BACB

year ended 31 December 2018

ANNUAL REPORT & FINANCIAL STATEMENTS


BACB
tailored
TRADE SOLUTIONS
At BACB
knowledge and expertise of
international trade is unprecedented.
We are working hard
building strong foundations
to deliver sustainable
profitable growth.
British Arab Commercial Bank plc authorised by the
Prudential Regulation Authority and regulated by the
Financial Conduct Authority and Prudential Regulation Authority
Company No. 1047302 Registered in England & Wales
Financial Services Register No. 204564

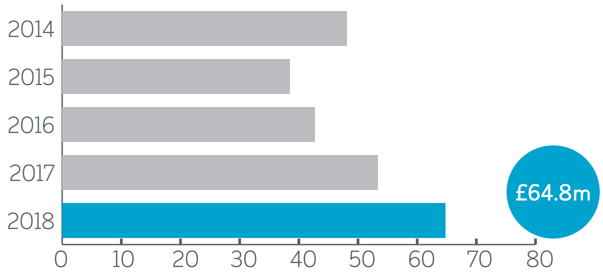
CONTENTS
section 1

CONTENTS
section 2

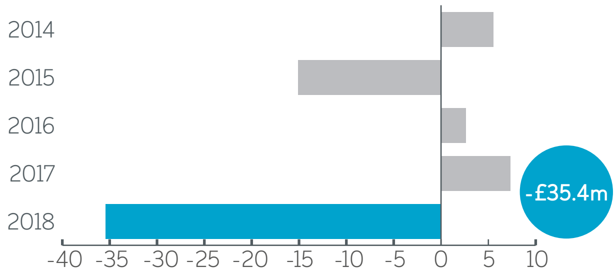
FINANCIAL HIGHLIGHTS

Record operating income, offset by significant credit impairments

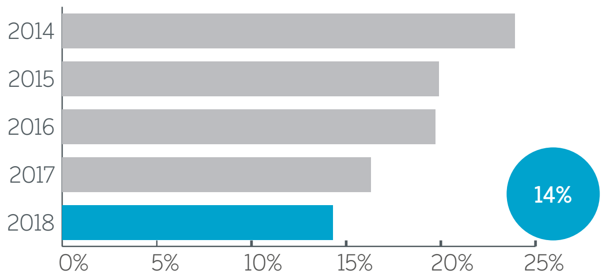
Operating Income up 21% to £64.8m



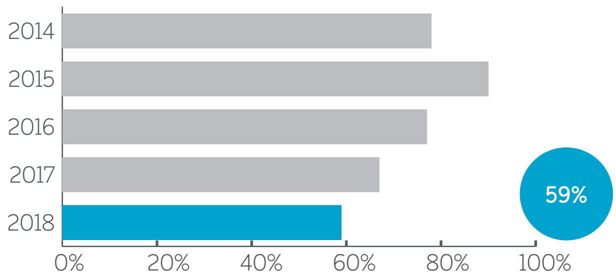
Profit/(loss) before tax down £42.6m to -£35.4m



Capital Strength impacted by credit impairments



Cost/Income Ratio down to 59%



	2018	2017	2016	2015	2014
FINANCIAL POSITION £m					
Operating Income before Loan impairments	**64.8**	53.4	42.7	38.5	48.1
Profit/(Loss) before income tax	**(35.4)**	7.3	2.6	(15.1)	5.5
Profit/(Loss) for the year	**(35.3)**	6.8	2.7	(14.5)	4.7
Total Assets	**3,894**	2,953	2,939	3,021	2,916
Total Loans	**2,079**	2,086	1,624	1,596	1,765
Total Equity	**168**	217	208	210	202
Tier 1 & 2 Capital (Eligible Capital)	**233**	281	278	271	255
RATIOS %					
Capital Adequacy[1]	**14.3%**	16.3%	19.7%	19.9%	23.9%
Cost Income Ratio[2]	**59%**	67%	77%	90%	78%
Return on Tier 1 Capital	**-22%**	3%	1%	-7%	3%
Return on Tier 1 & 2 (Total Eligible Capital)	**-15%**	2%	1%	-6%	2%
Non Performing Loans %	**10%**	4%	3%	3%	2%

[1] Tier 1 and 2 capital divided by Risk Weighted Assets
[2] Based on Administrative Expenses divided by Operating Income before allowances for credit losses

BOARD OF DIRECTORS

The Board of Directors led by the Chairman Michael Stevenson.

PATRICIA SMITH
Company Secretary

BRAHIM SEMID
Non-Executive Director

ABDALLA NAAMA
Non-Executive Director

FAISAL OTHMAN
Non-Executive Director

MOHAMED ZINE
Independent Non-Executive Director

AHMED ABURKHIS
Non-Executive Director

JEHANGIR JAWANMARDI
Independent Non-Executive Director

MOHAMED SHOKRI
Vice Chairman
Non-Executive Director

MICHAEL STEVENSON
Chairman
Independent Non-Executive Director

SUSIE ALIKER
CEO
Executive Director

KHALED KAGIGI
Independent Non-Executive Director

CHAIRMAN'S STATEMENT

"The business opportunities for BACB in our core markets remain substantial."

2018 has been a challenging year at BACB. Solid progress during the year across our core business products was undermined by issues within the Commodity Finance book. Addressing these matters largely contributed to a very disappointing level of credit provisions and the reporting of a significant loss for the year.

The losses reported for 2018 have reduced shareholder value. However, actions taken by the Board are assisting the Bank to return to profitability and to rebuild its capital strength.

The Board is committed to strengthen the Bank, in line with its Strategy; utilising our quality people and working with our customers to deliver sustainable profitable growth and improved returns for our shareholders.

This year, 2019, the Bank is currently trading profitably. The Board and the Executive Team, led by our CEO, have implemented several initiatives which, taken together, will improve not only credit quality, conduct and culture, but also the robustness of our risk management and controls framework. The Board is also requesting efficiencies and enhancements to the control environment from our new core banking platform implemented in December 2018.

The business opportunities for BACB in our core markets remain substantial. We have a strong customer base and a strong reputation, especially in our core business of Trade Finance. We have quality executive leadership and knowledgeable teams in the Bank. The Board was delighted to see our CEO and Team recently collect the GTR Leaders in Trade 2019 Award as "Best Trade Finance Bank in North Africa".

With regard to cyber-crime, the Board continues to review the Executives' work on our defences against this constantly evolving threat. As well as upgrading our technology platform we have upskilled and increased our resources to counteract financial crime, with a strong focus on process and control enhancements. We are alert to the challenges the Bank faces from operating in high risk jurisdictions.

STRATEGY

Following the appointment of a new CEO mid-year, the Board initiated a strategic review of the Bank. Led by our CEO, the review resulted in a revised strategy launched in September and aimed at delivering long term sustainable profitable growth. During the latter part of the year, there were further changes to the composition of both the Board and the executive management with the objective of further improving the Bank's conduct, culture, risk and customer delivery capabilities.

To achieve its strategic objectives, the Board is refocusing BACB on its core products, markets and customers. While our traditional trade finance services to and from MENA and developing markets in Africa have been the main revenue sources, the UK real estate sector, mainly in London, has also contributed well during the year.

> *"We have made good progress in building a strong people-led performance culture within our organisation"*

OUR PEOPLE

The Board has refreshed its People Strategy to ensure BACB develops, retains and recruits talented people with the appropriate expertise. An important element of this People Strategy is the secondment programme with our majority shareholder, wherein we assist with the development of their future executive talent.

I would like to thank all our colleagues for their hard work and support during what has been a very challenging period for BACB. We have made good progress in building a strong people-led performance culture within our organisation. The recognition of conduct and culture remains a key priority.

SHAREHOLDERS AND SUSTAINABILITY

The Board recognises how important it is for our shareholders that BACB provides to all its customers, sustainable quality financial services across its chosen markets. To deliver those services BACB must be a strong bank with a sound control framework, capital strength and a robust liquidity position. The Board remains committed to this goal during 2019 and progress is being achieved by the Executive team on all fronts.

GOVERNANCE

In 2018, we had some significant changes in our Board with both the Chairman and CEO stepping down in the first half of the year. On 1st June, Susannah Aliker, was appointed the new CEO, and, on 1st July, I became Chairman.

I would like to welcome to the Board our new directors, Mr F Othman and Mr J Jawanmardi. Furthermore, I would like to thank Mr R.D. Dowie (former Chairman), Dr E. Ashur, Mr A. Grew, Mr P.A. Hartwell (former CEO), and Mr A. Naama who all stepped down from the Board after providing valuable service to the Bank.

MICHAEL J STEVENSON

Chairman

26 June 2019

BOARD OF DIRECTORS

The Board of Directors led by the Chairman Michael Stevenson.

> *"The Board is committed to strengthen the Bank, in line with its strategy, utilising our quality people and working with our customers to deliver sustainable profitable growth and improved returns for our shareholders"*

BUSINESS STRATEGY AND MARKET ENVIRONMENT

“Our strategy is focused on the delivery of sustainable, profitable growth”

2018 was a year of two stories for the Bank. We made strong progress in our core trade finance strategy and at the operating level before credit losses we had our best year ever. However, we suffered some significant challenges in our commodity based lending activity and the 2018 Result reflects an elevated, and frankly unacceptable, level of credit provisioning.

The significant year on year growth in operating profit before credit losses shows just what our business is capable of. The credit provisions are due to both a continuing lag of legacy and old exposures but also reflect the impact of an earlier drive for revenue quantity rather than quality, primarily in the commodity finance book. We have revised our risk appetite in order to improve the quality of the business we undertake. There remains a gap in achieving our ambition to deliver ‘sustainable profitable growth’. We are fully focused on closing this gap.

STRATEGIC REVIEW

Since I took over as CEO in mid-2018, the Board and the executive team have agreed on a strategy focused on delivering sustainable profitable growth. We are increasingly looking to the long-term and quality revenues to drive bottom-line growth.

We have reflected on what we do well, most notably trade to and from developing markets.

Our network is a key part of our value proposition and extends across more than 100 partner banks with coverage in 22 of the 54 countries in Africa, as well as across Europe, the Middle East and Asia. We have continued to embed our two-client approach wherein we serve clients on both sides of trade flows, having strong relationships with trading businesses in Europe and beyond. During 2018 we facilitated in excess of $3.5 billion of trade finance activity. Our strength as a niche player was recognised when we won the GTR Leaders in Trade 2019 Award as ‘Best Trade Finance Bank in North Africa’, as well as being runner-up in the West Africa category.

We undertook a deep reassessment of the Bank's long-term positioning during 2018. We considered macro-economic factors impacting our core markets, including China's Belt and Road strategy, as well as market disruptors such as emerging trade finance ecosystems and technology developments. With change comes opportunity, we have considered how we can best position BACB to provide value- add trade solutions to current and prospective clients in the years to come.

Implementation will take place progressively to ensure appropriate outcomes while maintaining our historic strengths.

STRENGTHENING THE BANK

We have challenged ourselves on areas where we need to improve. As a mid-size boutique bank we have limited capacity to absorb one-off shocks.

The Bank's commodity finance and commodity-backed structured finance activities have been part of the revenue growth story in recent years. The philosophy behind these activities is based on fully secured, self-liquidating structures. Some of the structures the Bank had entered have not met this objective, which has led to a careful reassessment of activities in this area. While strategically this remains a valuable complement to our core trade finance activity, we will be conducting these activities with a different focus going forward.

We have also changed our risk appetite. We continue to enhance our risk management processes, as well as to improve the cascade and embedding of a risk aware culture throughout the Bank. We have introduced increased oversight by the Board Credit Committee, as well as having made organisational changes that have strengthened our management team.

We recently agreed a settlement with the US Authorities Office of Foreign Assets Control (OFAC) on a review of historic (pre-2014) activities which may have violated US sanctions. This followed a voluntary self-disclosure in late 2014.

In addition, we delivered on the long running project to roll-out our new core banking system which went live in December 2018.

We have no doubt that we have emerged as a stronger and more focused organisation.

“We have no doubt that we have emerged as a stronger and more focused organisation”

FINANCIAL PERFORMANCE

2018 operating income before credit losses was the best ever achieved by BACB. This performance was delivered in a year of considerable geopolitical uncertainty and of negative sentiment on global trade specifically.

This result was, as already discussed, depressed by an unacceptably high level of credit provisions. Our focus has been to provide appropriately both on specific names and to reflect an element of continued risk as we reposition our commodity backed lending activity. Of the total credit provisions for the year of £59m, £53m relates to IFRS 9 'Stage 3' with impairments largely relating to commodity finance and commodity backed structured finance. These charges in the most part remain provisions rather than losses and the hope is that recoveries will follow but may take time.

We continue to increase operating efficiency. Our cost to income ratio reduced to 58% in 2018 - still higher than we want but much closer to a sustainable target range. Further efficiency gains should be delivered as we leverage our new core banking system which went live in December 2018.

We have also focused on using our balance sheet in an increasingly efficient manner. During the year we optimised the deployment of our capital resources, in particular expanding our origination capability through increased distribution of trade assets.

The Results include a settlement amount of £3m with OFAC. While no liability has been admitted, this puts a potentially significant uncertainty behind us.

The 2018 financial result has depleted the Bank's capital resources. We are fortunate in that, due to the short-term nature of our exposures, we have been able to rebuild capital capacity significantly since the year end. Tier 1 capital headroom and total capital headroom at the Balance Sheet date reflected a short-term requirement to partially utilise regulatory stress buffers. We have already recovered to a positive headroom position (unaudited).

The financial strength of the Bank has been subject to stress testing (see Strategic Report Principal Risks) including risks related to the repositioning of our commodity-backed lending activity, the impact of Brexit uncertainty on UK real estate values, as well as an elevated level of market uncertainty in some of the Bank's target markets. The Board is firmly of the opinion that the financial fundamentals of the Bank remain strong.

CLIENT SERVICE

Our growth strategy is focused on providing excellent service and value-add solutions to our clients.

Technology will play a key role in further enhancing our service delivery capability. We continue to make significant investment in IT and our new core banking system provides the foundation for growth. Delivery on this objective was furthered with the roll-out of our new electronic banking platform in mid-2019.

"Africa is a continent on the move. BACB is well placed to contribute to its growth"

Our clients place their trust in us. We acknowledge the need to be pro-active in the fight against financial and cyber-crime and we continue to invest heavily in these key areas. To enhance our capabilities we have both upskilled our team and implemented upgraded technology solutions.

We have established a Client Service Working Group which will ensure we are focusing on the right initiatives to continue to enhance all aspects of client delivery.

We have no doubt that Africa is a continent on the move. BACB is well placed to contribute to its exciting growth prospects by building on our client-centric approach, extensive network and the expertise of our multi-cultural, diverse and talented team.

PEOPLE, CULTURE AND CONDUCT

> *"An important differentiator for BACB is how we collaborate internally as a team and externally across our extensive network"*

Our People are at the heart of all we do. As the Chairman has outlined, we are also implementing a new People Strategy.

An important differentiator for BACB is how we collaborate internally as a team and externally across our extensive network.

Our new people strategy focuses on good conduct, as well as building a 'One Bank' culture. Our aim is to build a collaborative and enquiring culture, where personal and organisational learning and innovation are encouraged.

We recognise the calibre of the Team we have at the Bank. We are focusing on initiatives to help attract, develop and retain talent.

LOOKING FORWARD

We are firmly focused on delivering sustainable profitable growth. The 2018 result has been a set-back but we have emerged stronger. We continue to monitor the impact of Brexit on the Bank, which we currently assess to be limited. We are focused on how we take the Business forward and firmly believe we are well placed with the right people, a niche offering and a nimble approach to deliver on our strategic priorities.

SUSANNAH ALIKER

Chief Executive Officer

26 June 2019

BUSINESS AND PERFORMANCE OVERVIEW

OUR NETWORK

BACB

1. HEAD OFFICE UK

Representative offices:

2. GERMANY
3. ALGERIA
4. CÔTE D'IVOIRE
5. LIBYA
6. UAE

Shareholders:

5. LIBYA
Libyan Foreign Bank

3. ALGERIA
Banque Extérieure d'Algérie

7. MOROCCO
Banque Centrale Populaire

Sister Banks:

3. ALGERIA
8. BAHRAIN
9. BURKINA FASO
10. CHAD
11. EGYPT
12. FRANCE
13. ITALY
14. JORDAN
15. LEBANON
16. MALI
17. MAURITANIA
18. SPAIN
19. TOGO
20. TUNISIA
21. TURKEY
6. UAE
22. UGANDA

OVERVIEW

BACB is a London-based international commercial bank. It is an established provider of trade finance services to emerging markets covering flows principally to and from Africa the Middle East and Asia.

The Bank is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

THE BACB DIFFERENCE

BACB aims to build long-term added value relationships and solid growth in revenues leveraging its core competency in facilitating cross border trade with its target clients and markets.

BACB's strength lies in a robust network of relationships across its key markets, its client-centric approach and expertise across a range of trade-related products and services. The Bank also offers a niche UK real estate lending business. In supporting stakeholders at both ends of the supply chain, the Bank's two-client approach ensures that BACB offers maximum value at every point of trade flows.

The Bank's strategic plan, as approved by the Board, aims to deliver strong and sustainable business growth; optimal utilisation of the Bank's balance sheet; careful management of risk, governance and control structures; along with increased efficiency in the Bank's operations.

BUSINESS OVERVIEW

The Bank has six key business lines:

- TRADE FINANCE
- STRUCTURED FINANCE
- COMMODITY FINANCE
- BANKING SERVICES
- REAL ESTATE
- TREASURY

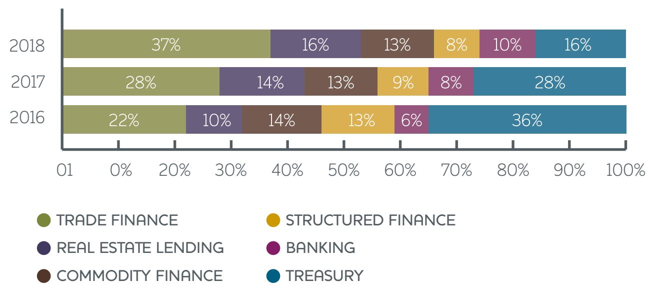
These are all complementary to the core trade franchise with the exception of the Real Estate business which forms part of the Bank's strategy to diversify its income streams and to provide some protection against the cyclical nature of global trade.

The Bank has a growing distribution capability which leverages our strong capability in originating quality trade assets and which further supports the effective utilisation of the balance sheet.

Trade finance contributed 37% of operating income in 2018 and was the key driver of growth. More broadly, trade related activity accounts for 73% of the Bank's revenue.

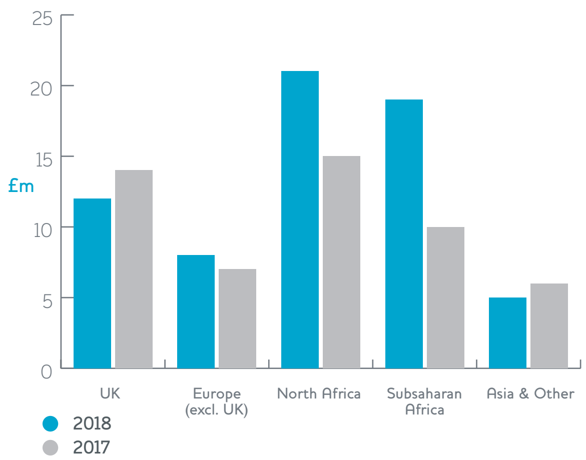
OPERATING INCOME BY BUSINESS LINE

(excludes credit provisions)



The Business mix demonstrates a healthy balance across business lines, as well as an increasingly balanced spread of geographies from which the Bank's revenues derive.

OPERATING INCOME BY REGION



The following analysis provides an overview by business line.

TRADE FINANCE

BACB is an experienced facilitator of trade for developing markets. The Bank's trade finance expertise, coupled with multi-lingual staff and a deep understanding of our target markets, ensures that client needs are met in accordance with local and international requirements. The Bank is able to leverage a network of sister banks, correspondents and its representative offices in Abidjan, Algiers, Dubai, Munich and Tripoli.

Trade Finance continues to be at the core of the Bank's strategy, and is our highest performing business sector. Year on year revenue growth in 2018 was 60%, and represented 37% of revenue. Over 2,000 trades were processed with a value in excess of $3.5bn. The portfolio has seen a steady growth from $0.6bn in 2016 to $1.1bn at the end of 2018.

Our strategic 'two-client' approach means we are able to leverage our network to focus on both our mainly European based corporate relationships on the exporter side, and our mainly financial institutions clients on the importer/buyer side in our target markets.

As part of servicing this expanding network, we opened our fifth representative office in Munich, Germany in 2018. This office has increased contribution to our business across the industrial German-speaking area of central Europe and is expected to be a key contributor to the Bank's future growth plans.

In addition, we have strengthened our distribution capability during the year. We have proven delivery in originating quality trade finance assets and we are an active player in both sell down and / or risk sharing activities with a range of counterparties including insurers.

STRUCTURED FINANCE

The Bank's lending strategy requires that new lending is linked to our own direct client relationships principally in support of the core trade business. We have renamed this business 'Structured Finance' during the year to reflect a renewed focus on quality trade related activity. The new strategy focuses on carefully targeted commodity underlyings and geographies, and compliments our trade finance business.

The Bank continues to manage down its historic loan book which comprises longer-dated primarily oil, gas and power-related project facilities to MENA sovereign-related borrowers. These loans, some of which are at lower margins than achieved on the newer areas referred to above, continue to run off.

COMMODITY FINANCE

As already described, this activity has in the past comprised short-term structured facilities to commodity traders secured by underlying commodities.

As outlined in the Principal Risks and Uncertainties section of the strategic report, the Bank's risk appetite for this activity has been revised. The Bank will focus on commodity finance activity which is complementary to the core trade finance business and more conservative lending structures.

We have carefully reassessed our activity in this area and while strategically this remains a valuable complement to our core trade finance activity, we will be conducting these activities very differently going forward. Our focus is firmly on revenue quality. Our risk appetite has been changed both in terms of client and transaction types. Going forward, we will offer commodity finance products and solutions which are complementary to our core trade finance activity and where the probability of default and loss given default are lower. We will lend smaller amounts to a wider client base utilising structures with much tighter security against a rationalised range of commodity underlyings.

We continue to enhance our risk management processes, as well as to improve the cascade and embedding of a risk aware culture throughout the Bank. We have introduced increased oversight by the Board Credit Committee, as well as having made organisational changes which have strengthened our management team.

The Bank's gross exposure to commodity finance has reduced from £265m at end December to less than £200m at the mid-year. However, there remains some risk as we continue to reposition this activity and before we rescale activity in this business area.

Going forwards, we will be aligning our commodity trade finance and structured commodity finance activities into a single business under new management.

BANKING SERVICES

BACB provides a range of banking services to corporate and financial institution clients. These include accounts in a range of currencies, international payments, payroll services and deposits.

REAL ESTATE

The real estate business is based on term lending facilities secured against high quality UK real estate assets, both residential and commercial, with conservative loan to value ratios.

As at 2018 year end, the real estate book stood at £502m. Revenues increased by 39% in the year to £10m.

This business is a key part of the Bank's diversification strategy and provides a reliable Sterling denominated annuity income flow at relatively attractive risk adjusted returns.

We continue to carefully assess the portfolio to ensure that risks of market softening due to Brexit have been minimised. As a result of the current uncertainty, our new lending activity requires increased levels of security.

TREASURY

Treasury undertakes two primary roles; as an institutional counterparty to the global financial markets and as the Bank's balance sheet management function.

Treasury acts as a conduit between the Bank's clients in Africa and Middle East and the global liquidity pools, actively dealing in products across interest rate, foreign exchange, derivative and debt capital markets. The customer service proposition of the Treasury department is the ability to combine professional execution across a wide range of treasury and capital markets products, with efficient settlement and competitive pricing, in a MiFID II compliant manner.

Foreign exchange is a primary focus, offering clients competitive pricing via FX trading portals. We are increasingly active in intermediating flows and specialise in African, Middle East and other niche regional debt markets. The Bank also offers a discrete range of structured products and Islamic finance.

Treasury combines its client centric mandate with the management of the Bank's own financial resources, namely: to manage the balance sheet structure; cash flow profiles; liquidity adequacy; and market risk hedging.

To mitigate funding and liquidity risks within regulatory and internal risk appetite, the Bank actively manages a significant portfolio of Bonds. To supplement income, the Treasury Team is mandated to manage a separate investment portfolio of bank and corporate debt securities issued principally by investment grade rated entities.

FINANCIAL POSITION

The key components of the Bank's assets were as follows:

	2018	2017
	£'000	£'000
Financial investments	1,774,166	788,066
Loans and advances to banks	997,428	1,017,510
Loans and advances to customers	1,081,161	1,068,589
Property, plant and equipment	8,378	8,291
Other	32,719	70,400
Balance sheet footings	**3,893,855**	**2,952,856**
Contingent liabilities	122,386	54,051
Other commitments	678,716	532,921

The growth in financial investments is largely made up by short term debt instruments resulting from an increase in deposits from banks.

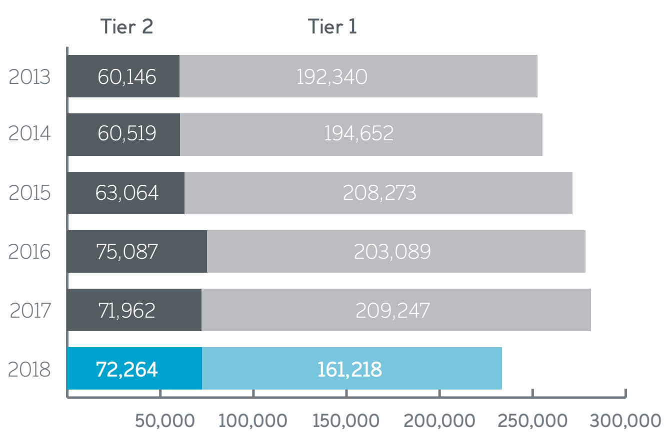
Contingent liabilities relate to guarantees issued, and other commitments are principally made up by documentary credits, credit lines and loan commitments.

CAPITAL ADEQUACY

The Bank's Tier 1 capital of £161m (2017: £209m) comprises share capital and reserves (adjusted as required by regulations) less intangible assets.

Tier 2 capital comprises issued term subordinated debt of £72m (2017: £72m),

TIER 1 AND TIER 2 CAPITAL



The following table shows the composition of the Bank's minimum capital requirement and capital adequacy position calculated in accordance with regulatory rules (the "Pillar 1 requirement") at 31 December 2018.

CAPITAL REQUIREMENT AND CAPITAL IN PLACE

	2018	2017
	£'000	£'000
Credit, Counterparty, CVA risk	119,040	130,931
Market risk	5,016	651
Operational risk	6,821	6,339
Total Pillar 1 capital requirement	**130,877**	**137,921**
Capital in place	233,482	281,209
Excess of capital in place over minimum requirement under Pillar 1	**102,605**	**143,288**

As at 31 December 2018 the Bank's capital adequacy ratio was 14% (2017: 16%).

The year-on-year increase in capital requirement reflects success during the year in building up business assets, particularly in the core trade finance business. However, the capital in place has been depleted by the unprecedented level of credit provisions.

The Bank's surplus Tier 1 capital and total capital over the total regulatory minimum as at 31 December 2018 required partial utilisation of regulatory stress buffers. Minimum capital requirements include buffers that are designed to be used in times of stress. The actions taken by the management team have already led to the recovery in the capital position and, together with the resilience and underlying profitability of the Bank, should ensure that the position is normalised quickly.

There is further discussion of capital adequacy risks on Page 1.23.

LIQUIDITY

BACB benefits from strong and stable liquidity, consistently and significantly exceeding all regulatory requirements.

The Bank sources most of its liquidity from its principal shareholder, Libyan Foreign Bank, and the Central Bank of Libya. The funding base remains concentrated; over the past five years this has remained stable and actually increased during the latter part of 2018.

Liquidity is managed by the Bank's Treasury department, overseen and guided by the Asset and Liability Committee, which reports via the Executive Committee to the Board. As a general principle and in recognition of its concentrated funding base, the Bank intentionally maintains liquidity ratios well in excess of regulatory requirements.

The Bank is exploring options to diversify its sources of funding including via accessing UK retail deposits.

INTERNAL OPERATIONS

The Bank is committed to operate in an efficient and compliant manner in all of its activities, key aspects of which are considered below.

REGULATORY COMPLIANCE

The Bank is committed to maintaining an effective regulatory compliance framework which is aligned to and calibrated with the requirements of a UK regulated institution operating within our target markets and service streams.

Significant regulatory and compliance projects and initiatives in 2018 included the embedding of the requirements of the Market in Financial Instruments Directive II, the General Data Protection Regulation 2018, Data Protection Act 2018, initiatives to further enhance governance, as well as updates within the Senior Management and Certification Regime framework.

Due to the significance of these regulatory obligations and increased focus on individual conduct and accountability, these areas have been subject to an increased level of Board oversight.

As well as separating the Compliance function from the Anti-Financial Crime area, significant work was undertaken to enhance the current compliance monitoring framework to ensure that it is more risk focussed and monitored accordingly.

ANTI-FINANCIAL CRIME

BACB takes its Anti-Money Laundering (AML) and Anti-Financial Crime (AFC) responsibilities very seriously, particularly given the potentially higher risk profile of some of the markets in which we operate.

We have continued to deliver substantial enhancements in the Bank's AML/AFC policies, procedures and systems, as well as upskilling our resources in these key areas. Recognising the significance of these responsibilities, we have separated Anti-Financial Crime from Compliance in our monitoring of principal risks, creating a focussed AFC Department. We have improved our transaction screening capabilities, with further developments planned in 2019. These enhancements will ensure additional dedicated focus on the Bank's AML/AFC responsibilities.

We recognise the need for continual enhancement, and this is shaped by our internal compliance monitoring, forthcoming regulations and taking into account regulatory news in particular from the FCA. The 5th AML Directive is the next significant regulatory development on the horizon and will be incorporated into the Bank's processes.

In late 2014, the Bank initiated a review of certain historical activities, which involved a voluntary self-disclosure to the U.S. Authorities of transactions that may have violated certain U.S. sanctions, principally related to Sudan. In June 2019, the Bank has agreed a settlement with the U.S. Office of Foreign Assets Control although no liability has been admitted.

No further civil or criminal enforcement proceedings are pending or threatened.

INFORMATION TECHNOLOGY

Information Technology remains a critical area for the Bank, both to ensure the delivery of excellent service to our clients and to underpin internal processes which are efficient and effectively controlled.

Our technology strategy aims to augment our client service capabilities and to deliver a systems infrastructure which will further enhance data integrity, quality and security across the Bank, with systems that support sound decision making and efficient processing in a controlled and compliant manner. We regularly test our IT security capabilities and are committed to a continuous programme of enhancing our operational resilience.

The upgrade to our core banking system and the implementation of the Temenos T24 platform was completed during 2018 and is a major milestone in the comprehensive Enterprise Architecture review that was carried out to define the Bank's technology requirements over a 5-year horizon, considering technology advances as well as the Bank's strategic business plan. This major implementation evidences the long-term commitment and support of the Bank's shareholders.

The core banking system implementation paves the way for future developments to improve service to our clients, including the roll-out of an innovative internet banking platform.

INTERNAL AUDIT

The Internal Audit function is independent of the business and has a primary reporting line to the Co-Chairs of the Audit, Risk & Conduct Committee. The function is fully outsourced to PricewaterhouseCoopers.

The Internal Audit function undertakes a risk-based programme of work to review the appropriateness and effectiveness of the Bank's internal controls, regulatory compliance and risk management processes and thereafter to provide independent assurance to the Audit, Risk & Conduct Committee.

PEOPLE

Our aim is to build an organisation where all staff feel empowered, accountable and engaged. Conduct is explicitly considered in reward and recognition structures, as well as performance. At the end of 2018, the Board approved a new People Strategy, which is directly aligned to our business strategy.

We strive to help our people to develop and grow to deliver the best service to our customers through collaboration, innovation and risk mitigation.

> *"Our aim is to build an organisation where all staff feel empowered, accountable and engaged"*

CULTURE AND CONDUCT

This remains a key area of focus for BACB as well as our regulators, and the banking industry more generally. Our objective is to ensure that staff know what good conduct means, recognising that how things should be done is as important as what we do.

The 2018 People Strategy considered steps to further embed the culture agenda, with initiatives established to promote team work and collaboration both internally across the Bank, as well as looking at life outside of work through external team events and volunteering initiatives to augment our social responsibilities.

We have enhanced our ability to measure both conduct and culture providing metrics to the Executive Committee, with escalation to the Board, where appropriate. In addition to metrics concentrating on misconduct, we consider it equally important to monitor metrics that highlight positive conduct and to make a clear linkage between good and bad behaviours and remuneration.

PERFORMANCE MANAGEMENT

In the coming year, we will be implementing changes to the Performance Management process including a new behaviours grading, facilitating an ongoing rather than annual dialogue, and enhancing feedback mechanisms. Our approach has been to better calibrate technical and behavioural competencies within the process to ensure that employee performance continues to be assessed based on both what is achieved and how it is achieved.

LEADERSHIP DEVELOPMENT

Employee development is critical for a successful organisation, and during 2018 we continued with our focus on developing skills and competencies for our manager population.

DIVERSITY

The Bank is a diverse and inclusive workplace which is reflective of the communities in which we do business. We recognise that a successful business benefits from embracing diversity, in order to maintain a competitive advantage.

HEALTH AND SAFETY

The Bank maintains the highest standards possible for the health, welfare and safety of its employees, clients and visitors.

CORPORATE SOCIAL RESPONSIBILITY

BUSINESS STANDARDS AND CONDUCT

BACB is committed to conducting business responsibly and ethically. The Bank aims to maintain the highest standards with regards to human rights, diversity and inclusion, and only accepts business which meets our strict ethical and legal criteria.

ENVIRONMENT AND SUSTAINABILITY

BACB is passionate about building a sustainable future. The Bank is committed to achieving environmental best practice, and we have policies, practices and targets in place to help us achieve this objective.

Since our establishment, a policy of 'reduce, reuse and recycle' has been encouraged across our operations. A number of initiatives have been progressed via our Sustainability Working Group, delivering cost savings for the Bank as well as environmental benefits.

We continue to participate in the Corporation of London's Clean City Award scheme and in 2018 were again presented with a Platinum award in recognition of our standards.

CHARITABLE SUPPORT

In 2018, the Bank made charitable donations of £4,975 (2017: £4,700) including support for employee fundraising through the Bank's "£ for £" scheme, matching fund raising up to £500 per employee per year.

The Bank facilitates "Give As You Earn" charitable giving by employees and matches holiday days for staff who undertake volunteer work in the UK or overseas.

The Bank also continues to support the Lord Mayor's Appeal by engaging the support of employees during its City Giving Day, raising funds for good causes in London and in the surrounding area.

CORPORATE SOCIAL RESPONSIBILITY

During 2019 we are better aligning our CSR and our culture initiatives and have launched a series of 'BACB Together Days' where BACB teams are spending a day working within a charitable cause. This initiative both helps us to give something back to the community as well as providing an opportunity to build internal teamwork and collaboration.

STRATEGIC REPORT

PRINCIPAL RISKS AND UNCERTAINTIES

PRINCIPAL RISKS AND UNCERTAINTIES

The Bank's overarching risk management objectives are to operate within a clearly articulated risk appetite in an environment which fosters a strong risk culture, supported by timely, complete, accurate and relevant risk reporting.

Risks are monitored within the framework of an 'overarching governance standard' which is underpinned by governance standards covering nine principal risk types. The Board considers an 'Enterprise Risk Assessment' at each meeting which assesses those risks which may present a threat to the stability or sustainability of its business franchise.

This risk management framework is described in greater detail in Note 4. Principal risks and uncertainties are considered below.

CREDIT RISK

Acceptance of credit risk remains the Bank's principal source of revenue and in consequence, its principal source of financial risk. The degree of credit risk the Bank is prepared to accept is calibrated to its Board approved business plan and the supporting risk appetite framework.

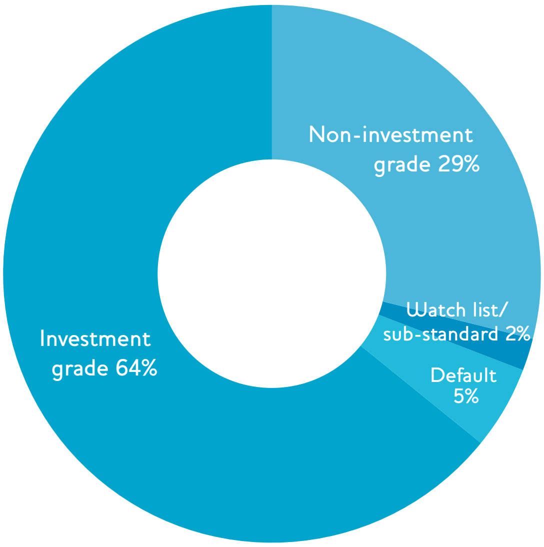
The Bank's strategic geographical focus means that a significant portion of credit risk is aligned to the lower end of the credit grading spectrum. However the intent of the Bank's trade and commodity finance business streams involves short-term, secured and self-liquidating exposures, with the Real Estate lending book being fully secured at prudent loan-to-value levels. The Bank manages its credit risk by employing a number of mitigants including:

- A framework of concentration limits and guidelines to avoid excessive exposures to individual counterparties, countries, regions or sectors;
- Limits which govern the quantum nature and tenor of exposures;
- Use of cash collateral and other forms of security, including distribution more recently;
- Business asset decision making made with reference to risk adjusted return criteria.

Approximately two-thirds of the Bank's exposures are classified as investment grade.

CREDIT EXPOSURE BY GRADE

Rated by BACB internal grading system



Of the Bank's total credit exposures, 2% by value are on the 'watch-list' and 5% are classified as impaired. The individually assessed impairment charge relates to a small number of exposures.

The IFRS 9 Financial Instruments accounting standard was adopted from 1 January 2018. The IFRS 9 transitional adjustment to the allowance for credit losses was calculated as £7.5m while allowance for credit losses for year ended 31 December 2018 amounted to £59.0m.

The ensuing analysis considers key matters related to credit provisions and the consequent impact on the Bank's capital position as at 2018 year end, both of which have been subject to stress testing.

CREDIT PROVISIONS AND CAPITAL ADEQUACY RISK ASSESSMENT AND STRESS MODELLING

CREDIT PROVISIONS RISK ASSESSMENT

The 2018 result includes £59m of credit impairments split as follows:

- Commodity Finance Stage 3 £34m
- Structured Finance Stage 3 £18m
- Legacy Stage 3 £9m
- Real Estate Stage 3 £2m
- Trade Finance Stage 3 £1m
- Stage 1&2 £(5)m

Overall IFRS 9 'Stage 3' exposures are £220m, of which Commodity and Structured Finance exposures total £178m with an average impairment level of 39%.

Going forward the Bank's Commodity Finance and commodity-backed Structured Lending activities are being repositioned both with regards client and transaction types. This will include reduced tenor on any stock lending, increased security and/or net worth of clients and tighter transaction structures.

The gross exposure on the commodity related exit book has reduced to £88m today, of which 31% is provided. Given this book has a number of loans already in default combined with the repositioning of these activities, this is an area of potentially higher risk. There is significant focus on maximising recoveries on these exposures.

Initiatives are also progressing in the risk management area including the revision of the risk appetite and other enhancements to the risk framework.

The directors believe they have provided appropriately, however, lending does involve risk and consequently there remains a level of uncertainty particularly as the Bank repositions its approach and activities. The credit provisioning on commodity related exposures have been subject to stress testing. For example, if the Bank only received a 50% of the current un-provided amount on the commodity related exit book credit provisions would increase by c.£25m.

In addition to the above, there is credit risk across the whole portfolio which the directors continue to monitor and stress.

CAPITAL ADEQUACY RISK ASSESSMENT

As at 31 December 2018, the capital requirement exceeded capital in place by £29.7m at the Tier 1 level (£1.0m at the total capital level) following adjustments for year end provisions, resulting in the Bank partially utilising its regulatory stress buffers. The capital stress was caused in the main by the high level of year end credit provisions discussed above.

Since the year end, capital headroom (unaudited) has recovered substantially through careful management of risk weighted assets (including restricting new business take-on and sale of some positions). RWAs as at end May 2019 have reduced by c.10% since the year end.

The capital position at the date of signing the accounts shows that Headroom (at both the Total and the Tier 1 level) has recovered to a position in excess of all regulatory requirements (unaudited). This position will be strengthened further following additional management actions including a proposed interim profits review, which will allow the 2019 profit (currently unaudited) to be added to capital. In line with the Strategy, the Board is working with the shareholders to strengthen the capital base of the Bank to support future business growth.

The Directors have considered a number of stress scenarios on the Bank's capital adequacy, including the risk of additional credit provisions and/or Brexit related impacts on the real estate portfolio. Any such modelling considers the impact of further depletion in capital resources and which, if severe, could lead to the Bank being unable to meet the threshold criteria to the satisfaction of the PRA which is essential in order for the Bank to be permitted to trade. However, if the Bank's results for the year were in line with the combined stressed loss as per the ICAAP submitted to the PRA, capital headroom can be maintained in line with regulatory requirements. An even more extreme scenario would be a stress combining losses noted above on the commodity exit book as well as Brexit related stresses on the UK real estate book. This stress, whilst not considered likely, would significantly deplete capital but the Board still considers that the Bank would be in a position to manage the risk through further restricting capacity to take on new Business. The Bank remains relatively resilient in large part due to the short-term nature of most of the asset base.

The Directors' assessment is that with on-going careful management of new risk weighted assets, capital headroom can be restored and maintained at a level which permits profitable growth – as evidenced in 2019 year to date (unaudited) performance.

FUNDING CONCENTRATION

The funding model of the Bank is concentrated and dependent on its principal shareholder, the Libyan Foreign Bank, and the Central Bank of Libya. The political and economic situation in Libya has been volatile in recent years and the outlook for the country remains challenging, which could lead to disruption or curtailment of the Bank's primary source of funding.

LIQUIDITY ANALYSIS

The directors have considered a detailed analysis of contractual cash-flows and are confident of the Bank's ability to meet all of its obligations as they fall due should the Bank's funding from Libya reduce materially or cease. This is due to the highly liquid nature of the majority of the Bank's assets, the relatively short-term nature of much of its lending and the quality of the underlying security, particularly its UK real estate assets.

This liquidity analysis is based on key assumptions, most notably around the impact of property prices on its UK real estate lending portfolio, which have been stressed to allow for Brexit uncertainty, future credit losses and the Bank's ability to generate new secured funding at a reasonable level.

LIBYA POLITICAL CHALLENGES

The political challenges in Libya continue to be the subject of much interest, and more so with the most recent developments.

Significant efforts by the international community to resolve the issues in the best interests of the people of Libya continue. There remains momentum towards finding a stable and lasting solution involving a unified and internationally recognised government, as well as signs of an emergent interest from external parties to invest in Libya.

Current funding levels from Libya remain both stable and strong, with the maturity profile of the deposit base being broadly consistent. BACB remains strategically important to Libya in its interaction with the global economy and as a means of providing access to the international financial markets, including for its oil and gas revenues. Furthermore, if, as happened in 2011, the Libyan political situation results in the imposition of international sanctions, the funding would become permanent for their duration.

The Bank is not reliant on business flows to and from Libya. Net exposure to Libya after risk mitigation is less than 1% of total exposures. While Libya continues to be a key market for the Bank, its strategy of geographic diversification has diluted the overall impact of the current situation and, as and when stability returns to Libya, this market holds significant upside potential.

In summary, the directors' assessment is that the risks posed to the Bank as a result of its concentrated funding base do not pose a material uncertainty.

COUNTERPARTY BANKS

The directors continue to monitor relationships with BACB's international counterparties and the need for counterparty banks to continue to transact with the Bank. Across the whole sector, the trend for counterparties to review the potential regulatory and legal risks associated with clearing transactions initiated by other banks has continued. The directors acknowledge these concerns may be heightened due to the Bank's connections with Libya.

The Board monitors the impact and level of de-risking by its counterparties but cannot control the actions of the market. Recognising this, the Bank maintains a close and continuous dialogue with its principal counterparty and correspondent banks. The significant progress made in strengthening the Bank's governance and control procedures and continued investment in sanctions monitoring, Anti-Money Laundering and Counter Terrorist Financing controls demonstrates the Bank's commitment to ensuring the robustness of its operations and assists in providing the necessary comfort to ensure that BACB remains a safe counterparty with which to transact business. The closure of the review of historic activities with OFAC removes any potential uncertainty related to this matter.

The Board is reassured by the continuing stability of the Bank's principal correspondent banks and other counterparty bank relationships.

In summary: The directors' assessment is that the risks posed to the Bank as a result of its counterparty bank relationships do not pose a material uncertainty.

REPUTATIONAL RISKS

The Bank protects itself from material damage to its reputation by ensuring that any business activity is satisfactorily assessed and managed by the appropriate level of management and governance oversight.

OTHER IMPORTANT RISKS

The Bank faces a range of other risks including compliance, market, operational and conduct and culture risks.

A description of the full range of risks faced by the Bank and its approach to managing these risks is set out in Note 4.

Conduct and culture risk has been a key area of focus for the Bank during 2018 culminating in the launch of a revised People Strategy, outlining a number of initiatives to be rolled out in 2019 following the introduction of 'The BACB Way' code of conduct.

Regulatory compliance remains a key area of focus. The Bank operates in some of the international markets' more challenging countries, and often with clients for whom it may be difficult to obtain the required level of information to satisfy KYC, AML and Sanctions screening criteria. There has been ongoing investment in screening tools and resources, as well as the personnel responsible for client and transaction screening.

Note 32 provides details of the recently agreed settlement with the US Authorities (OFAC) on a review of historic (pre-2014) activities which may have violated US sanctions. No liability has been admitted.

BACB has a zero risk appetite for regulatory breaches and/or breaches of economic sanctions imposed by appropriate authorities. We have stringent criteria to determine when enhanced due diligence should be conducted (including for all Libyan payments) and continue to invest in tools and people to support client due diligence and screening processes.

The Bank-wide project to upgrade the core banking IT system went live at the end of 2018 with further improvements scheduled to be rolled out in 2019. This is already helping to rationalise the Bank's IT infrastructure. Other projects, including Regulatory change initiatives, are subject to close oversight by Executive Management and the Board.

The Bank seeks to avoid risk and uncertainty for our critical information assets and systems and has a low appetite for material incidents affecting these or the wider operations and reputation of the Bank.

The impact of the UK's decision to leave the European Union is being monitored. In the short-term, any weakening of Sterling against the US dollar will enhance revenues but, given the denomination of the Bank's asset and capital base, may also result in higher capital demands. Longer-term, the assessment remains that Brexit will have a minimal direct impact on BACB, given the Bank's market geographical focus outside the EU.

The above risks and uncertainties have been fully considered by the directors as part of the Bank's going concern assessment.

STRATEGIC REPORT

CORPORATE GOVERNANCE

SHAREHOLDERS

The Bank's shareholders as at the reporting date were:

- Libyan Foreign Bank (87.65%);
- Banque Extérieure d'Algérie (6.175%); and
- Banque Centrale Populaire (6.175%).

The Bank's majority Shareholder, the Libyan Foreign Bank ('LFB') has a substantial international portfolio of investments, involving over 40 participations in 25 countries. In its 2018 accounts (unaudited), LFB reported total assets of c.$18bn and net assets of c.$4bn, including significant cash reserves.

GOVERNANCE

The governance arrangements followed by the Bank's Board of Directors (the Board) are mandated in a Shareholders' Agreement and in its Articles of Association.

These agreements provide that shareholders of the Bank may appoint directors in accordance with the proportion of their shareholdings. They also provide for the appointment of the Chairman and the Chief Executive, and for the formation of certain committees to oversee the day-to-day running of the Bank. Schedules of Reserved Matters specify various issues which must be decided by the Board (as opposed to Executive Management) and those other matters reserved for approval and decision by shareholders.

The Board governance arrangements are complemented by an executive governance structure which has been strengthened significantly in recent years. The executive governance structure benefits from clearly articulated governance principles and risk management objectives, underpinned by an articulation of the principal risk types incurred by the Bank and associated minimum controls for the management and reporting of these risks in accordance with the Bank's overall risk appetite. The Bank has adopted the market accepted 'three lines of defence' model with the outsourced Internal Audit function acting as the third-line of defence and providing independent assurance to the Audit, Risk and Conduct Committee on the appropriateness and effectiveness of the system of internal control.

BOARD ARRANGEMENTS

The Bank benefits from the skills and experience of its Board members. Shareholder appointees bring experience of BACB markets. Differences in the skills, experience, background, race, gender and other distinctions between directors are considered in shaping the optimum composition of the Board.

As at 31 December 2018, the following individuals served on the Board:

BOARD MEMBER	SUB-COMMITTEE MEMBER	STATUS
Mr MICHAEL STEVENSON *Chairman*	ARCC/NRC	I-NED
Mr MOHAMED SHOKRI *Vice-Chairman*	ARCC/NRC	NED
Mr AHMED ABURKHIS	ARCC/NRC	NED
Mrs SUSIE ALIKER[1]		ED
Mr JEHANGIR JAWANMARDI[2]	ARCC/BCC	I-NED
Dr KHALED KAGIGI[3]	ARCC/BCC	I-NED
Mr ABDALLA NAAMA[9]	ARCC/BCC	NED
Mr FAISAL OTHMAN[2]	ARCC/BCC	NED
Mr BRAHIM SEMID	BCC	NED
Mr MOHAMED ZINE[4]	ARCC/BCC	I-NED

Note 1: Mrs Susannah Aliker resigned as Secretary to the Board on 6th July 2018, and Mrs Patricia Smith was appointed as Secretary to the Board on 6th July 2018.

Note 2: Mr Jehangir Jawanmardi and Mr Faesal Othman were appointed to the Board on 28th September 2018.

Note 3: The appointment of Dr Khaled Kagigi as Senior I-NED and Chair of the Risk and Conduct Committee is subject to regulatory approval.

Note 4: Mr Mohammed Zine was reclassified as an I-NED on 6th July 2018.

Note 5: Mr Paul Hartwell resigned from the Board on 8th June 2018.

Note 6: Mr Robert Dowie resigned from the Board on 30th June 2018.

Note 7: Mr Akram Grew resigned from the Board on 12th July 2018.

Note 8: Mr Ezzedine Ashur resigned from the Board on 7th October 2018.

Note 9: Mr Abdullah Naama resigned from the Board on 1st May 2019.

The Board includes four independent non-executive directors, one of whom is the Chair of the Board, two of whom are Co-Chairs of the Audit, Risk and Conduct Committee (of which one remains subject to Regulatory approval). The Chief Executive is a full time employee of the Bank and is regarded as an Executive Director. All of the other directors are regarded as Non-Executive Directors.

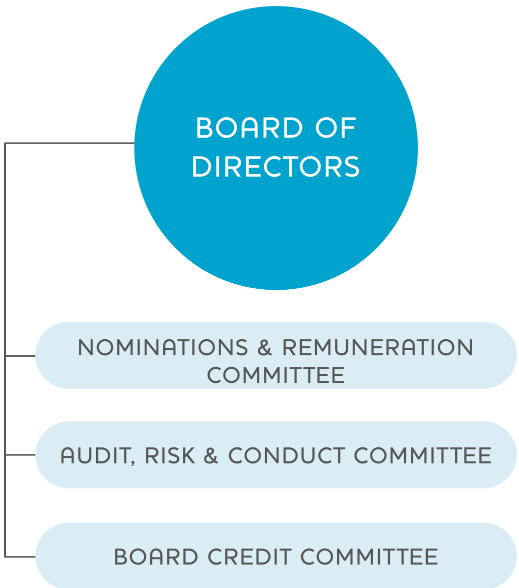
The Board met on six occasions during 2018.

GOVERNANCE FRAMEWORK

The Board has ultimate responsibility for establishing, approving and periodically reviewing the strategy of the Bank and its governance framework. The Board oversees senior management to ensure that they manage the Bank's activities in a manner which is consistent with the strategy and governance framework.

BOARD SUB-COMMITTEES

The Board has established a number of Sub-Committees in order to enhance and streamline its decision making, as outlined below.



NOMINATIONS AND REMUNERATION COMMITTEE ("NRC")

The Nominations and Remuneration Committee has a mandate to agree the remuneration and employment policies of the Bank and to make key appointments.

AUDIT, RISK & CONDUCT COMMITTEE ("ARCC")

Non-Executive Directors are eligible to sit on the Audit, Risk & Conduct Committee. The Committee considers the Bank's financial reporting, the nature and scope of audit reviews, and the effectiveness of the systems of internal control, conduct, compliance and risk management.

Meetings are separated into agendas for Audit matters and Risk and Conduct matters, with separate Chairs.

The CEO, CRO and CFO attend each meeting of the ARCC, along with the Bank's external auditors, its outsourced internal auditors, and other Executives as required.

The Audit, Risk and Conduct Committee met six times during 2018.

BOARD CREDIT COMMITTEE ("BCC")

The Board has delegated authority to approve the granting of credit applications to executive management subject to certain limits. Applications above those limits must be referred to the Board Credit Committee for consideration and approval. The Committee considers applications as they arise.

EXECUTIVE GOVERNANCE

Led by the Chief Executive, the Executive Committee ('ExCo') has a business and prudential remit and is responsible for:

- Formulating and endorsing the Bank's strategy and annual operating plan for approval by the Board;
- Ensuring the Bank is managed in accordance with the strategy;
- Ensuring the Bank is managed in a sound, prudent and ethical manner and in accordance with all relevant laws, regulation and guidance;

- Managing the Bank's interface to its principal stakeholders including the Board, regulators and auditors.

The members of ExCo are:

- Chief Executive Officer
- Chief Financial Officer
- Chief Risk Officer
- Chief Operations and Controls Officer
- Human Resources Director
- Head of Corporate and Institutional Banking

The Company Secretary attends as a standing invitee.

ExCo has established five Committees which cover risk management, governance, regulatory and compliance, operating and business development matters.

The ExCo Sub-Committee structure is as summarised below:

Following review and recommendation by the ExCo, the Board approved the establishment of a Management Committee, effective April 2019, to complement the existing Governance Framework. This will enable a greater level of engagement with and understanding of Bank-wide governance across a wider group of SMF and Certified staff.

The Strategic Report was approved by the Board of Directors on 26 June 2019.

PATRICIA SMITH

Secretary to the Board

26 June 2019

STATEMENT OF

DIRECTORS' RESPONSIBILITIES

IN RESPECT OF THE STRATEGIC REPORT, THE DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS

STATEMENT OF

DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE STRATEGIC REPORT, THE DIRECTORS' REPORT AND THE FINANCIAL STATEMENTS

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

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with International Financial Reporting Standards as adopted by the European Union (IFRSs as adopted by the EU) and applicable law.

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

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

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

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 2018

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 2018

The directors present their annual report and the audited financial statements for the year ended 31 December 2018. These financial statements have been prepared in accordance with the Companies Act 2006 and applicable accounting standards.

FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Bank's objectives and policies with regard to financial and other risks are set out in Note 4 to the financial statements, together with an indication of the exposure to financial risk.

RESULTS

The loss after taxation for the year amounted to £35,308,000 (2017: Profit of £6,825,000).

GOING CONCERN

These Financial Statements have been prepared on a going concern basis as the directors are satisfied that the Bank has the resources to continue in business for the foreseeable future. Their rationale is discussed further in Note 2.

COMPANY NAME AND NUMBER

British Arab Commercial Bank plc is an unlisted public company registered in England and Wales. The company number is 1047302.

DIRECTORS AND THEIR INTERESTS

A list of the directors who served during the year is shown on page 1.28. None of the directors holds or has held shares in the Bank. All of the directors benefited from qualifying third party indemnity insurance in place during the financial year and at the date of this report.

AUDITORS

KPMG LLP was appointed as the auditor of the Bank at its Annual General Meeting on 23 March 2018, to hold office until the conclusion of the next General Meeting at which Financial Statements are laid before the company. In accordance with Section 489 of the Companies Act of 2006, a resolution for the reappointment of KPMG LLP as auditor of the Bank is to be proposed at the forthcoming Annual General Meeting.

DIRECTORS' REPRESENTATION

The directors who held office at the date of approval of this Directors' Report confirm that, so far as they each are aware, there is no relevant audit information of which the Bank's auditors are unaware; and directors have taken all steps that they ought to have taken as directors to make themselves aware of any relevant audit information and to establish that the Bank's auditors are aware of that information.

PATRICIA SMITH

Secretary to the Board

By order of the Board

26 June 2019

INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF BRITISH ARAB COMMERCIAL BANK PLC

INDEPENDENT AUDITOR'S REPORT

TO THE MEMBERS OF BRITISH ARAB COMMERCIAL BANK PLC

1. OUR OPINION IS UNMODIFIED

We have audited the financial statements of British Arab Commercial Bank plc ("the Bank") for the year ended 31 December 2018 which comprise the Statement of Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity and Statement of Cash Flow, and the related notes, including the accounting policies in note 3.

In our opinion the financial statements:

- give a true and fair view of the state of Bank's affairs as at 31 December 2018 and of its loss for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

BASIS FOR OPINION

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

Following a competitive tender process in the summer of 2017, we were reappointed as auditor of the Bank for the period ending 31 December 2017 and subsequent financial periods. We were originally appointed as auditor by the directors on 27 September 1996. The period of total uninterrupted engagement is for the twenty-three financial years ended 31 December 2018.

We have fulfilled our ethical responsibilities under, and we remain independent of the Bank in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

2. MATERIAL UNCERTAINTY RELATED TO GOING CONCERN

	THE RISK	OUR RESPONSE
Going concern **We draw attention to note 2 (a) to the financial statements which indicates the risk to the Bank of the capital position of the Bank at 31 December 2018, combined with the uncertainty around the impact on capital of the level of future credit provisions. Solely in respect of these events and conditions in relation to regulatory capital and the impact of the level of future credit provisions, there is a material uncertainty that may cast significant doubt on the Bank's ability to continue as a going concern.** **Our opinion is not modified in respect of this matter.**	**Disclosure quality** Financial statements explain how the Board has formed a judgement that it is appropriate to adopt the going concern basis of preparation for the Bank. That judgement is based on an evaluation of the inherent risks to the Bank's business model, including the impact of Brexit, and how those risks might affect the Bank's financial resources or ability to continue operations over a period of at least a year from the date of approval of the financial statements. There are three areas of risk: the Bank's regulatory capital position and the impact of the level of future credit provisions; that the funding model of the Bank is concentrated and dependent on its principal shareholder Libyan Foreign Bank, and its shareholder the Central Bank of Libya	**Our procedures over the Bank's capital position included:** **Evaluating directors' assessment:** by evaluating their analysis of the Bank's capital position; **Enquiry of the regulator:** Meeting with the Prudential Regulatory Authority (PRA) to discuss its views on the Bank's current and future capital positions, proposed plans and use of buffers; **Our sector experience:** Using our banking and capital knowledge to assess the calculations prepared as part of management's analysis; **Evaluating directors' plans:** Evaluating the achievability of the actions the Directors consider they would take to improve the position; **Assessing transparency:** Considering the adequacy of disclosures relating to going concern in the financial statements. **Our procedures over the Bank's funding concentration included:** **Evaluating directors' assessment**: by evaluating their analysis of the Bank's liquidity and funding; **Our experience:** Applying our knowledge of the Bank's business and assessing its forecasts and projections, and liquidity requirements, and considering less predictable but realistic second order impacts, such as the impact of Brexit and the possible consequential drop in UK real estate prices which could increase credit losses and reduce the Bank's ability to finance any potential future liquidity gaps by borrowing against this loan book; **Independent research:** Performing independent research on recent political and economic developments in Libya;

and their future funding is uncertain; and the Bank has a concentrated number of relationships with counterparty banks and these facilities are critical to its operations such that, should any of these key relationships be ended, this may cause difficulties for the Bank to continue operating under its current business model.

The risk for our audit is whether or not one or more of those risks are such that they amount to a material uncertainty that may cast significant doubt about the ability to continue as a going concern. If so, that fact is required to be disclosed, as has been done in respect of the regulatory capital and credit exposure, and, along with a description of the circumstances, is a key financial statement disclosure.

Stress testing: With the assistance of our own liquidity specialists, independently performing stress testing;

Enquiry of the regulator: Meeting with the Prudential Regulatory Authority (PRA) to discuss its views and insights on the Bank;

Assessing transparency: Considering the adequacy of disclosures relating to going concern in the financial statements.

Our procedures over the Bank's counterparty banks included:

Evaluating directors' assessment: by evaluating their analysis of the Bank's counterparty bank position;

Reviewing regulatory correspondence: Reviewing correspondence between the Bank and the PRA to identify any matters arising;

Enquiry of Directors: Meeting with the Directors and enquiring about the status of the counterparty bank relationships;

Enquiry of the regulator: Meeting with the Prudential Regulatory Authority (PRA) to discuss its views and insights on the Bank;

Assessing transparency: Considering the adequacy of disclosures relating to going concern in the financial statements.

Our results

We found the disclosures of no material uncertainty as relates to the Bank's funding concentration and counterparty banks, and of a material uncertainty as relates the Bank's capital position to be acceptable.

3. OTHER KEY AUDIT MATTERS: INCLUDING OUR ASSESSMENT OF RISKS OF MATERIAL MISSTATEMENT

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. Going concern is a significant key audit matter and is described in section 2 of our report. We summarise below the other key audit matters in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	THE RISK	OUR RESPONSE
The impact of uncertainties due to the UK exiting the European Union on our audit **Refer to pages 1.21-1.26 (Principal Risks)**	**Unprecedented levels of uncertainty** All audits assess and challenge the reasonableness of estimates, in particular as described in Impairment loss provisions below, and related disclosures and the appropriateness of the going concern basis of preparation of the financial statements (see above). All of these depend on assessments of the future economic environment and the Bank's future prospects and performance. Brexit is one of the most significant economic events for the UK and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes, with the full range of possible effects unknown.	**We developed a standardised firm-wide approach to the consideration of the uncertainties arising from Brexit in planning and performing our audits. Our procedures included:** **Our Brexit knowledge:** We considered the directors' assessment of Brexit-related sources of risk for the Bank's business and financial resources compared with our own understanding of the risks. We considered the directors' plans to take action to mitigate the risks. **Sensitivity analysis:** When addressing Impairment loss provisions and other areas that depend on forecasts, we compared the directors' analysis to our assessment of the full range of reasonably possible scenarios resulting from Brexit uncertainty and, where forecast cash flows are required to be discounted, considered adjustments to discount rates for the level of remaining uncertainty. **Assessing transparency:** As well as assessing individual disclosures as part of our procedures on funding concentration and loan impairment allowances we considered all of the Brexit related disclosures together, including those in the strategic report, comparing the overall picture against our understanding of the risks.

Our results

As reported impairment loss provisions, we found the resulting estimates and related disclosures of impairment loss provisions and disclosures in relation to going concern to be acceptable. However, no audit should be expected to predict the unknowable factors or all possible future implications for a company and this is particularly the case in relation to Brexit.

Impairment loss provisions

(£92.2 million; 2017: £48.8 million)

Refer to page 2.15 (accounting policy) and page 2.49 (financial disclosures).

Subjective estimate

These are judgemental areas due to the level of subjectivity inherent in estimating the recoverability of loan balances. The Bank adopted IFRS 9 Financial Instruments on 1 January 2018.

There is also an incentive on management to influence credit provisioning to fraudulently manipulate earnings.

The Bank has a diverse range of credit exposures. These include a book of longer dated loans to counterparties in the Middle East and North Africa, trade and commodity finance portfolios, and a UK real estate portfolio. The Bank's business model involves the regular extension of credit to counterparties in countries which are subject to increased levels of political and economic instability.

A model is used to calculate the level of expected credit losses and the model is reliant on certain subjective assumptions. The model is sensitive to changes and movements in these assumptions.

Our procedures included:

Control design: Testing the design and operating effectiveness of key controls over the monitoring and reporting of loans and advances, and the completeness of provisioning watchlists;

Independent evaluation: Undertaking a detailed assessment of a selection of exposures for indicators of credit deterioration;

Reperformance: Reperforming calculations and agreeing data inputs to third party documentation, including collateral valuation reports;

Our entity experience: Critically assessing and challenging the assumptions used by the Bank in its impairment models, including considering varying the quantum of assumptions, using our understanding of the Bank, current and past performance of its loans and our knowledge of the industry in respect of similar loan types;

Our sector experience: Evaluating the appropriateness of the criteria for determining the stages of impairment using our knowledge of the industry;

Financial risk modelling expertise: Involving our own specialists to assist in evaluating the accuracy of the IFRS 9 models;

Our results

We found the ECL charge and provision recognised to be acceptable.

4. OUR APPLICATION OF MATERIALITY AND AN OVERVIEW OF THE SCOPE OF OUR AUDIT

Materiality for the financial statements as a whole was set at £736 thousand (2017: £405 thousand), determined with reference to a benchmark of normalised profit before tax, normalised to exclude the review of historic activities as disclosed in note 12 and by averaging over the last three years on an absolute basis, due to fluctuations in the business cycle, of £14.7 million (2017: £8.1 million), of which it represents 5% (2017: 5%).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £37 thousand (2017: £20 thousand), in addition to other identified misstatements that warranted reporting on qualitative grounds.

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

5. WE HAVE NOTHING TO REPORT ON THE STRATEGIC REPORT AND THE DIRECTORS' REPORT

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

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

- we have not identified material misstatements in those reports;
- in our opinion the information given in the strategic report and the directors' report for the financial year is consistent with the financial statements; and
- in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. WE HAVE NOTHING TO REPORT ON THE OTHER MATTERS ON WHICH WE ARE REQUIRED TO REPORT BY EXCEPTION

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

- adequate accounting records have not been kept by the Bank, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

7. RESPECTIVE RESPONSIBILITIES

DIRECTORS' RESPONSIBILITIES

As explained more fully in their statement set out on page 1.32, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

AUDITOR'S RESPONSIBILITIES

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

A fuller description of our responsibilities is provided on the FRC's website at:
www.frc.org.uk/auditorsresponsibilities.

IRREGULARITIES – ABILITY TO DETECT

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

The potential effect of these laws and regulations on the financial statements varies considerably.

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

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

Through our audit procedures we became aware that, without accepting liability, the Bank has agreed a settlement payment with the United States regulatory authorities as described more fully by the directors in Note 32.

Other than this matter the limited procedures described above did not identify actual or suspected non-compliance.

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

8. THE PURPOSE OF OUR AUDIT WORK AND TO WHOM WE OWE OUR RESPONSIBILITIES

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

DAVID TODD
Senior Statutory Auditor
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square, London, E14 5GL
26 June 2019

STATEMENTS OF

COMPREHENSIVE INCOME
FINANCIAL POSITION
CHANGES IN EQUITY
CASH FLOW

AND NOTES TO THE ACCOUNTS

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018	2017
Interest and similar income	8	81,564	*61,614*
Less: Interest expense and similar charges	8	(44,358)	*(33,196)*
Net interest income		**37,206**	***28,418***
Fee and commission income	9	22,667	*15,609*
Less: Fee and commission expense	9	(372)	*(325)*
Net fee and commission income		**22,295**	***15,284***
Net trading income	10	5,358	*4,730*
Other operating income	11	(23)	*4,964*
Operating income before allowance for credit losses		**64,836**	***53,396***
Allowance for credit losses	13	(59,043)	*(10,131)*
Net operating income		**5,793**	***43,265***
Administrative expenses	12	(38,018)	*(36,000)*
Regulatory charge	32	(3,141)	*-*
(Loss) / profit before income tax		**(35,366)**	***7,265***
Income tax credit / (charge)	14	58	*(440)*
(Loss) / profit for the year		**(35,308)**	***6,825***
Other comprehensive income/(expense):			
Items that will not be reclassified to profit or loss			
Remeasurement of defined benefit liability	25	(1,075)	*1,277*
Related Tax	14	183	*(217)*
Equity investments designated at fair value through other comprehensive income	15	(928)	*-*
Related Tax	14	177	*-*
		(1,643)	*1,060*
Items that are or may be reclassified to profit or loss			
Change in fair value of available for sale financial assets		-	*5,137*
Fair value gains attributable to available for sale financial assets transferred to income		-	*(4,587)*
Related Tax	14	-	*5*
Change in fair value for debt securities designated at fair value through other comprehensive income		(5,950)	*-*
Expected credit loss on debt securities recognised in the income statement		445	*-*
Fair value gains attributable to debt securities transferred to income		373	*-*
Related Tax	14	1,085	*-*
		(4,047)	*555*
Other comprehensive (loss) / gain for the year, net of tax		**(5,690)**	***1,615***
Total comprehensive (loss) / gain for the year		**(40,998)**	***8,440***

All of the profit for the financial year and the prior year was derived from continuing activities. The Notes on pages 37 to 104 form part of these financial statements.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2018

	Note	2018	*2017*
Assets			
Cash, notes and coins		110	*143*
Financial investments	15	1,774,166	*788,066*
Loans and advances to banks	16	997,428	*1,017,510*
Loans and advances to customers	17	1,081,161	*1,068,589*
Property, plant and equipment	19	8,378	*8,291*
Intangible assets	19	10,954	*6,796*
Derivatives	20	1,249	*547*
Corporation tax receivable		677	*-*
Deferred tax assets	24	2,914	*341*
Prepayments, accrued income and other debtors	21	16,815	*62,573*
Total assets		**3,893,852**	***2,952,856***
Liabilities			
Deposits from banks	22	3,047,548	*2,095,638*
Other deposits	22	585,058	*555,556*
Other liabilities, accruals and deferred income	23	16,044	*10,019*
Derivatives	20	1,119	*1,271*
Corporation tax payable		-	*339*
Net pension liability	25	584	*898*
Subordinated liabilities	26	75,321	*72,302*
Total liabilities		**3,725,674**	***2,736,023***
Called up share capital	27	104,357	*104,149*
Capital redemption reserve	28	4,104	*4,104*
Other reserves	28	59,717	*108,580*
Capital and reserves attributable to the Bank's equity holders	28	**168,178**	***216,833***
Total liabilities and equity		**3,893,852**	***2,952,856***

The Notes on pages 37 to 104 form part of these financial statements.

Signed:

Mr M Stevenson
Chairman

Mr M Shokri
Vice Chairman

Mrs S Aliker
Chief Executive

26 June 2019

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2018

	Share capital	Capital redemption reserve	Other reserves			Total equity
			Retained earnings	Fair Value reserve	Total	
Balance at 31 December 2016	***104,149***	***4,104***	***98,976***	***1,164***	***100,140***	***208,393***
Profit for the year	-	-	*6,825*	-	*6,825*	*6,825*
Other comprehensive (loss)	-	-	*1,060*	*555*	*1,615*	*1,615*
Balance at 31 December 2017	**104,149**	**4,104**	**106,861**	**1,719**	**108,580**	**216,833**
Changes on initial application of IFRS 9:						
- Adjustment to impairments	-	-	(7,447)		**(7,447)**	**(7,447)**
- DTA impact	-	-	1,288		**1,288**	**1,288**
Restated balance as at 1st Jan 2018	**104,149**	**4,104**	**100,702**	**1,719**	**102,421**	**210,674**
Loss for the year	-	-	(35,308)	-	(35,308)	(35,308)
Other comprehensive income	-	-	(892)	(4,798)	(5,690)	(5,690)
Total comprehensive income for the period	-	-	(36,200)	(4,798)	(40,998)	(40,998)
Transactions with owners, recorded directly in equity						
Issue of ordinary shares	208	-	(208)	-	(208)	-
Dividends	-	-	(1,498)	-	(1,498)	(1,498)
Total contributions by and distributions to owners	**208**	**-**	**(1,706)**	**-**	**(1,706)**	**(1,498)**
Balance at 31 December 2018	**104,357**	**4,104**	**62,796**	**(3,079)**	**59,717**	**168,178**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

STATEMENT OF CASH FLOW

FOR THE YEAR ENDED 31 DECEMBER 2018

	Note	2018	*2017*
Cash flows from operating activities			
(Loss)/profit before taxation		(35,366)	*7,265*
Adjustments for:			
Allowance for credit losses	13	59,043	*10,131*
Profit on realisation of equity shares and investments	15	-	*-*
Depreciation and amortisation	12,19	1,024	*1,401*
Loss on sale or impairment of property, plant and equipment	12	1,101	*665*
Other non-cash items included in net profit	12	1,731	*(748)*
Non-cash items included in net profit		**62,899**	***11,449***
Loans, advances and other debt securities other than cash and cash equivalents		263,435	*(672,228)*
Other debtors and prepayments		41,805	*(51,334)*
Change in operating assets		**305,240**	***(723,562)***
Customer accounts and deposits by banks		839,143	*144,902*
Other liabilities		8,238	*(1,338)*
Change in operating liabilties		**847,381**	***143,564***
Income tax received/(paid)		(782)	*1,774*
Net cash (used in)/generated from operating activities		**1,179,372**	***(559,510)***
Cash flows from investing activities			
Proceeds of redemptions of equity shares and investments	15	-	*206*
Purchase/disposal of property, plant and equipment	19	(644)	*(472)*
Purchase of intangible assets	19	(5,744)	*(3,477)*
Net cash used in investing activities		**(6,388)**	***(3,743)***
Cash flows from financing activities			
Dividend paid		(1,498)	*-*
Net cash generated from financing activities		**(1,498)**	***-***
Net decrease in cash and cash equivalents		**1,171,486**	***(563,253)***
Cash and cash equivalents at the beginning of the year		625,253	*1,226,225*
Effect of exchange rate change on cash and cash equivalents		24,912	*(37,719)*
Cash and cash equivalents at the end of the year		**1,821,651**	***625,253***
Cash and cash equivalents comprise:			
Cash, notes and coin		110	*143*
Loans and advances to banks of original maturity three months or less		627,016	*588,102*
Loans and advances to non-banks of original maturity three months or less		191,951	*-*
Certificates of deposit and other debt securities of three months original maturity or less		1,002,574	*37,008*
Cash and cash equivalents		**1,821,651**	***625,253***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2018

1. General information

British Arab Commercial Bank plc ("the Bank" or "BACB") is a public company, limited by shares. The Bank was incorporated in England and Wales on 23 March 1972 as UBAF Limited. The Bank's name was changed to UBAF Bank Limited on 4 January 1977 and to British Arab Commercial Bank Limited on 4 March 1996. On 2 June 2009, the Bank was re-registered as a public company, and its name changed to the current style. The Bank's registered office (and principal place of business) is situated in England and is currently at 8-10 Mansion House Place, London EC4N 8BJ.

The Bank carries on the business of international banking. The Bank is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

The financial statements were authorised for issue by the Board of Directors on 26 June 2019.

2. Basis of preparation

a) Going Concern

These financial statements have been prepared on a going concern basis as the directors are satisfied that the Bank has the resources to continue in business for the foreseeable future, being at least the next year.

In making this assessment, the directors have considered a wide range of information relating to present and future conditions. Information relevant to this assessment regarding the Bank's principal activities, strategic direction and challenges and uncertainties are described in the Strategic Report on pages 15-19. This assessment includes a review of current and future projections of profitability, capital resources and liquidity, which the directors have subjected to stress testing.

Libya continues to face significant challenges. The continuing lack of resolution of the situation in Libya presents a degree of risk given the funding model of the Bank, which is concentrated and dependent on its principal shareholder, Libyan Foreign Bank (LFB), and LFB's shareholder, the Central Bank of Libya (CBL). Details of the funding provided by LFB and CBL are set out in Note 34.

LFB's ability to continue to provide funding is potentially dependent on the situation in Libya. The directors have considered the recent escalation of tension in the country. However, the key parties in Libya have co-operated in the production of oil with the proceeds flowing into CBL and LFB, which place deposits with the Bank. The situation remains uncertain, however, and ongoing developments can be negative as well as positive. The greatest risk to the Bank with regard to the Libya situation appears to be either the breakdown of co-operation between the key parties or a sustained worsening of the flow of oil revenues, which could result in a severe reduction in the Bank's funding. Whilst the provision of liquidity has remained steadfast during the period since the current instability commenced in 2011, it does represent a potential uncertainty linked to the ongoing political situation in Libya.

The directors have considered, and are confident of, the Bank's ability to meet repayment of its deposits were the renewal of funding from Libya to reduce materially or cease. This is due to the liquid nature of much of the Bank's asset base and the relatively short-term nature of much of its lending. The Bank's dependency, in this situation, is on key assumptions, most notably around the impact of property prices on its UK real estate lending portfolio as part of which the potential impact of Brexit has been considered, as well as the risk of future credit losses and the Bank's ability to raise new secured funding at a reasonable haircut.

The directors have also considered LFB's intent to continue to support the Bank. Over the years, the directors have received positive assurances and evidence of support from LFB. This has included the provision of additional capital in June 2015 and assurances of the strategic importance of BACB to the country of Libya. The directors remain confident of the ongoing support of their principle Shareholder but do note that LFB this year have stopped providing an annual formal statement to the directors confirming their intent to provide financial support, including meeting the Bank's ongoing liquidity needs for at least the next twelve months. The directors have taken into account (i) LFB's policy towards all of its participations, (ii) the Bank's continuing positive liquidity noting that during the course of the year LFB increased its deposits to BACB and (iii) ongoing discussions with LFB with regards the provision of additional cash collateral to BACB and, in light of the Bank's funding risk, are confident of the Bank's continuing positive liquidity.

The directors have considered the need for counterparty banks to continue to operate with BACB and to provide critical facilities. This review has specifically considered a sector-wide trend in recent years for counterparty banks to review such relationships due to the potential reputational and legal risks associated with clearing transactions initiated by other banks, particularly those who operate with clients linked to countries perceived as higher risk. The directors acknowledge the dependency of the Bank on preserving these essential correspondent banking relationships and the Board is reassured by the continuing stability of the Bank's principal correspondent and the stability of other counterparty bank relationships.

In addition, as described in note 29 and the Strategic Report (page 16) the Bank did not meet its regulatory capital headroom limits at 31 December 2018 due to significant increases in credit provisions.

Over the period since the year end the directors have carefully managed the capital requirements of new risk weighted assets that the Bank has entered into. The capital position at the date of signing of the accounts has improved materially and (unaudited) analysis indicates that headroom is now within all regulatory requirements. The directors have stressed the future business performance and credit provision scenarios and based on this analysis, within the background of the broader business risks discussed above, have a reasonable expectation that, with on-going careful management of the capital requirements of new risk weighted assets entered into by the Bank, the capital can be maintained at a level in accordance with all current regulatory requirements. However, as set out in the Strategic Report (page 16) the Bank has a number of loans where the ultimate levels of recovery have a high degree of estimation uncertainty. The directors have estimated the recoverable amounts under these loans and considered reasonable stresses, but because of the estimation uncertainty there is a materially wide range of possible outcomes. If ultimately the amounts recovered are less than those estimated, this would further reduce the regulatory capital position and if severe could lead to the Bank being unable to meet the threshold criteria to the satisfaction of the PRA which is essential in order for the bank to be permitted to trade. The directors note that the capital position of the Bank, combined with the risk of future credit provisions, constitutes a material uncertainty which may cast significant doubt on the Bank's ability to continue as a going concern and, therefore, to continue realising its assets and discharging its liabilities in the normal course of business. The financial statements do not include any adjustments that would result from the basis of preparation being inappropriate.

b) Compliance with International Financial Reporting Standards

The Bank has prepared its financial statements in accordance with IFRS as adopted by the EU (Adopted IFRS) and effective for the Bank's reporting for the year ended 31 December 2018. IFRS comprise accounting standards issued by the International Accounting Standards Board (IASB) and its predecessor body or adopted as interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) and its predecessor body.

The financial statements have been prepared in the Bank's functional and presentation currency, Sterling, rounded to the nearest thousand. They are prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments, financial instruments held at fair value through the profit and loss account, financial instruments held at fair value through other comprehensive income and the defined benefit pension fund.

The preparation of financial statements in conformity with Adopted IFRS requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. The results form the basis for making judgements about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of Adopted IFRS that have a significant effect on the financial statements and estimates with a significant risk of material adjustment in the next year are discussed in Note 5.

c) Accounting Standards adopted during the year

The Bank has initially adopted IFRS 9 and IFRS 15 from 1 January 2018. Due to the transition method chosen by the Bank in applying IFRS 9, comparative information throughout these financial statements has not been restated to reflect its requirements and is reported under IAS 39. The Bank's accounting policies under IAS 39 can be seen in the 2017 Annual Report and Financial Statements.

The adoption of IFRS 15 did not impact the timing or amount of fee and commission income from contracts with customers and the related assets and liabilities recognised by the Bank. Accordingly, the impact of the comparative information is limited to new disclosure.

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

- an increase in impairment losses recognise on financial assets (see Note 6);
- additional disclosures related to IFRS 9 (see Notes 3, 6 and 13); and
- additional disclosures related to IFRS 15 (see Note 3).

Except for the changes below, the Bank has consistently applied the accounting policies as set out in Note 3 to all periods presented in these financial statements.

IFRS 9 Financial Instruments

This Standard forms part of the International Accounting Standard Board’s project to replace the existing standard (IAS 39) on the recognition and measurement of financial instruments, and includes requirements for the classification and measurement of financial assets and liabilities, impairment of financial assets and hedge accounting.

Differences in the carrying amounts of financial assets and liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

Classification and measurement
IFRS 9 requires all financial assets to be classified and measured on the basis of the entity’s business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. The Standard also differs from previous requirements for accounting for financial assets in various other areas, such as embedded derivatives and the recognition of fair value adjustments in the Statement of Other Comprehensive Income (OCI).

Impairment

The expected credit loss model applies to all financial assets measured at amortised cost and FVOCI, and certain loan commitments and financial guarantee contracts. Under this approach, (i) if there has been a significant increase in credit risk, lifetime expected credit losses would be recognised, or (ii) if there has not been significant credit deterioration, a 12-month expected credit loss is recognised. Financial assets where there has not been a significant increase in credit risk are in 'stage 1'; financial assets that are considered to have experienced a significant increase in credit risk since initial recognition are in 'stage 2'; and financial assets which are credit impaired are in 'stage 3'. The assessment of credit risk and estimation of expected credit losses (ECL) are required to be unbiased and probability-weighted, incorporating all available information relevant to the assessment. The estimation of ECL also takes into account the time value of money. Moving from an incurred loss approach to an expected loss approach has required management to incorporate forward-looking information into the Bank's impairment models.

Hedge accounting

IFRS 9 also includes revised requirements on hedge accounting which attempt to more closely align an entity's risk management strategies and risk management objectives. The IASB is working on a separate project to address the accounting for open portfolios. Until this project is complete the Bank will continue to apply IAS 39 hedge accounting.

Transitional impact

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below:

i. Loans and receivables to banks and to customers that were classified as loans and receivables under IAS 39 are measured at amortised cost under IFRS 9;
ii. Financial assets designated at fair value through profit and loss (FVTPL) continue to be classified at FVTPL under IFRS 9;
iii. Debt securities classified as available for sale under IAS 39 are measured at fair value through OCI (FVOCI) under IFRS 9;
iv. Equity investments classified as available for sale under IAS 39 are measured at FVOCI under IFRS 9. Although equity investments fail the solely payments of principal and interest test (SPPI test), meaning that they need to be measured at FVTPL, the Bank has taken the option within IFRS 9 to make an irrevocable election to classify as FVOCI.

IFRS 15 Revenue from Contracts with Customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaces existing revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes. The Standard had an effective date of 1 January 2018, and has been applied retrospectively, with no impact to existing revenue recognition.

d) Future developments in Accounting Standards

IFRS 16 Leases

IFRS 16 sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer (lessee) and the supplier (lessor). The new standard introduces a single lessee accounting model and requires lessees to recognise a right of use ('ROU') asset, which is amortised over the length of the lease, and a corresponding financial liability, which is measured at amortised cost. Lessor accounting remains substantially the same as under IAS 17.

The changes introduced by the new standard impact the accounting treatment of the leasehold land at the Bank's main office and the leases for the office facilities used by the Bank's overseas representative offices. The Bank has adopted the standard using the modified retrospective approach whereby the Bank recognises a lease liability, being the present value of the remaining lease payments, and a ROU asset, which is based on the lease liability adjusted by prepaid or accrued lease payments. The increase in the balance sheet as result of the recognition of the lease liability and ROU asset as at 1 January 2019 will be approximately £4m, however the actual impact may change as judgements and estimates are refined.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to both years presented in these financial statements, except where changed as a result of the adoption of new accounting standards as discussed below.

a) Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised in the income statement using the effective interest rates of the financial assets or financial liabilities to which they relate. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability.

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

Interest received on securities held for dealing purposes, and associated funding costs, are included within Interest and similar income, and Interest expense and similar charges, respectively.

b) Fee and commission income

The Bank earns fee income from a range of services which it provides to its customers. Fee income is accounted for as follows:

i. income earned on transaction-based arrangements which are recognised at a point in time when we have fully provided the service to the customer (for example, fees arising from negotiating, or participating in the negotiation of, a transaction for a third party, such as the arrangement for the acquisition of securities);
ii. income earned on services provided over time, where the income is recognised on a systematic basis over the life of the agreement; and
iii. income which is an integral part of the effective interest rate of a financial instrument and is recognised as an adjustment to the effective interest rate (for example, loan origination fees) and recorded in interest income (See Note 3a).

The Bank provides certain guarantee facilities which are dependent on uncertain future events. These facilities include surety, fidelity, performance, bid and advance payment bonds. For the majority of these transactions the guarantees given by the Bank are covered by matching counter-indemnities provided by a third party. Fees and commissions arising from the provision of such services are recognised over the period for which the service is provided.

c) Foreign currencies

The directors regard Sterling as the currency of the primary economic environment in which the Bank operates. Accordingly, Sterling is regarded as being the functional currency of the Bank and is also the reporting currency of the Bank.

Transactions in foreign currencies are recorded in Sterling at the rate of exchange prevailing on the date on which the transaction arose. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the balance sheet date. Any resulting exchange differences are included in the income statement or, for FVOCI assets, in other comprehensive income. Non-monetary assets and liabilities (shareholders' equity, property plant and equipment, and intangible assets) that are measured in terms of historical cost in a foreign currency are translated into the functional currency using the rate of exchange at the date of the initial transaction.

d) Net trading income

Net trading income comprises gains, less losses related to financial assets designated at fair value through profit and loss, and includes all realised and unrealised fair value changes and foreign exchange differences.

e) Income tax

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

Current tax is the tax expected to be payable or receivable on the taxable profit or loss for the year, calculated using tax rates enacted or substantially enacted by the balance sheet date, and any adjustment to tax payable in respect of previous years. Current tax assets and liabilities are offset when the Bank intends to settle on a net basis and the legal right to set off exists.

Deferred tax is recognised on temporary differences between the carrying amount of assets and liabilities in the statement of financial position and the amount attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent it is probable that future taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax is calculated using the tax rates expected to apply in the years in which the assets will be realised or the liabilities settled.

Deferred tax relating to actuarial gains and losses arising from defined benefit pension plans are recognised in other comprehensive income.

Deferred tax relating to fair value re-measurement of available-for-sale investments is recognised in other comprehensive income and, subsequently, in the income statement when the related investment is realised.

f) Derivatives and hedge accounting

Derivatives held for risk management purposes include all derivative assets and liabilities that are not classified as trading assets or liabilities. Derivatives are measured at fair value in the statement of financial position.

Hedge accounting

The Bank designates certain derivatives held for risk management as hedging instruments in qualifying hedging relationships. On initial designation of the hedge, the Bank formally documents the relationship between the hedging instrument(s) and hedged item(s), including the risk management objective and strategy in undertaking the hedge, together with the method that will be used to assess the effectiveness of the hedging relationship. The Bank makes an assessment, both at inception of the hedge relationship and on an ongoing basis, of whether the hedging instrument(s) is (are) expected to be highly effective in offsetting the changes in the fair value of the respective hedged item(s) during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80–125%.

There were no contracts designated as hedging instruments as at 31 December 2018.

Fair value hedges

When a derivative is designated as the hedging instrument in a hedge of the change in fair value of a recognised asset or liability or a firm commitment that could affect the income statement, changes in the fair value of the derivative are recognised immediately in the income statement in Interest and similar income, together with changes in the fair value of the hedged item that are attributable to the hedged risk.

If the hedging derivative expires or is sold, terminated or exercised, or the hedge no longer meets the criteria for fair value hedge accounting, or the hedge designation is revoked, then hedge accounting is discontinued prospectively. However, if the derivative is novated to a central counterparty by both parties as a consequence of laws or regulations without changes in its terms except for those that are necessary for the novation, then the derivative is not considered as expired or terminated.

Any adjustment up to the point of discontinuation to a hedged item for which the effective interest method is used is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

X-Valuation Adjustment ('XVA')

XVA fair value adjustments comprise Credit Valuation Adjustments ("CVA"), Debt Valuation Adjustments ("DVA") and Funding Valuation Adjustments ("FVA"). CVA is the mark to market cost of protection required to hedge credit risk from counterparties in the Bank's derivative and repo portfolios, and depends on expected and potential future exposures, default probability and recovery rates. DVA is taken to reflect the credit quality of the Bank in the valuation of liabilities measured at fair value, and is measured symmetrically to the CVA on the same products and calculation methodologies, based on the negative potential and expected exposures and the Company's own creditworthiness. FVA measures the impact to funding for valuation estimates for derivatives.

The Bank monitors derivative and repo portfolios, and based upon the credit quality of counterparties, and the short term maturity profile of contracts has concluded that applicable XVA is immaterial.

g) Financial assets

The Bank has classified its financial assets in the following categories: financial assets at fair value through profit or loss, financial assets through other comprehensive income and financial assets at amortised cost. Management determined the classification of its investments on adoption of IFRS 9.

i. Financial assets at amortised cost

Financial assets at amortised cost consist of those where both of the following conditions are met:
a) The contractual terms of the contract give rise on specific dates to cash flows that are solely payments of principal and interest on the principal outstanding and
b) The financial asset is held within a business model whose objective is to hold the asset in order to collect contractual cash flows.

ii. Financial assets at fair value through other comprehensive income

Financial assets at fair value through other comprehensive income consist of those where both of the following conditions are met:
a) The contractual terms of the contract give rise on specific dates to cash flows that are solely payments of principal and interest on the principal outstanding and
b) The financial asset is held within a business model whose objective is achieved by both collecting the contractual cash flows and selling the financial assets.

The Bank has taken the irrevocable election to classify equity investments at fair value through other comprehensive income.

iii. Financial assets at fair value through profit and loss

This category comprises which do not fall into either of the above categories.

2017 accounting policy under IAS 39

The Bank has classified its financial assets in the following categories: financial assets at fair value through profit or loss; loans and receivables and available-for-sale financial assets. Management has determined the classification of its investments on adoption of IFRS, and thereafter on initial recognition.

i. Financial assets at fair value through profit and loss

This category comprises three sub-categories:

- financial assets held for trading;
- financial assets designated at fair value through profit and loss at inception as part of a fair value hedge;
- derivatives

ii. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term. They arise when the Bank provides money, goods or services to a debtor with no intention of trading the receivable.

iii. Available-for-sale

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

h) Fair value measurement

Derivatives

Derivatives are recognised on trade date, being the date on which an irrevocable commitment to enter into a contract is executed. They are subsequently carried at fair value. Fair values are obtained from quoted market prices in active markets, or by using valuation techniques, including recent market transactions, where an active market does not exist. Valuation techniques include discounted cash flow models and option pricing models as appropriate. All derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative.

In the normal course of business, the fair value of a derivative on initial recognition is considered to be the transaction price (i.e. the fair value of the consideration given or received). However, in certain circumstances the fair value of an instrument will be evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets, including interest rate yield curves, option volatilities and currency rates. When such evidence exists, the Bank recognises a trading profit or loss on inception of the derivative. If observable market data is not available, the initial increase in fair value indicated by the valuation model, but based on unobservable inputs, is not recognised immediately in the income statement but is recognised over the life of the transaction on an appropriate basis, or recognised in the income statement when the inputs become observable, or when the transaction matures or is closed out.

Financial assets

Loans are recognised when cash is advanced to the borrowers. Purchases and sales of financial assets which are fair value through profit and loss or fair value through other comprehensive income are recognised on trade date, being the date on which an irrevocable commitment to enter into a contract is executed. Financial assets are initially recognised at fair value plus directly attributable transaction costs for all financial assets not carried at fair value through profit or loss. Loans and advances are subsequently carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are included in the income statement in the year in which they arise. Gains and losses arising from changes in financial assets at fair value through other comprehensive income are recognised in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity is recognised in profit and loss. However, interest calculated using the effective interest method is recognised in the income statement. Dividends on available-for-sale equity instruments are recognised in the income statement when the Bank's right to receive payment is established.

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Bank establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

2017 accounting policy under IAS 39

Derivatives

Derivatives are recognised on trade date, being the date on which an irrevocable commitment to enter into a contract is executed. They are subsequently carried at fair value. Fair values are obtained from quoted market prices in active markets, or by using valuation techniques, including recent market transactions, where an active market does not exist. Valuation techniques include discounted cash flow models and option pricing models as appropriate. All derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative.

In the normal course of business, the fair value of a derivative on initial recognition is considered to be the transaction price (i.e. the fair value of the consideration given or received). However, in certain circumstances the fair value of an instrument will be evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets, including interest rate yield curves, option volatilities and currency rates. When such evidence exists, the Bank recognises a trading profit or loss on inception of the derivative. If observable market data is not available, the initial increase in fair value indicated by the valuation model, but based on unobservable inputs, is not recognised immediately in the income statement but is recognised over the life of the transaction on an appropriate basis, or recognised in the income statement when the inputs become observable, or when the transaction matures or is closed out.

Financial assets

Purchases and sales of financial assets which are available-for-sale are recognised on settlement date, being the date on which the Bank makes payment to receive the asset. Loans are recognised when cash is advanced to the borrowers. Financial assets are initially recognised at fair value plus directly attributable transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets at fair value through profit and loss are recognised on trade date, being the date on which an irrevocable commitment to enter into a contract is executed.

Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are carried at amortised cost using the effective interest method.

Gains and losses arising from changes in the fair value of the "financial assets at fair value through profit or loss" category are included in the income statement in the year in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised in income to the extent that the change in value arises from a fair value hedging relationship with the balance recognised directly in equity, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in equity is recognised in profit and loss. However, interest calculated using the effective interest method is recognised in the income statement. Dividends on available-for-sale equity instruments are recognised in the income statement when the Bank's right to receive payment is established.

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Bank establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants.

i) Offsetting financial instruments

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

j) De-recognition of financial assets and liabilities

Financial assets are de-recognised when the rights to receive cash flows from the assets have expired; or where the Bank has transferred its contractual right to receive the cash flows of the financial assets and either:

- substantially all the risks and rewards of ownership have been transferred;
- substantially all the risks and rewards have neither been retained nor transferred but control is not retained; or
- the asset has been substantially modified, so that an old asset is derecognised and a new one recognised in its place.

On de-recognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss. Any interest in transferred financial assets that qualify for de-recognition that is created or retained by the Bank is recognised as a spate asset or liability.

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

Financial liabilities are de-recognised when they are extinguished, i.e. when the obligation is discharged or cancelled or expired.

k) Impairment of financial assets

The Bank recognises impairment allowances for ECL on the following financial instruments that are not measured at FVTPL:

- lending exposures including funded Trade Finance exposures and reportable undrawn commitments;
- debt instruments held for liquidity purposes;
- money market deposits and placements classified as loans and advances at amortised cost; and
- letters of credit and guarantees offered by the Bank.

No impairment loss is recognised on equity investments, debt securities held for trading and derivatives held at FVTPL.

12 month ECL is the portion of ECL that results from default events on financial instruments that are possible within the 12 months after the reporting date. Financial instruments for which a 12-month ECL is recognised are referred to as '**Stage 1 financial instruments**'.

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

Measurement of ECL

ECL is a probability weighted estimate of credit losses. It is measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls, i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive over the shorter of 12 months or the period to maturity;
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive over the shorter of 12 months or or the period to maturity; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover over the shorter of 12 months or the period to maturity.

The recognition and measurement of ECL is highly complex and involves the use of significant judgement and estimation, which include the formulation and incorporation of forward looking probability weighted scenarios into the calculation of ECL. Scenarios used for IFRS 9 are formally reassessed periodically, and at least quarterly, for continued appropriateness and to ensure the scenarios are unbiased and meet the requirements of IFRS 9. The Bank uses three economic scenarios which represent the most likely outcome, referred to as the 'BAU scenario', and two less likely scenarios, referred to as 'optimistic' and 'downturn' scenarios. The probability weighting for each scenario is based on the geographic area of the underlying exposure and, depending on the specific geography of the exposure, falls within the following ranges for each of the scenarios:

- BAU – 70-85%
- Optimistic – 0-5%
- Downturn – 10-25%

The probability weightings are determined by management using where available external, independent forecasts and information. Under normal economic circumstances it is expected that the substantial majority of the probability weightings will be in the BAU category, with much smaller weightings applied to the optimistic and downside scenarios. However greater weighting may be given to the downturn scenario in periods of economic stress.

The conditions which exist under the BAU scenario are based on current economic forecasts, with the downside scenario based on a projected period of Global economic recession and the upside based on a period of Global economic growth, with each of the scenarios updated for specific events or factors which would impact the Banks credit exposures. During 2019 we adjusted the scenarios for a number of current economic impacts. These included: Brexit; political and economic developments in North Africa, the Middle East and Turkey; and potential conflicts between the United States and its trade partners.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised and ECL is measured as follows:

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset; and
- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

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

Evidence that a financial asset is credit impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the client on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.
- the purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses.

A loan that has been renegotiated due to deterioration in the borrower's condition is usually considered to be credit impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment.

Presentation of allowance for ECL in the statement of financial position

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

- *financial assets measured at amortised cost*: as a deduction from the gross carrying amount of the assets;
- *loan commitments and financial guarantee contracts*: generally, as a provision;
- *where a financial instrument includes both a drawn and an undrawn component, and 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. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- *debt instruments measured at FVOCI:* no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-offs

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

Recoveries of amounts previously written off are included in 'Allowance for credit losses' in the statement of profit or loss and OCI.

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

2017 accounting policy under IAS 39

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or portfolio of financial assets is impaired. A financial asset or a portfolio of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a “loss event”) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or portfolio of financial assets that can be reasonably estimated. Objective evidence that a financial asset or portfolio of assets is impaired includes observable data that comes to the attention of the Bank about the following loss events:

i significant financial difficulty of the issuer or obligor;
ii a breach of contract, such as default or delinquency in interest or principal payments;
iii the Bank granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
iv it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
v the disappearance of an active market for that financial asset because of financial difficulties; or
vi observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:
- adverse changes in the payment status of borrowers in the portfolio; or
- national or local economic conditions that correlate with defaults in the portfolio of assets.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a portfolio of financial assets with similar credit risk characteristics and collectively assesses them for impairment. The Bank also considers whether to make collective provision for impairments that have been incurred but not yet reported.

The Bank closely monitors and actively manages receivables which are not paid on their due date (past due amounts). If the reasons for the delay are indicative of difficulty being experienced by the counterparty, then, even if it is decided not to recognise impairment, all of the balances due from that counterparty will be classified as being on "watch list", resulting in increased management scrutiny and action.

Interest on impaired assets continues to be recognised through the unwinding of the discount.

Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the income statement. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

Loans (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is no realistic prospect of recovery of these amounts and, for collateralised loans, when the proceeds from the realisation of security have been received.

If in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed to the extent it is now excessive by reducing the loan impairment allowance account. The amount of any reversal is recognised in the income statement.

Available-for-sale assets

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or a portfolio of financial assets is impaired. For investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss, measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss, is removed from equity and recognised in the income statement.

l) Reverse repos

Securities purchased under commitments to resell ("reverse repos") are not recognised on the balance sheet. Rather, a loan receivable is recorded in respect of the initial consideration paid. Non trading reverse repos are measured at amortised cost. The difference between the purchase and resale price is treated as interest and recognised in net interest income over the life of the agreement.

m) Property, plant and equipment

Property, plant and equipment are stated at cost less depreciation calculated on a straight line basis to write off the assets over their estimated useful lives as follows:

Long leasehold premises and improvements	
Leasehold improvements	10 years
Leasehold premises	50 years
Other assets	
Equipment	3 or 5 years
Motor vehicles	5 years
Furniture, fixtures and fittings	10 years

Leasehold premises and leasehold land comprise the Bank's principal office at 8-10 Mansion House Place, London, EC4N 8BJ. The premises, but not the land, are categorised as a finance lease, capitalised and depreciated over 50 years. All property plant 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. All other repairs and maintenance are charged to the income statement during the financial year in which they are incurred. The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date.

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 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. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Gains and losses on disposals are included in the income statement.

n) Intangible assets

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software, including directly incurred internal costs. Costs associated with maintaining computer software programs are recognised as an expense as incurred.

The capitalised cost of computer software is amortised over either 3 or 5 years, or the remaining term of the software licence, from the date on which it is available for use. 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 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. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use. Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

o) Leases

Lease agreements which transfer substantially all the risks and rewards of the ownership of assets are classified as finance leases and all other lease agreements are classified as operating leases. The Bank's lease agreements relate to its main office at 8-10 Mansion House Place, London EC4N 8BJ, as well as the rental of office facilities for each of the overseas representative offices. The lease agreement for the main London office whereby the Bank is the lessee is treated as a finance lease in respect of the leasehold premises, but an operating lease in respect of the leasehold land. The Bank also sub-lets a part of the office. This sub-lease agreement, in which the Bank acts as lessor, is classified as an operating lease. The rental agreements for the representative offices are treated as operating leases.

The cost of the finance lease is based upon the lease premium paid upon inception of the lease. The premises element of the premium is capitalised and depreciated over its useful economic life. Impairment testing of the asset is carried out as if the premises were owned by the Bank.

The cost of the leasehold land is based upon the lease premium paid upon inception of the lease. The land element of the premium is charged to profit and loss over the lease term with the amount not yet charged shown as a prepayment. This charge, together with the ground rent charge, is charged within administrative expenses.

The minimum non-cancellable payments and receipts in respect of operating leases are disclosed. In respect of payment commitments, these are the minimum ground rent payments due in relation to the Bank's main London office as well as that due for each of the representative offices. In respect of receipts from the sub-lessee, these are minimum rent and service charge receipts until the date of the break clause in the sub-lease.

p) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents include unrestricted highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months' maturity from the date of acquisition, and include cash, notes and coin, treasury bills and other eligible bills, professional market placements to banks, amounts held at correspondents and certificates of deposit.

q) Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are determined by discounting the expected future cash flows at a pre-tax discount rate that reflects the current market assessment of the time value of money and, where appropriate, the risks specific to the liability.

r) Contingent liabilities

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably.

Contingent liabilities are not recognised in the financial statements but are disclosed, unless they are remote.

s) Employee benefits

The Bank provides both a defined benefit and a defined contribution pension scheme for its staff. The defined benefit scheme was closed to future accrual in 2014. In each case, the assets of the schemes are held separately from those of the Bank. A defined benefit scheme is a pension plan that defines an amount of pension benefit that an employee will receive on retirement, usually dependent on one or more factors such as age, years of service and compensation. A defined contribution scheme is a pension plan under which the Bank pays fixed contributions into a separate entity, and where the Bank has no legal or constructive obligations to pay further contributions.

The net asset or liability recognised in the statement of financial position in respect of the defined benefit pension plan is the fair value of the plan assets less the present value of the defined benefit obligation at the balance sheet date. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows. The discount rate is the yield at the reporting date on AA credit-rated bonds that have maturity dates approximating the terms of the Bank's obligations.

Actuarial gains and losses arising from experience adjustments and changes in actuarial assumptions are charged or credited to other comprehensive income. Other gains and losses are recognised in the income statement.

For the defined contribution scheme, the Bank pays contributions to the BACB Defined Contribution Retirement Benefit Scheme. The Bank has no further payment obligations once the contributions have been paid. The contributions are recognised as employee benefit expense when they are due. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

t) Share capital

Share issue costs

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

Dividends on ordinary shares

Dividends are recognised in equity in the year in which they are approved by the Bank's shareholders.

Foreign currencies

Share capital is defined as a non-monetary liability (see Note 3c), and is measured in terms of historical cost in a foreign currency as translated into the functional currency using the rate of exchange at the date of the initial transaction.

4. Risk management

a) Risk Management Objectives

The Bank's overarching risk management objectives are to ensure that:

- there is a clearly articulated risk appetite statement which is calibrated to the financial resources of the Bank and its budget aspirations;
- there is a risk culture, which is embedded in daily operational activity;
- risks are identified and accepted within risk appetite, or approved as exceptions where not;
- risks are monitored to ensure they remain within, or come back within, risk appetite in agreed timescales and action is taken promptly and effectively if that is not the case; and

- there is timely, complete, accurate and relevant risk reporting within the Bank and to the Board.

b) Approach to Risk Management

The Bank has adopted a "three lines of defence" model of risk management and control, as summarised below:

- **1st LINE**: Each business area and function within the Bank is responsible for identifying, understanding and managing their risks and maintaining internal controls.
- **2nd LINE**: The second line of defence establishes the policies and tools, as required by the Bank's Governance Standards, to provide the framework for managing each Principal Risk Type and provides oversight and monitoring over the first line risks and controls.
- **3rd LINE**: The third line of defence, comprising Internal Audit, provides independent assurance on the effectiveness of governance, risk management and internal controls, including the manner in which the first and second lines of defence achieve risk management and control objectives.

c) Principal Risks

The Bank's principal risks and uncertainties as at the reporting date are referenced in the Strategic Report on pages 15 - 19 and these risks are each subject to ongoing active review by management and the Board.

The Bank has identified nine Principal Risk Types across three overarching risk categories which might adversely impact its ability to achieve its strategic objectives, and defines its risk appetite through a range of scope and scale measures across these risk types that define the level of acceptable risk.

The summary below outlines the risk categories as currently adopted by the Bank.

Risk Category	Principal Risk Type
Reputational	Reputational Culture and Conduct
Financial	Credit Country Market Liquidity
Operational	Operational Compliance Financial Crime

A brief description of each of the Principal Risk Types and the framework for managing them is set out below.

REPUTATIONAL RISK

Definition:
Reputational Risk is the current and prospective impact on earnings and enterprise value arising from negative stakeholder opinion. Reputational Risk is a threat or danger to the good name or standing of the Bank. It can occur through a number of ways: directly as the result of the actions of the company itself; indirectly due to the actions of an employee or employees; or tangentially through other peripheral parties, such as joint venture partners or suppliers or false rumours. In addition to having good governance practices and transparency, companies also need to be socially responsible and environmentally conscious to avoid Reputational Risk.

BACB has a very limited appetite for Reputational Risk, however it is recognised Reputational Risk cannot be eradicated completely and such risk is inherent within the banking environment and, in particular, in some of the higher risk countries with which BACB does business. It is recognised that Reputational Risk can arise from a wide variety of sources, some controllable, some less so.

Risk Management:
The Bank recognises that some of the countries in which its counterparties operate results in an enhanced exposure to Reputational Risk. As a result its principal defence against Reputational Risk is through adherence to its objectives of operating at all times in conformity with all applicable laws and regulations including sanctions and anti-money laundering requirements. Governance and risk management frameworks are intended to safeguard the Bank from reputational damage that might arise from trading related losses.

Risk Mitigation:
The Bank has implemented a range of initiatives to mitigate its exposure to Reputational Risks. These include:

- strategic alignment including Board oversight, integration of risk management into strategy setting and effective communications and brand building;
- cultural alignment built on corporate values, supported by appropriate performance incentives and a positive culture regarding compliance with laws and regulations;
- quality commitment including a focus on stakeholder interactions and open, transparent and quality public reporting;
- focusing on mainly non-complex products and a wholesale customer base, supported by a new product review and approval process;
- an operational focus on a strong control environment and appropriate organisational resilience;
- a proactive corporate communications strategy designed to safeguard the reputation of the Bank.

Note 32 provides details of the agreed settlement with the U.S. Office of Foreign Assets Control in relation to sanctions.

CULTURE AND CONDUCT RISK

Definition:
Conduct is 'what the Bank does'; and Culture is 'how the Bank does it'.

Conduct Risk is the risk that detriment is caused to the Bank, its customers, clients or counterparties because of the inappropriate execution of its business activities. Conduct Risk comprises a wide variety of activities and types of behaviour which fall outside the other main categories of risk, such as market, credit, liquidity and operational risk. In essence it refers to risks attached to the way in which the Bank and its employees conduct themselves. Although there is no official definition, it is generally agreed to incorporate matters such as how customers are treated, remuneration of employees and how the Bank deals with conflicts of interest.

The Bank's **culture** refers to the shared values, attitudes, standards, and beliefs of the Bank's employees. BACB's culture is rooted in our goals, strategies, structure, and approaches to employee engagement, customers, investors, and the greater community. As such, it is an essential component in any business's ultimate success or failure.

Risk Management:
The Chief Executive Officer has primary responsibility for managing Culture and Conduct Risk. The Bank has established a set of values and behaviours which it expects all staff to display in their interactions with clients, competitors and each other, such behaviours being designed to drive a client-centric business model characterised by the levels of teamwork required to operate as a high performance organisation. These expectations are encapsulated in the Bank's code of conduct 'The BACB Way', to which all staff have been asked to sign up to.

The overall framework for management of this risk is set out in the Culture and Conduct Risk Standard and Policy. Compliance with this Policy is overseen by the Executive Committee of the Bank, with regular (at least bi-annual) reporting to the Board.

Risk Mitigation:

- the Bank conducted a culture survey, the results of which became the basis for 'The BACB Way', our code of conduct;
- the Bank's staff performance appraisal system requires that all staff appraisals include consideration of behaviours and compliance with the Bank's Code of Conduct, which informs in part levels of fixed and variable compensation;
- the Chief Executive Officer carries out a regular risk assessment, which is considered by the Executive Committee and by the Audit and Risk Committee of the Board. Culture and Conduct Risk is a standing agenda item for the Executive Committee;
- Culture and Conduct MI has been developed, which continues to evolve and draws inter alia on Operational Risk, Compliance and HR Metrics; and
- the Nominations and Remuneration Committee of the Board has regard to compliance with the Bank's values and behaviours when assessing the levels of individual compensation for executive management.

CREDIT AND COUNTRY RISKS

Definitions:
Credit Risk is the risk of the Bank suffering financial loss if any of its customers, clients or market counterparties fails to fulfil their contractual obligations to the Bank. The Bank's principal sources of credit risk are:

- exposures to banks, multilateral institutions and sovereigns in respect of foreign exchange and money market activities and the management of the Bank's liquidity portfolios;
- on and off-balance sheet exposures to bank and corporate counterparties in respect of obligations under trade finance transactions including letters of credit, guarantees and bonds; and
- loans and overdrafts to corporates, partnerships and private individuals arising from the Bank's commercial, real estate and commodity finance lending activities.

Country Risk is the risk that obligors may not be able to meet their obligations in a country for a variety of non-obligor specific reasons, including political or economic changes or other actions by a government that may prevent the conversion of local currency into non-local currency and/or the transfer of funds outside the country.

Risk Management:
For the Bank, country risk largely arises as a result of the Bank taking credit risk on borrowers or counterparties outside the UK. Consequently the Bank's risk management of these two risk types is aligned and largely managed alongside and together with each other.

The Bank's appetite for credit and country risks is set in response to its business plans and overall risk appetite. The Chief Risk Officer and his direct report, the Head of Credit, are responsible for:

- development and oversight of the credit and country risk management frameworks;
- developing credit and country risk policies, tools and frameworks across the business, including credit grading systems;
- managing effective credit and country risk assessment strategies and independent challenge of requests from the first line for new, increased or extended limits;
- oversight of credit and country risk activities undertaken by the first line;
- credit reporting and performance monitoring, including stress testing and portfolio modelling; and
- monitoring and managing the Bank's impaired exposures, and making recommendations jointly with the Chief Financial Officer on required levels of individual and collective impairment provisions and write-offs. With effect from 1 January 2018, the above has been carried out in compliance with IFRS 9.

Credit and country risk management is overseen at an executive level by the Credit Risk Committee which reviews and makes recommendations via the Executive Committee to the Audit and Risk Committee at least annually on the Bank's credit and country risk appetite and policies, or approves proposals within delegated authority, having regard to the Bank's business plans and Credit and Country Risk standards as approved by the

Board from time to time. Significant credit decisions are escalated to the Board Credit Committee (previously the External Credit Committee).

Risk Mitigation:

The Bank's strategic focus means that a significant portion of its credit and country risks are towards the lower end of its grading systems. In order to mitigate its credit and country risks the Bank employs a number of risk mitigants:

- a framework of concentration limits and guidelines which diversify the risk of excessive exposure to individual countries, regions or sectors and to individual counterparties within those concentrations;
- limits are established for individual countries and counterparties based on their grading;
- these limits govern quantum, nature and tenor of exposure. Typically the Bank will no longer enter into transactions in excess of one year other than in its real estate activity or for strategic customers or counterparties of appropriate credit quality;
- the Bank takes cash collateral for a significant portion of its exposures and employs other risk mitigants to the extent possible. Other mitigants include back-to-back commitments from financial institutions of acceptable quality, or security;
- liquidity buffers are only used to purchase the securities of OECD governments and multilateral development bank fixed and floating rate securities which qualify as High Quality Liquid Assets under the PRA's Liquidity Coverage Ratio regime; and
- other surplus liquidity is primarily placed with or invested in the bonds of highly rated financial institutions.

Credit risk quantitative disclosures

Credit risk is assessed below using various analyses of the following balances disclosed in these financial statements:

	2018	*2017*
Cash, notes and coins	110	*143*
Financial investments: debt securities (note 15)	1,767,556	*780,528*
Loans and advances to banks (note 16)	997,428	*1,017,510*
Loans and advances to customers (note 17)	1,081,161	*1,068,589*
Derivatives	1,249	*547*
Total on balance sheet	**3,847,504**	***2,867,317***
Financial guarantees (note 30)	122,386	*54,051*
Other commitments (note 30)	556,330	*532,921*
Less: off balance sheet exposures impaired by provision on balance sheet	(2,039)	*(809)*
Total off balance sheet	**676,677**	***586,163***
Total	**4,524,181**	***3,453,480***

The Bank holds collateral against certain of its credit exposures. The table below sets out the principal types of collateral held against different types of financial assets.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Type of credit exposure	Percentage of exposure that is subject to collateral 2018	2017	Principal types of collateral held
On-balance sheet:			
Loans and advances to banks			
Professional market placements	**52.8%**	*2.9%*	Debt securities
Term lending	**20.1%**	*9.4%*	Cash and guarantees
Bills discounted	**9.5%**	*9.7%*	Cash and guarantees
Overdrafts and other advances	**52.7%**	*93.8%*	Cash
Loans and advances to customers			
Professional market placements to non banks	**100.0%**	*99.7%*	Debt securities
Term and Real Estate lending	**72.1%**	*64.3%*	Cash + Residential/Commercial property
Bills discounted	**100.0%**	*n/a*	Cash
Overdrafts and other advances	**11.8%**	*12.6%*	Cash and guarantees
Off-balance sheet:			
Credit lines and other commitments	**28.4%**	*20.2%*	Cash and guarantees

The maximum exposure to credit risk for financial assets, including derivatives, recognised on the Statement of Financial Position is typically the carrying amount and is represented in the table below which analyses maximum exposure to credit risk by asset class, representing credit risk arising from counterparty default.

31 December 2018	Maximum exposure	Cash collateral *	Property collateral	Debt securities	Guarantees	Net exposure to credit risk
On-balance sheet:						
Cash, notes and coins	110	-	-	-	-	110
Financial investments: debt securities (note 15)	1,767,556	-	-	-	-	1,767,556
Loans and advances to banks						
Funds held at correspondent banks	369,113	-	-	-	-	369,113
Professional market placements	255,424	-	-	(134,747)	-	120,677
Term lending	165,235	(6,198)	-	-	(26,981)	132,056
Bills discounted	207,837	(13,898)	-	-	(5,823)	188,116
Overdrafts and other advances	2,695	(1,419)	-	-	-	1,276
Less: Provisions for impairments (note 13)	(2,876)	-	-	-	-	(2,876)
Loans and advances to customers						
Professional market placements to non banks	191,951	-	-	(191,831)	-	120
Term and Real Estate lending	721,135	-	(502,456)	-	(17,196)	201,483
Bills discounted	26,484	(26,474)	-	-	-	10
Overdrafts and other advances	228,515	-	-	-	(27,012)	201,503
Less: Provisions for impairments (note 13)	(86,924)	-	-	-	-	(86,924)
Derivatives	1,249	-	-	-	-	1,249
Total on balance sheet	**3,847,504**	**(47,989)**	**(502,456)**	**(326,578)**	**(77,012)**	**2,893,469**
Off-balance sheet:						
Credit lines and other commitments	676,677	(179,047)	-	-	(13,255)	484,375
Total off balance sheet	**676,677**	**(179,047)**	**-**	**-**	**(13,255)**	**484,375**
Total	**4,524,181**	**(227,036)**	**(502,456)**	**(326,578)**	**(90,267)**	**3,377,844**

*In the markets where the Bank operates, with higher instances of fraud and government or other action, then the quality of and access to collateral can be less certain.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

31 December 2017	Maximum exposure	Cash collateral*	Property collateral	Debt securities	Guarantees	Net exposure to credit risk
On-balance sheet:						
Cash, notes and coins	*143*	*-*	*-*	*-*	*-*	*143*
Financial investments: debt securities (note 15)	*780,528*	*-*	*-*	*-*	*-*	*780,528*
Loans and advances to banks						
Funds held at correspondent banks	*274,942*	*(17)*	*-*	*-*	*-*	*274,925*
Professional market placements	*153,580*	*(4,437)*	*-*	*-*	*-*	*149,143*
Term lending	*221,558*	*(5,941)*	*-*	*-*	*(14,870)*	*200,747*
Bills discounted	*364,885*	*(15,369)*	*-*	*-*	*(19,984)*	*329,532*
Overdrafts and other advances	*3,634*	*(3,406)*	*-*	*-*	*-*	*228*
Less: Provisions for impairments (note 13)	*(1,089)*	*-*	*-*	*-*	*-*	*(1,089)*
Loans and advances to customers						
Professional market placements to non banks	*190,047*	*-*	*-*	*(189,512)*	*-*	*535*
Term and Real Estate lending	*688,562*	*-*	*(437,411)*	*-*	*(5,466)*	*245,685*
Overdrafts and other advances	*236,885*	*(201)*	*-*	*-*	*(29,607)*	*207,077*
Less: Provisions for impairments (note 13)	*(46,905)*		*-*	*-*		*(46,905)*
Derivatives	*547*	*-*	*-*	*-*	*-*	*547*
Total on balance sheet	***2,867,317***	***(29,371)***	***(437,411)***	***(189,512)***	***(69,927)***	***2,141,096***
Off-balance sheet:						
Credit lines and other commitments	*586,163*	*(116,631)*	*-*	*-*	*(1,480)*	*468,052*
Total off balance sheet	***586,163***	***(116,631)***	***-***	***-***	***(1,480)***	***468,052***
Total	***3,453,480***	***(146,002)***	***(437,411)***	***(189,512)***	***(71,407)***	***2,609,148***

Real estate lending is collateralised with residential or commercial property. The value of collateral for property loans is based on the most recently available valuations from independent sources. Given current weakness in the residential sector, all residential exposures have been subject to at least desktop valuation during 2018. In addition commercial properties where there is objective evidence either on a standalone or sectoral basis of value decline have been subject to revaluation.

In certain cases cash collateral is held against other forms of lending and off-balance sheet exposures. At 31 December 2018 the value of cash collateral held and utilised by the Bank on terms under which set off can be applied in the event of default by the counterparty was £266,610,000 (*2017: £146,003,000*). This includes the utilised portion of a US$350,000,000 deposit (2017: US$250,000,000) placed by Libyan Foreign Bank as collateral for the obligations of itself, affiliated entities and a number of other Libyan counterparties. Collateral may also be taken in the form of personal guarantees given by individuals associated with the obligating counterparty, but no value is ascribed in these circumstances. Other mitigants include credit insurance and back-to-back commitments from financial institutions of acceptable quality, or security.

Residential and commercial mortgage lending

The table below stratifies credit exposures for residential and commercial property loans by ranges of loan-to-value (LTV) ratio. LTV is calculated as the ratio of the gross amount of the loan to the value of the collateral. The gross amounts exclude any impairment allowance.

	2018	*2017*
LTV ratio		
Less than 55%	100,221	*73,480*
55 - 65%	246,592	*259,859*
66 - 75%	125,837	*93,462*
76 - 85%	29,806	*10,610*
Total	**502,456**	***437,411***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

By industry, concentrations of credit risk were as follows:

	2018	*2017*
Financial institutions (including central banks)		
Banks	1,436,507	*1,166,036*
Multilateral development banks	334,103	*490,416*
Other financial intermediaries	514,813	*478,469*
	2,285,423	***2,134,921***
Corporates		
Commodities	342,122	*315,743*
Construction and engineering	1,345	*11,302*
Energy	164,362	*185,494*
Transport and storage	22,587	*7,151*
Real estate	428,880	*414,103*
Other	115,356	*97,157*
	1,074,652	***1,030,950***
Public administration	**1,161,494**	***246,452***
Others	**94,450**	***89,960***
Impairments (note 13)	(91,838)	*(48,803)*
Maximum exposure to credit risk	**4,524,181**	***3,453,480***

Credit grading

The Bank uses a credit grading system, to facilitate the monitoring of the portfolio and individual exposures.

A credit grade is a numerical measure of the Probability of Default (PD), which is the likelihood that a customer will default within the next twelve months. Credit grades range from 1 to 20 as per the Bank's Master Rating Scale. A credit grade of 20 is used if the customer or customer Group is in default. In addition to the credit grade a Watchlist grade is also utilised for customers exhibiting unsatisfactory features or considered to be of concern.

A credit grade must be agreed for each customer and reviewed at least annually, or when new information is received, to ensure that it is at all times a reasonable representation of the PD for that customer.

Credit grades are determined through the use of a model or methodology appropriate to the customer type using financial and non-financial information. Financial information includes the most recent available audited financial statements. Non-financial information includes:

- Country Capping, i.e. the maximum credit grading available to customers from a specific domicile;
- Post balance sheet date events; and
- External credit ratings or benchmark credit grades for peer companies.

The Watchlist Grades are defined as follows:

- WL1: A temporary/cautionary classification for clients who exhibit some unsatisfactory features, however we consider viability sound.
- WL2: We have some concerns over the viability. This also captures any accounts that have been on Watchlist over 12 months. At this stage, a lifetime Expected Loss would be run.
- WL3: Sub-standard. We have real concerns that if the position deteriorates the Bank could be at risk of loss.
- 20: Default

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Master Rating Scale

Category	Grade	Probability of Default*	S&P From	S&P To	Moody's From	Moody's To	Fitch From	Fitch To
			External benchmarks					
Investment Grade	1 - 10	0.001% - 0.660%	AAA	BBB-	Aaa	Baa3	AAA	BBB-
Non-Investment Grade	11 - 18	0.661% - 25.000%	BB+	CCC	Ba1	Caa2	BB+	CCC
Watchlist 1	W15 - W18	3.714% - 25.000%	B	CCC	B2	Caa2	B	CCC
Watchlist 2	W18	12.001% - 25.000%	CCC	CCC	Caa2	Caa2	CCC	CCC
Watchlist 3 Sub-Standard	W19	25.001% - 50.000%	CCC-	CCC-	Caa3	Caa3	CCC-	CCC-
Default	20	100%	CC/D	CC/D	Ca	Ca	DDD-D	DDD-D

**Source: Moody's*

Credit risks assessed in accordance with that methodology are shown below.

31 December 2018 Grade	Financial guarantees and other commitments	Cash, loans and advances, debt securities and derivatives	Maximum exposure to credit risk	Cash collateral	Net credit exposure
Grades 1- 10 (Investment Grade)	134,594	2,638,883	2,773,477	-	2,773,477
Grades 11 - 17 (Non-Investment Grade)	281,429	994,330	1,275,759	-	1,275,759
Grades 18 - 19 (Watchlist + Substandard)	255,266	91,984	347,250	(227,036)	120,214
Grade 20 (Default)	7,427	212,106	219,533	-	219,533
	678,716	**3,937,303**	**4,616,019**	**(227,036)**	**4,388,983**
Loss allowance	**(2,039)**	**(89,799)**	**(91,838)**	**-**	**(91,838)**
Carrying amount	**676,677**	**3,847,504**	**4,524,181**	**(227,036)**	**4,297,145**

31 December 2017 Grade	*Financial guarantees and other commitments*	*Cash, loans and advances, debt securities and derivatives*	*Maximum exposure to credit risk*	*Cash collateral*	*Net credit exposure*
Grades 1- 10 (Investment Grade)	*80,486*	*1,608,967*	*1,689,453*	*(408)*	*1,689,045*
Grades 11 - 17 (Non-Investment Grade)	*323,122*	*1,178,650*	*1,501,772*	*(29,237)*	*1,472,535*
Grades 18 - 19 (Watchlist + Substandard)	*183,244*	*44,099*	*227,343*	*(112,952)*	*114,391*
Grade 20 (Default)	*120*	*83,595*	*83,715*	*(3,405)*	*80,310*
	586,972	***2,915,311***	***3,502,283***	***(146,002)***	***3,356,281***
Loss allowance	***(809)***	***(47,994)***	***(48,803)***	***-***	***(48,803)***
Carrying amount	***586,163***	***2,867,317***	***3,453,480***	***(146,002)***	***3,307,478***

There are exposures with credit grade 18 which are based upon country caps, but have not displayed a significant increase in credit risk.

Credit quality analysis

The following tables set out information about the credit quality of financial assets measured at amortised cost. The amounts in the table represent the gross carrying amounts. For financial guarantees and other commitments, the amounts in the table represent the amounts guaranteed or committed respectively.

Loans and advances to banks - 31 December 2018

Gross exposure	Stage 1	Stage 2	Stage 3	Total
Grades 1- 10 (Investment Grade)	582,627	-	-	582,627
Grades 11 - 17 (Non-Investment Grade)	304,984	45,169	-	350,153
Grades 18 - 19 (Watchlist + Substandard)	66,555	-	-	66,555
Grade 20 (Default)	-	-	969	969
	954,166	**45,169**	**969**	**1,000,304**
Loss allowance	**(1,945)**	**(259)**	**(672)**	**(2,876)**
Carrying amount	**952,221**	**44,910**	**297**	**997,428**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Loans and advances to customer - 31 December 2018

Gross exposure	Stage 1	Stage 2	Stage 3	Total
Grades 1- 10 (Investment Grade)	263,659	-	-	263,659
Grades 11 - 17 (Non-Investment Grade)	536,322	126,387	-	662,709
Grades 18 - 19 (Watchlist + Substandard)	26,499	4,080	-	30,579
Grade 20 (Default)	-	-	211,138	211,138
	826,480	**130,467**	**211,138**	**1,168,085**
Loss allowance	**(1,840)**	**(3,371)**	**(81,713)**	**(86,924)**
Carrying amount	**824,640**	**127,096**	**129,425**	**1,081,161**

Off balance sheet - 31 December 2018

Gross exposure	Stage 1	Stage 2	Stage 3	Total
Grades 1- 10 (Investment Grade)	134,306	705	-	135,011
Grades 11 - 17 (Non-Investment Grade)	273,391	7,072	-	280,463
Grades 18 - 19 (Watchlist + Substandard)	245,971	9,843	-	255,814
Grade 20 (Default)	-	-	7,428	7,428
	653,668	**17,620**	**7,428**	**678,716**
Loss allowance	**(854)**	**(19)**	**(1,170)**	**(2,043)**
Carrying amount (provision)	**(854)**	**(19)**	**(1,170)**	**(2,043)**

Loans and advances to banks - 1 January 2018

Gross exposure	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Grades 1- 10 (Investment Grade)	*455,306*	*-*	*-*	*455,306*
Grades 11 - 17 (Non-Investment Grade)	*537,692*	*-*	*-*	*537,692*
Grades 18 - 19 (Watchlist + Substandard)	*22,196*	*-*	*-*	*22,196*
Grade 20 (Default)	*-*	*-*	*3,406*	*3,406*
	1,015,194	***-***	***3,406***	***1,018,600***
Loss allowance	***(3,131)***	***-***	***-***	***(3,131)***
Carrying amount	***1,012,063***	***-***	***3,406***	***1,015,469***

Loans and advances to customer - 1 January 2018

Gross exposure	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Grades 1- 10 (Investment Grade)	*382,083*	*4,452*	*-*	*386,535*
Grades 11 - 17 (Non-Investment Grade)	*560,589*	*66,258*	*-*	*626,847*
Grades 18 - 19 (Watchlist + Substandard)	*10,934*	*7,552*	*-*	*18,486*
Grade 20 (Default)	*-*	*-*	*83,625*	*83,625*
	953,606	***78,262***	***83,625***	***1,115,493***
Loss allowance	***(2,959)***	***(4,963)***	***(43,477)***	***(51,398)***
Carrying amount	***950,647***	***73,299***	***40,148***	***1,064,095***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Off balance sheet - 1 January 2018

Gross exposure	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Grades 1- 10 (Investment Grade)	*78,790*	*1,253*	*-*	*80,043*
Grades 11 - 17 (Non-Investment Grade)	*316,744*	*6,923*	*22*	*323,689*
Grades 18 - 19 (Watchlist + Substandard)	*171,343*	*11,898*	*-*	*183,241*
Grade 20 (Default)	*-*	*-*	*-*	*-*
	566,877	***20,074***	***22***	***586,973***
Loss allowance	***(1,453)***	***(24)***	***(20)***	***(1,497)***
Carrying amount (provision)	***(1,453)***	***(24)***	***(20)***	***(1,497)***

The Bank provides facilities to in excess of 460 counterparties encompassing exposures in over 75 countries and territories (*2017: in excess of 400 counterparties encompassing exposures in over 65 countries and territories*).

Regional concentrations of credit risk arising from operations were as follows:

31 December 2018	**Financial guarantees and other commitments**	**Cash, loans and advances, debt securities and derivatives**	**Total**
United Kingdom	103,327	687,563	790,890
Europe excluding UK	116,666	744,251	860,917
Libya	221,126	41,164	262,290
Other Middle East and Africa	201,684	563,636	765,320
United States	7,853	1,252,674	1,260,527
Other Countries	28,060	648,015	676,075
Impairments	(2,039)	(89,799)	(91,838)
Maximum exposure to credit risk	**676,677**	**3,847,504**	**4,524,181**

31 December 2017	*Financial guarantees and other commitments*	*Cash, loans and advances, debt securities and derivatives*	*Total*
United Kingdom	*96,273*	*647,740*	*744,013*
Europe excluding UK	*80,759*	*503,582*	*584,341*
Libya	*153,361*	*12,161*	*165,522*
Other Middle East and Africa	*229,274*	*854,473*	*1,083,747*
United States	*10,260*	*121,679*	*131,939*
Other Countries	*17,045*	*775,676*	*792,721*
Impairments	*(809)*	*(47,994)*	*(48,803)*
Maximum exposure to credit risk	***586,163***	***2,867,317***	***3,453,480***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

MARKET AND LIQUIDITY RISKS

Definitions:
Market Risk is the risk that the Bank's earnings or capital, or its ability to meet business objectives, will be adversely affected by changes in the level or volatility of market rates or prices such as interest rates, credit spreads, commodity prices and foreign exchange rates.

Liquidity Risk is the risk of the Bank, although solvent, being unable to meet its payment obligations as they fall due. This may be caused by the Bank's inability to liquidate assets or to obtain funding to meet its liquidity needs, or by contractual mismatches between the contractual timings on cash inflows and outflows.

Funding Risk is a subset of Liquidity Risk relating to its longer-term funding requirements and is the risk that the Bank does not have stable sources of funding in the medium and long-term to meet its financial obligations as they fall due.

Risk Management:
The Bank's appetite for market and liquidity risks is set in response to its business plans and overall risk appetite.

The Chief Risk Officer and his direct report, the Market Risk Manager, are responsible for:
- development and oversight of the market and liquidity risk management frameworks;
- developing market and liquidity risk policies, tools and frameworks across the business;
- managing effective market and liquidity risk assessment strategies and independent challenge of requests from the first line for new, increased or extended limits;
- oversight of market and liquidity risk activities undertaken by the first line, including daily monitoring and reporting of compliance with limits designed to ensure adherence with the Bank's risk appetite in respect of market and liquidity risks; and
- market and liquidity risk reporting and performance monitoring, including stress testing.

Market and liquidity risk management is overseen at an executive level by the Asset and Liability Committee which reviews and makes recommendations via the Executive Committee to the Audit and Risk Committee at least annually on the Bank's market and liquidity risk appetite and policies, or approves where within delegated authority, having regard to the Bank's business plans and market and liquidity risk policies as approved by the Board from time to time.

Risk Mitigation:
The Bank's Treasury function has day-to-day responsibility for managing its market and liquidity exposures. The Bank does not budget for more than 10% of its revenue to be earned from principal position trading exposures to bonds, interest rates or foreign exchange, and profits should be driven where feasible by customer flows. Derivative contracts are used in both the banking and trading books to modify market risk exposures in the light of perceptions about future movements in those markets. In the banking book, in particular, derivative contracts are used to hedge market risk exposure (interest rate risk) arising from banking book positions, which in the absence of those contracts, would result in unwanted exposures, or excesses to market risk limits. The Bank does not deal in complex derivative transactions.

Exchange rate risk

The Bank manages its exposures to foreign exchange risk by way of limits on the size of permitted positions. Overnight trading positions should be protected by stop-loss orders placed with reputable correspondent banks. The size of the position limits is consistent with the amount of profit that the Bank is prepared to place at risk in the foreign exchange markets. With the exception of the revenues deriving from its real estate activity the Bank earns the majority of its revenues in currencies other than Sterling, but incurs the majority of its operating costs in Sterling. This mismatch is hedged at the discretion of the Bank's Asset and Liability Committee.

The Bank's overall net short position (on foreign exchange open positions and cash arising on settled trades) at 31 December 2018 (being the Sterling equivalent value of all the currencies where the currency obligations were higher than currency receivables) was £829,000 (*2017: £663,000*). Were these currencies to strengthen by 5% against the remaining currencies, then the Bank would lose £41,000 (*2017: £33,000*).

Overall net short positions as calculated on a daily basis were as follows:

	2018	*2017*
Maximum	2,227	*2,726*
Minimum	6	*380*
Average	650	*1,016*

As at the reporting date, there was no significant exposure to any one currency representing more than 10% of the Bank's equity.

Interest rate risk

The Bank is exposed to changes in interest rates in various currencies arising from gaps in the future dates of repricing of assets, liabilities and derivative instruments. The Bank manages that risk by calculating sensitivity of changes in the present value of committed future cash flows to a 0.01% change in interest rates using the Price Value of a Basis Point ("PVBP") methodology. Limits are placed on the overall amount of calculated PVBP with sub-limits for the overall banking book and for the Bank's trading books. The Bank considers the impact of changes in future interest rates on its future income streams by reference to these interest rate gaps.

As at 31 December 2018, PVBP amounted to £42,534 (*2017: £32,056*). PVBP (calculated on a daily basis) was as follows:

	2018	*2017*
Maximum	50	*39*
Minimum	16	*13*
Average	35	*24*

Hedges

Derivative contracts are used in both the banking and trading books to modify market risk exposures in the light of perceptions about future movements in those markets. In the banking book, in particular, derivative contracts are used to reduce market risk exposure arising from banking book interest rate and currency positions, which in the absence of those contracts, would result in unwanted exposures, or excesses to market risk limits. Such contracts are described as hedges. Hedge accounting transactions are documented as such at inception, and the positions being hedged are clearly identified at the outset.

Changes in the fair value of derivatives that are designated and qualify as fair value hedging instruments are recorded in the Statement of comprehensive income in Interest and similar income, together with changes in the fair value of the asset or liability or portfolio thereof that are attributable to the hedged risk.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The repricing characteristics of the Bank's statement of financial position are set out below:

31 December 2018	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Non-interest bearing**	**Total**
Financial investments	661,609	987,688	29,661	87,402	1,195	6,610	1,774,165
Loans and advances to banks	639,270	235,980	122,179	-	-	-	997,429
Loans and advances to customers	519,957	504,805	53,788	2,611	-	-	1,081,161
Other assets	984	88	20	-	-	40,005	41,097
Total assets	**1,821,820**	**1,728,561**	**205,648**	**90,013**	**1,195**	**46,615**	**3,893,852**
Deposits from banks	2,029,213	428,160	541,108	37,768	-	11,300	3,047,549
Other deposits	262,785	87,431	219,650	15,117	-	75	585,058
Subordinated liabilities	-	30,757	-	19,604	24,960	-	75,321
Other liabilities and shareholders' funds	13,840	82	42	357	-	171,603	185,924
Total equity and liabilities	**2,305,838**	**546,430**	**760,800**	**72,846**	**24,960**	**182,978**	**3,893,852**
Derivatives (at contract value)							
Receivable	13,742	3,926	-	-	-	-	
Payable	(7,852)	-	(5,889)	(3,926)	-	-	
Overall gap	**(462,424)**	**1,186,057**	**(549,262)**	**21,093**	**(23,764)**	**(136,363)**	
Reverse Cumulative gap	**35,337**	**497,761**	**(688,296)**	**(139,034)**	**(160,127)**	**(136,363)**	

31 December 2017	*Up to 1 month*	*1-3 months*	*3-12 months*	*1-5 years*	*Over 5 years*	*Non-interest bearing*	*Total*
Financial investments	*185,964*	*435,466*	*63,532*	*91,251*	*4,315*	*7,538*	*788,066*
Loans and advances to banks	*516,227*	*315,853*	*184,900*	*530*	*-*	*-*	*1,017,510*
Loans and advances to customers	*572,826*	*436,067*	*54,782*	*4,828*	*-*	*86*	*1,068,589*
Other assets	*52,017*	*153*	*32*	*58*	*-*	*26,431*	*78,691*
Total assets	***1,327,034***	***1,187,539***	***303,246***	***96,667***	***4,315***	***34,055***	***2,952,856***
Deposits from banks	*1,171,215*	*448,576*	*432,094*	*43,753*	*-*	*-*	*2,095,638*
Other deposits	*257,683*	*71,801*	*41,950*	*184,122*	*-*	*-*	*555,556*
Subordinated liabilities	*41,957*	*30,345*	*-*	*-*	*-*	*-*	*72,302*
Other liabilities and shareholders' funds	*10,218*	*178*	*57*	*36*	*-*	*218,871*	*229,360*
Total equity and liabilities	***1,481,073***	***550,900***	***474,101***	***227,911***	***-***	***218,871***	***2,952,856***
Derivatives (at contract value)							
Receivable	*12,953*	*3,701*	*4,885*	*-*	*-*	*-*	
Payable	*-*	*-*	*(4,885)*	*(16,654)*	*-*	*-*	
Overall gap	*(141,086)*	*640,340*	*(161,085)*	*(114,590)*	*4,315*	*(184,816)*	
Reverse Cumulative gap	***227,894***	***368,980***	***(271,360)***	***(110,275)***	***4,315***	***(184,816)***	

Non-interest bearing items comprise share capital, accumulated impairments, tangible and intangible assets and other sundry debtors and creditors not subject to interest.

Derivatives include interest rate futures and swaps whose purpose is to reduce economic exposure to interest rate risk. Futures are used to manage the overall quantum of interest rate risk whereas swaps are taken as hedges against specific transactions. Swaps are used to ensure that longer dated interest rate re-pricings, such as typically arise from fixed rate loans or deposits, are converted into shorter periods that can be accommodated within the gap limits.

Trading book

The Bank's trading book activities are limited to transactions in financial instruments mainly comprising the trading of foreign exchange, interest rate futures and debt securities. As well as PVBP limits to manage the interest rate risk in those books, risk is mitigated through:

- limits as to the size of particular books and individual positions within those books; and
- stop loss limits to prevent the accumulation of losses from the Bank's principal position trading activities.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Liquidity risk

Liquidity risk is assessed annually through the Internal Liquidity Adequacy Assessment Process ("ILAAP") carried out under the rules of the Bank's regulator. The Bank manages its exposure to liquidity risk by ensuring that it holds a buffer of High Quality Liquid Assets that will enable it to meet its obligations as they fall due under normal and a range of stressed conditions. In addition, the Bank monitors the ratio of its longer dated assets to capital and longer-term funding to mitigate the funding risk deriving from maturity transformation.

The table below analyses the Bank's assets and liabilities into relevant maturity buckets based on the remaining period from the balance sheet date to the contractual maturity date. The table has not been adjusted to reflect any behavioural characteristics that may have been observed by the Bank. Examples include the Bank's portfolio of trading securities that are purchased with the intention of trading before their contractual maturity, and the Bank's ability to liquidate banking book securities in the event of an unforeseen liquidity event.

At 31 December 2018	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Undated**	**Total**
Financial investments	394,624	704,346	32,881	610,417	31,897	-	1,774,166
Loans and advances to banks	639,389	191,260	150,982	15,797	-	-	997,428
Loans and advances to customers	411,038	41,332	90,068	520,181	18,543	-	1,081,161
Other assets	13,449	29	49	59	-	27,512	41,097
Total assets	**1,458,500**	**936,967**	**273,979**	**1,146,454**	**50,440**	**27,512**	**3,893,852**
Deposits from banks	1,841,514	387,549	622,603	195,883	-	-	3,047,548
Other deposits	262,859	87,431	40,645	194,122	-	-	585,058
Subordinated liabilities	-	-	-	19,604	55,717	-	75,321
Other liabilities and shareholders' funds	16,680	82	42	357	584	168,178	185,925
Total equity and liabilities	**2,121,053**	**475,062**	**663,291**	**409,966**	**56,302**	**168,178**	**3,893,852**
Net liquidity gap	**(662,553)**	**461,904**	**(389,312)**	**736,488**	**(5,862)**	**(140,665)**	

At 31 December 2017	*Up to 1 month*	*1-3 months*	*3-12 months*	*1-5 years*	*Over 5 years*	*Undated*	*Total*
Financial investments	*52*	*103,791*	*122,001*	*546,098*	*16,124*	*-*	*788,066*
Loans and advances to banks	*513,242*	*251,680*	*230,302*	*22,286*	*-*	*-*	*1,017,510*
Loans and advances to customers	*419,827*	*67,495*	*47,983*	*519,916*	*13,368*	*-*	*1,068,589*
Other assets	*52,017*	*153*	*32*	*58*	*-*	*26,431*	*78,691*
Total assets	***985,138***	***423,119***	***400,318***	***1,088,358***	***29,492***	***26,431***	***2,952,856***
Deposits from banks	*986,173*	*352,377*	*617,136*	*139,952*	*-*	*-*	*2,095,638*
Other deposits	*257,683*	*47,961*	*65,790*	*184,122*	*-*	*-*	*555,556*
Subordinated liabilities	*-*	*-*	*-*	*-*	*72,302*	*-*	*72,302*
Other liabilities and shareholders' funds	*10,240*	*178*	*57*	*36*	*898*	*217,951*	*229,360*
Total equity and liabilities	***1,254,096***	***400,516***	***682,983***	***324,110***	***73,200***	***217,951***	***2,952,856***
Net liquidity gap	***(268,958)***	***22,603***	***(282,665)***	***764,248***	***(43,708)***	***(191,520)***	

OPERATIONAL RISK

Definitions:

Operational Risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

Risk Management:

The Bank's appetite for operational risk is set in response to its business plans and overall risk appetite. The Chief Risk Officer and his direct report, the Head of Operational Risk and Compliance, are responsible for:

- development and oversight of the operational risk management frameworks;
- developing operational risk policies, tools and frameworks across the business, including operational risk incident reporting, root cause analysis and recording and remedial action tracking;

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

- managing effective Risk and Control Self-Assessment processes to identify and evaluate the Bank's exposures to operational risks;
- oversight of operational risk management activities undertaken by the first line; and
- reporting and performance monitoring.

The Bank's Chief Operations and Control Officer is in the 1st Line of Defence (see Section 4b – Approach to Risk Management) and reports to the Chief Executive Officer. The Chief Operations and Control Officer has day to day responsibility for assuring the completeness and performance of the Bank's operational risk control processes.

Operational risk management is overseen at an executive level by the Governance and Control Committee, which reviews and makes recommendations via the Executive Committee to the Audit and Risk Committee at least annually on the Bank's operational risk appetite and policies, or approves where within delegated authority, having regard to the Bank's business plans and Operational Risk Standards as approved by the Audit and Risk Committee.

Operational risk losses in the year to 31 December 2018 amounted to £198,000 (*2017: £109,000*).

Risk Mitigation:
The Bank seeks to mitigate its operational risks using accepted operational risk management concepts and strategies including but not limited to:

- identification of mission critical processes and potential points of failure, and ensuring that adequate controls are in place;
- IT technical standards and change control procedures;
- HR policies, processes and controls;
- project management policies and procedures;
- implementing an information security management system framework consistent with the ISO 27000 family of standards;
- business continuity planning;
- escalation and reporting of operational incidents to ensure that timely actions are taken to resolve the incident and root cause analysis performed to mitigate the likelihood of recurrence; and
- insurance policies to cover relevant risk exposures. Insurance is viewed as complementary to and not a replacement for a robust control environment.

COMPLIANCE RISK

Definition:
Compliance Risk is defined as the risk of legal and / or regulatory sanctions, material financial loss, or loss to reputation that the Bank may suffer as a result of a failure to comply with laws, regulations, internal policies, codes of conduct and standards, responsibility for which has been allocated to the Compliance Department. In the context of BACB, this encompasses primarily regulatory requirements in respect of Conduct Risk, Market Abuse and Fair Treatment of Customers.

The Bank's principal sources of Compliance Risk are:

- Enterprise-wide compliance risks including supervision and oversight, regulatory reporting and notifications, material outsourcing and / or failure to adequately implement existing and new regulatory requirements;
- Business related including the risk that the Bank fails to conduct its activities appropriately, which may include consumer treatment, conflicts of interest, and / or complaints handling, as well as managing client money and assets;

Risk Management:
The decision was taken in 2018 to allocate oversight responsibility for Compliance to the Head of Operational Risk (now Head of Operational Risk and Compliance) to better balance responsibilities. The Bank's objective is to comply with the letter and spirit of all applicable regulations and laws, and to embed a robust risk and compliance culture throughout the organisation.

The Compliance Department is responsible for:
- developing applicable principles, standards and guidelines for compliance, communicating them and verifying adherence;
- providing advice to individual business units on applicable laws, directives, standards, and regulations as well as providing compliance support;
- providing regular training and education for staff on applicable regulations, rules and internal standards;
- regulatory scanning to ensure that any relevant developments or emerging risks are identified and appropriately addressed; and
- communicating with regulators.

Compliance Risk is overseen by the Audit Risk and Conduct Committee, to whom the Head of Operational Risk Compliance provides periodic reports. At an executive level, Compliance risk, including mitigation controls along with action and remediation plans, is overseen by the Governance and Control Committee.

Risk Mitigation:
The Bank seeks to minimise the risk of compliance failure by seeking to:
- ensure an up-to-date understanding of regulatory requirements which need to be complied with;
- ensure that procedures and controls are in place and designed to minimise the risk of breaching those requirements;
- provide training for staff throughout the organisation aimed at promoting a good understanding of compliance; and
- undertaking a risk-based monitoring programme aimed at detecting shortcomings in, or failures of, compliance controls or processes.

FINANCIAL CRIME

Definition:
Financial Crime Risk is the risk that the Bank may be used to further financial crime activity by breaching financial sanctions, laundering the proceeds of crime, terrorist financing, tax evasion, offering or accepting bribes or being used to channel funds from corrupt practices.

Risk Management:
As noted above the decision was taken during 2018 to reallocate responsibilities for Compliance and Financial Crime to permit the MLRO to focus full time on the Financial Crime agenda. This has also resulted in Financial Crime being categorised as a Principal Risk Type of the Bank on a standalone basis (previously it was combined with Compliance).

The Anti Financial Crime department is responsible for:
- Implementing an anti-financial crime risk management framework designed to mitigate the risk of the Bank being used as a vehicle to facilitate financial crime and breaches of sanctions applicable to the Bank.
- ensuring that any occurrences which give reason to suspect money laundering or the financing of terrorism are identified and reported to the relevant authorities;
- maintaining effective policies, systems and controls to combat and identify financial crime;
- monitoring that those policies and controls are being adhered to;
- providing regular and mandatory training on both a Bank-wide and targeted basis;
- horizon scanning to identify and prepare for forthcoming regulatory change;

- providing management information and reporting to management on the effectiveness of the Bank's anti-financial crime controls; and
- maintaining an independent second line function.

Financial Crime Risk is overseen by the Audit, Risk and Conduct Committee, to whom the MLRO provides periodic reports. At an executive level, Compliance risk, including mitigation controls along with action and remediation plans, is overseen by the Governance and Control Committee.

Risk Mitigation:

- the Bank has invested heavily in enhancing both the quantity and calibre of resources in the first line who are responsible for ensuring compliance, subject to oversight, and in the case of higher risk cases, additional due diligence by the second line compliance team;
- the Bank employs a range of tools and processes, including technology solutions, to monitor new and existing customers and to monitor transactions for risk indicators, which will be investigated if triggered;
- the Bank has established a High Risk Advisory Committee, which consists of a senior members of executive management, to which the MLRO brings higher risk issues which in his opinion should be escalated for information or for discussion, in order to help the ultimate decision makers arrive at their decisions;
- the Bank has developed a Financial Crime Risk Appetite Statement to assist with decision making; and
- the Anti-Financial Crime team operates a risk based monitoring programme to ensure controls are effective

Note 32 provides details of the agreed settlement with the U.S. Office of Foreign Assets Control in relation to sanctions.

5. Critical accounting estimates and judgements in applying accounting policies

The Bank makes estimates and assumptions that may affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Valuation of financial instruments

The Bank's accounting policy on fair value measurements is discussed in Note 3h. The judgements made in assessing valuations of financial instruments are described in Note 7.

Impairment losses on loans and advances

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the income statement, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from individual loans and advances. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a portfolio, or national or local economic conditions that correlate with defaults on assets in the portfolio. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

As noted in the Basis of Preparation the directors view the estimation uncertainty due to credit provisions to be heightened this year.

ECL for not credit-impaired financial assets is made up by 12 month ECL (Stage 1) and lifetime ECL (Stage 2). This ECL is made up by:

- financial assets: the present value of all cash shortfalls, i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive;
- undrawn loan commitments: the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover

The assessment of collective impairments for 2017 under IAS 39 used default rates and loss rates based on historical trends for assets with credit risk characteristics similar to those in the loan portfolio. Management made an adjustment where economic and credit conditions were such that the actual loses were likely to be greater or lesser than suggested by historical trends.

At 31 December 2018 16 loans to customers were impaired (*2017: loans to seven customers*). The restructuring of two loans were the subject of continuing negotiations between lending syndicates and the borrowers, the outcomes of which were uncertain at 31 December 2018. Assumptions have been made regarding the outcome of these negotiations, and hence future cash flows based on information regarding the value of underlying assets and businesses, and on indicative secondary market pricing where available.

If recoveries on the 16 impaired loans are 10% lower than has been estimated, then the amount of the impairment which would have been charged in 2018 in respect of those loans would have been increased by £13,631,000 *(2017: £4,024,000 in respect of seven loans)*.

Pension fund

The Bank assesses the value of its defined benefit pension fund assets and obligations in accordance with IAS 19. The standard requires that certain assumptions be made which are set out in Note 25. Note 25 also sets out an analysis of the sensitivity of the defined benefit obligations to changes in certain assumptions.

Software

Computer software is included in intangible assets. It includes purchased software. It may also include, on an exceptional basis for specific projects, internal development costs. Costs incurred in the ongoing maintenance of software are expensed immediately as incurred.

Deferred taxation

The Bank has carry forward tax losses that are available to offset against future taxable profit. However, deferred tax assets are recognised only to the extent that it is probable that taxable profit will be available against which the unused tax losses or tax credits can be utilised. Management judgement is exercised in assessing whether this is the case, taking into account future profitability expectations. To the extent that actual outcomes differ from management's estimates, income tax charges or credits, and changes in current and deferred tax assets or liabilities, may arise in future periods.

Other

The Bank's directors are not aware of any other judgement areas that would materially affect the income statement.

6. Analysis of financial assets and liabilities by measurement basis

Financial assets and financial liabilities are measured on an ongoing basis either at fair value or at amortised cost. The summary of significant accounting policies in Note 3 describes how the classes of financial instruments are measured, and how income and expense, including fair value gains and losses, are recognised.

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

	Original classification under IAS 39	New classificaiton under IFRS 9	Original carrying amount under IAS 39	New carrying amount under IFRS 9
Assets				
Cash, notes and coins	Loans and receivables	Amortised cost	143	143
Financial investments - debt securities held for trading	FVTPL	FVTPL (manditorily)	3,690	3,690
Financial investments - other debt securities	Available for sale	FVOCI	776,838	776,838
Financial investments - equity investments	Available for sale	FVOCI	7,538	7,538
Loans and advances to banks	Loans and receivables	Amortised cost	1,017,510	1,015,470
Loans and advances to customers	Loans and receivables	Amortised cost	1,068,589	1,064,096
Derivatives	FVTPL	FVTPL (manditorily)	547	547
Total financial assets			**2,874,854**	**2,868,321**
Liabilities				
Deposits from banks	Amortised cost	Amortised cost	2,095,638	2,095,638
Other deposits	Amortised cost	Amortised cost	555,556	555,556
Derivatives	FVTPL	FVTPL (manditorily)	1,271	1,271
Subordinated liabilities	Amortised cost	Amortised cost	72,302	72,302
Total financial liabilities			**2,724,767**	**2,724,767**

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

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
Financial assets held at amortised cost				
Cash, notes and coins	**143**	**-**	**-**	**143**
Loans and advances to banks				
Opening balance	1,017,510	-	-	1,017,510
Increase in impairment allowance	-	-	(2,040)	(2,040)
Total loans and advances to banks	**1,017,510**	**-**	**(2,040)**	**1,015,470**
Loans and advances to customers				
Opening balance	1,068,589	-	-	1,068,589
Increase in impairment allowance	-	-	(4,493)	(4,493)
Total loans and advances to customers	**1,068,589**	**-**	**(4,493)**	**1,064,096**
Financial assets held at available for sale				
Financial investments - debt securities				
Opening balance	776,838			
Reclassification to FVOCI		(776,838)	-	
Closing balance	776,838	(776,838)	-	-
Financial investments - equity securities				
Opening balance	7,538			
Reclassification to FVOCI		(7,538)	-	
Closing balance	7,538	(7,538)	-	-
Total financial assets at available for sale	**784,376**	**(784,376)**	**-**	**-**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

	IAS 39 carrying amount 31 December 2017	Reclassification	Remeasurement	IFRS 9 carrying amount 1 January 2018
Financial assets held at FVOCI				
Financial investments - debt securities				
Opening balance	-			
Reclassification from available for sale		776,838	-	
Closing balance	-	776,838	-	776,838
Financial investments - equity securities				
Opening balance	-			
Reclassification from available for sale		7,538	-	
Closing balance	-	7,538	-	7,538
Total financial assets held at FVOCI	**-**	**784,376**	**-**	**784,376**
Financial assets designated at FVTPL				
Financial investments - debt securities	3,690	-	-	3,690
Derivatives	547	-	-	547
Total financial assets designated at FVTPL	**4,237**	**-**	**-**	**4,237**
Deferred tax asset				
Opening balance	341	-	-	341
DTA recognised on impairment allowance	-	-	1,304	1,304
Total deferred tax asset	**341**	**-**	**1,304**	**1,645**
Financial liabilities held at amortised cost				
Deposits from banks	2,095,638	-	-	2,095,638
Other deposits	555,556	-	-	555,556
Subordinated liabilities	72,302	-	-	72,302
Total financial liabilities at amortised cost	**2,723,496**	**-**	**-**	**2,723,496**
Financial liabilties designated at FVTPL				
Derivatives	1,271	-	-	1,271
Total financial liabilties designated at FVTPL	**1,271**	**-**	**-**	**1,271**
Other liabilities, accruals and deferred income				
Loss allowance provision on financial guarantees and other commitments	809	-	687	1,496
Total	**809**	**-**	**687**	**1,496**
Retained earnings				
Opening balance	106,861	-	-	106,861
Increase in impairment allowance	-	-	(7,463)	(7,463)
Deferred tax on remeasurement	-	-	1,304	1,304
Total retained earnings	**106,861**	**-**	**-**	**100,702**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The following table analyses the financial assets and liabilities in the statement of financial position by the class of financial instrument to which they are assigned and therefore by the measurement basis.

31 December 2018	**Assets and liabilities held at amortised cost**	**Debt securities held at FVOCI**	**Equity Investments held at FVOCI**	**Assets and liabilities manditorily designated at FVTPL**	**Total**
Assets					
Cash, notes and coins	110	-	-	-	**110**
Financial investments	-	1,762,634	6,610	4,922	**1,774,166**
Loans and advances to banks	997,428	-	-	-	**997,428**
Loans and advances to customers	1,081,161	-	-	-	**1,081,161**
Derivatives	-	-	-	1,249	**1,249**
Total financial assets	2,078,699	1,762,634	6,610	6,171	**3,854,114**
Total non-financial assets					**39,738**
Total assets					**3,893,852**
Liabilities					
Deposits from banks	3,047,548	-	-	-	**3,047,548**
Other deposits	585,058	-	-	-	**585,058**
Derivatives	-	-	-	1,119	**1,119**
Subordinated liabilities	75,321	-	-	-	**75,321**
Total financial liabilities	3,707,927	-	-	1,119	**3,709,046**
Total equity and non-financial liabilities					**184,805**
Total equity and liabilities					**3,893,852**

31 December 2017	*Loans and receivables*	*Financial assets and liabilities at amortised cost*	***Total assets and liabilities held at amortised cost***	*Available for sale*	*At fair value through profit and loss*	*Derivatives designated as fair value hedging instruments*	***Total assets and liabilties held at fair value***	*Total*
Assets								
Cash, notes and coins	-	143	**143**	-	-	-	**-**	**143**
Financial investments	-	-	**-**	784,376	3,690	-	**788,066**	**788,066**
Loans and advances to banks	1,017,510	-	**1,017,510**	-	-	-	**-**	**1,017,510**
Loans and advances to customers	1,068,589	-	**1,068,589**	-	-	-	**-**	**1,068,589**
Derivatives	-	-	**-**	-	501	46	**547**	**547**
Total financial assets	2,086,099	143	**2,086,242**	784,376	4,191	46	**788,613**	**2,874,855**
Total non-financial assets								**78,001**
Total assets								**2,952,855**
Liabilities								
Deposits from banks	-	2,095,638	**2,095,638**	-	-	-	**-**	**2,095,638**
Other deposits	-	555,556	**555,556**	-	-	-	**-**	**555,556**
Derivatives	-	-	**-**	-	1,271	-	**1,271**	**1,271**
Subordinated liabilities	-	72,302	**72,302**	-	-	-	**-**	**72,302**
Total financial liabilities	-	2,723,496	**2,723,496**	-	1,271	-	**1,271**	**2,724,767**
Total equity and non-financial liabilities								**228,089**
Total equity and liabilities								**2,952,855**

Of the total £6,171,000 (*2017: £4,190,000*) assets at fair value through the profit and loss account, £6,171,000 (*2017: £4,190,000*) represents financial assets and derivatives held for trading purposes.

Of the total £1,119,000 *(2017: £1,271,000)* liabilities at fair value through the profit and loss account, £1,119,000 (*2017: £1,271,000)* represents derivatives held for trading purposes. As at 31 December 2018, there were no financial liabilities designated at fair value through the profit and loss account at inception *(2017: nil)*.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

7. Fair values of financial assets and liabilities

a) Financial assets and liabilities held at amortised cost

The fair values of assets and liabilities held at amortised costs are required to be estimated and disclosed, and the table below summarises both the carrying amounts and the estimated fair values of those financial assets and liabilities. Bid prices are used to determine fair values of assets, whereas offer prices are applied for liabilities. Observable market prices are not available for many of the Bank's financial assets and liabilities not measured at fair value.

The fair values set out below are based on indices for proxy assets and liabilities not already carried at fair value which are considered to be similar, but not identical, to those held by the Bank. Further, these fair values have been determined using internal models, the results of which might not be equivalent to those which would be arrived at between willing buyer and willing seller. Internal models may use inputs which are unobservable, or be based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

31 December 2018	**Level 1**	**Level 2**	**Level 3**	**Total**	**Carrying value (note 6)**
Cash, notes and coins	-	110	-	110	110
Loans and advances to banks	-	-	996,819	996,819	997,428
Loans and advances to customers	-	-	1,081,081	1,081,081	1,081,161
Financial assets held at amortised cost	**-**	**110**	**2,077,900**	**2,078,010**	**2,078,699**
Deposits from banks	-	-	3,116,318	3,116,318	3,047,548
Other deposits	-	-	596,355	596,355	585,058
Subordinated liabilities	-	-	68,117	68,117	75,321
Financial liabilities held at amortised cost	**-**	**-**	**3,780,790**	**3,780,790**	**3,707,927**

31 December 2017	*Level 1*	*Level 2*	*Level 3*	*Total*	*Carrying value (note 6)*
Cash, notes and coins	*-*	*143*	*-*	*143*	*143*
Loans and advances to banks	*-*	*-*	*1,017,341*	*1,017,341*	*1,017,510*
Loans and advances to customers	*-*	*-*	*1,069,816*	*1,069,816*	*1,068,589*
Financial assets held at amortised cost	***-***	***143***	***2,087,157***	***2,087,300***	***2,086,242***
Deposits from banks	*-*	*-*	*2,096,284*	*2,096,284*	*2,095,638*
Other deposits	*-*	*-*	*555,471*	*555,471*	*555,556*
Subordinated liabilities	*-*	*-*	*68,110*	*68,110*	*72,302*
Financial liabilities held at amortised cost	***-***	***-***	***2,719,865***	***2,719,865***	***2,723,496***

Loans and advances to banks and customers

Loans and advances to banks include professional market placements and other loans and advances, net of accumulated impairments.

The estimated fair value of professional market placements (which are for terms up to one year) is based on discounted cash flows using prevailing market interest rates for the relevant periods.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The estimated fair value of term and real estate lending is derived by comparing the actual yields being received on loans advanced by the Bank with observed yields from corporate and financial bond indices considered to be of similar credit quality and duration. At 31 December 2018 observed market yields for those indices were higher than those being achieved, and as a result the estimated fair market value of the loans at that date represents an overall discount to their carrying value as shown above. The Bank has no current intention of disposing of any of these loans, and accordingly, in the opinion of the directors, the amount of the discount is not indicative of an impairment which should be recognised through the Bank's accounts. Loans and advances which are impaired are stated at their book value without further adjustment.

Deposits

The estimated fair value of deposits with no stated maturity, which includes non-interest-bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits and other borrowings without a quoted market price is based on discounted cash flows using market interest rates for debts with similar remaining maturity.

The market interest and exchange rates as at year end for the principal currencies in which the Bank has assets and liabilities, and by reference to which assets and liabilities have been valued, were as follows:

	31 December 2018			***31 December 2017***		
	Sterling	***US Dollars***	***Euro***	***Sterling***	***US Dollars***	***Euro***
Interest rates						
3 month	0.91%	2.81%	-0.31%	*0.51%*	*1.68%*	*-0.39%*
6 month	1.03%	2.77%	-0.24%	*0.57%*	*1.85%*	*-0.32%*
1 year	1.08%	2.75%	-0.23%	*0.87%*	*2.20%*	*-0.23%*
5 year	1.25%	2.55%	0.16%	*1.04%*	*2.27%*	*0.32%*
Exchange rates	1.0000	1.2735	1.1130	*1.0000*	*1.3511*	*1.1270*

Subordinated liabilities

Subordinated liabilities represent term obligations. The obligations are not quoted, and a valuation has been estimated using discounted cash flow techniques based on yields observed in the market for subordinated instruments issued by other similar organisations with similar credit profile.

As other financial institutions use different valuation methodologies and assumptions in determining fair values, comparisons of fair values between financial institutions may not be meaningful and users are advised to exercise caution when using this data.

Cash, notes and coins

Fair value is disclosed as being the same as carrying value for cash, notes and coins given the nature of the assets.

b) Financial assets and liabilities held at fair value

The majority of the Bank's financial instruments measured at fair value are valued using quoted market prices or market standard valuation techniques based on observable market data.

The Bank measures fair values using the following fair value hierarchy that reflects the significance of inputs used in making the measurements.

Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.

Level 2: Valuation techniques based on observable inputs, either directly (i.e., as prices) or indirectly (i.e. derived from prices). This category comprises instruments valued using reference to quoted market data such as yield curves.

Level 3: Valuation techniques using significant unobservable inputs. This category comprises equity investments valued by reference to published accounts or third party valuations.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

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

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist, Black-Scholes and polynomial option pricing models and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other data used in estimating discount rates, bond prices and foreign currency exchange rates. The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The table below analyses financial instruments measured at fair value at the end of the reporting year, by the level in the fair value hierarchy into which measurement is categorised.

31 December 2018	**Level 1**	**Level 2**	**Level 3**	**Total fair value (Note 6)**
Financial investments	1,767,556	-	6,610	1,774,166
Derivative assets	1,090	160	-	1,249
Total assets held at fair value	**1,768,645**	**160**	**6,610**	**1,775,415**
Derivative liabilities	1,081	38	-	1,119
Total liabilities held at fair value	**1,081**	**38**	**-**	**1,119**

31 December 2017	*Level 1*	*Level 2*	*Level 3*	*Total fair value (Note 6)*
Financial investments	*780,528*	*-*	*7,538*	*788,066*
Derivative assets	*501*	*46*	*-*	*547*
Total assets held at fair value	***781,029***	***46***	***7,538***	***788,613***
Derivative liabilities	*1,243*	*28*	*-*	*1,271*
Total liabilities held at fair value	***1,243***	***28***	***-***	***1,271***

There were no significant transfers of assets between levels during 2018, and no significant changes in valuation techniques.

Debt securities

The aggregate fair values of listed debt securities are calculated based on quoted market prices and are all categorised accordingly as Level 1. Unlisted debt securities would be valued by reference to discounted cash flows using market interest rates for debts with similar remaining maturity.

Equity shares and investments

Assets categorised as Level 3 comprise the Bank's investments in equity shares and investments. These assets are valued by reference to reports from fund managers, and from the audited annual reports (which may be a year in arrears) of the companies in which the Bank is invested. The sensitivity of value of these assets is therefore directly related to the movements in the value of the net assets of the investee entities, subject to currency fluctuations. Movements during the year of these assets are set out in Note 15.

Derivative assets and liabilities

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The fair values of spot and forward foreign exchange contracts and interest futures are based upon quoted prices in active markets and are all categorised accordingly as Level 1. The fair values of interest rate swaps and foreign exchange options are derived from net present value and discounted cash flow models, with interest rates derived from yield curves derived from market data. These instruments are categorised as Level 2.

Loans and advances and deposits from banks

Certain of these assets and liabilities are held at fair value. These fair values are also derived from net present value and discounted cash flow models, with interest rates derived from yield curves derived from market data. These instruments are categorised as Level 2.

8. Net interest income

Interest income is made up as follows:

	2018	*2017*
Interest income		
Professional market placements and debt securities	25,450	*20,143*
Loans, advances and overdrafts	56,106	*41,450*
Other	9	*21*
	81,564	***61,614***
Interest income comprises		
Interest arising on financial assets at fair value through the income statement	1,079	*682*
Gains / (losses) arising from the change in fair value of fair value hedges		
- on hedging instruments	35	*87*
- on hedged items attributable to the hedged risk	(52)	*(81)*
Other interest	80,502	*60,926*
	81,564	***61,614***

The amount recorded in the income statement in respect of the ineffectiveness of fair value hedges was £nil in the year ended 31 December 2018 *(2017:£nil)*

Interest expense is made up as follows:

	2018	*2017*
Interest expense		
Deposits from banks and other deposits	(41,516)	*(30,616)*
Subordinated loans	(2,842)	*(2,568)*
Other	-	*(12)*
	(44,358)	***(33,196)***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

9. Net fee and commission income

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

	2018	*2017*
Fee and commission income		
Safe custody	129	*147*
Trade services:		
Guarantees	731	*647*
Documentary credit and trade finance fees	17,632	*11,284*
Other trade services income	162	*257*
Term lending (other than amounts which form part of the effective interest rate)	260	*212*
Banking payments and services	3,753	*3,062*
	22,667	***15,609***
Fee and commission expense		
Brokerage and other fees	**(372)**	***(325)***

10. Net trading income

Net trading income is made up as follows:

	2018	*2017*
Foreign exchange dealing	5,563	*4,180*
Debt securities	(300)	*327*
Other	95	*223*
	5,358	***4,730***

Foreign exchange dealing income includes gains and losses from spot and forward contracts, options and translated foreign currency assets and liabilities.

11. Other operating income

Other operating income is made up as follows:

	2018	*2017*
Rent recovery	185	*185*
Gains on equity shares and investment funds	164	*401*
Losses on debt securities at fair value through other comprehensive income	(373)	*-*
Gains on available for sale financial assets	-	*4,378*
	(23)	***4,964***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

12. Administrative expenses

	2018	*2017*
Staff costs:		
Salaries and other emoluments	16,431	*14,711*
Social security costs	1,966	*2,039*
Other pension costs:		
Defined benefit scheme (note 25)	317	*280*
Defined contribution scheme (note 25)	1,723	*1,532*
Total fixed employment costs (Permanent Staff)	**20,437**	***18,562***
Variable staff costs: performance awards	(153)	*2,432*
Total staff employment costs	**20,284**	***20,994***
Reorganisation costs	314	*405*
Other employment related costs (see below)	3,730	*3,276*
Total staff costs	**24,328**	***24,675***
Fees payable to the Bank's auditors for the audit of the Bank's annual financial statements	315	*292*
Fees payable to the Bank's auditors for other services :		
Other services pursuant to legislation	15	*15*
All other services	-	*-*
Depreciation (including amortisation of intangibles)	1,024	*1,338*
Amounts payable in respect of operating leases:		
Amortisation of prepaid rental on land	63	*63*
Ground rental	143	*143*
Loss/(gain) on sale or impairment of tangible and intangible assets	1,101	*665*
Regulatory supervision fees	99	*83*
Other administrative expenses		
Premises & Technology	6,084	*4,973*
Legal & Professional	1,452	*1,151*
Other	3,394	*2,227*
General administrative expenses	**38,018**	***35,625***
Review of historic activities	**-**	***375***
Administrative expenses	**38,018**	***36,000***

Other Administrative expenses includes VAT refunds of £1,190,000 in 2017

The average number of employees in place during the year was 228 (*2017: 211*).

Other employment related costs include contractors.

Charges for the review of historic activities (also refer Note 32) comprises legal costs incurred and includes a provision for additional costs committed as at 31 December 2017.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

directors' remuneration included above totalled £1,046,000 *(2017:* £1,516,000*)*. The emoluments of the highest paid director were £319,000 *(2017:* £685,000*)* and the amount of their accrued pension as at balance sheet date was £nil *(2017: £nil)*. There were no pension contributions for any directors during the year *(2017: £nil)*.

13. Allowance for credit losses

The below table shows the movement in impairment provisions on loans and advances to banks and customers at amortised cost, debt securities at amortised cost, and on financial guarantees and other commitments for the year ended 31 December 2018.

31 December 2018	**Loans**	**Debt**	**Off-balance sheet positions**	**Total**
Balance at 31 December 2017	**47,994**	**-**	**809**	**48,803**
Impact of transition to IFRS9	6,535	224	687	7,447
Balance at 1 January 2018	**54,529**	**224**	**1,496**	**56,250**
Exchange translation and other movements	2,964	-	62	3,026
New allowances	58,415	145	483	59,043
Allowance for credit losses	**58,415**	**145**	**483**	**59,043**
Reversal of allowances for loans written off	(26,108)	-	-	(26,108)
Balance at 31 December	**89,800**	**369**	**2,042**	**92,211**
Credit impaired	82,377	-	1,171	83,548
Not credit impaired	7,423	369	872	8,664
Total credit losses allowance against loans and off balance positions	**89,800**	**369**	**2,043**	**92,212**

The contractual amount outstanding on financial assets that were written off during the reporting period and are still subject to enforcement activity was £26,108,000 (2017: £nil).

The below table shows the movement in impairment provisions on loans and advances to banks and customers, and on financial guarantees and other commitments under IAS 39 for the year ended 31 December 2017.

31 December 2017	*Loans*	*Off-balance sheet positions*	*Total*
Balance at 1 January	***40,719***	***250***	***40,969***
Exchange translation and other movements	*(2,319)*	*-*	*(2,319)*
Allowances recovered	*-*	*22*	*22*
New allowances	*9,850*	*537*	*10,387*
Reversal of allowances no longer required	*(256)*	*-*	*(256)*
Recoveries of amounts written off in previous periods	*-*	*-*	*-*
Allowance for credit losses	***9,594***	***537***	***10,131***
Balance at 31 December	***47,994***	***809***	***48,803***
Individually assessed	*43,477*	*22*	*43,499*
Collectively assessed	*4,517*	*787*	*5,304*
Total credit losses allowance against loans and off balance positions	***47,994***	***809***	***48,803***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The Bank is active in wholesale markets. Accordingly, its portfolio of financial assets comprises a relatively small number of individually significant claims, rather than a large number of individually insignificant claims as would be the case for financial institutions acting in retail markets. This means that each claim due to the Bank is subject to individual impairment review at the reporting date taking account of the factors described in Note 3k.

Impairment loss allowances on not credit-impaired financial assets and off balance sheet exposures are made up by 12 month ECL (Stage 1) and lifetime ECL (Stage 2), and total £8,664,000 for 2018.

Collective impairments in 2017 arose in respect of the Bank's exposures with similar risk characteristics for which previous experience indicated that impairment had taken place at the balance sheet date, but whose existence has not yet emerged. The Bank assessed its collective impairment at £5,304,000 for 2017. This covered all of the Bank's exposures (excluding those that are individually provided for, and net of eligible credit mitigation) and included an increased emphasis on sectors which were under a greater level of stress.

Further information with regard to impaired and other facilities is shown in the table below. There were a total of 16 impaired facilities at 31 December 2018 (*2017: 7 facilities*), with new impairment allowances recognised for 14 of those facilities during the year (*2017: 5 facilities*). Of the 16 facilities impaired as at 31 December 2018, 9 facilities had no collateral in place (*2017: 4 facilities*).

	2018		*2017*	
	Number of Facilities	**Gross Exposure**	*Number of Facilities*	*Gross Exposure*
Impaired facilities				
Total impaired facilities	16	219,533	*7*	*83,715*
Impaired facilities against which there was no collateral	9	158,708	*4*	*51,500*
Of the above:				
Facilities formally restructured on terms which may be less favourable to the Bank (impairment in respect of this facility £2,487,043)	1	16,352	-	-
Facilities in the process of being restructured as at the reporting date. Impairment in respect of these facilities £6,038,789 (2017: £2,715,011)	2	12,710	*2*	*20,221*
Companies in liquidation. Impairment in respect of these facilities £1,223,612 (2017: £24,609,771)	2	3,508	*1*	*24,610*
Waiver on repayments. Impairment in respect of these facilities £31,339,485 (2017: £2,000,834)	3	84,959	*1*	*6,669*
Shortfall to be paid on maturing underlying contracts (impairment in respect of this facility £7,857,691)	1	41,179	-	-
Unimpaired facilities subject to forbearance, restructuring or close monitoring				
Watchlist or substandard facilities subject to closer monitoring than normal	3	2,761	*8*	*38,018*
Relaxations of material covenants or temporary relaxations of repayment terms at reporting date	-	-	*1*	*458*
Breach of covenant, which is being addressed	2	10,582	*2*	*10,913*

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Forbearance: as part of its banking and trade services business the Bank may renegotiate loans to customers in financial difficulties (referred to as 'forbearance' activities) to maximise collection opportunities and minimise the risk of default. Loan forbearance may be 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 may include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants.

'Watchlist' items are so designated where there may have been some deterioration in the financial strength of the counterparty. The Bank may have granted forbearance in such cases, or may simply be monitoring the position more closely with no element of forbearance granted.

Impact of multiple economic scenarios on the ECL and sensitivity to alternative assumptions

The ECL recognised in the financial statements reflects the effect on expected credit losses of a range of possible outcomes, calculated on a probability-weighted basis, based on the economic scenarios. The probability-weighted amount is typically a higher number than would result from using only the base economic scenario. Credit losses and defaults typically have a non-linear relationship to the many factors which influence credit losses, such that more favourable macroeconomic factors do not reduce expected losses as much as less favourable macroeconomic factors increase expected losses.

The credit impairment provision is sensitive to reasonably possible alternative economic scenarios and weightings. A 10% increase in the scenario weighting of the downturn scenario (from 10-25% to 20-35%), coupled with a 10% decrease in the weighting of the BAU scenario (from 70-85% to 60-75%) would result in an increase of £0.7 million in the impairment provision. Applying a weighting of 100% to the downside scenario would result in an increase of £5.8 million in the impairment provision.

14. Income tax

	2018	*2017*
Current tax		
Total UK corporation tax (credit)/charge	(257)	*122*
Of which: amount recognised in other comprehensive income	-	-
Current tax on items taken through the income statement	(257)	*122*
Current tax adjustment in respect of previous periods	24	*(198)*
Deferred tax (note 24)		
Origination and reversal of timing differences	416	*214*
Effect of tax rate change	(17)	*4*
Deferred tax adjustment in respect of previous periods	-	*25*
Deferred tax adjustment in respect of unused losses	(224)	*273*
	175	*516*
Total income tax charge / (credit)	**(58)**	*440*

The tax charge on the profit for the year is based on the average UK corporation tax rate of 19% *(2017: 19.25%)*. A reduction in the UK corporation tax rate to 19% (effective from 1 April 2017) and to 17% (from 1 April 2020) was substantively enacted on 6 September 2016. Deferred tax as at 31 December 2018 has been calculated taking into account the impact of these rates.

The tax charge for the year is lower *(2017: lower)* than the charge resulting from applying the standard rate of UK corporation tax. The differences are explained below:

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

	2018	*2017*
(Loss)/Profit on ordinary activities before tax	**(35,366)**	*7,265*
(Loss)/Profit on ordinary activities multiplied by standard rate of corporation tax in the UK	(6,719)	*1,398*
Effects of:		
Chargeable gains	-	*-*
Adjustment in respect of previous periods	24	*(198)*
Effect of change in tax rate	(17)	*4*
Non taxable income	(4)	*(32)*
Non deductible items	71	*160*
Losses on which no deferred tax has been recognised	7,068	*-*
Prior period losses recognised as a deferred tax asset	(224)	*273*
Losses on which prior period losses have been utilised	-	*(1,165)*
Other items	(257)	*-*
Total income tax charge / (credit)	**(58)**	*440*

Income tax recognised in other comprehensive income is made up as follows:

		2018			*2017*	
	Before tax	Tax	Net of tax	*Before tax*	*Tax*	*Net of tax*
Actuarial gain/(loss) on pension fund	(1,075)	183	(892)	*1,277*	*(217)*	*1,060*
Change in fair value of equity investments designated at FVOCI	(928)	177	(751)			
Change in fair value of debt securities designated at FVOCI	(5,950)	1,156	(4,794)	*-*	*-*	*-*
Fair value losses/(gains) attributable to FVOCI financial assets transferred to income	373	(71)	302	*-*	*-*	*-*
Change in fair value of available for sale financial assets	-	-	-	*5,137*	*(866)*	*4,271*
Fair value losses/(gains) attributable to available for sale financial assets transferred to income	-	-	-	*(4,587)*	*871*	*(3,716)*
	(7,580)	**1,445**	**(6,135)**	***1,827***	***(212)***	***1,615***

The analysis below has been compiled on the basis of the location of office where transactions are recorded.

		2018			
Nature of activities	**Geographical location**	**Turnover**	**Loss before tax**	**Corporation tax paid**	**Average number of employees**
Banking	United Kingdom	5,793	(35,366)	782	228

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

			2017		
Nature of activities	*Geographical location*	*Turnover*	*Profit before tax*	*Corporation tax refund*	*Average number of employees*
Banking	*United Kingdom*	*43,265*	*7,265*	*(1,774)*	*211*

Turnover above has been defined as net operating income. No public subsidies were received during the reporting year. This disclosure has been prepared in accordance with the Capital Requirements (Country-by-Country Reporting) Regulations 2014.

15. Financial investments

	2018	*2017*
Debt issued by governments and multilateral development banks	1,456,160	*652,731*
Other listed debt securities issued by banks	297,132	*112,681*
Other listed debt securities issued by non-banks	9,342	*11,426*
Debt securities held for trading	4,922	*3,690*
Total debt securities	**1,767,556**	***780,528***
Equity shares and investment funds	**6,610**	***7,538***
	1,774,166	***788,066***

An impairment loss allowance of £369,000 related to debt securities is shown against other comprehensive income.

Debt securities with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £1,204,445,000 *(2017: £94,537,000).*

Equity shares comprise long-term participations of not more than 10% of the share capital of the following company: International Company for Leasing SAE: 1,727,999 ordinary shares of Egyptian Pounds 10.

Investment funds comprise long-term participations in limited partnership investment funds managed by third parties, whose purpose is to identify growing companies in the Middle East North Africa region.

Equity shares and investment funds are categorised by the Bank as “Level 3” investments (see Note 7). The movements on these investments were as follows:

	2018	*2017*
Balance at 1 January	7,538	*8,790*
Changes in fair value during the year	(928)	*(1,046)*
Realised (gain)/loss	-	*-*
Disposals	-	*(206)*
Balance at 31 December	**6,610**	***7,538***
Comprising:		
Equity shares	1,964	*1,868*
Investment funds	4,646	*5,670*
	6,610	***7,538***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

16. Loans and advances to banks

	2018	*2017*
Funds held at correspondent banks	369,113	*274,942*
Professional market placements	255,424	*153,580*
Term lending	165,235	*221,558*
Bills discounted	207,837	*364,885*
Overdrafts and other advances	2,695	*3,634*
Less: Provisions for impairments (note 13)	(2,876)	*(1,089)*
	997,428	***1,017,510***

The following tables show the gross carrying amount and impairment loss allowances subject to 12 month and lifetime ECL on loans and advances to banks at amortised cost at 1 January 2018 and at 31 December 2018.

The opening gross carrying amount and impairment loss allowance on loans and advances to banks at amortised cost is presented as those subject to 12 month and lifetime ECL measurement following the adoption of IFRS 9, with no comparative restatement of 31 December 2017 positions, which are measured under IAS 39. The Bank had no financial assets that were initially purchased or originated credit-impaired during the year ended 31 December 2018.

31 December 2018

Gross exposure	Stage 1	Stage 2	Stage 3	Total
Funds held at correspondent banks	369,114	-	-	369,114
Professional market placements	255,424	-	-	255,424
Term lending	127,432	37,803	-	165,235
Bills discounted	200,004	7,366	467	207,837
Overdrafts and other advances	2,193	0	502	2,695
Total	**954,167**	**45,168**	**969**	**1,000,304**

Impairment allowance	Stage 1	Stage 2	Stage 3	Total
Funds held at correspondent banks	(22)	-	-	(22)
Professional market placements	(34)	-	-	(34)
Term lending	(725)	(226)	-	(950)
Bills discounted	(864)	(33)	(468)	(1,365)
Overdrafts and other advances	(2)	(0)	(502)	(504)
Total	**(1,648)**	**(259)**	**(970)**	**(2,876)**

Net Exposure	Stage 1	Stage 2	Stage 3	Total
Funds held at correspondent banks	369,092	-	-	369,092
Professional market placements	255,390	-	-	255,390
Term lending	126,708	37,577	-	164,285
Bills discounted	199,139	7,333	(0)	206,471
Overdrafts and other advances	2,191	0	(0)	2,190
Total	**952,519**	**44,910**	**(1)**	**997,428**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

1 January 2018

Gross exposure	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Funds held at correspondent banks	*274,942*	-	-	*274,942*
Professional market placements	*153,580*	-	-	*153,580*
Term lending	*221,558*	-	-	*221,558*
Bills discounted	*364,885*	-	-	*364,885*
Overdrafts and other advances	*228*	-	*3,406*	*3,634*
Total	***1,015,194***	**-**	***3,406***	***1,018,600***

Impairment allowance	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Funds held at correspondent banks	*(3)*	-	-	*(3)*
Professional market placements	*(224)*	-	-	*(224)*
Term lending	*(1,168)*	-	-	*(1,168)*
Bills discounted	*(1,735)*	-	-	*(1,735)*
Overdrafts and other advances	*(1)*	-	-	*(1)*
Total	***(3,131)***	**-**	**-**	***(3,131)***

Net Exposure	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Funds held at correspondent banks	*274,939*	-	-	*274,939*
Professional market placements	*153,356*	-	-	*153,356*
Term lending	*220,390*	-	-	*220,390*
Bills discounted	*363,151*	-	-	*363,151*
Overdrafts and other advances	*227*	-	*3,406*	*3,633*
Total	***1,012,063***	**-**	***3,406***	***1,015,470***

The following table shows the reconciliation from the opening to the closing balance of the impairment loss allowance.

	Provision for impairments			
	Stage 1	**Stage 2**	**Stage 3**	**Total**
Balance as at 1 January	3,130	-	-	3,130
Transfer to Stage 1	3	(3)	-	
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	-	-
Change in other risk parameter (incl change in account balances)	(2)	3	-	1
New financial assets originated or purchased	1,939	259	970	3,168
Financial assets that have been derecognised	(3,423)	-	-	(3,423)
Write-offs	-	-	-	-
Unwind of discount	-	-	-	-
Foreign exchange and other movements		-	-	
Balance as at 31 December	**1,648**	**259**	**970**	**2,876**

Loans and advances to banks with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £nil (*2017: £531,000).*

Professional market placements includes £134,745,000 *(2017: £nil)* lent to other institutions against the security of OECD government debt securities by way of sale and repurchase transactions executed in accordance with market standard terms (reverse repo transactions).

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

17. Loans and advances to customers

	2018	*2017*
Professional market placements to non banks	191,951	*190,047*
Term and Real Estate lending	721,135	*688,562*
Bills discounted	26,484	*-*
Overdrafts and other advances	228,515	*236,885*
Less: Provisions for impairments (note 13)	(86,924)	*(46,905)*
	1,081,161	***1,068,589***

The following tables show the gross carrying amount and impairment loss allowances subject to 12 month and lifetime ECL on loans and advances to customers at amortised cost at 1 January 2018 and at 31 December 2018.

The opening gross carrying amount and impairment loss allowance on loans and advances to customers at amortised cost is presented as those subject to 12 month and lifetime ECL measurement following the adoption of IFRS 9, with no comparative restatement of 31 December 2017 positions, which are measured under IAS 39. The Bank had no financial assets that were initially purchased or originated credit-impaired during the year ended 31 December 2018.

31 December 2018

Gross exposure	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Professional market placements to non banks	191,951	-	-	191,951
Term and Real Estate lending	495,951	129,119	96,065	721,135
Bills discounted	26,484	-	-	26,484
Overdrafts and other advances	112,431	1,349	114,735	228,515
Total	**826,817**	**130,468**	**210,801**	**1,168,085**

Impairment allowance	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Professional market placements to non banks	-	-	-	-
Term and Real Estate lending	(1,417)	(3,371)	(49,595)	(54,383)
Bills discounted	-	-	-	-
Overdrafts and other advances	(413)	()	(32,128)	(32,541)
Total	**(1,830)**	**(3,371)**	**(81,723)**	**(86,924)**

Net Exposure	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Professional market placements to non banks	191,951	-	-	191,951
Term and Real Estate lending	494,533	125,748	46,470	666,752
Bills discounted	26,484	-	-	26,484
Overdrafts and other advances	112,019	1,348	82,608	195,975
Total	**824,987**	**127,097**	**129,078**	**1,081,161**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

1 January 2018

Gross exposure	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Professional market placements to non banks	*190,047*	*-*	*-*	*190,047*
Term and Real Estate lending	*526,674*	*78,263*	*83,625*	*688,562*
Bills discounted	*-*	*-*	*-*	*-*
Overdrafts and other advances	*236,885*	*-*	*-*	*236,885*
Total	***953,606***	***78,263***	***83,625***	***1,115,494***

Impairment allowance	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Professional market placements to non banks	*-*	*-*	*-*	*-*
Term and Real Estate lending	*(1,864)*	*(4,963)*	*(43,478)*	*(50,305)*
Bills discounted	*-*	*-*	*-*	*-*
Overdrafts and other advances	*(1,094)*	*-*	*-*	*(1,094)*
Total	***(2,958)***	***(4,963)***	***(43,478)***	***(51,399)***

Net Exposure	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Professional market placements to non banks	*190,047*	*-*	*-*	*190,047*
Term and Real Estate lending	*524,810*	*73,300*	*40,148*	*638,258*
Bills discounted	*-*	*-*	*-*	*-*
Overdrafts and other advances	*235,791*	*-*	*-*	*235,791*
Total	***950,648***	***73,300***	***40,148***	***1,064,096***

The following tables show reconciliations from the opening to the closing balance of the impairment loss allowance.

	Provision for impairments			
	Stage 1	**Stage 2**	**Stage 3**	**Total**
Balance as at 1 January	2,958	4,963	43,478	51,399
Transfer to Stage 1	302	(1,695)		(1,394)
Transfer to Stage 2	(567)	2,137		1,570
Transfer to Stage 3	(443)	(842)	26,183	24,899
Change in other risk parameter (incl change in account balances)	351	(856)	19,730	19,225
New financial assets originated or purchased	2,572	330	16,498	19,400
Financial assets that have been derecognised	(4,067)	(965)	(26,108)	(31,140)
Write-offs	-	-	-	-
Unwind of discount	-	-	-	-
Foreign exchange and other movements	724	298	1,942	2,964
Balance as at 31 December	**1,830**	**3,371**	**81,723**	**86,923**

Loans and advances to customers with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £nil (*2017: £4,701,000).*

Professional market placements comprises £191,951,000 *(2017: £190,047,000)* lent to other institutions against the security of OECD government debt securities by way of sale and repurchase transactions executed in accordance with market standard terms (reverse repo transactions).

18. Operating lease commitments

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The leasehold land at the Bank's main office is categorised as an operating lease, as is a sub-lease of part of the premises (see Note 19). The Bank has obligations to make payments for ground rent in its capacity as lessee, and is entitled to rental and service charge receipts in its capacity as sub-lessor. The Bank's leases in relation to the office facilities rented by the representative offices are also categorised as operating leases.

The amounts shown below are the minimum non-cancellable amounts payable in relation to both the Bank's main office and the representative offices. They take account of a long-term basic rent obligation up to August 2147 for the Bank's main office, as well as short-term additional obligations, in the Bank's position as lessee. They also take account of receivables in respect of a sub-lease entered into by the Bank as lessor during 2014 for five years.

The lease premium (prepaid over the lease term), is disclosed in Note 21.

31 December 2018	**Less than one year**	**Between one and five years**	**More than five years**	**Total**
Operating lease payments due	360	445	9,813	10,618
Operating lease receipts due	(33)	-	-	(33)
Net payment / (receipt) commitment	**327**	**445**	**9,813**	**10,585**

31 December 2017	*Less than one year*	*Between one and five years*	*More than five years*	*Total*
Operating lease payments due	*148*	*473*	*9,893*	*10,514*
Operating lease receipts due	*(238)*	*(33)*	*-*	*(271)*
Net payment / (receipt) commitment	***(90)***	***440***	***9,893***	***10,243***

19. Property, plant and equipment and intangible assets

	Property, plant and equipment			**Intangible assets**	
	Long leasehold premises and improvements	**Other assets**	**Total**	**Computer software**	**Total**
Cost					
Balance at 1 January 2018	15,616	2,897	18,513	11,870	30,383
Additions during the year	497	147	644	5,744	6,388
Disposals during the year	(3)	(68)	(71)	-	(71)
At 31 December 2018	16,110	2,976	19,086	17,614	36,700
Less: accumulated depreciation					
Balance at 1 January 2018	8,021	2,201	10,222	5,074	15,296
Charge for the year	324	214	538	486	1,024
Disposals during the year	(2)	(50)	(52)	-	(52)
Impairment loss	-	-	-	1,100	1,100
At 31 December 2018	8,343	2,365	10,708	6,660	17,368
Net book value at 31 December 2018	**7,767**	**611**	**8,378**	**10,954**	**19,332**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Cost					
Balance at 1 January 2017	*15,433*	*2,682*	*18,115*	*8,393*	*26,508*
Additions during the year	*202*	*270*	*472*	*3,477*	*3,949*
Disposals during the year	*(19)*	*(55)*	*(74)*	*-*	*(74)*
At 31 December 2017	*15,616*	*2,897*	*18,513*	*11,870*	*30,383*
Less: accumulated depreciation					
Balance at 1 January 2017	*7,680*	*1,947*	*9,627*	*4,385*	*14,012*
Charge for the year	*341*	*308*	*649*	*689*	*1,338*
Disposals during the year	*-*	*(54)*	*(54)*	*-*	*(54)*
Impairment loss	-	-	-	-	-
At 31 December 2017	*8,021*	*2,201*	*10,222*	*5,074*	*15,296*
Net book value at 31 December 2017	***7,595***	***696***	***8,291***	***6,796***	***15,087***

The long leasehold premises are at 8-10 Mansion House Place, London EC4N 8BJ. No future lease payments are due in respect of these premises (although they are in respect of land, see Note 18).

The net book value of £7,767,000 *(2017: £7,595,000)*, including improvements, excludes the lease of land, which is accounted for as an operating lease, and which has a balance sheet value represented by a prepayment (see Note 21) of £8,036,000 *(2017: £8,132,000)*, making a total asset value of £15,803,000 *(2017: £15,727,000)*. On 31 March 2018, the Bank received a valuation report in connection with this asset prepared by qualified chartered surveyors familiar with the market for such assets estimating that the market value of the Bank's interest at that time amounted to £29,350,000. This valuation will be updated in 2023.

Other assets comprise: technology hardware; furniture, fixtures and fittings; and motor vehicles.

Additions during the year of £6,388,000 *(2017: £3,949,000)* including expenditure of £5,709,000 *(2017: £3,342,000)* related to Enterprise Architect intangible assets for the new core banking system. In evaluating the recoverable amount of intangible assets the directors have considered future profitability of the Bank.

The original cost of fully depreciated tangible and intangible assets still in use by the Bank at year end was £10,065,000 (*2017: £9,213,000*).

There were commitments for capital expenditure on 31 December 2018 of £240,000 (*2017: £119,000*).

20. Derivatives

Derivative positions at 31 December were as follows:

		31 December 2018	
	Contract amount	**Positive fair values (Assets)**	**Negative fair values (Liabilities)**
Spot and forward foreign exchange contracts held for trading purposes	554,298	1,070	681
Interest rate swaps held for trading	17,668	121	-
Interest futures held for trading purposes	951,628	20	400
Options on foreign exchange for trading purposes	116,967	38	38
		1,249	**1,119**

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

	31 December 2017		
	Contract amount	*Positive fair values (Assets)*	*Negative fair values (Liabilities)*
Spot and forward foreign exchange contracts held for trading purposes	*208,346*	*489*	*1,207*
Interest rate swaps held for trading	*4,885*	*-*	*28*
Interest rate swaps qualifying as fair value hedges	*16,654*	*46*	*-*
Interest futures held for trading purposes	*144,332*	*12*	*36*
		547	***1,271***

The Bank's activities expose it primarily to the financial risk of changes in foreign currency exchange rates, and interest rates. The Bank uses foreign exchange forward contracts and options, interest rate swaps and futures, and similar instruments to hedge these exposures. Derivative positions may also be held for trading purposes.

Foreign exchange risk

A spot foreign exchange transaction is an agreement between two parties to buy one currency against selling another currency at an agreed price for settlement on the spot date.

A forward foreign exchange contract is an agreement by which a fixed amount of one currency is exchanged for a fixed amount of a different currency on a specified future date. The contract amount in the table above is the amount receivable.

A foreign exchange option contract is an agreement that gives the right but not the obligation to exchange money denominated in one currency into another currency at a pre-agreed exchange rate on a specified date. Foreign exchange options at fair value through the profit and loss account represent either contracts executed for customers against similar contracts with market counterparties, or else represent trading positions.

Interest rate risk

An interest rate swap is an agreement through which two parties agree to exchange interest rate cash flows, based on a specified notional amount from a fixed rate to a floating rate (or vice versa) or from one floating rate to another.

Interest rate swaps qualifying as fair value hedges are entered into in order to allow the Bank to more easily accommodate within its risk management policies interest bearing assets or liabilities with fixed interest rates.

Interest rate swaps at fair value through the profit and loss account represent hedges of economic exposure, but not qualifying for hedge accounting in accordance with IAS39. Interest rate cap, collar and floor contracts at fair value through the profit and loss account are regarded as being hedges of economic exposures, but do not qualify for hedge accounting in accordance with IAS39.

Interest rate futures are exchange traded contracts whose price is determined by reference to changes in interest rates between the date the contract is entered into, and the valuation date, calculated in respect of notional deposits with future start and maturity dates. Interest rate futures at fair value through the profit and loss account comprise economic hedges against fixed rate banking book positions. Interest rate futures held for trading comprise economic hedges against trading book positions.

Derivatives entered into by the Bank are in accordance with standard market terms.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

21. Prepayments, accrued income and other debtors

	2018	*2017*
Prepaid rental for land	8,069	*8,132*
Prepayments and accrued income	1,051	*74*
Unsettled trade receivables	-	*48,386*
Other debtors	7,695	*5,981*
	16,815	***62,573***

The prepaid rental for land arises from its treatment as an operating lease and represents the lease premium in respect of land being expensed over the lease term. The Bank is also obliged to pay ground rent in respect of its leasehold land interest over the remaining life of the lease. Both of these expenses for the year are disclosed in Note 11. Future commitments in respect of ground rent are disclosed in Note 18.

Unsettled trade receivables as at 31 December 2017 were amounts due from forward foreign exchange swaps.

22. Deposits

Deposits from banks totalled £3,047,548,000 (*2017 £2,095,638,000*) of which deposits with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £95,769,000 *(2017: £47,164,000).*

Other deposits totalled £585,058,000 (*2017: £555,556,000*) of which deposits with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £26,616,000 *(2017: £27,427,000).*

The Bank did not default on any principal or interest, nor did it breach any covenants with respect to its own liabilities during the year.

23. Other liabilities, accruals and deferred income

	2018	*2017*
Other liabilities	8,582	*7,741*
Accruals and deferred income	5,419	*1,469*
Loss allowance provision on financial guarantees and other commitments (note 30)	2,043	*809*
	16,044	***10,019***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

24. Deferred taxation

	Balance at 1 January 2018	Recognised in Profit or Loss	Recognised in Other Comprehensive Income	Balance at 31 December 2018	Deferred tax assets	Deferred tax liabilities
Property, plant and equipment and intangible assets	(199)	-	-	(199)	-	(199)
Staff benefits	93	(24)	-	69	69	-
Unused tax losses loss carried forward	806	224	-	1,030	1,030	-
Tax assets on pension liabilities (note 25)	150	(232)	183	100	100	-
Debt securities classified at fair value through OCI	(318)	-	1,085	767	767	-
Equity Investments classified at fair value through OCI	(191)	-	177	(14)	-	(14)
IFRS 9 Transitional adjustment	1,304	(143)	-	1,161	1,161	-
Deferred tax assets (liabilities)	**1,645**	**(175)**	**1,445**	**2,914**	**3,127**	**(213)**

Deferred tax asset and liability balances are off-settable.

The Bank has recognised a deferred tax asset of £1,030,000 in respect of tax losses brought forward (*2017: £806,000*). The Bank has unused tax losses of £42,173,000 (*2017: £5,766,000*) for which no deferred tax asset is recognised in the Statement of Financial Position. These losses do not have a fixed expiry date.

25. Pension funds

Defined benefit scheme

The Bank sponsors the Scheme which is a funded defined benefit arrangement and which closed to future pension accrual during 2014. This is a separate trustee administered fund holding the pension scheme assets to meet long-term liabilities for 269 deferred or pensioner members as at 31 December 2018 *(2017: 280 deferred or pensioner members)*. The level of retirement benefit is based on basic salary at 1 April 2014, or on leaving the scheme if earlier than this, and is linked to changes in inflation up to retirement.

The Scheme is subject to the funding legislation, which came into force on 30 December 2005, outlined in the Pensions Act 2004. This, together with documents issued by the Pensions Regulator and Guidance Notes adopted by the Financial Reporting Council, set out the framework for funding defined benefit occupational pension schemes in the UK.

The trustees of the Scheme are required to act in the best interest of the Scheme's beneficiaries. The appointment of the trustees is determined by the Scheme's trust documentation. It is policy that at least one third of all trustees should be nominated by the members.
This actuarial valuation showed a deficit of £5,283,000. The company has agreed with the trustees that it will aim to eliminate the deficit over a period of 3 years and 8 months from 1 January 2017 by the payment of annual contributions of £1,472,000, payable in monthly instalments, in respect of the deficit. In addition and in accordance with the actuarial valuation, the Bank agreed with the trustees that it will pay monthly contributions of £20,000 in respect of the expenses of the scheme and that it will also meet the levies payable to the Pension Protection Fund. From 1 July 2018, the monthly contributions of £20,000 ceased with the Bank instead agreeing to meet the expenses directly.

The Bank has considered the impact of IFRIC 14 and concluded that the Bank would have an unconditional right to any residual surplus from the Scheme.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

For the purposes of IAS19 the actuarial valuation as at 31 December 2016 has been updated on an approximate basis to 31 December 2018. There have been no changes in the valuation methodology adopted for this year's disclosures compared to the previous year's disclosures.

Amounts included in the statement of financial position

	2018	*2017*
Fair value of Scheme assets	72,023	*80,220*
Present value of defined benefit obligation	(72,607)	*(81,118)*
Deficit in the Scheme - net liability	**(584)**	***(898)***

The present value of Scheme liabilities is measured by discounting the best estimate of future cash flows to be paid out by the Scheme using the projected unit credit method. The value calculated in this way is reflected in the net liability on the balance sheet as shown above. Consistent with the Bank's strategy to reduce future risk, the Scheme has purchased insurance policies to match the liabilities in relation to the pensioner members. A further buy-in was completed in 2015 and the liabilities related to all pensioner members as at that time were fully insured.

The projected unit credit method is an accrued benefits valuation method in which allowance is made for projected earnings increases. The accumulated benefit obligation is an alternative actuarial measure of the Scheme liabilities, whose calculation differs from that under the projected unit credit method in that it includes no assumption for future earnings increases. In assessing this figure for the purpose of these disclosures, allowance has been made for future statutory revaluation of benefits up to retirement. At the balance sheet date the accumulated benefit obligation was £72,607,000 (i.e. the same as the defined benefit obligation).

All actuarial gains and losses will be recognised in the year in which they occur in Other Comprehensive Income (OCI).

Reconcilation of opening and closing present value of the Defined Benefit Obligation

	2018	*2017*
Defined benefit obligation at start of period	81,118	*85,315*
Expenses	196	*203*
Interest expense	1,954	*2,254*
Actuarial losses due to scheme experience	424	*(2,250)*
Actuarial losses due to changes in demographic assumptions	11	*(2,129)*
Actuarial gains/(losses) due to changes in financial assumptions	(4,971)	*1,589*
Benefits paid and expenses	(6,125)	*(3,864)*
Defined benefit obligation at end of period	**72,607**	***81,118***

The Scheme closed to future accrual on 1 April 2014. The curtailment has been measured at this date based on actuarial assumptions consistent with market conditions at this date. The curtailment measures the reduction in liabilities due to active members' benefits no longer being linked to future salary growth.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Reconciliation of opening and closing values of the Fair Value of Plan Assets

	2018	2017
Fair value of scheme assets at start of period	80,220	*81,708*
Interest income	1,947	*2,177*
Return on scheme assets (excluding amounts included in interest income)	(5,611)	*(1,513)*
Contributions by the Bank	1,592	*1,712*
Benefits paid and expenses	(6,125)	*(3,864)*
Fair value of scheme assets at end of period	**72,023**	***80,220***

The actual return on the Scheme's assets over the year ended 31 December 2018 was (£3,662,000).

Defined benefit costs recognised in Profit and Loss

	2018	2017
Expenses	196	*203*
Net interest cost	5	*77*
Defined benefit costs recognised in profit and loss	**201**	***280***

Defined benefit costs recognised in other Comprehensive Income

	2018	2017
Return on scheme assets (excluding amounts included in interest income) - gain/(loss)	(5,611)	*(1,513)*
Experience losses arising on the defined benefit obligation	(424)	*2,250*
Effects of changes in the demographic assumptions underlying the present value of the defined benefit obligation - gain / (loss)	(11)	*2,129*
Effects of changes in the financial assumptions underlying the present value of the defined benefit obligation - gain / (loss)	4,971	*(1,589)*
Total amount recognised in other comprehensive income - gain / (loss)	**(1,075)**	***1,277***

Assets

	2018	2017
Liability Driven Investment (LDI)	11,716	*15,194*
Diversified Growth Funds	21,031	*22,955*
Cash	629	*296*
Purchased Annuities	38,647	*41,775*
Total assets	**72,023**	***80,220***

None of the fair values of the assets shown above include any direct investments in the Bank's own financial instruments or any property occupied by, or other assets used by, the Bank. All of the Scheme assets have a quoted market price in an active market with the exception of the Purchased Annuities and the Scheme bank account balance.

It is the policy of the trustees and the Bank to review the investment strategy at the time of each funding valuation. The trustees' investment objectives and the processes undertaken to measure and manage the risks inherent in the Scheme investment strategy are documented in the Scheme's Statement of Investment Principles.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

Significant Actuarial Assumptions

	2018 % per annum	*2017 % per annum*
Rate of discount	2.85	*2.50*
Inflation (RPI)	3.30	*3.30*
Allowance for revaluation of deferred pensions of RPI or 7.5% p.a. if less	3.30	*3.30*
Allowance for pension in payment increases of RPI or 7.5% p.a. if less	3.30	*3.30*
Allowance for commutation of pension for cash at retirement	75% of Post A-Day	*75% of Post A-Day*

The mortality assumptions adopted at 31 December 2018 are 100% of the standard tables S2PxA_L, Year of Birth, no age rating for males and females, projected using CMI_2017 (CMI Mortality Projection Model) converging to 1.00% p.a. These imply the following life expectancies:

	2018	*2017*
	Life expectancy at age 60 (years)	*Life expectancy at age 60 (years)*
Male retiring in 2018	27.6	*27.7*
Female retiring in 2018	28.6	*28.7*
Male retiring in 2028	28.1	*28.2*
Female retiring in 2028	29.3	*29.3*

The following table analyses of the sensitivity to the principal assumptions of the present value of the Defined Benefit Obligation:

	Change in assumption	***Change in liabilities***
Discount rate	Decrease of 0.25% p.a.	*Increase by 4.7%*
Rate of inflation	Increase of 0.25% p.a.	*Increase by 4.7%*
Rate of mortality	Increase in life expectancy of 1 year	*Increase by 3.6%*
Rate of mortality	Mortality improvement - long term rate 0.75%	*Decrease by 0.9%*
Cash commutation	50% of post A-day maximum using current factors	*Increase by 1.1%*

The sensitivities shown above are approximate. Each sensitivity calculation considers one change in isolation. The inflation sensitivity includes the impact of changes to the assumptions for revaluation and pension increases. The average duration of the defined benefit obligation at the year ended 31 December 2018 is 19 years.

The Scheme typically exposes the Bank to actuarial risks such as investment risk, interest rate risk, mortality risk and longevity risk. A decrease in corporate bond yields, a rise in inflation or an increase in life expectancy would result in an increase to Scheme liabilities. This would detrimentally impact the balance sheet position and may give rise to increased charges in future profit and loss accounts. The trustees have in part managed these risks by securing some pensioner liabilities with insurance policies which exactly match the benefits provided under the Scheme.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The best estimate of contributions to be paid by the Bank to the scheme for the year commencing 1 January 2019 is £1,472,000.

Defined contribution scheme

At 31 December 2018 183 employees *(2017: 166 employees)* were members of the BACB Defined Contribution Retirement Benefit Scheme. Contributions to this Scheme are made by both employer and employee in accordance with a fixed formula. In the year ended 31 December 2018, the Bank paid £1,548,000 *(2017: £1,393,000)* by way of contributions into that scheme. There were no outstanding or pre-paid contributions to this scheme at 31 December 2018 *(2017: £nil)*.

26. Subordinated liabilities

Subordinated loans in issue are denominated in US dollars and Euros, and are subordinated in all respects to the claims of other creditors. The loans can only be repaid before their due dates either on liquidation of the borrower after all other claims have been satisfied, or with express permission granted by the Prudential Regulation Authority. The loans, which have been subscribed in full by the Bank's principal shareholder, Libyan Foreign Bank, qualify for inclusion in the Bank's capital base as Tier 2 capital as at 31 December 2018 and bear interest based on inter-bank offered rates for dollar and euro deposits. The amounts disclosed below include accrued interest.

	2018	*2017*
Due 29 April 2023	19,604	*18,445*
Due 29 October 2025	24,960	*23,484*
Due 17 June 2025	30,757	*30,373*
	75,321	***72,302***

27. Called up share capital

Authorised share capital comprises 115,000,000 Ordinary Shares of £1 each, 140,000,000 Ordinary Shares of US$1 each and 5,000,000 Deferred Non-Voting Shares of £1 each. Each paid up Ordinary £1 share carries the same rights as each paid up Ordinary $1 share. No rights attach to the Deferred Non-Voting shares until such time as they become paid up.

Issued share capital comprises:

	Number of shares ('000)		**Paid up amount**	
	2018	*2017*	**2018**	*2017*
Ordinary Shares of £1 each fully paid	30,403	*30,403*	30,403	*30,403*
Ordinary Shares of US$1 each fully paid	115,488	*115,224*	73,954	*73,746*
Deferred Non-Voting Shares of £1 each nil paid	5,000	*5,000*	-	-
	150,891	***150,627***	**104,357**	***104,149***

On 31 December 2018, the Bank issued 264,396 US Dollar ordinary shares of $1 each, creating £207,926 of new equity capital.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

28. Capital and reserves attributable to the Bank's equity holders

	2018	*2017*
Called up share capital (note 27)	104,357	*104,149*
Capital redemption reserve	4,104	*4,104*
Other reserves		
Retained earnings	62,796	*106,861*
Revaluation Reserve	(3,079)	*1,719*
	59,717	108,580
	168,178	***216,833***

The Capital Redemption reserve arose on the purchase and cancellation of issued share capital in 2008.

The Revaluation reserve arises in respect of changes in the market value of assets categorised as being fair value through other comprehensive income (Note 3g).

Retained earnings and the Revaluation reserve are available for distribution subject to the maintenance of adequate capital resources.

The directors declared a dividend of £1,706,000 in respect of the year ended 31 December 2018 *(2017: £nil).*

29. Capital maintenance

The Bank's capital comprises share capital and reserves (Note 28) and subordinated liabilities (Note 26). It is subject to the regulatory capital requirements of the Prudential Regulation Authority. The Bank's objectives in the management of capital are to maintain appropriate levels of capital to support its business strategy and to meet its regulatory requirements.

Capital resources are made up by:

	2018	*2017*
Capital and reserves attributable to the Bank's equity holders	168,178	*216,833*
Less: Intangible Assets	(10,954)	*(6,796)*
Less: Adjustments as required by regulations	(1,777)	*(790)*
Add: IFRS9 transition adjustment	5,771	-
Tier 1 capital	**161,218**	*209,247*
Subordinated liabilities less accrued interest	74,880	*71,962*
Less: amortisation of subordinated liabilities	(2,616)	-
Tier 2 capital	**72,264**	*71,962*
Capital resources	**233,482**	***281,209***

The Bank's surplus Tier 1 capital over the total regulatory minimum as at 31 December 2018 required utilisation of regulatory stress buffers totalling £29.7m. Surplus total capital over the total regulatory minimum as at 31 December 2018 required utilisation of regulatory stress buffers totalling £1.0m. This is discussed further in the Strategic Review.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

30. Financial guarantees and other commitments

The Bank extends commercial facilities to customers which provide for the issuance of performance guarantees, bid and bail bonds, and other types of guarantees.

From 1 January 2018 financial guarantees and other commitments have been classified and measured in accordance with IFRS 9. This involves measuring the loss allowance provision for financial guarantees and other commitments on a 12 month or lifetime ECL approach.

Prior to the adoption of IFRS 9, provisions in respect of financial guarantees and other commitments were measured in accordance with IAS 37. Prior period comparative figures have not been restated.

	2018	*2017*
Financial guarantes	122,386	*54,051*
Other commitments comprise:		
Credit lines and other commitments to lend: original maturity		
under one year	76,524	*112,045*
over one year	-	*13,309*
Documentary credits and short-term trade-related transactions	474,229	*400,924*
Own acceptances	5,577	*6,643*
	678,716	***586,973***

The following tables show the contract amount and loss allowance provisions subject to 12 month and lifetime ECL on financial guarantees and other commitments at 1 January 2018 and at 31 December 2018.

31 December 2018

Contract amount	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Financial guarantees	99,528	15,432	7,427	122,387
Other commitments	553,804	2,188	337	556,329
Total	**653,332**	**17,620**	**7,764**	**678,716**

Loss allowance provision	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Financial guarantees	(412)	(18)	(1,119)	(1,548)
Other commitments	(443)	(1)	(51)	(495)
Total	**(854)**	**(19)**	**(1,170)**	**(2,043)**

1 January 2018

Contract amount	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Financial guarantees	*36,292*	*17,293*	*22*	*53,607*
Other commitments	*530,019*	*2,781*	*-*	*532,800*
Total	***566,312***	***20,074***	***22***	***586,408***

Loss allowance provision	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Financial guarantees	*(142)*	*(22)*	*(20)*	*(184)*
Other commitments	*(1,310)*	*(2)*	*-*	*(1,312)*
Total	***(1,453)***	***(24)***	***(20)***	***(1,496)***

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

The loss allowance provision as at 31 December 2017 was £809,000 and was measured under IAS 39.

The following tables show reconciliations from the opening to the closing balance of the contract amount and the loss allowance provision.

	Provision for impairments			
	Stage 1	**Stage 2**	**Stage 3**	**Total**
Balance as at 1 January	1,452	24	20	1,496
Transfer to Stage 1	3	(3)	-	
Transfer to Stage 2	-	-	-	-
Transfer to Stage 3	-	-	254	254
Change in other risk parameter (incl change in account balances)	(45)	2	2	(41)
New positions originated or purchased	633	2	894	1,529
Financial assets that have been derecognised	(1,247)	(7)	-	(1,254)
Foreign exchange and other movements	58	1	-	59
Balance as at 31 December	**854**	**19**	**1,170**	**2,043**

31. Foreign currency assets / liabilities

Foreign currency assets and liabilities for the Bank were as follows:

31 December 2018	**Sterling**	**Dollars**	**Euro**	**Other currencies**	**Total**
Total assets	724,078	2,327,008	799,336	43,430	3,893,852
Total equity and liabilities	(585,142)	(2,431,094)	(851,536)	(26,080)	(3,893,852)
Derivatives (at contract notional value)	(135,244)	101,490	51,298	(17,544)	-
Net exposures	**3,692**	**(2,595)**	**(903)**	**(195)**	**-**
Contingent liabilities and other commitments	67,632	404,875	196,515	9,694	678,716

31 December 2017	*Sterling*	*Dollars*	*Euro*	*Other currencies*	*Total*
Total assets	*695,305*	*1,635,773*	*604,709*	*17,069*	*2,952,856*
Total equity and liabilities	*(725,280)*	*(1,666,619)*	*(547,735)*	*(13,222)*	*(2,952,856)*
Derivatives (at contract notional value)	*29,503*	*31,163*	*(57,608)*	*(3,058)*	*-*
Net exposures	***(472)***	***317***	***(634)***	***789***	***-***
Contingent liabilities and other commitments	*78,813*	*320,470*	*173,212*	*14,477*	*586,972*

The Bank's policies for managing the risk of exchange revaluations on foreign currency assets and liabilities are explained in Note 4.

32. Legal proceedings

In late 2014, the Bank initiated a review of certain historical activities which involved a voluntary self-disclosure to the U.S. Authorities of transactions which may have violated certain U.S. sanctions principally related to Sudan.

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

In June 2019, the Bank agreed a settlement of $4 million (£3 million) with the U.S. Office of Foreign Assets Control although no liability has been admitted. A formal settlement agreement will follow at which point the timing of outflows will be confirmed. This has been recognised at the end of the period in the Statement of Comprehensive Income as a Regulatory Charge of £3 million (2017: £nil). Discussions with the U.S. Department of Justice are at a preliminary stage but no liability is expected.

No further civil or criminal enforcement proceedings are pending or threatened.

33. Business line review

The Bank has six business lines which comprise its principal operating departments. While sharing customers in common, the departments offer different products and services with different risk and operational characteristics. Internal management information is constructed to measure separately the operational and risk characteristics of these departments, together with the resources they consume, and the financial results that they produce. Business decisions are made with reference to risk adjusted return on capital. The summary below describes the operations of each of the Bank's business lines:-

- Trade Finance. The provision of payment and other guarantee type facilities in support of the international trade ambitions of its customers.
- Real Estate Lending. The Bank provides finance to investors in respect of residential properties in Central London and commercial properties in England.
- Commodity Finance. The provision of short-term secured facilities to commodity companies to support their day-to-day trading activities.
- Term Lending. The Bank provides lending facilities principally in support of the Bank's core trade and commodity finance businesses.
- Banking Services. The Bank acts as a banking correspondent for its customers providing tailored account and international payment services.
- Treasury. In addition to servicing the Bank's own funding and market risk management requirements, the Treasury provides access to the international financial markets for the Bank's customers, and assumes a limited amount of market risk by way of own account trading activities.
- Other. This represents items not specifically allocated to the Bank's business lines, principally rental income, returns on investments and foreign exchange revaluation.

Information regarding the results of each business line is included below. Performance is measured based on net business line profit as included in the internally generated management information and is stated after charging (or crediting) interest between business lines in respect of the assets or liabilities which either require or generate funding. There are no other significant transactions between business lines.

Operating income before allowance for credit losses by business line is as follows:

31 December 2018	Trade Finance	Real Estate	Commodity Finance	Lending	Banking	Treasury	Other	Total
Net interest income	6,857	9,899	5,527	4,859	4,142	5,922	-	37,207
Net fee and commission income	17,221	155	2,736	101	2,272	(191)	-	22,295
Net trading income	-	-	-	-	-	5,358	-	5,358
Other operating income	-	-	-	-	-	(373)	350	(23)
Total Operating income	**24,078**	**10,054**	**8,263**	**4,960**	**6,414**	**10,716**	**350**	**64,836**

31 December 2017	*Trade Finance*	*Real Estate*	*Commodity Finance*	*Lending*	*Banking*	*Treasury*	*Other*	*Total*
Net interest income	*4,127*	*7,130*	*4,554*	*4,732*	*2,177*	*5,770*	*(72)*	*28,418*
Net fee and commission income	*10,787*	*86*	*2,500*	*1*	*2,023*	*(113)*	*-*	*15,284*
Net trading income	*-*	*-*	*-*	*-*	*-*	*4,730*	*-*	*4,730*
Other operating income	*-*	*-*	*-*	*-*	*-*	*4,378*	*586*	*4,964*
Total Operating income	***14,914***	***7,216***	***7,054***	***4,733***	***4,200***	***14,765***	***514***	***53,396***

The analysis of total operating income below is based on the location of the customer giving rise to the revenue. Revenue from the Bank's main shareholder market of Libya is included within MENA and comprises 23% of the total *(2017: 13%).*

	2018	*2017*
United Kingdom	11,824	*14,413*
Europe / Americas (excl. UK)	8,186	*7,287*
MENA (incl Libya)	21,043	*15,139*
Sub - Saharan Africa	18,777	*10,494*
Asia, Levant and Other	5,006	*6,062*
	64,836	***53,396***

A number of presentation changes have been made to the geographic segmentation analysis compared to the 2017 Annual Report and Financial Statement. In 2017 BACB's geographic segments were reported as: United Kingdom, Europe (excluding UK), North Africa, Sub-Saharan Africa, Middle East and Asia, and Other. The Americas have now been included within Europe/Americas (excl. UK), and the Middle East and North Africa (which includes Libya) have been combined within MENA. Asia and Levant regions form a small percentage of the total and are combined with other. These segmental changes have been made to align the analysis with how the business is currently managed and with internal Management Information.

34. Related parties

The Bank regards the following as being related parties in accordance with IAS24:

a) The Bank regards Libyan Foreign Bank as its parent company. Libyan Foreign Bank and all of its subsidiaries, together with Libyan Foreign Bank's owner, the Central Bank of Libya and all of its subsidiaries, are considered to be related parties. The Bank considers these parties to be in a position to exert significant influence over the Bank. The Bank enters into commercial transactions in the ordinary course of business with these parties on an arm's-length basis. The ultimate parent company of the Bank is the Central Bank of Libya.

b) Key management personnel, including the Bank's directors, and identified Executive Managers.

The analysis below sets outs balances with related parties:

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

	2018	*2017*
Balances outstanding		
Loans and advances	12,068	*37,984*
Deposits	2,405,408	*1,644,487*
Subordinated liabilities	75,321	*72,302*
Derivatives (contract amount)	125	*11*
Contingent liabilities and other commitments	103,035	*99,549*
Volumes executed during the year		
Loans and advances	109,107	*700,345*
Deposits	73,346,062	*130,244,553*
Derivatives (contract amount)	9,751,778	*5,173,534*
Contingent liabilities and other commitments	164,530	*366,779*
Included in income statement		
Interest receivable	176	*33*
Interest payable	25,738	*25,874*
Fees and commissions receivable	6,259	*4,576*
Fees and commissions payable	14	*14*

At 31 December 2018 no amount was outstanding in respect of interest free loans or interest bearing loans due from Executive Managers of the Bank (*2017: £nil*). No amount was outstanding from any director.
In addition, the Bank has entered into the following related party transactions:

i. The Bank meets the employment costs of executives seconded to it by related parties. The costs of these secondments were £641,000 *(2017: £564,000)*.

ii. Key management personnel compensation:

	2018	*2017*
Directors' attendance and standing fees	555	*567*
Executive Managers		
Salaries and other short term benefits	2,070	*3,560*
Post-employment benefits	40	*83*

c) During the year the Bank received funding from the Libyan Foreign Bank and the Central Bank of Libya. The following tables set out the deposits at year end:

Funding received	2018	*2017*
Libyan Foreign Bank	898,103	*809,507*
Cental Bank of Libya	845,286	*795,687*
Total	1,743,389	*1,605,194*

Weighted average maturity	2018
Libyan Foreign Bank	0.11 years
Cental Bank of Libya	0.97 years

ALL AMOUNTS IN £'000s UNLESS OTHERWISE STATED

35. Events after the reporting period

There are no matters that have taken place since the year end that require disclosure.

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striving to make a difference