Gross carrying amount/ Fair value
	€	€	€	€	€	€
As at 31 December 2022						
Financial assets						
Balances with Central Bank of Malta	32,615,923	-	-	-	2,163,884	34,779,807
Loans and advances to banks	2,044,281	-	-	-	-	2,044,281
Loans and advances to customers	2,186,118	15,230,290	96,149,495	95,871,119	-	209,437,022
Financial investments	4,564,182	58,412,636	-	30,257,410	-	93,234,228
Other assets	681,313	2,302,590	-	-	429,781	3,413,684
	42,091,817	**75,945,516**	**96,149,495**	**126,128,529**	**2,593,665**	**342,909,022**
Financial liabilities						
Amounts owed to customers	137,853,324	120,983,271	5,248,699	-	-	264,085,294
Amounts owed to institutions	27,428,369	-	-	-	-	27,428,369
Other liabilities	1,743,840	-	-	-	4,000,000	5,743,840
	167,025,533	**120,983,271**	**5,248,699**	**-**	**4,000,000**	**297,257,503**
Maturity gap	(124,933,716)	(45,037,755)	90,900,796	126,128,529		
Cumulative gap	(124,933,716)	(169,971,471)	(79,070,675)	47,057,854		

5. Operational risk

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

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

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

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

The Bank is subject to externally imposed capital requirements only in respect of the Bank's activities as a credit institution.

6. ESG Risks

In today's dynamic financial landscape, Environmental, Social, and Governance (ESG) considerations have emerged as pivotal factors shaping the strategies of banks worldwide. As awareness of pressing global issues like climate change, social inequality, and ethical corporate behaviour grows, so too does the demand for sustainable financial products from investors. The reputation and business success of financial institutions are increasingly tied to their commitment to sustainability and responsible corporate conduct. ESG principles have thus become integral to navigating the evolving market environment and fostering long-term value creation for banks. Sustainability is rapidly gaining importance and the increasing awareness of issues such as climate change, social inequality, and corporate misconduct is changing the market environment. Investors across the globe are showing increased demand for sustainable financial products. Sustainability and corporate conduct are influencing the reputation and business success of financial institutions.

In late 2022 a Dear CEO letter was communicated whereby the MFSA outlined its expectations for the Bank with regards to Climate Related Risks and our preparedness.

As a result, the MFSA has established the following the below are the main four expectations that credit institutions under their supervision are to comply with in 2023have been requested:

1. The MFSA expects to see clear leadership and momentum from the Board in addressing climate and environmental risks. This includes active engagement from the Board, integration of climate and environmental risk considerations into approved documents and providing designated training to Board members.
2. Banks should include climate and environmental (C&E) risk limits in their Risk Appetite Statements and have data to measure their performance. They should also document how these limits were identified, how key performance indicators (KPIs) will be monitored, and how they will be incorporated into escalation policies and risk reporting.
3. Banks should determine and provide evidence of how they communicate C&E related internal policies to their first line staff and the process of implementing these policies.
4. The MFSA expects banks to develop plans for client engagement that outline how they intend to engage with clients on climate and environmental risk. It is crucial for first-line business managers to incorporate climate assessments into their discussions with clients in order to encourage the provision of relevant data in the future.

In 2023, the Bank embarked on its business environment risk assessment, with a proactive stance from the risk department signalling a firm commitment to addressing Environmental, Social, and Governance (ESG) considerations. Recognizing the complexity of the task, the Bank enlisted the expertise of PricewaterhouseCoopers (PwC), a reputable external service provider, to conduct a thorough evaluation of climate-related and environmental risks within its lending portfolio.

Tailored to the unique business model of FCM Bank (‘FCM’), the assessment focused on the period ending 31 March 2023, aiming to pinpoint and evaluate potential risks inherent in the Bank's lending activities. The approach consisted of four key steps:

Portfolio Segmentation: The Bank primarily engages in real-estate lending in Malta, prompting a focused assessment of climate and environmental (C&E) risks relevant to this sector. To evaluate its exposure effectively, the real-estate lending portfolio was segmented into homogeneous groups based on repayment sources, loan purposes, and property types.

Research Analysis: A comprehensive research analysis was conducted to identify C&E risk drivers pertinent to FCM Bank's lending portfolio, particularly focusing on physical and transition risks. For physical risks, attention was given to potential events in Malta such as tsunamis, floods, and rising sea levels. Transition risks were assessed in light of policies like carbon taxation, energy standards, and the Carbon Border Adjustment Mechanism (CBAM).

6. **ESG Risks** - continued

Materiality Assessment: Utilizing data from the research analysis and portfolio characteristics, the Bank assessed the potential impact of identified risk drivers on its risk profile and operations. This assessment considered factors such as financial losses, business disruptions, legal claims, and reputational damages to gauge materiality.

C&E Risks Response: Based on the findings, the Bank is formulating a response plan categorized into:

Risk Appetite and Policy Change: Establishing the risk appetite for C&E risks and updating internal policies accordingly.
Customer Engagement: Determining the level of interaction with customers to enhance materiality assessment and ensure alignment with the Bank's C&E risk appetite and policies.

By systematically addressing these steps, the Bank aims to integrate C&E risks into its strategic and risk management framework effectively, fostering resilience and sustainability in its operations.

7. Capital management

7.1 Capital adequacy

The Bank adheres to the regulations outlined in the Capital Requirements Directive (CRD) and the Capital Requirements Regulations (CRR) for its Pillar 1 capital requirements. The bank is in conformity with these regulations. Other material risks are also allocated capital as part of the Internal Capital Adequacy Process (ICAAP) embedded in the Pillar II process. This process helps to measure with greater risk sensitivity the amount of regulatory capital which the Bank requires to cover risks assumed in the course of its business, including risks not covered in Pillar I.

The following is an analysis of the Bank's capital base in accordance with the CRD's requirements.

Minimum capital requirements are computed for credit, market and operational risks. The MFSA requires a bank to maintain a ratio of total regulatory capital to risk-weighted assets and instruments (the capital requirements ratio) at or above the prescribed minimum of 8%. The capital requirements ratio expresses own funds as a proportion of risk-weighted assets and off-balance sheet items in relation to credit risk together with notional risk-weighted assets in respect of operational risk and market risk.

The risk-weighted assets are measured by means of a hierarchy of risk weights classified according to the nature of, and reflecting an estimate of credit, market and other risks associated with each asset and counterparty, taking into account any eligible collateral or guarantees. A similar treatment is adopted for off-balance sheet exposures, with some adjustments to reflect the more contingent nature of the potential losses. Risk-weighted assets are measured using the 'standardised approach' for credit risk with risk weights being assigned to assets and off-balance sheet items according to their asset class and credit assessment. For the determination of credit assessments, independent rating agencies are nominated as required.

Total risk-weighted assets are determined by multiplying the capital requirements for market risk and operational risk by 12.5 (i.e. the reciprocal of the minimum capital ratio of 8 per cent) and adding the resulting figures to the sum of risk-weighted assets for credit risk.

7. Capital management – continued

7.1 Capital adequacy – continued

	Carrying amount €	Risk weighted amount €	Capital requirement €
Central governments	64,108,221	-	-
Institutions	11,009,227	2,827,445	226,196
Corporates	422,558,913	266,704,668	27,868,696
Other items	14,266,713	8,242,558	659,405
	511,943,074	277,774,671	28,754,297
Off-balance sheet	146,166,162	139,705,773	11,176,462
Total credit risk		417,480,444	39,930,759
Operational risk		15,402,745	1,232,220
Total		**432,883,189**	**41,162,979**
Own funds			**75,375,649**
Capital adequacy ratio			**17,4%**

7. Capital management - continued

7.1 Capital adequacy - continued

EU CC1 - Composition of regulatory own funds

		(a)
		Amounts
	Common Equity Tier 1 (CET1) capital: instruments and reserves	
1	Capital instruments and the related share premium accounts	52,250,000
	of which: Instrument type 1	52,250,000
	of which: Instrument type 2	
	of which: Instrument type 3	
2	Retained earnings	2,863,483
3	Accumulated other comprehensive income (and other reserves)	-1,913,720
EU-3a	Funds for general banking risk	
4	Amount of qualifying items referred to in Article 484 (3) CRR and the related share premium accounts subject to phase out from CET1	
5	Minority interests (amount allowed in consolidated CET1)	
EU-5a	Independently reviewed interim profits net of any foreseeable charge or dividend	
6	**Common Equity Tier 1 (CET1) capital before regulatory adjustments**	**53,199,763**
	Common Equity Tier 1 (CET1) capital: regulatory adjustments	
7	Additional value adjustments (negative amount)	
8	Intangible assets (net of related tax liability) (negative amount)	-96,259
9	Empty set in the EU	
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) CRR are met) (negative amount)	
11	Fair value reserves related to gains or losses on cash flow hedges of financial instruments that are not valued at fair value	
12	Negative amounts resulting from the calculation of expected loss amounts	
13	Any increase in equity that results from securitised assets (negative amount)	
14	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	
15	Defined-benefit pension fund assets (negative amount)	
16	Direct, indirect and synthetic holdings by an institution of own CET1 instruments (negative amount)	
17	Direct, indirect and synthetic holdings of the CET 1 instruments of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution (negative amount)	
18	Direct, indirect and synthetic holdings by the institution of the CET1 instruments of financial sector entities where the institution does not have a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)	
19	Direct, indirect and synthetic holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)	
20	Empty set in the EU	
EU-20a	Exposure amount of the following items which qualify for a RW of 1250%, where the institution opts for the deduction alternative	
EU-20b	of which: qualifying holdings outside the financial sector (negative amount)	
EU-20c	of which: securitisation positions (negative amount)	
EU-20d	of which: free deliveries (negative amount)	
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability where the conditions in Article 38 (3) CRR are met) (negative amount)	
22	Amount exceeding the 17,65% threshold (negative amount)	
23	of which: direct, indirect and synthetic holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities	
24	Empty set in the EU	
25	of which: deferred tax assets arising from temporary differences	

EU-25a	Losses for the current financial year (negative amount)	
EU-25b	Foreseeable tax charges relating to CET1 items except where the institution suitably adjusts the amount of CET1 items insofar as such tax charges reduce the amount up to which those items may be used to cover risks or losses (negative amount)	
26	Empty set in the EU	
27	Qualifying AT1 deductions that exceed the AT1 items of the institution (negative amount)	
27a	Other regulatory adjustments to CET1 capital *(including IFRS 9 transitional adjustments when relevant)*	
28	**Total regulatory adjustments to Common Equity Tier 1 (CET1)**	
29	**Common Equity Tier 1 (CET1) capital**	**53,103,504**
	Additional Tier 1 (AT1) capital: instruments	
30	Capital instruments and the related share premium accounts	17,492,939
31	of which: classified as equity under applicable accounting standards	17,492,939
32	of which: classified as liabilities under applicable accounting standards	
33	Amount of qualifying items referred to in Article 484 (4) CRR and the related share premium accounts subject to phase out from AT1 as described in Article 486(3) CRR	
EU-33a	Amount of qualifying items referred to in Article 494a(1) CRR subject to phase out from AT1	
EU-33b	Amount of qualifying items referred to in Article 494b(1) CRR subject to phase out from AT1	
34	Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interests not included in row 5) issued by subsidiaries and held by third parties	
35	of which: instruments issued by subsidiaries subject to phase out	
36	**Additional Tier 1 (AT1) capital before regulatory adjustments**	**17,492,939**
	Additional Tier 1 (AT1) capital: regulatory adjustments	
37	Direct, indirect and synthetic holdings by an institution of own AT1 instruments (negative amount)	
38	Direct, indirect and synthetic holdings of the AT1 instruments of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution (negative amount)	
39	Direct, indirect and synthetic holdings of the AT1 instruments of financial sector entities where the institution does not have a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)	
40	Direct, indirect and synthetic holdings by the institution of the AT1 instruments of financial sector entities where the institution has a significant investment in those entities (net of eligible short positions) (negative amount)	
41	Empty set in the EU	
42	Qualifying T2 deductions that exceed the T2 items of the institution (negative amount)	
42a	Other regulatory adjustments to AT1 capital	
43	**Total regulatory adjustments to Additional Tier 1 (AT1) capital**	
44	**Additional Tier 1 (AT1) capital**	**17,492,939**
45	**Tier 1 capital (T1 = CET1 + AT1)**	**70,596,433**
	Tier 2 (T2) capital: instruments	
46	Capital instruments and the related share premium accounts	4,853,584
47	Amount of qualifying items referred to in Article 484 (5) CRR and the related share premium accounts subject to phase out from T2 as described in Article 486(4) CRR	
EU-47a	Amount of qualifying items referred to in Article 494a (2) CRR subject to phase out from T2	
EU-47b	Amount of qualifying items referred to in Article 494b (2) CRR subject to phase out from T2	
48	Qualifying own funds instruments included in consolidated T2 capital (including minority interests and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties	
49	of which: instruments issued by subsidiaries subject to phase out	
50	Credit risk adjustments	
51	**Tier 2 (T2) capital before regulatory adjustments**	**4,853,584**
	Tier 2 (T2) capital: regulatory adjustments	
52	Direct, indirect and synthetic holdings by an institution of own T2 instruments and subordinated loans (negative amount)	
53	Direct, indirect and synthetic goldings of the T2 instruments and subordinated loans of financial sector entities where those entities have reciprocal cross holdings with the institution designed to inflate artificially the own funds of the institution (negative amount)	
54	Direct, indirect and synthetic holdings of the T2 instruments and subordinated loans of financial sector entities where the institution does not have a significant investment in those entities (amount above 10% threshold and net of eligible short positions) (negative amount)	
54a	Empty set in the EU	

55	Direct, indirect and synthetic holdings by the institution of the T2 instruments and subordinated loans of financial sector entities where the institution has a significant investment in those entities (net of eligible short positions) (negative amount)	
56	Empty set in the EU	
EU-56a	Qualifying eligible liabilities deductions that exceed the eligible liabilities items of the institution (negative amount)	
EU-56b	Other regulatory adjustments to T2 capital	
57	**Total regulatory adjustments to Tier 2 (T2) capital**	
58	**Tier 2 (T2) capital**	**4,853,584**
59	**Total capital (TC = T1 + T2)**	**75,450,027**
60	**Total Risk exposure amount**	**432,883,189**
	Capital ratios and buffers	
61	Common Equity Tier 1 (as a percentage of total risk exposure amount)	12,30%
62	Tier 1 (as a percentage of total risk exposure amount)	16,3%
63	Total capital (as a percentage of total risk exposure amount)	17,4%
64	Institution CET1 overall capital requirement (CET1 requirement in accordance with Article 92 (1) CRR, plus additional CET1 requirement which the institution is required to hold in accordance with point (a) of Article 104(1) CRD, plus combined buffer requirement in accordance with Article 128(6) CRD) expressed as a percentage of risk exposure amount)	9,5%
65	of which: capital conservation buffer requirement	10,822,080
66	of which: countercyclical buffer requirement	1,152,519
67	of which: systemic risk buffer requirement	57,577
EU-67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	
68	**Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)**	
69	[non relevant in EU regulation]	
70	[non relevant in EU regulation]	
71	[non relevant in EU regulation]	
Amounts below the thresholds for deduction (before risk weighting)		
72	Direct and indirect holdings of own funds and eligible liabilities of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	
73	Direct and indirect holdings by the institution of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 17.65% thresholds and net of eligible short positions)	
74	Empty set in the EU	
75	Deferred tax assets arising from temporary differences (amount below 17,65% threshold, net of related tax liability where the conditions in Article 38 (3) CRR are met)	
Applicable caps on the inclusion of provisions in Tier 2		
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	
78	Credit risk adjustments included in T2 in respect of exposures subject to internal ratings-based approach (prior to the application of the cap)	
79	Cap for inclusion of credit risk adjustments in T2 under internal ratings-based approach	
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2014 and 1 Jan 2022)		
80	Current cap on CET1 instruments subject to phase out arrangements	
81	Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	
82	Current cap on AT1 instruments subject to phase out arrangements	
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	
84	Current cap on T2 instruments subject to phase out arrangements	
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	

7. **Capital management** - continued

7.1 **Capital adequacy** - continued

In anticipation of the forthcoming CRR3 regulation, the Bank is proactively addressing the impending changes to ensure compliance and continued financial stability. The CRR3 introduces significant amendments aimed at enhancing the regulatory framework governing banking institutions. Notably, the inclusion of new terms such as Acquisition, Development, and Construction (ADC) loans, Income Producing Real Estate (IPRE), and Exposure to Value (ETV) assets necessitates a thorough understanding and adaptation within the Bank's risk management practices.
To navigate these alterations effectively, the Bank has initiated a comprehensive gap analysis. This process aims to identify any potential shifts in Risk-Weighted Assets (RWAs) resulting from the introduction of these new terms. By undertaking this analysis, the Bank ensures that appropriate levels of capital are maintained to support its operations and regulatory requirements. Through diligent preparation and proactive measures, the Bank remains steadfast in its commitment to upholding regulatory compliance and safeguarding its financial resilience amidst evolving regulatory landscapes.

7.2 **Internal capital adequacy assessment process (ICAAP)**

The Bank developed a comprehensive Internal Capital Adequacy Assessment Process (“ICAAP”), as part of its 2023 plan to enhance its risk management process, in accordance with Banking Rule 12 ‘The Supervisory Review Process’ (BR12) and the recommendations proposed by the MFSA in the results of the Supervisory and Review Process (SREP). As part of this process, the Bank is required to assess its overall capital adequacy in relation to risk profile and a strategy for maintaining capital levels.

The purpose of the ICAAP is to formalise the process by which the Bank performs ongoing assessment of its risks, mitigates those risks and determines how much current and future capital is necessary having considered other mitigating factors.

The ICAAP has therefore been adopted by both the Board of Directors and the Bank’s senior management to ensure that there is adequate identification, measurement and monitoring of the Bank’s risks and that adequate internal capital is held by the Bank in relation to its risk profile. Furthermore, the Bank has utilised this ICAAP to assess its current risk management practices and to determine those practices which need to be developed further.

For this ICAAP, the Bank adopted a minimum capital requirement approach, using the audited figures as at 31 December 2023 as the benchmark year, which is based on Pillar I capital requirements together with the assessment of extra capital proportionate to Pillar II risks and supplementary stress testing to assess the impact of a possible prolonged economic recession on the Bank.

The ICAAP process was led by the Bank’s Risk Department and was challenged by the Bank’s Board of Directors to ensure that the proposed strategy is in line with the Bank’s risk profile. The final document was approved by the Bank’s Board of Directors in April 2023 and presented to the MFSA. The results show that the Bank is comfortably meeting its capital and liquidity targets over the regulatory minimum even in times of stress.

8 Remuneration Policy

The Bank's Remuneration Policy is based on the following principles:

- Clarity and transparency for all stakeholders.
- Adherence to the Bank's long-term objectives with reference to the relevant level of risk involved in attaining these goals.
- Maintaining a reasonable proportion between the fixed and variable part of remuneration package.
- The review of the annual staff remuneration considers the Bank's results, performance, as well as local market trends in the financial sector and individual performance in view of the risk level involved in the long term.
- Market data is considered and target remuneration brackets per job position are set in view to level of expertise, years in the position, attraction of talent and high performers.
- European Banking Authority Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013.

Total remuneration payable to senior management, composed of the CEO and four other beneficiaries, in 2023 was €445,607, all of which was fixed.

The Bank has appointed a Remuneration Committee whose objective is to ensure that all remuneration, including benefits and variable remuneration, follows legal requirements and market rates. All members appointed on the Remuneration Committee are not management members except for the CEO, whose membership is ex-officio. The Remuneration Committee meets at least twice a year, and the minutes are formally kept by the Company Secretary. The Remuneration Committee undertakes periodic studies into compensation market rates, including variable rates, and other benefits. All variable compensation for senior management is submitted to be authorised by the Remuneration Committee. The Remuneration Policy is subject to the Remuneration Committee's scrutiny and authorisation.

The Bank will determine the employee's remuneration and benefits by reference to market rates for specific roles and the Bank's own needs at a particular time. Remuneration for senior management staff is recommended to the Remuneration Committee for authorisation. The Bank incentive schemes are tied to the performance evaluation system and will always be subject to the Remuneration Committee's approval on the basis of a structured and measured approach, which must be tied to the adoption of sound operating procedures and risk practices. The Bank will not implement incentive schemes which will encourage its management and employees to commit the Bank to take on risks which in the view of the Board of Directors are not in line with the risk profile of the Bank. The Bank will also not implement incentive schemes which will constrain or endanger its financial position or capital base.

- Variable remuneration will not encourage excessive risk-taking beyond the tolerated risk level of the Bank.
- Variable remuneration will be in line with business strategy, long-term bank objectives and the avoidance of conflicts of interest.
- The implementation of basic remuneration policy (salaries) is subject to the Remuneration Committee's authorisation both at contracting stage and at periodic increase stage. The implementation of the variable remuneration policy is subject to the Remuneration Committee's scrutiny and authorisation both at initial stages, when drawing up performance targets and measures, and at recommendation stage, prior to decisions made on variable remuneration levels.

8 Remuneration Policy – continued

- Staff in control functions are independent from the business units they oversee and are remunerated according to independent market rates and according to the targets and measures included in their performance evaluation forms.

Variable remuneration shall be subject to the Bank's overall performance, to the achievement of targets previously established, which targets include behavioural objectives and to the following considerations:

- The Bank does not offer guaranteed variable remuneration unless the latter is part of the initial contracting process, which would only happen as a one-off factor during the first year of employment.
- The total variable remuneration value shall not in any manner constrain the Bank's capital base.
- The total level of variable remuneration shall not exceed 25% of the level of basic salary, unless specifically authorised by the Board of Directors in exceptional circumstances. In the case of the latter, such a decision would not constrain the Bank's capital base and would not be higher than 50% of basic salary.
- Variable remuneration of the most senior Bank officers may be set in a multi-year framework which will take into consideration the Bank's longer-term performance and its underlying business cycle. This may include variable remuneration being settled over a period of years corresponding to the Bank's business cycle.

EU REM1 – Remuneration awarded for the financial year

	MB Supervisory functions	**MB Management functions**	**Other Senior Management**	**Other identified staff**
Number of identified staff	4.80	7.40	0.20	0.00
Total fixed remuneration	255,461	692,100	14,916	-
of which: cash-based	255,461	607,719	14,916	-
of which: shares or equivalent ownership interests	-	0	-	-
of which: share-linked instruments or equivalent non-cash	-	0	-	-
of which other instruments	-	0	-	-
of which: other forms	-	84,381	-	-
Number of identified staff	**4.80**	**7.40**	**0.20**	**-**
Total variable remuneration	**7,923**	**355,210**	**6,810**	**-**
of which: cash-based	7,923	355,210	6,810	-
of which: shares or equivalent ownership interests	-	-	-	-
of which: share-linked instruments or equivalent non-cash	-	-	-	-
of which other instruments	-	-	-	-
of which : other forms	-	-	-	-

8 Remuneration Policy – continued

EU REM2 – Special payments to staff whose professional activities have a material impact on institutions' risk profile (identified staff)

	MB Supervisory functions	MB Management functions	Other Senior Management	Other identified staff
Guaranteed variable remuneration award				
Number of identified staff	-	-	-	-
Total amount	-	-	-	-
of which guaranteed variable remuneration awards paid during the financial year, that are not taken into account in the bonus cap	-	-	-	-
Severance payments awarded in previous periods, that have been paid out during the financial year				
Number of identified staff	-	-	-	-
Total amount	-	-	-	-
Severance payments awarded during the financial year				
Number of identified staff	-	2	-	-
Total amount	-	27,676	-	-
of which paid during the financial year	-	27,676	-	-
of which deferred	-	-	-	-
of which severance payment paid during the financial year, that are not taken into account in the bonus cap	-	-	-	-
of which highest payment that has been awarded to a single person	-	21,677	-	-

EU REM5 – Information of remuneration of staff whose professional activities have a material impact on institutions' risk profile (identified staff)

	Management Body remuneration			Business Areas						
	MB Supervisory function	MB Management function	TOTAL MB	Investment banking	Retail banking	Asset Managmeent	Corporate functions	Independent internal control functions	All other	Total
Total number of identified staff*	4.80	7.60	**12.40**	0.2	0	0	6.4	5.8	0	**12.4**
of which: members of the MB	4.80	7.40	**12.20**	0	0	0	6.4	5.8	0	**12.2**
of which: other senior managment	0.00	0.20	**0.2**	0.2	0	0	0	0	0	**0.2**
of which: other identified stafff	0	0	**0**	0	0	0	0	0	0	**0**
Total remuneration of identified staff	263,384	1,069,035	**1,332,419**	21,726	0	0	952,915	357,778	0	**1,332,419**
of which: variable remuneration	7,923	362,019	**369,943**	6,810	0	0	354,642	8,491	0	**369,942**
of which: fixed remuneration	255,461	707,016	**962,476**	14,916	0	0	598,273	349,287	0	**962,476**

Based on assessment of the Bank REM3 'Deferred Remuneration' and REM4 'Remuneration of 1 million EUR or more' per year table is not applicable. In an overview of the institution's policy there in no deferral, payout in instrument, retention periods and vesting of variable remuneration to the identified staff. Ther are no ex-post adjustments (malus during deferral and clawback after vesting) and no payouts of 1 million EUR or above.

9 Recruitment policy

The Bank is an equal opportunity employer and will not discriminate between candidates on grounds of race, religion, sex, status and disability. The Bank will strive to identify candidates who are best suited to the post on the basis of their academic achievements, work experience and career history.

10 Internal audit

The Internal Auditors support the Board of Directors by independently assessing the effectiveness of the Bank's system of internal controls and compliance of the Bank with statutory, legal and regulatory requirements. All key issues raised by Internal Audit are communicated to the management responsible via formal audit reports. The Audit Committee and Board of Directors are informed of findings and actions being taken to implement improvements.

The Internal Auditors have unrestricted access to all accounts, books and records and are provided with all information and data needed to fulfil their duties. Coordination and close cooperation with the external auditors play an important role to enhance the efficiency of Internal Audit's work.

11 Encumbered and unencumbered assets

	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
	€	€	€	€
As at 31 December 2023				
Assets	37,639,622	37,639,622	474,303,451	474,303,451

	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
	€	€	€	€
As at 31 December 2022				
Assets	40,267,926	40,267,926	310,650,296	310,650,296

12 Return on assets

The return on assets as at 31 December 2023 is 0.7% (2022: 1.3%). This is calculated as income after tax divided by total assets.