BACB

ANNUAL REPORT AND FINANCIAL STATEMENTS

year ended 31 December 2017

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British Arab Commercial Bank plc
registered number 1047302

striving to make a difference

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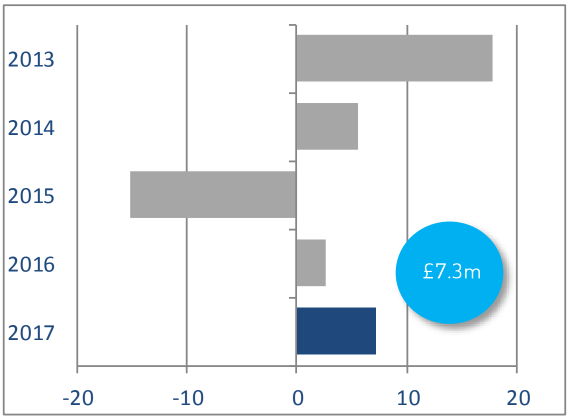
FINANCIAL HIGHLIGHTS

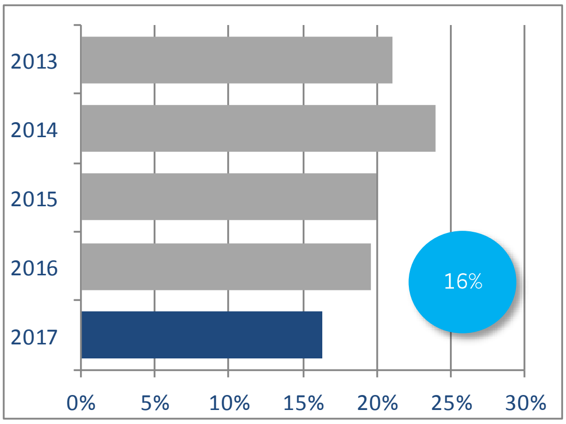
Unlocking capital to boost operating income and profit, whilst driving down the cost/income ratio

Operating Income up 25% to £53.4m

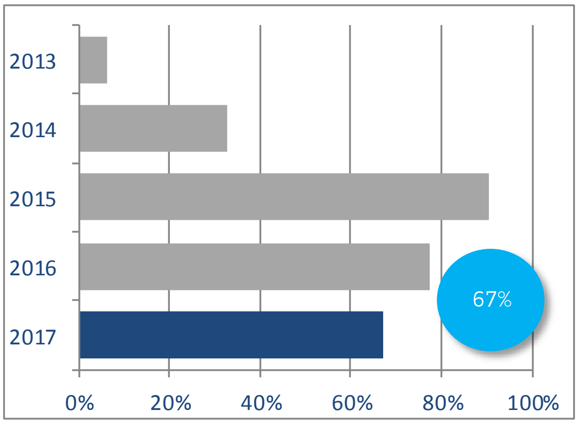
Profit/(Loss) before tax up £4.7m to £7.3m



Capital Strength above regulatory minimum at 16%



Cost/Income Ratio down to 67%



	2017	2016	2015	2014	2013
Financial Position £m					
Operating Income before Loan impairments	53.4	42.7	38.5	48.1	44.2
Profit/(Loss) before income tax	7.3	2.6	(15.1)	5.5	17.8
Profit/(Loss) for the year	6.8	2.7	(14.5)	4.7	13.8
Total Assets	2,953	2,939	3,021	2,916	2,402
Total Loans	2,086	1,624	1,596	1,765	1,608
Total Equity	217	208	210	202	197
Total Tier 1 & 2 capital (Eligible Capital)	281	278	271	255	252
Ratios %					
Capital Adequacy	16%	20%	20%	24%	21%
Cost Income Ratio*	67%	77%	90%	78%	54%
Return on Tier 1 Capital	3%	1%	(7%)	3%	9%
Return on Tier 1 & 2 (Total Eligible Capital)	3%	1%	(6%)	2%	7%
Non Performing Loans %	4%	3%	3%	2%	2%

****Based on Administrative Expenses divided by Operating Income before allowances for credit losses***

CHAIRMAN'S STATEMENT

BACB is a true niche player with a promising future

Throughout a period of profound political and economic change around the world, BACB has made progress in building long-term added value relationships, leveraging our core competency in facilitating trade and capital flow in and between our target markets. We are dedicated to the clients, communities and countries we serve, whilst also delivering a return for our shareholders.

The Bank reported profit after tax of £6.8m, some £4.1m (151%) higher than last year. This performance is a result of significant progress across all business lines, but most notably in our core trade finance business.

Let me first consider the external context.

Market environment

The global economy finally broke through the doldrums in 2017, marking the first time since 2011 that global growth has topped 3%. The stage appears to be set for continued, solid growth in 2018, with ongoing expansion anticipated in the US and emerging markets, set to offset plateauing in the Eurozone.

BACB builds value by leveraging our core competency in facilitating cross-border trade

The WTO is forecasting that global trade will expand and comments that "Trade has the potential to strengthen global growth if the movement of goods and supply of services across borders remains largely unfettered".

However, there remains a degree of unpredictability regarding the direction of the global economy and global trade flows. In 2017, trade finance revenues among the world's largest banks fell despite the fact that overall trade volumes performed well (an increase of 4.5% according to the CPB World Trade Monitor). Lack of clarity on monetary, fiscal and trade policies raises the risk that trade activity could be stifled. Furthermore, there is a risk of imposition of trade barriers, which could undermine future growth.

We continue to monitor the potential impacts of BREXIT on BACB. Our assessment remains that the direct impact will be limited, but with potential second order effects on our largely US dollar denominated balance sheet.

Looking at the Bank's core African markets, 2017 saw some moments of huge significance - leadership changes where the incumbents had been in place for decades, courts demonstrating remarkable judicial independence around elections, and citizens demanding change. 2018 may offer similar pivotal moments.

Economic growth on the African continent is expected to reach 3.5%, although progress could be undermined by instability and environmental shocks, as well as fluctuating commodity prices.

Political uncertainty in Libya, the 'home market' of BACB's majority shareholder, continues to present its own challenges. However, the will to resolve the situation remains intact and efforts continue towards agreeing a stable and lasting political solution. An important transition is ahead for Libya as a new round of UN-backed talks aims to secure a resolution to the country's political divisions and to prepare for Presidential and Parliamentary elections. Thanks in no small part to the support we have received from my fellow Directors, our principal shareholder the Libyan Foreign Bank and the Central Bank of Libya, BACB has risen to these challenges in a robust and timely manner.

The Bank's revenues from Libya are not critical to its overall performance but remain stable and, as a result of successful geographic diversification, Libya represents a much reduced share of total revenues. A return to stability in Libya offers a significant opportunity to the Bank.

Strategic direction 2017 performance

BACB's strategy is to build long-term value leveraging our core competency in facilitating cross border trade.

We continue to extend selectively into new markets, focusing on our recently opened Representative Offices in Dubai and Côte d'Ivoire, whilst also considering other sub-Saharan Africa markets. In addition, we have recently established a presence in Munich, Germany to facilitate exporter-led growth and to capture both sides of trade flows between Developed and Developing markets.

Continued growth, led by the core trade business

Our geographic diversification efforts are complemented by product diversification, with continued growth of our UK real estate and commodity finance businesses which reduce our exposure to the cyclical nature of global trade flows.

In terms of the Board's contribution to the BACB agenda, we have focused on supporting the Executive team as they drive the business forward, whilst ensuring a strong corporate governance framework, a clear risk appetite, efficient internal operations and a robust control framework.

We continue to enhance the efficiency of the operating environment. Most notably, we are investing in an upgrade of the core banking system, which will be implemented during 2018. This investment further evidences shareholder support for the BACB franchise and will help to deliver the scalable business required to support revenue and profitability growth, as well as to enhance the quality of service delivery to our clients.

The Bank's strong and committed Team remains our greatest asset. The Board takes a close interest in not just what the Bank does, but also how it goes about its business.

Future Prospects

The Bank is financially strong. We project continued growth across the business, led by the core trade finance business, underpinned by our prudent financial positioning and clearly defined risk appetite.

Our focus for 2018 is on driving the business forward, continuing to build a truly client-centric solution driven business, which will deliver long-term sustainable relationships, reinforced by a strong governance and control framework. The Bank enjoys the full support of its shareholders and benefits from a Statement of Support from the Libyan Foreign Bank, which confirms continued provision of financial and liquidity support.

I thank my fellow directors and all the staff for their valuable contributions to BACB in 2017.

R D Dowie
Chairman
23 March 2018

STRATEGIC REPORT: BUSINESS STRATEGY AND MARKET ENVIRONMENT

A new dawn for BACB

At BACB we are passionate about what we do –delivering quality solutions and services to our clients, making a difference in the countries in which we do business and committing to build longer term, sustainable relationships. But it is of equal importance to understand how we operate and engage with our clients and other key stakeholders. In 2017 we launched 'The BACB Way' which defines our 'Conduct and Culture' strategy that is underpinned by the four pillars of: Leadership, Behaviours, Competencies and Values. 'The BACB Way' is our manifesto for 'what we do' (conduct) and 'how we do it' (culture) – it is this framework, coupled with the cultural diversity of the Bank's staff and the experience gained over 45-years of dealing in difficult markets and challenging economic conditions, that will enable it to continue to offer its clients valuable access to important markets and position itself for future sustainable growth.

The provision of trade finance solutions is at the core of our business operating model. The global trade finance market is in the main liquid and well-functioning, particularly between developed markets. It has, however, experienced periods of stress, most notably right after the financial crisis in 2008, but now it is beginning to undergo structural change in response to the relaxation of economic sanctions. However, following the 2017 change in the US Administration, there is also a degree of uncertainty about whether these changes will last. International economic sanctions are a common and recurring feature of political interactions between states. It is the United States which has most frequently applied negative economic sanctions. In a parallel way, several measures, imposed by a multilateral organisation like the United Nations, have also taken place in recent years.

Making a difference in the countries where we do business and committing to build longer term, sustainable relationships

Trade agreements also have a major impact on trade and investment worldwide. They are responsible for shaping business relationships among companies across the globe. In order to succeed in the international market, small business exporters need to be aware of the impact trade agreements have had and will have on their businesses. Likewise, lenders must be familiar with trade agreements in order to better understand the needs and financial concerns of their customers.

Recent political events, such as the UK BREXIT vote and President Trump's intention to review the trade agreements of the USA and the possible implementation of trade tariffs, mean that both new bilateral and multilateral trade agreements will influence the size and shape of future international trade flows.

Given the prevailing political and economic uncertainty, it is therefore not surprising that many large multi-national banks, which have historically dominated the financing of international trade flows, are now nervous and reluctant to commit to new trade finance activity, particularly where it is needed the most - in and across emerging markets. This situation is exacerbated by the increasingly burdensome and costly regulatory compliance requirements associated with doing business in 'more challenging' markets.

To the external observer it does, however, appear unusual for banks not to commit to supporting trade finance business when losses on short-term trade finance portfolios historically have been extremely low. Moreover, given their short-term nature, banks have been able to quickly reduce their exposures in times of stress.

The result is a growing funding gap for trade finance. The African Development Bank estimates that this currently amounts to some $120bn for sub-Saharan Africa alone and it is the 'Small and Medium sized Enterprises' , which are typically the engine room for economic growth, that are suffering the most.

This is where banks such as BACB have an important role to play. At the heart of our business strategy is a commitment to providing trade finance support and solutions to clients and banks in and across emerging markets, but with a particular focus on the trade and capital flows into and out of Africa. We understand the need not just to sell product, but also to develop long term sustainable relationships with our clients in order to better understand their unique problems and to provide bespoke solutions.

BACB has a long standing and well-deserved reputation for being the 'go to' bank for trade finance in our target markets

BACB has a long standing and well-deserved reputation for being the 'go to' bank for trade finance in our target markets. Over the past 12-months we have seen our trade finance volumes grow by more than 50% to over 2,200 transactions and the underlying value has more than doubled to $3.3bn.

The lifting of economic sanctions on Sudan in October 2017 has now permitted the Bank to re-enter a market where it has enjoyed considerable success in the past and, coupled with an improving but still modest level of business from Libya, the outlook for further growth in trade finance is encouraging.

But it is also important to ensure the long term stability of the Bank by developing complementary businesses to balance its trade finance franchise. Relying solely on trade finance flows, particularly between emerging markets, can result in a vulnerability to economic cyclicality and geopolitical risk. It is for this reason that over the past few years we have not only diversified our geographic focus, but also further developed alternative revenue streams.

In this regard, we have built a real estate business that focuses on providing residential finance to high net worth investors in the 'Golden Postcodes' of London, and to commercial business opportunities in England where there are stable underlying cash flows. The real estate book currently stands at around £437m (with undrawn commitments of a further c.£70m) and it generates a sustainable and predictable source of revenue across a diversified portfolio of assets, underpinned by conservative loan to value margins.

Our commodity finance business has also been a focus for continued growth and we have seen outstandings on this book of assets grow from $70m 3-years ago to $350m today, with projected growth by the end of 2018 to $500m. This is a great business for the bank to be in because it enables us to leverage our access to a plentiful supply of short-term funding to support transactions which are secured and self-liquidating.

The Bank's Treasury department continues to manage the balance sheet carefully and prudently. Given the concentration of funding from the Bank's Libyan shareholders, and notwithstanding the historic stability of these funds and the strategic importance of BACB in providing the Libyan economy with access to the international financial markets, we ensure the Bank's liquidity always remains considerably in excess of the regulatory minima. In this regard, and with a view to diversifying our source of funding, we aim to launch a UK retail deposit initiative in 2018. Our ability to access retail deposits will support the accumulation of stable, longer term GBP liquidity and the partial matched funding of our UK real estate portfolio.

Helping to build trade relations between the UK and developing markets

BACB operates as a UK bank out of London, regulated by the Prudential Regulation Authority and the Financial Conduct Authority, which reinforces its position as a safe, secure and financially stable organisation with which to do business. We recognise the significant advantages of being able to play the 'UK' card and, in this regard, have both hosted and participated in trade missions between the UK and its target markets. We consider ourselves advocates in helping to build trade relations between the UK and the developing markets, not just by helping to bring about change, but by being part of it.

BACB is evidence that a bank does not always have to be big or, indeed, a household name in order to be successful. The Bank is an unashamedly niche player that knows what it is good at, and can deliver the type and quality of service that clients trading in and between emerging markets require in order for them to be successful. Through building sustainable partnerships with clients in our target markets, often when the scale or complexity of the business opportunities are not aligned to the strategies of the larger and more established financial institutions, BACB has been able to support the growth of local economies and at the same time establish a profitable operating model benefitting its clients and shareholders whilst supporting the impetus that the UK must now build to establish bilateral trade agreements post-BREXIT.

In 2017 BACB celebrated its 45th anniversary as a British bank. Throughout its existence it has had a primary focus on delivering trade finance solutions to clients in some of the more challenging countries around the world and prided itself on being able to help and support the development of trade and capital flows in and between those economies that might otherwise struggle to access the services of an international bank.

So, as ever, at BACB we will continue striving to make a difference!

P.A. Hartwell
Chief Executive Officer
23 March 2018

STRATEGIC REPORT: BUSINESS AND PERFORMANCE OVERVIEW

OVERVIEW

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

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

Strategic Direction

The Bank 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 is in its client-centric approach and largely trade-related products and services. The Bank also offers a niche UK real estate lending business.

The Bank's strategic plan, as approved by the Board, aspires to the delivery of strong and sustainable business growth, optimal utilisation of the Bank's balance sheet, underpinned by robust risk management, governance and control structures, and increased efficiency in the Bank's operations.

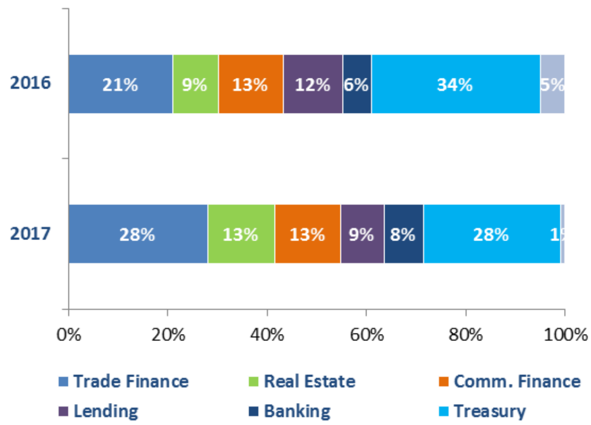
Business Overview

The Bank has six key Business lines. Trade finance, structured short and medium-term lending, commodity finance, treasury and banking services are all complementary to the core trade franchise. The development of the real estate finance business forms part of the Bank's strategy to diversify its income streams and to deliver sustainable revenue growth and provide some level of protection against the cyclical nature of global trade.

In addition, the Bank has a growing syndication and distribution business, which will be leveraged as the Bank looks to more effectively utilise its balance sheet.

Trade finance alone contributed 28% of operating income in 2017 and was a key area of growth during the year. Trade related activity accounts for 50% of the Bank's revenue.

Operating Income by Business Line (excludes credit provisions)



The Bank maintains a modest risk appetite by mainly lending short-term and secured through the underlying asset.

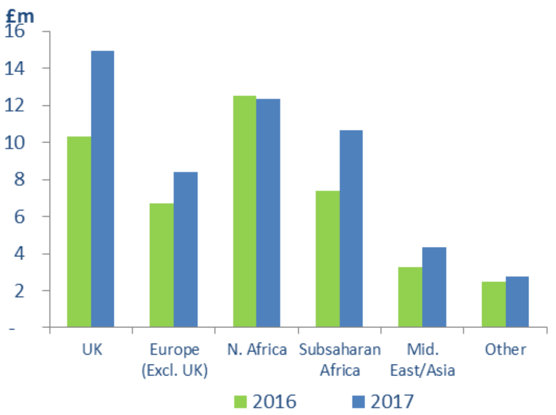
Core to BACB's franchise is its trade related business

The Business mix demonstrates a healthy balance across the Bank's key business lines and an increasingly balanced spread of geographies from which the Bank's revenues derive as a result of targeted geographic diversification.

A significantly reduced portion of the Bank's revenues emanate from Libya compared to 3 years ago, and most of the Libyan exposures are cash collateralised. These steps mitigate the idiosyncratic risk posed to the business by continuing instability in Libya – the home market of the Bank's principal shareholder.

While Libya currently represents a reduced share of the Bank's business, it offers a significant opportunity to BACB when this strategically important country returns to stability.

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 risk appetite and trade finance expertise, coupled with multi-lingual staff and a deep understanding of our target markets, ensure 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 Algiers, Tripoli, Abidjan and Dubai.

The Bank's trade finance business was the 'star performer' in 2017 with year on year revenue growth of 67%. Over 2,200 transactions were processed with a value in excess of $3.3bn, being more than double the value in 2016. The Trade Finance portfolio increased from $0.7bn at the end of 2016 to $1.2bn at the end of 2017.

Our business strategy targets an increased focus on exporter-driven business, where our corporate clients have trade flows with developing markets, thus enabling us to capture the business by leveraging our network and capabilities from both a buyer and a seller perspective.

The recently opened offices in Abidjan and Dubai have generated increased contribution and are expected to be key contributors to the Bank's future growth plans.

We have recently received approval to open a Representative Office in Munich, Germany. This location which was specifically targeted as a significant manufacturing hub, which will allow us to further develop our trade finance capabilities and to optimally support trade flows from Germany to our target markets.

Lending

The Bank's lending strategy requires that new lending is linked to our own direct client relationships principally in support of the core trade, commodity finance and real estate businesses.

We only participate in other banks' syndicated transactions where the business is trade-related or promotes the development of bilateral client relationships.

The Bank's lending business lines comprise:

- **Term Lending:** mainly structured loan facilities to corporate borrowers and 'vanilla' loans, principally where they are complementary to our core trade finance business;
- **Real Estate:** term lending facilities secured against high quality UK real estate assets, both residential and commercial; and
- **Commodity Finance:** short-term structured facilities to commodity traders secured by the underlying commodities.

Term and real estate lending balances increased to £0.9bn at December 2017.

The movement in the lending book during 2017 has involved a considerable positive shift in the quality of new lending activity, in line with the Bank's lending strategy and risk appetite.

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.

As at 2017 Year End, the **UK real estate** book stood at £437m (48% of total lending), and revenues increased by 85% in the year. This book is secured on high quality residential and commercial assets, with conservative loan to value ratios. 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.

2017 saw continued strong growth in our **commodity finance** business. This business provides bilateral financing facilities, principally to UK and European trading companies. The facilities are on-demand overdrafts or short-term (30-180 days) for the financing of purchases and sales of commodities by those companies. The facilities are secured by title to the underlying predominantly pre-sold goods.

Banking Services

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

Treasury

The Treasury department continued to undertake the dual role of servicing the needs of our clients in the global markets and acting as corporate treasury on behalf of the Bank.

The Treasury department provides the Bank's clients with access to the London financial markets, servicing their requirements in the interest rate, foreign exchange, derivative and debt capital markets.

The needs of our clients are serviced through responsive and competitive pricing in the international bond markets, specialising in the African, Turkey and niche regional debt markets. Foreign exchange is an additional key service, offering access to liquidity via leading edge FX trading portals; we seek to provide more competitive rates than can be found locally by our clients. The Bank also offers a discrete range of structured products and Islamic finance.

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.

Treasury combines the aforementioned client mandate with the management of the Bank's own financial resources, including its balance sheet structure, cash flow, liquidity management and hedging.

Under the requirements of the UK regulatory liquidity rules, the Bank maintains a High Quality Liquid Asset portfolio comprising OECD government and multilateral development bank fixed and floating rate securities. These instruments tend to yield a return commensurate to their risk rating which the Bank seeks to supplement by way of a separate investment portfolio of bank and corporate debt securities issued principally by investment grade rated entities.

FINANCIAL RESULT

The 2017 result is a Profit after Tax of £6.8m *(2016: £2.7m)*.

The 2017 result reflects considerable success in all business lines as the Bank continues to deliver sustainable and complementary revenue streams.

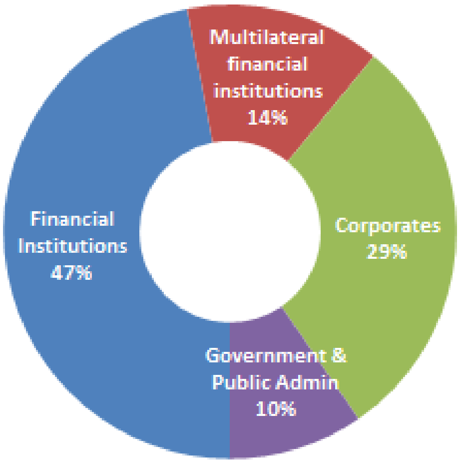
The Bank has a clear strategy for driving future business growth and an increasingly scalable business model to support this growth. The Bank's key performance indicators (KPIs) are shown on page 2.

Operating Income

Operating income for the year was £53.4m, an increase of £10.7m (25%) compared to 2016. This financial performance reflects considerable success as the Bank continues to develop sustainable and complementary revenue streams, with particularly strong growth in the core trade finance, commodity finance and real estate businesses.

The Bank's revenues continue to be largely derived from financial counterparties, including multilateral development banks, followed by governmental bodies and carefully targeted corporates.

Credit Exposure by Counterparty type



Allowances for Credit Losses

The 2017 allowance for credit losses amounted to £10.1m *(2016: £7.1m)*. Overall, only a very small number of the Bank's facilities are impaired and non-performing loans represent only 4.0% of total loans *(2016: 3.4%),* of which 1.2% relates to just one non-performing loan in Morocco.

The Bank's level of provisioning continues to reflect a desire to ensure that all known and emergent risks are adequately provided for.

In recognition of the prevailing market conditions and in accordance with industry norms, the Bank has maintained its collective impairment provision at £5.3m *(2016: £5.8m)*.

The collective provision is expected to offset a substantial component of the one-off impact on transition to an IFRS9 compliant 'Expected Credit Loss' (ECL) approach to credit provisions. Under IFRS 9, which is effective January 1 2018, the ECL would increase by c.£3m compared with the position as at 31 December 2017 and assuming the release of the existing collective, which is no longer required.

Administrative Expenses

At £36.0m *(2016: £33.0m)*, administrative expenses increased by 9% year-on-year.

The average number of employees during 2017 was 211 *(2016: 181).* Total staff costs have increased by 17% to £24.7m, which principally reflects an investment in revenue generating staff in order to grow the business. This includes staff in the recently established Representative Offices.

Other Administrative Expenses increased by £0.7m during the year, mainly due to technology costs and in part related to the core banking system upgrade, as well as increased costs related to the new Representative Offices. A one-off cost recovery of £1.2m was received during the year. 'Exceptional' costs of £0.4m *(2016: £1.7m)* relate to the review of historic business activities.

The Bank's cost income ratio reduced by 10% during the year to 67%.

The Bank continues to invest in initiatives to strengthen the operating environment and to position itself for future growth. This will be further supported by the investment in the new core banking technology platform, Temenos T24.

It is anticipated that the business will become increasingly scalable, with future business growth not requiring a commensurate increase in costs.

FINANCIAL POSITION

Totals assets were broadly flat year-on-year.

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

	2017	*2016*
	£'000	*£'000*
Financial investments	788,066	*1,288,442*
Loans and advances to banks	1,017,510	*759,716*
Loans and advances to customers	1,068,589	*864,311*
Property, plant and equipment	8,291	*8,488*
Other	70,400	*18,307*
Balance sheet footings	**2,952,856**	***2,939,264***
Contingent liabilities	54,051	*57,123*
Other commitments	532,921	*308,915*

Growth in loans and advances to customers were offset in large part by reductions in liquid assets and inter-bank placements

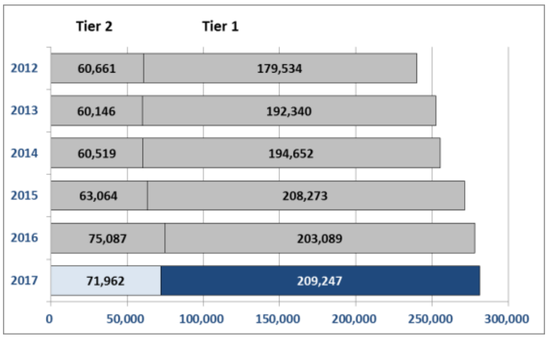
Contingent liabilities relate to guarantees issued, and other commitments are principally made up by documentary credits, credit lines and loan commitments.

Capital Adequacy

The Bank's Tier 1 capital of £209m *(2016: £203m)* comprises share capital and reserves (adjusted as required by regulations) less intangible assets.

Tier 2 capital comprises issued term subordinated debt of £72m *(2016: £75m)*, the year-on-year reduction being entirely due to foreign exchange conversion impacts.

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 2017.

Capital Requirement and Capital in Place

	2017	*2016*
	£'000	*£'000*
Credit, Counterparty, CVA risk	130,931	*106,612*
Market risk	651	*194*
Operational risk	6,339	*6,518*
Total Pillar 1 capital requirement	**137,921**	***113,324***
Capital in place	281,209	*278,176*
Excess of capital in place over minimum requirement under Pillar 1	**143,288**	***164,852***

As at 31 December 2017 the Bank's capital adequacy ratio was 16% *(2016: 20%)*.

The year-on-year increase in capital requirement, and consequent reduction in the capital ratio, reflects success during the year in building up business assets, particularly in the core trade finance business and the UK real estate lending business. This 'business' asset growth has been offset by an anticipated reduction in Treasury assets, as we continue to strive to ensure optimal use of the Bank's balance sheet capacity.

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; as a consequence, its funding base remains concentrated but nevertheless has remained stable. During the year, the Bank was successful in renewing key deposits from its parent, the Libyan Foreign Bank.

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 intends to diversify its sources of funding 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 that is aligned to and calibrated with the requirements of a British bank operating in our target markets. Accordingly, the detail and impact of new regulations are continually monitored and reviewed.

Significant regulatory and compliance tasks in 2017 included the embedding of the Senior Management and Certification Regime and its extension to include the Individual Accountability Regime and Non-Executive Directors, embedding the fourth Money Laundering Directive, a Supervisory Review of the Bank's Individual Liquidity Adequacy Assessment Process (ILAAP), preparation for MiFID II (and it's go-live in January 2018) and the new General Data Protection Regulations, as well as actively managing other regulatory changes.

We recognise the criticality of the Bank's regulatory reporting and risk management capabilities, both of which have been independently assessed and validated.

We continue to focus on our Financial Crime responsibilities. Going forward, this critical area will be separated out from Compliance as a 'Principal Risk' type as outlined in Note 4. Furthermore, we have implemented enhancements in both our organisation structure and data resources in order to further enhance the Bank's capabilities in this key area.

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.

A comprehensive Enterprise Architecture review has defined the Bank's technology requirements over a 5-year horizon, considering technology advances as well as the Bank's strategic business plan.

This review culminated in a decision to invest in a significant upgrade of the core banking platform, as well as continuing to deliver incremental enhancements in the Bank's technology systems. The decision to replace the core banking system further evidences the long-term commitment and support of the Bank's shareholders.

The first phase, a major upgrade to the IT infrastructure was completed in 2016 providing increased stability, reliability and productivity to the general IT and end-user working environment. The second phase, the upgrade to our core banking system and the implementation of the Temenos T24 platform will be completed during 2018. We regularly test our IT security capabilities and are committed to a continuous programme of enhancing our operational resilience.

Progress continues to be made to further strengthen systems and controls to protect the Bank from cyber and other data security risks. During 2017 we implemented a fully autonomous 'immune system' for cyber and data security defence.

Internal Audit

The Internal Audit function is independent of the business and has a primary reporting line to the Chairman of the Audit and Risk 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 and Risk Committee.

Human Resources

During the course of 2017, the senior management team progressed a number of initiatives to further embed the Bank's People Strategy.

We are committed to being an equal opportunities employer that values diversity in its broadest sense in order to ensure access to the best pool of talent we can find.

Our people are our most important asset

Culture and Conduct: During 2017, the Bank launched its new cultural manifesto and code of conduct in the form of 'The BACB Way'.

We are committed to promoting an inclusive environment where everyone plays their part in ensuring that the needs of our customers remain paramount, and where everyone has an opportunity to succeed and be rewarded fairly for their endeavours.

We continue to focus on two core values, namely, client focus and teamwork.

Performance Management: The Bank-wide performance appraisal process aligns reward recommendations with our People Strategy. During 2017, we further embedded our approach 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, always ensuring adherence to 'The BACB Way'.

The level of performance awards increased in 2017 to £2.4m *(2016: £2.0m)* as a result of the increase in headcount and in recognition of the need to reward and retain key talent.

Leadership Development: Employee development is critical to any high performing organisation. During 2017, we have focused on developing the skills and competencies of our manager population.

Diversity: The Bank is proud of its diverse and inclusive workplace, which is also reflective of the communities in which we do business. We approach diversity in the broadest sense, recognising that successful businesses flourish through 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 2017 were again presented with a Platinum award in recognition of our standards.

Charitable support: In 2017, the Bank made charitable donations of £4,700 (*2016: £2,000*) including support for employee fundraising through the Bank's "£ for £" scheme, matching fund raising up to £500 per employee per year.

The Bank also facilitates "Give As You Earn" charitable giving by employees, as well as matching holiday days for staff who undertake volunteer work in the UK or overseas.

STRATEGIC REPORT: PRINCIPAL RISKS AND UNCERTAINTIES

The Bank's overarching risk management objectives are to operate within a clearly articulated risk appetite and 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 specific governance standards covering eight 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.

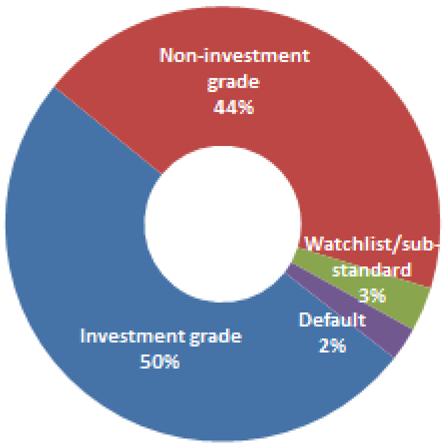
The Bank's strategic geographical focus means that a significant portion of credit risk is aligned to the lower end of the credit grading spectrum. However the nature of the Bank's trade and commodity finance business streams generally involves short-term, secured and self-liquidating exposures, with 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;
- Business asset decision making made with reference to risk adjusted return criteria.

More than half of the Bank's exposures are classed as investment grade.

Credit Exposure by Grade

Rated by BACB internal grading system



Of the Bank's total credit exposures, 3.4% by value are on the 'watch-list' and 2.4% are classified as impaired. The individually assessed impairment charge relates to a small number of exposures only, with more than half related to just one exposure.

In addition, to the specific impairment provisions, the Bank maintained a collectively assessed impairment provision of £5.3m in 2017 *(2016: £5.8m)*, which covers all the Bank's non-impaired exposures. This provision will offset a significant amount of the impact of transition to an IFRS9 compliant Expected Credit Loss model effective 1 January 2018.

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, future credit losses and the Bank's ability to raise new secured funding at a reasonable haircut.

Libya Political challenges

The political challenges in Libya continue to be the subject of much interest.

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 3% of total exposures and a substantial portion of this is cash collateralised. 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.

Other Initiatives

The Bank continues to consider options to diversify its funding base. An initiative to source UK retail deposits is at an advanced stage of due diligence.

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 Board is reassured by the continuing stability of the Bank's principal correspondent bank and other counterparty bank relationships, including the ability to open new correspondent banking relationships when needed.

Other Important Risks

The Bank faces a range of other risks including reputational, 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 2017 culminating in the launch of its new code of conduct 'The BACB Way', which is described more fully in the preceding Business Overview.

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.

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.

It is worthy of note that the international money-laundering watchdog, the Financial Action Task Force (FATF), recently confirmed that Libya complies with all the requirements and obligations to combat money laundering and terrorism financing crimes, in accordance with international standards.

The Bank-wide project to upgrade the core banking IT system continues, with a target implementation during mid-2018. This will significantly rationalise the Bank's IT infrastructure. Other projects, including Regulatory change initiatives, are subject to close oversight by Executive Management and the Board.

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 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 (87.8%);
- Banque Extérieure d'Algérie (6.1%); and
- Banque Centrale Populaire (6.1%).

Libyan Foreign Bank ('LFB') has a substantial international portfolio of investments, involving over 40 participations in 25 countries. In its latest accounts (unaudited), LFB reported total assets of c.$19bn and net assets of c.$5bn, 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 Internal Audit function acting as the third-line of defence and providing independent assurance to the Audit and Risk 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 2017, the following individuals served on the Board:

Board Member	Sub-Committee Member	Status
Mr Robert D. Dowie CHAIRMAN	ARC/NRC/ECC	I-NED
Mr Mohamed Shokri VICE-CHAIRMAN	ARC / NRC	NED
Mr Ahmed Aburkhis	ARC / NRC	NED
Mrs Susannah Aliker[3]		EXEC DIR
Dr Ezzeddin Ashur	NRC/ ECC	NED
Mr Akram Grew	ECC	NED
Mr Paul Hartwell		EXEC DIR
Dr Khaled Kagigi [1]	ARC	I-NED
Mr Abdullah Naama		NED
Mr Brahim Semid[3]		NED
Mr Michael Stevenson	ARC (Chair)/ NRC	I-NED
Mr Mohamed Zine	ARC	NED

Note 1: Dr K. Kagigi was reclassified as an Independent Non-Executive Director on 27th January 2017.
Note 2: Mr M. Norris resigned from the Board on 21st August 2017.
Note 3: Mrs S. Aliker and Mr B. Semid were appointed to the Board on 15th September 2017.

The Board includes three independent non-executive directors, one of whom is the Chair of the Board and one of whom is the Chair of the Audit and Risk Committee. The Chief Executive and the Chief Financial Officer are full time employees of the Bank and are regarded as Executive Directors. All of the other directors are regarded as Non-Executive Directors.

The Board met on 6 occasions during 2017.

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.

External Credit Committee ("ECC")

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 External Credit Committee for consideration and approval. The Committee considers applications as they arise.

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 and Risk Committee ("ARC")

Non-Executive Directors are eligible to sit on the Audit and Risk 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, compliance and risk management.

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

The Audit and Risk Committee met seven times during 2017.

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
- MD Corporate and Institutional Banking
- MD Marketing and Communications

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:

ExCo receives reports from the Sub-Committee Chairs at each meeting in order to ensure appropriate oversight over key matters.

The ExCo meets monthly throughout the year.

STRATEGIC PLANNING

The Board is fully engaged in driving the strategic direction of the Bank. A Board Strategy meeting takes place on an annual basis.

The Business Plan aspires to the delivery of strong business growth in the Bank's target markets and products, underpinned by robust risk management and governance, and increased efficiency in the Bank's operations.

The Board considers that the Bank is strongly positioned to achieve these goals.

The Strategic Report was approved by the Board of Directors on 23 March 2018.

Susannah L. Aliker,
Secretary to the Board
23 March 2018

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The Directors are responsible for preparing the Strategic Report, 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 (IFRS) as adopted by the EU and applicable law.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period.

In preparing these financial statements, the Directors are required to:

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

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They 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 2017

The Directors present their annual report and the audited financial statements for the year ended 31 December 2017. 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 profit after taxation for the year amounted to £6,825,000 (2016: *£2,719,000*).

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 18. None of the Directors holds or has held shares in the Bank. All of the Directors benefited from qualifying third party indemity insurance in place during the financial year and at the date of this report.

Auditors

KPMG LLP was appointed to act as the Bank's auditors for the year ended 31 December 2017.

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 each Director has taken all steps that he ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Bank's auditors are aware of that information.

Susannah L. Aliker
Secretary
By order of the Board
23 March 2018

All amounts in £'000s unless otherwise stated

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 2017 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 2017 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the Audit and Risk 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 twenty-two financial years ended 31 December 2017.

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. Key audit matters: 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. We summarise below the key audit matters, in decreasing order of audit significance, 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.

All amounts in £'000s unless otherwise stated

The risk	Our response
Funding concentration *Refer to page 33 (Basis of preparation)*	
Loss of future liquidity 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. The political and economic situation in Libya has been volatile in recent years and the future outlook of the country remains challenging which could lead to the disruption or curtailment of the bank's primary source of funding. Future funding is a key factor for the Directors in their consideration of going concern.	**Our procedures 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; ▪ **Independent research:** Performing independent research on recent political and economic developments in Libya; ▪ **Independent Re-performance:** Re-performing calculations and agreeing data elements to underlying agreements and contracts; ▪ **Stress testing:** Using our own liquidity specialists to independently perform 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 results** ▪ We found the Bank's judgement that there was no material uncertainty to be disclosed to be appropriate.
Counterparty banks *Refer to page 33 (Basis of Preparation)*	
Loss of future trade The Bank has a concentrated number of relationships with counterparty banks and these facilities are critical to its operations. There has been a sector-wide trend in recent years for counterparty banks to review such relationships, and not take on new ones, due to the potential reputational and legal risks associated with clearing transactions initiated by other banks, particularly those who	**Our procedures 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; ▪ **Inspecting contracts**: Inspecting contracts and agreements supporting the Bank' and counterparty

All amounts in £'000s unless otherwise stated

operate with clients linked to countries perceived as higher risk.

Future correspondent banking relationships is a key factor for the Directors in their consideration of going concern.

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 Bank's judgement that there was no material uncertainty to be disclosed to be appropriate.

Individually and collectively assessed loan impairment provisions

(£48.8m; 2016: £41.0m)

Refer to page 40 (accounting policy) and pages 67-68 (financial disclosures)

Subjective estimate

These are judgemental areas due to the level of subjectivity inherent in estimating the recoverability of loan balances.

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 the collective provision and the model is reliant on certain subjective assumptions. The model is sensitive to changes 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;
- **Re-performance:** Re-performing calculations and agreeing data inputs to third party documentation, including valuation reports;
- **Our experience:** Critically assessing and challenging the assumptions used by the Bank in its impairment models 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;
- **Benchmarking assumptions:** Comparing the Bank's assumptions to independently derived data in relation to key inputs such as probability of default and loss emergence periods;
- **Sensitivity analysis:** Considering the sensitivity of the collective provisioning models to changes in the key assumptions.

Our results

- We found the individually and collectively assessed loan impairment provisions to be acceptable.

All amounts in £'000s unless otherwise stated

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

Materiality for the financial statements as a whole was set at £405,000 (2016: £585,000), 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 due to fluctuations in the business cycle, of £8.1 million (2016: £11.7 million), of which it represents 5% (2016: 5%).

We agreed to report to the Audit and Risk Committee any corrected or uncorrected identified misstatements exceeding £20,000 (2016: £29,000), 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.

The Bank is adopting IFRS 9 Financial Instruments from 1 January 2018 and has included an estimate of the financial impact of the change in accounting standard in accordance with IAS 8 Changes in Accounting Estimates and Errors as set out in note 2. This disclosure notes that the Bank continues to refine its expected credit loss model and embed its operational processes which may change the actual impact on adoption. While further testing of the financial impact will be performed as part of our 2018 year-end audit, we have performed sufficient audit procedures for the purposes of assessing the disclosures made in accordance with IAS 8. Specifically we have:

- Considered the appropriateness of key technical decisions, judgements, assumptions and elections made by management;
- Considered key Classification and Measurement decisions, including Business Model Assessments and Solely Payment of Principal and Interest (SPPI) outcomes;
- Considered transitional controls and governance processes related to the approval of the estimated transitional impact.

4. We have nothing to report on going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

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.

All amounts in £'000s unless otherwise stated

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 21, 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, other irregularities, 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. The risk of not detecting a material misstatement resulting from fraud or other irregularities is higher than for one resulting from error, as they may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control and may involve any area of law and regulation not just those directly affecting 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 relevant areas of laws and regulations that could have a material effect on the financial statements from our sector experience, through discussion with the Directors and other management (as required by auditing standards), and from inspection of the Bank's regulatory correspondence.

We had regard to laws and regulations in areas that directly affect the financial statements including financial reporting (including related company legislation) and taxation legislation. We considered the extent of compliance with those laws and regulations as part of our procedures on the related annual accounts items.

In addition we considered the impact of laws and regulations in the specific areas of 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. With the exception of any known or possible non-compliance, and as required by auditing standards, our work in respect of these was limited to enquiry of the Directors and other management and inspection of regulatory correspondence. We considered the effect of any known or possible non-compliance in these areas as part of our procedures on the related annual accounts items.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit. 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.

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

23 March 2018

All amounts in £'000s unless otherwise stated

STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2017

	Note	2017	*2016*
Interest and similar income	8	61,614	*47,872*
Less: Interest expense and similar charges	8	(33,196)	*(25,397)*
Net interest income		**28,418**	***22,475***
Fee and commission income	9	15,609	*12,335*
Less: Fee and commission expense	9	(325)	*(357)*
Net fee and commission income		**15,284**	***11,978***
Net trading income	10	4,730	*6,157*
Other operating income	11	4,964	*2,129*
Operating income before allowance for credit losses		**53,396**	***42,739***
Allowance for credit losses	13	(10,131)	*(7,122)*
Net operating income		**43,265**	***35,617***
Administrative expenses	12	(36,000)	*(33,038)*
Profit before income tax		**7,265**	***2,579***
Income tax (charge) / credit	14	(440)	*140*
Profit for the year		**6,825**	***2,719***
Other comprehensive income/(expense):			
Items that will not be reclassified to profit or loss			
Remeasurement of defined benefit liability	25	1,277	*(3,250)*
Related Tax	14	(217)	*494*
		1,060	*(2,756)*
Items that are or may be reclassified to profit or loss			
Change in fair value of available for sale financial assets		5,137	*3,522*
Fair value gains attributable to available for sale financial assets transferred to income		(4,587)	*(5,279)*
Related Tax	14	5	*17*
		555	*(1,740)*
Other comprehensive gain / (loss) for the year, net of tax		**1,615**	***(4,496)***
Total comprehensive gain / (loss) for the year		**8,440**	***(1,777)***

All of the profit for the financial year and the prior year was derived from continuing activities. The Notes on pages 33 to 85 form part of these financial statements.

All amounts in £'000s unless otherwise stated

STATEMENT OF FINANCIAL POSITION

As at 31 December 2017

	Note	2017	*2016*
Assets			
Cash, notes and coins		143	*87*
Financial investments	15	788,066	*1,288,442*
Loans and advances to banks	16	1,017,510	*759,716*
Loans and advances to customers	17	1,068,589	*864,311*
Property, plant and equipment	19	8,291	*8,488*
Intangible assets	19	6,796	*4,008*
Derivatives	20	547	*769*
Corporation tax receivable		-	*1,358*
Deferred tax assets	24	341	*1,069*
Prepayments, accrued income and other debtors	21	62,573	*11,016*
Total assets		**2,952,856**	***2,939,264***
Liabilities			
Deposits from banks	22	2,095,638	*2,019,036*
Other deposits	22	555,556	*622,896*
Other liabilities, accruals and deferred income	23	10,019	*7,959*
Derivatives	20	1,271	*1,960*
Corporation tax payable		339	*-*
Net pension liability	25	898	*3,607*
Subordinated liabilities	26	72,302	*75,413*
Total liabilities		**2,736,023**	***2,730,871***
Called up share capital	27	104,149	*104,149*
Capital redemption reserve	28	4,104	*4,104*
Other reserves	28	108,580	*100,140*
Capital and reserves attributable to the Bank's equity holders	28	**216,833**	***208,393***
Total liabilities and equity		**2,952,856**	***2,939,264***

The Notes on pages 33 to 85 form part of these financial statements.

Signed:

Mr R D Dowie
Chairman

Mr M Shokri
Vice Chairman

Mr P A Hartwell
Chief Executive

All amounts in £'000s unless otherwise stated

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2017

	Share capital	Capital redemption reserve	Other reserves			Total equity
			Retained earnings	AFS reserve	Total	
Balance at 31 December 2015	***104,149***	***4,104***	***99,013***	***2,904***	***101,917***	***210,170***
Profit for the year	-	-	*2,719*	-	*2,719*	*2,719*
Other comprehensive (loss)	-	-	*(2,756)*	*(1,740)*	*(4,496)*	*(4,496)*
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 income	-	-	1,060	555	1,615	1,615
Total comprehensive income for the period	-	-	7,885	555	8,440	8,440
Balance at 31 December 2017	**104,149**	**4,104**	**106,861**	**1,719**	**108,580**	**216,833**

All amounts in £'000s unless otherwise stated

STATEMENT OF CASH FLOW

For the year ended 31 December 2017

	Note	2017	*2016*
Cash flows from operating activities			
Profit/(Loss) before taxation		7,265	*2,579*
Adjustments for:			
Allowance for credit losses	13	10,131	*7,122*
Profit on realisation of equity shares and investments	15	-	*(3,822)*
Depreciation and amortisation	12,19	1,401	*1,694*
Loss on sale or impairment of property, plant and equipment	12	665	*(50)*
Other non-cash items included in net profit	12	(748)	*(332)*
Non-cash items included in net profit		**11,449**	***4,612***
Loans, advances and other debt securities other than cash and cash equivalents		(672,228)	*(129,256)*
Other debtors and prepayments		(51,334)	*(1,042)*
Change in operating assets		**(723,562)**	***(130,298)***
Customer accounts and deposits by banks		144,902	*(483,032)*
Other liabilities		(1,338)	*595*
Change in operating liabilties		**143,564**	***(482,437)***
Income tax received/(paid)		1,774	*2,256*
Net cash (used in)/generated from operating activities		**(559,510)**	***(603,288)***
Cash flows from investing activities			
Proceeds of redemptions of equity shares and investments	15	206	*4,058*
Purchase of property, plant and equipment	19	(472)	*(493)*
Purchase of intangible assets	19	(3,477)	*(3,014)*
Net cash used in investing activities		**(3,743)**	***551***
Net decrease in cash and cash equivalents		**(563,253)**	***(602,737)***
Cash and cash equivalents at the beginning of the year		1,226,225	*1,623,993*
Effect of exchange rate change on cash and cash equivalents		(37,719)	*204,969*
Cash and cash equivalents at the end of the year		**625,253**	***1,226,225***
Cash and cash equivalents comprise:			
Cash, notes and coin		143	*87*
Loans and advances to banks of original maturity three months or less		588,102	*427,449*
Certificates of deposit and other debt securities of three months original maturity or less		37,008	*798,689*
Cash and cash equivalents		**625,253**	***1,226,225***

All amounts in £'000s unless otherwise stated

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2017

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 23 March 2018.

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.

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 15-17. 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 political challenges. The continuing lack of resolution of the political 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).

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 highly liquid nature of the majority of the Bank's assets 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, future credit losses and the Bank's ability to raise new secured funding at a reasonable haircut. The Directors further note that the majority of the Bank's business is not Libyan based.

The Directors are of the opinion that the situation in Libya has, overall, remained broadly stable since 2016. 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 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. The Directors are pleased to note that the international money-laundering watchdog, the Financial Action Task Force (FATF), recently confirmed that Libya complies with all the requirements and obligations to combat money laundering and terrorism financing crimes, in accordance with international standards.

The Directors have received positive assurances and evidence of support from LFB, including (i) the provision of additional capital in June 2015; (ii) a formal statement from LFB which confirms their intent to provide financial

All amounts in £'000s unless otherwise stated

support, including meeting the Bank's ongoing liquidity needs for at least the next twelve months and (iii) assurances of the strategic importance of BACB to the country of Libya. However, 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.

Taking all this into account, the Directors have considered the Bank's funding risk and are confident of the Bank's continuing positive liquidity.

In addition, the Directors have considered the need for counterparty banks to continue to operate with BACB, 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, including the opening of new correspondent banking relationships.

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 2017. 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 classified as being available-for-sale 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 did not adopt any new IFRS standards during the reporting period.

d) Future developments in Accounting Standards

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. The standard has an effective date of 1 January 2018.

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 existing 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 will apply 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 deterioration 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 would be recognised. Financial assets where there has not been a significant deterioration 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 will require 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

The Bank plans to take advantage of exemptions allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes.

Based on financial assets held as at 31 December 2017 and expectations around changes to balance sheet composition, the Bank expects that:

i. Loans and receivables to banks and to customers that are classified as loans and receivables under IAS 39 will be measured at amortised cost under IFRS 9;
ii. Financial assets designated at fair value through profit and loss (FVTPL) will continue to be classified at FVTPL under IFRS 9;
iii. Debt securities classified as available for sale under IAS 39 will be measured at fair value through OCI (FVOCI) under IFRS 9;
iv. Equity investments classified as available for sale under IAS 39 will be 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 will avail of the option within IFRS 9 to make an irrevocable election to classify as FVOCI.

The systems and the associated controls that are in place to comply with the new requirements have not been operational for a full reporting period and therefore estimates and judgments may be subject to refinement. However, preliminary estimates are that opening shareholders' equity is expected to decrease by approximately £3m on transition to the new Standard as a result of an increase in impairment allowance. This is the net impact after collective provisions are reversed.

All amounts in £'000s unless otherwise stated

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 has an effective date of 1 January 2018, and must be applied retrospectively. A restatement is not expected on initial application of this standard.

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 Bank is assessing the potential impact on its financial statements resulting from the application of IFRS 16. The Standard is expected to be effective for periods beginning on or after 1 January 2019, subject to EU endorsement.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to both years presented in these financial statements.

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. if the income is earned on the execution of a significant act, it is recognised as revenue when the significant act has been completed (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. if the income is earned as services are provided, it is recognised as revenue as the services are provided (for example, documentary credit confirmation fees, custody and banking service fees); and
iii. if the income is an integral part of the effective interest rate of a financial instrument, it 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. In each case, the guarantees given by the Bank are covered by matching counter-indemities 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.

All amounts in £'000s unless otherwise stated

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 available for sale assets, in other comprehensive income. Non-monetary assets and liabilities 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 trading assets and liabilities, 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%.

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 Banks'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; 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

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.

All amounts in £'000s unless otherwise stated

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:

i. substantially all the risks and rewards of ownership have been transferred;
ii. substantially all the risks and rewards have neither been retained nor transferred but control is not retained; or
iii. 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 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.

All amounts in £'000s unless otherwise stated

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 3 or 5 years, 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. The main lease agreement 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 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 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.

All amounts in £'000s unless otherwise stated

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.

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 strong 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 effective 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.

The Chief Executive submits to each meeting of the Audit & Risk Committee an 'Enterprise Risk Assessment' that identifies those risks which may present a franchise risk to the Bank. This assessment includes details of:

▪ The scope of the risk	▪ Risk appetite and tolerance
▪ The nature of the risk	▪ Risk response and controls
▪ Stakeholders	▪ Direction of risk tendency
▪ Risk evaluation	▪ Strategy and policy developments
▪ Loss experience / potential	

c) Principal Risks

The Bank's principal risks and uncertainties as at the reporting date are referenced in the Strategic Report on pages 15-17 and these risks are each subject to ongoing active review by management and the Board.

The Bank has identified eight 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.

All amounts in £'000s unless otherwise stated

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

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

During 2018, Financial Crime risk will be separated out from Compliance Risk and will become a ninth Principal Risk Type.

A brief description of each of the (current eight) 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, indeed, 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 rigorous adherence to its compliance objectives of operating at all times in strict conformity with all applicable laws and regulations including sanctions and anti-money laundering requirements. Robust 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 strong Board oversight, integration of risk management into strategy setting and effective communications and brand building;
- cultural alignment built on strong 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;

All amounts in £'000s unless otherwise stated

- focusing on mainly non-complex products and a wholesale customer base, supported by a robust 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.

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 Money-Laundering, Financial Crime, Conduct Risk 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 and / or complaints handling, as well as managing client money and assets;
- Financial Crime matters which could include the Bank being used as a vehicle to facilitate financial crime, breaches of sanctions applicable to the Bank and market abuse.

Risk Management:
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 which recognises the higher level of risk attaching to many of the countries with which the Bank transacts.

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;
- monitoring trades, transactions and business processes in order to identify any potential compliance risks;
- implementing any measures arising from the anti-money laundering program;
- ensuring that any occurrences which give reason to suspect money laundering or the financing of terrorism are identified and reported to the relevant authorities;
- 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 and Risk Committee, to whom the Head of Compliance provides a quarterly report. 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 financial crime matters;
- in respect of regulatory requirements relating to sanctions, anti-money laundering and terrorist financing in particular, 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; and
- undertaking a risk-based monitoring programme aimed at detecting shortcomings in, or failures of, compliance controls or processes.

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 Banks 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 recently updated 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 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.

All amounts in £'000s unless otherwise stated

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 including the management of the Bank's liquidity portfolios;
- 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 will be 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 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;

All amounts in £'000s unless otherwise stated

- 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; 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:

	2017	***2016***
Cash, notes and coins	143	*87*
Financial investments: debt securities (note 15)	780,528	*1,279,652*
Loans and advances to banks	1,017,510	*759,716*
Loans and advances to customers (note 17)	1,068,589	*864,311*
Derivatives	547	*769*
Total on balance sheet	**2,867,317**	***2,904,535***
Contingent liabilities (note 29)	54,051	*57,123*
Other commitments (note 30)	532,921	*308,915*
Less: off balance sheet exposures impaired by provision on balance sheet	(809)	*(250)*
Total off balance sheet	**586,163**	***365,788***
Total	**3,453,480**	***3,270,323***

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

Type of credit exposure	**Percentage of exposure that is subject to collateral 2017**	*2016*	**Principal types of collateral held**
On-balance sheet:			
Loans and advances to banks			
Funds held at correspondent banks	**0.0%**	*0.1%*	Cash
Professional market placements	**2.9%**	*68.0%*	Cash
Term lending	**9.4%**	*3.1%*	Cash and guarantees
Bills discounted	**9.7%**	*5.1%*	Cash and guarantees
Overdrafts and other advances	**93.8%**	*37.4%*	Cash
Loans and advances to customers			
Professional market placements to non banks	**99.7%**	*100.0%*	Debt securities
Term and Real Estate lending	**64.3%**	*48.9%*	Cash + Residential/Commercial property
Overdrafts and other advances	**12.6%**	*5.7%*	Cash and guarantees
Off-balance sheet:			
Credit lines and other commitments	**20.2%**	*26.9%*	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

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**

31 December 2016	***Maximum exposure***	***Cash collateral***	***Property collateral***	***Debt securities***	***Guarantees***	***Net exposure to credit risk***
On-balance sheet:						
Cash, notes and coins	*87*	-	-	-	-	*87*
Financial investments: debt securities (note 15)	*1,279,652*	-	-	-	-	*1,279,652*
Loans and advances to banks						
Funds held at correspondent banks	*31,080*	*(40)*	-	-	-	*31,040*
Professional market placements	*322,254*	*(4,301)*	-	*(214,970)*	-	*102,983*
Term lending	*228,421*	*(7,138)*	-	-	-	*221,283*
Bills discounted	*168,639*	*(8,660)*	-	-	-	*159,979*
Overdrafts and other advances	*10,461*	*(3,914)*	-	-	-	*6,547*
Less: Provisions for impairments (note 13)	*(1,139)*	-	-	-	-	*(1,139)*
		-	-	-	-	
Loans and advances to customers		-	-	-	-	
Professional market placements to non banks	*78,394*	-	-	*(78,394)*	-	-
Term and Real Estate lending	*651,679*	*(9,056)*	*(309,399)*	-	-	*333,224*
Overdrafts and other advances	*173,818*	*(943)*	-	-	*(8,953)*	*163,922*
Less: Provisions for impairments (note 13)	*(39,580)*	-	-	-	-	*(39,580)*
Derivatives	*769*	-	-	-	-	*769*
Total on balance sheet	***2,904,535***	***(34,052)***	***(309,399)***	***(293,364)***	***(8,953)***	***2,258,767***
Off-balance sheet:						
Credit lines and other commitments	*365,788*	*(95,147)*	-	-	*(3,077)*	*267,564*
Total off balance sheet	***365,788***	***(95,147)***	-	-	***(3,077)***	***267,564***
Total	***3,270,323***	***(129,199)***	***(309,399)***	***(293,364)***	***(12,030)***	***2,526,331***

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. These valuations may not be from the current year.

All amounts in £'000s unless otherwise stated

In certain cases cash collateral is held against other forms of lending and off-balance sheet exposures. At 31 December 2017 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 £146,003,000 (*2016: £129,199,000*). This includes the utilised portion of a US$250,000,000 deposit placed by Libyan Foreign Bank as collateral for the obligations of itself and affiliated entities. 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.

	2017	*2016*
LTV ratio		
Less than 55%	73,480	48,945
55 - 65%	259,859	220,784
66 - 75%	93,462	39,670
76 - 80%	10,610	-
Total	**437,411**	**309,399**

By industry, concentrations of credit risk were as follows:

	2017	*2016*
Financial institutions (including central banks)		
Banks	1,166,036	*1,157,077*
Multilateral development banks	490,416	*721,590*
Other financial intermediaries	478,469	*132,024*
	2,134,921	***2,010,691***
Corporates		
Commodities	315,743	*266,002*
Construction and engineering	11,302	*12,652*
Energy	185,494	*194,690*
Transport and storage	7,151	*2,482*
Real estate	414,103	*236,436*
Other	97,157	*129,195*
	1,030,950	***841,457***
Public administration	**246,452**	***366,889***
Other Entities	**89,960**	***92,255***
Impairments (note 13)	(48,803)	*(40,969)*
Maximum exposure to credit risk	**3,453,480**	***3,270,323***

The Bank uses a credit grading system, to facilitate the monitoring of the portfolio and individual exposures. Credit risks assessed in accordance with that methodology are shown below.

All amounts in £'000s unless otherwise stated

31 December 2017 Grade	Contingent liabilities and other commitments	Cash, loans and advances, debt securities and derivatives	Maximum exposure to credit risk	Cash collateral	Net credit exposure
Grade 1 (Investment Grade)	-	847,007	847,007	-	847,007
Grade 2 (Investment Grade)	-	247,730	247,730	-	247,730
Grade 3 (Investment Grade)	-	2,615	2,615	-	2,615
Grade 4 (Investment Grade)	11,108	54,422	65,530	(137)	65,393
Grade 5 (Investment Grade)	760	11,552	12,312	-	12,312
Grade 6 (Investment Grade)	5,476	70,293	75,769	-	75,769
Grade 7 (Investment Grade)	-	3,398	3,398	-	3,398
Grade 8 (Investment Grade)	2,890	62,757	65,647	-	65,647
Grade 9 (Investment Grade)	27,949	45,216	73,165	-	73,165
Grade 10 (Investment Grade)	32,303	263,977	296,280	(271)	296,009
Grade 11 (Non-Investment Grade)	39,580	355,636	395,216	(201)	395,015
Grade 12 (Non-Investment Grade)	91,695	290,269	381,964	-	381,964
Grade 13 (Non-Investment Grade)	6,951	27,331	34,282	-	34,282
Grade 14 (Non-Investment Grade)	13,149	69,733	82,882	-	82,882
Grade 15 (Non-Investment Grade)	63,723	88,645	152,368	(8,698)	143,670
Grade 16 (Non-Investment Grade)	72,102	298,559	370,661	(16,606)	354,055
Grade 17 (Non-Investment Grade)	35,922	48,477	84,399	(3,732)	80,667
Grade 18 (Watchlist)	183,244	44,099	227,343	(112,952)	114,391
Grade 19 (Sub-Standard)	-	-	-	-	-
Grade 20 (Default)	120	83,595	83,715	(3,405)	80,310
Less: impairments	(809)	(47,994)	(48,803)	-	(48,803)
Total credit exposures	**586,163**	**2,867,317**	**3,453,480**	**(146,002)**	**3,307,478**

31 December 2016 Grade	Contingent liabilities and other commitments	Cash, loans and advances, debt securities and derivatives	Maximum exposure to credit risk	Cash collateral	Net credit exposure
Grade 1 (Investment Grade)	11	793,053	793,064	-	793,064
Grade 2 (Investment Grade)	-	320,078	320,078	-	320,078
Grade 3 (Investment Grade)	-	242,314	242,314	-	242,314
Grade 4 (Investment Grade)	6,423	75,171	81,594	(140)	81,454
Grade 5 (Investment Grade)	252	48,844	49,096	-	49,096
Grade 6 (Investment Grade)	5,569	85,133	90,702	-	90,702
Grade 7 (Investment Grade)	-	16,797	16,797	-	16,797
Grade 8 (Investment Grade)	3,592	84,910	88,502	-	88,502
Grade 9 (Investment Grade)	176	10,312	10,488	-	10,488
Grade 10 (Investment Grade)	32,673	326,345	359,018	(294)	358,724
Grade 11 (Non-Investment Grade)	14,110	103,083	117,193	(943)	116,250
Grade 12 (Non-Investment Grade)	36,198	228,421	264,619	-	264,619
Grade 13 (Non-Investment Grade)	18,236	37,321	55,557	-	55,557
Grade 14 (Non-Investment Grade)	37,543	65,830	103,373	(14)	103,359
Grade 15 (Non-Investment Grade)	17,213	161,874	179,087	-	179,087
Grade 16 (Non-Investment Grade)	39,221	181,039	220,260	(10,277)	209,983
Grade 17 (Non-Investment Grade)	57,602	59,545	117,147	(7,044)	110,103
Grade 18 (Watchlist)	94,597	49,229	143,826	(110,487)	33,339
Grade 19 (Sub-Standard)	-	4,055	4,055	-	4,055
Grade 20 (Default)	2,622	51,899	54,521	-	54,521
Less: impairments	(250)	(40,718)	(40,968)	-	(40,968)
Total credit exposures	**365,788**	**2,904,535**	**3,270,323**	**(129,199)**	**3,141,124**

All amounts in £'000s unless otherwise stated

The Bank provides facilities to in excess of 400 counterparties encompassing exposures in over 65 countries and territories (*2016: in excess of 370 counterparties encompassing exposures in over 60 countries and territories*).

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

31 December 2017	Contingent liabilities 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
Other Countries	27,305	897,355	924,660
Impairments	(809)	(47,994)	(48,803)
Maximum exposure to credit risk	**586,163**	**2,867,317**	**3,453,480**

31 December 2016	*Contingent liabilities and other commitments*	*Cash, loans and advances, debt securities and derivatives*	*Total*
United Kingdom	*51,896*	*606,449*	*658,345*
Europe excluding UK	*72,649*	*532,564*	*605,213*
Libya	*66,319*	*9,439*	*75,758*
Other Middle East and Africa	*144,653*	*756,686*	*901,339*
Other Countries	*30,521*	*1,040,116*	*1,070,637*
Impairments	*(250)*	*(40,719)*	*(40,969)*
Maximum exposure to credit risk	***365,788***	***2,904,535***	***3,270,323***

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.

All amounts in £'000s unless otherwise stated

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 look to profit other than to a small extent from principal position trading exposures to bonds, interest rates or foreign exchange. 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. 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 2017 (being the sterling equivalent value of all the currencies where the currency obligations were higher than currency receivables) was £663,000 (*2016: £504,000*). Were these currencies to strengthen by 5% against the remaining currencies, then the Bank would lose £33,000 (*2016: £25,000*).

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

	2017	*2016*
Maximum	2,726	*5,546*
Minimum	380	*3*
Average	1,016	*1,108*

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

All amounts in £'000s unless otherwise stated

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 2017, PVBP amounted to £32,056 (*2016: £32,074*). PVBP (calculated on a daily basis) was as follows:

	2017	*2016*
Maximum	39	*37*
Minimum	13	*3*
Average	24	*18*

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.

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

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)**	

All amounts in £'000s unless otherwise stated

31 December 2016	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing	Total
Financial investments	438,650	611,917	136,427	92,658	-	8,790	1,288,442
Loans and advances to banks	449,585	138,509	171,510	112	-	-	759,716
Loans and advances to customers	441,974	334,713	81,508	143	5,380	593	864,311
Other assets	848	434	22	17	-	25,474	26,795
Total assets	**1,331,057**	**1,085,573**	**389,467**	**92,930**	**5,380**	**34,857**	**2,939,264**
Deposits from banks	898,550	485,647	598,463	36,376	-	-	2,019,036
Other deposits	340,180	79,605	11,385	191,726	-	-	622,896
Subordinated liabilities	45,970	29,443	-	-	-	-	75,413
Other liabilities and shareholders' funds	9,410	-	-	-	-	212,509	221,919
Total equity and liabilities	**1,294,110**	**594,695**	**609,848**	**228,102**	**-**	**212,509**	**2,939,264**
Derivatives (at contract value)	-	-	-	-	-	-	
Receivable	14,215	4,061	5,361	-	-	-	
Payable	-	-	-	(23,637)	-	-	
Overall gap	51,162	494,939	(215,020)	(111,535)	5,380	(177,652)	
Reverse Cumulative gap	**224,926**	**173,764**	**(321,175)**	**(106,155)**	**5,380**	**(177,652)**	

Non-interest bearing items comprise share capital, accumulated impairments, tangible and intangible assets and other sundry debtors and creditors not subject to interest. Such net non-interest bearing liabilities are used to fund the Bank's assets by way of internal placements, and give rise to a structural interest rate position. Gap limits available to the Bank's dealers for the management of interest rate risk in the banking book are stated net of these placements.

A simultaneous increase in interest rates of 0.5% in all currencies, and in all maturities on 1 January 2018 would increase earnings from the financial assets associated with the non-interest bearing liabilities during 2018 by £693,000 (*2016: a 0.5% increase in interest rates in all currencies would increase earnings in 2017 by £589,000*).

Derivatives include interest rate and currency swap transactions, the purpose of which are to reduce economic exposure to interest rate risk, whether formally qualifying as hedges or otherwise. The purpose of such hedges is 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.

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.

All amounts in £'000s unless otherwise stated

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)**	

At 31 December 2016	*Up to 1 month*	*1-3 months*	*3-12 months*	*1-5 years*	*Over 5 years*	*Undated*	*Total*
Financial investments	*165,724*	*114,230*	*169,911*	*836,671*	*1,807*	*99*	*1,288,442*
Loans and advances to banks	*439,861*	*91,017*	*228,726*	*112*	*-*	*-*	*759,716*
Loans and advances to customers	*287,537*	*40,489*	*87,461*	*411,125*	*37,198*	*501*	*864,311*
Other assets	*848*	*434*	*22*	*17*	*-*	*25,474*	*26,795*
Total assets	***893,970***	***246,170***	***486,120***	***1,247,925***	***39,005***	***26,074***	***2,939,264***
Deposits from banks	*643,452*	*382,917*	*793,834*	*198,833*	*-*	*-*	*2,019,036*
Other deposits	*340,180*	*79,605*	*11,385*	*191,726*	*-*	*-*	*622,896*
Subordinated liabilities	*-*	*-*	*-*	*-*	*75,413*	*-*	*75,413*
Other liabilities and shareholders' funds	*9,410*	*-*	*-*	*-*	*-*	*212,509*	*221,919*
Total equity and liabilities	***993,042***	***462,522***	***805,219***	***390,559***	***75,413***	***212,509***	***2,939,264***
Net liquidity gap	***(99,072)***	***(216,352)***	***(319,099)***	***857,366***	***(36,408)***	***(186,435)***	

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 Management, 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;
- 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.

All amounts in £'000s unless otherwise stated

Operational risk losses in the year to 31 December 2017 amounted to £109,000 (*2016: £60,000*).

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.

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.

In assessing collective impairment, the Bank uses default rates and loss rates based on historical trends for assets with credit risk characteristics similar to those in the portfolio. Management makes an adjustment if current economic and credit conditions are such that the actual loses are likely to be greater or lesser than is suggested by historical trends.

At 31 December 2017 seven loans to customers were impaired (*2016: loans to five 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 2017. 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.

All amounts in £'000s unless otherwise stated

If recoveries on the seven impaired loans are 10% lower than has been estimated, then the amount of the impairment which would have been charged in 2017 in respect of those loans would have been increased by £4,024,000 *(2016: £1,231,000 in respect of five 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 analyses the financial assets and liabilities in the statements of financial position by the class of financial instrument to which they are assigned and therefore by the measurement basis.

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								**2,952,856**
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								**2,952,856**

All amounts in £'000s unless otherwise stated

31 December 2016	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	-	87	**87**	-	-	-	**-**	**87**
Financial investments	-	-	**-**	1,288,442	-	-	**1,288,442**	**1,288,442**
Loans and advances to banks	759,716	-	**759,716**	-	-	-	**-**	**759,716**
Loans and advances to customers	864,311	-	**864,311**	-	-	-	**-**	**864,311**
Derivatives	-	-	**-**	-	752	17	**769**	**769**
Total financial assets	1,624,027	87	**1,624,114**	1,288,442	752	17	**1,289,211**	**2,913,325**
Total non-financial assets								**25,939**
Total assets								**2,939,264**
Liabilities								
Deposits from banks	-	2,019,036	**2,019,036**	-	-	-	**-**	**2,019,036**
Other deposits	-	622,896	**622,896**	-	-	-	**-**	**622,896**
Derivatives	-	-	**-**	-	1,834	126	**1,960**	**1,960**
Subordinated liabilities	-	75,413	**75,413**	-	-	-	**-**	**75,413**
Total financial liabilities	-	2,717,345	**2,717,345**	-	1,834	126	**1,960**	**2,719,305**
Total equity and non-financial liabilities								**219,959**
Total equity and liabilities								**2,939,264**

Of the total £4,190,000 (*2016: £752,000*) assets at fair value through the profit and loss account, £4,190,000 (*2016: £752,000*) represents financial assets and derivatives held for trading purposes.

Of the total £1,271,000 *(2016: £1,834,000)* liabilities at fair value through the profit and loss account, £1,271,000 (*2016: £1,834,000)* represents derivatives held for trading purposes. As at 31 December 2017, there were no financial liabilities designated at fair value through the profit and loss account at inception *(2016: nil)*.

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.

All amounts in £'000s unless otherwise stated

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**

31 December 2016	*Level 1*	*Level 2*	*Level 3*	*Total*	*Carrying value (note 6)*
Cash, notes and coins	-	*87*	-	*87*	*87*
Loans and advances to banks	-	-	*760,160*	*760,160*	*759,716*
Loans and advances to customers	-	-	*858,214*	*858,214*	*864,311*
Financial assets held at amortised cost	**-**	***87***	***1,618,374***	***1,618,461***	***1,624,114***
Deposits from banks	-	-	*2,019,906*	*2,019,906*	*2,019,036*
Other deposits	-	-	*622,931*	*622,931*	*622,896*
Subordinated liabilities	-	-	*59,059*	*59,059*	*75,413*
Financial liabilities held at amortised cost	**-**	**-**	***2,701,896***	***2,701,896***	***2,717,345***

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.

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 2017 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:

All amounts in £'000s unless otherwise stated

	31 December 2017			*31 December 2016*		
	Sterling	US Dollars	Euro	*Sterling*	*US Dollars*	*Euro*
Interest rates						
3 month	0.51%	1.68%	-0.39%	*0.55%*	*1.52%*	*-0.32%*
6 month	0.57%	1.85%	-0.32%	*0.68%*	*1.26%*	*-0.26%*
1 year	0.87%	2.20%	-0.23%	*0.83%*	*1.80%*	*-0.12%*
5 year	1.04%	2.27%	0.32%	*0.86%*	*2.01%*	*0.07%*
Exchange rates	1.0000	1.3511	1.1270	*1.0000*	*1.2311*	*1.1627*

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.

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.

All amounts in £'000s unless otherwise stated

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**

31 December 2016	***Level 1***	***Level 2***	***Level 3***	***Total fair value (Note 6)***
Financial investments	*1,279,652*	*-*	*8,790*	*1,288,442*
Derivative assets	*675*	*94*	*-*	*769*
Total assets held at fair value	***1,280,327***	***94***	***8,790***	***1,289,211***
Derivative liabilities	*1,646*	*314*	*-*	*1,960*
Total liabilities held at fair value	***1,646***	***314***	***-***	***1,960***

There were no significant transfers of assets between levels during 2017, 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
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.

All amounts in £'000s unless otherwise stated

8. Net interest income

Interest income is made up as follows:

	2017	*2016*
Interest income		
Professional market placements and debt securities	20,143	*17,952*
Loans, advances and overdrafts	41,450	*29,910*
Other	21	*10*
	61,614	***47,872***
Interest income comprises		
Interest arising on financial assets at fair value through the income statement	682	*588*
Gains / (losses) arising from the change in fair value of fair value hedges		
- on hedging instruments	87	*73*
- on hedged items attributable to the hedged risk	(81)	*(63)*
Other interest	60,926	*47,274*
	61,614	***47,872***

The amount recorded in the income statement in respect of the ineffectiveness of fair value hedges was £nil in the year ended 31 December 2017 *(2016:£nil)*

Interest expense is made up as follows:

	2017	*2016*
Interest expense		
Deposits from banks and other deposits	(30,616)	*(23,109)*
Subordinated loans	(2,568)	*(2,288)*
Other	(12)	*-*
	(33,196)	***(25,397)***

9. Net fee and commission income

Fee and commission income less fee and commission expense is made up as follows:

	2017	*2016*
Fee and commission income		
Safe custody	147	*153*
Trade services:		
Guarantees	647	*821*
Documentary credit and trade finance fees	11,284	*7,776*
Other trade services income	257	*490*
Term lending (other than amounts which form part of the effective interest rate)	212	*664*
Banking payments and services	3,062	*2,431*
	15,609	**12,335**
Fee and commission expense		
Brokerage and other fees	**(325)**	***(357)***

All amounts in £'000s unless otherwise stated

10. Net trading income

Net trading income is made up as follows:

	2017	*2016*
Foreign exchange dealing	4,180	*4,090*
Debt securities	327	*35*
Other	223	*2,032*
	4,730	***6,157***

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:

	2017	*2016*
Rent recovery	185	*186*
Gains on equity shares and investment funds	401	*1,943*
Gains on available for sale financial assets	4,378	-
	4,964	***2,129***

Gains on available for sale financial assets has been classified to other operating income for 2017, having been classified to Interest and similar income in 2016. The comparative balance for 2016 was £1,167,000

All amounts in £'000s unless otherwise stated

12. Administrative expenses

	2017	2016
Staff costs:		
Salaries and other emoluments	14,711	*12,190*
Social security costs	2,039	*1,801*
Other pension costs:		
- Defined benefit scheme (note 25)	280	*240*
- Defined contribution scheme (note 25)	1,532	*1,354*
Total fixed employment costs (Permanent Staff)	**18,562**	***15,585***
Variable staff costs: performance awards	2,432	*1,946*
Total staff employment costs	**20,994**	***17,531***
Reorganisation costs	405	*432*
Other employment related costs (see below)	3,276	*3,073*
Total staff costs	**24,675**	***21,036***
Fees payable to the Bank's auditors for the audit of the Bank's annual financial statements	292	*200*
Fees payable to the Bank's auditors for other services :		
- Other services pursuant to legislation	15	*20*
- All other services	-	*16*
Depreciation (including amortisation of intangibles)	1,338	*1,631*
Amounts payable in respect of operating leases:		
- Amortisation of prepaid rental on land	63	*63*
- Ground rental	143	*131*
Loss/(gain) on sale or impairment of tangible and intangible assets	665	*(50)*
Regulatory supervision fees	83	*94*
Other administrative expenses		
- Premises & Technology	4,973	*4,028*
- Legal & Professional	1,151	*1,217*
- Other	2,227	*2,916*
General administrative expenses	**35,625**	***31,302***
Review of historic activities	**375**	***1,736***
Administrative expenses	**36,000**	***33,038***

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

The average number of employees in place during the year was 211 (*2016: 181*).

Other employment related costs include contractors.

Charges for the review of historic activities (also refer Note 33) comprises legal costs incurred and includes a provision for additional costs committed as at 31 December 2017.

Directors' remuneration included above totalled £1,516,000 *(2016:* £1,646,000*)*. The emoluments of the highest paid director were £685,000 *(2016:* £584,000*)* and the amount of their accrued pension as at balance sheet date

All amounts in £'000s unless otherwise stated

was £nil *(2016: £nil)*. There were no pension contributions for any directors during the year *(2016: £nil)*.The aggregate amount of compensation to directors in respect of loss of office was £300,000.

13. Allowance for credit losses

The allowance for credit losses consists of an allowance for loan losses and an allowance for off-balance sheet positions.

The movements in the allowance for credit losses were as follows:

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**

31 December 2016	***Loans***	***Off-balance sheet positions***	***Total***
Balance at 1 January	***26,360***	***1,431***	***27,791***
Exchange translation and other movements	*4,472*	*106*	*4,578*
Allowances recovered/(written off)	*2,498*	*(1,020)*	*1,478*
New allowances	*13,909*	*(80)*	*13,829*
Reversal of allowances no longer required	*(4,022)*	*(187)*	*(4,209)*
Recoveries of amounts written off in previous periods	*(2,498)*	*-*	*(2,498)*
Allowance for credit losses	***7,389***	***(267)***	***7,122***
Balance at 31 December	***40,719***	***250***	***40,969***
Individually assessed	*35,169*	*-*	*35,169*
Collectively assessed	*5,550*	*250*	*5,800*
Total credit losses allowance against loans and off balance positions	***40,719***	***250***	***40,969***

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.

All amounts in £'000s unless otherwise stated

Collective impairments arise in respect of the Bank's exposures with similar risk characteristics for which previous experience indicates that impairment has taken place at the balance sheet date, but whose existence has yet to emerge. Recognising the challenging market conditions, the Bank has assessed its collective impairment at £5,304,000 in 2017 (*2016: £5,800,000*). This covers all of the Bank's exposures (excluding those that are individually provided for, and net of eligible credit mitigation) with an increased emphasis on sectors which are currently 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 7 impaired facilities at 31 December 2017 (*2016: 5 facilities*), with new impairment allowances recognised for 5 of those facilities during the year (*2016: 4 facilities*). Of the 7 facilities impaired as at 31 December 2017, 4 facilities had no collateral in place (*2016: 3 facilities*).

	2017		*2016*	
	Number of Facilities	Gross Exposure	*Number of Facilities*	*Gross Exposure*
Impaired facilities				
Total impaired facilities	7	83,715	*5*	*51,899*
Impaired facilities against which there was no collateral	4	51,500	*3*	*37,457*
Of the above:				
Facilities formally restructured on terms which may be less favourable to the Bank	-	-	*1*	*7,333*
Facilities in the process of being restructured as at the reporting date (impairment in respect of these facilities £2,715,011)	2	20,221	*1*	*27,008*
Companies in liquidation (impairment in respect of these facilities £24,609,771)	1	24,610	-	-
Waiver on repayments, shareholders covering interest and start up costs (impairment in respect of these facilities £2,000,834)	1	6,669	-	-
Unimpaired facilities subject to forbearance, restructuring or close monitoring				
Facilities formally restructured on terms which may be less favourable to the Bank but which do not give rise to an impairment	-	-	*1*	*4,055*
Watchlist or substandard facilities subject to closer monitoring than normal (which may include some of the unimpaired balances above) at reporting date	8	38,018	*4*	*44,793*
Relaxations of material covenants or temporary relaxations of repayment terms at reporting date	1	458	*2*	*8,990*
Breach of covenant, which is being addressed	2	10,913	-	-

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

All amounts in £'000s unless otherwise stated

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.

14. Income tax

	2017	*2016*
Current tax		
Total UK corporation tax (credit)/charge	122	*418*
Of which: amount recognised in other comprehensive income	-	-
Current tax on items taken through the income statement	122	*418*
Current tax adjustment in respect of previous periods	(198)	-
Deferred tax (note 24)		
Origination and reversal of timing differences	214	*129*
Effect of tax rate change	4	*79*
Deferred tax adjustment in respect of previous periods	25	-
Deferred tax adjustment in respect of unused losses	273	*(766)*
	516	*(558)*
Total income tax charge / (credit)	**440**	*(140)*

The tax charge on the profit for the year is based on the average UK corporation tax rate of 19.25% *(2016: 20%)*. 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 2017 has been calculated taking into account the impact of these rates.

The tax charge for the year is lower *(2016: lower)* than the charge resulting from applying the standard rate of UK corporation tax. The differences are explained below:

	2017	*2016*
Profit/(Loss) on ordinary activities before tax	**7,265**	*2,579*
Profit on ordinary activities multiplied by standard rate of corporation tax in the UK	1,398	*516*
Effects of:		
Chargeable gains	-	*763*
Adjustment in respect of previous periods	(198)	-
Effect of change in tax rate	4	*79*
Non taxable income	(32)	*(820)*
Non deductible items	160	*88*
Prior period losses recognised as a deferred tax asset	273	*(766)*
Losses on which prior period losses have been utilised	(1,165)	-
Total income tax charge / (credit)	**440**	*(140)*

All amounts in £'000s unless otherwise stated

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

	2017			*2016*		
	Before tax	**Tax**	**Net of tax**	***Before tax***	***Tax***	***Net of tax***
Actuarial gain/(loss) on pension fund	1,277	(217)	1,060	*(3,250)*	*494*	*(2,756)*
Change in fair value of available for sale financial assets	5,137	(866)	4,271	*3,522*	*(1,120)*	*2,402*
Fair value losses/(gains) attributable to available for sale financial assets transferred to income	(4,587)	871	(3,716)	*(5,279)*	*1,087*	*(4,192)*
Effect of change in tax rates	-	-	-	*-*	*50*	*50*
	1,827	**(212)**	**1,615**	***(5,007)***	***511***	***(4,496)***

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

		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

		2016			
Nature of activities	*Geographical location*	*Turnover*	*Loss before tax*	*Corporation tax refund*	*Average number of employees*
Banking	*United Kingdom*	*35,617*	*2,579*	*(2,256)*	*181*

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

	2017	*2016*
Debt issued by governments and multilateral development banks	652,731	*1,081,179*
Other listed debt securities issued by banks	112,681	*178,667*
Other listed debt securities issued by non-banks	11,426	*19,806*
Debt securities held for trading	3,690	-
Total debt securities	**780,528**	***1,279,652***
Equity shares and investment funds	**7,538**	***8,790***
	788,066	***1,288,442***

Debt securities with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £94,537,000 *(2016: £130,688,000).*

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.

All amounts in £'000s unless otherwise stated

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:

	2017	***2016***
Balance at 1 January	8,790	*15,530*
Changes in fair value during the year	(1,046)	*1,140*
Realised (gain)/loss	-	*(3,822)*
Disposals	(206)	*(4,058)*
Balance at 31 December	**7,538**	***8,790***
Comprising:		
Equity shares	1,868	*1,807*
Investment funds	5,670	*6,983*
	7,538	***8,790***

16. Loans and advances to banks

	2017	***2016***
Funds held at correspondent banks	274,942	*31,080*
Professional market placements	153,580	*322,254*
Term lending	221,558	*228,421*
Bills discounted	364,885	*168,639*
Overdrafts and other advances	3,634	*10,461*
Less: Provisions for impairments (note 13)	(1,089)	*(1,139)*
	1,017,510	***759,716***

Loans and advances to banks with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £531,000 (*2016: £nil).*

Professional market placements includes £nil *(2016: £214,972,000)* 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).

17. Loans and advances to customers

	2017	***2016***
Professional market placements to non banks	190,047	*78,394*
Term and Real Estate lending	688,562	*651,679*
Overdrafts and other advances	236,885	*173,818*
Less: Provisions for impairments (note 13)	(46,905)	*(39,580)*
	1,068,589	***864,311***

Loans and advances to customers with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £4,701,000 (*2016: £5,503,000).*

All amounts in £'000s unless otherwise stated

Professional market placements comprises £190,047,000 *(2016: £78,394,000)* 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

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 amounts shown below are the minimum non-cancellable amounts payable and receivable. They take account of a long-term basic rent obligation up to August 2147, 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 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**

31 December 2016	*Less than one year*	*Between one and five years*	*More than five years*	*Total*
Operating lease payments due	*148*	*541*	*9,973*	*10,662*
Operating lease receipts due	*(173)*	*(271)*	*-*	*(444)*
Net payment / (receipt) commitment	***(25)***	***270***	***9,973***	***10,218***

All amounts in £'000s unless otherwise stated

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 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)
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**
Cost					
Balance at 1 January 2016	*15,351*	*2,376*	*17,727*	*7,022*	*24,749*
Additions during the year	*82*	*411*	*493*	*3,014*	*3,507*
Disposals during the year	-	*(105)*	*(105)*	*(1,643)*	*(1,748)*
At 31 December 2016	*15,433*	*2,682*	*18,115*	*8,393*	*26,508*
Less: accumulated depreciation					
Balance at 1 January 2016	*7,334*	*1,715*	*9,049*	*5,125*	*14,174*
Charge for the year	*346*	*329*	*675*	*956*	*1,631*
Disposals during the year	-	*(97)*	*(97)*	*(1,593)*	*(1,690)*
Impairment loss	-	-	-	*(103)*	*(103)*
At 31 December 2016	*7,680*	*1,947*	*9,627*	*4,385*	*14,012*
	-	-	-	-	-
Net book value at 31 December 2016	***7,753***	***735***	***8,488***	***4,008***	***12,496***

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 £7,595,000 *(2016: £7,753,000)*, 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 £8,132,000 *(2016: £8,195,000)*, making a total asset value of £15,727,000 *(2016: £15,948,000)*. On 10 May 2012, 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 £17,850,000. This valuation will be updated in 2018.

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

Additions during the year of £3,949,000 *(2016: £3,507,000)* include costs related to the ongoing Enterprise Architect project to upgrade the core banking system. Of these costs £3,342,000 *(2016: £2,976,000)* relates to intangible assets and £92,000 *(2016: £209,000)* relates to tangible assets which are not yet in use, and therefore have not been depreciated.

The original cost of fully depreciated tangible and intangible assets still in use by the Bank at year-end was £9,213,000 (*2016: £6,722,000*).

There were commitments for capital expenditure on 31 December 2017 of £119,000 (*2016: £762,000*), of which £101,000 *(2016: £735,000)* related to the Enterprise Architect project.

All amounts in £'000s unless otherwise stated

20. Derivatives

Derivative positions at 31 December were as follows:

	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**

	31 December 2016		
	Contract amount	*Positive fair values (Assets)*	*Negative fair values (Liabilities)*
Spot and forward foreign exchange contracts held for trading purposes	*216,861*	*672*	*1,646*
Interest rate swaps held for trading	*5,361*	*-*	*111*
Interest rate swaps qualifying as fair value hedges	*18,276*	*17*	*126*
Interest futures held for trading purposes	*50,000*	*3*	*-*
Foreign exchange options			
Purchased	*43,944*	*77*	*-*
Sold	*43,944*	*-*	*77*
		769	***1,960***

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.

All amounts in £'000s unless otherwise stated

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.

21. Prepayments, accrued income and other debtors

	2017	***2016***
Prepaid rental for land	8,132	*8,195*
Prepayments and accrued income	74	*118*
Unsettled trade receivables	48,386	-
Other debtors	5,981	*2,703*
	62,573	***11,016***

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 are amounts due from forward foreign exchange swaps.

22. Deposits

Deposits from banks totalled £2,095,638,000 (*2015 £2,019,036,000*) of which deposits with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £47,164,000 *(2016: £nil).*

Other deposits totalled £555,556,000 (*2016: £622,896,000*) of which deposits with fixed interest rates (other than those with a single interest period less than 1 year) amounted to £27,427,000 *(2016: £5,159,000).*

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

	2017	***2016***
Other liabilities	8,550	*6,420*
Accruals and deferred income	1,469	*1,539*
	10,019	***7,959***

All amounts in £'000s unless otherwise stated

24. Deferred taxation

	Balance at 1 January 2017	Recognised in Profit or Loss	Recognised in Other Comprehensive Income	Balance at 31 December 2017	Deferred tax assets	Deferred tax liabilities
Property, plant and equipment and intangible assets	(214)	15	-	(199)	-	(199)
Staff benefits	108	(15)	-	93	93	-
Unused tax losses loss carried forward	1,079	(273)	-	806	806	-
Tax assets on pension liabilities (note 25)	610	(243)	(217)	150	150	-
Available For Sale debt securities	(127)		(191)	(318)	-	(318)
Equity Investments	(387)	-	196	(191)	-	(191)
Deferred tax assets (liabilities)	**1,069**	**(516)**	**(212)**	**341**	**1,049**	**(708)**

	Balance at 1 January 2016	*Recognised in Profit or Loss*	*Recognised in Other Comprehensive Income*	*Balance at 31 December 2016*	*Deferred tax assets*	*Deferred tax liabilities*
Property, plant and equipment and intangible assets	*(331)*	*117*	*-*	*(214)*	*-*	*(214)*
Staff benefits	*165*	*(57)*	*-*	*108*	*108*	*-*
Unused tax losses loss carried forward	*907*	*748*	*-*	*1,079*	*1,079*	*-*
Tax assets on pension liabilities (note 25)	*366*	*(250)*	*494*	*610*	*610*	*-*
Available For Sale debt securities	*577*	*-*	*(703)*	*(127)*	*-*	*(127)*
Equity Investments	*(1,107)*	*-*	*720*	*(387)*	*-*	*(387)*
Deferred tax assets (liabilities)	***-***	***558***	***511***	***1,069***	***1,797***	***(728)***

Deferred tax asset and liability balances are off-settable.

The Bank has recognised a deferred tax asset of £806,000 in respect of tax losses brought forward. The Bank has unused tax losses of £5,766,000 (*2016: £10,968,000*) 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 280 deferred or pensioner members as at 31 December 2017 *(2016: 284 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.

A full actuarial valuation was carried out as at 31 December 2016 in accordance with the Scheme funding requirements of the Pensions Act 2004. The funding of the Scheme is agreed between the Bank and the

All amounts in £'000s unless otherwise stated

trustees in line with those requirements. These funding requirements in particular require the surplus or deficit to be calculated using prudent, as opposed to best estimate actuarial assumptions.

This actuarial valuation showed a deficit of £5,283,000. The Bank 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 addition and in accordance with the actuarial valuation, the Bank has agreed with the trustees that it will pay monthly contributions of £20,000 in respect of the expenses of the Scheme and will also meet the levies to the Pension Protection Fund.

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.

For the purposes of IAS19 the actuarial valuation as at 31 December 2016 has been updated on an approximate basis to 31 December 2017. 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

	2017	***2016***
Fair value of Scheme assets	80,220	*81,708*
Present value of defined benefit obligation	(81,118)	*(85,315)*
Deficit in the Scheme - net liability	**(898)**	***(3,607)***

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 £81,118,000 (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).

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

	2017	***2016***
Defined benefit obligation at start of period	85,315	*71,089*
Expenses	203	*198*
Interest expense	2,254	*2,733*
Actuarial losses due to scheme experience	(2,250)	*(1,286)*
Actuarial losses due to changes in demographic assumptions	(2,129)	*(2,697)*
Actuarial gains/(losses) due to changes in financial assumptions	1,589	*17,496*
Benefits paid and expenses	(3,864)	*(2,218)*
Defined benefit obligation at end of period	**81,118**	***85,315***

All amounts in £'000s unless otherwise stated

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.

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

	2017	*2016*
Fair value of scheme assets at start of period	81,708	*69,258*
Interest income	2,177	*2,693*
Return on scheme assets (excluding amounts included in interest income)	(1,513)	*10,263*
Contributions by the Bank	1,712	*1,712*
Contributions by scheme participants	-	-
Benefits paid and expenses	(3,864)	*(2,218)*
Fair value of scheme assets at end of period	**80,220**	***81,708***

The actual return on the Scheme's assets over the year ending 31 December 2017 was £664,000.

Defined benefit costs recognised in Profit and Loss

	2017	*2016*
Expenses	203	*198*
Net interest cost	77	*42*
Defined benefit costs recognised in profit and loss	**280**	***240***

Defined benefit costs recognised in other Comprehensive Income

	2017	*2016*
Return on scheme assets (excluding amounts included in interest income) - gain/(loss)	(1,513)	*10,263*
Experience losses arising on the defined benefit obligation	2,250	*1,286*
Effects of changes in the demographic assumptions underlying the present value of the defined benefit obligation - gains	2,129	*2,697*
Effects of changes in the financial assumptions underlying the present value of the defined benefit obligation - gains	(1,589)	*(17,496)*
Total amount recognised in other comprehensive income - gain / (loss)	**1,277**	***(3,250)***

Assets

	2017	*2016*
Liability Driven Investment (LDI)	15,194	*15,454*
Diversified Growth Funds	22,955	*22,198*
Cash	296	*386*
Purchased Annuities	41,775	*43,670*
Total assets	**80,220**	***81,708***

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.

All amounts in £'000s unless otherwise stated

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.

Significant Actuarial Assumptions

	2017 % per annum	***2016 % per annum***
Rate of discount	2.50	*2.70*
Inflation (RPI)	3.30	*3.40*
Allowance for revaluation of deferred pensions of RPI or 7.5% p.a. if less	3.30	*3.40*
Allowance for pension in payment increases of RPI or 7.5% p.a. if less	3.30	*3.40*
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 2017 are 100% of the standard tables S2PxA_L, Year of Birth, no age rating for males and females, projected using CMI_2016 (CMI Mortality Projection Model) converging to 1.00% p.a. These imply the following life expectancies:

	Life expectancy at age 60 (years)	***Life expectancy at age 60 (years)***
Male retiring in 2017	27.7	*28.2*
Female retiring in 2017	28.7	*29.3*
Male retiring in 2027	28.2	*29.0*
Female retiring in 2027	29.3	*30.3*

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 4.8%*
Rate of inflation	Increase of 0.25% p.a.	*Increase by 4.8%*
Rate of mortality	Increase in life expectancy of 1 year	*Increase by 3.4%*
Rate of mortality	Mortality improvement - long term rate 0.75%	*Decrease by 1.6%*
Cash commutation	50% of post A-day maximum using current factors	*Increase by 1.0%*

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 ending 31 December 2017 is 20 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

All amounts in £'000s unless otherwise stated

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.

The best estimate of contributions to be paid by the Bank to the scheme for the year commencing 1 January 2018 is £1,712,000.

Defined contribution scheme
At 31 December 2017, 166 employees *(2016: 150 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 2017, the Bank paid £1,393,000 *(2016: £1,233,000)* by way of contributions into that scheme. There were no outstanding or pre-paid contributions to this scheme at 31 December 2017 *(2016: £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 2017 and bear interest based on inter-bank offered rates for dollar and euro deposits. The amounts disclosed below include accrued interest.

	2017	*2016*
Due 29 April 2023	18,445	*20,223*
Due 29 October 2025	23,484	*25,748*
Due 17 June 2025	30,373	*29,442*
	72,302	***75,413***

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**	
	2017	*2016*	**2017**	*2016*
Ordinary Shares of £1 each fully paid	30,403	*30,403*	30,403	*30,403*
Ordinary Shares of US$1 each fully paid	115,224	*115,224*	73,746	*73,746*
Deferred Non-Voting Shares of £1 each nil paid	5,000	*5,000*	-	-
	150,627	***150,627***	**104,149**	***104,149***

All amounts in £'000s unless otherwise stated

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

	2017	*2016*
Called up share capital (note 27)	104,149	*104,149*
Capital redemption reserve	4,104	*4,104*
Other reserves		
Retained earnings	106,861	*98,976*
AFS Reserve	1,719	*1,164*
	108,580	100,140
	216,833	**208,393**

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

The Available-for-sale ("AFS") reserve arises in respect of changes in the market value of assets categorised as being available for sale (Note 3g).

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

The Directors have not declared a dividend in respect of the year ended 31 December 2017 *(2016: £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.

30. Contingent liabilities

The Bank extends commercial facilities to customers which provide for the issuance of performance guarantees, bid and bail bonds, and other types of guarantees. Such transactions amounted to £54,051,000 at 31 December 2017 *(2016: £57,123,000).*

The Bank's practice is to extend such facilities against a counter-indemnity. Accordingly, the Bank's risk in such transactions is a failure of both the party providing the counter-indemnity, and a failure under the underlying contract resulting in the guarantee being called. £nil arose from such contracts in the year ended 31 December 2017 *(2016: Losses totalling £1,020,000).*

All amounts in £'000s unless otherwise stated

31. Other commitments

	2017	*2016*
Other commitments comprise:		
Credit lines and other commitments to lend: original maturity		
under one year	112,045	*72,192*
over one year	13,309	*-*
Documentary credits and short-term trade-related transactions	400,924	*234,986*
Own acceptances	6,643	*1,737*
	532,921	***308,915***

32. Foreign currency assets / liabilities

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

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

31 December 2016	***Sterling***	***Dollars***	***Euro***	***Other currencies***	***Total***
Total assets	*837,914*	*1,630,433*	*468,167*	*2,750*	*2,939,264*
Total equity and liabilities	*(860,453)*	*(1,734,659)*	*(328,388)*	*(15,764)*	*(2,939,264)*
Derivatives (at contract notional value)	*22,177*	*103,972*	*(139,698)*	*13,549*	*-*
Net exposures	***(362)***	***(254)***	***81***	***535***	***-***
Contingent liabilities and other commitments	*13,049*	*308,694*	*116,588*	*16,930*	*455,261*

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

33. Legal proceedings

In late 2014, the Bank initiated a review of certain historical activities and no civil or criminal enforcement proceedings are pending or threatened.

34. 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.

All amounts in £'000s unless otherwise stated

- 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 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**

31 December 2016	***Trade Finance***	***Real Estate***	***Commodity Finance***	***Lending***	***Banking***	***Treasury***	***Other***	***Total***
Net interest income	*1,309*	*3,573*	*3,378*	*4,784*	*835*	*7,609*	*(5)*	*21,483*
Net fee and commission income	*7,687*	*320*	*2,239*	*310*	*1,577*	*(155)*	*-*	*11,978*
Net trading income	*-*	*-*	*-*	*-*	*-*	*6,157*	*-*	*6,157*
Other operating income	*-*	*-*	*-*	*-*	*-*	*1,001*	*2,120*	*3,121*
Total Operating income	***8,996***	***3,893***	***5,617***	***5,094***	***2,412***	***14,612***	***2,115***	***42,739***

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 North Africa and *comprises 13% of the total (2016: 19%).*

All amounts in £'000s unless otherwise stated

	2017	*2016*
United Kingdom	14,929	*10,331*
Europe (excluding UK)	8,388	*6,714*
North Africa	12,379	*12,528*
Subsaharan Africa	10,585	*7,402*
Middle East and Asia	4,350	*3,294*
Other	2,765	*2,470*
	53,396	***42,739***

A number of presentational changes have been made in the preceding business line review compared to the 2016 Annual Report and Financial Statements. These changes align more closely with how the business is managed and with internal Management Information. These presentation changes are summarised below:

- In 2016 BACB's geographic segments were reported as: United Kingdom, Europe (excluding UK), Libya, Other Middle East and Africa, and Other. The 'Other Middle East and Africa' segment has been sub-divided into three regions: North Africa (which includes Libya), Sub-Saharan Africa, and Middle East and Asia.
- Operating income by business segment 2016 comparatives have also been revised to reflect enhancements made to internal allocations of funding costs resulting from enhancements made to the Bank's Funds Transfer Pricing model.
- A reallocation of Operating Income between Lending and Treasury, reflecting the management control of these assets.
- A reallocation between Net interest income and Other operating income for Treasury for gains on available for sale financial assets.

35. 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

	2017	*2016*
Balances outstanding		
Loans and advances	37,984	*25,415*
Deposits	1,644,487	*1,742,532*
Subordinated liabilities	72,302	*75,413*
Derivatives (contract amount)	11	*-*
Contingent liabilities and other commitments	99,549	*88,250*
Volumes executed during the year		
Loans and advances	700,345	*143,984*
Deposits	130,244,553	*118,249,439*
Derivatives (contract amount)	5,173,534	*13,893,273*
Contingent liabilities and other commitments	366,779	*168,111*
Included in income statement		
Interest receivable	33	*386*
Interest payable	25,874	*21,407*
Fees and commissions receivable	4,576	*4,093*
Fees and commissions payable	14	*14*

At 31 December 2017 no amount was outstanding in respect of interest free loans or interest bearing loans due from Executive Managers of the Bank (*2016: £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 £564,000 *(2016: £342,000)*.
ii. Key management personnel compensation:

	2017	*2016*
Directors' attendance and standing fees	567	*564*
Executive Managers		
Salaries and other short term benefits	3,560	*3,442*
Post-employment benefits	83	*146*

36. Events after the reporting period

There are no matters that have taken place since the Year End that require disclosure.

All amounts in £'000s unless otherwise stated

London Head Office and Registered Office

British Arab Commercial Bank plc
8-10 Mansion House Place
London EC4N 8BJ England
Telephone: [44] (20) 7648 7777
Website: www.bacb.co.uk

Algiers Representative Office

British Arab Commercial Bank plc
Tour Algeria Business Centre
12eme Etage, Pins Maritimes
El Mohammadia
16212 Algiers, Algeria
Telephone: [213] (21) 89 1434

Abidjan Representative Office

British Arab Commercial Bank plc
15 bis Avenue Franchet d'Esperey
Immeuble Ollo, 1er Etage, Escalier B
Abidjan Plateau
Côte d'Ivoire
Telephone: [225] 203 04939

Tripoli Representative Office

British Arab Commercial Bank plc
Tripoli Tower
Floor 11, Office No. 111
PO Box 91051
Tripoli, Libya
Telephone: [218] (21) 335 1489
Facsimile: [218] (21) 335 1732

Dubai Representative Office

British Arab Commercial Bank plc
Office 504, Standard Chartered Tower
Level 5, Emaar Square
Downtown, Burj Khalifa
Dubai, United Arab Emirates
Telephone: [971] (04) 313 2448

Munich Representative Office

British Arab Commercial Bank plc
Office Number 309
Maximilianstraße 13
Munich, Bayern 80539
Germany
Telephone: [49] (0) 89 20 300 6309
Facsimile: [49] (0) 89 20 300 6450

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