

The HSBC Group

HSBC Bank Malta p.l.c. is a member of the HSBC Group, whose ultimate parent company is HSBC Holdings plc. Headquartered in London, HSBC Holdings plc is one of the largest banking and financial services organisations in the world. The HSBC Group's international network comprises around 7,500 offices in over 80 countries and territories in Europe, the Asia-Pacific region, the Americas, the Middle East and Africa.

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Chairman's Statement



I am pleased to advise that 2011 was a good year for HSBC Bank Malta p.l.c. during which it delivered a solid performance in spite of very challenging market conditions.

Results

Profit before taxation was €88m, representing an increase of 6% over prior year. On a like for like basis, excluding one-off items in 2010 and 2011, profit before tax was up 1%. Against the current economic backdrop, the worst in living memory, this represents a credible performance and was underpinned by positive contributions by all business lines.

By being prudent, yet proactive, HSBC Bank Malta has managed to navigate successfully through these troubled waters. Particular note should be taken of the excellent work during 2011 to reduce risk on the bank's investment portfolio. The bank has continued to grow its loan book and retains its position as the leading international bank in Malta.

Profit attributable to shareholders increased by 7% to €58m. On the basis of these results the Board is recommending a final gross ordinary dividend of 7.2 cent per share. Together with the interim gross dividend of 8.2 cent per share (5.3 cent net of tax) paid in August 2011, the total dividend for the year is 15.4 cent.

During 2011, the number of the bank's shareholders stood at around 10,400, many of which have remained loyal over the years. As testimony to our commitment to communicate better and more frequently with our shareholders we launched a new bilingual online publication, L-Azzjonist. This eco-friendly publication is available in the Investor Relations section of the HSBC Bank Malta website and has already proved to be popular with investors of the bank.

HSBC Bank Malta p.l.c. is a subsidiary of London-based HSBC Holdings plc, one of the world's leading financial services organisations, and remains the largest company listed on the Malta Stock Exchange with a market capitalisation of around €750m.

Strategy

2011 was the first year of implementing the HSBC group approved four-year Medium Term Outlook (MTO). This is the bank's strategic plan for the period 2011-2014 which establishes a clear direction of the bank's future and development opportunities in Malta and the strategic imperatives needed to achieve sustainable growth.

The overall strategy is based on building the business organically and consolidating the bank's market position by sustaining its strong domestic franchise and growing internationally by leveraging its global reach through the HSBC Group's worldwide network and internationally recognised brand. By playing to its strengths and focusing on its natural competitive advantages as a global organisation, the bank will seek to capitalise on the increasing market opportunities and play a leading role in Malta's growth as an international financial services centre.

During the year under review, the bank has continued to transform the organisation in line with the MTO by focusing on its segmentation strategy in its principal customer groups, generating efficiencies by streamlining processes and operations, making greater use of Regional Centres of Excellence, investing in technology and automated channels and delivering an unrivalled customer experience. Furthermore, the bank has been very active in facilitating cross-border commercial activity through its leading international business strategy and playing a more active role in the area of global banking and markets.

Reflecting customer behavioural trends of lower teller activity and the need for continued productivity and cost effectiveness, the bank has announced an €11m restructuring charge that will see a reduction in its staff complement and the closure of six branches. This restructuring is necessary to achieve long-term goals and will not involve any staff compulsory redundancies. Displaced employees will be redeployed elsewhere within the organisation or may choose to apply for a voluntary redundancy/early voluntary retirement scheme that has been made available.

Against this backdrop, it is worth noting that the bank remains committed to its substantial investment programme in Malta. During 2011 the bank implemented a new state-of-the-art core banking system with a capital investment of €10m. In addition to this, HSBC Malta continues the roll out of its €11m project to upgrade its branch network in line with Group global standards and introduce next-generation ATMs with increased functionality for greater customer convenience.

In December the bank sold its card acquiring business to Global Payments Inc. for a consideration of €11m. This is in line with HSBC Group strategy of exiting this part of the business around the world. Global Payments is a recognised worldwide leader in payments processing and together with HSBC Bank Malta will continue to provide customers with the card acceptance flexibility, convenience, service and support they need. The new acquiring business will continue to trade under the HSBC brand for the time being and will be called HSBC Merchant Services Ltd.

Corporate Sustainability

The key for HSBC Bank Malta and the HSBC Group remains long term corporate sustainability. As such the bank recognises the importance of continuing its programme of investments in the Maltese community. The principal focus areas are:

- Environment
- Education, in particular disadvantaged children, and
- Heritage

The HSBC Malta Foundation is the bank's main channel for corporate sustainability activity. In 2011 the Foundation supported a wide range of activities around Malta. Some of the key events included:

Environment

The afforestation project at Taht Chambray in Gozo

The project will cost €200,000 and it will be equally financed by the Foundation and the Maltese Government. HSBC has been a sponsor of the afforestation project in Malta from the start and has so far planted over 25,000 trees as part of this national programme.

Eco-Schools

The HSBC Malta Foundation has been supporting the Eco-Schools Programme for the past 6 years. Over 40,000 students have participated in this programme and so far at least 20 schools have secured the International Green Flag Award, a prestigious accreditation for their environmental practices at school.

Education

Young Enterprise

HSBC has been the sponsor of the Junior Achievement Young Enterprise Malta for the past 11 years. The programme offers a high-quality education programme that teaches students entrepreneurship and business skills in a practical way.

Caritas Malta

The Foundation is a long-time supporter of Caritas Malta in running its educational programme in primary and secondary schools with the aim of instilling sound values and promoting prevention against substance abuse.

Heritage

Support for Casa Rocca Piccola's celebration of lace

The Foundation is proud to be associated with a unique Maltese lace competition held annually at Casa Rocca Piccola in Valletta. In 2011 the competition honoured 58 traditional lace makers, including four children.



HSBC Malta employees participate in the HSBC Climate Partnership programme as part of HSBC's long standing commitment to protecting the environment and tackling climate change.

Chairman's Statement (continued)

Gozo historical documents

HSBC was the main sponsor of an exhibition of some 30 historical documents, etchings, plans and photographs relating to herbs, health and hospitals of Gozo at the National Archives in Victoria.

Throughout the year, in addition to signature sponsorships such as those noted above and the bank's participation with L-Istrina, a large number of HSBC staff have generously given their time to work within the community. It is this that makes HSBC's corporate sustainability work particularly special.

Board

During 2011 there was one change to the Board of Directors from the majority shareholder. Ms Sally Robson retired from the HSBC Group after a long and successful career in which she spent her last five years in Malta as a Director, Chief Operating Officer and subsequently Chief Technology and Services Officer. Ms Robson was succeeded by Philip Farrugia who is the current Chief Technology and Services Officer of the bank.

I would like to express my gratitude to Alan Richards who has served as a Director and CEO of the bank since 2008. From the beginning of 2012, Mr Richards has been appointed CEO for HSBC Indonesia. I thank Mr Richards for his positive contribution to the bank over the years and wish him every success in his new position. I also warmly welcome Mark Watkinson as an incoming Director and new CEO of the bank. Mr Watkinson joined us from HSBC North America and has been with the HSBC Group for 26 years, working in many countries around the world. I am certain Mr Watkinson will use his knowledge and significant international experience to continue the success of HSBC Malta.

I am fortunate to be the Chairman of a Board whose members have a wealth of both local and international knowledge. Collectively we have managed to provide the necessary leadership and vision to successfully guide our organisation through exceptionally challenging times.

The Board comprises myself as Chairman, an expatriate executive director who is also Chief Executive Officer of the bank, one local executive director who also serves as Chief Technology and Services Officer, five prominent non-executive directors who are all Maltese and one overseas-based director who is Chief Executive Officer, Continental Europe for HSBC.

I am confident that through the contributions of its members, the Board will continue to build on its achievements and lead the bank forward in the future.



HSBC Malta received FT's The Banker Award 2011 in recognition for its achievements and best overall performance.

International Recognition

HSBC Bank Malta has been named Bank of the Year in Malta for 2011 by the prestigious Financial Times monthly publication The Banker.

Winning this international award is a fitting accolade for the strong performance the bank delivered across all business areas in spite of increasingly difficult market conditions and is also a great tribute to the HSBC team in Malta.

The well-deserved award also enhances our credentials as Malta's leading local and international bank.

Outlook

2012 is anticipated to be an even more challenging year than 2011. The global and eurozone economic climate remains very difficult at best. However, the bank is well positioned to tackle the year ahead and remains very much open for business.

I would like to take this opportunity to thank the Board of Directors, Management and Staff of the bank for their hard work, loyalty and commitment in making 2011 a successful year. The HSBC Malta team remains the bank's greatest asset and key differentiation.

I thank our Shareholders for their ongoing support and our customers for their continued trust in our organisation.

With a clear strategy and a very strong global parent, I am confident that we can build on our business in Malta in 2012.

Albert Mizzi, Chairman
24 February 2012

Chief Executive Officer's Review



HSBC Bank Malta produced a solid result in 2011 against a backdrop of one of the most challenging economic times in living memory. Profit before tax increased by 6% to €88m and the business generated a return on equity of 15.7%.

On a like for like basis, excluding non-recurring items, the performance was 1% up on 2010.

The three main business lines, Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets all contributed positively to the overall performance.

During the year the bank continued to execute against its key transformation programme with a view to building long-term sustainability. In this light and reflecting changing customer behaviour patterns, an announcement was made in relation to a branch optimisation programme and the launch of a staff early voluntary retirement scheme. In addition to this, the bank disposed of its card acquiring business in line with an HSBC Group strategy to exit acquiring globally. The impact of the voluntary retirement scheme (€11m) and the sale of the acquiring business (€11m) was broadly neutral financially.

The bank has continued its investment programme with the implementation of a new €10m computer banking system and an €11m project to upgrade its branches and ATMs.

While I have only just taken the helm of HSBC Malta, I would like to express my thanks to the HSBC Bank Malta staff team for all the hard work over the last 12 months, without which the positive performance of the bank would not have been possible.

Performance

Profit before taxation for 2011 amounted to €88m, an increase of 6% over the previous year. This is a good result considering the ongoing volatility in international markets and underlines the excellent work undertaken to de-risk the bank's available-for-sale investment portfolio.

As noted above, the results reflect an €11m non-recurring staff cost in relation to an employee voluntary retirement programme and €11m sales proceeds from the sale of the card acquiring business.

Net interest income improved by 5% to €129m compared to €123m in 2010. This was attributable to asset growth and effective balance sheet management.

Net fees and commission income of €34m in 2011 was marginally down on prior year. Growth in account services fees were offset by a decline in stockbroking fees largely due to the slowdown in local capital markets bond issuance activity.

The life insurance subsidiary generated a profit before tax of €11m compared to €13m in 2010. Underlying new business generation, particularly with respect to protection, was encouraging. The business benefitted from a non-recurring gain of €7m as a result of a refinement in the methodology used to calculate the present value of in-force long-term insurance business. This benefit was eroded during the year as the yield curve continued to fall and the overall market value of the investment holdings reduced.

In view of significantly heightened stress in the eurozone debt markets, the bank reduced its risk exposure through the sale of holdings in higher risk eurozone countries from the available-for-sale bond portfolio at a net loss of €2m.

Chief Executive Officer's Review (continued)

Net other operating income increased significantly, from €5m in 2010 to €24m in 2011. The rise was driven by the above noted sale of the card acquiring business and the non-recurring gain in the Life insurance subsidiary relating to a methodology change.

Operating expenses of €98m were €11m or 12% higher compared to the previous year with a cost-to-income ratio of 50.4% compared to 49.7% in 2010. Costs increased principally due to the previously noted employee voluntary retirement provision of €11m and due to higher costs relating to utilities, regulatory fees and compliance.

At a consolidated level, net impairments rose from €5m to €8m in 2011. This was principally due to a €4m provision taken on Greek Government bonds held by the Life insurance subsidiary. The Life insurance subsidiary exposure to Greek debt is currently minimal and stands at €2m.

Other than the above exposure and investments in Maltese Government debt, the group has no exposure to southern European government debt.

The group's available-for-sale investments portfolio remains well diversified and conservative.

At a bank level, while there was a marginal deterioration in non-performing loans from 4% to 5%, in general asset quality remains good and loan impairments declined to €4m (11 basis points of the overall loan book) against €5m in 2010.

Net loans and advances to customers increased by €54m to €3,344m. Mortgage market share remained stable. Gross new lending to customers amounted to €656m which reflects the bank's continued support to the local economy.

Liabilities rose by €142m during the year and stood at €5,458m at the year end. The increase in liabilities reflected a rise in placements with the bank and a small fall in customer deposits.

The bank's liquidity position remains strong with an advances to deposits ratio of 76%, compared with 74% at 31 December 2010.

The bank strengthened its capital ratio by 140 basis points during the year and this now stands at 11.6%. This is well in excess of the 8% minimum regulatory requirement. The bank intends to maintain a conservative approach to capital and will continue to build capital where appropriate.

Based on the results the Board is recommending a final gross ordinary dividend of 7.2 cent per share.

Retail Banking and Wealth Management

During 2011, Retail Banking and Wealth Management continued to provide customers with the high quality service and brand experience for which HSBC is renowned.

The focus in Premier was to deepen existing relationships with our valued customer base. During 2011 the new Life Stage Tool was launched to provide customers with a user friendly way to map their life stages and wealth management needs against the products and services offered by HSBC. Furthermore, an exciting range of new discounts and privileges were made available to Premier customers and benefits were extended to family members.

The bank's Financial Planning Advisors and Private Client Managers have access to an unrivalled range of both HSBC and third party investment solutions including life protection and retirement planning. In 2011, in view of the volatile global markets, the focus was on developing structured investment products that provide capital protection to give customers peace of mind.

HSBC's Trust business continues to provide a highly bespoke service to our customer base. Group referrals from other overseas offices remains positive.

Shareshop provides access to international stock exchanges and facilitates the buying and selling of bonds and equities for our retail customers.

The bank remains very active in the domestic mortgage sector and during 2011 saw a growth in business both from first time buyers and those who were looking for a second property.

HSBC Global Asset Management Malta had another solid year despite difficult market conditions. The business registered stable performance in the level of assets under management driven by institutional business and retail funds.

Underlying insurance sales, particularly relating to protection, were strong. The overall result of the business, however, was hampered by market volatility on its investment portfolio although this was offset by beneficial changes in the methodology for recognising the emergence of insurance manufacturing profits.

HSBC Insurance Management Services (Europe) Limited was established to carry out regulated insurance management activities for other HSBC entities across the wider Group. In addition to support our own local insurance manufacturing business, insurance administration services are already being provided to HSBC Life (Europe) Ltd operating out of Dublin and Zurich.

From an insurance regulatory perspective, work on Solvency II implementation continues with significant progress made on all aspects of adopting the future risk based methodologies.

Commercial Banking

The Commercial Banking business delivered a strong performance during 2011 in spite of the global economic headwinds and political turmoil in North Africa. The lending book remains healthy and well secured and the 2012 pipeline is positive.

Customer service remains a key focus of the commercial banking strategy. During the year we have remained close to our customers to better understand their requirements and to provide them with support where necessary in an increasingly challenging economic environment.

During 2011 we continued to concentrate on the Leading International Business strategy. This is proving to be a very successful part of our commercial banking business. We have participated in a number of business delegations and overseas networking events leveraging HSBC's international reach. A partner support agreement was signed with the Malta Chamber of Commerce, Enterprise and Industry to help those enterprises wanting to expand their business internationally. An agreement was also signed with the Maltese-Chinese Chamber of Commerce to support entrepreneurs from both countries. This follows the launch of the Renminbi trade settlement account that established HSBC as the first bank in Malta to enable Maltese companies to directly trade in the Chinese currency, thus facilitating trade and investment with Chinese counterparts.

The HSBC Trade Connections quarterly forecast anticipates that trade in Malta will continue to grow over the next 12 months. Malta is expected to remain

an important trading route between Europe and North Africa, gaining hugely from its location within Europe and also its proximity to the key markets of the Middle East.

Two successful HSBC Trade Summits were held in Shanghai and Hamburg and were attended by a number of key customers from Malta with an international focus. Feedback from the events was very positive and enabled the customers concerned to network with potential clients and suppliers from around the world.

For the second consecutive year, HSBC sponsored the European Business Awards. Malta International Airport plc and Camilleri Holdings Ltd won a Ruban d'Honneur prize and represented the very best of Maltese businesses at the event.

For our small and medium local businesses we launched the Knowledge Centre information facility, a free resource, offering our business customers practical information to help run or start a new venture. Our Business Banking Direct proposition was also introduced to highlight the bank's online and call centre capabilities for smaller businesses.

In 2011, a group of bank "business advisors" coached a Young Enterprise team. The young entrepreneurs involved went on to win the Malta Finals and subsequently participate in the European finals in Oslo, Norway.

Global Banking and Markets

Despite increasing financial stress across the eurozone, Global Banking and Markets has continued to deliver above plan results. This has been achieved through prudent management of the bank's investments and markets risks, whilst also re-positioning all business units to play a leading role in driving Malta's growth as a hub for international financial services.



HSBC Bank Malta together with the the British High Commission Malta hosted an event for British Foreign Secretary Rt Hon. William Hague to meet members of local British Business Forum during a one-day visit to Malta on his way to Libya.

Chief Executive Officer's Review (continued)

In keeping with HSBC Group's policy of pro-active risk management, the Global Markets team sold the bank's investments in peripheral European debt during the year. The current book of high quality assets has benefitted from the anticipated 'flight to quality'. This has resulted in a positive adjustment to reserves. The adoption of a prudent investment approach and the use of sophisticated risk management techniques boosted net interest income in 2011.

The Global Markets team has seen a 40% increase in foreign exchange activity as it leverages the HSBC Group's global network to provide best in class services to our international corporate and institutional customers. We have also seen a significant increase in the sales of capital protected investment products, tailored to meet our retail customers' needs, in partnership with Retail Banking and Wealth Management. HSBC Stockbrokers continues to be the largest broker on the Malta Stock Exchange.

In order to support the growth of the financial services sector in Malta and to provide an attractive proposition to financial institutions setting up or relocating to Malta, we established a dedicated Financial Institutions team during the year. The team is comprised of both local and international staff and offers market leading advice and services. Coupled with this initiative the fund administration and custody business was restructured to drive higher customer service levels and to prepare for an increasingly challenging international regulatory environment.

HSBC Securities Services (HSS) made good progress during the year and generated a profit before tax of €1.5m. HSS remains a key area for investment. We have launched a governance programme to oversee a number of significant initiatives to enhance the international proposition of the business.

Overall, the Global Banking and Markets business has become an important contributor to the bank's bottom line and plays a pivotal role in the implementation of our strategy.

Technology and Services

During 2011 we brought to fruition various technological and services projects with the aim of enhancing customer experience, improving operational efficiency, and reducing operational costs.

The biggest single initiative in 2011 was the upgrade of our core banking computer system with an investment of over €10m. This new HSBC Group system enabled us to standardise our banking systems, our processes and our products to meet the ever-changing needs of our customers, and to make it easier for them to do business with the bank from anywhere in the world. The implementation of this project was carried out seamlessly and efficiently without affecting the normal daily services to our customers.

Investments were also made in workflow processes and imaging systems, whilst further standardised processes were migrated to Group and Regional Centres of Excellence, thereby enabling the bank to improve internal efficiency and free more resources for utilisation in more profitable areas.

We have continued our branch refurbishing programme and completed another five branches to add to the four renovated in 2010. These branches are now in line with the highest HSBC Group standards around the world and reflect the changing behaviour pattern of our customers who increasingly look for mortgage and wealth management advice in branches but prefer to transact either online or through one of our call centres.



HSBC Malta is investing €11 million to upgrade its branches and ATMs. The new branches are designed to give more privacy and space to customers visiting HSBC to plan their financial future and manage their wealth.

A Commercial Banking Contact Centre was established during the year to provide a high quality and efficient telephone service to our commercial customers.

Another important initiative was the upgrade and increase of our ATM network across the island. A total of 14 next-generation ATMs were installed in various localities, offering instant value for cash deposits to customers, with cheque deposit functionality to be provided later in 2012.

Customer behaviour is changing. During 2011 teller activity in our branch network dropped by 14% whilst the use of Internet Banking increased by 13% and card usage at point of sale by 11%. It is, therefore, important that we continue to invest in providing more and better self-service facilities to satisfy the changing needs of our customers.

As a result of better property management, the bank disposed of vacant freehold and leasehold properties including a significant part of its ex-Head Office in Republic Street, Valletta.

People

Our people remain our greatest strength and it needs to be recognised that only through our talented and professional workforce could our good results in 2011 have been achieved.

During 2011 we signed new Collective Agreements that provide for improved working conditions, benefits and opportunities for all staff.

We continue to invest in our people through training, professional development and talent management.

A number of staff benefitted from overseas programmes run by the HSBC Group and we continue to look for and promote international attachment/secondment opportunities for key talent.

As I noted earlier, during the year the bank announced an early voluntary retirement scheme for its employees as part of the continued transformation programme of the business. Such programmes remain entirely voluntary but at the option of the bank.

In 2012 we will continue to introduce more staff-related initiatives and invest to maintain the highest standards of professionalism.

Outlook

The Maltese economy has performed reasonably well over the last twelve months and showed considerable resilience since the global troubles began in late 2008. The economy has registered above-average EU and eurozone GDP growth in both 2010 and 2011. The banking system remains robust and the economy has not suffered from a housing or sovereign debt crisis.

GDP growth is likely to remain positive in 2012 but lower than 2011. The continued travails of the eurozone and economic uncertainty will weigh on confidence. Bank and domestic corporate profitability will remain under pressure and companies will focus on driving operational efficiencies and sustainable costs savings while real growth is hard to achieve. Nevertheless, we remain cautiously optimistic as the key banks in the market remain well capitalised and open for business, tourist numbers continue to grow, the housing market while soft has not declined significantly, the local regulatory atmosphere is pro-business and real growth and opportunity is seen as Malta develops its international financial services platform.

HSBC Bank Malta remains well positioned for the challenging year ahead. The balance sheet is strong, the strategy is clear and key transformation programmes are well underway. The focus will remain on investing in our local franchise and leveraging our international competitive advantage through our parent, HSBC Holdings, one of the world's largest and strongest financial organisations.



Mark Watkinson, *Chief Executive Officer*
24 February 2012

Board of Directors



Albert Mizzi, NON-EXECUTIVE CHAIRMAN

Non-Executive Chairman of HSBC Bank Malta p.l.c. since June 1999. In 1946, joined family business Alf. Mizzi & Sons Ltd. and was Chairman for several years. In the 1960s he was heavily involved in private banking and appointed director of Medport. Established a number of Malta's important parastatal businesses: Air Malta, Sea Malta, Medserv, Mediterranean Insurance Brokers and Middle Sea Insurance. Following the setting up of Air Malta in 1973, he served as its Chairman for 19 years.

Alan Richards, DIRECTOR AND CHIEF EXECUTIVE OFFICER

Director and Chief Executive Officer of HSBC Bank Malta p.l.c. from May 2008 until 1 January 2012. A Senior Associate of the Australasian Institute of Banking and Finance and a member of the Institute of Financial Services. He was formerly Director and Deputy Chief Executive Officer of HSBC Australia and Director and Head of Retail Banking, HSBC Bank A.S. Turkey. Previously, he has also held the posts of Director of HSBC Broking Asia and prior to that of General Manager HSBC Bank Malaysia. Resigned on 1 January 2012 as he was appointed Chief Executive Officer HSBC Indonesia.



Mark Watkinson, DIRECTOR AND CHIEF EXECUTIVE OFFICER

Appointed Chief Executive Officer on 1 January 2012 and Director on 14 February 2012. Prior to taking up his appointment in Malta, he was Head of Commercial Banking for North America based in New York. He has worked for HSBC for 26 years. In the past 5 years he has worked in New York, Toronto as Head of Commercial Banking for HSBC Canada and as President and Chief Executive Officer for HSBC Bank in the Philippines.

Philip Farrugia, DIRECTOR AND CHIEF TECHNOLOGY AND SERVICES OFFICER

Chief Technology and Services Officer from January 2011 and Director on 15 February 2011. Has been employed with the bank since 1969 and has occupied a number of senior posts in both branches and Head Office departments. In 1980, he was seconded to the home loans company (Lohombus), rising to lead the company as Deputy General Manager and Company Secretary. In 2005 he was appointed Head of Service Delivery for the Bank, and has been a member of the executive team for six years.



Peter William Boyles, NON-EXECUTIVE DIRECTOR

Non-Executive Director since 6 May 2010. Mr Boyles is Director of HSBC Bank plc. and Chief Executive Officer Continental Europe. He is also Chairman of HSBC Bank A.S. Turkey, Deputy Chairman HSBC France and a member of the HSBC Trinkaus Supervisory Board. Mr Boyles commenced his career with HSBC as an International Manager in 1975. His most recent roles include HSBC France CEO (where he managed the integration of CCF into the Group) and HSBC Group Head of Human Resources.

Philip Farrugia Randon, NON-EXECUTIVE DIRECTOR

Director of HSBC Bank Malta p.l.c. since June 2004. Graduated LL.D. in 1973 and joined the bank in 1974 as a legal adviser. Held the post of Company Secretary and the post of Head of Group Legal Department of the bank for several years. Retired from the bank in May 2008.





Charles John Farrugia, NON-EXECUTIVE DIRECTOR

Director of HSBC Bank Malta p.l.c. since November 2004. Joined the bank in 1975. Was appointed Chief Dealer in 1995, Group Senior Treasury Manager in 1999 and Managing Director of HSBC Stockbrokers (Malta) Limited in 2001. Held the post of Head of Global Banking and Markets of HSBC Bank Malta p.l.c. for several years. Retired from the bank January 2010.

Peter Paul Testaferrata Moroni Viani, NON-EXECUTIVE DIRECTOR

Non-Executive Director of HSBC Bank Malta p.l.c. since March 2001. Holds various executive positions and directorships within the Testaferrata Group of companies.



Saviour sive Sonny Portelli, NON-EXECUTIVE DIRECTOR

Appointed Director of HSBC Bank Malta p.l.c. on 9 October 2006. Mr Portelli is a senior Maltese businessman who is currently the Chairman of The Malta Council for Economic and Social Development. Mr Portelli had an early career in the Malta Civil Service which he left to join the Tourist Sector. Besides being a Marketing Specialist he sits as non-executive director on the boards of various Maltese companies.

James Dunbar Cousin, NON-EXECUTIVE DIRECTOR

Appointed Director of the Bank on 1 April 2009. Joined Barclays Bank D.C.O. in 1968. Occupied various managerial roles within the branch network of Mid-Med Bank Ltd. Subsequently, he occupied the roles of Executive Manager and later Head of Commercial Banking of the bank. Mr Dunbar Cousin retired from the bank at the end of 2008.



George Brancaleone, COMPANY SECRETARY

Company Secretary of HSBC Bank Malta p.l.c. since June 2004. Joined the bank in 1980 and graduated LL.D. in 1988. Company Secretary of various HSBC subsidiaries in Malta since 2001. Presently holds the post of Senior Manager at Audit, Compliance and Legal Department of HSBC Bank Malta p.l.c.

Financial Review

Summary of Financial Performance

Group profit

Against a backdrop of very challenging economic conditions in Europe, HSBC Bank Malta p.l.c. delivered a good performance in 2011. The reported profit before tax of €88m increased by 6%, or €5m compared to 2010 driven primarily by an improved level of revenues.

Profit attributable to shareholders was €58m, an increase of €4m over prior year figure.

Net operating income of €195m increased by €19m compared with €176m in 2010. Net interest income increased by €6m to €129m.

Operating expenses were €98m, an increase of €11m over prior year but this included restructuring costs of €11m.

The group's cost to income ratio is 50.4% compared to a prior year ratio of 49.7%.

Shareholder ratios

Earnings per share of 19.7 cent compared to 18.4 cent for the same period in 2010, with the pre-tax return on shareholders' funds at 24.1% compared to 24.9% in 2010.

The Directors propose a final gross dividend of 7.2 cent per share. This follows on the gross interim dividend of 8.2 cent paid in August 2011.

Net interest income

Net interest income improved by 5% to €129m compared to €123m last year attributable to asset growth and effective balance sheet management. However, liability margins remain under pressure given the low interest rate environment.

Non-interest income

Non-interest income increased significantly from €53m in 2010 to €66m in 2011 benefiting from net gains of €10m arising from the sale of our card acquiring business to Global Payments Inc and increase in life insurance present value of in-force long-term insurance business. Underlying performance of the bank's core business remained satisfactory given the volatile market conditions with investment activity impacted by weak investor sentiment.

Net fees and commission income of €34m in 2011 was marginally down on 2010. Growth in account services fees were offset by a decline in stockbroking fees largely due to the slow-down in local capital markets bond issuance activity.

Trading profits of €8m increased by 22% or €1m compared to €7m in 2010 due to good growth in foreign exchange volumes.

The second half of 2011 was dominated by the continuing volatility in the global markets and specifically the significant deterioration in the eurozone sovereign crisis. The bank anticipated this in the first half of the year and positioned the balance sheet to significantly reduce market risk at a net loss of €2m as at 31 December 2011.

The life insurance subsidiary generated a profit before tax of €11m compared to €13m in 2010. Underlying new business performance generation particularly with respect to protection was encouraging. The business benefited from a non-recurring gain of €7m as a result of a refinement in the methodology used to calculate the present value of in-force long-term insurance business. This benefit was eroded during the year as the Euro swap curve continued to fall and the overall market value of investment holdings reduced.

Operating expenses

Operating expenses of €98m were €11m or 12% higher compared to the previous year with a cost to income ratio of 50.4% compared to 49.7% in 2010. Costs increased, principally due to staff voluntary retirement scheme provision of €11m reported in Employee compensation and benefits and due to higher costs relating to utilities and compliance costs.

General and administrative expenses increased by €3m to €33m as a result of investment in channel migration, offshoring, improving systems as well as the cost of higher utilities and compliance costs.

Depreciation and amortisation charges of €6m decreased by €0.7m compared to the previous year.

Net impairment

Net impairment of €8m included an impairment of €4m relating to the available-for-sale Greek government bonds held by the Life insurance subsidiary.

At a bank level, while there was a marginal deterioration in non-performing loans from 4% to 5%, the general asset quality remains good and impairments declined to €4m (11 basis points of overall loan book) against €5m in 2010.

Impairment reversals contributed €5m to profitability. New impairment allowances of €7m were raised and bad debt write-offs of €1m were effected.

Taxation

The 2011 effective rate of tax was 34.8% per cent. Tax expense for 2011 amounted to €31m.

Assets

Total assets amounted to €5,825m, 3% higher than at 31 December 2010. The main increases were reported in debt securities investments as part of the bank's liquidity management.

Balances with Central Bank of Malta, Treasury Bills and cash holdings reduced from a prior year end level of €380m to a year end level of €233m.

Net loans and advances to customers increased by €54m to €3,344m supported mainly by growth in the personal sector.

The bank's liquidity position remains strong with advances to deposit ratio of 76% compared with 74% at 31 December 2010.

The balance sheet remains well diversified and conservative with negligible exposure to sovereign debt in the peripheral eurozone countries following the sale of holdings in the higher risk eurozone countries during 2011.

The available-for-sale investment portfolio increased by €246m to €937m. A fair value gain of €1m was reported during the year. The mark-up was credited to revaluation reserve, net of tax.

Life insurance business assets, are primarily designated as financial assets at fair value through profit or loss. This portfolio increased by €64m to €370m from a prior year end level of €306m.

Liabilities

Total liabilities increased by €142m to €5,458m at year end. The increase in liabilities reflected a rise in placements with the bank and a small fall in customer liabilities.

Customer deposits of €4,403m as at 31 December 2011 reduced by €60m compared to 31 December 2010 reflecting the levels of volatility of deposits from the institutional sector. Retail deposits were broadly stable despite continuing competitive pressures for deposits including from local government bond issuances.

Funds under management by the group reached a year end closing level of €694 million.

Liabilities under insurance contracts issued increased by €26m during the year to reach a year end level of €437m.

Shareholders' funds

Equity totaled €366m at year end following dividend payments of €30m during 2011.

The number of shareholders as at 31 December 2011 stood at 10,366.

The capital adequacy ratio at 11.6% is well above regulatory capital requirements.

Report of the Directors

Results for 2011

The group reported a profit on ordinary activities before tax of €88m for the year under review. The group's profit attributable to shareholders of the bank was €58m.

A gross interim ordinary dividend of 8.2 cent was paid on 24 August 2011. The Directors have proposed a gross final dividend of 7.2 cent per ordinary share. The final dividend will be payable to shareholders on the bank's register as at 19 March 2012.

Further information about the results is provided in the group income statement and the statement of comprehensive income on pages 29 and 30.

Principal activities

Principal activities of parent company

The bank is authorised to carry on the business of banking under the Banking Act, 1994 as a credit institution. It is also an authorised dealer in terms of the Exchange Control Act and a licensed financial intermediary in terms of the Financial Markets Act, 1990. The bank also holds Category 3 and Category 4 Investment Services licenses issued by the Malta Financial Services Authority in terms of the Investment Services Act, 1994. These licenses authorise the bank to provide both investment services to third parties and trustee or custodian services for collective investment schemes.

The bank provides a comprehensive range of banking and financial related services.

The group had the following subsidiaries at 31 December 2011: HSBC Life Assurance (Malta) Ltd, HSBC Global Asset Management (Malta) Limited, HSBC Securities Services (Malta) Limited, HSBC Stockbrokers (Malta) Limited and HSBC Insurance Management Services (Europe) Limited.

Principal activities of subsidiaries

HSBC Life Assurance (Malta) Ltd is authorised by the Malta Financial Services Authority to carry on business of insurance in Malta under the Insurance Business Act, 1998. HSBC Bank Malta p.l.c. is enrolled as a tied insurance intermediary for HSBC Life Assurance (Malta) Ltd under the Insurance Intermediaries Act 2006. On 28 April 2011, HSBC Life established a new subsidiary HSBC Insurance Management Services (Europe) Limited with the main objective of providing operational support to HSBC Group Insurance Companies. It has already entered into two formal agreements for the provision of insurance operational and administrative services to HSBC Life Assurance (Malta) Ltd and HSBC Life (Europe) Ltd based in Dublin. Beyond these two initial appointments, this company will be marketed within the HSBC Group as a Centre of Excellence for Insurance Operational support and administrative services seeking similar appointments from other Group Insurance Companies.

HSBC Global Asset Management (Malta) Limited is the investment management arm of the bank. It manages a range of domestic and international funds, specialising in the development of structured capital secured investments products, and in the provision of tailor-made discretionary portfolio management services. The company offers both Open and Close ended types of funds and investments.

HSBC Securities Services (Malta) Limited is licensed under the Investment Services Act, 1994 and its main business activity is the provision of fund administration services to proprietary and third party investment funds. It also provides back office support to HSBC Bank Malta p.l.c. in the distribution of third party investment funds through the bank network.

HSBC Stockbrokers (Malta) Limited is a member of the Malta Stock Exchange and is regulated under the Investment Services Act, 1994 by the Malta Financial Services Authority. The company is principally engaged in providing stockbroking business on the Malta Stock Exchange and to arrange/support the listing of stocks and shares on the Exchange.

Business review

A review of the business of the bank and its subsidiaries during the year under review and an indication of likely future developments are given in the 'Chief Executive Officer's Review' on pages 5 to 9.

Transactions in own shares

The bank holds units in a mutual fund which invests in the bank's shares. During the year, the bank indirectly acquired 25,838 additional own shares bringing the total number of shares indirectly held at 31 December 2011 to 61,455.

Shareholder Register Information pursuant to Listing Rule 5.64

HSBC Bank Malta p.l.c. (the 'bank') authorised share capital is €141,000,000. The issued and fully paid up capital is €87,552,000 divided into 291,840,000 Ordinary Shares of a nominal value of 30.0 cent each. The issued share capital consists of one class of ordinary shares with equal voting rights attached and freely transferable.

HSBC Europe B.V. holds 70.03% of the bank's shares.

The largest single shareholder of the bank, provided it holds at least thirty three per cent (33%) of the ordinary issued share capital of the bank, shall be entitled to appoint the Chairman from amongst the Directors appointed or elected to the Board.

Every shareholder owning eleven per cent (11%) of the ordinary issued share capital, shall be entitled to appoint one Director for each and every eleven per cent (11%) of the ordinary issued share capital of the bank owned by such shareholder. Any fractional shareholding not so utilised in the appointment of Director(s) shall be entitled to participate in the voting for the election of further Directors.

There is an Achievement Shares scheme in existence whereby employees in the GCB3 grade and higher can be awarded shares in HSBC Holdings plc, depending on their performance. Share awards will be released to the individual after 3 years, provided the participant remains continuously employed within the Group. During the 3-year period the employee has no voting rights whatsoever.

The rules governing the appointment of Board members are contained in Articles 77 to 80 of the bank's Articles of Association. An extraordinary resolution approved by the shareholders in the general meeting is required to amend the Articles of Association.

The powers of the Directors are outlined in Articles 73, 74 and 85 of the bank's Articles of Association. In terms of Article 12 of the said Articles of Association, the bank may, subject to the provisions of the Companies Act 1995, acquire or hold any of its shares.

The Collective Agreement regulates redundancies, early retirement, resignation or termination of employment of employees. There are no contracts between the bank and the Directors on the bank's Board.

It is hereby declared that, as at 31 December 2011, the requirements pursuant to Listing Rules 5.64.7 and 5.64.10 did not apply to the bank.

Shareholder Register Information

Directors' interest in the share capital of the company or in related companies at 31 December 2011:

Albert Mizzi	8,000 shares
Philip Farrugia Randon	6,400 shares
Saviour sive Sonny Portelli	4,700 shares

Mr Charles John Farrugia has a non-beneficial interest of 7,511,587 ordinary shares in HSBC Bank Malta p.l.c. through the shareholding held by Amalgamated Investments Sicav p.l.c. and a non-beneficial interest of 15,000 ordinary shares through the shareholding held by Industrial Management Ltd.

Mr Peter Paul Testaferrata Moroni Viani has a beneficial interest of 58,800 ordinary shares in HSBC Bank Malta p.l.c. through the shareholding of Testaferrata Moroni Viani (Holdings) Limited, 40,000 ordinary shares through the shareholding of Testaferrata Moroni Viani Limited, 40,000 ordinary shares through the shareholding of Viani Limited and 5,000 ordinary shares through the shareholding of Sales and Letting Limited.

Report of the Directors (continued)

He also has a non-beneficial interest of 130,680 ordinary shares in HSBC Bank Malta p.l.c. through the shareholding of Santumas Shareholdings p.l.c. under Custodianship of HSBC Bank Malta p.l.c.

There were no changes to Directors' interest from 31 December 2011 to 31 January 2012.

Shareholders holding five per cent (5%) or more of the equity capital at 31 January 2012:

HSBC Europe B.V. 70.03%

Number of shareholders at 31 January 2012:

One class of shares 10,356 shareholders
(All shares have equal voting rights)

Number of shareholders analysed by range

Range of shareholding	31 January 2012	
	Total shareholders	Shares
1 – 500	2,146	661,035
501 – 1,000	1,619	1,312,527
1,001 – 5,000	4,148	10,460,522
5,001 and over	2,443	279,405,916
Total Shareholding	10,356	291,840,000

Standard licence conditions

In accordance with SLC 7.35 of the Investment Services Rules For Investment Services Providers regulated by the Malta Financial Services Authority, license holders are required to include in the Directors' Report breaches of standard licence conditions. Accordingly, the Directors confirm that no breaches of the standard licence conditions and no other breach of regulatory requirements, which were subject to administrative penalty or regulatory sanction were reported.

Board of Directors

The Directors who served during the year and after year end are as follows:

Albert Mizzi (Chairman)	Philip Farrugia Randon
Alan Richards (resigned on 1 January 2012)	Charles John Farrugia
Mark Watkinson (appointed on 14 February 2012)	Peter Paul Testaferrata Moroni Viani
Sally Robson (resigned on 9 February 2011)	Saviour sive Sonny Portelli
Philip Farrugia (appointed on 15 February 2011)	James Dunbar Cousin
Peter William Boyles	

Senior management

As at 31 December 2011, the senior management of the group was composed of the following:

Mark Watkinson	Chief Executive Officer (appointed on 1 January 2012)
Alan Richards	Chief Executive Officer (resigned on 1 January 2012)
Philip Farrugia	Chief Technology and Services Officer
Chris Bond	Head of Global Banking and Markets
Michel Cordina	Head of Commercial Banking
Paul Steel	Head of Retail Banking and Wealth Management
Josephine Magri	Chief Financial Officer
Stewart Luscott-Evans	Chief Risk Officer
Mark Sims	Head of Human Resources
John Sammut	Head of Audit, Compliance and Legal
Joseph Borg	Head of IT
James Hewitson	Managing Director HSBC Life Assurance (Malta) Ltd
Brian Tortell	Head of Marketing
Peter Calleya	Head of Capital Management and Planning
Franco Aloisio	Head of Communications

Auditors

KPMG have expressed their willingness to continue in office. A resolution proposing the reappointment of KPMG as auditors of the bank will be submitted at the forthcoming Annual General Meeting.

Going Concern

As required by Listing Rule 5.62, upon due consideration of the bank's profitability and statement of financial position, capital adequacy and solvency, the Directors confirm the bank's ability to continue operating as a going concern for the foreseeable future.

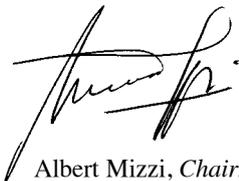
Statement by the Directors pursuant to Listing Rule 5.70.1

Pursuant to Listing Rule 5.70.1 there were no material contracts to which the bank, or anyone of its subsidiary undertakings, was party to and in which anyone of the Directors was directly or indirectly interested.

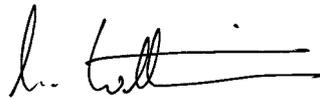
Statement by the Directors pursuant to Listing Rule 5.68

We, the undersigned, declare that to the best of our knowledge, the financial statements prepared in accordance with the requirements of International Financial Reporting Standards as adopted by the EU give a true and fair view of the assets, liabilities, financial position and profit or loss of the bank and its subsidiaries included in the consolidation taken as a whole and that this report includes a fair review of the development and performance of the business and the position of the bank and its subsidiaries included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

Signed on behalf of the Board on 24 February 2012 by:



Albert Mizzi, *Chairman*



Mark Watkinson, *Chief Executive Officer*

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

Pursuant to the Malta Financial Services Authority Listing Rules, HSBC Bank Malta p.l.c. (the 'bank') as a company whose equity securities are listed on a regulated market endeavours to adopt the Code of Principles of Good Corporate Governance (the 'Principles') embodied in Appendix 5.1 to Chapter 5 of the Listing Rules. The bank is obliged in terms of Listing Rule 5.94 to prepare a report explaining how it has complied with the provisions of the said Code. The bank hereby includes a Statement divided in two sections: the first part detailing the effective measures adopted by the bank to ensure compliance with the Principles and the second part explaining the reasons behind instances of non-compliance.

Although the Principles are not mandatory, the Board of Directors (the 'Board') of the bank believes in their adoption, and has endorsed them except where there exist particular circumstances that warrant non-adherence thereto. The Board believes that adherence to the Principles has been and will remain a top priority for the bank and considers it to be a responsibility which starts with the Board and permeates down throughout the bank. The Board is proud of the fact that the bank has a good corporate governance framework that ensures that directors work collectively through an effective Board, oversee the management of the business, set the tone from the top, ensure the integrity of financial reporting, set a risk management framework for the bank and communicate with shareholders. The Board firmly believes that adherence to the Principles is crucial to ensure more transparent governance structures, increased accountability and improved relations within the market which should enhance market integrity and confidence.

Compliance with the Code

Principle 1: The Board

The bank is headed by an effective Board which leads and controls the bank. All the Directors, individually and collectively, are of the appropriate calibre, with the necessary skills and experience to assist them in providing leadership, integrity and judgement in directing the bank. The integrity, honesty and diligence of the Directors guarantee that the bank adheres to HSBC Group's high ethical business values.

Board members are accountable for their performance and that of their delegates. Besides having a broad knowledge of the bank's business they are also conversant with the statutory and regulatory requirements regulating this business.

The Board determines the bank's strategic aims and organizational structures and regularly reviews management performance. It ensures that the bank has the appropriate financial and human resources to meet its objectives.

The Board delegates specific responsibilities to a number of committees, notably the Audit Committee, the Remuneration Committee, the Executive Committee, the Asset and Liability Management Committee, the Group Risk Management Committee and the Credit Risk Management Committee.

Further detail in relation to the Committees and the responsibilities of their respective boards can be found under Principle 8 of this Statement.

Principle 2: Chairman and Chief Executive Officer

The position of the Chairman and that of the Chief Executive Officer are occupied by different individuals. There is a clear division of responsibilities between the running of the board and the Chief Executive Officer's responsibility in managing the bank's business. This separation of roles of the Chairman and Chief Executive Officer avoids concentration of authority and power in one individual and differentiates leadership of the board from the running of the business.

The Chairman exercises independent judgement even though he is appointed by the majority shareholder. He leads the Board, sets the agenda and ensures that the Directors receive precise, timely and objective information and at the same time ensures effective communication with shareholders. During Board meetings, he leads the Board and encourages active engagement by all board members for the discussion of complex and contentious issues and stimulates constructive challenge of senior management.

On the other hand, the Chief Executive Officer is Chairman of most of the Board Committees and subsidiary companies. His main role and responsibility is to execute agreed strategy and manage the business.

Principle 3: Composition of the Board

The Board considers that the size of the Board is the most appropriate to ensure an effective management and oversight over the bank's operations as demonstrated throughout the years.

The Board is composed of individuals who have a range of skills, competence, knowledge and experience that enable them to fulfil their roles diligently and are capable of understanding and fully appreciating the business risk issues and key performance indicators.

In line with Principle 3, the Board is composed of a non-executive Chairman, two executive Directors, three non-executive Directors and three independent non-executive Directors.

The independent non-executive Directors are the following:

Mr Saviour sive Sonny Portelli

Mr Peter Paul Testaferrata Moroni Viani

Mr James Dunbar Cousin

In determining the independence or otherwise of its Directors, the Board has considered, inter alia, the principles relating to independence embodied in the code, the Group's own practice as well as general good practice principles.

The Board considers that the fact that one of the Directors is a former employee of the bank and the other has a significant business relationship with the bank do not undermine the said Directors' ability to exercise independent judgement when considering the issues brought before the Board. Moreover, these two Directors were nominated by the minority shareholders.

In terms of Principle 3.4 each non-executive Director has confirmed in writing to the Board that he undertook:

- a) to maintain in all circumstances his independence of analysis, decision and action;
- b) not to seek or accept any unreasonable advantages that could be considered as compromising his independence; and
- c) to clearly express his opposition in the event that he finds that a decision of the Board may harm the bank.

Principle 4: The Responsibilities of the Board

The Board concentrates primarily on strategy, policy setting, business plans and financial information. It reviews and evaluates corporate strategy, major operational and functional plans, risk policy and financial performance objectives. It also monitors implementation of such objectives and corporate performance within the parameters of all relevant laws, regulations and codes of best practice. The board ensures that a balance is maintained between enterprise and control.

The Board's informed assessment of management's performance results from a clear internal and external reporting system. The Board continuously assesses and monitors the bank's present and future operations, opportunities, threats and risks in the external environment and current and future strengths and weaknesses. The evaluation of the management's implementation of corporate strategy and financial obligations is based on the use of key performance indicators enabling the bank to adopt expedient corrective measures. These key business risks and performance indicators are benchmarked against industry norms so as to ensure that the bank's performance is effectively evaluated.

The Board ensures that the bank has appropriate policies and procedures in place that guarantee that the bank and its employees maintain the highest standards of corporate conduct and compliance with the applicable laws, regulations, business and ethical standards.

Statement of Compliance with the Code of Principles of Good Corporate Governance (continued)

Principle 5: Board Meetings

The Board meets on a quarterly basis, unless further meetings are required to discharge its duties effectively.

The Chairman ensures that all relevant issues are on the agenda, supported by all the available information. The agenda strikes a balance between long-term strategic objectives and shorter-term performance issues. Notice of the dates of Board meetings together with supporting materials are circulated to the Directors well in advance of the meetings.

During Board meetings minutes are prepared that records faithfully attendance, discussed matters and decisions. These minutes are subsequently circulated to all the Directors as soon as practicable after the meeting.

Directors' Attendance at Board Meetings:

Members	Attended
Albert Mizzi	4
Alan Richards*	4
Peter W. Boyles	3
Philip Farrugia	4
Charles John Farrugia	4
Philip Farrugia Randon	4
Peter Paul Testaferrata Moroni Viani	4
Saviour sive Sonny Portelli	4
James Dunbar Cousin	4

*Mr Alan Richards resigned from the post of Director and Chief Executive of the Bank, with effect from 1 January 2012. Mr Mark Watkinson was appointed Chief Executive Officer with effect from 1 January 2012 and director with effect from 14 February 2012.

Principle 6: Information And Professional Development

The Board appoints the Chief Executive Officer of the bank upon guidance and recommendation from the HSBC Group. This enables the bank to avail itself of the vast wealth of competence, talent and experience found across the Group.

Upon joining the Board, a Director is provided with a handbook containing the main provisions of law, which regulate his office. The Director also attends a presentation made by the functional heads on the activities of their respective business units in the bank. The Directors also receive updates on changes, if any, to the Group's short term strategic and operational plans and quarterly updates by the Chief Technology and Services Officer, Chief Financial Officer, the Chief Risk Officer and by the Heads of Retail Banking and Wealth Management, Commercial Banking, Global Banking and Markets and Marketing.

Directors also have access to the advice and services of the Company Secretary who is responsible for adherence to Board procedures as well as effective information flows within the Board, its Committees and with senior management. The Company Secretary also directs Board members to seminars or conferences which serve as professional development for Directors. Moreover, Directors have access to independent professional advice, at the bank's expense.

The Chairman of the Board and the Chairman of the Audit committee attend on an annual basis the Group Chairman's Non-Executive Directors' Forum and the Audit Committee Chairmen Forum where they are updated on the latest Group's strategy and global financial and economic developments.

As part of the succession planning and talent management the Board and the Chief Executive Officer ensure that the bank implements appropriate schemes to recruit, retain and motivate high quality executive officers, to encourage members of management to move to the higher ranks within the organisation and to maintain high morale amongst the bank's staff.

Principle 7: Evaluation of the Board Performance

The Board undertook an evaluation of its own performance, the Chairman's performance and that of its Committees. The Board did not appoint an ad hoc committee to carry out this performance evaluation but the evaluation exercise was conducted through a Board Effectiveness Questionnaire by the Company Secretary in liaison with the Chairman modelled on a Board Effectiveness Questionnaire used by the Group.

Although no material changes resulted from an analysis of the responses to this Board Effectiveness Questionnaire certain minor changes were implemented in order to increase the Board's effectiveness.

Principle 8: Committees

The Board delegates specific responsibilities to Committees, which operate under their respective formal terms of reference. The Board has established the following Committees:

Audit Committee

The Audit Committee met five times during this year. Its Terms of Reference were originally modelled mainly on the recommendations in the Cadbury Report, the UK Walker Review and are compliant with the Listing Rules. This year these Terms of Reference have been amended in order to increase the Audit Committee's oversight on risk factors.

The primary purpose of this Committee is to protect the interests of the bank's shareholders and assist the Directors in conducting their role effectively so that the bank's decision-making capability and the accuracy of its reporting and financial results are maintained at a high level at all times.

The Audit Committee also scrutinises and approves related party transactions. It considers the materiality and the nature of the related party transaction carried out by the bank to ensure that the arms' length principle is adhered to at all times.

The members of the Audit Committee are Messrs Saviour sive Sonny Portelli (Chairman) and Peter Paul Testaferrata Moroni Viani who are independent non-executive directors and Dr Philip Farrugia Randon LL.D. who is a non-executive director. Executives of the bank are invited to attend any of the meetings as directed by the Committee. The Chief Executive Officer, the Chief Technology and Services Officer, the Chief Risk Officer and a representative of the external auditors attend the meetings. In line with Listing Rule 5.131, the Head of Internal Audit is always present for its meetings and has a right of direct access to the Chairman of the Committee at all times. The Head of Continental Europe Group Audit sometimes attends these meetings.

Mr Saviour sive Sonny Portelli was appointed by the Board as the director who is independent and competent in accounting and/or auditing in terms of Listing Rule 5.117 on the basis that he has a long and distinguished career in both public companies and private enterprise. Presently, Mr Portelli is also Chairman of the Malta Council for Economic and Social Development. Mr Portelli has served on the Bank's Board of Directors since October 2006 where his contributions have demonstrated that he is highly competent in accounting and au courant with accounting standards and practices and that he also possesses the qualities and experience required to discharge his duties as Chairman of this Committee.

As Chairman of the Audit Committee Mr Portelli attends the Group's annual Audit Committee Chairmen's Forum. This provides the Chairman with the latest updates on key considerations, priorities and challenges facing the Committee.

In terms of Listing Rule 5.127.7, the Audit Committee is responsible for developing and implementing a policy on the engagement of the external auditor to supply non-audit services. Since HSBC Holdings plc is a Securities Exchange Commission (SEC) registered company, non-audit services provided by the external auditor are regulated in terms of the SEC rules.

Remuneration Committee (REMCO)

The Remuneration Committee is dealt with under the Remuneration Report on pages 26 and 27, which also includes the Remuneration Statement in terms of Code Provisions 8.A.3 and 8.A.4.

Executive Committee (EXCO)

The Executive Committee meets on a monthly basis to oversee the overall day-to-day management of the bank in accordance with such policies and directions as the Board may from time to time determine. The Chief Executive Officer chairs this Committee which is composed of the Chief Technology and Services Officer together with the top management of the bank.

Statement of Compliance with the Code of Principles of Good Corporate Governance (continued)

Asset And Liability Management Committee (ALCO)

This Committee reviews the financial risks of the group in Malta and ensures their prudent management: interest rate risk, liquidity and funding risk, foreign exchange risk, capital solvency, market sector risk and country risk. Furthermore, ALCO monitors the external environment and measures the impact on profitability of factors such as interest rate volatility, market liquidity, exchange rate volatility, monetary and fiscal policies and competitor banks activity.

The Chief Executive Officer has primary responsibility for ensuring efficient development of asset and liability management. Membership consists of senior executives with responsibility for the following functions: corporate banking, retail banking, treasury, financial control, marketing, and credit. The ALCO, which is chaired by the Chief Executive Officer and deputised by the Chief Technology and Services Officer, meets once a month.

Credit Risk Management Committee

This committee reviews the credit risk management issues of the group in Malta. It meets on a monthly basis and is chaired by the Chief Executive Officer. Membership consists of senior executives with responsibility for the following functions: credit and risk management, corporate banking, retail banking, treasury, consumer finance and audit and compliance.

Group Risk Management Committee

This Committee reviews the operational risks of the group in Malta: the identification, measurement, monitoring and controlling operational business risks and determines and agrees strategies and policies to mitigate these risks.

This Committee which meets on a quarterly basis is chaired by the Chief Risk Officer and is composed of the Chief Technology and Services Officer, the Chief Risk Officer, the Head of Audit, Compliance and Legal, Head of Security and Fraud and by other Business and Functional Heads and Managing Directors of some of the Subsidiary Companies.

Principles 9 and 10: Relations With Shareholders And With The Market, and Institutional Shareholders

The bank maintains ongoing communication with its shareholders and the market on its strategy and performance in order to enhance trust and confidence in the bank. During the period under review the bank has issued various company announcements and media releases to explain ongoing corporate developments and material events and transactions which have taken place and their impact on the financial position of the bank.

The principal contact with shareholders takes place through the Annual General Meeting (further detail is provided under the section regarding General Meetings) and Extraordinary General Meetings when necessary. Furthermore, communication with shareholders takes place through the Annual Report and Accounts being sent to every shareholder, which are physically delivered to the shareholders and which can be accessed by shareholders through the bank's website, primarily the Investor Relations' section, and a specific periodical shareholder publication entitled "L-Azzjonist".

The bank also holds meetings for stockbrokers, financial intermediaries and the media to explain the salient features of the interim and annual financial results.

The bank maintains an open channel of communication with its shareholders through the Company Secretarial Office and through the Head of Communications.

The Chairman ensures that the views of shareholders are communicated to the Board as a whole. Moreover, the Chairman arranges for all Directors to attend the Annual General Meeting and for the Chairmen of the Audit Committee and the Remuneration Committee to be available to answer questions. The conduct of the meeting is conducive to valid discussion and appropriate decision making.

In terms of the bank's Articles of Association the Directors shall on the requisition of members of the company holding not less than one-tenth of the paid up share capital proceed duly to convene an Extraordinary General Meeting of the bank. Minority shareholders are not prohibited from formally presenting an issue to the Board of Directors.

Principle 11: Conflicts of Interests

Directors are aware that their primary responsibility is always to act in the interest of the bank and its shareholders as a whole irrespective of who appointed them to the Board. This entails that they avoid conflicts of interest at all times and that their personal interests never take precedence over those of the bank and its shareholders.

By virtue of the bank's Articles of Association a director is bound not to vote at a Board meeting on any contract or arrangement or any other proposal in which he has a material interest, either directly or indirectly.

On joining the Board and regularly thereafter, Directors are informed and reminded of their obligations on dealing in securities of the bank within the parameters of law and the Listing Rules. A proper procedure of reporting advance notices to the Chairman by a director who intends to deal in the bank's shares has been endorsed by the Board in line with the Principles, the Listing Rules and the internal code of dealing.

Principle 12: Corporate Sustainability

HSBC's Corporate Sustainability (CS) activities take place within the context of the Group wide strategy. In Malta the bank fulfils the Group's CS strategy primarily through the HSBC Malta Foundation.

This charitable Foundation is committed to investing in the local community and looks to bring about lasting benefit to society. It deals with issues that concern the public in general by supervising projects in relation to disadvantaged children, the environment and Malta's national heritage. These activities have a significant impact on a large majority of Maltese citizens which shows the bank's strong commitment towards social investment.

Non-Compliance with the Code

Principle 4 (Code Provision 4.2.7)

Code Provision 4.2.7. recommends "the development of a succession policy for the future composition of the Board of Directors and particularly the executive component thereof, for which the Chairman should hold key responsibility".

In view of the fact that appointment of Directors is a matter reserved exclusively to the bank's shareholders (except where the need arises to fill a casual vacancy) the bank does not consider it appropriate to adopt such a succession policy. However, as explained under Principle 6 the bank continues to pursue an active succession policy for senior executive positions, especially by seeking to post local senior staff members abroad within the Group in order to enhance their international banking experience.

Principle 8B (Nomination Committee)

The Memorandum of Association of the bank specifically regulates the appointment of Directors. The Board consists of not more than nine Directors who are appointed/elected by the shareholders. Unless appointed for a shorter or longer period but not exceeding three years, a Director shall hold office from the end of one Annual General Meeting to the end of the next. Every shareholder owning 11% of the ordinary share capital is entitled to appoint one Director for each 11% shareholding. The majority shareholder therefore has the right to appoint six Directors. Furthermore, any excess fractional shareholding not so utilised may be used to participate in the voting for the election of further Directors. Shareholders who own less than 11% of the ordinary share capital participate in the election of the remaining three Directors.

The largest single shareholder (subject to a minimum 33% holding of the ordinary issued share capital of the bank), is entitled to appoint a Chairman from amongst the Directors appointed or elected to the Board. Every poll for the election of Directors is overseen by the bank's external auditors.

Within this context, the Board does not deem it necessary to appoint a Nomination Committee.

Principle 9 (Code Provision 9.2)

This Code Provision recommends the bank to have in place a mechanism to resolve conflicts between minority shareholders and controlling shareholders. Although the bank does not have such mechanism in place there is ongoing open dialogue between the bank's senior management and the non-executives directors to ensure that no such conflicts arise.

Statement of Compliance with the Code of Principles of Good Corporate Governance (continued)

Internal Control

The Board is ultimately responsible for the bank's system of internal control and for reviewing its effectiveness. Such procedures are designed to manage rather than to eliminate the risk of failure, to achieve business objectives and can only provide reasonable and not absolute assurance against material error, losses or fraud.

The bank has delegated specific, clear and unequivocal authority to the Chief Executive Officer to manage activities of the bank within the limits set by it. Functional, operating and financial reporting standards are applicable within all entities of the HSBC Group. These are supplemented by operating standards set by the bank's management, as required.

Systems and procedures are in place in the bank to identify, control and to report on the major risks including credit, changes in the market prices of financial instruments, liquidity, operational error and fraud. Exposure to these risks is monitored by the Asset and Liability Management Committee, Credit Risk Management Committee and by the Group Risk Management Committee.

Comprehensive annual financial plans are prepared, reviewed and approved by the Board. Results are monitored and reports on progress compared with plan are prepared monthly. Financial accounting and reporting and certain management reporting standards have been established. Centralised functional control is exercised over all computer system developments and operations. Common systems are employed where possible for similar business processes.

Responsibilities for financial performance against plans and for capital expenditure, credit exposures and market risk exposures are delegated with limits to line management. In addition, functional management in the bank has been given the responsibility to implement HSBC policies, procedures and standards in the areas of finance; legal and regulatory compliance; internal audit; human resources; credit risk; market risk; operational risk; computer systems and operations; property management; and for certain HSBC Group business and product lines.

The Chief Risk Officer is responsible for the management of specific risks within the Bank including credit risk in the wholesale and retail portfolios, markets risk and operational risk. Risks are monitored via regular Risk Management Committees and through reporting to the Executive Committee and the Board.

The internal audit function monitors compliance with policies and standards and the effectiveness of internal control structures within the bank and its subsidiaries. The work of the internal audit function focuses on areas of greatest risk as determined by a risk management approach.

The bank's Compliance Department ensures that HSBC Bank Malta group and its employees maintain the highest standards of corporate conduct including compliance with all the local and international regulatory obligations and HSBC Group ethical standards and regulations.

Through the Audit Committee, the Board reviews the processes and procedures to ensure the effectiveness of the system of internal control of the bank and its subsidiaries, which are monitored by internal audit.

Listing Rule 5.97.5

The information required by this Listing rule is found in the Directors' Report on pages 14 to 17.

General Meetings

The General Meeting is the highest decision making body of the bank. A General Meeting is called by twenty-one days' notice and it is conducted in accordance with the Articles of Association of the bank.

The Annual General Meeting deals with what is termed as "ordinary business", namely the receiving or adoption of the annual financial statements, the declaration of a dividend, the appointment of the Board (which may or may not involve an election), the appointment of the external auditors and the grant of the authority to the Board to fix the external auditors' emoluments. Other business which may be transacted at a General Meeting will be dealt with as Special Business.

All shareholders registered in the shareholders' Register on the record date as defined in the Listing Rules, have the right to attend, participate and vote in the General Meeting. A shareholder or shareholders holding not less than 5% in nominal value of all the shares entitled to vote at the General Meeting may request the bank to include items on the agenda of a General Meeting and/or table draft resolutions for items included in the agenda of a general meeting. Such requests are to be received by the bank at least forty six days before the date set for the relative general meeting.

A shareholder who cannot participate in the General Meeting can appoint a proxy by written or electronic notification to the bank. Every shareholder represented in person or by proxy is entitled to ask questions which are pertinent and related to items on the agenda of the General Meeting and to have such questions answered by the Director or such persons as the Directors may delegate for that purpose.

Remuneration Report

1. Terms of Reference and Membership

The Remuneration Committee (the Committee) is primarily responsible to make recommendations on the reward policy, on fixed and variable pay and for ensuring their implementation.

The Committee's membership consists of an independent chairman and two independent non-executive Directors. During the period under review the Committee was composed of Mr Albert Mizzi as Chairman and Dr Philip Farrugia Randon and Mr Peter Paul Testaferrata Moroni Viani as members who are non-executive directors. Mr Sonny Portelli replaced Mr Albert Mizzi as Chairman of the Committee on 4 November 2011.

The Committee is authorised to obtain such legal, remuneration or other professional advice as it deems appropriate.

2. Meetings

Two meetings were held by the Committee during 2011 and attendance was as follows:

Mr Albert Mizzi (Chairman)	(1 out of 1)
Mr Saviour sive Sonny Portelli (Chairman)	(1 out of 1)
Dr Philip Farrugia Randon	(2 out of 2)
Mr Peter Paul Testaferrata Moroni Viani	(2 out of 2)

Mr Alan Richards, CEO and Mr Mark Sims, Head of HR were in attendance at the two meetings.

3. Activities

The Committee considered various matters including the following:-

- Total Variable Pay spend for Performance Year 2011
- Fixed and Variable Pay for Senior Management (i.e. Business Heads)
- Fixed and Variable Pay for Middle Management
- Fixed and Variable Pay for Junior Managers and Clerical employees
- Variable Pay for Global Markets
- Retention of key senior employees by devising appropriate remuneration packages
- Update on Collective Agreement negotiations

In determining remuneration levels for performance year 2011 the Committee applied HSBC Group's remuneration strategy and policy, taking into account the interests of the shareholders and the broader external context.

4. Remuneration Statement

4.1 Reward Policy

The reward policy which formalised the Bank's previous practice and policies was approved by the Board in the year under review. No changes to this policy are being envisaged during 2012.

The bank's reward policy was formulated in accordance with the Banking Rule BR/12, the Capital Requirements Directive and the Group's reward strategy. This strategy provides a reward framework and includes key elements such as:

- a. an assessment of reward with reference to clear and relevant objectives.
- b. a focus on total compensation (fixed pay, variable pay and the value of long term incentives) with variable pay (namely bonus and the value of long term incentives) differentiated by company and individual performance; and
- c. a total remuneration package (salary, bonus, long term incentive awards and other benefits) which is competitive in relation to comparable organisations in the local market.

The Committee considers the total variable pay spend relative to the bank's performance with the key driver being Profit before Tax. Other key measures are taken into account such as Efficiency Ratio, Cost Target, Revenue Target and Return on Risk Weighted Assets.

For clerical employees and junior managers fixed pay is determined by a Collective Agreement and awards are differentiated by individual performance and grade. The Committee considers the allocation of variable pay to this part of the workforce collectively taking account of company profitability and key measures mentioned above.

Senior and Middle Management are eligible for an annual fixed pay review and variable pay award. A Fixed pay pool is determined by the Committee based on a percentage of the total salary costs of the Senior and Middle Managers. The variable pay is also established by the Committee and determined by company and individual performance of the Senior and Middle Managers.

The determination of the variable pay spend for Global Markets takes account of the local performance of the function as well as the overall profitability of the Global Markets function across the world.

The Chief Executive Officer's reward package is also reviewed and approved by the HSBC Group Remuneration Committee.

4.2 Code Provision 8.A.5

Emoluments of Senior Executives

<i>Fixed Remuneration</i>	<i>Variable Remuneration</i>	<i>Share Options</i>	<i>Others</i>
€452,271	€201,932	€78,280	€267,452

Reference to 'Senior Executives' shall mean the Chief Executive Officer and the Chief Technology and Services Officer who are also executive Directors.

Emoluments of Directors

<i>Fixed Remuneration</i>	<i>Variable Remuneration</i>	<i>Share Options</i>	<i>Others</i>
€163,964	None	None	None

Details of Directors' fees for the financial year under review were as follows:

	€
Albert Mizzi	36,954
Saviour sive Sonny Portelli	37,537
Peter Paul Testaferrata Moroni Viani	26,842
Philip Farrugia Randon	28,007
James Dunbar Cousin	17,312
Charles John Farrugia	<u>17,312</u>
Total	<u>163,964</u>

Fees payable to Directors or Committee members who are not employees of the bank are set by reference to market practice, taking into account the time commitment and complexity of the work undertaken and relative fees paid throughout the HSBC Group.

The Directors' fees are approved in aggregate by the shareholders at the Annual General Meeting. Those Directors who are employed with the bank are not paid any fees for their directorship.

Directors' Responsibilities Statement

The Companies Act, 1995 requires the Directors of HSBC Bank Malta p.l.c. (the 'bank') to prepare financial statements for each financial period which give a true and fair view of the financial position of the bank and the group as at the end of the financial period and of the profit or loss of the bank and the group for that period in accordance with the requirements of International Financial Reporting Standards as adopted by the EU.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy, at any time, the financial position of the bank and the group and to enable them to ensure that the financial statements have been properly prepared in accordance with the provisions of the Companies Act, 1995 and the Banking Act, 1994.

The Directors are also responsible for safeguarding the assets of the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors, through oversight of management, are responsible to ensure that the bank establishes and maintains internal control to provide reasonable assurance with regard to reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.

Management is responsible, with oversight from the Directors, to establish a control environment and maintain policies and procedures to assist in achieving the objective of ensuring, as far as possible, the orderly and efficient conduct of the group's business. This responsibility includes establishing and maintaining controls pertaining to the bank's objective of preparing financial statements as required by the Companies Act, 1995 and managing risks that may give rise to material misstatements in those financial statements. In determining which controls to implement to prevent and detect fraud, management considers the risks that the financial statements may be materially misstated as a result of fraud.

Signed on behalf of the Board of Directors by:



Albert Mizzi, *Chairman*



Mark Watkinson, *Chief Executive Officer*

Income Statements for the year 1 January 2011 to 31 December 2011

	<i>Note</i>	<i>Group</i>		<i>Bank</i>	
		2011	2010	2011	2010
		€000	€000	€000	€000
Interest and similar income					
– on loans and advances, balances with Central Bank of Malta, Treasury Bills and other instruments	6	153,397	151,582	153,399	151,583
– on debt and other fixed income instruments	6	22,565	17,430	19,208	13,607
Interest expense	7	(46,703)	(46,170)	(47,053)	(46,813)
Net interest income		129,259	122,842	125,554	118,377
Fee and commission income		36,597	36,993	32,653	32,702
Fee and commission expense		(3,047)	(2,713)	(2,814)	(2,448)
Net fee and commission income	8	33,550	34,280	29,839	30,254
Dividend income	9	1	–	24,987	7,538
Trading profits	10	8,306	6,816	8,306	6,816
Net (expense)/income from insurance financial instruments designated at fair value	12	(6,455)	19,707	–	–
Net losses on sale of available-for-sale financial investments	11	(2,107)	(369)	(2,113)	(370)
Net earned insurance premiums	12	64,459	58,738	–	–
Net other operating income	12	23,575	5,162	10,057	1,061
Total operating income		250,588	247,176	196,630	163,676
Net insurance claims incurred and movement in policyholders' liabilities	12	(55,723)	(70,988)	–	–
Net operating income		194,865	176,188	196,630	163,676
Employee compensation and benefits	13	(58,807)	(50,723)	(55,910)	(48,380)
General and administrative expenses		(33,333)	(30,081)	(31,011)	(28,357)
Depreciation		(5,200)	(5,821)	(5,196)	(5,802)
Amortisation		(860)	(980)	(815)	(896)
Net operating income before impairment charges and provisions		96,665	88,583	103,698	80,241
Net impairment	14	(8,250)	(5,496)	(4,103)	(5,266)
Net provisions for liabilities and other charges		(110)	1	(96)	20
Profit before tax	15	88,305	83,088	99,499	74,995
Tax expense	16	(30,738)	(29,327)	(32,940)	(24,696)
Profit for the year		57,567	53,761	66,559	50,299
Profit attributable to shareholders		57,567	53,761	66,559	50,299
Earnings per share	17	19.7c	18.4c	22.8c	17.2c

The notes on pages 35 to 90 are an integral part of these financial statements.

Statements of Comprehensive Income for the year 1 January 2011 to 31 December 2011

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Profit attributable to shareholders	57,567	53,761	66,559	50,299
Other comprehensive income/(expense)				
Available-for-sale investments:				
– fair value gains	1,193	1,178	4,778	1,997
– fair value losses transferred to profit or loss on disposal	2,107	369	2,113	370
– amounts transferred to profit or loss on impairment	4,179	198	–	–
– income taxes	(2,580)	(610)	(2,374)	(828)
Properties:				
– revaluation	–	2,117	–	2,117
– income taxes	–	(89)	–	(89)
Other comprehensive income for the year, net of tax	4,899	3,163	4,517	3,567
Total comprehensive income for the year, net of tax	62,466	56,924	71,076	53,866

The notes on pages 35 to 90 are an integral part of these financial statements.

Statements of Financial Position at 31 December 2011

	Note	Group		Bank	
		2011	2010	2011	2010
		€000	€000	€000	€000
Assets					
Balances with Central Bank of Malta,					
Treasury Bills and cash	18	233,388	379,985	233,387	379,984
Cheques in course of collection		22,685	9,011	22,685	9,011
Derivatives	19	17,136	11,489	17,856	11,686
Financial assets designated at fair value	20	370,080	305,569	–	–
Financial investments	21	936,830	690,606	883,747	593,107
Loans and advances to banks	22	637,956	714,901	637,903	714,850
Loans and advances to customers	23	3,344,224	3,290,435	3,344,224	3,290,435
Shares in subsidiary companies	24	–	–	35,707	35,707
Intangible assets	25	89,011	70,655	12,497	7,583
Property, plant and equipment	26	60,113	65,487	60,195	65,580
Investment property	27	14,598	14,591	11,663	11,668
Non-current assets held for sale	28	12,978	9,674	12,978	9,674
Current tax assets		–	4,712	–	4,516
Deferred tax assets	33	14,005	10,181	13,744	9,902
Other assets	29	31,209	34,425	8,606	9,439
Prepayments and accrued income	30	40,629	38,710	35,527	34,256
Total assets		5,824,842	5,650,431	5,330,719	5,187,398
Liabilities					
Derivatives	19	17,810	12,311	17,810	12,313
Deposits by banks	31	389,170	232,790	389,170	232,790
Customer accounts	32	4,402,975	4,462,861	4,440,646	4,517,763
Current tax liabilities		4,134	2,603	3,198	953
Deferred tax liabilities	33	18,113	19,604	–	–
Liabilities to customers under investment contracts	34	16,920	18,962	–	–
Liabilities under insurance contracts issued	35	436,672	410,461	–	–
Other liabilities	36	38,145	33,024	33,925	29,321
Accruals and deferred income	37	35,979	34,287	35,152	33,310
Provisions for liabilities and other charges	38	11,251	2,548	11,031	2,511
Subordinated liabilities	39	87,208	87,150	87,933	87,880
Total liabilities		5,458,377	5,316,601	5,018,865	4,916,841
Equity					
Called up share capital	40	87,552	87,552	87,552	87,552
Revaluation reserve	41	32,872	28,674	32,099	28,283
Retained earnings	41	246,041	217,604	192,203	154,722
Total equity		366,465	333,830	311,854	270,557
Total liabilities and equity		5,824,842	5,650,431	5,330,719	5,187,398
Memorandum items					
Contingent liabilities	42	130,763	128,947	132,466	128,970
Commitments	43	1,084,509	977,718	1,084,509	977,718

The notes on pages 35 to 90 are an integral part of these financial statements.

The financial statements on pages 29 to 90 were approved and authorised for issue by the Board of Directors on 24 February 2012 and signed on its behalf by:


Albert Mizzi, Chairman


Mark Watkinson, Chief Executive Officer

Statements of Changes in Equity for the year 1 January 2011 to 31 December 2011

	<i>Note</i>	<i>Share capital</i> €000	<i>Revaluation reserve</i> €000	<i>Retained earnings</i> €000	<i>Total equity</i> €000
<i>Group</i>					
At 1 January 2011		<u>87,552</u>	<u>28,674</u>	<u>217,604</u>	<u>333,830</u>
Profit for the year		<u>–</u>	<u>–</u>	<u>57,567</u>	<u>57,567</u>
Other comprehensive income					
Available-for-sale investments:					
– fair value gains, net of tax		–	813	–	813
– fair value losses transferred to profit or loss on disposal, net of tax		–	1,370	–	1,370
– amounts transferred to profit or loss on impairment, net of tax		–	2,716	–	2,716
Properties:					
– release of revaluation reserve on disposal, net of tax		–	(701)	701	–
Total other comprehensive income		<u>–</u>	<u>4,198</u>	<u>701</u>	<u>4,899</u>
Total comprehensive income for the year		<u>–</u>	<u>4,198</u>	<u>58,268</u>	<u>62,466</u>
Transactions with owners, recorded directly in equity					
Contributions by and distributions to owners:					
– share-based payments		–	–	331	331
– dividends	45	–	–	(30,162)	(30,162)
Total contributions by and distributions to owners		<u>–</u>	<u>–</u>	<u>(29,831)</u>	<u>(29,831)</u>
At 31 December 2011		<u>87,552</u>	<u>32,872</u>	<u>246,041</u>	<u>366,465</u>
At 1 January 2010		<u>87,552</u>	<u>25,825</u>	<u>193,210</u>	<u>306,587</u>
Profit for the year		<u>–</u>	<u>–</u>	<u>53,761</u>	<u>53,761</u>
Other comprehensive income					
Available-for-sale investments:					
– fair value gains, net of tax		–	766	–	766
– fair value losses transferred to profit or loss on disposal, net of tax		–	240	–	240
– amounts transferred to profit or loss on impairment, net of tax		–	129	–	129
Properties:					
– release of revaluation reserve on disposal, net of tax		–	(314)	314	–
– revaluation of properties, net of tax		–	2,028	–	2,028
Total other comprehensive income		<u>–</u>	<u>2,849</u>	<u>314</u>	<u>3,163</u>
Total comprehensive income for the year		<u>–</u>	<u>2,849</u>	<u>54,075</u>	<u>56,924</u>
Transactions with owners, recorded directly in equity					
Contributions by and distributions to owners:					
– share-based payments		–	–	481	481
– dividends	45	–	–	(30,162)	(30,162)
Total contributions by and distributions to owners		<u>–</u>	<u>–</u>	<u>(29,681)</u>	<u>(29,681)</u>
At 31 December 2010		<u>87,552</u>	<u>28,674</u>	<u>217,604</u>	<u>333,830</u>

The notes on pages 35 to 90 are an integral part of these financial statements.

Statements of Changes in Equity for the year 1 January 2011 to 31 December 2011 (continued)

<i>Note</i>	<i>Share capital</i> €000	<i>Revaluation reserve</i> €000	<i>Retained earnings</i> €000	<i>Total equity</i> €000
<i>Bank</i>				
At 1 January 2011	<u>87,552</u>	<u>28,283</u>	<u>154,722</u>	<u>270,557</u>
Profit for the year	<u>–</u>	<u>–</u>	<u>66,559</u>	<u>66,559</u>
Other comprehensive income				
Available-for-sale investments:				
– fair value gains, net of tax	–	3,143	–	3,143
– fair value losses transferred to profit or loss on disposal, net of tax	–	1,374	–	1,374
Properties:				
– release of revaluation reserve on disposal, net of tax	–	(701)	701	–
Total other comprehensive income	<u>–</u>	<u>3,816</u>	<u>701</u>	<u>4,517</u>
Total comprehensive income for the year	<u>–</u>	<u>3,816</u>	<u>67,260</u>	<u>71,076</u>
Transactions with owners, recorded directly in equity				
Contributions by and distributions to owners:				
– share-based payments	–	–	383	383
– dividends	45	–	(30,162)	(30,162)
Total contributions by and distributions to owners	<u>–</u>	<u>–</u>	<u>(29,779)</u>	<u>(29,779)</u>
At 31 December 2011	<u>87,552</u>	<u>32,099</u>	<u>192,203</u>	<u>311,854</u>
At 1 January 2010	<u>87,552</u>	<u>25,030</u>	<u>133,814</u>	<u>246,396</u>
Profit for the year	<u>–</u>	<u>–</u>	<u>50,299</u>	<u>50,299</u>
Other comprehensive income				
Available-for-sale investments:				
– fair value gains, net of tax	–	1,298	–	1,298
– fair value losses transferred to profit or loss on disposal, net of tax	–	241	–	241
Properties:				
– release of revaluation reserve on disposal, net of tax	–	(314)	314	–
– revaluation of properties, net of tax	–	2,028	–	2,028
Total other comprehensive income	<u>–</u>	<u>3,253</u>	<u>314</u>	<u>3,567</u>
Total comprehensive income for the year	<u>–</u>	<u>3,253</u>	<u>50,613</u>	<u>53,866</u>
Transactions with owners, recorded directly in equity				
Contributions by and distributions to owners:				
– share-based payments	–	–	457	457
– dividends	45	–	(30,162)	(30,162)
Total contributions by and distributions to owners	<u>–</u>	<u>–</u>	<u>(29,705)</u>	<u>(29,705)</u>
At 31 December 2010	<u>87,552</u>	<u>28,283</u>	<u>154,722</u>	<u>270,557</u>

The notes on pages 35 to 90 are an integral part of these financial statements.

Statements of Cash Flows for the year 1 January 2011 to 31 December 2011

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
<i>Note</i>	€000	€000	€000	€000
Cash flows from/(used in) operating activities				
Interest, commission and premium receipts	266,521	254,711	196,076	187,992
Interest, commission and claims payments	(76,988)	(70,799)	(49,450)	(48,109)
Payments to employees and suppliers	(83,774)	(81,139)	(77,701)	(75,101)
Operating profit before changes in operating assets/liabilities	105,759	102,773	68,925	64,782
(Increase)/decrease in operating assets:				
Trading instruments	(76,592)	(43,064)	–	–
Reserve deposit with Central Bank of Malta	(956)	(8,335)	(956)	(8,335)
Loans and advances to customers and banks	(63,014)	(104,527)	(63,013)	(104,591)
Treasury Bills	167,308	(202,915)	170,555	(197,099)
Other receivables	(13,582)	(21,249)	(15,965)	3,173
(Decrease)/increase in operating liabilities:				
Customer accounts and deposits by banks	(59,710)	374,995	(76,971)	370,291
Other payables	3,212	32,313	7,325	7,573
Net cash from operating activities before tax	62,425	129,991	89,900	135,794
Tax paid	(32,653)	(26,840)	(25,597)	(25,183)
Net cash from operating activities	29,772	103,151	64,303	110,611
Cash flows from/(used in) investing activities				
Dividends received	785	281	17,950	6,650
Interest received from financial investments	34,624	25,575	24,403	16,036
Purchase of financial investments	(599,079)	(307,715)	(599,079)	(307,688)
Proceeds from sale and maturity of financial investments	344,079	94,246	302,557	94,246
Purchase of property, plant and equipment, investment property and intangible assets	(9,031)	(11,038)	(8,986)	(10,998)
Proceeds on sale of property, plant and equipment and intangible assets	2,094	453	2,094	412
Proceeds on disposal of card acquiring business	11,075	–	11,075	–
Net cash flows used in investing activities	(215,453)	(198,198)	(249,986)	(201,342)
Cash flows used in financing activities				
Dividends paid	(30,162)	(30,162)	(30,162)	(30,162)
Cash used in financing activities	(30,162)	(30,162)	(30,162)	(30,162)
Decrease in cash and cash equivalents	(215,843)	(125,209)	(215,845)	(120,893)
Effect of exchange rate changes on cash and cash equivalents	17,485	31,624	17,485	31,624
Net decrease in cash and cash equivalents	(233,328)	(156,833)	(233,330)	(152,517)
	(215,843)	(125,209)	(215,845)	(120,893)
Cash and cash equivalents at beginning of year	423,606	548,815	423,554	544,447
Cash and cash equivalents at end of year	46 207,763	423,606	207,709	423,554

The notes on pages 35 to 90 are an integral part of these financial statements.

Notes on the Financial Statements

1 Reporting entity

HSBC Bank Malta p.l.c. (the 'bank') is a limited liability company domiciled and incorporated in Malta.

The consolidated financial statements of the bank as at and for the year ended 31 December 2011 comprise the bank and its subsidiaries (together referred to as the 'group' and individually as 'group entities').

2 Basis of preparation

a *Statement of compliance*

These financial statements have been prepared and presented in accordance with International Financial Reporting Standards as adopted by the EU ('the applicable framework'). All references in these financial statements to IAS, IFRS or SIC/IFRIC interpretations refer to those adopted by the EU.

They have also been drawn up in accordance with the provisions of the Banking Act, 1994 and the Companies Act, 1995, enacted in Malta.

b *Basis of measurement*

Assets and liabilities are measured at historical cost except for certain intangible assets measured at the present value of in-force long-term insurance business, and the following that are measured at fair value:

- Derivatives;
- Financial instruments designated at fair value through profit or loss;
- Available-for-sale financial investments; and
- Property.

c *Functional and presentation currency*

The financial statements are presented in euro (€), which is the group's functional currency.

d *Use of estimates and assumptions*

The preparation of financial statements in conformity with IFRSs requires the use of estimates and assumptions about future conditions. The use of available information and application of judgement are inherent in the formation of estimates, actual results in the future may differ from those reported.

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 and in any future periods affected.

Information about significant areas of estimation, uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in notes 4, 25 and 53.

3 Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, and have been applied consistently by group entities.

a *Basis of consolidation*

i *Subsidiaries*

Subsidiaries are entities controlled by the bank. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

ii *Transactions eliminated on consolidation*

Intra-group balances and income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Notes on the Financial Statements (continued)

3 Significant accounting policies (continued)

b Financial instruments

i Non-derivative financial instruments

Non-derivative financial instruments are recognised on trade date when the group enters into contractual arrangements with counterparties. These financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below:

Cash and cash equivalents

Cash and cash equivalents comprise cash balances and deposits with contractual maturity of less than three months. Loans and advances to banks and Amounts owed to banks that are repayable on demand or have a contractual maturity of three months or less and which form an integral part of the group's cash management are included as a component of cash and cash equivalents for the purpose of the Statement of Cash Flows. Subsequent to initial recognition cash and cash equivalents are measured at amortised cost.

Trading assets and trading liabilities

Treasury Bills, debt securities, equity shares and short positions in securities are classified as held for trading if they have been acquired principally for the purpose of selling or repurchasing in the near term, or they form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. Subsequent to initial recognition, their fair values are remeasured, and all gains and losses from changes therein are recognised in profit or loss in Trading profits as they arise.

Financial instruments designated at fair value

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below, and are so designated by management. The group designates financial instruments at fair value when the designation:

- eliminates or significantly reduces valuation or recognition inconsistencies that would otherwise arise from measuring financial assets or financial liabilities, or recognising gains and losses on them, on different basis. Under this criterion, the only class of financial instruments designated by the group is financial assets and financial liabilities under investment contracts.

Liabilities to customers under linked contracts are determined based on the fair value of the assets held in the linked funds, with changes recognised in profit or loss. Liabilities to customers under other types of investment contracts would be measured at amortised cost. If no designation was made for the assets relating to the customer liabilities they would be classified as available-for-sale and the changes in fair value would be recorded directly in other comprehensive income. These financial instruments are managed on a fair value basis and management information is also prepared on this basis. Designation at fair value of the financial assets and liabilities under investment contracts allows the changes in fair values to be recorded in profit or loss and presented in the same line.

- applies to groups of financial assets, financial liabilities or combinations thereof that are managed, and their performance evaluated, on a fair value basis in accordance with a documented risk management or investment strategy, and where information about the groups of financial instruments is reported to management on that basis. Under this criterion certain financial assets held to meet liabilities under insurance contracts are the main class of financial instruments so designated. The group has documented risk management and investment strategies designed to manage such assets at fair value, taking into consideration the relationship of assets to liabilities in a way that mitigates market risks. Reports are provided to management on the fair value of the assets.

The fair value designation, once made, is irrevocable. Subsequent to initial recognition, the fair values are remeasured, and gains and losses from changes therein are recognised in Net income from insurance financial instruments designated at fair value through profit or loss.

3 Significant accounting policies (continued)

b Financial instruments (continued)

i Non-derivative financial instruments (continued)

Available-for-sale

Treasury Bills, debt securities and equity shares intended to be held on a continuing basis, other than those designated at fair value, are classified as available-for-sale.

Available-for-sale financial investments are subsequently remeasured at fair value, and changes therein are recognised in other comprehensive income until the financial assets are either sold or become impaired. When available-for-sale financial investments are sold, cumulative gains or losses previously recognised in other comprehensive income are recognised in profit or loss as Net (losses)/gains on sale of available-for-sale financial investments.

Loans and advances to banks and customers

Loans and advances to banks and customers are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and advances are recognised when the cash is advanced to the borrowers. They are subsequently measured at amortised cost using the effective interest method, less impairment losses.

ii Derivative financial instruments

Derivatives are recognised initially and are subsequently remeasured at fair value. Fair values of exchange traded derivatives are obtained from quoted market prices. Fair value of over-the-counter derivatives are obtained using valuation techniques, including discounted cash flow models and option pricing models. All derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative.

Derivatives may be embedded on other financial instruments. Embedded derivatives are treated as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host contract; the terms of the embedded derivative would meet the definition of a stand-alone derivative if they were contained in a separate contract; and the combined contract is not held for trading or designated at fair value. These embedded derivatives are measured at fair value with changes therein recognised in profit or loss.

The method of recognising fair value gains and losses depends on whether derivatives are held for trading or are designated as hedging instruments, and if the latter, the nature of the risks being hedged.

Derivatives that do not qualify for hedge accounting

All gains and losses from changes in the fair values of derivatives that do not qualify for hedge accounting are recognised immediately in profit or loss. These gains and losses are reported in Trading profits, except where derivatives are managed in conjunction with financial instruments designated at fair value in which case gains and losses are reported in Net income from insurance financial instruments designated at fair value through profit or loss.

Hedge accounting

When derivatives are designated as hedges, the bank classifies them as either:

- hedges of the change in fair value of recognised assets or liabilities or firm commitments ('fair value hedges'); or
- hedges of the variability in highly probable future cash flows attributable to a recognised asset or liability, or a forecast transaction ('cash flow hedges').

Hedge accounting is applied to derivatives designated as hedging instruments in a fair value or cash flow hedge provided certain criteria are met.

At the inception of a hedging relationship, the bank documents the relationship between the hedging instruments and the hedged items, its risk management objective and its strategy for undertaking the hedge. The bank also requires a documented assessment, both at hedge inception and on an ongoing basis, of whether or not the hedging instruments, primarily derivatives, that are used in hedging transactions are highly effective in offsetting the changes attributable to the hedging risks in the fair value of the hedged items. Interest on designated qualifying hedges is included in Net interest income.

Changes in the fair value of derivatives that are designated and qualify as fair value hedging instruments are recorded in profit or loss, along with changes in the fair value of the hedged items or group thereof that are attributable to the hedged risk.

Notes on the Financial Statements (continued)

3 Significant accounting policies (continued)

b Financial instruments (continued)

ii Derivative financial instruments (continued)

If a hedging relationship no longer meets the criteria for hedge accounting, the cumulative adjustment to the carrying amount of the hedged item is amortised to profit or loss based on a recalculated effective interest rate over the residual period to maturity, unless the hedged item has been derecognised, in which case, it is released to profit or loss immediately.

Hedge effectiveness testing

To qualify for hedge accounting, the bank requires that at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective (prospective effectiveness), and demonstrate actual effectiveness (retrospective effectiveness) on an ongoing basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method adopted by the group to assess hedge effectiveness will depend on its risk management strategy.

For prospective effectiveness, the hedging instrument must be expected to be highly effective in offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated. For actual effectiveness to be achieved, the changes in fair value or cash flows must offset each other in the range of 80.0 per cent to 125.0 per cent.

Hedge ineffectiveness is recognised in profit or loss in Trading profits.

iii Derecognition of financial assets and liabilities

Financial assets are derecognised when the right to receive cash flows from the assets has expired or when the group has transferred its contractual right to receive the cash flows of the financial assets, and either

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

Financial liabilities are derecognised when they are extinguished, that is when the obligation is discharged, cancelled or expires.

iv Offsetting financial assets and financial liabilities

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

v Repurchase transactions

The group enters into purchases of investments under agreement to resell substantially identical investments at a certain date in the future at a fixed price. Investments purchased subject to commitments to resell at future dates are not recognised. The amounts paid are recognised in loans and advances to either banks or customers. The receivables are shown as collateralised by the underlying security. Investments sold under repurchase agreements continue to be recognised in the statement of financial position and are measured in accordance with the accounting policy for either assets held for trading or available-for-sale as appropriate. The proceeds from sale of the investments are reported as liabilities to either banks or customers.

The difference between the sale and repurchase consideration is recognised using the effective interest method over the period of the transactions and is included in interest.

c Investment in subsidiaries

Investment in subsidiaries is shown in the separate statement of financial position at cost less any impairment losses. Dividend income is recognised in profit or loss on the date that the bank's right to receive payment is established.

d Intangible assets

Intangible assets include software and the present value of in-force long-term insurance business.

Software acquired by the group is initially measured at cost and subsequently stated net of accumulated amortisation and any impairment losses. Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in profit or loss as incurred.

3 Significant accounting policies (continued)

d Intangible assets (continued)

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful life of software, from the date it is available for use. The estimated useful life of software ranges between 3 – 5 years.

For the accounting policy governing the present value of in-force long-term insurance business see note 3i (iv).

e Property and equipment

i Owned assets

Property and equipment are initially measured at cost. Freehold and long leasehold properties are remeasured to fair value on the basis of their existing use. Revaluations are performed by a professionally qualified architect with sufficient regularity such that the carrying amount does not differ materially from that which would be determined using fair values at the reporting date. Any surpluses arising on revaluation are credited to a revaluation reserve, net of deferred tax. Any deficiencies resulting from decreases in value are deducted from this reserve to the extent that it is sufficient to absorb them, with any excess charged to profit or loss.

Items of property and equipment are stated net of accumulated depreciation and any impairment losses.

Gains and losses on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognised net in profit or loss within Net other operating income or expense. When revalued assets are sold, the amounts included in the revaluation surplus reserve are transferred to retained earnings.

ii Finance and operating leases

Leases in terms of which the group assumes substantially all the risks and rewards of ownership are classified as finance leases.

When the group is a lessee under finance leases, the leased assets are capitalised and included in Property and Equipment and the corresponding liability to the lessor is included in Other liabilities. A finance lease and its corresponding liability are recognised initially at the fair value of the asset or, if lower, the present value of the minimum lease payments. Finance charges payable are recognised in Net interest income over the period of the lease based on the interest rate implicit in the lease so as to give a constant rate of interest on the remaining balance of the liability.

All other leases are classified as operating leases. When the group is the lessee, leased assets are not recognised on the statement of financial position. Rentals payable and receivable under operating leases are accounted for on a straight-line basis over the periods of the leases and are included in General and administrative expenses and Net other operating income or expense respectively.

iii Subsequent costs

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

iv Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each component of an item of property and equipment. Land is not depreciated. The estimated useful lives for the current and comparative period are as follows:

- | | |
|--|--------------------|
| – long leaseholds, freehold buildings and improvements | 50 years |
| – short leaseholds and improvements to rented property | over term of lease |
| – equipment, furniture and fittings | 3 – 10 years |

Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

f Investment property

Property held for long-term rental yields or for capital appreciation or both that is not occupied by the group is classified as investment property.

Notes on the Financial Statements (continued)

3 Significant accounting policies (continued)

f Investment property (continued)

Investment properties are included in the statement of financial position at fair value with changes therein recognised in profit or loss in the period of change. Fair values are determined by professional valuers who apply recognised valuation techniques.

g Impairment

i Financial assets not at fair value through profit or loss

At each reporting date an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. An impairment loss in respect of an available-for-sale financial investment is calculated as the difference between the financial investment's acquisition cost (net of any principal repayments and amortisation) and the current fair value (less any previous impairment loss recognised in profit or loss).

All impairment losses are recognised in profit or loss. Any cumulative loss in respect of an available-for-sale financial investment recognised previously in equity is removed from other comprehensive income and transferred to profit or loss.

Losses for impaired loans are recognised promptly when there is objective evidence that impairment of a loan or portfolio of loans has occurred.

There are two basic methods of calculating impairment losses, those calculated on individual loans and those losses assessed on a collective basis. Impairment losses are recorded as charges to profit or loss. The carrying amount of impaired loans on the statement of financial position is reduced through the use of impairment allowances accounts. Losses expected as a result of future events, no matter how likely, are not recognised in profit or loss.

ii Calculation of recoverable amount

At each reporting date, the group assesses on a case-by-case basis whether there is any objective evidence that a loan is impaired. This procedure is applied to all accounts that are considered individually significant. In determining impairment losses on these loans, the following factors are considered:

- the group's aggregate exposure to the customer;
- the viability of the customer's business model and their capability to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
- the amount and timing of expected receipts and recoveries;
- the extent of other creditors' commitments ranking ahead of, or *pari passu* with, the group and the likelihood of other creditors continuing to support the customer;
- the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- the realisable value of security (or other credit risk mitigants) and likelihood of successful repossession; and
- the likely deduction of any costs involved in recovery of amounts outstanding.

Impairment losses are calculated by discounting the expected future cash flows of a loan at its original effective interest rate, and comparing the resultant present value with the loan's carrying amount.

Impairment is assessed on a collective basis in two circumstances:

- to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment; and
- for homogeneous groups of loans that are not considered individually significant.

Individually assessed loans for which no evidence of loss has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for the purpose of calculating an estimated collective loss. This reflects impairment losses incurred at the reporting date which will only be individually identified in the future.

The collective impairment allowance is determined after taking into account:

- historical loss experience in portfolios of similar risk characteristics (for example, by industry sector, loan grade or product);

3 Significant accounting policies (continued)

g Impairment (continued)

ii Calculation of recoverable amount (continued)

- the estimated period between impairment occurring and the loss being identified and evidenced by the establishment of an appropriate allowance against the loss on an individual loan; and
- management's experienced judgement as to whether the current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience.

The period between a loss occurring and its identification is identified by local management for each identified portfolio.

For homogeneous groups of loans that are not considered individually significant, two alternative methods are used to calculate allowances on a portfolio basis:

- When appropriate empirical information is available, the group utilises roll rate methodology. This methodology employs a statistical analysis of historical trends of delinquency and default to estimate the likelihood that loans will progress through the various stages of delinquency and ultimately prove irrecoverable. The estimated loss is the difference between the present value of expected future cash flows, discounted at the original effective interest rate of the portfolio, and the carrying amount of the portfolio. Current economic conditions are also evaluated when calculating the appropriate level of allowance required to cover inherent loss.
- In other cases, when the portfolio size is small or when information is insufficient or not sufficiently reliable to adopt a roll rate methodology, the group adopts a formulaic approach which allocates progressively higher percentage loss rates the longer a customer's loan is overdue. Loss rates are calculated from the discounted expected future cash flows from a portfolio.

In normal circumstances, historical experience provides the most objective and relevant information from which to assess inherent loss within each portfolio. In certain circumstances, historical loss experience provides less relevant information about the inherent loss in a given portfolio at the reporting date, for example, where there have been changes in economic, regulatory or behavioural conditions, such that the most recent trends in the portfolio risk factors are not fully reflected in the statistical models. In these circumstances, such risk factors are taken into account when calculating the appropriate level of impairment allowances by adjusting the impairment allowances derived solely from historical loss experience.

Roll rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

iii Non-financial assets

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

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

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists.

The recoverable amount of non-financial assets is the greater of their net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

iv Reversals of impairment

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised.

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the loan impairment allowance account accordingly. For financial assets measured at amortised cost and available-for-sale financial investments that are debt securities, the reversal is recognised in profit or loss. For available-for-sale financial investments that are equity securities, the reversal is recognised directly in other comprehensive income.

Notes on the Financial Statements (continued)

3 Significant accounting policies (continued)

g Impairment (continued)

iv Reversals of impairment (continued)

An impairment loss on non-financial assets is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

v Loan write-offs

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 realising the security have been received.

h Non-current assets held for sale

Non-current assets that are expected to be recovered primarily through sale rather than through continuing use are classified as held for sale. Immediately before classification as held for sale, the assets are remeasured in accordance with the group's accounting policies. Thereafter generally the assets are measured at the lower of their carrying amount and fair value less cost to sell. Impairment losses on initial classification as held for sale and subsequent gains or losses on remeasurement are recognised in profit or loss. Gains are not recognised in excess of any cumulative impairment loss.

i Insurance and investment contracts

Through its insurance subsidiary, the group issues contracts to customers that contain insurance risk, financial risk or a combination thereof. A contract under which the group accepts significant insurance risk from another party by agreeing to compensate that party on the occurrence of a specified uncertain future event, is classified as an insurance contract. An insurance contract may also transfer financial risk, but is accounted for as an insurance contract if the insurance risk is significant.

Insurance contracts are accounted for as follows:

i Premiums

Premiums for life insurance contracts are accounted for when receivable, except in unit-linked business where premiums are accounted for when liabilities are established.

Reinsurance premiums are accounted for in the same accounting period as the premiums for the direct insurance contracts to which they relate.

ii Claims and reinsurance recoveries

Gross insurance claims for life insurance contracts reflect the total cost of claims arising during the year, including claim handling costs and any policyholder bonuses allocated in anticipation of a bonus declaration. Claims arising during the year include maturities, surrenders and death claims. Maturity claims are recognised when due for payment. Surrenders are recognised when paid or at an earlier date on which, following notification, the policy ceases to be included within the calculation of the related insurance liabilities. Death claims are recognised when notified.

Reinsurance recoveries are accounted for in the same period as the related claims.

iii Liabilities under insurance contracts

Liabilities under non-linked life insurance contracts are calculated based on actuarial principles.

Liabilities under unit-linked life insurance contracts are at least equivalent to the surrender or transfer value which is calculated by reference to the value of the relevant underlying funds or indices.

A liability adequacy test is carried out on insurance liabilities to ensure that the carrying amount of the liabilities is sufficient in the light of current estimates of future cash flows. When performing the liability adequacy test, all contractual cash flows are discounted and compared against the carrying value of the liability. Where a shortfall is identified it is charged immediately to profit or loss.

3 Significant accounting policies (continued)

i Insurance and investment contracts (continued)

iv Present value of in-force long-term insurance business

The value placed on insurance contracts that are classified as long-term insurance business, and are in force at the reporting date is recognised as an asset.

The present value of in-force long-term insurance business is determined by discounting future cash flows expected to emerge from business currently in force, using appropriate assumptions in assessing factors such as future mortality, lapse rates and levels of expenses and a risk discount rate that reflects the risk premium attributable to the respective long-term insurance business. Movements in the present value of in-force long-term insurance business are included in Net other operating income on a gross of tax basis.

v Investment contracts

Investment contracts are those contracts where there is no significant insurance risk.

Customer liabilities under unit-linked investment contracts and the linked financial assets are designated at fair value through profit or loss, and the movements in fair value are recognised in profit or loss in Net income from insurance financial instruments designated at fair value through profit or loss.

Premiums receivable and amounts withdrawn are accounted for as increases/decreases in the liability recorded in respect of investment contracts.

Liabilities under unit-linked investment contracts are at least equivalent to the surrender or transfer value which is calculated by reference to the value of the relevant underlying funds or indices.

Investment management fees receivable are recognised in profit or loss over the period of the provision of the investment management services in Net fee and commission income.

The incremental costs directly related to the acquisition of new investment contracts or renewal of existing investment contracts are deferred and amortised over the period of the provision of the investment management services.

j Provisions

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

Restructuring

A provision for restructuring is recognised when the group has approved a detailed and formal restructuring plan and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

k Financial guarantee contracts

Financial guarantees are contracts that require the group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognised at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The financial guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment when a payment under the guarantee has become probable. Financial guarantees are included within customer accounts.

l Interest income and expense

Interest income and expense for all interest-bearing financial instruments except those classified as held for trading or designated at fair value through profit or loss are recognised in Interest receivable and Interest payable in profit or loss using the effective interest method. The effective interest method is a way of calculating the amortised cost of a financial asset or a financial liability (or groups of financial assets or financial liabilities) and of allocating the Interest receivable or Interest payable over the relevant period.

Notes on the Financial Statements (continued)

3 Significant accounting policies (continued)

l Interest income and expense (continued)

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

Interest on impaired financial assets is recognised using the original effective interest rate.

m Non-interest income

i Net fee and commission income

Fee income is recognised as follows:

- on the execution of a significant act when the significant act has been completed; and
- as the services are provided except where the fee is charged to cover the cost of a continuing service to, or risk borne for, the customer, or is interest in nature. In these cases, the fee is recognised on an appropriate basis over the relevant period.

Income which forms an integral part of the effective interest rate of a financial instrument is recognised as an adjustment to the effective interest rate and recorded in Net interest income.

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

ii Dividend income

Dividend income is recognised on the date the entity's right to receive income is established which in the case of quoted securities is usually the ex-dividend date.

iii Net income from insurance financial instruments designated at fair value

Net income from financial instruments designated at fair value includes:

- all gains and losses from changes in the fair value of financial assets and financial liabilities designated at fair value through profit or loss; and
- interest income and expense and dividend income arising on these financial instruments.

n Employee benefits

i Defined contribution plan

The group contributes towards the State pension defined contribution plan in accordance with local legislation and to which it has no commitment beyond the payment of fixed contributions. Obligations for contributions are recognised as an employee benefit in profit or loss in the periods during which services are rendered by employees.

ii Termination benefits

Termination benefits are recognised as an expense when the group is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised as an expense if the group has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably. If benefits are payable more than 12 months after the reporting date, then they are discounted to their present value.

iii Share-based payment transactions

Share-based payment arrangements in which the group receives goods or services as consideration for equity instruments in the ultimate parent company are accounted for as equity-settled share-based payment transactions.

The grant date fair value of share-based payment awards granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period that the employees unconditionally become entitled to the awards. The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

3 Significant accounting policies (continued)

o Foreign currencies

Transactions in foreign currencies are recorded in the functional currency at the spot rate of exchange prevailing on the date of transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the reporting date. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency using the rate of exchange at the date the fair value was determined. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences arising on retranslation are recognised in profit or loss except for differences arising on retranslation of available-for-sale equity instruments, which are recognised directly in equity.

p Income tax

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

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised for unused tax losses and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

q Operating segments

The group's operating segments are organised into three customer groups, Retail Banking and Wealth Management (RBWM), Commercial Banking (CMB) and Global Banking and Markets (GBM). The group's chief decision maker regularly reviews operating activity by customer group. The group's operating segments were determined to be customer groups because the chief decision maker uses information on customer group segments in order to make decisions about resource allocation and assessing performance assessment. The group's chief decision maker is the Executive committee.

Measurement of segment assets, liabilities, income and expenses is based on the group's accounting policies. Segment income and expenses include transfers between segments. Shared costs are included in segment on the basis of the actual recharges made.

r New standards and interpretations not adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2011, and have not been applied in preparing these financial statements. None of these is expected to have a significant effect on these financial statements.

4 Financial instruments and risk management

a Use of financial instruments

The nature of the group's core banking operations implies that financial instruments are extensively used in the course of its routine business. The group's financial instruments consist of primary instruments and include cash balances with banks, loans and advances to customers, securities and amounts due to banks and customers.

The group is exposed to a mixed blend of risks and hence operates a risk management strategy with the objective of controlling and minimising their impact on group financial performance and position.

The principal categories of risk are credit risk, market risk and liquidity risk. These categories of risk in relation to life insurance business are described in note 4(e) and excluded from group figures disclosed in notes 4(b) to 4(c).

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

b Credit risk

i Credit risk management

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. It arises principally from lending, trade finance and treasury business. It also arises when issuers of debt securities are downgraded and as a result the value of group's holdings of these assets fall. The group has standards, policies and procedures dedicated to control and monitor the risk arising from all such activities.

Within the overall framework of the group policy, the group has an established risk management process encompassing credit approvals, the control of exposures, credit policy direction to business units and the monitoring and reporting of exposures both on an individual and a portfolio basis which includes the management of adverse trends. Management is responsible for the quality of its credit portfolios and follows a credit process involving delegated approval authorities and credit procedures, the objective of which is to build and maintain risk assets of high quality. Regular reviews are undertaken to assess and evaluate levels of risk concentrations by market sector and product.

Special attention is paid to problem loans. Specialist units are established by the group to provide customers with support in order to help them avoid default wherever possible.

a Collateral and other credit enhancements

Collateral can be an important mitigant of credit risk. Nevertheless, it is group's policy to establish that loans are within the customer's capacity to repay rather than to over rely on security. In certain cases, depending on the customer's standing and the type of product, facilities may be unsecured.

The group is required to implement guidelines on the acceptability of specific classes of collateral or credit risk mitigation, and determine suitable valuation parameters. Such parameters are expected to be conservative, reviewed regularly and supported by empirical evidence. Security structures and legal covenants are required to be subject to regular review to ensure that they continue to fulfil their intended purpose and remain in line with local market practice.

At the reporting date the principal type of collateral held consisted of immovable properties. Collateral held as security for financial assets other than loans and advances is determined by the nature of the instrument. Financial investments are generally unsecured.

b Credit quality of loans and advances

Group's credit risk rating processes are designed to highlight exposures which require closer management attention because of their greater probability of default and potential loss. Risk ratings are reviewed regularly and amendments, where necessary, are implemented promptly. The credit quality of unimpaired loans is assessed by reference to the Group's standard credit rating system.

ii Credit exposure

The group's maximum exposure to credit risk on financial instruments, whether recognised or unrecognised, before taking account of any collateral held or other credit enhancements can be classified in the following categories:

- Recognised financial assets comprise Balances with Central Bank of Malta, Treasury Bills and cash, Cheques in course of collection, Financial assets at fair value through profit or loss, Financial investments, loans and advances and acceptances and endorsements. The maximum exposure of these financial assets to credit risk, equals their carrying amount.
- Financial guarantees granted. The maximum exposure to credit risk is the full amount that the group would have to pay if the guarantees are called upon.
- Loan commitments and other credit related commitments that are irrevocable over the life of the respective facilities. The maximum exposure to credit risk is the full amount of the committed facilities.

4 Financial instruments and risk management (continued)

b Credit risk (continued)

ii Credit exposure (continued)

Concentration of credit risk exists when a number of counterparties are engaged in similar activities, or operate in the same industry sector and so their ability to meet contractual obligations is similarly affected by certain conditions.

The following industry concentrations are considered significant for gross Loans and advances to customers:

	<u>2011</u>	<u>2010</u>
	€000	€000
<i>Group/Bank</i>		
Agriculture	4,500	4,834
Fishing	2,024	1,671
Mining and quarrying	2,100	3,283
Manufacturing	107,400	122,105
Electricity, gas and water supply	108,304	111,734
Water supply, sewerage waste management and remediation activities	31,117	30,667
Construction	420,473	434,219
Wholesale and retail trade; repairs	350,411	357,877
Transport, storage and communication	54,554	50,290
Accommodation and food service activities	157,123	153,303
Information and communication	80,649	77,766
Financial and insurance activities	75,079	63,575
Real estate activities	63,776	57,046
Professional, scientific and technical activities	26,201	37,948
Administrative and support service activities	18,175	16,730
Public administration and defence; compulsory social security	110,222	107,625
Education	1,769	1,578
Human health and social work activities	30,398	24,567
Arts, entertainment and recreation	2,675	3,525
Other services activities	6,483	6,065
Household and individuals	1,748,859	1,675,160
Gross loans and advances to customers	<u>3,402,292</u>	<u>3,341,568</u>

Debt securities and other bills by rating agency (S&P Rating Agency) designation:

	<i>Treasury</i>	<i>Debt</i>	<i>Total</i>
	<i>Bills</i>	<i>securities</i>	<i>Total</i>
	€000	€000	€000
<i>Group</i>			
At 31 December 2011			
AAA	–	266,652	266,652
AA- to AA+	–	11,918	11,918
A- to A+	97,804	592,045	689,849
Lower than A-	–	12,805	12,805
	<u>97,804</u>	<u>883,420</u>	<u>981,224</u>
At 31 December 2010			
AAA	20,707	138,242	158,949
AA- to AA+	–	11,797	11,797
A- to A+	244,193	406,166	650,359
Lower than A-	–	36,607	36,607
	<u>264,900</u>	<u>592,812</u>	<u>857,712</u>

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

b Credit risk (continued)

iii Credit quality of financial assets

The following tables provide a detailed analysis of the credit quality of the group's lending portfolio:

a Distribution of gross loans and advances by credit quality

	<i>Loans and advances to customers</i>	<i>Loans and advances to banks</i>	<i>Loans and advances to customers</i>	<i>Loans and advances to banks</i>
	2011	2011	2010	2010
	€000	€000	€000	€000
<i>Group/Bank</i>				
Gross loans and advances:				
– neither past due nor impaired	3,109,247	637,903	3,058,656	714,850
– past due but not impaired	119,136	–	163,893	–
– impaired	173,909	–	119,019	–
	<u>3,402,292</u>	<u>637,903</u>	<u>3,341,568</u>	<u>714,850</u>

Loans and advances to banks booked in subsidiary undertakings are neither past due nor impaired.

b Distribution of loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired at the reporting date can be assessed by reference to group's standard credit grading system. The following information is based on that system:

	<i>Loans and advances to customers</i>	<i>Loans and advances to banks</i>	<i>Loans and advances to customers</i>	<i>Loans and advances to banks</i>
	2011	2011	2010	2010
	€000	€000	€000	€000
<i>Group/Bank</i>				
Satisfactory risk	2,724,158	637,903	2,701,925	714,850
Watch list and special attention	243,156	–	194,375	–
Sub-standard but not impaired	141,933	–	162,356	–
	<u>3,109,247</u>	<u>637,903</u>	<u>3,058,656</u>	<u>714,850</u>

Loans and advances to banks booked in subsidiary undertakings are of satisfactory risk.

c Loans and advances which were past due but not impaired

The past due ageing analysis includes loans and advances less than 90 days past due amounting to €112,596,000 (2010: €132,973,000).

	<i>Loans and advances to customers</i>	
	2011	2010
	€000	€000
<i>Group/Bank</i>		
Past due up to 29 days	84,959	104,172
Past due 30 – 59 days	20,021	20,624
Past due 60 – 89 days	7,616	8,177
Past due 90 – 179 days	5,426	3,976
Past due over 180 days	1,114	26,944
	<u>119,136</u>	<u>163,893</u>

Renegotiated loans that would otherwise be past due or impaired totalled €130,701,000 (2010: €93,669,000).

4 Financial instruments and risk management (continued)

b Credit risk (continued)

iii Credit quality of financial assets (continued)

d Individually impaired gross loans by segment

	<i>Loans and advances to customers</i>	
	2011	2010
	€000	€000
<i>Group/Bank</i>		
Personal banking	43,092	28,369
Commercial and corporate	123,831	83,614
Other	6,986	7,036
	173,909	119,019

iv Movement in allowance accounts for loans and advances to customers

	<i>Individually assessed allowances</i>	<i>Collective allowances</i>	<i>Individually assessed allowances</i>	<i>Collective allowances</i>
	2011	2011	2010	2010
	€000	€000	€000	€000
<i>Group/Bank</i>				
Change in allowances for uncollectability:				
At 1 January	38,365	12,768	32,529	12,425
Additions	13,483	(168)	11,909	343
Reversals	(4,497)	–	(4,503)	–
Discount unwind	(1,883)	–	(1,570)	–
At 31 December	45,468	12,600	38,365	12,768

v Settlement risk

The group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to failure of a counterparty to honour its obligations to deliver cash, securities or other assets as contractually agreed.

For certain types of transactions the group mitigates this risk by conducting settlements through a settlement/clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations.

c Liquidity risk

Liquidity risk is the risk that the group does not have sufficient financial resources to meet its financial obligations when they fall due or will have to do so at excessive cost. This risk can arise from mismatches in timing of cash flows.

The objective of the group's liquidity and funding management is to ensure that all foreseeable funding commitments and deposit withdrawals can be met when due. It is the group's objective to maintain a diversified and stable funding base with the objective of enabling the group to respond quickly and smoothly to unforeseen liquidity requirements.

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

c Liquidity risk (continued)

The group's liquidity and funding management process includes:

- projecting cash flows by considering the level of liquid assets necessary in relation thereto;
- monitoring liquidity ratios against internal and regulatory requirements;
- maintaining a diverse range of funding sources with adequate back-up facilities;
- managing the concentration and profile of debt maturities;
- monitoring depositor concentration in order to avoid undue reliance on large individual depositors and ensure a satisfactory overall funding mix; and
- maintaining liquidity and funding contingency plans. These plans identify early indicators of stress conditions and describe actions to be taken in the event of difficulties arising from systematic or other crisis while minimising adverse long-term implications for the business.

Current accounts and savings deposits payable on demand or at short notice form a significant part of the group's funding. The group places considerable importance on maintaining the stability of these deposits.

Cash flows payable by the group under financial liabilities by remaining maturities

	<i>Due within 3 months</i>	<i>Due between 3 and 12 months</i>	<i>Due between 1 and 5 years</i>	<i>Due after 5 years</i>	<i>Gross nominal outflow</i>
	€000	€000	€000	€000	€000
<i>Group</i>					
At 31 December 2011					
Deposits by banks	395,588	984	17	–	396,589
Customer accounts	3,271,718	929,693	223,698	–	4,425,109
Subordinated liabilities	2,203	2,203	17,627	92,305	114,338
Other financial liabilities	35,388	377	170	–	35,935
	3,704,897	933,257	241,512	92,305	4,971,971
Loan commitments	799,372	78,999	188,816	–	1,067,187
At 31 December 2010					
Deposits by banks	231,866	788	70	368	233,092
Customer accounts	3,272,792	954,127	261,159	–	4,488,078
Subordinated liabilities	2,203	2,203	17,627	96,706	118,739
Other financial liabilities	42,388	425	475	–	43,288
	3,549,249	957,543	279,331	97,074	4,883,197
Loan commitments	695,953	9,843	123,681	132,834	962,311

Cash flows payable by the group under investment contracts and insurance contracts issued are disclosed in note 4e(iii).

Derivatives are assumed to be payable on demand and not by contractual maturity because trading liabilities are typically held for short periods of time.

4 Financial instruments and risk management (continued)

c Liquidity risk (continued)

	<i>Due within 3 months</i>	<i>Due between 3 and 12 months</i>	<i>Due between 1 and 5 years</i>	<i>Due after 5 years</i>	<i>Gross nominal outflow</i>
	€000	€000	€000	€000	€000
<i>Bank</i>					
At 31 December 2011					
Amounts owed to banks	395,588	984	17	–	396,589
Amounts owed to customers	3,302,597	936,762	223,698	–	4,463,057
Subordinated liabilities	2,224	2,224	17,795	93,114	115,357
Other financial liabilities	31,238	377	170	–	31,785
	<u>3,731,647</u>	<u>940,347</u>	<u>241,680</u>	<u>93,114</u>	<u>5,006,788</u>
Loan commitments	<u>799,372</u>	<u>78,899</u>	<u>188,816</u>	<u>–</u>	<u>1,067,187</u>
At 31 December 2010					
Amounts owed to banks	231,866	788	70	368	233,092
Amounts owed to customers	3,327,356	955,281	261,159	–	4,543,796
Subordinated liabilities	2,224	2,224	17,795	97,562	119,805
Other financial liabilities	38,685	425	475	–	39,585
	<u>3,600,131</u>	<u>958,718</u>	<u>279,499</u>	<u>97,930</u>	<u>4,936,278</u>
Loan commitments	<u>695,953</u>	<u>9,843</u>	<u>123,681</u>	<u>132,834</u>	<u>962,311</u>

The balances in the above tables do not agree directly to the amounts in the financial position as the tables incorporate all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments. Furthermore, loan commitments are not recognised on the Statements of Financial Position.

Assets available to meet these liabilities and to cover outstanding commitments, include balances with Central Bank of Malta, Treasury Bills and cash, cheques in course of collection, loans to banks and to customers, marketable debt securities.

The group would meet unexpected net cash outflows by accessing additional funding sources such as interbank lending, or by selling securities such as Treasury Bills or debt securities.

d Market risk

Market risk is the risk that movements in market risk factors, including foreign exchange rates, interest rates and market prices will reduce the group's income or the value of its portfolios.

The objective of the group's market risk management is to manage and control market risk exposures in order to optimise return on risk while maintaining a market profile consistent with the group's status as a premier provider of financial products and services.

The group manages market risk through risk limits approved by HSBC Holdings plc. Limits are set by product and risk type with market liquidity being a principal factor in determining the level of limits set.

The group's interest rate exposures comprise those originating in its treasury activities and those originating in other banking activities. The primary source of interest rate risk originating in other banking activities arises from the employment of non-interest liabilities, such as shareholders' equity and current accounts, as well as fixed rate loans and liabilities, other than those generated by treasury business. The group's Asset and liability management Committee (ALCO) assesses the interest rate risks which arise in the business. The primary objective of such interest rate risk management is to limit potential adverse effects of interest rate movements on Net interest income.

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

d Market risk (continued)

i Fair value and price verification control

Where certain financial instruments are measured at fair value, the valuation and the related price verification processes are subject to independent validations. The determination of fair values is therefore a significant element in the reporting of the group's global market activities.

Certain of the group's financial assets and liabilities are carried at cost or amortised cost and not at fair value.

a Investments – Equity and other non-fixed income instruments available-for-sale

Certain unlisted equity investments are carried at cost and amount to €354,000 (2010: €354,000). There is no market for these investments and no recent transactions that provide evidence of the current fair value. Discounted cash flow techniques do not provide a reliable measure of the fair value of these investments.

b Loans and advances to banks and customers

This category of asset is reported net of impairment allowances to reflect the estimated recoverable amounts. As at 31 December 2011 the group's carrying amount was €3,982,180,000 (2010: €4,005,336,000), and the bank's carrying amount was €3,982,127,000 (2010: €4,005,285,000)

The loans and advances to customers category of asset amounts to €3,344,224,000 (2010: €3,290,435,000). This carrying value approximates to fair value in the case of loans which are repriced at the group's discretion. These loans constitute a significant element of the total loan portfolio.

The loans and advances to banks category of asset amounts to €637,956,000 (2010: €714,901,000) for the group and €637,903,000 (2010: €714,850,000) for the bank. For loans and advances to banks within the 'less than one year' maturity band, fair value is taken to be the amount carried at the reporting date. As at 31 December 2011, 86% of loans and advances to banks had a contractual repricing within the 'less than three months' band. Interest rates on these loans and advances reflect current market rates, and therefore the carrying amount approximates to fair value.

c Non-current assets held for sale

Assets acquired in satisfaction of debt amounting to €11,108,000 as at 31 December 2011 (2010: €7,662,000) consist mainly of repossessed immovable property measured at the lower of cost and their forced-sale value.

d Amounts owed to banks and customers

This category of liability is carried at amortised cost and as at 31 December 2011 amounts to €4,792,145,000 (2010: €4,695,651,000) for the group and €4,829,816,000 (2010: €4,750,553,000) for the bank. Of this liability, 65% has contractual repricing with the 'less than three months' band, 10% reprices within the 'between three months and one year' band whilst 25% reprices within the 'between one year and five years' band. For demand deposits and deposits maturing within one year, fair value is taken to be the amount payable on demand at the reporting date.

e Subordinated liabilities

This category of liability is carried at amortised cost. Fair value based on quoted market prices at the reporting date without deduction for transaction costs amounts to €90,788,000 as at 31 December 2011 (2010: €91,631,000).

4 Financial instruments and risk management (continued)

d Market risk (continued)

ii Basis of valuing financial assets and liabilities measured at fair value

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, HSBC will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable.

	<i>Valuation techniques</i>			Total
	<i>Quoted market price</i>	<i>Using observable inputs</i>	<i>With significant unobservable inputs</i>	
	Level 1	Level 2	Level 3	
	€000	€000	€000	
<i>Group</i>				
At 31 December 2011				
Assets				
Derivatives	–	17,136	–	17,136
Financial assets designated at fair value	370,080	–	–	370,080
Financial investments: available-for-sale	936,461	369	–	936,830
Liabilities				
Derivatives	–	17,810	–	17,810
Liabilities to customers under investment contracts	16,920	–	–	16,920
At 31 December 2010				
Assets				
Derivatives	–	11,489	–	11,489
Financial assets designated at fair value	305,569	–	–	305,569
Financial investments: available-for-sale	690,239	367	–	690,606
Liabilities				
Derivatives	–	12,311	–	12,311
Liabilities to customers under investment contracts	18,962	–	–	18,962

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

d Market risk (continued)

ii Basis of valuing financial assets and liabilities measured at fair value (continued)

	<i>Valuation techniques</i>			Total
	<i>Quoted</i>	<i>Using</i>	<i>With</i>	
	<i>market</i>	<i>observable</i>	<i>significant</i>	
	<i>price</i>	<i>inputs</i>	<i>unobservable</i>	
Level 1	Level 2	Level 3		
€000	€000	€000	€000	
<i>Bank</i>				
At 31 December 2011				
Assets				
Derivatives	–	17,856	–	17,856
Financial investments: available-for-sale	883,378	369	–	883,747
Liabilities				
Derivatives	–	17,810	–	17,810
At 31 December 2010				
Assets				
Derivatives	–	11,686	–	11,686
Financial investments: available-for-sale	592,740	367	–	593,107
Liabilities				
Derivatives	–	12,313	–	12,313

iii Credit risk adjustment methodology

The group adopts a credit risk adjustment against over the counter derivative transactions to reflect within fair value the possibility that the counterparty may default, and it may not receive the full market value of the transactions.

The group calculates the credit risk adjustment by applying the probability of default of the counterparty to the expected positive exposure to the counterparty, and multiplying the result by the loss expected in the event of default. The calculation is performed over the life of the potential exposure.

For most products, the group uses a simulation methodology to calculate the expected positive exposure. The methodology simulates the range of potential exposures of the group to the counterparty over the life of an instrument. The range of exposures is calculated across the portfolio of transactions with a counterparty to arrive at an expected overall exposure. The probability of default assumptions are based upon historic rating transition matrices. The credit rating used for a particular counterparty is that determined by the bank's internal credit process. Rating transition is taken account of throughout the duration of the exposure. A standard loss given default assumption is generally adopted. The Group considers that an appropriate spread to reflect its own probability of default within the credit risk adjustment calculation is currently zero. Consequently, HSBC does not derive the adjustment on a bilateral basis and has a zero adjustment against derivative liabilities, often referred to as a 'debit valuation adjustment'. The simulation methodology includes credit mitigants such as counterparty netting agreements and collateral agreements with the counterparty.

4 Financial instruments and risk management (continued)

d Market risk (continued)

iv Value at risk (VAR)

One of the principal tools used by the group to monitor and limit market risk exposure is VAR. VAR is a technique that estimates potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence.

The VAR models used by the group are predominantly based on historical simulation. The historical simulation models derive plausible future scenarios from historical market rate time series, taking account of inter-relationships between different markets and rates, for example, between interest rates and foreign exchange rates.

The historical simulation models used by the group incorporate the following features:

- potential market movements are calculated with reference to data from the last two years;
- historical market rates and prices are calculated with reference to foreign exchange rates and commodity prices, interest rates, equity prices and the associated volatilities;
- VAR is calculated to a 99.0 per cent confidence level; and
- VAR is calculated for a one-day holding period.

Although a valuable guide to risk, VAR should always be viewed in the context of its limitations, for example:

- the use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- the use of a one-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a one-day holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99.0 per cent confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and
- VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

The group recognises these limitations by augmenting its VAR limits with other position and sensitivity limit structures.

The VAR for the group was as follows:

	2011	2010
	€000	€000
At 31 December	2,367	1,074
Average	1,827	1,082
Minimum	1,056	825
Maximum	2,480	1,610

The major cause of the increase in VAR as at 31 December 2011 in comparison with 31 December 2010 was an increase in the investment portfolio as part of the asset and liability management strategy.

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

d Market risk (continued)

v Sensitivity of net interest income

A principal part of HSBC's management of market risk is to monitor the sensitivity of projected net interest income under varying interest rate scenarios (simulation modelling). For simulation modelling, business use a combination of scenarios relevant to local businesses and local markets and standard scenarios which are required throughout HSBC.

The table below sets out the impact on future net income/net assets of an incremental 50 basis points parallel fall or rise in all yield curves worldwide on the first day of the following year based on current balance sheet position/risk profiles:

	<i>Impact on profit for the year</i>	<i>Impact on net assets</i>	<i>Impact on profit for the year</i>	<i>Impact on net assets</i>
	<u>2011</u>	<u>2011</u>	2010	2010
	€000	€000	€000	€000
<i>Group/Bank</i>				
+ 50 basis points	4,373	(5,847)	5,315	(1,133)
- 50 basis points	(10,613)	(393)	(11,939)	(5,491)

vi Currency concentration

	<i>Reporting currencies</i>	<i>Other currencies</i>	<i>Total</i>	<i>Reporting currencies</i>	<i>Other currencies</i>	<i>Total</i>
	<u>2011</u>	<u>2011</u>	<u>2011</u>	2010	2010	2010
	€000	€000	€000	€000	€000	€000
<i>Group</i>						
Assets						
Balances with Central Bank of Malta, Treasury Bills and cash	230,989	2,399	233,388	373,863	6,122	379,985
Cheques in course of collection	22,078	607	22,685	8,709	302	9,011
Derivatives	12,359	4,777	17,136	10,546	943	11,489
Financial assets designated at fair value	298,900	71,180	370,080	223,840	81,729	305,569
Financial investments	820,608	116,222	936,830	671,883	18,723	690,606
Loans and advances to banks	67,120	570,836	637,956	48,200	666,701	714,901
Loans and advances to customers	3,305,068	39,156	3,344,224	3,248,210	42,225	3,290,435
Other assets	261,649	894	262,543	246,337	2,098	248,435
Total assets	5,018,771	806,071	5,824,842	4,831,588	818,843	5,650,431

4 Financial instruments and risk management (continued)

d Market risk (continued)

vi Currency concentration (continued)

	<i>Reporting</i>	<i>Other</i>	<i>Total</i>	<i>Reporting</i>	<i>Other</i>	<i>Total</i>
	<i>currencies</i>	<i>currencies</i>		<i>currencies</i>	<i>currencies</i>	
	2011	2011		2010	2010	
	€000	€000	€000	€000	€000	€000
<i>Group</i>						
Liabilities and equity						
Derivatives	13,539	4,271	17,810	10,880	1,431	12,311
Deposits by banks	374,097	15,073	389,170	208,849	23,941	232,790
Customer accounts	3,691,786	711,189	4,402,975	3,767,559	695,302	4,462,861
Liabilities to customers						
under investment contracts	16,920	–	16,920	18,962	–	18,962
Liabilities under insurance						
contracts issued	436,672	–	436,672	410,461	–	410,461
Subordinated liabilities	87,208	–	87,208	87,150	–	87,150
Other liabilities	103,695	3,927	107,622	87,174	4,892	92,066
Total equity	366,465	–	366,465	333,830	–	333,830
Total liabilities and equity	5,090,382	734,460	5,824,842	4,924,865	725,566	5,650,431
	<i>Reporting</i>	<i>Other</i>		<i>Reporting</i>	<i>Other</i>	
	<i>currencies</i>	<i>currencies</i>	<i>Total</i>	<i>currencies</i>	<i>currencies</i>	<i>Total</i>
	2011	2011	2011	2010	2010	2010
	€000	€000	€000	€000	€000	€000
<i>Bank</i>						
Assets						
Balances with Central Bank of Malta,						
Treasury Bills and cash	230,988	2,399	233,387	373,862	6,122	379,984
Cheques in course of collection	22,078	607	22,685	8,709	302	9,011
Derivatives	13,079	4,777	17,856	10,546	1,140	11,686
Financial investments	768,749	114,998	883,747	575,662	17,445	593,107
Loans and advances to banks	67,067	570,836	637,903	48,149	666,701	714,850
Loans and advances to customers	3,305,068	39,156	3,344,224	3,248,210	42,225	3,290,435
Other assets	190,023	894	190,917	186,426	1,899	188,325
Total assets	4,597,052	733,667	5,330,719	4,451,564	735,834	5,187,398
Liabilities and equity						
Derivatives	13,539	4,271	17,810	10,880	1,433	12,313
Deposits by banks	374,097	15,073	389,170	208,849	23,941	232,790
Customer accounts	3,729,457	711,189	4,440,646	3,820,998	696,765	4,517,763
Subordinated liabilities	87,933	–	87,933	87,880	–	87,880
Other liabilities	79,428	3,878	83,306	61,203	4,892	66,095
Total equity	311,854	–	311,854	270,557	–	270,557
Total liabilities and equity	4,596,308	734,411	5,330,719	4,460,367	727,031	5,187,398

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

e Insurance risk

The insurance risk of the group represents that faced by the life insurance subsidiary company. The principal insurance risk is that the cost of claims combined with acquisition and administration costs may exceed the aggregate amount of premiums received and investment income. The group manages its insurance risks through the application of formal underwriting, reinsurance and claims procedures designed to ensure compliance with regulations.

The following table provides an analysis of the insurance risk exposures by type of business:

	<i>Group</i>	
	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>
Life insurance (non-linked)		
Insurance contracts with discretionary participation feature	317,835	285,546
Term assurance and other long-term contracts	2,276	12,569
Total non-linked	<u>320,111</u>	298,115
Life insurance (linked)	<u>116,561</u>	112,346
Liabilities under insurance contracts issued	436,672	410,461
Investment contracts	<u>16,920</u>	18,962
Total insurance liabilities	<u>453,592</u>	<u>429,423</u>

Present value of in-force long-term insurance business (PVIF)

The HSBC life insurance business is accounted for using the embedded value approach, which, inter alia, provides a comprehensive framework for the evaluation of insurance and related risks.

The following table shows the effect on the PVIF of reasonably possible changes in the main economic assumptions across the life insurance business:

		<i>PVIF Impact</i>	
		<u>2011</u>	<u>2010</u>
		<u>€000</u>	<u>€000</u>
Assumptions	Movement		
As published			
Risk free rate	+100 basis points	1,951	4,341
Risk free rate	-100 basis points	(3,420)	(1,076)
Expenses inflation	+100 basis points	(436)	(245)
Expenses inflation	-100 basis points	487	271
Lapse rate	+100 basis points	(852)	(826)
Lapse rate	-100 basis points	766	860

HSBC's life insurance business is exposed to a range of financial risks, including market risk, credit risk and liquidity risk. The nature and management of these risks is described below.

i Market risk

a Interest rate risk

Life insurance business is exposed to interest rate risk when there is a mismatch in terms of duration or yields between assets and liabilities. The group manages the interest rate risk arising from its insurance underwriting business by establishing limits centrally. These govern the sensitivity of the net present values of expected future cash flows.

Interest rate risk is also assessed by measuring the impact of defined movements in interest yield curves on the profits after tax and net assets of the insurance underwriting business.

4 Financial instruments and risk management (continued)

e Insurance risk (continued)

i Market risk (continued)

b Equity risk

The group manages the equity risk arising from its holdings of equity securities centrally by setting limits on the maximum market value of equities that the insurance underwriting business may hold. Equity risk is also monitored by estimating the effect of predetermined movements in equity prices on the profit for the year and total net assets of the insurance underwriting business.

An immediate and permanent movement in interest yield curves as at the reporting date would have the following impact on the profit for the year and net assets at that date:

	2011		2010	
	<i>Impact on profit for the year</i>	<i>Impact on net assets</i>	<i>Impact on profit for the year</i>	<i>Impact on net assets</i>
	€000	€000	€000	€000
+100 basis points shift in yield curves	(2,342)	(2,342)	(642)	(642)
- 100 basis points shift in yield curves	1,047	1,047	(817)	(817)
+10 per cent increase in equity prices	614	614	182	182
- 10 per cent increase in equity prices	(742)	(742)	(719)	(719)

ii Credit risk

HSBC's life insurance underwriting business is exposed to credit risk in respect of its investment portfolios and reinsurance transactions. The Investment Committee is responsible for the quality and performance of the investment portfolios and follows a credit process involving delegated approval authorities and credit procedures, the objective of which is to build and maintain risk assets of high quality.

The following table presents the analysis of debt securities within insurance business by rating agency (S & P Rating Agency):

	<i>Treasury Bills</i>	<i>Debt securities</i>	<i>Total</i>
	€000	€000	€000
At 31 December 2011			
AAA	–	65,914	65,914
AA- to AA+	–	41,978	41,978
A- to A+	3,248	130,417	133,665
Lower than A-	–	12,799	12,799
Unrated	–	13,958	13,958
	3,248	265,066	268,314
At 31 December 2010			
AAA	–	37,085	37,085
AA- to AA+	–	30,871	30,871
A- to A+	7,460	129,818	137,278
Lower than A-	–	19,373	19,373
Unrated	–	13,508	13,508
	7,460	230,655	238,115

Notes on the Financial Statements (continued)

4 Financial instruments and risk management (continued)

e Insurance risk (continued)

iii Liquidity risk

It is an inherent characteristic of almost all insurance contracts that there is uncertainty over the amount and the timing of settlement of claims liabilities that may arise, and this leads to liquidity risk. As part of the management of this exposure, estimates are prepared for most lines of life insurance business of cash flows expected to arise from insurance funds at the reporting date.

The following table shows the expected maturity of insurance liabilities at the reporting date:

	<i>Due within 3 months</i>	<i>Due between 3 and 12 months</i>	<i>Due between 1 and 5 years</i>	<i>Due after 5 years</i>	<i>Gross nominal outflow</i>
	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>
At 31 December 2011					
Liabilities to customers under investment contracts	143	374	3,183	25,717	29,417
Liabilities under insurance contracts issued	12,123	25,788	81,757	510,457	630,125
At 31 December 2010					
Liabilities to customers under investment contracts	470	145	1,765	16,582	18,962
Liabilities under insurance contracts issued	2,203	7,173	81,559	306,957	397,892

With effect from 2011, the company has changed the methodology for estimating liquidity risk. The key changes are:

- Linked Insurance Reserves are derived via undiscounted cash flows on a statutory basis. No future premiums are assumed and investment returns are not included in the provisions. All decrements are considered.
- Linked Investment Reserves are as above but only consider contractual maturities and no other form of decrement.
- Non-Linked Reserve are derived via undiscounted statutory reserves run-off on a reporting basis. All future premiums are considered and provisions based on all expected decrements. Timing of cash flows are based on the expected run-off of the reserve.

5 Capital management and allocation

HSBC's capital management approach is driven by its strategy taking into account the regulatory, economic and commercial environment in which it operates. HSBC's capital management policy is to maintain a strong capital base to support the development of its business and to meet regulatory capital requirements at all times.

Capital management policy is monitored by ALCO. An annual group capital plan is drawn up and approved by the Board with the objective of maintaining both the optimal amount of capital and the mix between the different components of capital. The group recognises the impact on shareholder returns by the level of equity capital employed and seeks to maintain a prudent balance between the advantages and flexibility afforded by a strong capital position and the higher returns on equity from increased leverage.

In implementing the EU's directives which regulate capital requirements, the Malta Financial Services Authority (MFSA) supervises the group on a consolidated basis and the bank on a solo basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, the group and the bank.

The group's capital base is divided in two tiers, as defined in BR/03 (the Own Funds of Credit Institutions Authorised Under the Banking Act 1994):

- Original own funds comprise share capital, retained earnings and reserves created by appropriations of retained earnings. The book values of intangible assets, 50% of investment in HSBC Life Assurance (Malta) Ltd and final dividend are deducted in arriving at original own funds calculation. Depositor compensation scheme reserve is excluded from original own funds.

5 Capital management and allocation *(continued)*

- Additional own funds comprise qualifying subordinated loan capital, collective impairment allowances, and unrealised gains arising on the fair valuation of financial investments held as available-for-sale. Additional own funds also include reserves arising from the revaluation of properties. The remaining 50% of the book value of the investment in HSBC Life Assurance (Malta) Ltd is deducted in arriving at additional own funds calculation.

The group's risk and capital management policy is based on the Basel II framework which is structured on three pillars. These have been adopted by the MFSA by way of banking rules as follows:

- Pillar 1 – BR/04 (Capital Requirements of Credit Institutions Authorised Under the Banking Act 1994) defines the minimum capital resources requirements for credit, counterparty, market and operational risks. The risk is expressed in Risk Weighted Assets (RWAs) terms. The group has adopted the Standardised Approach in determining the material risks on its banking operations and operational risk.

Banking operations are categorised as either trading book or banking book and risk-weighted assets are determined accordingly. Banking book risk-weighted assets are measured by means of a hierarchy of risk weightings classified according to the nature of each asset and counterparty, taking into account any eligible collateral or guarantees. Banking book contingent liabilities and commitments giving rise to credit, foreign exchange or interest rate risk are assigned weights appropriate to the category of the counterparty, taking into account any eligible collateral or guarantees. Trading book risk-weighted assets are determined by taking into account market related risks such as foreign exchange, interest rate and equity position risks and counterparty risk.

- Pillar 2 – BR/12 (The Supervisory Review Process of Credit Institutions Authorised Under the Banking Act 1994) involves both the credit institution and the regulator in assessing whether the institution should hold additional capital against risks not covered under pillar 1. An integral part of pillar 2 is the Internal Capital Adequacy Assessment Process (ICAAP) which is the institutions's self-assessment of the levels of capital it needs to hold. An ICAAP was undertaken during the first half of the year. This document was approved by ALCO, EXCO and subsequently by the Board on 29 July 2011 and presented to the MFSA for review. The ICAAP is performed annually and is based upon a pillar 1 plus approach whereby the pillar 1 capital requirements for credit and operational risks are supplemented by an assessment of other material risks not fully addressed under pillar 1. The risks considered for ICAAP include concentration, liquidity, reputational and strategic risks, interest rate risk in the banking book and risks arising from the macroeconomic environment. The group assesses credit risk by utilising the embedded operational infrastructure for the pillar 1 capital calculation together with an additional suite of models that take into account the internal assessment of diversification of risks, within our portfolios and similarly, any concentrations of risk that arise. The bank maintains a prudence stance of capital coverage, ensuring that any model risk is mitigated. Interest rate risk in the Banking book (IRRBB) is defined as the exposure of non-trading products to interest rates. IRRBB economic capital is measured as the amount of capital necessary to cover an unexpected loss in the value of our non-trading products over one year to a 99.0% level of confidence.

Following the ICAAP submission, the regulator carries out the Supervisory Review Evaluation Process (SREP) and enters into discussion with the bank on the appropriate level of capital adequacy to cover pillar 2 risks. These discussions are ongoing.

- *Stress and scenario testing*

Stress testing forms part of the group's risk and capital framework and is an integral component of ICAAP. As a key risk management tool, stress testing highlights to senior management potential adverse unexpected outcomes related to a mixture of risks and provides an indication of how much capital might be required to absorb losses, should adverse scenarios occur. Stress testing is used to assess risk concentrations, estimate the impact of stressed earnings, impairments and write-downs on the overall capital adequacy under a variety of adverse scenarios.

Macroeconomic stress testing considers the impact on both earnings and capital for a range of scenarios. It entails multi-year systemic shocks to assess the group's ability to meet its capital requirements and liabilities as they fall due under a downturn in the business cycle and/or macroeconomic environment.

The principal business benefits of the stress testing framework include: understanding the impact of recessionary scenarios; assessing material risk concentrations; and forecasting the impact of market stress and scenarios on the group's balance sheet liquidity.

At group level, a series of stress events are monitored on a regular basis to assess the potential impact of an extreme yet plausible event on the group. As a result, senior management are continuously enhancing internal controls to monitor the situation on an ongoing basis. In an adverse scenario, the group also has at its disposal a range of mitigating actions it can use. The latter also form part of the ICAAP document.

5 Capital management and allocation (continued)

	<i>Group</i>	<i>Bank</i>
	2011	2011
	€000	€000
Total own funds		
Tier 1		
Called up share capital	87,552	87,552
Retained earnings	186,647	188,835
Exclusions/deductions:		
– Depositor compensation scheme reserve	(22,871)	(22,871)
– Investment in HSBC Life Assurance (Malta) Ltd	(14,289)	(14,289)
– Final dividend	(13,707)	(13,707)
– Intangible assets	(12,507)	(12,497)
	210,825	213,023
Tier 2		
Available-for-sale reserve	4,716	4,791
Property revaluation reserve	30,684	30,676
Collectively assessed allowances	12,600	12,600
Subordinated liabilities	87,933	87,933
Deductions:		
– Investment in HSBC Life Assurance (Malta) Ltd	(14,289)	(14,289)
	121,644	121,711
Total own funds	332,469	334,734
Capital adequacy ratio at 31 December 2011		
Tier 1 Ratio	7.4%	7.4%
Total capital ratio	11.6%	11.7%
Capital adequacy ratio at 31 December 2010		
Tier 1 Ratio	6.5%	6.3%
Total capital ratio	10.2%	10.0%

6 Interest and similar income

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
On loans and advances to banks	3,072	2,875	3,072	2,875
On loans and advances to customers	147,102	144,948	147,104	144,949
On balances with Central Bank of Malta	1,148	848	1,148	848
On Treasury Bills	2,075	2,911	2,075	2,911
	153,397	151,582	153,399	151,583
On debt and other fixed income instruments	29,714	23,301	26,652	19,063
Amortisation of net premiums	(7,149)	(5,871)	(7,444)	(5,456)
	22,565	17,430	19,208	13,607
	175,962	169,012	172,607	165,190
Interest receivable and similar income from:				
– Group companies	3,040	2,843	3,040	2,843
– subsidiary companies	–	–	2	1

Discount unwind on impaired loans and advances to customers included in interest receivable on loans and advances to customers amounted to €1,883,000 (2010: €1,570,000).

Notes on the Financial Statements (continued)**7 Interest expense**

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
On deposits by banks	3,853	1,433	3,853	1,433
On customer accounts	38,370	40,225	38,720	40,868
On subordinated liabilities	4,446	4,502	4,446	4,502
On finance leases	34	10	34	10
	46,703	46,170	47,053	46,813
Interest payable to:				
– Group companies	3,780	1,384	3,780	1,384
– subsidiary companies	–	–	350	643

8 Net fee and commission income

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Net fee and commission income that is not an integral part of the effective interest method on:				
– financial assets or liabilities not at fair value through profit or loss	20,965	21,203	21,015	21,203
– trust and other fiduciary activities that result in the holding or investing of assets on behalf of individuals and other institutions	9,684	10,503	5,051	5,343
– other	2,901	2,574	3,773	3,708
	33,550	34,280	29,839	30,254
Net fee and commission income from:				
– Group companies	1,311	1,082	1,027	888
– subsidiary companies	–	–	3,306	3,312

Net fee and commission income for the bank include €3,243,000 (2010: €3,419,000) derived from investment services activities.

9 Dividend income

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Available-for-sale financial investments	1	–	–	–
Subsidiary companies	–	–	24,987	7,538
	1	–	24,987	7,538

10 Trading profits

	2011	2010
	€000	€000
<i>Group/Bank</i>		
Profit on foreign exchange activities	8,386	7,149
Net losses on financial instruments at fair value through profit or loss	(80)	(333)
	8,306	6,816

11 Net losses on sale of available-for-sale financial investments

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Net revaluation losses transferred from equity	(2,107)	(369)	(2,113)	(370)
	(2,107)	(369)	(2,113)	(370)

12 Net operating income

Net operating income includes net income from Life insurance business analysed as follows:

	<i>Group</i>	
	2011	2010
	€000	€000
Net fee and commission income	795	577
Net (expense)/income from insurance financial instruments designated at fair value	(6,455)	19,707
Net earned insurance premiums	64,459	58,738
Net other operating income	13,657	4,411
	72,456	83,433
Net insurance claims incurred and movement in policyholders' liabilities	(55,723)	(70,988)
	16,733	12,445

a Net earned insurance premiums

	<i>Group</i>	
	2011	2010
	€000	€000
Life insurance		
Gross premium written	68,130	62,519
Outward reinsurance premiums	(3,671)	(3,781)
	64,459	58,738

b Net insurance claims incurred and movement in policyholders' liabilities

	<i>Group</i>					
	<i>Gross</i>	<i>Reinsurance</i>	<i>Net</i>	<i>Gross</i>	<i>Reinsurance</i>	<i>Net</i>
	2011	2011	2011	2010	2010	2010
	€000	€000	€000	€000	€000	€000
Life insurance						
Claims paid	27,268	(374)	26,894	24,318	(1,121)	23,197
Change in technical provision	36,574	(8,183)	28,391	49,112	(2,307)	46,805
Change in claims provision	1,275	(837)	438	11,056	(10,070)	986
	65,117	(9,394)	55,723	84,486	(13,498)	70,988

c Disposal of card acquiring business

The bank disposed of its card acquiring business in line with HSBC Group strategy to exit acquiring businesses globally for a consideration of €11m. The bank recorded a net operating income amounting to €9.7m in relation to this sale. This is included in Net other operating income.

Notes on the Financial Statements (continued)

13 Employee compensation and benefits

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Wages, salaries and allowances	46,397	46,329	43,855	44,107
Defined contribution social security costs	2,445	2,368	2,313	2,273
Retirement benefits	9,326	1,297	9,135	1,297
Share-based payments	639	729	607	703
	58,807	50,723	55,910	48,380
	<i>Number</i>	<i>Number</i>	<i>Number</i>	<i>Number</i>
Average number of employees				
– executive and senior managerial	273	267	252	248
– other managerial, supervisory and clerical	1,235	1,261	1,169	1,223
– others	43	47	43	47
	1,551	1,575	1,464	1,518

During the year the bank announced an early voluntary retirement scheme for its employees as part of the continued transformation programme for the business. The provision as at 31 December 2011 amounted to €10,518,600 while the charge for the year amounted to €9,326,000 (2010: €1,297,000) for the group and €9,135,000 (2010: €1,297,000) for the bank.

In order to align the interests of staff with those of shareholders, share options in ordinary shares of the ultimate parent company are offered to group employees under all-employee share plans and achievement shares awarded to group middle management and above, under discretionary incentive plans. The company offered two types of share option schemes to its employees.

Under the HSBC Holdings savings-related share option plans, options are offered at nil consideration at an exercise price discounted at a rate of 20% of the market value immediately preceding the date of invitation. The options are exercisable either on the first, third or fifth anniversary of the commencement of the relevant savings contract.

Options awarded up to 31 December 2004 under the discretionary HSBC Holdings Group Share Option Plan were offered for nil consideration and granted at market value and are normally exercisable between the third and tenth anniversaries of the date of grant, subject to vesting conditions.

Shares in HSBC Holdings plc awarded under the discretionary HSBC Holdings Group Achievement Share Scheme are offered at nil consideration. Shares are released to individuals after three years provided they remain employed by the Group. There is no performance condition attached to these awards. For those receiving share awards, additional awards will be made during the three year life of the award, representing equivalent value to dividends reinvested in shares. At the end of the three year period, the value of the award will have grown in line with HSBC's total shareholder return over the same period.

	<i>Group</i>			
	<i>Options</i>	<i>Weighted average exercise price (€)</i>	<i>Options</i>	<i>Weighted average exercise price (€)</i>
	2011	2011	2010	2010
Savings related Share Option Plans				
Outstanding at 1 January	774,896	3.87	96,759	9.71
Granted during the year	100,299	5.92	821,708	3.65
Exercised during the year	(28,817)	5.95	(86,717)	4.75
Closed during the year	(78,156)	5.51	(56,854)	6.34
Outstanding at 31 December	768,222	3.89	774,896	3.87
Exercisable at 31 December	7,990	7.64	5,438	8.03

13 Employee compensation and benefits (continued)

	<i>Group</i>			
	<i>Options</i>	<i>Weighted average exercise price (€)</i>	<i>Options</i>	<i>Weighted average exercise price (€)</i>
	2011	2011	2010	2010
Group Share Option Plans				
Outstanding at 1 January	601,793	6.99	620,040	8.70
Exercised during the year	(2,524)	7.21	(10,443)	6.99
Released during the year	(116,277)	8.07	(7,804)	8.38
Outstanding at 31 December	482,992	8.15	601,793	7.88
Exercisable at 31 December	166,118	7.21	214,659	6.99

The options outstanding at reporting date had a contractual life of between one and five years.

The weighted average share price and exercise price are denominated in pounds sterling and disclosed in euro equivalent using the exchange rates prevailing at the reporting date.

Fair value of share option schemes

Fair values of share options awarded under all-employee share option plans in 2011, measured at the date of grant of the option, are calculated using a Black-Scholes model.

The expected life of options depends on the behaviour of option holders, which is incorporated into the option model consistent with historic observable data. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitations of the model used. The significant weighted average assumptions used to estimate the fair value of the options granted in 2011 were as follows:

	<i>1 year savings-related share option schemes</i>	<i>3 year savings-related share option schemes</i>	<i>5 year savings-related share option schemes</i>
Risk-free interest rate (%)	0.8	1.7	2.5
Expected volatility (%)	25.0	25.0	25.0
Expected life (years)	1	3	5

The risk-free interest rate was determined from the UK gilts zero-coupon yield curve. Expected volatility is estimated by considering both historic average share price volatility and implied volatility for traded options over HSBC shares of similar maturity to those of the employee options. Expected life is not a single input parameter but a function of various behavioural assumptions. Expected dividend yield was determined to be 4.5 per cent per annum, in line with consensus analyst options.

14 Net impairment

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Write-downs				
Investments				
– available-for-sale debt instruments	(3,981)	–	–	–
– available-for-sale equity instruments	(198)	(198)	–	–
	(4,179)	(198)	–	–
Property, plant and equipment	(529)	–	(529)	–

Notes on the Financial Statements (continued)**14 Net impairment** (continued)

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Loans and advances to customers				
– specific allowances	(7,423)	(8,744)	(7,423)	(8,744)
– collective allowances	–	(343)	–	(343)
– bad debts written off	(1,110)	(1,324)	(1,110)	(1,324)
	(8,533)	(10,411)	(8,533)	(10,411)
Other assets				
– specific allowances	–	(32)	–	–
Reversals of write-downs				
Loans and advances to customers				
– specific allowances	4,497	4,503	4,497	4,503
– collective allowances	168	–	168	–
– bad debts recovered	294	642	294	642
	4,959	5,145	4,959	5,145
Other assets				
– specific allowances	32	–	–	–
Net impairment	(8,250)	(5,496)	(4,103)	(5,266)

15 Profit before tax

	2011	2010
	€000	€000
<i>Group/Bank</i>		
Profit before tax is stated after charging:		
Directors' emoluments		
– fees	164	135
– other emoluments	1,000	996
	1,164	1,131

Profit before tax for the group is also stated after charging the following fees (excluding VAT) in relation to services provided by the external auditors of the group:

- auditors' fees of €172,000;
- other assurance services fees of €61,000;
- tax advisory services fees of €12,000; and
- other non-audit services fees of €22,000.

16 Tax expense

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
The charge for income tax, which is based on the taxable profit for the year at a rate of 35%, comprises:				
– current	38,896	30,651	39,395	26,987
– deferred	(8,158)	(1,324)	(6,455)	(2,291)
	30,738	29,327	32,940	24,696

16 Tax expense (continued)

The tax on profit and the result of accounting profit multiplied by the applicable tax rate are reconciled as follows:

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Profit before tax	88,305	83,088	99,499	74,995
Tax at the applicable rate of 35%	30,907	29,081	34,825	26,248
Tax effect of non-taxable income	(17)	(26)	–	–
Tax effect of profits taxed at different rates	–	–	(1,708)	(1,750)
Tax effect of non-deductible expenses	33	83	31	79
Tax effect of depreciation charges not deductible by way of capital allowances	321	294	321	294
Tax effects of property sales tax consequences	62	(33)	61	(33)
Tax effect of bonus shares received	35	89	–	–
Tax effect of additional deductions	(45)	(46)	(45)	(46)
Tax effect of taxable temporary differences not previously recognised	(558)	(115)	(545)	(96)
Tax expense	30,738	29,327	32,940	24,696

17 Earnings per share

The calculation of earnings per share of the group and the bank is based on the profit attributable to shareholders of the bank as shown in profit or loss, divided by the number of shares in issue as at 31 December 2011.

18 Balances with Central Bank of Malta, Treasury Bills and cash

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Balances with Central Bank of Malta	104,624	90,982	104,624	90,982
Malta Government Treasury Bills	97,804	264,900	97,804	264,900
Cash	30,960	24,103	30,959	24,102
	233,388	379,985	233,387	379,984

Balances with Central Bank of Malta include a reserve deposit requirement in terms of Regulation (EC) No. 1745/2003 of the European Central Bank. The average reserve deposit requirement as at the reporting date was €87,682,000 (2010: €86,726,000) in respect of the group and the bank.

19 Derivatives

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Derivative assets				
Held for trading	17,136	11,405	17,856	11,602
Fair value hedging instruments	–	84	–	84
	17,136	11,489	17,856	11,686
Held for trading and fair value hedging instruments held with:				
– Group companies	4,137	1,783	4,137	1,783
– subsidiary companies	–	–	720	197

Notes on the Financial Statements (continued)

19 Derivatives (continued)

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Derivative liabilities				
Held for trading	17,810	12,311	17,810	12,313
Held for trading instruments held with:				
– Group companies	12,972	9,951	12,972	9,951
– subsidiary companies	–	–	–	2

a Derivatives held for trading

	<i>Notional</i>	<i>Fair value assets</i>	<i>Fair value liabilities</i>	<i>Notional</i>	<i>Fair value assets</i>	<i>Fair value liabilities</i>
	2011	2011	2011	2010	2010	2010
	€000	€000	€000	€000	€000	€000
<i>Group</i>						
Interest rate derivatives						
Over the counter products						
– interest rate swaps						
purchased	177,888	11,134	–	182,488	9,103	–
– interest rate swaps written	177,888	–	11,716	182,488	–	9,585
Currency derivatives						
Over the counter products						
– foreign exchange contracts	128,494	2,973	2,949	92,156	935	1,357
– foreign exchange options						
purchased	11,322	1,148	142	9,424	148	–
– foreign exchange options written	11,322	26	1,148	9,424	–	150
Equity derivatives						
Over the counter products						
– equity index options						
purchased	12,768	1,855	–	19,573	1,219	–
– equity index options written	12,768	–	1,855	19,573	–	1,219
		17,136	17,810		11,405	12,311
<i>Bank</i>						
Interest rate derivatives						
Over the counter products						
– interest rate swaps						
purchased	177,888	11,134	–	182,488	9,103	–
– interest rate swaps written	177,888	–	11,716	182,488	–	9,585
Currency derivatives						
Over the counter products						
– foreign exchange contracts	138,468	3,693	2,949	101,772	1,132	1,359
– foreign exchange options						
purchased	11,322	1,148	142	9,424	148	–
– foreign exchange options written	11,322	26	1,148	9,424	–	150
Equity derivatives						
Over the counter products						
– equity index options						
purchased	12,768	1,855	–	19,573	1,219	–
– equity index options written	12,768	–	1,855	19,573	–	1,219
		17,856	17,810		11,602	12,313

19 Derivatives (continued)

b Fair value hedging instruments

	<u>Notional</u>	<u>Fair value assets</u>	<u>Fair value liabilities</u>	<u>Notional</u>	<u>Fair value assets</u>	<u>Fair value liabilities</u>
	2011	2011	2011	2010	2010	2010
	€000	€000	€000	€000	€000	€000
<i>Group/Bank</i>						
Fair value hedging instruments						
Over the counter products						
– interest rate swaps purchased	–	–	–	66,042	84	–

The group uses interest rate swaps to hedge its exposure to changes in fair value of certain fixed rate deposit liabilities attributable to changes in market sector interest rates. There were no designated hedging instruments as at 31 December 2011.

20 Financial assets designated at fair value

	<i>Group</i>	
	<u>2011</u>	<u>2010</u>
	€000	€000
Debt, Treasury Bills and other fixed income instruments	216,172	141,547
Equity and other non-fixed income instruments	153,908	164,022
	370,080	305,569

a Debt, Treasury Bills and other fixed income instruments

	<i>Group</i>	
	<u>2011</u>	<u>2010</u>
	€000	€000
Issued by public bodies		
– local government	57,468	54,599
– foreign government	70,559	45,188
Issued by other issuers		
– local banks	3,184	1,948
– foreign banks	27,702	9,230
– others local	3,860	4,710
– others foreign	53,399	25,872
	216,172	141,547
Listing status		
– listed on the Malta Stock Exchange	64,512	62,015
– listed elsewhere	151,660	79,532
	216,172	141,547
At 1 January		
Exchange adjustments	34	(49)
Additions	157,258	66,654
Disposals/Redemptions	(81,304)	(24,781)
Changes in fair value	(1,363)	(650)
At 31 December	216,172	141,547

Notes on the Financial Statements (continued)

20 Financial assets designated at fair value (continued)

b Equity and other non-fixed income instruments

	<i>Group</i>	
	2011	2010
	€000	€000
Issued by other issuers		
– others local	43,376	35,553
– others foreign	110,532	128,469
	153,908	164,022
Listing status		
– listed on the Malta Stock Exchange	43,376	13,298
– listed elsewhere	110,532	150,724
	153,908	164,022
At 1 January	164,022	147,456
Exchange adjustments	1,838	2,393
Additions	80,441	22,914
Disposals	(83,311)	(22,227)
Changes in fair value	(9,082)	13,486
At 31 December	153,908	164,022

21 Financial investments

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Debt and other fixed income instruments				
– available-for-sale	934,837	688,650	883,378	592,740
Equity and other non-fixed income instruments				
– available-for-sale	1,993	1,956	369	367
	936,830	690,606	883,747	593,107

a Debt and other fixed income instruments available-for-sale

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Issued by public bodies				
– local government	602,171	409,624	569,953	353,608
– foreign government	127,303	88,341	120,436	64,670
Issued by other issuers				
– foreign banks	52,419	106,553	46,865	100,036
– local others	491	492	–	–
– foreign others	152,453	83,640	146,124	74,426
	934,837	688,650	883,378	592,740
Amounts include:				
– issued by Group companies	42	72	–	–
Listing status				
– listed on the Malta Stock Exchange	602,662	410,116	569,953	353,608
– listed elsewhere	332,175	278,534	313,425	239,132
	934,837	688,650	883,378	592,740

21 Financial investments (continued)

a Debt and other fixed income instruments available-for-sale (continued)

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
At 1 January	688,650	468,172	592,740	371,014
Exchange adjustments	(3,580)	2,927	(3,034)	2,891
Amortisation	(7,193)	(5,884)	(7,466)	(5,470)
Additions	599,119	307,684	599,077	307,688
Disposals/Redemptions	(344,150)	(85,338)	(302,557)	(85,338)
Changes in fair value	1,991	1,089	4,618	1,955
At 31 December	934,837	688,650	883,378	592,740

Debt instruments with a carrying amount of €125,720,000 (2010: €168,616,000) have been pledged against the provision of credit lines by the Central Bank of Malta. At 31 December 2011, no balances were outstanding against these credit lines. In addition debt securities with a carrying amount of €17,979,000 (2010: €14,826,000) have been pledged in favour of the Depositors' Compensation Scheme (refer to note 41).

b Equity and other non-fixed income instruments available-for-sale

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Issued by other issuers				
– local others	1,979	1,943	355	354
– foreign others	14	13	14	13
	1,993	1,956	369	367
Listing status				
– local unlisted	1,979	1,943	355	354
– foreign unlisted	14	13	14	13
	1,993	1,956	369	367
At 1 January	1,956	1,909	367	367
Changes in fair value	37	47	2	–
At 31 December	1,993	1,956	369	367

As at the reporting date, total impairment loss on the group's equity and other non-fixed income instruments available-for-sale amounted to €4,574,000 (2010: €395,000).

22 Loans and advances to banks

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Repayable on call and at short notice	295,662	72,978	295,609	72,927
Term loans and advances	342,294	641,923	342,294	641,923
	637,956	714,901	637,903	714,850
Amounts include:				
– due from Group companies	622,726	654,402	622,726	654,402

Notes on the Financial Statements (continued)**23 Loans and advances to customers**

	2011	2010
	€000	€000
<i>Group/Bank</i>		
Repayable on call and at short notice	444,167	474,100
Term loans and advances	2,958,125	2,867,468
Gross loans and advances to customers	3,402,292	3,341,568
Allowances for uncollectability	(58,068)	(51,133)
Net loans and advances to customers	3,344,224	3,290,435
Allowances for uncollectability		
– individually assessed allowances	45,468	38,365
– collectively assessed allowances	12,600	12,768
	58,068	51,133

The balance of individually assessed allowances at the reporting date includes €25,157,000 (2010: €19,097,000) in respect of interest in suspense which has been netted off against interest receivable.

24 Shares in subsidiary companies

<i>Bank</i>	<i>Incorporated</i>	<i>Nature of</i>	<i>Equity</i>		
<i>Name of company</i>	<i>in</i>	<i>business</i>	<i>interest</i>	2011	2010
			%	€000	€000
HSBC Life Assurance (Malta) Ltd	Malta	Life insurance	99.99	28,578	28,578
HSBC Global Asset Management (Malta) Limited	Malta	Portfolio management services	99.99	5,940	5,940
HSBC Securities Services (Malta) Limited	Malta	Fund administration services	99.99	1,166	1,166
HSBC Stockbrokers (Malta) Limited	Malta	Stockbroking services	99.99	23	23
				35,707	35,707

During the year, HSBC Life Assurance (Malta) Ltd invested in the following subsidiary on incorporation:

<i>Name of company</i>	<i>Incorporated</i>	<i>Nature of</i>	<i>Equity</i>		
	<i>in</i>	<i>business</i>	<i>interest</i>	2011	2010
			%	€000	€000
HSBC Insurance Management Services (Europe) Limited	Malta	Insurance Management Services	99.99	25	–

25 Intangible assets

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Software	12,568	7,670	12,497	7,583
Present value of in-force long-term insurance business	76,443	62,985	–	–
	89,011	70,655	12,497	7,583

a Software

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Cost				
At 1 January	18,780	12,042	17,383	10,645
Additions	5,758	6,765	5,729	6,738
Disposals	(698)	(27)	(554)	–
At 31 December	23,840	18,780	22,558	17,383
Amortisation				
At 1 January	11,110	10,130	9,800	8,904
Charge for the year	860	980	815	896
Disposals	(698)	–	(554)	–
At 31 December	11,272	11,110	10,061	9,800
Carrying amount at 1 January	7,670	1,912	7,583	1,741
Carrying amount at 31 December	12,568	7,670	12,497	7,583

b Present value of in-force long-term insurance business

	<i>Group</i>	
	2011	2010
	€000	€000
At 1 January	62,985	58,779
Addition from current year new business	6,251	5,373
Movement from in-force business	7,207	(1,167)
At 31 December	76,443	62,985

The following are the key assumptions used in the computation of the group's PVIF in the current and comparative periods:

	<i>Group</i>	
	2011	2010
	%	%
Risk free rate	Euro swap curve	Euro swap curve
Risk adjusted discount rate	Euro swap curve + 50 bps	8.00
	Operational Risk Margin	
Expenses inflation	French inflation swap curve modified for Malta	French inflation swap curve modified for Malta
Lapse rate	Different rates for different products	Different rates for different products

The business benefitted from a non-recurring gain of €6,930,000 as a result of a refinement in the methodology used to calculate the present value of in-force long-term insurance business. The risk discount rate (RDR) used to calculate the present value of the expected future shareholder cash flows is now based on the euro swap rates curve with the inclusion of a 50bps margin to allow for operational risk. The RDR is now therefore term dependent as opposed to a fixed level rate as employed in 2010.

Notes on the Financial Statements (continued)

26 Property, plant and equipment

	<i>Land and buildings</i>	<i>Computer equipment</i>	<i>Others</i>	<i>Total</i>
	€000	€000	€000	€000
<i>Group</i>				
Cost/revaluation				
At 1 January 2011	46,978	19,208	49,007	115,193
Additions	71	422	2,779	3,272
Disposals	(2,816)	(2,436)	(6,767)	(12,019)
At 31 December 2011	44,233	17,194	45,019	106,446
Depreciation and impairment losses				
At 1 January 2011	1,678	15,315	32,713	49,706
Charge for the year	579	1,036	3,585	5,200
Impairment losses	–	–	529	529
Disposals	(1,142)	(2,436)	(5,524)	(9,102)
At 31 December 2011	1,115	13,915	31,303	46,333
Carrying amount at 1 January 2011	45,300	3,893	16,294	65,487
Carrying amount at 31 December 2011	43,118	3,279	13,716	60,113
Cost/revaluation				
At 1 January 2010	46,601	18,423	47,107	112,131
Additions	140	1,096	3,074	4,310
Revaluation	587	–	–	587
Disposals	(350)	(311)	(1,174)	(1,835)
At 31 December 2010	46,978	19,208	49,007	115,193
Depreciation and impairment losses				
At 1 January 2010	2,673	14,296	29,765	46,734
Charge for the year	553	1,328	3,940	5,821
Revaluation	(1,530)	–	–	(1,530)
Disposals	(18)	(309)	(992)	(1,319)
At 31 December 2010	1,678	15,315	32,713	49,706
Carrying amount at 1 January 2010	43,928	4,127	17,342	65,397
Carrying amount at 31 December 2010	45,300	3,893	16,294	65,487
				<i>Group</i>
				2011
				2010
				€000
				€000
Carrying amount of land and buildings occupied for own activities				43,021
				45,203
	<i>Land and buildings</i>	<i>Computer equipment</i>	<i>Others</i>	<i>Total</i>
	€000	€000	€000	€000
<i>Bank</i>				
Cost/revaluation				
At 1 January 2011	47,083	18,961	48,806	114,850
Additions	71	422	2,764	3,257
Disposals	(2,816)	(2,436)	(6,767)	(12,019)
At 31 December 2011	44,338	16,947	44,803	106,088

26 Property, plant and equipment (continued)

	<i>Land and buildings</i>	<i>Computer equipment</i>	<i>Others</i>	<i>Total</i>
	€000	€000	€000	€000
<i>Bank</i>				
Depreciation and impairment losses				
At 1 January 2011	1,678	15,069	32,523	49,270
Charge for the year	579	1,035	3,582	5,196
Impairment losses	–	–	529	529
Disposals	(1,142)	(2,436)	(5,524)	(9,102)
At 31 December 2011	1,115	13,668	31,110	45,893
Carrying amount at 1 January 2011	45,405	3,892	16,283	65,580
Carrying amount at 31 December 2011	43,223	3,279	13,693	60,195
Cost/revaluation				
At 1 January 2010	46,706	18,175	46,906	111,787
Additions	140	1,096	3,074	4,310
Revaluation	587	–	–	587
Disposals	(350)	(310)	(1,174)	(1,834)
At 31 December 2010	47,083	18,961	48,806	114,850
Depreciation and impairment losses				
At 1 January 2010	2,673	14,082	29,562	46,317
Charge for the year	553	1,372	3,877	5,802
Revaluation	(1,530)	–	–	(1,530)
Disposals	(18)	(385)	(916)	(1,319)
At 31 December 2010	1,678	15,069	32,523	49,270
Carrying amount at 1 January 2010	44,033	4,093	17,344	65,470
Carrying amount at 31 December 2010	45,405	3,892	16,283	65,580
				<i>Bank</i>
				2011
				2010
				€000
				€000
Carrying amount of land and buildings occupied for own activities				43,223
				45,405

The carrying amount of land and buildings that would have been included in the financial statements had these assets been carried at cost less depreciation is €14,672,000 (2010: €15,995,000) for the group and the bank.

Land and buildings were revalued in September 2010.

27 Investment property

	<i>Fair Value</i>	<i>Cost</i>	<i>Fair Value</i>	<i>Cost</i>
	2011	2011	2010	2010
	€000	€000	€000	€000
<i>Group</i>				
Freehold land and buildings				
As at 1 January	14,591	8,574	14,588	8,571
Additions	19	19	3	3
Fair value adjustments	(12)	–	–	–
At 31 December	14,598	8,593	14,591	8,574

Notes on the Financial Statements (continued)

27 Investment property (continued)

	<i>Fair Value</i>	<i>Cost</i>	<i>Fair Value</i>	<i>Cost</i>
	2011	2011	2010	2010
	€000	€000	€000	€000
<i>Bank</i>				
Freehold land and buildings				
As at 1 January	11,668	6,494	11,665	6,491
Additions	7	7	3	3
Fair value adjustments	(12)	–	–	–
At 31 December	11,663	6,501	11,668	6,494

During the year ended 31 December 2011, €787,000 (2010: €748,000) was recognised as rental income in profit or loss relating to investment property for the group. The bank recognised €596,000 (2010: €573,000) as rental income, which was received from a Group company.

28 Non-current assets held for sale

	<i>Group/Bank</i>	
	2011	2010
	€000	€000
Assets acquired in satisfaction of debt	11,108	7,662
Other	1,870	2,012
	12,978	9,674

Repossessed properties are made available for sale in an orderly fashion, with the proceeds used to reduce or repay the outstanding indebtedness. The group does not generally occupy repossessed properties for its business use. In the main, repossessed property consists of immovable property.

29 Other assets

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Acceptances and endorsements	2,015	5,139	2,015	5,139
Reinsurance assets	22,287	24,128	–	–
Other	6,907	5,158	6,591	4,300
	31,209	34,425	8,606	9,439
Amounts include:				
– due from Group companies	1,899	1,265	1,899	1,265

30 Prepayments and accrued income

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Accrued income	39,485	37,524	34,388	33,083
Prepayments	1,144	1,186	1,139	1,173
	40,629	38,710	35,527	34,256
Amounts include:				
– due from Group companies	510	508	464	435
– due from subsidiary companies	–	–	360	327

31 Deposits by banks

	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>
<i>Group/Bank</i>		
Term deposits	357,428	214,993
Repayable on demand	31,742	17,797
	<u>389,170</u>	<u>232,790</u>
Amounts include:		
– due to Group companies	<u>371,510</u>	<u>208,315</u>

32 Customer accounts

	<i>Group</i>		<i>Bank</i>	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>
Term deposits	1,876,167	1,941,628	1,885,426	1,943,129
Repayable on demand	2,526,808	2,521,233	2,555,220	2,574,634
	<u>4,402,975</u>	<u>4,462,861</u>	<u>4,440,646</u>	<u>4,517,763</u>
Amounts include:				
– due to Group companies	<u>106</u>	<u>744</u>	<u>106</u>	<u>744</u>
– due to subsidiary companies	<u>–</u>	<u>–</u>	<u>37,671</u>	<u>54,902</u>

33 Deferred tax

	<i>Group</i>		<i>Bank</i>	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>
Deferred tax and liabilities/(assets) are attributable to the following:				
– excess of capital allowances over depreciation	1,354	677	1,353	675
– allowances for uncollectibility	(19,716)	(15,682)	(19,509)	(15,533)
– property sales tax consequences	7,094	7,086	6,742	6,735
– fair value movements on investments	2,913	333	2,497	123
– value of in-force life insurance business	26,755	22,045	–	–
– fair value movement on policyholders' investments	(9,431)	(3,124)	–	–
– retirement benefits	(3,927)	(504)	(3,860)	(504)
– other	(934)	(1,408)	(967)	(1,398)
	<u>4,108</u>	<u>9,423</u>	<u>(13,744)</u>	<u>(9,902)</u>

	<i>Group</i>			
	<i>At</i>	<i>Recognised</i>	<i>Recognised</i>	<i>At</i>
	<i>1 January</i>	<i>in profit</i>	<i>in equity</i>	<i>31 December</i>
	<u>2011</u>	<u>or loss</u>	<u>in equity</u>	<u>2011</u>
	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	677	677	–	1,354
– allowances for uncollectibility	(15,682)	(4,034)	–	(19,716)
– property sales tax consequences	7,086	1	7	7,094
– fair value movements on investments	333	–	2,580	2,913
– value of in-force life insurance business	22,045	4,710	–	26,755
– fair value movement on policyholders' investments	(3,124)	(6,307)	–	(9,431)
– retirement benefits	(504)	(3,423)	–	(3,927)
– other	(1,408)	218	256	(934)
	<u>9,423</u>	<u>(8,158)</u>	<u>2,843</u>	<u>4,108</u>

Notes on the Financial Statements (continued)

33 Deferred tax (continued)

<i>Group</i>				
	<i>At 1 January 2010</i>	<i>Recognised in profit or loss</i>	<i>Recognised in equity</i>	<i>At 31 December 2010</i>
	€000	€000	€000	€000
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	852	(175)	–	677
– allowances for uncollectibility	(14,066)	(1,616)	–	(15,682)
– property sales tax consequences	7,023	–	63	7,086
– fair value movements on investments	(280)	3	610	333
– value of in-force life insurance business	20,573	1,472	–	22,045
– fair value movement on policyholders' investments	(2,698)	(426)	–	(3,124)
– retirement benefits	(350)	(154)	–	(504)
– other	(1,256)	(428)	276	(1,408)
	9,798	(1,324)	949	9,423
<i>Bank</i>				
	<i>At 1 January 2011</i>	<i>Recognised in profit or loss</i>	<i>Recognised in equity</i>	<i>At 31 December 2011</i>
	€000	€000	€000	€000
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	675	678	–	1,353
– allowances for uncollectibility	(15,533)	(3,976)	–	(19,509)
– property sales tax consequences	6,735	–	7	6,742
– fair value movements on investments	123	–	2,374	2,497
– retirement benefits	(504)	(3,356)	–	(3,860)
– other	(1,398)	199	232	(967)
	(9,902)	(6,455)	2,613	(13,744)
<i>Bank</i>				
	<i>At 1 January 2010</i>	<i>Recognised in profit or loss</i>	<i>Recognised in equity</i>	<i>At 31 December 2010</i>
	€000	€000	€000	€000
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	842	(167)	–	675
– allowances for uncollectibility	(13,997)	(1,536)	–	(15,533)
– property sales tax consequences	6,672	–	63	6,735
– fair value movements on investments	(708)	3	828	123
– retirement benefits	(350)	(154)	–	(504)
– other	(1,225)	(437)	264	(1,398)
	(8,766)	(2,291)	1,155	(9,902)

The group's deferred tax assets and liabilities on the statement of financial position have not been off-set to the extent that there is no legally enforceable right of set-off with the tax authorities.

34 Liabilities to customers under investment contracts

	<i>Group</i>	
	2011	2010
	€000	€000
At 1 January	18,962	16,853
Premiums received	552	1,653
Amounts paid on surrender and other termination during the year	(1,381)	(1,236)
Changes in unit prices and other movements	(1,213)	1,692
At 31 December	16,920	18,962

35 Liabilities under insurance contracts issued

	<i>Group</i>	
	<i>Gross</i>	<i>Gross</i>
	2011	2010
	€000	€000
Life insurance (non-linked)		
Provisions for policyholders	317,835	285,546
Outstanding claims	2,212	12,156
Total non-linked	320,047	297,702
Life insurance (linked)		
Provisions for policyholders	116,561	112,346
Outstanding claims	64	413
Total linked	116,625	112,759
Total liabilities under insurance contracts	436,672	410,461

	<i>Group</i>			
	<i>Non-linked business</i>	<i>Linked business</i>	<i>All business</i>	
	<i>Provisions for policy- holders</i>	<i>Provisions for policy- holders</i>	<i>Outstanding claims</i>	<i>Total</i>
	2011	2011	2011	2011
	€000	€000	€000	€000
At 1 January	285,546	112,346	12,569	410,461
Claims in respect of new business	–	28,288	2,251	30,539
Movement for the year	32,289	(24,073)	(891)	7,325
Previous year claims paid	–	–	(11,653)	(11,653)
At 31 December	317,835	116,561	2,276	436,672
	2010	2010	2010	2010
	€000	€000	€000	€000
At 1 January	260,187	88,572	2,754	351,513
Claims in respect of new business	–	333	12,988	13,321
Movement for the year	25,359	23,532	(1,897)	46,994
Previous year claims paid	–	(91)	(1,276)	(1,367)
At 31 December	285,546	112,346	12,569	410,461

Notes on the Financial Statements (continued)**36 Other liabilities**

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Bills payable	21,775	12,189	21,775	12,189
Cash collateral for commitments	190	136	190	136
Obligations under finance leases	67	136	67	136
Acceptances and endorsements	2,015	5,139	2,015	5,139
Other	14,098	15,424	9,878	11,721
	38,145	33,024	33,925	29,321

37 Accruals and deferred income

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
Accrued interest	18,553	18,432	18,670	18,570
Other	17,426	15,855	16,482	14,740
	35,979	34,287	35,152	33,310
Amounts include:				
– due to Group companies	3,723	2,582	3,296	2,213
– due to subsidiary companies	–	–	117	138

38 Provisions for liabilities and other charges

	<i>Group</i>		<i>Bank</i>	
	2011	2010	2011	2010
	€000	€000	€000	€000
At 1 January	2,548	577	2,511	514
Provisions made during the year	10,832	2,036	10,627	2,017
Provisions reversed during the year	(1,704)	(20)	(1,704)	(20)
Provisions utilised during the year	(425)	(45)	(403)	–
At 31 December	11,251	2,548	11,031	2,511

Provisions for liabilities and other charges include amounts raised in relation to litigations and early voluntary retirement scheme.

The bank is a party to legal actions arising from normal business operations. Management believes that adequate provisions have been made against these litigations, based on legal advice, on the timing and amount of the possible economic outflows.

Refer to note 13 for details of the early voluntary retirement scheme provision.

39 Subordinated liabilities

	<i>Group</i>		<i>Bank</i>	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>
4.60% subordinated unsecured loan stock 2017	58,082	58,052	58,082	58,052
5.90% subordinated unsecured loan stock 2018	29,126	29,098	29,851	29,828
	87,208	87,150	87,933	87,880
Subordinated loan liabilities held by:				
– subsidiary companies	<u>–</u>	<u>–</u>	<u>725</u>	<u>730</u>

The above liabilities will, in the event of the winding up of the bank, be subordinated to the claims of depositors and all other creditors. The group did not have any defaults of interest or other breaches with respect to its subordinated liabilities during the current and comparative period.

40 Share capital

	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>
Authorised		
470,000,000 Ordinary shares of 30c each	141,000	141,000
Issued and fully paid up		
291,840,000 Ordinary shares of 30c each	87,552	87,552

41 Reserves

Revaluation reserve

The revaluation reserve comprises the surplus arising on the revaluation of the group's freehold and long leasehold properties and the cumulative net change in fair values of available-for-sale financial investments held by the group, net of deferred taxation. The revaluation reserve is not available for distribution.

Depositors Compensation Scheme reserve

Retained earnings is inclusive of Depositors Compensation Scheme reserve amounting to €22,871,000. This reserve is excluded from the Own Funds calculation (refer to note 5).

As at 31 December 2011, debt securities with a carrying amount of €17,979,000 had been pledged in terms of the Depositor compensation scheme (refer to note 21a). Central Bank balances amounting to €5,900,000 have also been pledged in favour of the scheme.

42 Contingent liabilities

	<i>Group</i>		<i>Bank</i>	
	<i>Contract amount</i>	<i>Contract amount</i>	<i>Contract amount</i>	<i>Contract amount</i>
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
	<u>€000</u>	<u>€000</u>	<u>€000</u>	<u>€000</u>
Guarantees and assets pledged as collateral security				
– guarantees	91,493	98,070	93,196	98,093
– standby letters of credit	39,090	30,408	39,090	30,408
– other	180	469	180	469
	130,763	128,947	132,466	128,970
Amounts include:				
– in favour of Group companies	4,954	8,436	4,954	8,436
– in favour of subsidiary companies	<u>–</u>	<u>–</u>	<u>1,703</u>	<u>23</u>

Notes on the Financial Statements (continued)

43 Commitments

	<i>Contract amount</i>	
	2011	2010
	€000	€000
<i>Group/Bank</i>		
Documentary credits	17,321	15,405
Undrawn formal standby facilities, credit facilities and other commitments to lend	1,067,186	962,311
Uncalled share capital in other companies	2	2
	<u>1,084,509</u>	<u>977,718</u>

44 Capital and lease commitments

a *Capital commitments*

Capital commitments are made up of:

	2011	2010
	€000	€000
<i>Group/Bank</i>		
Intangible assets	318	158
Property and equipment	1,450	1,804
	<u>1,768</u>	<u>1,962</u>

b *Operating leases*

Total future minimum lease payments under non-cancellable operating leases not provided for:

	2011	2010
	€000	€000
<i>Group/Bank</i>		
Less than one year	1,265	1,957
Between one year and five years	615	1,376
More than five years	2,159	2,215
	<u>4,039</u>	<u>5,548</u>

c *Finance leases*

Finance lease payments, both principal and finance charge, are payable as follows:

	2011	2010
	€000	€000
<i>Group/Bank</i>		
Less than one year	89	70
Between one year and five years	-	77
Total minimum lease payments	89	147
Finance charges	(22)	(11)
Present value of minimum lease payments	<u>67</u>	<u>136</u>

45 Dividends

	<i>Bank</i>			
	<u>2011</u>	2010	<u>2011</u>	2010
	% per share	% per share	€000	€000
Gross of income tax				
% per 30c share				
– prior year's final	26	27	22,472	23,347
– interim	27	26	23,931	23,055
	53	53	46,403	46,402
	Euro cent per share	Euro cent per share	€000	€000
Net of income tax				
euro cent per 30c share				
– prior year's final	5.01	5.20	14,607	15,176
– interim	5.33	5.13	15,555	14,986
	10.34	10.33	30,162	30,162

The Directors have proposed a final gross ordinary dividend of 7.2 cent (2010: 7.7 cent) per share. The final dividend will be payable to shareholders on the bank's register as at 19 March 2012.

46 Cash and cash equivalents

	<i>Group</i>		<i>Bank</i>	
	<u>2011</u>	2010	<u>2011</u>	2010
	€000	€000	€000	€000
Balances of cash and cash equivalents are analysed below:				
Cash	30,960	24,103	30,959	24,102
Balances with Central Bank of Malta (excluding reserve deposit)	16,942	4,257	16,942	4,257
Loans and advances to banks	548,039	627,190	547,986	627,139
Deposits by banks	(388,178)	(231,944)	(388,178)	(231,944)
Per Statements of Cash Flows	207,763	423,606	207,709	423,554
Adjustment to reflect balances with contractual maturity of more than three months	556,809	657,334	186,729	351,765
Per Statements of Financial Position	764,572	1,080,940	394,438	775,319
Analysed as follows:				
Cash and balances with Central Bank of Malta (excluding reserve deposit)	47,902	28,360	47,901	28,359
Malta Government Treasury Bills	97,804	264,900	97,804	264,900
Financial assets designated at fair value	370,080	305,569	–	–
Loans and advances to banks	637,956	714,901	637,903	714,850
Deposits by banks	(389,170)	(232,790)	(389,170)	(232,790)
	764,572	1,080,940	394,438	775,319

Notes on the Financial Statements (continued)

47 Segmental information

a Class of business

	<i>Retail Banking and Wealth Management</i>	<i>Commercial Banking</i>	<i>Global Banking and Markets</i>	<i>Intersegment</i>	<i>Group Total</i>
	<u>2011</u>	<u>2011</u>	<u>2011</u>	<u>2011</u>	<u>2011</u>
	€000	€000	€000	€000	€000
<i>Group</i>					
Net interest income					
– External	44,614	68,129	16,516	–	129,259
– Inter-segment	16,514	(15,024)	(1,490)	–	–
	<u>61,128</u>	<u>53,105</u>	<u>15,026</u>	<u>–</u>	<u>129,259</u>
Net non-interest income					
– External	35,109	25,670	4,827	–	65,606
– Inter-segment	(694)	386	884	(576)	–
	<u>34,415</u>	<u>26,056</u>	<u>5,711</u>	<u>(576)</u>	<u>65,606</u>
External employee compensation and benefits	<u>(39,726)</u>	<u>(16,280)</u>	<u>(2,801)</u>	<u>–</u>	<u>(58,807)</u>
General and administrative expenses					
– External	(23,724)	(7,287)	(2,322)	–	(33,333)
– Inter-segment	(576)	–	–	576	–
	<u>(24,300)</u>	<u>(7,287)</u>	<u>(2,322)</u>	<u>576</u>	<u>(33,333)</u>
External Depreciation	<u>(3,752)</u>	<u>(1,448)</u>	<u>–</u>	<u>–</u>	<u>(5,200)</u>
External Amortisation	<u>(566)</u>	<u>(258)</u>	<u>(36)</u>	<u>–</u>	<u>(860)</u>
External Net impairment	<u>(6,102)</u>	<u>(2,180)</u>	<u>32</u>	<u>–</u>	<u>(8,250)</u>
External Net provisions for liabilities and other charges	<u>–</u>	<u>204</u>	<u>(314)</u>	<u>–</u>	<u>(110)</u>
Profit before tax	<u>21,097</u>	<u>51,912</u>	<u>15,296</u>	<u>–</u>	<u>88,305</u>
Assets					
Segment total assets	<u>2,426,619</u>	<u>1,689,620</u>	<u>1,708,603</u>	<u>–</u>	<u>5,824,842</u>
Average total assets	<u>2,355,091</u>	<u>1,689,947</u>	<u>1,692,599</u>	<u>–</u>	<u>5,737,637</u>
Total Equity	<u>174,733</u>	<u>168,127</u>	<u>23,605</u>	<u>–</u>	<u>366,465</u>

47 Segmental information (continued)

a Class of business

	<i>Retail Banking and Wealth Management</i>	<i>Commercial Banking</i>	<i>Global Banking and Markets</i>	<i>Intersegment</i>	<i>Group Total</i>
	2010	2010	2010	2010	2010
	€000	€000	€000	€000	€000
<i>Group</i>					
Net interest income					
– External	45,812	63,634	13,396	–	122,842
– Inter-segment	14,967	(12,814)	(2,153)	–	–
	<u>60,779</u>	<u>50,820</u>	<u>11,243</u>	<u>–</u>	<u>122,842</u>
Net non-interest income					
– External	32,444	15,208	5,694	–	53,346
– Inter-segment	(601)	144	796	(339)	–
	<u>31,843</u>	<u>15,352</u>	<u>6,490</u>	<u>(339)</u>	<u>53,346</u>
External employee compensation and benefits	<u>(35,890)</u>	<u>(12,453)</u>	<u>(2,380)</u>	<u>–</u>	<u>(50,723)</u>
General and administrative expenses					
– External	(21,219)	(7,031)	(1,831)	–	(30,081)
– Inter-segment	(339)	–	–	339	–
	<u>(21,558)</u>	<u>(7,031)</u>	<u>(1,831)</u>	<u>339</u>	<u>(30,081)</u>
External Depreciation	<u>(4,243)</u>	<u>(1,566)</u>	<u>(12)</u>	<u>–</u>	<u>(5,821)</u>
External Amortisation	<u>(668)</u>	<u>(247)</u>	<u>(65)</u>	<u>–</u>	<u>(980)</u>
External Net impairment	<u>(2,842)</u>	<u>(2,631)</u>	<u>(23)</u>	<u>–</u>	<u>(5,496)</u>
External Net provisions for liabilities and other charges	<u>20</u>	<u>–</u>	<u>(19)</u>	<u>–</u>	<u>1</u>
Profit before tax	<u>27,441</u>	<u>42,244</u>	<u>13,403</u>	<u>–</u>	<u>83,088</u>
Assets					
Segment total assets	<u>2,283,563</u>	<u>1,690,272</u>	<u>1,676,596</u>	<u>–</u>	<u>5,650,431</u>
Average total assets	<u>2,214,093</u>	<u>1,686,500</u>	<u>1,483,523</u>	<u>–</u>	<u>5,384,116</u>
Total Equity	<u>157,383</u>	<u>144,169</u>	<u>32,278</u>	<u>–</u>	<u>333,830</u>

b Geographical segments

The group's activities are carried out within Malta. There are no identifiable geographical segments or other material concentrations.

48 Comparatives

Certain amounts have been reclassified to comply with the current year's presentation.

Notes on the Financial Statements (continued)

49 Related party transactions

During the course of banking operations, the group conducted business transactions with entities owned by the ultimate parent and its subsidiaries on an arm's length basis.

Executive Directors participate in the HSBC Group share option plans (refer to note 13).

a Transactions, arrangements and agreements involving Directors and others

Particulars of transactions, arrangements and agreements entered into with Directors, connected persons and companies controlled by them and with key management personnel of HSBC Bank Malta p.l.c.:

	<i>Group</i>		<i>Bank</i>	
	<i>Balance at end of year 2011</i>	<i>Balance at end of year 2010</i>	<i>Balance at end of year 2011</i>	<i>Balance at end of year 2010</i>
	€000	€000	€000	€000
Directors, connected persons and companies controlled by them				
Loans	41,799	57,200	41,799	57,200
Credit card transactions	–	20	–	20
Guarantees	1,488	11,560	1,488	11,560
Commitments to lend	27,866	23,558	27,866	23,558
Senior executive management				
Loans	585	703	585	609
Credit card transaction	48	48	44	42

The above banking facilities are part of long-term commercial relationships and were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

b Compensation to Directors and key management personnel

	<i>Group</i>		<i>Bank</i>	
	<i>2011</i>	<i>2010</i>	<i>2011</i>	<i>2010</i>
	€000	€000	€000	€000
Short-term employee benefits	2,376	2,686	2,172	2,127
Retirement benefits	268	301	268	301
Other long-term benefits	–	2	–	2
Share-based payments	103	140	103	115
	2,747	3,129	2,543	2,545

Details of Directors' fees and emoluments are stated in note 15.

c Transactions with other related parties

Information relating both to transactions with HSBC Holdings plc and its subsidiaries as well as with subsidiary companies of HSBC Bank Malta p.l.c. are stated in the 'Notes on the Financial Statements' where the following are disclosed.

- Note 6 – interest and similar income
- Note 7 – interest expense
- Note 8 – net fee and commission income
- Note 9 – dividend income
- Note 13 – employee compensation and benefits
- Note 19 – derivatives
- Note 22 – loans and advances to banks
- Note 24 – shares in subsidiary companies

49 Related party transactions (continued)

c Transactions with other related parties (continued)

- Note 27 – investment property
- Note 29 – other assets
- Note 30 – prepayments and accrued income
- Note 31 – deposits by banks
- Note 32 – customer accounts
- Note 37 – accruals and deferred income
- Note 39 – subordinated liabilities
- Note 42 – contingent liabilities
- Note 43 – commitments

Included in Interest and similar income (refer to note 6) and in Interest expense (refer to note 7), the group recognised interest amounting to €2,880,000 (2010: €2,832,000) and €256,000 (2010: €199,000) respectively, on advances and deposits placed with an intermediate parent.

Included in Net fee and commission income (refer to note 8), the group recognised commission amounting to €997,000 (2010: €898,000) received from an intermediate parent.

Furthermore, expenditure relating to transactions with HSBC Holdings plc and its subsidiaries amounting to €2,838,000 (2010: €3,249,000) for the group and €2,634,000 (2010: €2,618,000) for the bank is included in Employee compensation and benefits and €10,539,000 (2010: €7,952,000) for the group and €9,578,000 (2010: €7,071,000) for the bank is included within General and administrative expenses.

50 Trust and custody activities

The group provides trust and custody services to individuals, trusts, retirement benefit plans and other institutions, whereby it holds and manages assets or invests funds received in various financial instruments at the direction of the customer. The group receives fee income for providing these services. Trust assets and assets held in custody are not assets of the group and are not recognised in the statements of financial position. The group is not exposed to any credit risk relating to such placements, as it does not guarantee these investments.

At 31 December 2011, the total assets held by the group on behalf of customers were €4,036,218,000 (2010: €2,588,033,000).

51 Registered office and ultimate parent company

The addresses of the registered and principal offices of the bank and its subsidiary companies included in the consolidated financial statements can be found in a separate statement which is filed at the Registrar of Companies in accordance with the provisions of the Fourth Schedule to the Companies Act, 1995.

The ultimate parent company of HSBC Bank Malta p.l.c. is HSBC Holdings plc, which is incorporated and registered in England. The registered address is 8 Canada Square, London E14 5HQ, United Kingdom. Copies of the HSBC Holdings plc *Annual Review 2011* and *Annual Report and Accounts 2011* may be obtained from its registered office, from 30 March 2012 or viewed on www.hsbc.com from 27 February 2012.

52 Investor compensation scheme

In accordance with the provisions of the Investor Compensation Scheme Regulations, 2003 issued under the Investment Services Act, 1994, licence holders are required to transfer a variable contribution to an Investor Compensation Scheme Reserve and place the equivalent amount with a bank, pledged in favour of the Scheme. Alternatively licence holders can elect to pay the amount of variable contribution directly to the Scheme.

HSBC Bank Malta p.l.c. and HSBC Stockbrokers (Malta) Limited have elected to pay the amount of the variable contribution directly to the Scheme.

Notes on the Financial Statements (continued)

53 Accounting estimates and judgements

In addition to disclosures set out in notes 4 and 25, the Directors considered the development, selection and disclosure of the group's critical accounting policies and estimates and the application of these policies and estimates. Estimates and judgements are continually evaluated and are based on historical and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Critical accounting judgement in applying accounting policies

i Impairment losses on loans and advances

The group reviews its loan portfolio to assess impairment on an ongoing basis as relevant generic data is observed concerning risks associated with groups of loans with similar risk characteristics (refer to note 3(g)(i)). As a result, the group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans, before the decrease is actually identified with an individual loan in that portfolio. The evidence may include observable data indicating that there has been an adverse change in the relative economic situation of an asset group or in the credit status of borrowers in a group. 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.

ii Policyholder claims and benefits

The determination of the liabilities under long-term insurance contracts is dependent on estimates made by the group. Estimates are made as to the expected number of deaths for each of the years in which the group is exposed to risk. The group bases these estimates on standard industry and national mortality tables that reflect recent historical mortality experience, adjusted where appropriate to reflect the group's own experience. The estimated number of deaths determines the value of the benefit payments and the value of the valuation premiums. The main source of uncertainty is that epidemics such as AIDS, SARS, pandemic flu, swine flu and wide-ranging lifestyle changes, such as in eating, smoking and exercise habits, could result in future mortality being significantly worse than in the past for the age groups in which the group has significant exposure to mortality risk.

Estimates are also made as to future investment income arising from the assets backing long-term insurance contracts. These estimates are based on current market returns as well as expectations about future economic and financial developments.

For long-term insurance contracts with fixed and guaranteed terms and with discretionary participation features, estimates of future deaths, investment returns and administrative expenses form the assumptions used for calculating the liabilities during the life of the contract. A margin for risk and uncertainty is added to these assumptions. New estimates are made each subsequent year to reflect the current long-term outlook.

iii Fair value of derivatives

The fair value of financial instruments that are not quoted in active markets are determined by using valuation techniques. Where valuation techniques (for example models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. All models are certified before they are used, and models are calibrated to ensure that outputs reflect actual data and comparative market prices. To the extent practical, models use only observable data, however areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial instruments.

iv Impairment of available-for-sale equity instruments

The group determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, the group evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology, and operational and financial cash flows.

Independent Auditors' Report to the Members of HSBC Bank Malta p.l.c.

Report on the financial statements

We have audited the financial statements of HSBC Bank Malta p.l.c. (the "bank") and of the group of which the bank is the parent, as set out on pages 29 to 90, which comprise the statements of financial position as at 31 December 2011 and the income statements and statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

As explained more fully in the Directors' Responsibilities Statement set out on page 28, the directors are responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU, the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act"), and the Banking Act, 1994 (Chapter 371, Laws of Malta), and, as regards the financial statements of the Group, Article 4 of the IAS Regulation, and for such internal control as the directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. This report, including the opinion, has been prepared for and only for the Company's members as a body in accordance with Article 179 of the Act, and Article 31 of the Banking Act, 1994 (Chapter 371, Laws of Malta), and may not be appropriate for any other purpose.

In addition, we read the other information contained in the Annual Report 2011 and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent material misstatements of fact or material inconsistencies with the financial statements.

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion on financial statements

In our opinion, the financial statements:

- give a true and fair view of the group's and the bank's financial position as at 31 December 2011, and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU; and
- have been properly prepared in accordance with the Companies Act, 1995 (Chapter 386, Laws of Malta), the Banking Act, 1994 (Chapter 371, Laws of Malta), and, as regards the financial statements of the group, Article 4 of the IAS Regulation.

Independent Auditors' Report to the Members of HSBC Bank Malta p.l.c. (continued)**Report on other legal and regulatory requirements**

Matters on which we are required to report by the Banking Act, 1994 (Chapter 371, Laws of Malta)

In our opinion:

- we have obtained all the information and explanations which, to the best of our knowledge and belief, were necessary for the purpose of our audit;
- proper books of account have been kept by the bank so far as appears from our examination thereof;
- the bank's financial statements are in agreement with the books of account; and
- to the best of our knowledge and belief and, on the basis of the explanations given to us, the financial statements give the information required by law in force in the manner so required.

Matters on which we are required to report by exception by the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act"), other than those reported upon above

We have nothing to report in respect of the following matters where the Act requires us to report to you if, in our opinion:

- the information given in the Report of the Directors for the financial year for which the financial statements are prepared is not consistent with the financial statements; or
- certain disclosures of directors' remuneration specified by the Act are not made.

Report required by Listing Rule 5.98 issued by the Listing Authority in Malta on the Directors' Statement of Compliance with the Code of Principles of Good Corporate Governance (the "Principles") outlined in Appendix 5.1 to Chapter 5 (Continuing Obligations) of the Listing Rules (the "Appendix")

Listing Rule 5.97 requires an Issuer whose securities are admitted to trading on a Regulated Market operating in Malta to prepare a corporate governance statement. In addition, as an Issuer registered in Malta, Listing Rule 5.94 requires that the Issuer endeavours to adopt the Principles and to prepare a report explaining how it has complied with the provisions of the Appendix.

Our responsibility as independent auditors of the bank, is laid down by Listing Rule 5.98, which requires us to issue a report on the Directors' Statement of Compliance with the Principles, which is set out on pages 18 to 25.

We review the Directors' Statement of Compliance, and report as to whether this Statement provides the disclosures required by Listing Rule 5.97. We are not required to, and we do not, consider whether the Board's statements on internal control and risk management systems cover all the risks and controls in relation to the financial reporting process, or form an opinion on the effectiveness of the group's corporate governance procedures or its risks and control procedures, nor on the ability of the group to continue in operational existence.

In our opinion, the Directors' Statement of Compliance set out on pages 18 to 25 provides the disclosures required by Listing Rule 5.97 issued by the Listing Authority of Malta.



Noel Mizzi (Partner) for and on behalf of

KPMG
Registered Auditors
Portico Building
Marina Street
Pietà PTA 9044
Malta

24 February 2012

Group Income Statements and Statements of Comprehensive Income: Five-Year Comparison

Group Income Statements

	2011	2010	2009	2008	2007
	€000	€000	€000	€000	€000
Interest receivable and similar income	175,962	169,012	169,038	245,510	237,580
Interest expense	(46,703)	(46,170)	(64,068)	(122,466)	(111,342)
Net interest income	129,259	122,842	104,970	123,044	126,238
Net non-interest income	65,606	53,346	54,689	65,257	72,453
Operating expenses	(98,200)	(87,605)	(83,769)	(90,409)	(83,672)
Net impairment	(8,250)	(5,496)	(4,429)	(1,907)	(42)
Net provisions for liabilities and other charges	(110)	1	(265)	102	(340)
Profit before tax	88,305	83,088	71,196	96,087	114,637
Tax expense	(30,738)	(29,327)	(25,329)	(32,972)	(38,322)
Profit for the year	57,567	53,761	45,867	63,115	76,315
Profit attributable to shareholders of the bank	57,567	53,761	45,867	63,115	76,315
Earnings per share	19.7c	18.4c	15.7c	21.6c	26.1c

Group Statements of Comprehensive Income

	2011	2010	2009	2008	2007
	€000	€000	€000	€000	€000
Profit attributable to shareholders	57,567	53,761	45,867	63,115	76,315
Other comprehensive income					
Available-for-sale investments:					
– fair value gains	1,193	1,178	17,496	(9,635)	(10,677)
– fair value losses transferred to profit or loss on disposal	2,107	369	(1,071)	(1,348)	(3,537)
– amounts transferred to profit or loss on impairment	4,179	198	–	–	–
Properties:					
– revaluation	–	2,117	–	–	9,789
Income taxes	(2,580)	(699)	(5,749)	3,844	3,800
Other comprehensive income for the year, net of tax	4,899	3,163	10,676	(7,139)	(625)
Total comprehensive income for the year, net of tax	62,466	56,924	56,543	55,976	75,690

Group Statements of Financial Position: Five-Year Comparison

	2011	2010	2009	2008	2007
	€000	€000	€000	€000	€000
Assets					
Balances with Central Bank of Malta,					
Treasury Bills and cash	233,388	379,985	172,671	130,682	472,136
Cheques in course of collection	22,685	9,011	10,764	9,308	3,103
Derivatives	17,136	11,489	11,746	11,823	15,980
Financial instruments designated at fair value	370,080	305,569	248,553	279,714	275,695
Financial investments	936,830	690,606	478,975	429,912	456,525
Loans and advances to banks	637,956	714,901	747,657	1,072,306	631,018
Loans and advances to customers	3,344,224	3,290,435	3,226,477	3,112,240	2,822,315
Intangible assets	89,011	70,655	60,691	64,256	36,110
Property, plant and equipment	60,113	65,487	65,397	70,684	77,820
Investment property	14,598	14,591	14,588	14,050	12,885
Non-current assets held for sale	12,978	9,674	10,604	9,168	11,922
Current tax assets	–	4,712	6,164	2,966	2,596
Deferred tax assets	14,005	10,181	9,053	15,916	11,553
Other assets	31,209	34,425	20,712	25,824	25,855
Prepayments and accrued income	40,629	38,710	33,748	47,239	39,576
Total assets	5,824,842	5,650,431	5,117,800	5,296,088	4,895,089
Liabilities					
Derivatives	17,810	12,311	11,044	11,381	15,043
Deposits by banks	389,170	232,790	168,771	462,185	87,142
Customer accounts	4,402,975	4,462,861	4,086,669	4,016,632	4,039,492
Current tax liabilities	4,134	2,603	207	688	11,043
Deferred tax liabilities	18,113	19,604	18,851	17,600	12,361
Liabilities to customers under investment contracts	16,920	18,962	16,853	15,122	18,947
Liabilities under insurance contracts issued	436,672	410,461	351,513	311,250	290,943
Other liabilities	38,145	33,024	35,479	36,734	32,303
Accruals and deferred income	35,979	34,287	33,422	53,930	53,147
Provisions for liabilities and other charges	11,251	2,548	577	312	414
Subordinated liabilities	87,208	87,150	87,827	87,777	57,962
Total liabilities	5,458,377	5,316,601	4,811,213	5,013,611	4,618,797
Total equity	366,465	333,830	306,587	282,477	276,292
Total liabilities and equity	5,824,842	5,650,431	5,117,800	5,296,088	4,895,089
Memorandum items					
Contingent liabilities	130,763	128,947	119,449	129,925	129,972
Commitments	1,084,509	977,718	923,900	1,110,572	1,148,034

Group Statements of Cash Flows: Five-Year Comparison

	<u>2011</u>	2010	2009	2008	2007
	<u>€000</u>	€000	€000	€000	€000
Net cash from/(used in) operating activities	<u>29,772</u>	103,151	293,498	(309,684)	343,005
Cash flows (used in)/from investing activities					
Dividends received	785	281	387	49	228
Interest received from financial investments	34,624	25,575	16,115	23,884	21,011
Purchase of financial investments	(599,079)	(307,715)	(218,285)	(83,733)	(278,768)
Proceeds from sale and maturity of financial investments	344,079	94,246	187,399	88,551	195,078
Purchase of property, plant and equipment, investment property and intangible assets	(9,031)	(11,038)	(4,174)	(7,556)	(9,981)
Proceeds on sale of property, plant and equipment and intangible assets	2,094	453	2,097	9,755	61
Proceeds on disposal of card acquiring business	11,075	–	–	–	–
Net cash flows (used in)/from investing activities	<u>(215,453)</u>	(198,198)	(16,461)	30,950	(72,371)
Cash flows used in financing activities					
Dividends paid	(30,162)	(30,162)	(32,817)	(50,649)	(93,677)
Maturity of debt securities in issue and subordinated loan stock	–	–	–	–	–
Issue of subordinated loan stock	–	–	–	30,000	58,234
Issue of units to minority interest	–	–	–	–	–
Subordinated loan stock issue costs	–	–	–	(226)	(302)
Net cash used in financing activities	<u>(30,162)</u>	(30,162)	(32,817)	(20,875)	(35,745)
(Decrease)/increase in cash and cash equivalents	<u>(215,843)</u>	(125,209)	244,220	(299,609)	234,889

Group Accounting Ratios: Five-Year Comparison

	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
	%	%	%	%	%
Net interest income and other operating income to total assets	3.3	3.1	3.1	3.6	4.1
Operating expenses to total assets	1.7	1.5	1.6	1.7	1.7
Cost to income ratio	50.4	49.7	52.5	48.0	42.1
Profit before tax to total assets	1.5	1.5	1.4	1.8	2.3
Profit before tax on equity	24.1	24.9	23.2	34.0	41.5
Profit after tax to equity	15.7	16.1	15.0	22.3	27.6
	<u>2011</u>	<u>2010</u>	<u>2009</u>	<u>2008</u>	<u>2007</u>
Shares in issue (millions)	291.8	291.8	291.8	291.8	291.8
Net assets per 30 euro cent share (cents)	125.6	114.4	105.1	96.8	94.7
Earnings per 30 euro cent share (cents)	19.7	18.4	15.7	21.6	26.1
Dividend per 30 euro cent share (cents)					
– gross	15.9	15.9	17.3	26.7	49.4
– net	10.3	10.3	11.2	17.4	32.1
Dividend cover	1.9	1.8	1.4	1.2	0.8

Group Financial Highlights in US dollars

	2011	2010
	US\$000	US\$000
Income statements		
Net operating income	252,048	227,890
Operating expenses	(127,017)	(113,313)
Net impairment	(10,671)	(7,109)
Net provisions for liabilities and other charges	(142)	1
Profit before tax	114,218	107,469
Tax expense	(39,758)	(37,933)
Profit for the year	74,460	69,536
Profit attributable to shareholders	74,460	69,536
Statements of Financial Position		
Assets		
Balances with Central Bank of Malta, Treasury Bills and cash	301,876	491,492
Cheques in course of collection	29,342	11,655
Derivatives	22,165	14,860
Financial assets designated at fair value through profit or loss	478,680	395,238
Financial investments	1,211,743	893,264
Loans and advances to banks	825,164	924,689
Loans and advances to customers	4,325,587	4,256,013
Intangible assets	115,131	91,389
Property and equipment	77,753	84,704
Investment property	18,882	18,873
Assets held for sale	16,786	12,513
Current tax assets	–	6,095
Deferred tax assets	18,115	13,169
Other assets	40,367	44,528
Prepayments and accrued income	52,552	50,069
Total assets	7,534,143	7,308,551
Liabilities and equity		
Derivatives	23,036	15,924
Deposits by banks	503,372	301,102
Customer accounts	5,695,028	5,772,488
Provision for current tax	5,347	3,367
Deferred tax liabilities	23,428	25,357
Liabilities to customers under investment contracts	21,885	24,526
Liabilities under insurance contracts issued	564,813	530,911
Other liabilities	49,340	42,715
Accruals and deferred income	46,538	44,349
Provisions for liabilities and other charges	14,553	3,296
Subordinated liabilities	112,799	112,724
Share capital	113,244	113,244
Revaluation reserve	42,518	37,088
Retained earnings	318,242	281,460
Total liabilities and equity	7,534,143	7,308,551

The US Dollar Exchange as at 31 December 2011 was €1= US\$1.29345. Comparative results have also been translated at these rates.

Branches and Offices

MALTA OFFICES

Registered Office/Head Office

116 Archbishop Street
Valletta VLT 1444
Tel: 2597 0000 Fax: 2380 4923

Retail Banking and Wealth Management

Business Banking Centre
80 Mill Street, Qormi QRM 3101
Tel: 2380 1895 Fax: 2380 4537

Premier Centre**Wealth Management Office**

Business Banking Centre
80 Mill Street, Qormi QRM 3101
Tel: 2148 9100 Fax: 2380 2219

Commercial Banking

Business Banking Centre
80 Mill Street, Qormi QRM 3101
Tel: 2380 1895 Fax: 2380 4532

International Banking Centre

Business Banking Centre
80 Mill Street Qormi
Tel: 2380 1895 Fax: 2380 2676

Trade Services

Business Banking Centre
80 Mill Street, Qormi QRM 3101
Tel: 2380 1828 Fax: 2380 4535

Operations Centre

80 Mill Street, Qormi QRM 3101
Tel: 2380 0000 Fax: 2380 4923

Card Products Division

Operations Centre
80 Mill Street, Qormi QRM 3101
Tel: 2380 2380 Fax: 2380 4924

Contact Centre

Operations Centre
80 Mill Street, Qormi QRM 3101
Tel: 2380 2380 Fax: 2149 0613

Legal Office

32 Merchants Street
Valletta VLT 1173
Tel: 2597 2406 Fax: 2597 2417

Contracts Centre

32 Merchants Street, Valletta VLT 1173
Tel: 2597 3382 Fax: 2597 3306

Inheritance Unit

1st Floor, 32 Merchants Street
Valletta VLT 1173
Tel: 2380 3360/1/2/3/4
Fax: 2380 3365

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Bertu Fenech Square BZN 1032
Tel: 2380 2380 Fax: 2380 1190

Birkirkara

1 Naxxar Road BKR 9049
Tel: 2380 2380 Fax: 2334 1690

Birżebbuġa

2 Birżebbuġa Road BBG 1508
Tel: 2380 2380 Fax: 2361 4790

Buġibba

Bay Square SPB 2511
Tel: 2380 2380 Fax: 2334 7390

Cospicua

50 Pilgrimage Street BML 1580
Tel: 2380 2380 Fax: 2293 4090

Fgura

Council of Europe Square FGR 1254
Tel: 2380 2380 Fax: 2361 8790

Gżira

196 The Strand GZR 1023
Tel: 2380 2380 Fax: 2324 3990

Hamrun

121 St. Joseph Road HMR 1017
Tel: 2380 2380 Fax: 2597 2390

Luqa (Bureau)

Malta International Airport, LQA 9400
Welcomers' Hall
Tel: 2380 2380 Fax: 2180 1938

Airside Arrivals Area (*Automated Office*)

Marsascala

St. Anthony Street MSK 9057
Tel: 2380 2380 Fax: 2163 6860

Mellieħa

6 Gorg Borg Olivier Street MLH 1027
Tel: 2380 2380 Fax: 2334 6890

Mosta

63 Constitution Street MST 9058
Tel: 2380 2380 Fax: 2334 6190

Msida, University of Malta

Room 6, Ground Floor
Humanities Building MSD 2080
Tel: 2380 2380 Fax: 2133 1377

Paola

12 Antoine De Paule Square PLA 1261
Tel: 2380 2380 Fax: 2361 1390

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38 St. Sebastian Street QRM 2331
Tel: 2380 2380 Fax: 2380 5490

Rabat

12 Saqqajja Square RBT 1190
Tel: 2380 2380 Fax: 2334 5890

San Ġwann

198 Naxxar Road SGN 9030
Tel: 2380 2380 Fax: 2324 7590

St. Julians

St. George's Road STJ 3202
Tel: 2380 2380 Fax: 2324 2090

St. Paul's Bay

St. Paul's Street SPB 3419
Tel: 2380 2380 Fax: 2334 6490

Sliema

High Street SLM 1549
Tel: 2380 2380 Fax: 2324 6090

Sliema ShareShop

High Street SLM 1549
Tel: 2380 2381 Fax: 2324 6046

Swieqi

St. Andrews Road SWQ 9020
Tel: 2380 2380 Fax: 2324 8894

Valletta

32 Merchants Street VLT 1173
Tel: 2380 2380 Fax: 2597 3320

Żabbar

19 Sanctuary Street ZBR 1010
Tel: 2380 2380 Fax: 2361 4290

Żebbuġ

254 Main Street ZBG 1304
Tel: 2380 2380 Fax: 2293 4490

Żejtun

25th November Avenue ZTN 2018
Tel: 2380 2380 Fax: 2361 5690

Żurrieq

38 High Street ZRQ 1318
Tel: 2380 2380 Fax: 2361 7890

GOZO OFFICES

Victoria

90 Republic Street VCT 1017
Tel: 2380 2380 Fax: 2293 7192

Victoria ShareShop

90 Republic Street VCT 1016
Tel: 2293 7103 Fax: 2293 7192

Nadur (Agency)

18 St. Peter & St. Paul Square
NDR 1010
Tel: 2380 2380 Fax: 2155 0952

Xaghra (Agency)

8th September Avenue XRA 1011
(Corner with Victory Street)
Tel: 2380 2380 Fax: 2155 6313

SUBSIDIARY COMPANIES

HSBC Global Asset Management (Malta) Ltd

Operations Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 5128 Fax: 2380 5191

HSBC Life Assurance (Malta) Ltd

Business Banking Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 8699 Fax: 2380 8690

HSBC Stockbrokers (Malta) Ltd

Business Banking Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 2211 Fax: 2380 2495

HSBC Securities Services (Malta) Ltd

Operations Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 5157 Fax: 2380 5190

HSBC Insurance Management Services (Europe) Limited

Business Banking Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 8699 Fax: 2380 8690

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