HSBC Bank Malta p.l.c.

Annual Report and Accounts 2014

HSBC

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 6,100 offices in 73 countries and territories in Europe, the Asia-Pacific region, the Americas, the Middle East and Africa.

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Chairman's Statement

Global economic and political conditions remain difficult, and while a small number of international economies are showing signs of some growth, there is no sense, at this stage, of a broad based recovery. European markets generally, and the Eurozone in particular, continue to be stressed, with challenges evident in all the key economies. Deflation is a priority concern for the European Central Bank (ECB) which is seeking means whereby to stimulate growth in the Eurozone while addressing significant issues around unemployment.

The local economy has seen some growth during the year. However the impact of the difficulties in Europe and North Africa are likely to act as a drag for some time to come. With these scenarios in mind, and in order to remain in line with HSBC Group risk parameters, the Board decided to adopt a more cautious approach to our business.

The operating environment for banks globally, and within the Eurozone in particular, has remained quite challenging. Interest rates are at record lows with the ECB applying negative rates of interest for the first time. Loan growth is muted and margins are under pressure. Coupled with the difficult operating environment, regulatory changes in the banking sector, at global, regional, and local levels, have presented the industry with issues around additional complexity, uncertainty, and cost.

Our own business in Malta reflects the challenges in the sector and hence, our decision to adopt a conservative and prudent approach, in the current volatile environment. This has had a direct impact on reported profitability. However the bank's key business lines remain profitable, and its strong capital and liquidity position justifies confidence that it is well positioned to weather the current conditions and benefit from an eventual upturn in the Eurozone.

Is-sitwazzjoni tal-ekonomija u l-politika globali għadha diffiċli, u minkejja li hemm numru żgħir ta' ekonomiji internazzjonali li qed juru l-ewwel sinjali ta' tkabbir, għadu ma jinħassx, f'dan l-istadju, li l-irkupru qiegħed verament jinfirex. Is-swieq Ewropej b'mod ġenerali, u dawk taż-Żona Ewro b'mod partikolari, għadhom jitħabtu biex jirpiljaw, taħt l-istress ta' sfidi li jidhru ċar fl-ekonomiji ewlenin kollha. Id-deflazzjoni hija fuq quddiem nett fost il-materji li qed iħassbu lill-Bank Ċentrali Ewropew (l-ECB), li qed jara kif jagħmel biex jistimula t-tkabbir fiż-Żona Ewro waqt li jindirizza l-problemi serji relatati mal-qgħad.

Matul is-sena kien hemm xi tkabbir anke fl-ekonomija lokali. Madankollu d-diffikultajiet fl-Ewropa u fl-Afrika ta' Fuq x'aktarx jibqgħu jservu ta' forza kuntrarja għal xi żmien 'il quddiem. B'dan ix-xenarju quddiemu, u bil-għan li jżomm mal-parametri ta' riskju tal-Grupp HSBC, il-Bord iddeċieda li jadotta politika ta' aktar kawtela fin-negozju tagħna.

L-ambjent operattiv li jaħdmu fih il-banek madwar id-dinja, u speċjalment dawk fiż-Żona Ewro, għadu jippreżenta sfidi kbar. Ir-rati tal-imgħax niżlu f'livelli rekord, bl-ECB saħansitra japplika rati negattivi għall-ewwel darba. It-tkabbir fis-self kważi xxejjen, u l-marġni qegħdin taħt pressjoni. U magħqud mal-ambjent operattiv diffiċli sar tibdil fir-regolamenti tas-settur bankarju, fuq livelli globali, reġjonali u lokali, li ġab miegħu lill-industrija problemi ta' żieda fil-komplessità, l-inċertezza u l-ispejjeż.

L-operat tagħna f'Malta jirrifletti l-isfidi li hemm fis-settur. Huwa għalhekk li ddeċidejna li nadottaw linja prudenti u konservattiva meta l-ambjent attwali huwa volatili. Dan kollu kellu impatt dirett fuq il-profittabilità rrapportata. Madankollu l-attività ċentrali tal-bank għadha profitabbli, u li l-pożizzjoni soda tal-kapital u l-likwidità tal-kumpanija jiġġustifikaw il-fiduċja

Results

Profit before taxation was €52m, a decrease of €38m or 42%, when compared to the results in 2013. Profit attributable to shareholders was down 43%, to €34m compared to the previous year, resulting in earnings per share of 10.4 cents.

The key contributors to the decline in profitability were a €19m increase in loan impairment charges resulting principally from lower valuations on the legacy commercial property portfolio, a €14m decrease in income associated with the current operating environment, and a €5m rise in costs due to additional compliance investments and regulatory fees.

On an underlying basis, operating profits, before provisions and excluding significant notable items (investment sales, ECB Comprehensive Assessment costs, together with lower insurance company releases) were 12% down on prior year.

Based on this performance, the Board is recommending a final gross dividend of 2.6 cent per share (1.7 cent net of tax). Together with the interim gross dividend of 4.5 cent per share paid out in September 2014, the total dividend for the year is 7.1 cent per share (4.6 cent net of tax). The Board is also recommending a bonus issue of 1 share for every 9 shares held as on 29 April 2015 through the capitalisation of reserves amounting to €11m. This will increase share capital from €97m to €108m.

The bank's dividend policy and distribution percentage remain unchanged from 2013. Similar to what happened in 2013, actual dividends in the hands of shareholders will be negatively impacted by the revised Malta Financial Services Banking Rule 09. This Rule, which regulates all banks in Malta, came into effect on 31 December 2013. According to the provisions of this Banking Rule, banks in Malta are, inter alia, required to hold additional reserves against non-performing loans.

Banks are obliged to determine the dividends that they intend to distribute to shareholders, and then hold back a portion of these dividends in the form of a reserve which is then included in the Tier 1 capital disclosed on their balance sheet. While the rule will not impact notional dividend pay-out rates, it will have an adverse effect on the amount of actual cash that banks can distribute to shareholders. HSBC Bank Malta is fully compliant with the provisions of Banking Rule 09.

Strategy

The HSBC Group's strategy is to become the world's leading international bank. The three key priorities under this strategy are: to grow the business, simplify operating

tagħna li l-bank jinsab f'qagħda tajba biex jiffaċċa l-kondizzjonijiet eżistenti, u biex igawdi vantaġġ meta ż-Żona Ewro terġa' taqbad it-triq 'il fuq.

Riżultati

Il-profitt qabel it-taxxa kien ta' €52m, tnaqqis ta' €38m, (42%), meta mqabbel mar-riżultat tal-2013. Il-profitt attribwibbli lill-azzjonisti niżel bi 43%, għal €34m meta mqabbel mas-sena ta' qabel. Dan ifisser li l-qligħ sehem b'sehem kien ta' 10.4 ċenteżmi.

Il-fatturi ewlenin li wasslu biex il-profitti jonqsu kienu ż-żieda ta' €19m fl-indeboliment tas-self, ikkawżata l-aktar għaliex tbaxxew l-istimi tal-proprjetà kummerċjali f'portafoll li ilu żmien f'idejn il-bank, it-tnaqqis ta' €14m fid-dħul mill-imgħax, riżultat tal-ambjent operattiv kurrenti, u l-ispejjeż addizzjonali ta' €5m minħabba l-investimenti meħtieġa biex jassiguraw konformità u ħlasijiet marbutin mal-obbligi regolatorji.

Jekk inħarsu lejn il-profitti mill-operat qabel il-provedimenti u bl-esklużjoni tat-transazzjonijiet ta' darba (bejgħ ta' investimenti, spejjeż tal-ECB Comprehensive Assessment, flimkien ma' rilaxxi aktar baxxi tal-kumpanija tal-assigurazzjoni), naraw li dawn kienu 12% inqas minn tas-sena l-oħra.

Abbażi ta' dawn ir-riżultati, il-Bord qed jirrakkomanda dividend finali gross ta' 2.6 ċenteżmi kull sehem (1.7 ċenteżmi wara t-taxxa). Magħdud mad-dividend interim gross ta' 4.5 ċenteżmi mħallas f'Settembru 2014, id-dividend totali għas-sena huwa ta' 7.1 ċenteżmi kull sehem (4.6 ċenteżmi wara t-taxxa). Il-Bord qed jirrakkomanda wkoll il-ħruġ bonus ta' sehem wieħed għal kull disa' ishma miżmuma fid-data tad-29 ta' April 2015, li jsir billi jiġu kkapitalizzati riżervi li jammontaw għal €11m. B'dan il-pass il-kapital azzjonarju jitla' minn €97m għal €108m.

Il-politika tad-dividendi u l-perċentwal ta' tqassim li adotta l-bank baqgħu kif kienu fl-2013. Kif ġara fl-2013, l-ammont attwali tad-dividend f'idejn l-azzjonisti se jintlaqat ħażin bir-Regola Bankarja Nru 09 tal-Awtorità tas-Servizzi Finanzjarji (l-MFSA) kif riveduta. Din ir-Regola, li tapplika għall-banek kollha f'Malta, daħlet fis-seħħ fil-31 ta' Diċembru 2013. Skont id-dispożizzjonijiet ta' din ir-Regola Bankarja, il-banek f'Malta huma obbligati, fost ħwejjeġ oħra, li jżommu riżervi addizzjonali biex jilqgħu għal self li ma jkunx qed jitħallas lura kif miftiehem.

Barra minn hekk, il-banek huma obbligati jistabilixxu d-dividendi li jkun bi ħsiebhom iqassmu lill-azzjonisti, imbagħad iżommu porzjon minn dawk id-dividendi fil-forma ta' riżerva li tiġi magħduda mal-kapital tal-Ewwel Saff li jidher fil-karta tal-bilanċ. Filwaqt li din processes and structures, and implement common standards across the globe in relation to financial crime and regulatory compliance.

Our strategy in Malta remains closely aligned to that of the HSBC Group. With respect to growth, the focus remains on assisting Maltese companies to access international markets and attracting high quality inward investment into Malta. The flagship HSBC Malta Trade for Growth initiative has turned out to be a significant success, with the underlying €50m fund taken up in nine months. Plans are now underway to launch a follow-on fund.

Initiatives to simplify our business have concentrated on achieving savings by streamlining processes, and investing in technology, as well as in our people. In addition to these initiatives, we have sought ways to improve customer access to our services, through the launch of the new and highly innovative Mobile Banking App. We have also upgraded our Commercial Banking online platform HSBCNet, and released our innovative GetRate system, which allows our commercial customers to buy foreign exchange online.

To continue improving our alignment with the HSBC Group's standards on financial crime and regulatory compliance, we have made significant investments throughout 2014. As a result the bank is now well positioned to meet the very considerable increase in regulatory expectations in this area.

Regulatory changes

Global regulatory changes remain a major area of concern throughout the financial services sector, requiring sustained and substantial investment. A recent survey in a

ir-regola m'għandhiex impatt fuq ir-rati nozzjonali tad-dividendi mħallsa, se tolqot ħażin l-ammont reali tal-flus li l-banek jistgħu jqassmu lill-azzjonisti. HSBC Bank Malta huwa totalment konformi mal-provedimenti tar-Regola Bankarja Nru 09.

Strateġija

L-istrateġija tal-Grupp HSBC hija li jsir l-aqwa bank internazzjonali fid-dinja. Hemm tliet prijoritajiet fil-qofol ta' din l-istrateġija, li huma: it-tkabbir tan-negozju, is-simplifikazzjoni tal-proċessi u l-istrutturi operattivi, u l-implimentazzjoni ta' standards komuni madwar id-dinja għar-rigward tar-reati finanzjarji u tal-konformità mar-regolamenti.

L-istrateġija tagħna f'Malta tibqa' miexja fil-qrib mal-linja li ħa l-Grupp HSBC. Għal dak li hu tkabbir, nibqgħu iffokati biex ngħinu lill-kumpaniji Maltin jidħlu fi swieq internazzonali u biex nattiraw investiment ta' kwalità lejn Malta. L-inizzjattiva ewlenija tal-HSBC, il-Malta Trade for Growth, irnexxielha tikseb suċċess ġmielu, bil-fond disponibbli ta' €50m jittieħed fi żmien disa' xhur. Issa diġà hemm pjani biex invaraw fond ieħor li jkompli miegħu.

L-inizzjattivi biex nissimplifikaw in-negozju kienu kkonċentrati fuq il-mira li niffrankaw mill-ispejjeż billi nirrazzjonalizzaw il-proċessi u ninvestu aktar fit-teknoloġija kif ukoll fin-nies tagħna. Flimkien ma' dawn l-inizzjattivi fittixna wkoll modi kif intejbu l-aċċess tal-klijenti għas-servizzi tagħna, billi inawgurajna servizz ġdid u tassew innovattiv, il-Mobile Banking App. Fl-istess ħin għollejna l-livell tal-HSBCNet, li huwa l-pjattaforma *online* tas-servizzi bankarji kummerċjali tagħna, u varajna s-sistema innovattiva GetRate, li tippermetti lill-klijenti kummerċjali tagħna li jixtru l-kambju *online*.

Former Italian Prime Minister and European Commissioner Mario Monti (centre) is flanked by senior bank officials along with Deputy Prime Minister Louis Grech during the first ever The Economist Business Roundtable, which HSBC Malta supported.

Eurozone market, not dissimilar to Malta, indicated that on average regulation accounts for 41% of the investment expenditure of banks, and some 10% of their total staff complement. The changes underway are likely to result in a permanently higher cost environment for banks, and other financial institutions.

Significant regulatory changes that have taken place or are underway include:

- Prudential regulation – Capital Requirements Directive IV and Regulations including the rules governing the Asset Quality Review
- Market regulation – European Market Infrastructure Regulation (EMIR), Directive on Markets in Financial Instruments (MiFID 2), Packaged Retail and Insurance-based Investment Products (PRIIPs) and Anti-Money Laundering Directive (AML IV)
- Fund regulation – Alternative Investment Fund Managers Directive (AIFMD) and Undertakings for Collective Investment in Transferable Securities Directive (UCITS V)
- Tax regulation – Foreign Account Tax Compliance Act (FATCA) and Common Reporting Standards (CRS)
- Payment regulation – Single European Payments Area (SEPA) and Payments Services Directive (PSD II)

In addition to the above, the ECB is currently in the process of rolling out guidelines on national deposit compensation schemes, establishing new rules in relation to a Eurozone-wide bank resolution fund and determining the fees that it will charge for its new oversight responsibility. These changes are expected to have significant cost implications for banks.

In 2014 regulatory costs rose substantially. This was driven by the cost of the ECB Comprehensive Assessment which was in excess of €3.0 million, and a near doubling of Malta Financial Services Authority fees.

In November the bank's lead supervisor changed from the MFSA to the ECB. Regulatory exchanges and guidance now take place through a Joint Supervisory Team based in Frankfurt. The team is chaired by the ECB but made up of members drawn from both the ECB and the MFSA.

As part of this change at the Regulator level, HSBC Bank Malta, and two other local banks, underwent the Comprehensive Assessment process during the year under review. This was a very challenging exercise in terms of resources, time, and expense. The focus of the review was on the capital standing of the banks undergoing the exercise. I was pleased to note the dedication and professionalism of the HSBC team involved in the process. The bank performed strongly,

Għar-rigward tar-reati finanzjarji u l-konformità regolatorja, ħadna passi biex nissintonizzaw aktar mal-istandards tal-Grupp HSBC billi għamilna investiment qawwi f'dan il-qasam matul l-2014. Riżultat ta' dan, il-bank issa jinsab attrezzat tajjeb biex jissodisfa ż-żieda konsiderevoli li kien hemm fl-aspettativi regolatorji f'dan il-qasam.

Bidliet regolatorji

It-tibdil li jsir fir-regolamenti globalment għadu qed ikun raġuni ta' tħassib fis-settur kollu tas-servizzi finanzjarji, minħabba l-investiment qawwi u kontinwu li jeħtieġ. Minn stħarriġ reċenti f'wieħed mis-swieq taż-Żona Ewro, li jixbah lil dak ta' Malta, deher li bħala medja 41% tal-ispiża fl-investiment tal-banek, u madwar 10% tal-impjegati tagħhom, huma ddedikati biss għar-regolamentazzjoni. It-tibdil li għadu għaddej jista' jġib miegħu sitwazzjoni permanenti ta' spiża ogħla għall-banek, kif ukoll għall-istituzzjonijiet finanzjarji l-oħra.

Tibdiliet sinjifikanti li saru jew għadhom qed isiru fir-regolamenti jinkludu:

- Regolamenti ta' prudenza – Id-Direttiva Nru IV tar-Rekwiżiti tal-Kapital u r-regolamenti li jinkludu r-regoli fuq ir-Reviżjoni tal-Kwalità tal-Assi
- Regolamenti tas-suq – Ir-Regolament tal-Infrastruttura tas-Suq Ewropew (EMIR), id-Direttiva għas-Swieq tal-Istrumenti Finanzjarji (MiFID 2), Pakketti ta' Prodotti ta' Investimenti Immirati għall-Konsumatur jew Ibbażati fuq Assigurazzjoni (PRIIPs) u d-Direttiva Kontra l-Ħasil tal-Flus (AML IV)
- Regolamenti għall-Fondi – Id-Direttiva għall-Managers ta' Fondi ta' Investiment Alternattiv (AIFMD) u d-Direttiva dwar l-Impriżi għall-Investiment Kollettiv f'Titoli Trasferibbli (UCITS V)
- Regolamenti tat-taxxa – L-Att dwar il-Konformità mat-Taxxa fuq Kontijiet Barranin (FATCA)
- Regolamenti tal-ħlas – Iż-Żona Unika għall-Pagamenti bl-Ewro (SEPA) u d-Direttiva dwar is-Servizzi ta' Pagament (PSD II)

Apparti dan kollu, l-ECB qiegħed fil-proċess li joħroġ linji gwida dwar l-iskemi nazzjonali ta' kumpens għad-depożitanti, filwaqt li jistabilixxi regoli ġodda għal fond ta' riżoluzzjoni għall-banek fil-firxa kollha taż-Żona Ewro u jiddetermina x'inhuma l-ispejjeż għar-responsabbiltà ġdida ta' sorveljanza li għandu. Dawn il-bidliet mistennija jkollhom implikazzjonijiet serji fuq l-ispiża tal-banek.

Fl-2014, l-ispejjeż regolatorji żdiedu drastikament. Dan wasal minħabba l-ispejjeż marbuta mal-Comprehensive Assessment tal-ECB u l-ispejjeż tal-Awtorità Maltija għas-Servizzi Finanzjarji li kważi rduppjaw.

with its key capital ratios significantly above the ECB benchmark requirements.

Sustainability

While conscious of the prevailing challenging times, the bank remains committed to its community activities. These align with the organisation's values and our listing requirements.

The key areas of focus are education, particularly of children, environment and heritage. The principal heritage initiatives are the restoration of the Church of Our Lady of Victories in Valletta, in conjunction with Din l-Art Ħelwa; and the Notarial Archives, which contain so much of Malta's rich history.

The leading environmental initiative, funded by a €500,000 grant from the HSBC Group, has been the Catch the Drop campaign. The initiative aims to reach every single student in the country during a three year period (nearly 50,000 in total), as well as all the Local Councils in Malta and Gozo. It raises awareness about water scarcity and provides information and suggestions about how people can tackle it. Key to the success of the programme is the on-going involvement of HSBC staff members. During the scholastic year of 2013/14 over 300 presentations were given to 19,000 students involving more than 200 staff volunteers.

As a result of the work on the Catch the Drop campaign the bank was awarded the Corporate Volunteering Award for 2014 by the Malta Council for the Voluntary Sector.

F'Novembru, is-sorveljanza ewlenija tal-bank imxiet minn għand l-MFSA għal għand l-ECB. Komunikazzjonijiet u gwida li għandhom x'jaqsmu mar-regolamenti issa qed isiru permezz ta' Tim Konġunt ta' Sorveljanza ibbażat fi Frankfurt u magħmul minn membri tal-ECB u tal-MFSA. Iċ-Chairman ta' dan it-tim huwa membru tal-ECB.

Bħala parti mill-bidla fuq il-livell ta' Regolatur, l-HSBC Bank Malta, flimkien ma' żewġ banek lokali oħra, għadda mill-proċess ta' Comprehensive Assessment matul is-sena li qed nitkellmu dwarha. Dan kien eżerċizzju ta' sfida qawwija f'dawk li huma riżorsi, ħin u spejjeż. L-eżami kien ikkonċentrat fuq il-qagħda tal-kapital tal-banek li kienu soġġetti għal dan l-eżerċizzju. Ħadt pjaċir ninnota d-dedikazzjoni u l-professjonaliżmu tal-membri tal-HSBC li kienu involuti fil-proċess. Il-bank ħareġ b'riżultati sodi, li wrew li r-relazzjonijiet ewlenin tal-kapital tal-bank kienu 'l fuq sew minn dawk rekwiżiti bħala n-norma tal-ECB.

Sostenibilità

Waqt li l-bank huwa konxju tal-isfidi li qed jiddominaw f'dawn iż-żminijiet, hu jibqa' dejjem jimpenja ruħu għall-attività fil-komunità. Din il-ħidma hija fi qbil mal-valuri tagħna u mar-rekwiżiti tas-sħubija fil-Borża.

L-oqsma ewlenin li niffokaw fuqhom huma l-edukazzjoni, speċjalment tat-tfal; l-ambjent; u l-patrimonju Malti. L-inizzjattivi prinċipali fil-qasam tal-patrimonju huma r-restawr tal-Knisja tal-Vitorja fil-Belt, li qed jitwettaq fi proġett konġunt ma' Din l-Art Ħelwa; u l-Arkivji Notarili, li fihom hemm tant rikkezza dwar l-istorja ta' Malta.

During the academic year of 2013-2014, staff volunteers for the HSBC Water Programme conducted 305 presentations for 19,438 students – nearly half of the total number the programme aims to reach by 2016.

HSBC Malta won the Corporate Volunteering Award 2014 by the Malta Council for the Voluntary Sector in recognition of mobilising hundreds of staff.

With respect to education, the bank is working closely with the Prince's Trust of the United Kingdom, the Office of the President, and the Education Ministry. Our objective is to attract the Prince's Trust to Malta, to work alongside young people with challenging backgrounds. The Prince's Trust has had significant success in the United Kingdom and it is very much hoped to leverage that success in Malta.

Board

During 2014, there were two changes in our Board of Directors.

Mr James Dunbar Cousin and Mr Ranjit Gokarn stepped down from their directorships. I would like to thank these gentlemen for their excellent work and dedication to the bank.

We have been pleased to welcome the following new members who joined during the year: Mr Christopher Davies and Prof. Juanito Camilleri.

Mr Christopher Davies is presently Chief Executive Officer International, HSBC Bank plc and a former Deputy Chief Executive Officer and Executive Director, of HSBC Bank China. Mr Davies has been with HSBC for nearly 30 years and has held senior appointments in the HSBC Group in a number of different business lines, and in various countries.

Prof. Juanito Camilleri is Vice Chancellor (Rector) of the University of Malta and Chairman of the University Group of Companies. He is also Chairman of the Centre for Entrepreneurship and Business Incubation, Chairman of the Centre for the Liberal Arts and Sciences, and Chairman of the Centre for Molecular and Bio-Banking. Prof. Camilleri is a member of the bank's Nomination and Remuneration Committee.

L-inizzjattiva ewlenija ambjentali kienet il-kampanja Catch the Drop, iffinanzjata b'għotja ta' €500,000 mill-Grupp HSBC. Il-mira ta' din l-inizzjattiva hi li tilħaq lil kull wieħed mill-istudenti fil-pajjiż fi żmien tliet snin (madwar 50,000 b'kollox), kif ukoll il-Kunsilli Lokali kollha f'Malta u Għawdex. Il-kampanja toħloq kuxjenza dwar l-iskarsità tal-ilma u tagħti informazzjoni u suġġerimenti kif nistgħu nittrattaw il-problema. Fil-qofol tas-suċċess tal-programm hemm l-involviment kontinwu tal-ħaddiema tal-HSBC. Matul is-sena skolastika 2013/14 kien hemm 'il fuq minn 200 voluntier mill-HSBC li taw aktar minn 300 preżentazzjoni lil 19,000 student.

Riżultat tal-ħidma fil-kampanja Catch the Drop il-bank ġie ppremjat bil-Corporate Volunteering Award għall-2014 mill-Kunsill Malti tas-Settur Volontarju.

Għar-rigward tal-edukazzjoni, il-bank qed jaħdem fil-qrib mal-Prince's Trust tar-Renju Unit, mal-Uffiċċju tal-President u mal-Ministeru tal-Edukazzjoni. Il-mira tagħna hi li niġbdu l-Prince's Trust lejn Malta, biex taħdem ma' żgħażagħ li ġejjin minn ambjenti ta' sfida. Il-Prince's Trust kellha suċċess tajjeb fir-Renju Unit u t-tama hi li jirnexxilha jkollha l-istess suċċess f'Malta.

Il-Bord

Matul l-2014 saru żewġ bidliet fil-Bord tad-Diretturi.

Is-Sur James Dunbar Cousin u s-Sur Ranjit Gokarn irtiraw mill-post ta' diretturi. Nixtieq nirrigrazzja lil dawn iż-żewġ sinjuri tax-xogħol eċċellenti u d-dedikazzjoni tagħhom lejn il-bank.

Kien pjaċir tagħna nilqgħu żewġ membri ġodda li ngħaqdu mal-Bord fl-2014: is-Sur Christopher Davies u l-Professur Juanito Camilleri.

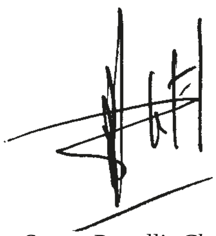
I am privileged to be the Chairman of a Board whose members have a wealth of knowledge and experience, at both local and international levels. While guiding the organisation my colleagues and I are vigilant that the decisions we take ensure benefits to our shareholders, the community, and our people.

Looking ahead

The current difficult environment is likely to remain with us for at least the medium term. However, I remain confident that with our strong Board, experienced executive team, and focused staff, we are in a position to move the bank forward and continue to fulfil our customers' expectations, both locally and internationally. The objective remains to build a business around long term sustainability. The difficult decisions that we have taken during 2014 support this priority.

We remain proud to be an important part of HSBC Group, the world's leading international bank, and will continue to leverage the very considerable benefits that the Group offers our business in Malta.

My appreciation and gratitude goes to the staff of the bank, for their commitment and hard work, alongside the management team, and the Board of Directors. I also thank our shareholders and our customers for continuing to place their trust in the long term future of this organisation.



Sonny Portelli, *Chairman*
23 February 2015

Is-Sur Christopher Davies hu attwalment il-Kap Eżekuttiv Internazzjonali tal-HSBC Bank plc u qabel kien Deputat Kap Eżekuttiv u Direttur Eżekuttiv tal-HSBC Bank China. Is-Sur Davies ilu kważi 30 sena mal-HSBC u okkupa pożizzjonijiet għoljin fil-Grupp HSBC f'għadd ta' setturi differenti u f'bosta pajjiżi.

Il-Professur Juanito Camilleri huwa Viċi Kanċillier (Rettur) tal-Università ta' Malta u Chairman tal-Grupp ta' Kumpaniji tal-Università. Huwa wkoll Chairman taċ-Ċentru tal-Intrapriża u Trawwim tan-Negozju, Chairman taċ-Ċentru għall-Arti u Xjenzi Liberali, u Chairman taċ-Ċentru għall-Mediċina Molekulari u l-Bijobanek. Il-Professur Camilleri huwa membru tal-Kumitat tal-bank għan-Nominazzjonijiet u r-Remunerazzjoni.

Huwa privileġġ tiegħi li nkun Chairman ta' Bord li l-membri tiegħu għandhom tant għerf u esperjenza, sew fuq livell lokali kemm fuq dak internazzjonali. Aħna u niggwidaw din l-Organizzazzjoni jien u l-kollegi tiegħi nkunu dejjem attenti li d-deċiżjonijiet li nieħdu jkunu tal-aħjar benefiċċju għall-azzjonisti, għall-komunità u għan-nies tagħna.

Inħarsu 'l quddiem

L-ambjent diffiċli ta' bħalissa x'aktarx li jibqa' magħna għall-anqas għal tul ta' żmien medju. Madankollu meta nqis il-Bord sod li għandna, l-esperjenza tal-eżekuttivi u l-ħidma ffokata tal-ħaddiema tagħna, jien għadni fiduċjuż li aħna f'pożizzjoni tajba biex immexxu l-bank 'il quddiem u nkomplu nilħqu l-aspettattivi tal-klijenti tagħna, sew f'Malta kemm barra. L-għan jibqa' dejjem li nibnu negozju li jibqa' sostenibbli fit-tul. Id-deċiżjonijiet diffiċli li ħadna fl-2014 isostnu din il-prijorità.

Aħna nibqgħu kburin li nifformaw parti mill-Grupp HSBC, li hu fuq quddiem nett fost il-banek internazzjonali tad-dinja. Aħna bi ħsiebna nibqgħu nibbenefikaw mill-vantaġġi kbar li l-Grupp joffri lin-negozju tagħna f'Malta.

Irrid nesprimi l-apprezzament u l-gratitudni tiegħi lejn il-ħaddiema tal-bank għall-impenn u l-ħidma soda tagħhom, id f'id mat-tim tal-management u mal-Bord tad-Diretturi. Irrid nirringrazzja wkoll lill-azzjonisti u lill-klijenti tagħna tal-fiduċja kontinwa li huma għandhom fil-futur fit-tul ta' din l-organizzazzjoni.

Chief Executive Officer's Review

2014 was a year of material challenges on a number of fronts. Operating conditions and a changing regulatory environment have each had their own significant impact. Nevertheless the underlying performance of the key business lines has shown resilience and I am confident that our prudent approach to risk will serve us well in the long term.

HSBC has an excellent franchise in Malta and the hard work and dedication of the bank's team during the past year needs to be recognised. Despite the difficult operating conditions, we continue to invest in the bank and to build a long term sustainable business that will serve the best interest of our customers, our staff, our shareholders and the community in which we work.

Performance

HSBC Bank Malta delivered a profit before tax of €52m for the year ended 31 December 2014. This was a decline of €38m or 42% on the prior year.

On an underlying basis, operating profits before provisions and excluding notable items (investment sales, ECB Comprehensive Assessment costs and lower insurance technical reserve releases), were 12% down on prior year.

All three main business lines – Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets – were profitable during the year under review.

Net interest income reduced by 4% to €120m compared with €125m in 2013. The fall in interest income was mainly impacted by: a tightening in interest margin earned on the loan portfolio; lower average lending balances associated with muted loan growth and higher loan repayments; and a decline in interest

L-2014 kienet sena ta' sfidi materjali minn għadd ta' aspetti. Il-kondizzjonijiet li fihom qed noperaw u l-ambjent ta' bidla fir-regolamenti kellhom it-tnejn effetti notevoli. B'danakollu l-prestazzjoni bażika tal-linji kummerċjali ewlenin tagħna żammet fuq sisien sodi u jiena fiduċjuż li l-prudenza li qed naħdmu biha se tibqa' taqdina tajjeb.

L-HSBC għandu negozju eċċellenti f'Malta, u rridu nirrikonoxxu l-ħidma soda u d-dedikazzjoni tal-ħaddiema tal-bank matul is-sena li għaddiet. Minkejja l-kondizzjonijiet diffiċli tal-operat, aħna għadna ninvestu fil-bank u nibnu negozju li huwa sostenibbli fit-tul u li jaqdi l-aħjar interessi tal-klijenti, tal-impjegati, tal-azzjonisti u tal-komunità li noperaw fiha.

Riżultati

L-HSBC Bank Malta ħalliet profitti qabel it-taxxa ta' €52m għas-sena li għalqet fil-31 ta' Diċembru 2014. Dan ifisser li ċ-ċifra kienet €38m jew 42% inqas minn dik tas-sena ta' qabel.

Fuq bażi fondamentali, il-profitti mill-operat qabel il-provvedimenti u bl-esklużjoni tat-transazzjonijiet ta' darba (bejgħ ta' investimenti, spejjeż tal-ECB Comprehensive Assessment, flimkien ma' rilaxxi aktar baxxi tal-kumpanija tal-assigurazzjoni) kienu 12% inqas minn tas-sena ta' qabel.

It-tliet linji kummerċjali ewlenin – ir-Retail Banking and Wealth Management, il-Commercial Banking u l-Global Banking and Markets – kollha għamlu profitt matul is-sena.

Id-dħul nett mill-imgħaxijiet niżel b'4% għal €120m imqabbel ma' €125m fl-2013. It-tnaqqis fid-dħul mill-imgħax ġara għal tliet fatturi: kien hemm issikkar tal-marġni fir-rati tal-imgħax fuq is-self; tbaxxiet il-medja tal-bilanċji mislufa, b'rabta ma' żieda x'aktarx kajmana

The AGM approved a board recommendation for a bonus share issue of one new share for every nine shares held by registered shareholders.

earned on investments as the proceeds of higher yielding maturing bonds were reinvested at lower rates. This was partially mitigated by a fall in the cost of funds as customers moved to shorter-dated deposits and deposit rates declined.

Net fee and commission income of €28 million was broadly in line with 2013. The fee and commission income performance was generally positive but the overall result was impacted by the winding down of the fund administration and custody business in early 2014.

HSBC Life Assurance (Malta) Limited reported a profit before tax of €9m compared with €13m in 2013. While new insurance business was 10% higher than the prior year, the result in 2014 was negatively impacted by downward yield curve movements and lower technical reserve releases.

A net gain of €2m was reported as a result of a repositioning of the investment portfolio compared to €4m in 2013.

Operating expenses of €98m were €5m or 6% higher compared with the previous year. 2014 expenses were impacted by additional compliance and regulatory costs of €5m associated with the build-up of the Compliance function, the ECB Comprehensive Assessment, higher regulatory fees and an increase of €1m in early voluntary retirement costs. Excluding these incremental costs, expenses were held flat to 2013 despite a 2.5% increase in staff salaries and the impact of inflation. Continued investment to improve technology was funded by savings from simplification and re-engineering of processes.

fil-portafoll tas-self u ma' ħlasijiet lura aktar mgħaġġla; u naqas l-imgħax mill-investimenti hekk kif bonds b'rati għolja bdew jimmaturaw u l-investiment fihom tpoġġa f'oħrajn b'rati aktar baxxi. Dan kollu ttaffa xi ftit billi naqas il-kost tal-fondi hekk kif il-klijenti għażlu aktar id-depożiti ta' skadenza qasira u waqgħu r-rati tal-imgħax fuq id-depożiti.

Id-dħul nett ta' €28m mid-drittijiet u l-kummissjonijiet kien bejn wieħed u ieħor bħal tal-2013. Id-dħul mid-drittijiet u l-kummissjonijiet kien ġeneralment tajjeb, madankollu l-prestazzjoni tagħna kienet milquta ħażin bil-ħruġ tagħna mix-xogħol tas-servizzi ta' sikurezza u kustodja fil-bidu tal-2014.

L-HSBC Life Assurance (Malta) irrapportat profitt qabel it-taxxa ta' €9m imqabbel ma' €13m fl-2013. Waqt li x-xogħol ġdid fl-assigurazzjoni kien ta' 10% ogħla minn tas-sena ta' qabel, ir-riżultat tal-2014 intlaqat b'mod negattiv minn redditi aktar baxxi fuq il-portafoll tal-investimenti u minn riduzzjoni fir-rilaxxi ta' darba mir-riżervi tekniċi.

Ġie rapportat qligħ nett ta' €2m bħala riżultat ta' ċaqliq fil-portafoll tal-investimenti. Dan kien €4m aktar baxx minn tal-2013.

L-ispejjeż tal-operat telgħu għal €98m, li huma €5m jew 6% ogħla meta mqabbla ma' tas-sena ta' qabel. L-ispejjeż tal-2014 batew l-effett ta' piżijiet addizzjonali ta' €5.6m relatati mar-regolamentazzjoni u l-obbligi ta' konformità. Dawn kienu marbuta mat-tisħiħ tal-funzjoni ta' konformità, mal-Comprehensive Assessment tal-ECB, maż-żieda fl-ispejjeż regolatorji tal-MFSA, u ma' ħlasijiet ta' €1m għal min irtira minn jeddu qabel iż-żmien.

The cost efficiency ratio, that compares operating expenses to net operating income, was at 57% compared with 50% in 2013.

Loan impairment charges were €23m compared to €3m in 2013. As noted by the Chairman, in the current challenging environment the Board adopted a cautious approach to existing legacy non-performing commercial loans. This was particularly the case where lower valuations were received from bank approved architects on property held as security for loans. Overall, however, asset quality remains good with a high percentage of tangible security held against the bank's loan portfolio.

Gross new lending to customers increased by 19% to €710m (2013: €597m). This reflects the bank's continued support to the local economy. However, net loans and advances to customers at €3,273m were in line with 2013. In the current low interest rate environment there has been heightened tendency for customers, both commercial and retail, to use excess funds to repay loans early. The mortgage book, the bank's largest lending portfolio, continued to show positive net growth.

Deposits were up to €4,867m, an increase of 8% from 31 December 2013 despite continued competitive pressures.

The bank's available-for-sale investment portfolio is well diversified and conservatively positioned. All investments are rated BBB+ or better.

The bank's liquidity position is strong with an advances-to-deposit ratio of 67%, compared with 73% at 31 December 2013.

During 2014, the bank continued to grow its Tier 1 capital ratio and this improved from 9.9% (re-stated under CRD IV from a reported 9.4%) to 10.6%.

Profit attributable to shareholders was down 43% to €34m compared with the previous year resulting in earnings per share of 10.4 cents. The Board is recommending a final gross dividend 2.6 cent per share (1.7 cent net of tax).

Retail Banking and Wealth Management ('RBWM')

The continued low interest rate environment made 2014 a difficult year for the retail banking franchise. In addition to this, our focus on a value proposition for all customers resulted in a short-term fall in returns but will see long term gains from improved customer loyalty.

We have made good progress building on our 'customer needs fulfilled' proposition that removed

Fuq bażi fondamentali, meta neskludu l-investiment fil-qasam tal-konformità u l-ispiża tal-Comprehensive Assessment tal-ECB, l-ispejjeż baqgħu livelli ma' dawk tal-2013, minkejja żieda ta' 2.5% fil-pagi tal-ħaddiema u l-impatt tal-inflazzjoni. L-investiment kontinwu fit-titjib teknoloġiku kien iffinanzjat minn tifdil li sar billi ċerti proċessi ġew iddiżinjati mill-ġdid u ssimplifikati.

Ir-relazzjoni bejn l-ispejjeż u l-effiċjenza, li tqabbel l-ispejjeż tal-operat mad-dħul nett mill-operat, kienet ta' 57% meta mqabbla ma' 50% fl-2013.

Id-deduzzjonijiet għall-indeboliment tas-self ammontaw għal €23m, imqabbla ma' €3m fl-2013. Kif osserva ċ-Chairman, in vista tal-isfidi fl-ambjent li qed naħdmu fih, il-Bord adotta linja aktar konservattiva lejn ċertu self kummerċjali li ilu hemm żmien twil u li mhux jippresta ruħu kif miftiehem. Dan ġara speċifikament f'każ fejn il-periti baxxew il-valutazzjonijiet li taw lill-bank dwar proprjetà miżmuma bħala garanzija fuq self. Madankollu, b'mod ġenerali, il-kwalità tal-assi għadha tajba u għad hemm perċentwal għoli ta' sigurtà tanġibbli li l-bank għandu f'idejh bħala garanzija għas-self li ta.

Self ġdid gross lill-klijenti żdied b'19% għal €710m (2013: €597m). Dan jirrifletti l-appoġġ kontinwu tal-bank għall-ekonomija lokali. Madankollu s-self nett mogħti lill-klijenti, li laħaq €3,273m, kien fl-istess livell ta' dak tal-31 ta' Diċembru 2013. Fis-sitwazzjoni attwali ta' rati ta' imgħax baxxi, kompliet matul is-sena x-xejra tal-klijenti, sew kummerċjali kemm personali, li jagħżlu li jaqtgħu d-dejn qabel iż-żmien. Minkejja dan, ir-reġistru tas-self għax-xiri tad-djar, li hu l-akbar portafoll ta' self li għandu l-bank, wera tkabbir nett pożittiv.

Id-depożiti telgħu għal €4,867m, żieda ta' 8% mill-31 ta' Diċembru 2013 minkejja l-kompetizzjoni qawwija li ma tieqafx.

Il-portafoll ta' investimenti *available-for-sale* li għandu l-bank huwa wieħed diversifikat sew u li għandu pożizzjoni konservattiva. L-investimenti kollha huma kklassifikati BBB+ jew aqwa.

Il-pożizzjoni tal-likwidità tal-bank hija soda, b'relazzjoni tas-self mad-depożiti ta' 67%, imqabbla ma' 73% fil-31 ta' Diċembru 2013.

Matul l-2014 il-bank kompla jkabbar ir-relazzjoni ewlenija tal-kapital tal-Ewwel Saff, hekk li dan mexa minn 9.9% (kif dikjarat mill-ġdid wara li kien muri bħala 9.4% taħt CRD IV) għal 10.6%.

Il-profitt li jiġi attribwit lill-azzjonisti niżel bi 43% għal €34m meta mqabbel mas-sena ta' qabel, li jirriżulta fi qligħ sehem b'sehem ta' 10.4 ċenteżmi. Il-Bord qed jirrakkomanda dividend finali gross ta' 2.6 ċenteżmi kull sehem (1.7 ċenteżmi wara t-taxxa).

Minister for Gozo Anton Refalo, Victoria Mayor Dr Samuel Azzopardi, and Bishop Mario Grech joined officials and staff at the opening of upgraded Victoria branch.

product specific sales targets for staff and placed meeting the needs of our customers at the heart of everything that we do. This has led to a material improvement in the quality of interactions with our customers.

Throughout the year, various products and initiatives were launched, the most important of which was the new mortgage campaign. The bank has continued to position itself as the best value for money provider and this has led to significant increases in sales.

In 2014, the retail business continued to build on its digital capability with the launch of a market leading Mobile Banking App that allows customers to access their accounts on the move. We saw three times the forecast level of Mobile Banking App downloads during the year and this was one of the highest per customer rates in the HSBC Group.

We maintained our retail network investment strategy during the year and finalised the branch improvements in Gozo and completed the refurbishment of our flagship branch in Valletta. We have commenced work to change Fgura branch to an assisted self-service branch, and in order to help our customers with visual impairments, we have introduced 'talking ATMs'.

Commercial Banking ('CMB')

The Commercial Banking business remained profitable but was negatively impacted by the level of prudent impairments taken on legacy facilities. Despite this, CMB continued to focus on improving customer experience, growing revenues in Trade, Payments and Cash Management and Receivables Finance and its drive

Servizzi Bankarji Personali (RBWM)

Is-sitwazzjoni prevalenti fl-2014 ta' rati baxxi ta' imgħax għamlitha sena diffiċli għan-negozju tas-servizzi bankarji personali. Barra minn hekk, il-proposta tagħna li niffokaw biex nagħtu valur lill-klijenti kollha tagħna ġabitilna tnaqqis għal żmien qasir fl-introjtu imma se ġġibilna aktar qligħ fit-tul minħabba li jiżdiedu l-klijenti li jagħżlu li jibqgħu magħna.

Għamilna progress tajjeb għaliex bnejna fuq il-proposta li ressaqna li 'inwettqu l-ħtiġijiet tal-klijenti'. Din il-proposta warrbet il-miri li kellhom l-impjegati ta' bejgħ ta' prodotti speċifiċi u daħħlet it-twettiq tal-ħtiġijiet tal-klijenti fil-qalba ta' kull ma nagħmlu. B'hekk il-kwalità tal-interazzjoni mal-klijenti tagħna tjiebet sostanzjalment.

Tul is-sena varajna diversi prodotti u inizzjattivi, l-aktar importanti fosthom il-kampanja ta' self ġdid għad-djar. Il-bank baqa' jżomm il-pożizzjoni ta' dak li jagħti l-aqwa valur għall-flus, u dan wassal għal żidiet notevoli fil-bejgħ.

Fl-2014 in-negozju tas-servizzi personali kompla jwessa' l-kapaċità diġitali tiegħu meta nieda l-Mobile Banking App, prodott fuq ta' quddiem fis-suq li jippermetti lill-klijenti jaċċessaw il-kontijiet tagħhom kull fejn ikunu. Innotajna li l-Mobile Banking App tniżżel mill-klijenti tliet darbiet aktar milli konna antiċipajna, u dan kien wieħed mill-ogħla rati ta' użu mill-klijenti fil-Grupp HSBC.

Matul is-sena żammejna l-istrateġija li kellna ta' investiment fil-fergħat. Spiċċajna t-tisbiħ fil-fergħa

Guests and staff at the opening of the refurbished Valletta branch witnessing a live demonstration of Talking ATMs by a visually-impaired HSBC customer.

for international business growth through the success of the Malta Trade for Growth fund.

The Malta Trade for Growth initiative and the €50m fund, launched in December 2013, have been a significant success. The fund was fully committed after nine months, clearly underlining the interest amongst the business community in international growth opportunities. A second fund will be launched in the second quarter of 2015. The 'Why Malta?' video, that was launched late in 2013, is assisting the business and our customers to promote Malta internationally as a place to invest. The video is in the process of being produced in five different languages, including Mandarin.

During the year we continued to work with key stakeholders on Malta's potential to become a major logistics hub in the centre of the Mediterranean. Malta's strategic location with close proximity to the European and North African markets offers a real opportunity for broad based long term economic growth.

Further important enhancements took place during the year to the HSBCNet internet banking platform. One of the key additions was the roll out of HSBCNet GetRate. This allows our commercial customers to view and instantly book foreign exchange rates when making cross-currency payment to third parties or effecting inter-account transfers.

Global Banking and Markets (GB&M)

The overall performance of the business was down on 2013 as a result of lower one-off disposals from

t'Għawdex u temmejna r-rinnovament tal-fergħa ewlenija tagħna fil-Belt Valletta. Bdejna x-xogħol biex il-fergħa tal-Fgura tinbidel f'fergħa *self-service* assistita, u biex naġevolaw lill-klijenti neqsin mid-dawl daħħalna ATMs li jitkellmu.

Servizzi Bankarji Kummerċjali (CMB)

In-negozju tas-Servizzi Bankarji Kummerċjali kompla jagħmel profitt, imma ntlaqat ħażin mill-ammont ta' self li ilu fuq il-kotba tagħna żmien twil li bi prudenza ġie dikjarat indebolit. Minkejja dan, is-CMB kompla jiffoka fuq it-titjib tal-esperjenza tal-klijent u fuq it-tkabbir tad-dħul mill-Kummerċ, Pagamenti u Mmaniġġjar tal-Flus u mill-Finanzjament tad-Debiti, kif ukoll mill-ispinta biex ikabbar il-kummerċ internazzjonali bis-suċċess tal-Malta Trade for Growth Fund.

L-inizzjattiva Malta Trade for Growth u l-fond ta' €50m, imnedija f'Diċembru tal-2013, kellhom suċċess notevoli. Il-fond kien meħud kollu f'temp ta' disa' xhur, li juri biċ-ċar l-interess li hemm fost il-komunità kummerċjali għal oppotunitajiet ta' tkabbir barra minn Malta. Fond ieħor se jiġi varat fit-tieni kwart tal-2015. Il-*video* 'Why Malta?', li ħareġ tard fl-2013, qiegħed jgħin lilna u lill-klijenti tagħna biex nirreklamaw lil Malta internazzjonalment bħala post għall-investiment. Għaddej il-proċess biex issir il-produzzjoni ta' dan il-*video* f'ħames lingwi differenti, inkluż iċ-Ċiniż.

Matul is-sena komplejna naħdmu ma' partijiet ewlenin interessati fil-potenzjal ta' Malta li ssir ċentru maġġuri loġistiku f'nofs il-Mediterran. Il-pożizzjoni strateġika ta' Malta li hija qrib ħafna tas-swieq sew tal-Ewropa kemm tal-Afrika ta' Fuq toffri opportunità reali għal tkabbir ekonomiku wiesgħa li jkampa fit-tul.

Sar aktar xogħol matul is-sena fuq titjib importanti li jgħolli l-livell tal-HSBCNet, il-pjattaforma tas-servizzi bankarji fuq l-internet. Fost iż-żidiet ewlenin li saru kien hemm l-HSBCNet GetRate, li tippermetti l-klijenti kummerċjali tagħna li jaraw u jirriżervaw immedjatament ir-rati tal-kambju meta jkunu qed iħallsu lil terzi persuni, jew jagħmlu trasferiment bejn kontijiet, b'valuta differenti.

Servizzi Bankarji u Swieq Globali (GBM)

Il-prestazzjoni ġenerali f'dan ix-xogħol iddgħajfet paragun mal-2013, minħabba li kien hemm inqas disponimenti ta' darba mill-portafoll tal-investimenti u għax ir-rati baxxi tal-imgħax għamluha diffiċli biex wieħed isib fejn jerġa' jinvesti. Madankollu, billi saru xi aġġustamenti dwar transazzjonijiet ta' darba tas-sena ta' qabel, ir-riżultat ġie fil-livell tal-2013.

HSBC Head of RMB Business Development, Europe, Global Banking & Markets, Ms Rongrong Huo addressing the rising aspiration for trade in Renminbi.

the investment portfolio and a difficult re-investment environment as a result of low interest rates. However after adjusting for prior year one-off items, the business was in line with 2013.

GB&M had a strong year in relation to underlying foreign exchange sales. In addition to this, the strong partnership with CMB around client hedging and capital markets solutions promises well for 2015. These are important areas of opportunity for both businesses where the technical excellence of HSBC Group provides a market competitive advantage.

The available-for-sale portfolio is wholly investment grade and this continues to serve the business well in these uncertain times. The portfolio has no holding of stressed peripheral European sovereign debt.

In 2015 and beyond, GB&M is focused on building out its risk management solutions business, developing China Renminbi currency opportunities and advising clients on capital financing alternatives. The key medium term challenge remains re-investment risk in a low interest rate environment.

HSBC Technology and Services ('HTS')

The HTS function is the backbone of the bank in Malta and is responsible for the infrastructure and operational support that allows the three business lines to serve their customers. Key areas within HTS are Information Technology (IT), Service Delivery, Change Delivery, Procurement and Real Estate.

The IT team was busy during the year launching a number of critical system upgrades. Amongst these were the successful launch of HSBCNet GetRate and a new staff front end for the Call Centre that has provided additional functionality to both customers and users.

Il-GBM kellu sena b'saħħitha għar-rigward tal-bejgħ bażiku ta' munita barranija. Magħqud ma' dan, is-sħubija soda mas-CMB dwar soluzzjonijiet ta' *hedging* għall-klijenti u ta' swieq kapitali tawgura tajjeb għall-2015. Dawn huma oqsma importanti għaż-żewġ dipartimenti għax joffru opportunitajiet kbar, u l-eċċellenza teknika tal-Grupp HSBC tista' tagħtihom vantaġġ kompetittiv fis-suq.

Il-portafoll ta' investimenti *available-for-sale* huwa kollu ta' grad tal-investiment, u dan jibqa' jiswa tajjeb lin-negozju f'dawn iż-żminijiet inċerti. Il-portafoll ma fih ebda investiment f'dejn sovran Ewropew periferali li huwa taħt stress.

Għall-2015 u s-snin li ġejjin, il-GBM qed jiffoka fuq it-tfassil ta' negozju bbażat fuq soluzzjonijiet għall-immaniġġjar tar-riskju, fuq l-iżvilupp ta' opportunitajiet fil-munita Renminbi taċ-Ċina, u fuq l-għoti ta' pariri lill-klijenti dwar alternattivi ta' finanzjament tal-kapital. Imma l-isfida ewlenija fit-terminu medju tibqa' r-riskju marbut mal-investiment mill-ġdid ta' fondi rikavati meta r-rati tal-imgħax għadhom baxxi.

Teknoloġija u Servizzi (HTS)

Il-funzjoni tal-HTS hija s-sinsla tal-bank f'Malta u hija responsabbli għall-infrastruttura u l-appoġġ operazzjonali li jippermettu lit-tliet linji kummerċjali li jaqdu lill-klijenti. L-oqsma ewlenin fl-HTS huma Information Technology (IT), Service Delivery, Change Delivery, Procurement u Real Estate.

It-tim tal-IT kien okkupat matul is-sena bil-ħruġ ta' għadd ta' *upgrades* kritiċi tas-sistema. Fosthom kien hemm l-inawgurazzjoni b'suċċess tal-HSBCNet GetRate kif ukoll *front end* ġdid għall-Call Centre li kompla jżid il-funzjonalità sew għall-klijenti kemm għall-utenti.

Service Delivery is focused on supporting the key processes of the bank such as payments and in 2014 launched a very important project to digitalise client records. The records management project will generate significant efficiencies.

Change Delivery manages all key bank wide change projects and has been at the heart of the important initiatives to implement the United States FATCA tax regulations and the on-going introduction of common global standards in relation to financial crime and regulatory risk.

Procurement is a relatively new independent function that has introduced important additional discipline around how the bank buys products and services from third parties.

Real Estate continues to be closely involved in the management of the bank's property portfolio and has done an excellent job around the relatively recent refurbishment of our Victoria and Valletta flagship branches. These refurbishments bring the total number of renovated branches to 14.

Risk

During 2014, as a result of worsening conditions in the Eurozone and in line with HSBC Group risk parameters, the bank undertook a review of its lending portfolio. The majority of the book continues to perform well but against a backdrop of a fall in valuations on property held as security, principally on a number of legacy commercial real estate projects, the Board determined that it was prudent to take a more cautious approach to impairments. This resulted in a material increase in provisions against the prior year and impacted the performance of the Commercial Banking business. Having taken the impairments the commercial real estate portfolio is conservatively positioned.

In line with HSBC's global strategy, the Compliance function underwent a significant transformation in early 2014 and was divided into two distinct sub-functions: Financial Crime Compliance (FCC) and Regulatory Compliance (RC). Throughout 2014 we continued to invest in the function with a view to build a robust and effective compliance framework so as to address changing global regulations around anti-money laundering, sanctions, anti-bribery and corruption risks. The local HSBC Compliance team is now nearly four times the size that it was three years ago and this underlines our very significant commitment both locally and globally to prepare the business for continued regulatory change and heightened regulatory expectations.

Is-Service Delivery għandu l-mira li jagħti appoġġ fil-proċessi ewlenin tal-bank, pereżempju fil-pagamenti, u fl-2014 nieda proġett importanti biex ir-rekords tal-klijenti jsiru diġitali. Dan il-proġett ta' żamma tar-rekords se jżid l-effiċjenza sostanzjalment.

Iċ-Change Delivery jieħu ħsieb il-proġetti kollha ewlenin ta' tibdil fil-bank, u kien fiċ-ċentru tal-inizzjattivi importanti fl-implimentazzjoni tal-FATCA (ir-regolamenti Amerikani tat-taxxa), u fid-dħul li qed isir ta' standards globali komuni marbuta mar-reati finanzjarji u r-riskju regolatorju.

Il-Procurement hija funzjoni indipendenti relattivament ġdida, li daħħlet aktar dixxiplina fil-mod kif il-bank jixtri l-prodotti u s-servizzi minn għand terzi persuni.

Ir-Real Estate jibqa' involut fil-qrib fil-ġestjoni tal-proprjetà tal-bank u wettaq biċċa xogħol eċċellenti fit-tiġdid li m'ilux li sar fil-fergħat ewlenin tar-Rabat, Għawdex u l-Belt Valletta. Dawn il-proġetti tellgħu in-numru ta' fergħat imġedda għal 14.

Riskju

Matul l-2014, riżultat tal-kondizzjonijiet imwiegħra fiż-Żona Ewro u b'konformità mal-parametri tal-Grupp HSBC, il-bank dar dawra sew mal-portafoll tiegħu tas-self. Il-maġġoranza tal-kontijiet għadhom sejrin tajjeb. Madankollu kien hemm xi proprjetajiet miżmuma bħala garanzija, prinċipalment fuq numru ta' proġetti ta' proprjetà kummerċjali li ilhom għaddejjin, illi l-istima tagħhom waqgħet. Għalhekk il-Bord iddeċieda li jkun prudenti li tittieħed linja aktar konservattiva għar-rigward tal-indebolimenti. Dan ġab żieda materjali fil-provedimenti kontra s-sena ta' qabel u kellu impatt fuq ir-riżultati tal-Commercial Banking Business. Issa li ġew meqjusa l-indebolimenti, il-portafoll tal-proprjetà kummerċjali jinstab f'pożizzjoni konservattiva.

Bi qbil mal-istrateġija globali tal-HSBC, il-funzjoni tal-Konformità għaddiet minn trasformazzjoni kbira fil-bidu tal-2014 u nqasmet f'żewġ sottofunzjonijiet distinti: il-Konformità dwar Reati Finanzjarji (FCC) u l-Konformità Regolatorja (RC). Tul l-2014 investejna aktar fil-funzjoni bil-għan li nibnu qafas ta' konformità sod u effettiv, biex nindirizzaw it-tibdil globali li jsir fir-regolamenti relatati mar-riskji tal-ħasil tal-flus, tas-sanzjonijiet, tat-tixħim, u tal-korruzzjoni. It-tim li l-HSBC għandu lokalment fuq il-Konformità issa jgħodd kważi erba' darbiet dak li kien tliet snin ilu, u dan juri ċar l-impenn serju tagħna sew f'Malta kemm fid-dinja li nkunu mħejjija għal tibdil regolatorju kontinwu u għal aspettativi regolatorji aktar għolja.

People

In 2014 we continued to develop our talent management proposition and launched a number of activities and initiatives that will support our key staff taking their professional skills to the next level. This included leadership training and development and increased exposure to senior management across the region, participation in an external industry leadership programme and short term international assignments.

During the year, we delivered Values Led High Performance Culture training to all senior managers and will continue to roll out similar training to all employees in 2015. Key changes to the performance management process were implemented during the year and this placed heightened importance on values in the measurement of performance.

The local internship scheme for undergraduates continues to gather positive momentum and has now become an excellent feeder into our Graduate Management programme. Last year we recruited a further 6 people onto the graduate programme and will be shortly launching the 2015 scheme. This is a critical part of building the next generation talent pipeline and strengthening local succession plans.

We are proud of our engaged professional work force as it is through their dedication, commitment and hard work that we continue to be able to deliver results, meet our customer needs and be viewed as an employer of choice.

Executive Committee ('EXCO')

The bank's Executive Committee at the date of this report is made up of the following team members:

Mark Watkinson	Chief Executive Officer
Decca Fan	Chief Operating Officer
Paul Steel	Head of RBWM
Michel Cordina	Head of CMB
James Woodeson	Head of GB&M
Rashid Daurov	Chief Financial Officer
Joyce Grech	Chief Risk Officer
Mandy Garner	Head of Human Resources
John R. Sammut	Head of Internal Audit
Henry Firmstone	General Counsel

I would like to thank former EXCO member Josephine Magri who has moved on to a new role in the last 12 months and welcome her replacement Rashid Daurov as the new Chief Financial Officer. I wish them both the very best of luck in their new roles.

In-nies

Fl-2014 komplejna niżviluppaw il-proposta ta' trawwim tat-talent u nedejna għadd ta' attivitajiet u inizzjattivi li jgħinu lill-impjegati ewlenin tagħna jtellgħu l-ħiliet professjonali tagħhom fuq livell ogħla. Il-parteċipanti ngħataw taħriġ u żvilupp fil-*leadership* u ġew esposti aktar għall-membri anzjani tat-tmexxija fir-reġjun kollu, ipparteċipaw fi programm ta' tmexxija f'industrija esterna u ngħataw inkarigi ta' xogħol internazzjonali għal żmien qasir.

Matul is-sena tajna taħriġ lis-*senior managers* kollha fil-Values Led High Performance Culture u se nibqgħu nagħtu taħriġ simili lill-impjegati kollha fl-2015. Saru tibdiliet fil-proċess tal-*performance measurement* illi taw importanza akbar lill-valuri mdaħħla fil-kejl tal-prestazzjoni tal-ħaddiema.

L-iskema lokali ta' *internship* għal studenti li għadhom ma ggradwawx qed tkompli tikber u issa saret triq eċċellenti biex kandidati jidħlu fil-programm tagħna ta' Graduate Management. Is-sena l-oħra daħħalna sitt persuni ġodda fil-programm tal-gradwati u dalwaqt se nvaraw l-iskema tal-2015. Din hija parti kritika fil-bini ta' ġenerazzjoni ġdida ta' talent u fit-tisħiħ tal-pjani ta' suċċessjoni lokali.

Aħna kburin bil-ħaddiema professjonali u impenjati tagħna, għaliex huwa bid-dedikazzjoni, l-impenn u l-ħidma soda tagħhom li nistgħu nkomplu nġibu r-riżultati, naqdu l-ħtiġijiet tal-klijenti, u nuru li aħna għażla tajba għal min jixtieq jaħdem magħna.

Il-Kumitat Eżekuttiv ('EXCO')

Il-Kumitat Eżekuttiv tal-bank fid-data ta' dan ir-rapport huwa magħmul minn dawn il-membri:

Mark Watkinson	Kap Eżekuttiv
Decca Fan	Kap Operattiv
Paul Steel	Kap tal-RBWM
Michel Cordina	Kap tas-CMB
James Woodeson	Kap tal-GB&M
Rashid Daurov	Kap tal-Finanzi
Joyce Grech	Kap tar-Riskju
Mandy Garner	Kap tar-Riżorsi Umani
John R. Sammut	Kap tal-Verifika Interna
Henry Firmstone	Avukat Ġenerali

Nixtieq nirringrazzja lil Josephine Magri, li kienet membru tal-EXCO u li mxiet fi rwol ġdid f'dawn l-aħħar tnax-il xahar u nilqa' lil Rashid Daurov, li daħal minflokha bħala l-Kap ġdid tal-Finanzi. Nawguralhom it-tnejn l-akbar suċċess fil-post il-ġdid tagħhom.

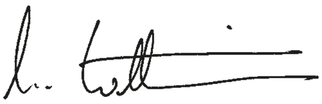
Outlook

The next 12 months are likely to remain very difficult with the Eurozone going through a period of considerable stress and with interest rates forecast to remain low. Against this, reduced oil prices and a steady recovery in the United States may provide some limited ground for optimism. Ultimately however the economic picture is likely to remain uncertain, particularly in Europe.

The business in Malta is well capitalised and liquid, as evidenced by the bank's strong performance in the ECB Comprehensive Assessment, and as part of one of the world's largest financial groups is positively positioned to weather the current market difficulties and address continued regulatory challenges.

HSBC Bank Malta is committed to the market and to building a strong and sustainable business for the long term. This is evidenced by our ongoing investment in our business and our people. Our purpose is to be relevant in the sectors of the economy that we feel represent the core, long term growth opportunity for the nation and its people and to support broad based economic growth.

I would like to thank our customers, staff, shareholders, management and our Board for their support in 2014. I reiterate that it is indeed a privilege and honour to work for HSBC Bank Malta p.l.c.



Mark Watkinson, *Chief Executive Officer*
23 February 2015

Ħarsa 'l quddiem

It-tnax-il xahar li ġejjin x'aktarx li jibqgħu diffiċli. Iż-Żona Ewro għadha għaddejja minn żmien ta' stress qawwi u r-rati tal-imgħax huma previsti li jibqgħu baxxi. B'kuntrast, il-prezzijiet orħos taż-żejt u l-irkupru konsistenti tal-Istati Uniti jistgħu jnisslulna xi ftit ottimiżmu. Fl-aħħar mill-aħħar, iżda, l-istampa ekonomika x'aktarx li tibqa' inċerta, speċjalment fl-Ewropa.

In-negozju tagħna f'Malta għandu kapital u likwidità sodi, kif ħareġ ċar mill-prestazzjoni tajba tal-bank fil-Comprehensive Assessment tal-ECB, u l-fatt li huwa parti minn wieħed mill-akbar gruppi finanzjarji fid-dinja jqiegħdu f'pożizzjoni vantaġġjuża biex jiffaċċa d-diffikultajiet attwali tas-suq u jindirizza l-isfidi kontinwi regolatorji.

L-HSBC Bank Malta huwa kommess lejn is-suq u lejn il-bini ta' negozju b'saħħtu u sostenibbli fit-tul. Dan jidher ċar mill-investiment kontinwu li nagħmlu fix-xogħol u fin-nies tagħna. L-għan tagħna hu li nkunu rilevanti f'dawk is-setturi tal-ekonomija li naħsbu li jirrappreżentaw l-opportunità l-aktar kruċjali u dejjiema ta' tkabbir għan-nazzjon u l-poplu tiegħu u li nsostnu t-tkabbir ekonomiku fuq firxa wiesgħa.

Nixtieq nirringrazzja lill-klijenti, lill-ħaddiema, lill-azzjonisti, lill-*management* u 'l-Bord għall-appoġġ tagħhom fl-2014. Irrid nerġa' ngħid li hu tassew ta' privileġġ u ta' ġieħ għalija li naħdem għall-HSBC Bank Malta p.l.c.

Board of Directors and Company Secretary

Saviour sive Sonny Portelli, NON-EXECUTIVE CHAIRMAN
Appointed Chairman of HSBC Bank Malta p.l.c. on 31 May 2013 after having served as Director on the Board since 9 October 2006. Mr Portelli also has directorships in companies forming part of the Malta University Group. He has a background in tourism, the hospitality industry, telecoms and general management, with significant international experience. In connection with these roles, Mr Portelli served on a number of Boards and trade organisations. His previous roles included being Chairman of the Board and of the Executive Committee of GO p.l.c., Executive Chairman of Air Malta p.l.c., Director of Forthnet SA (Greece), and Chairman of the Malta Council for Economic and Social Development. Mr Portelli is also former Chairman of the bank's Audit and Risk Committee and of the Remuneration Committee.

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, Mr Watkinson was Head of Commercial Banking for North America based in New York. Mr Watkinson has been with HSBC for 29 years. Mr Watkinson has worked in nine different countries for HSBC and has a strong background in commercial banking. From 2007 to 2010 Mr Watkinson was Chief Executive Officer for HSBC Bank in the Philippines.

Christopher Davies, NON-EXECUTIVE DIRECTOR
Appointed Director of the bank on 9 May 2014. Chief Executive Officer International, HSBC Bank plc since November 2013. Mr Davies also has directorships in companies forming part of the HSBC Group. Former Deputy Chief Executive Officer and Executive Director, HSBC Bank (China) Company Limited. Prior to moving to China, Mr Davies ran HSBC's Commercial Banking business in North America, following a series of senior appointments across all of HSBC's major business lines, principally in the UK and the Americas.

Brian Robertson, NON-EXECUTIVE DIRECTOR
Appointed Director of the bank on 5 May 2013. Former Group Managing Director and Chief Executive Officer of HSBC Bank plc. Presently Chairman of HSBC Latin America, Chairman of HSBC Turkey and Director of HSBC North America Holdings. Mr Robertson also has directorships in companies forming part of the HSBC Group.

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. Member of the bank's Audit and Risk Committee and of the Nomination and Remuneration Committee.

John Bonello, NON-EXECUTIVE DIRECTOR
Appointed Director of the bank on 15 July 2013. Chairman of the bank's Audit and Risk Committee and of the bank's Nomination and Remuneration Committee. He is a Chartered Accountant and a Certified Public Accountant and holds three other directorships in Maltese public listed and private companies. He was formerly the Chairman and Senior Partner of PricewaterhouseCoopers in Malta from where he retired in December 2009. Member of the Joint Disciplinary Board of the Accountancy Board and Fellow of the Malta Institute of Accountants. Also contact member in Malta for the Institute of Chartered Accountants in England and Wales.

Caroline Zammit Testaferrata Moroni Viani, NON-EXECUTIVE DIRECTOR
Non-Executive Director of the bank since 18 April 2013. Holds various directorships and executive positions within the Mercury Group of companies (Mercury p.l.c. being the ultimate parent company) whose main investments range from hotels and leisure oriented commercial properties to a high end business centre and portfolio investments held by a group company which is registered on the Malta Stock Exchange as a Collective Investment Scheme. A former director of HSBC Life Assurance (Malta) Limited and former member of the MTA.

Andrew Muscat, NON-EXECUTIVE DIRECTOR
Appointed Director of the bank on 16 January 2014. Partner at Mamo TCV Advocates where he heads the Corporate & Banking Department. Professor at the Faculty of Laws of the University of Malta. Professor Muscat also has two directorships in two different groups of companies and two other directorships in other companies. Former Director of Mid-Med Bank p.l.c. and also former member of the Board of Governors of the Malta Financial Services Authority.

Juanito A. Camilleri, NON-EXECUTIVE DIRECTOR
Appointed Director of the bank on 5 September 2014. Holds the post of vice-Chancellor (Rector Magnificus) of the University of Malta since July 2006. Former CEO of MobIsle Communications Ltd and of Melita Cable p.l.c. Presently Chairman of the Malta University Group of Companies, Chairman of the Centre for Entrepreneurship and Business Incubation, Chairman of the Centre for the Liberal Arts and Sciences and Chairman of the Centre for Molecular and Bio-Banking. He also has directorships in two other companies.

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. Registered office 116, Archbishop Street, Valletta. Tel: 2380 2404.

Executive Committee

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, Mr Watkinson was Head of Commercial Banking for North America based in New York. Mr Watkinson has been with HSBC for 29 years. Mr Watkinson has worked in nine different countries for HSBC and has a strong background in commercial banking. From 2007 to 2010 Mr Watkinson was Chief Executive Officer for HSBC Bank in the Philippines.

Decca Fan, CHIEF OPERATING OFFICER
Decca Fan was appointed as Chief Operating Officer for HSBC Bank Malta p.l.c. on 1 March 2014. She has been with the HSBC Group for over 26 years, having worked in Retail Banking and Wealth Management in Hong Kong, as Head of Operations at the Shanghai Processing Centre, Head of Operations at the Group Service Centre in Malaysia and recently as Managing Director of Group Service Centre in Sri Lanka before moving to Malta.

Paul Steel, HEAD OF RBWM
Appointed in the current role in October 2011. Previously the Head of Retail Distribution for Continental Europe, based out of Paris, managing countries such as Russia, Kazakhstan, Poland, France and Turkey. Prior to this, he was Deputy Head of Retail Banking and Wealth Management in France as well as Head of Network. Mr Steel has been with HSBC for 8 years.

Michel Cordina, HEAD OF CMB
Appointed Head of Commercial Banking on 1 June 2011. Prior to taking up this appointment, Mr Cordina was Deputy Head of CMB. Mr Cordina is a banking professional and has over 31 years experience with HSBC. He has worked in the United Kingdom as the Head of Sales Performance for CMB, in the branch network in Malta for both retail and commercial banking and in a number of Head Office departments, where he was Deputy Head of Operations and Head of Business Transformation.

James Woodeson, HEAD OF GB&M
Appointed as Head of Global Banking & Markets, HSBC Bank Malta p.l.c in December 2013. Mr Woodeson has worked for HSBC for 13 years and has held senior positions within the Global Markets and Global Asset Management businesses in London and Hong Kong. Prior to taking up his appointment in Malta, he was Head of Global Markets and subsidiary Board Director, HSBC Jersey.

Rashid Daurov, CHIEF FINANCIAL OFFICER
Appointed Chief Financial Officer on 29 November 2014. Holds an MSc degree in Management from University of Bristol, UK and is a Certified Public Accountant (US). Mr Daurov joined HSBC in 2010 and worked as Head of Group Reporting and Planning in Kazakhstan and most recently as Chief Financial Officer for HSBC Kazakhstan. Prior to HSBC, Mr Daurov worked in audit and financial advisory with Ernst and Young and Deloitte.

Joyce Grech, CHIEF RISK OFFICER
Appointed Chief Risk Officer in April 2013. Ms Grech has worked with HSBC for 18 years. During her career, Ms Grech has undertaken a number of roles, principally in Malta. Ms Grech started her career in Trade Finance and Commercial Banking before moving to the bank's Credit department where she spent over 5 years, the last three of which she was the Deputy Head of Credit. Before taking up her role as Chief Risk Officer she worked in the bank's Retail Banking and Wealth Management division where she headed the Customer Value Management department.

Mandy Garner, HEAD OF HUMAN RESOURCES
With 21 years of experience in human resources, Ms Mandy Garner moved to Malta in July 2013 from HSBC in Jersey Channel Islands, where she supported the expat business and took a lead role on all HR issues across the Channel Islands and Isle of Man. Ms Garner previously worked for Santander and the UK National Health Service and was educated in the UK, holding an MA in Law and Employee Relations and is also a Member of the Institute of Personnel and Development.

John Sammut, HEAD OF INTERNAL AUDIT
John Sammut, Head of Internal Audit of HSBC Bank Malta p.l.c. since January 2007. Graduated in MA Financial Services and BA (Hons) Accountancy from the University of Malta. He is an Associate of the Institute of Financial Services UK and also a Fellow of the Malta Institute of Accountants. Mr Sammut joined the bank in 1977 and has occupied a number of senior posts.

Henry Firmstone, GENERAL COUNSEL
Appointed General Counsel on 1 June 2013. Prior to taking up his appointment in Malta, Mr Firmstone was General Counsel for HSBC New Zealand for 10 years including 5 years as Head of Compliance. He has also worked for HSBC in Hong Kong and Barclays Bank in London. Mr Firmstone has been a lawyer for 26 years.

Summary of Financial Performance

The financial performance of HSBC Bank Malta and its subsidiaries for the year ended 31 December 2014 has been negatively impacted by the challenging economic conditions – continuous market difficulties in Europe, decreasing interest rates, tighter credit spreads and changing regulatory environment. Reported profit before tax of €52m decreased by 42%, or €38m compared to 2013. This was principally caused by higher loan impairments, reducing interest margin earned due to the persisting low interest rate environment and intensified pressure from the competition, lower one-off income from the disposal of available-for-sale instruments and from the release of insurance reserve, and higher costs.

Profit attributable to shareholders was €34m, a decrease of €25m over prior year.

Net operating income of €173m reduced by €14m compared with €187m in 2013.

Operating expenses at €98m were €5m above prior year primarily as a result of significant notable items – increased regulatory costs and restructuring costs. Excluding these items, expenses rose by 1% on prior year.

The cost efficiency ratio was 57% compared with a prior year ratio of 50%.

Shareholder ratios

Earnings per share in 2014 stood at 10.4 cent compared with 18.1 cent in 2013. The latter has been restated to reflect the bonus share issue of 1 for every 9 shares held undertaken during 2014. The pre-tax return on shareholders' funds in 2014 was 12% compared to 21% in 2013.

The Directors propose a final gross dividend of 2.6 cent per share. This follows on the gross interim dividend of 4.5 cent paid in September 2014.

During 2014, the bank continued to build up the General Banking Risk Reserve in line with the revised Banking Rule 09 published by the Malta Financial Services Authority ('MFSA') in December 2013. The revised rule impacts all banks in Malta that do not have a Tier 1 Capital ratio of 14% or higher. The impact of the new rule during the year under review was to reduce gross final dividend to 2.6 cent per share instead of a final gross dividend of 4.3 cent which would otherwise have been distributed.

The Board is recommending a bonus issue of 1 share for every 9 shares held as on 29 April 2015 by the capitalisation of reserves amounting to €11m increasing share capital from €97m to €108m.

Net interest income

Net interest income decreased by €5m to €120m compared with prior year. The fall in interest income by €9m reflected the impact of a tightening in interest margin earned on the loan portfolio as competition intensified, lower average lending balances associated with a slow economy and higher loan repayments and a continuous decline in interest earned on investments as the proceeds of higher yielding maturing bonds were re-invested at lower rates. This was partially mitigated by a fall in the cost of funds by €4m compared to 2013 as customers moved to shorter-dated deposits and deposit rates decline.

Non-interest income

Non-interest income of €53m fell by €9m or 15% compared with €62m in 2013.

Net fee and commission income of €28m was broadly in line with 2013. The fee and commission income performance was generally positive but the overall result was impacted by the winding down of fund administration and custody business in early 2014.

A net gain of €2 million was reported as a result of a repositioning of the investment portfolio compared to €4 million in 2013.

HSBC Life Assurance (Malta) Limited reported a profit before tax of €9m compared with €13m in 2013. While new insurance business was 10% higher than the prior year, the result in 2014 was negatively impacted by downward yield curve movements and lower technical reserve releases.

Operating expenses

Operating expenses of €98m were €5m or 6% higher compared with the previous year.

The rise in expenses was primarily driven by increased regulatory fees associated with the ECB Comprehensive Assessment (€3 million), higher MFSA fees, investments in Compliance staff and staff early voluntary retirement costs. The increase was partially offset by savings generated as the bank continued to simplify and re-engineer its processes. Excluding these incremental costs, expenses were held flat to 2013 despite a 2.5% increase in staff salaries and the impact of inflation.

Net impairment

Against a difficult Eurozone economic back-drop, the Board determined to take a more cautious approach to loan provisioning. This resulted in impairment costs rising to €23 million for the year from €3 million in 2013. Higher costs were largely driven by lower valuations and revised estimates as to the time taken to recover proceeds from the sale of collateral on legacy commercial real estate loans. Overall asset quality remains acceptable with a high percentage of tangible security held for the overall loan portfolio.

Taxation

The 2014 effective rate of tax was 35.5%. Tax expense for 2014 amounted to €19m.

Assets

Total assets were €7,199 million. This was up 26% on the prior year as a result of the acquisition of a life assurance portfolio from HSBC Ireland.

Net loans and advances to customers at €3,273 million were €28 million lower than at 31 December 2013. This decrease was the result of higher customer loan repayments despite a 19% rise year on year in gross advances.

Life assurance business assets increased by 198% on the prior year to €1,422 million following the acquisition noted above.

The bank's available for sale investment portfolio remains well diversified and conservatively positioned.

Liabilities

Total liabilities increased by 27% on the prior year to €6,754 million as a result of the acquisition of a life assurance portfolio from HSBC Ireland.

Customer deposits at €4,867 million increased by €349 million or 8% as the business continued to attract accounts.

The bank's liquidity position remains strong with the advances to deposit ratio improving to 67%.

Liabilities under investment contracts amounted to €1,021 million as a result of the acquisition of the Irish portfolio in 2014. Liabilities under insurance contracts issued increased by €78 million or 15% during the year.

Shareholders' funds

Total equity increased by €22 million to €445 million, as the local group earned €34 million, paid dividends of €19 million and saw an increase in revaluation reserves of €7 million.

The number of shareholders as at 31 December 2014 stood at 10,065.

The bank continued to maintain a strong total capital ratio of 13%. Tier 1 capital ratio as at 31 December 2014 increased to 10.6%.

During 2014 HSBC Bank Malta participated in the ECB Comprehensive Assessment. This included an Asset Quality Review (AQR) and a stress test. These were carried out by the ECB in cooperation with the MFSA. The AQR was carried out first, followed by the stress test. For the AQR, the minimum benchmark was set at 8% Common Equity Tier 1 Capital (CET1). The stress test was based on adjusted capital post – AQR and the stress test benchmark was set by the ECB at a CET1 of 5.5%. The bank successfully passed the stress test with its CET1 ratios well in excess of the ECB requirements.

Results for 2014

HSBC Bank Malta p.l.c. and its subsidiaries (the 'local group') reported a profit before tax of €52m for the year under review. The local group's profit attributable to shareholders of the bank was €34m.

A gross interim ordinary dividend of 4.5 cent per share was paid on 4 September 2014. The Directors have proposed a gross final dividend of 2.6 cent per ordinary share. The final dividend will be payable to shareholders on the bank's register as at 23 March 2015. The Directors are recommending a bonus share of 1 share for every 9 shares held as on 29 April 2015 by capitalising retained earnings amounting to €11m.

Further information about the results is provided in the local group statement of profit or loss and the statement of profit or loss and other comprehensive income on pages 43 and 44.

Principal activities

Principal activities of parent company

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

The bank is authorised to carry on the business of banking, under the Banking Act, 1994 as a credit institution. It is also 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 local group comprised the following subsidiaries at 31 December 2014: HSBC Life Assurance (Malta) Limited, HSBC Global Asset Management (Malta) Limited, HSBC Securities Services (Malta) Limited, HSBC Stockbrokers (Malta) Limited and HSBC Insurance Management Services (Europe) Limited. HSBC Stockbrokers (Malta) Limited and HSBC Securities Services (Malta) Limited are undergoing a voluntary winding up process.

Principal activities of subsidiaries

HSBC Life Assurance (Malta) Limited is authorised by the Malta Financial Services Authority to carry on business of insurance in Malta under the Insurance Business Act, 1998. It offers a range of protection and investment life assurance products distributed mainly through HSBC Bank Malta p.l.c. which is enrolled as a tied insurance intermediary for HSBC Life Assurance (Malta) Limited under the Insurance Intermediaries Act, 2006.

HSBC Insurance Management Services (Europe) Limited is authorised by the Malta Financial Services Authority to act as an insurance manager. It provides operational support to HSBC Life Assurance (Malta) Limited and HSBC Life (Europe) Limited based in Dublin.

HSBC Global Asset Management (Malta) Limited is the investment solutions provider of the HSBC Group in Malta. It manages an array of funds which have exposure to both Maltese and international financial markets. HSBC Global Asset Management (Malta) Limited specialises in the provision of tailor-made discretionary portfolio management services for institutions and family offices.

Additional regulatory disclosures

Banking Rule 07 (Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised under the Banking Act 1994) partly repealed by certain provisions in Regulation (EU) No 575/2013 (CRR) is related to market discipline and aims to make credit institutions more transparent by requiring them to publish specific disclosures on the credit institution's risk and capital management under Basel II framework. However the local group is considered as a significant subsidiary of HSBC Holdings plc and therefore exempt, in terms of Article 24 of the revised BR 07 and Article 13 of CRR, from certain risk disclosure requirements under Pillar 3, on the basis that such disclosures are required at the consolidated level which is HSBC Holdings plc level. HSBC Holdings plc publishes full Pillar 3 disclosures as a separate document on the Group Investor Relations website.

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 9 to 17.

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 €97,281,414 divided into 324,271,380 Ordinary shares of a nominal value of 30 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 a Restricted Share Awards scheme in existence whereby employees in the GCB3 grade and higher can be awarded shares in HSBC Holdings plc. Share awards will be released to the individual staggered over 3 years, provided the participant remains continuously employed within the Group. Vesting of these awards are generally not subject to performance conditions. 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 providing for compensation on resignation or termination of directorship.

It is hereby declared that, as at 31 December 2014, 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 bank or in related companies at 31 December 2014:

Saviour sive Sonny Portelli	5,223 shares
Philip Farrugia Randon	7,112 shares
John Bonello	36,667 shares

Mrs Caroline Zammit Testaferrata Moroni Viani has a beneficial interest of 65,334 ordinary shares in the bank through the shareholding of Testaferrata Moroni Viani (Holdings) Limited, 44,445 ordinary shares through the shareholding of Testaferrata Moroni Viani Limited and 5,556 ordinary shares through the shareholding of Sales and Letting Limited.

There were no changes to Directors' interest from 31 December 2014 to 31 January 2015.

Shareholders holding five per cent (5%) or more of the equity capital at 31 January 2015:

HSBC Europe B.V.	70.03%

Number of shareholders at 31 January 2015:

One class of shares (All shares have equal voting rights)	10,065 shareholders

Number of shareholders analysed by range

	31 January 2015	
Range of shareholding	Total shareholders	Shares
1 – 500	1,672	493,605
501 – 1,000	1,326	962,700
1,001 – 5,000	4,262	10,174,042
5,001 and over	2,805	312,641,033
Total shareholding	**10,065**	**324,271,380**

Standard licence conditions applicable under the Investment Services Act, 1994

In accordance with SLC 7.35 of the Investment Services Rules For Investment Services Providers regulated by the Malta Financial Services Authority, licence holders are required to include breaches of standard licence conditions applicable under the Investment Services Act, 1994, in the Report of the Directors. Accordingly, the Directors confirm that no breaches of the standard licence conditions and no other breach of regulatory requirements under the Investment Services Act, 1994, which were subject to administrative penalty or regulatory sanction, were reported.

Board of Directors

The Directors who served during the year and up till the date of this report are as follows:

Saviour sive Sonny Portelli
Mark Watkinson
Brian Robertson
Philip Farrugia Randon
Caroline Zammit Testaferrata Moroni Viani
John Bonello
Andrew Muscat (appointed on 16 January 2014)
Ranjit Gokarn (resigned on 9 May 2014)
Christopher Davies (appointed on 9 May 2014)
James Dunbar Cousin (resigned on 1 July 2014)
Juanito Camilleri (appointed on 5 September 2014)

Executive committee

As at 31 December 2014, the bank's Executive Committee of the local group was composed of the following:

Mark Watkinson	Chief Executive Officer
Decca Fan	Chief Operating Officer
Paul Steel	Head of RBWM
Michel Cordina	Head of CMB
James Woodeson	Head of GB&M
Rashid Daurov	Chief Financial Officer
Joyce Grech	Chief Risk Officer
Mandy Garner	Head of Human Resources
John Sammut	Head of Internal Audit
Henry Firmstone	General Counsel

Auditors

The Audit and Risk Committee recommended that, in view of the fact that HSBC Group had after a competitive tender process decided to appoint PricewaterhouseCoopers as its external auditor, it was advisable to appoint the same audit firm for the local group. The Board has endorsed the said recommendation. The appointment of PricewaterhouseCoopers as the bank's external auditors will be proposed at the forthcoming Annual General Meeting. Subject to the approval of the shareholders, PricewaterhouseCoopers will undertake the audit of the HSBC local group for the year ending 31 December 2015.

The Board thanks KPMG for their professionalism and care they have demonstrated in their role as external auditors since 1999.

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 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 23 February 2015 by:

Sonny Portelli, *Chairman*

Mark Watkinson, *Chief Executive Officer*

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

The Board of Directors (the 'Board') of HSBC Bank Malta p.l.c. (the 'bank') is committed to the HSBC global values of dependability, openness to different ideas and cultures, and connection with customers, communities, regulators and each other. The Board ensures that each employee, through ongoing training, is aware of the obligation to ensure that his or her conduct consistently matches the bank values so as to serve positively the customers who entrust their financial needs to HSBC.

The Board is proud of the fact that the bank and its subsidiaries (the 'local group') has a solid corporate governance framework that is built around the principles of control and accountability. This culture stems from a philosophy that puts the protection of investors and the interest of customers at the forefront.

Corporate governance is subject to regulation by the Malta Financial Services Authority Listing Rules. As a company whose equity securities are listed on a regulated market, HSBC Bank Malta p.l.c. endeavours to adopt the Code of Principles of Good Corporate Governance (the 'Code' or 'Principles') embodied in Appendix 5.1 to Chapter 5 of the Listing Rules.

In terms of Listing Rule 5.94, the bank is obliged to disclose compliance and non-compliance with the provisions of the said Code. The bank strives to maintain the highest standards of disclosure in reporting the effective measures adopted to ensure compliance with the Principles, and to explain the instances of non-compliance.

Compliance with the Code

Principle 1: The Board

The bank is headed by an effective Board that leads and controls the business. The Board is currently made up of nine members who are honest, competent and solvent, and thus fit and proper to direct the business of the bank. Directors, individually and collectively, are of the appropriate calibre, having the necessary skills and experience to provide leadership, integrity and judgement in directing the bank. The courageous integrity, honesty and diligence of the Directors guarantee that the bank adheres to HSBC Group's (the 'Group') highly ethical business values and this is reflected in the bank's decision and policy-making process. Through their effective contribution Directors enhance shareholders value, protect the bank's assets and safeguard the interest of third parties.

Board members are accountable for their performance and that of their delegates to shareholders and relevant stakeholders. 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 organisational structures and regularly reviews management performance. It ensures that the bank has the appropriate financial and human resources to meet its objectives. Moreover, it exercises prudent and effective controls which enable risk to be assessed and managed in order to achieve the short and long term sustainability of the business.

The Board delegates specific responsibilities to a number of committees, notably the Audit and Risk Committee, the Nomination and Remuneration Committee and the Executive Committee. Further detail in relation to the committees and their responsibilities can be found under principle 4 of this statement.

The process of appointment of Directors is conducted in terms of the Memorandum and Articles of Association of the company. The Board consists of not more than nine Directors who are appointed/elected by the shareholders. Every shareholder owning 11 per cent of the ordinary share capital is entitled to appoint one Director for each 11 per cent 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 per cent of the ordinary share capital participate in the election of the remaining three Directors. The largest single shareholder (subject to a minimum 33 per cent 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.

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 encourages active engagement by all Board members for the discussion of complex and contentious issues and ensures that Directors constructively challenge senior management.

The Chief Executive Officer develops, drives and delivers performance within strategic goals, commercial objectives and business plans agreed by the Board. He effectively leads the senior management in the day-to-day running of the bank, ensures compliance with appropriate policies and procedures and maintains an effective framework of internal controls over risk in relation to the business. He is also responsible for the recruitment and appointment of senior management, after consultation with the Board.

Principle 3: Composition of the Board

Experience has shown that the size of the Board is appropriate to ensure the effective management and oversight over the bank's operations. The Board is composed of nine Directors; each of whom is skilful, competent, knowledgeable and experienced to fulfil one's role diligently. Each Director possesses the requisite ability to assess business risk and to identify key performance indicators.

In terms of the Board Diversity Policy, board appointments are based on merit and potential board members are considered against objective criteria, having due regard for the benefits of diversity on the Board, including gender.

As at 31 December 2014 the Board was composed of a non-executive independent Chairman, an executive Director, seven non-executive Directors, five of whom are deemed to be independent. The non-executive Directors bring an external perspective to the Board when they constructively challenge and help develop proposals on strategy, scrutinise the performance of management, and monitor the risk profile and the reporting of performance.

The independent non-executive Directors as at 31 December 2014 were the following:
Sonny Portelli
Philip Farrugia Randon
Caroline Zammit Testaferrata Moroni Viani
John Bonello
Andrew Muscat
Juanito Camilleri

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 local group's own practice as well as general principles of good practice.

In accordance with the Code Provision 3.2, the Board has determined that the fact that:

- Mr Portelli, Dr Farrugia Randon and Professor Muscat are appointed by the majority shareholder;
- the law firm of which Professor Muscat is a partner, provides legal services to the bank; and
- Mrs Zammit Testaferrata Moroni Viani has directorships in a number of companies which form part of a group of companies which has a business relationship with the bank;

does not in any way impair these Directors' ability to consider appropriately the issues which are brought before the Board. On the other hand, in accordance with Code Provision 3.2.1, the Board believes that Chris Davies' employment with the Group and Brian Robertson's connection with the Group within the last three years renders these directors non-independent from the bank. This should not however, in any manner, detract from the non-independent Directors' ability to maintain independence of free judgement and character at all times.

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

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

Principle 4: The Responsibilities of the Board

The Board develops the bank's strategy, policies and business plans. During 2014, a strategy off-site meeting was specifically held for this purpose. The Board of Directors monitors effectively the implementation of strategy and policy by management 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 evaluation of 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 risk and performance indicators are benchmarked against industry norms so as to ensure that the bank's performance is effectively evaluated.

The Board's informed assessment of management's performance emanates from a clear internal and external reporting system. The Board continuously assesses the bank's strengths and weaknesses in the micro-environment and its opportunities and threats in the macro-environment.

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

The Board ensures that its level of power is known by all Directors and the senior management of the bank. Any delegation of responsibility and functions is clearly documented in the Terms of Reference (TOR) embodied in the corporate governance framework.

The Board delegates specific responsibilities to Committees, which operate under their respective formal TOR:

Audit and Risk Committee

The TOR of this Committee are modelled on the recommendations in the Cadbury Report, the UK Walker Review, and are compliant with the Listing Rules.

The Committee protects the interests of the bank's shareholders. As the name of the Committee suggests, this Committee has a dual function: that of audit and that of risk. This Committee has non-executive responsibility for oversight of, and advice to, the Board on matters relating to financial reporting. From a risk aspect, this Committee is responsible for advising the Board on high level risk related matters. In providing such oversight and advice to the Board, the Committee shall oversee: current and forward looking risk exposures, the bank's risk's appetite and future risk strategy, including capital and liquidity management strategy, and management of risk within the bank.

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

The Committee met seven times during 2014. The members of the Audit and Risk Committee are Mr John Bonello (Chairman), Dr Philip Farrugia Randon LL.D. and Mrs Caroline Zammit Testaferrata Moroni Viani who are independent non-executive Directors.

Attendance at the meetings of this Committee was as follows:

Members	Attended
John Bonello	7 out of 7
Philip Farrugia Randon	5 out of 7
Caroline Zammit Testaferrata Moroni Viani	7 out of 7

Senior Managers of the bank are invited to attend any of the meetings as directed by the Committee. The Chief Executive 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.

Mr Bonello 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 is a Fellow of the Institute of Chartered Accountants in England and Wales and is also a Certified Public Accountant, Auditor and Fellow of the Malta Institute of Accountants. He was formerly the Chairman and Senior Partner of PricewaterhouseCoopers in Malta from where he retired in 2009.

In terms of Listing Rule 5.127.7, the Audit and Risk Committee is responsible for developing and implementing 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.

Nomination and Remuneration Committee
The remuneration aspect of this Committee is dealt with under the Remuneration Report, which also includes the Remuneration Statement in terms of Code Provision 8.A.4.

During 2014 the former Remuneration Committee was reconstituted into a Nomination and Remuneration Committee with the expanded responsibility of leading the process for Board and Board Committee appointments. In its nomination function, the Committee is primarily tasked with identifying and nominating new Board and Board Committees' candidates for the approval of the Board and to periodically assess the structure, size, composition and performance of the Board and make recommendations to the Board with regard to any changes. It is also tasked with considering issues related to succession planning and reviewing the policy of the Board for selection and appointment of senior management. This Committee is also responsible to periodically assess the skills, knowledge and experience of individual directors and report on this to the Board.

Executive Committee ('EXCO')
EXCO 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 Operating Officer together with the senior management of the bank. The EXCO Committee is empowered by its TOR to sub-delegate its powers to sub-committees:

- **The Risk Management Committee**
  This Committee meets on a monthly basis and is chaired by the Chief Executive Officer, with the Chief Risk Officer acting as Deputy Chairman. Membership also includes the Chief Operating Officer, the Chief Financial Officer, the Head of Retail Banking and Wealth Management, the Head of Commercial Banking, the Head of Global Banking and Markets, the Head of Wholesale and Markets Risk, the Head of Credit Risk Management, Analytics and Systems, the Head of Internal Audit, General Counsel and the Head of Security and Fraud Risk.

  This Committee is responsible for all risks in all businesses, functions and subsidiaries under the ownership of HSBC Bank Malta p.l.c., including inter alia Credit Risk, Market Risk, Operational Risk, Concentration Risk, Legal and Regulatory Risk, Security and Fraud Risk and Reputational Risk. The Risk Management Committee is also responsible for the setting and monitoring of a Risk Appetite Framework for EXCO and Board approval, signing off on material credit risk models, and consideration of top and emerging risks, risk map and scenario analysis. Individual risk acceptance and approval is not within the TOR of the Committee, and continues to be approved under existing delegated authorities within the management structure of the bank.

  Minutes of meetings of this Committee are circulated to the members of the Board. The Chief Risk Officer also attends Board meetings and meetings of the Audit and Risk Committee in which representations are made about the overall risk profile associated with the business including a comprehensive assessment of the bank's management of risk.

- **The Asset and Liability Management Committee ('ALCO')**
  This Committee reviews the financial risks of the local group and oversees the prudent management of interest rate risk, liquidity and funding risk, capital, foreign exchange risk, solvency risk, 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. ALCO monitors the capital adequacy making use of capital forecasts to ensure that enough capital is readily available at all times to meet the demand arising from business expansion and regulation. ALCO monitors and reviews the duration and cash flow matching of insurance assets and liabilities.

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 Operating Officer, meets once a month.

- **Global Standards In-Country Execution Committee**

  The Global Standards In-Country Execution Committee manages delivery and execution of the Global Standards Programme, a Group-wide initiative aimed to ensure consistent application of the highest standards throughout the Group.

  The membership of this Committee, which is chaired by the bank's Chief Executive Officer, is composed of all the senior managers and key Global Standards personnel. This Committee meets on a monthly basis.

Principle 5: Board Meetings

The Board meets on a quarterly basis, unless further meetings are required to discharge its duties effectively. During the period under review the Board held seven meetings.

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 short 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.

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

Besides Board meetings, Directors participate in strategy sessions and seminars on the bank's financial performance. They also attend other bank functions like the Let's Lead Conference and meetings with the bank's Talent Pool. All the Directors dedicate the necessary time and attention to their duties as Directors of the bank.

Directors' Attendance at Board Meetings:

Members	Attended
Saviour sive Sonny Portelli	7 out of 7
Mark Watkinson	7 out of 7
Ranjit Gokarn (resigned on 9 May 2014)	1 out of 3
Christopher Davies (appointed on 9 May 2014)	3 out of 6
Brian Robertson	4 out of 7
Philip Farrugia Randon	7 out of 7
James Dunbar Cousin (resigned on 1 July 2014)	4 out of 5
Caroline Zammit Testaferrata Moroni Viani	7 out of 7
John Bonello	7 out of 7
Andrew Muscat (appointed on 16 January 2014)	7 out of 7
Juanito Camilleri (appointed on 5 September 2014)	1 out of 1

Principle 6: Information and Professional Development

The Board appoints the Chief Executive Officer of the bank upon guidance and recommendation from the HSBC Group. The Board is consulted on the appointment of other members of senior management. This enables the bank to avail itself of the vast wealth of competence, talent and experience found across the Group.

Full, formal and tailored induction programmes, with particular emphasis on the systems of risk management and internal controls are arranged for newly appointed Directors. The programmes consist of a series of meetings with senior executives to enable new Directors to familiarise themselves with the bank's strategy, risk appetite, operations and internal controls. Directors also receive comprehensive guidance on Directors' duties and liabilities.

Directors also have access to the advice and services of the Company Secretary who is responsible for adherence to Board procedures as well as for effective information flows within the Board, its Committees and with senior management. The Company Secretary also coordinates a development programme based on the Director's individual needs.

Directors are given opportunities to update and develop their skills and knowledge, through briefings by senior executives and externally-run seminars throughout their directorship. Moreover, Directors have access to independent professional advice, at the bank's expense.

The Chairman of the Board and the Chairman of the Audit and Risk 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 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. They also encourage members of management to move to the higher ranks within the organisation and seek to maintain high morale amongst the bank's personnel.

Principle 7: Evaluation of the Board Performance

During the year an external evaluation of the performance of the Chairman, the Board and that of its committees was conducted by the Company Secretary of UK HSBC Bank plc. The aim of this evaluation was to ascertain the effectiveness of the roles and responsibilities of the Board and its committees, Board structure and composition, Board processes and Board behaviour. This review consisted of separate interviews with each Board member and key EXCO members and an analysis of Board practices, procedures and documentation.

No material recommendations resulted from this thorough Board evaluation exercise.

Principle 8: Committees

The Nomination and Remuneration Committee is dealt with under the Remuneration Report, which also includes the Remuneration Statement in terms of Code provisions 8.A.4.

The Nomination Committee is dealt with under Principle 4 and under the Remuneration Report.

Principles 9 and 10: Relations with Shareholders, with the Market, and with Institutional Shareholders

The bank maintains on-going 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 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 bank communicates with shareholders in two main ways:

- through the 'Annual Report and Accounts' which is mailed to every shareholder and is available on the bank's website;
- at the Annual General Meeting and Extraordinary General Meetings (further detail is provided under the section 'General Meetings').

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. Moreover, the Chairmen of the Audit and Risk Committee and the Nomination and Remuneration Committee are available to answer questions during the Annual General Meeting. 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 request 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.

In line with HSBC Group best practice, the Board operates a Conflicts Policy. In terms of this policy a Director is to avoid situations in which he or she has, or could have, a direct or indirect interest that conflicts, or possibly may conflict, with the interest of the bank. This policy stipulates that there is a basic assumption that any position outside the HSBC Group held in the financial services sector will be assumed to be in conflict unless separately approved by the Chairman together with an explanation as to why no conflict would be deemed to exist.

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 (the Foundation).

Sustainability is core to the way we operate at HSBC and it is recognised that the bank has a responsibility that spreads far wider. The three pillars of the HSBC Malta Foundation aim to improve the quality of life and education for children, especially those disadvantaged, to promote and work towards a more sustainable environment and to preserve Malta's rich and unique historical heritage.

Voluntary work is highly encouraged and pride is taken in HSBC staff who contribute to the charities and causes that they feel passionate about and are encouraged to take an active role in initiatives supported by the Foundation with an extra day's leave granted for voluntary work. HSBC staff are divided into five teams under the "HSBC Cares" to help to drive our commitment and passion for assisting in the community with the key objective of taking part and broadening the involvement level across the bank.

Sustainability and our role as a good corporate citizen remains a core part of HSBC. Last year the Catch the Drop Campaign was launched and this will reach every student in Malta with the main emphasis on water shortage, water consumption reduction and water harvesting over a 3 year period. Our employees are at the heart of this campaign with over 200 members of staff volunteering to deliver the information sessions in the various schools.

Ongoing with this campaign HSBC Malta and HSBC staff in Malta are also helping a school in Ghana improve its access to safe water and better sanitation and hygiene.

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'. The bank discloses that it can comply with this provision only partially. In terms of its Memorandum and Articles of Association, the bank's shareholders lead the process for Board appointments, unless the need arises to fill in casual vacancies. The Board is nonetheless satisfied that the HSBC Group has talented persons within its global structures who could fill in vacant executive positions at Board level, thus ensuring an orderly succession thereto.

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-executive Directors to ensure that no such conflicts arise.

Listing Rule 5.97.4

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 and mitigate 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 Group is reviewing the risk management and internal control structure referred to as the 'three lines of defence' to ensure we achieve our commercial aims while meeting regulatory, legal as well as Group requirements. It is a key part of our operational risk management framework.

- First line – The First Line of Defence consists of Risk Owners and Control Owners. The bank's Global business employees are the 'Risk Owners'. They own the risk, set the risk appetite and are accountable for managing the risk associated with their commercial activities. In managing the risk they are responsible to both manage their own controls and work closely with other Control Owners who sit outside of their area. 'Control Owners' exist in global Businesses, global functions and HTS (HSBC Technology Services). They are accountable for the controls required to manage the risk associated with our commercial activities. They are required to monitor and provide an opinion on the effectiveness of the controls relied upon by the Risk Owners to manage their risk(s).
- Second line – The Second Line of Defence consists of 'Risk Stewards' and their teams. It is made up in part (but not exclusively) by leaders within Global Risk and other Global Functions. They set policy, give advice and provide independent challenge. In doing this, they oversee and assess the risk management activities carried out by the First Line. The Risk Stewards set the overall maximum risk appetite for their particular risk type (e.g. financial crime risk, regulatory compliance risk, legal risk, tax risk, accounting risk, people risk, fraud risk) and support the Risk Owners with setting their risk appetite within Group's overall risk appetite.
- Third line – The Third Line Defence is Global Audit, and it independently assures that the design and operating effectiveness of Group's framework of risk management, governance and internal control are adequate.

HSBC's key risk management and internal control procedures include the following:

- Global standards. Functional, operating, financial reporting and certain management reporting standards are established by global function management committees, for application throughout HSBC globally. These are supplemented by operating standards set by functional and local management as required for the type of business and geographical location of each subsidiary.
- Delegation of authority within limits set by the Board. The Board has delegated specific, clear and unequivocal authority to the Chief Executive Officer to manage the day-to-day affairs of the business for which he is accountable within limits set by the Board. Delegation of authority from the Board requires the CEO to maintain appropriate apportionment of significant responsibilities and to oversee the establishment and maintenance of systems of control that are appropriate to the business.
- Risk identification and monitoring. Systems and procedures are in place to identify, control and report on the major risks facing the bank including credit, market, liquidity, capital, financial management, model, reputational, strategic, sustainability and operational (including accounting, tax, legal, compliance, fiduciary, information, external fraud, internal fraud, political, physical, business continuity, systems operations, project and people risk). Exposure to these risks is monitored by the Risk Management Committee, Asset and Liability Committee and Executive Committee.
- Changes in market conditions/practices. Processes are in place to identify new risks arising from changes in market conditions/practices or customer behaviours, which could expose the bank to heightened risk of loss or reputational damage. During 2014, attention was focused on: regulatory developments including transition to the single Supervisory Mechanism; regulatory commitments and consent orders including the Deferred Prosecution Agreement; challenges to achieving our strategy in a downturn; internet crime and fraud; social media risk; level of change creating operational complexity and heightened execution risk; information security risk.

- IT operations. Centralised functional control is exercised over all IT developments and operations. Common Group systems are employed for similar business processes wherever practicable. In order to ensure consistency and benefit from economies of scale, Common Group systems are employed, where possible, for similar business processes.
- Comprehensive annual financial plans are prepared, reviewed and approved by the Board. Results are monitored and progress reports are prepared on a monthly basis to enable comparisons with plan. Financial accounting and management reporting standards have been established.
- Responsibilities for financial performance against plans and for capital expenditure, credit exposures and market risk exposures are delegated with limits to executive management. In addition, functional management in the bank has been given the responsibility to implement HSBC policies, procedures and standards for business and product lines; finance; legal and regulatory compliance; internal audit; human resources; credit risk; market risk; operational risk; computer systems and operations and property management.
- The Chief Risk Officer is responsible for the management of specific risks within the bank including credit risk in the wholesale and retail portfolios, compliance risks, markets risk and operational risk. Risks are monitored via regular Risk Management Committee's meetings and via reporting to the Executive Committee, the Audit and Risk Committee and to the Board.
- Internal Audit. The establishment and maintenance of appropriate systems of risk management and internal control is primarily the responsibility of business management. The Internal Audit function reports to the Board. It provides independent and objective assurance in respect of adequacy of the design and operating effectiveness of the bank's framework of risk management, control and governance processes focusing on the areas of greatest risk to the bank using a risk-based approach. The Head of Internal Audit also reports to the Head of Global Internal Audit in so far as independence and resourcing are concerned.
- Internal Audit recommendations. Executive management is responsible for ensuring that recommendations made by the Internal Audit function are implemented within an appropriate and agreed timetable. Confirmation to this effect must be provided to Internal Audit.
- The bank's Compliance Department ensures that HSBC Bank Malta Group maintains 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 and Risk 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.

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 and remuneration 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 entitle 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 is unable to 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 Directors or such persons as the Directors may delegate for that purpose.

Governance

Role of the Remuneration Committee

The bank's Nomination and Remuneration Committee (the Committee) within its remuneration oversight responsibilities is primarily responsible for making recommendations on the reward policy, on fixed and variable pay, and for ensuring their implementation.

The Committee works in conjunction with the HSBC Group Remuneration Committee (the 'Group's Committee'). However it has its own TOR, which sets out its key responsibilities in relation to HSBC Bank Malta p.l.c.

During the year the Committee amended its TOR to reconstitute itself into a Nomination and Remuneration Committee endowing the Committee with the power to lead the process for Board and Board Committee appointments.

Membership & Meetings

The Committee's membership consists of an independent Chairman and two independent non-executive Directors.

During the period under review the Committee was originally composed of Mr John Bonello as Chairman and Dr Philip Farrugia Randon (independent non-executive director) and Mr James Dunbar Cousin (independent non-executive director) as members. Subsequently, Prof. Juanito Camilleri (independent non-executive director) was appointed Member of the Committee in lieu of Mr James Dunbar Cousin. Dr Philip Farrugia Randon retained his membership on the Committee.

Two meetings were held by the Committee during 2014 and were attended as follows:

John Bonello	(2 out of 2)
Philip Farrugia Randon	(1 out of 2)
James Dunbar Cousin	(1 out of 1)
Juanito Camilleri	(Did not attend as he was appointed after the Committee's last meeting)

The Chief Executive Officer, the Chief Risk Officer and the Head of Human Resources attended all the Committee's meetings. None of the executives participated in the discussion regarding their own remuneration.

In 2014, the Committee did not engage any external adviser. It will only seek specific legal and/or remuneration advice independently as and when it considers this to be necessary.

Remuneration Strategy and Policy, and the link to Performance and Risk

HSBC Bank Malta p.l.c. remuneration policy

The bank's reward policy was approved by the Board of the bank in 2011 and is reviewed annually. There were no significant changes to this policy during 2014. No material changes are being envisaged during 2015.

The bank's reward policy is aligned to the Banking Rule 12, the Capital Requirements Directive and the Group's reward strategy.

In determining remuneration levels for performance year 2014, the Committee applied the bank's remuneration strategy and policy, which takes into account the interests of shareholders, HSBC Group and the broader external context.

The Bank's Reward Strategy

The quality and long-term commitment of all employees is fundamental to the bank's success. The bank therefore aims to attract, retain and motivate the very best people who are committed to maintaining a long-term career with the bank, and who will perform their role in the long-term interests of the shareholders. HSBC's reward package comprises three key elements:

a. Fixed Pay,
b. Benefits, and
c. Annual Variable Pay.

These elements support the achievement of the bank's objectives through balancing reward for both short-term and long-term sustainable performance. This strategy is designed to reward only success, and aligns employees' remuneration with the bank's risk framework and risk outcomes.

For senior employees, where appropriate, part of their reward is deferred, and thereby subject to malus, that is, it can be cancelled if warranted by events. In order to ensure alignment between what the bank pays its employees and the bank's business strategy, individual performance is assessed against annual and long-term financial and non-financial objectives summarised in performance scorecards. This assessment also takes into account adherence to the HSBC Values of being 'open, connected and dependable' and acting with 'courageous integrity'. Altogether, performance is therefore judged not only on what is achieved over the short and long term but also importantly on how it is achieved, as the bank believes the latter contributes to the long-term sustainability of the business.

Structure of Remuneration

The following table shows the purpose and relevant features of each of the three key elements of the HSBC's reward package. For the purposes of the Annual Variable Pay element, Material Risk Takers represent those members of staff whose professional activities have a material impact on the risk profile of the bank.

Description	Purpose and Relevant features	Senior Management	NEDs
Fixed Pay	Fixed pay reflects the individual's role, experience and responsibility. Changes are made within the context of local requirements and market practice. Base salaries are benchmarked on an annual basis against relevant comparator groups.	Y	
Fees	The fee levels payable reflect the time commitment and responsibilities required of a non-executive Director. Fees are determined by benchmark against other companies and banks.		Y
Variable Pay – annual incentive	Drives and rewards performance against annual financial and non-financial measures and adherence to HSBC Values which are consistent with the medium to long-term strategy and aligns to shareholder interests. Deferral structure provides retention value and the ability to apply malus. For higher earners, part of the annual incentive is deferred over a period of three years. The award is non-pensionable. For employees designated as Material Risk Takers ('MRTs') the variable component of remuneration will not exceed 100% of the fixed component.	Y	

Variable Pay Funding

Funding of the bank's annual variable pay pool is determined in the context of profitability and affordability. The Committee considers many factors in approving the overall variable pay pool. These include, but are not limited to, the performance of the bank and the performance of the HSBC Group, considered within the context of the bank's risk appetite. This ensures that the variable pay pool is shaped by risk considerations and factors in any local or Group-wide notable events. The Committee reviews the pay-out-ratio within the context of profitability and affordability. The commercial requirement to remain competitive in the market is also taken into account.

Performance Measurement and Risk Adjustment

Under the bank's remuneration framework, remuneration individual decisions are made based on a combination of: performance against objectives, general individual performance of the role, and adherence to the HSBC values, business principles, Group risk-related policies and procedures and Global Standards.

In order solely to reward genuine performance, individual awards are made on the basis of a risk adjusted view of both financial and non-financial performance. In light of this, the bank has discretion to reduce an employee's current year variable pay to reflect detrimental conduct or involvement in Group-wide notable events or local issues.

The Committee can also make recommendations to the Group Remuneration Committee, which has the authority in certain circumstances, to reduce or cancel all or part of any unvested deferred award under the applicable malus provision. Appropriate circumstances include (but are not limited to) conduct detrimental to the business; past performance being materially worse than originally understood; restatement, correction or amendment of any financial statements; or improper or inadequate risk management. The Group Remuneration Committee can also suspend the vesting of unvested deferred awards granted in prior years where the awards are scheduled to vest before the outcome of a review of a Group-wide notable event is known.

Adjustments would generally be made to the current year variable pay before application of malus and clawback is considered. Details of the circumstances where an adjustment, malus and/or clawback will be considered is set out below:

Type of action	Type of variable pay award affected	Circumstances where it may apply (including, but not limited to):
Adjustment	Current year variable pay	• Detrimental conduct or conduct which brings the business into disrepute. • Involvement in Group-wide events resulting in significant operational losses, including events which have caused or have the potential to cause significant harm to HSBC. • Non-compliance with HSBC Values and other mandatory requirements. • For specified individuals, insufficient yearly progress in developing an effective AML and sanctions compliance programme or non-compliance with the DPA and other relevant orders.
Malus	Unvested deferred awards granted in prior years	• Detrimental conduct or conduct which brings the business into disrepute. • Past performance being materially worse than originally reported. • Restatement, correction or amendment of any financial statements. • Improper or inadequate risk management.
Clawback	Vested or paid awards	• Participation in or responsibility for conduct which results in significant losses. • Failing to meet appropriate standards of fitness and propriety. • Reasonable evidence of misconduct or material error that would justify, or would have justified, summary termination of a contract of employment. • HSBC or a business unit suffers a material failure of risk management within the context of Group risk management standards, policies and procedures.

Remuneration Policy – Non Executive Directors

Non-executive Directors are not employees and receive a fee for their services as Directors. In addition, it is common practice for non-executive Directors to be reimbursed expenses incurred in performing their role and any related tax. They are not eligible to receive a base salary, fixed pay allowance, benefits, pension or any variable pay.

The fee levels payable reflect the time commitment and responsibilities required of a non-executive Director. Fees are determined by reference to other Maltese companies and international banks.

The Board reviews each component of the fees periodically to assess whether, individually and in aggregate, they remain competitive and appropriate in light of changes in roles, responsibilities, and/or the time commitment required for the non-executive Directors and to ensure that individuals of the appropriate calibre are retained or can be appointed. The Board (excluding the non-executive Directors) may approve changes to the fees within the ranges prescribed in the remuneration policy. The Board may also introduce any new component of fee for non-executive Directors subject to the principles, parameters and other requirements set out in the remuneration policy.

The Director’s fees are approved in aggregate by the shareholders at the Annual General Meeting. No change is proposed for the fees of non-executive Directors for 2015.

Remuneration amounts – Non Executive Directors

Fixed Remuneration **€000**	*Variable Remuneration* **€000**	*Share Options* **€000**	*Others* **€000**
178	None	None	None

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

	€
Saviour sive Sonny Portelli	36,000
Caroline Zammit Testaferrata Moroni Viani	27,000
Philip Farrugia Randon	28,800
James Dunbar Cousin	9,900
John Bonello	39,600
Andrew Muscat	17,250
Brian Robertson	13,500
Juanito Camilleri	6,000
Total	178,050

Directors who are employed with the bank or with HSBC Group are not paid any fees for their directorship.

Policy of Senior Executive Contracts

Standard contracts for Senior Executives employed locally would generally be indefinite. Normal retirement from the bank would be in line with local legislation. A three month notice period is required for Senior Executives, who would similarly be entitled to a notice of a minimum of three months in the event that the bank terminates the employment on grounds of redundancy.

International assignees appointed to Senior Executive positions are covered by the standard Group contracts policy. The period of notice required to be given to terminate by either party can be up to six months.

For the purposes of information provided hereunder 'Senior Executives'/'Senior Management' shall mean Executive Committee members.

Remuneration amounts – Senior Management

Fixed Remuneration **€000**	*Variable Remuneration* **€000**	*Share Options* **€000**	*Others* **€000**
1,713	658	119	830

Remuneration Amounts – MRTs

The following tables show the remuneration awards made to MRTs in the bank for 2014. Individuals have been identified as MRTs based on the qualitative and quantitative criteria set out in the Regulatory Technical Standard EU 604/2014.

Aggregate remuneration expenditure

The aggregate remuneration expenditure in the table below includes salary and incentives awarded in respect of performance in the years 2014 (including deferred component) and any pension or benefits outside of policy.

	Global business aligned				
	Retail Banking and Wealth Management	Commercial Banking	Global Banking and Markets	**Non-global business aligned**	**Total**
	€000	**€000**	**€000**	**€000**	**€000**
Aggregate remuneration expenditure	1,326	547	503	2,519	4,895

Remuneration – fixed and variable amounts

	2014		
	Senior management	MRTs (non-senior management)	Total
Number of MRTs	10	45	55
	€000	**€000**	**€000**
Fixed Variable			
Cash	448	405	853
Non-deferred shares	124	36	159
Deferred cash	82	24	106
Deferred shares	82	31	114
Total variable pay	738	496	1,234

Deferred remuneration

	2014		
	Senior management	MRTs (non-senior management)	Total
	€000	**€000**	**€000**
Deferred remuneration at 31 December 2014			
Outstanding, unvested	351	5	356
Awarded during the year	167	–	167
Paid out	115	5	120
Reduced through malus	–	–	–

Sign-on and severance payments

No sign-on and severance payments, the latter by way of early voluntary retirement payments, were made to MRTs during 2014.

MRT remuneration by band

	2014		
	Senior management	MRTs (non-senior management)	Total
€0 – €1,000,000	2,097	2,798	4,895
€1,000,001 – €1,500,000	–	–	–
€1,500,001 – €2,000,000	–	–	–

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 bank and its subsidiaries (the 'local group') as at the end of the financial period and of the profit or loss of the bank and the local 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 local 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, except for the exemptions applicable to the local group, in terms of Article 24 of the Banking Rule 07 (Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised under the Banking Act 1994) partly repealed by certain provisions in Regulation (EU) No 575/2013 (CRR) and Article 13 of CRR in relation to the local group's risk and capital management, on the basis that such disclosures are required at the consolidated level which is HSBC Holdings plc level. The Directors also ensure that the financial statements of the local group are prepared in accordance with Article 4 of the IAS regulation.

The Directors are also responsible for safeguarding the assets of the local 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 local 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:

Sonny Portelli, *Chairman*

Mark Watkinson, *Chief Executive Officer*

Statements of Profit or Loss for the year 1 January 2014 to 31 December 2014

		Group		Bank	
		2014	2013	**2014**	2013
	Note	**€000**	€000	**€000**	€000
Interest and similar income					
– on loans and advances, balances with Central Bank of Malta and Treasury Bills	*7*	**136,234**	143,314	**136,324**	143,306
– on debt and other fixed income instruments	*7*	**17,155**	18,792	**16,646**	18,069
Interest expense	*8*	**(33,227)**	(37,395)	**(33,351)**	(37,503)
Net interest income		**120,162**	124,711	**119,619**	123,872
Fee and commission income		**30,805**	31,332	**27,983**	28,339
Fee and commission expense		**(2,354)**	(1,795)	**(1,688)**	(1,596)
Net fee and commission income	*9*	**28,451**	29,537	**26,295**	26,743
Dividend income	*10*	**–**	–	**20,462**	12,308
Trading profits	*11*	**8,785**	9,523	**8,785**	9,523
Net income from insurance financial instruments designated at fair value		**48,642**	25,528	**–**	–
Net gains on sale of available-for-sale financial investments	*12*	**1,719**	4,295	**1,719**	4,352
Movement in present value of in-force long-term insurance business		**(11,486)**	(3,130)	**–**	–
Net other operating income	*13*	**1,584**	1,676	**1,689**	969
Net earned insurance premiums	*14*	**60,031**	66,073	**–**	–
Total operating income		**257,888**	258,213	**178,569**	177,767
Net insurance claims incurred and movement in policyholders' liabilities	*15*	**(84,628)**	(71,201)	**–**	–
Net operating income		**173,260**	187,012	**178,569**	177,767
Employee compensation and benefits	*16*	**(51,744)**	(48,539)	**(49,123)**	(45,335)
General and administrative expenses		**(40,175)**	(38,483)	**(37,170)**	(35,829)
Depreciation	*29*	**(3,460)**	(3,449)	**(3,449)**	(3,440)
Amortisation	*28*	**(3,092)**	(2,844)	**(3,036)**	(2,824)
Net operating income before impairment charges and provisions		**74,789**	93,697	**85,791**	90,339
Net impairment	*17*	**(22,545)**	(3,272)	**(22,545)**	(3,272)
Net provisions for liabilities and other charges	*41*	**(123)**	52	**(123)**	52
Profit before tax	*18*	**52,121**	90,477	**63,123**	87,119
Tax expense	*19*	**(18,504)**	(31,760)	**(22,741)**	(30,704)
Profit for the year		**33,617**	58,717	**40,382**	56,415
Profit attributable to shareholders		**33,617**	58,717	**40,382**	56,415
Earnings per share	*20*	**10.4c**	18.1c	**12.5c**	17.4c

The notes on pages 49 to 119 are an integral part of these financial statements.

Statements of Profit or Loss and Other Comprehensive Income for the year 1 January 2014 to 31 December 2014

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Profit for the year	**33,617**	58,717	**40,382**	56,415
Other comprehensive income				
Items that may be reclassified to Profit or Loss:				
Available-for-sale investments:				
– fair value gains	**13,656**	305	**13,810**	655
– fair value gains transferred to profit or loss on disposal	**(1,719)**	(4,295)	**(1,719)**	(4,352)
– income taxes	**(4,178)**	1,396	**(4,232)**	1,294
	7,759	(2,594)	**7,859**	(2,403)
Items that will not be reclassified to Profit or Loss:				
Properties:				
– revaluation	**(28)**	84	**(28)**	84
– income taxes	**3**	(20)	**3**	(20)
	(25)	64	**(25)**	64
Other comprehensive income for the year, net of tax	**7,734**	(2,530)	**7,834**	(2,339)
Total comprehensive income	**41,351**	56,187	**48,216**	54,076

The notes on pages 49 to 119 are an integral part of these financial statements.

Statements of Financial Position at 31 December 2014

		Group		*Bank*	
		2014	2013	**2014**	2013
	Note	**€000**	€000	**€000**	€000
Assets					
Balances with Central Bank of Malta, Treasury Bills and cash	*21*	**118,033**	151,458	**118,033**	151,457
Cheques in course of collection		**10,990**	9,703	**10,990**	9,703
Derivatives	*22*	**13,170**	12,666	**13,098**	12,666
Financial assets designated at fair value	*23*	**1,421,580**	477,345	**–**	–
Financial investments	*24*	**1,153,884**	918,292	**1,137,697**	897,794
Loans and advances to banks	*25*	**875,095**	564,790	**796,257**	564,675
Loans and advances to customers	*26*	**3,273,381**	3,300,982	**3,284,881**	3,300,982
Shares in subsidiary companies	*27*	**–**	–	**34,541**	35,707
Intangible assets	*28*	**73,971**	86,618	**8,989**	10,093
Property, plant and equipment	*29*	**59,481**	61,491	**59,573**	61,575
Investment property	*30*	**16,326**	14,529	**11,667**	11,660
Non-current assets held for sale	*31*	**9,297**	11,783	**9,297**	11,783
Current tax assets		**8,833**	7,939	**3,258**	2,720
Deferred tax assets	*36*	**13,612**	12,522	**13,602**	12,504
Other assets	*32*	**106,604**	52,735	**8,946**	9,432
Prepayments and accrued income	*33*	**44,730**	38,677	**35,898**	33,673
Total assets		**7,198,987**	5,721,530	**5,546,727**	5,126,424
Liabilities					
Derivatives	*22*	**13,870**	12,929	**13,419**	12,929
Deposits by banks	*34*	**59,848**	41,794	**59,848**	41,794
Customer accounts	*35*	**4,867,124**	4,517,862	**4,931,485**	4,554,104
Current tax liabilities		**172**	16	**–**	–
Deferred tax liabilities	*36*	**28,244**	25,195	**–**	–
Liabilities under investment contracts	*37*	**1,020,594**	16,763	**–**	–
Liabilities under insurance contracts	*38*	**602,712**	524,999	**–**	–
Other liabilities	*39*	**44,103**	38,274	**30,138**	30,707
Accruals and deferred income	*40*	**27,514**	30,230	**26,070**	29,419
Provisions for liabilities and other charges	*41*	**2,417**	3,211	**2,417**	3,149
Subordinated liabilities	*42*	**87,284**	87,273	**88,093**	88,040
Total liabilities		**6,753,882**	5,298,546	**5,151,470**	4,760,142
Equity					
Called up share capital	*43*	**97,281**	87,552	**97,281**	87,552
Revaluation reserve	*44*	**42,510**	35,107	**42,139**	34,636
Retained earnings	*44*	**305,314**	300,325	**255,837**	244,094
Total equity		**445,105**	422,984	**395,257**	366,282
Total liabilities and equity		**7,198,987**	5,721,530	**5,546,727**	5,126,424
Memorandum items					
Contingent liabilities	*45*	**133,448**	111,852	**135,151**	113,555
Commitments	*46*	**1,291,225**	1,269,222	**1,295,275**	1,273,196

The notes on pages 49 to 119 are an integral part of these financial statements.

The financial statements on pages 43 to 119 were approved and authorised for issue by the Board of Directors on 23 February 2015 and signed on its behalf by:

Sonny Portelli, *Chairman*

Mark Watkinson, *Chief Executive Officer*

Statements of Changes in Equity for the year 1 January 2014 to 31 December 2014

	Note	*Share capital* €000	*Revaluation reserve* €000	*Retained earnings* €000	*Total equity* €000
Group					
At 1 January 2014		**87,552**	**35,107**	**300,325**	**422,984**
Profit for the year		**–**	**–**	**33,617**	**33,617**
Other comprehensive income					
Available-for-sale investments:					
– fair value gains, net of tax		**–**	**8,877**	**–**	**8,877**
– fair value gains transferred to profit or loss on disposal, net of tax		**–**	**(1,118)**	**–**	**(1,118)**
Properties:					
– release of revaluation reserve on disposal, net of tax		**–**	**(331)**	**331**	**–**
– revaluation of properties, net of tax		**–**	**(25)**	**–**	**(25)**
Total other comprehensive income		**–**	**7,403**	**331**	**7,734**
Total comprehensive income for the year		**–**	**7,403**	**33,948**	**41,351**
Transactions with owners, recognised directly in equity					
Contributions by and distributions to owners:					
– share-based payments		**–**	**–**	**119**	**119**
– dividends	*48*	**–**	**–**	**(19,349)**	**(19,349)**
– bonus issue	*43*	**9,729**	**–**	**(9,729)**	**–**
Total contributions by and distributions to owners		**9,729**	**–**	**(28,959)**	**(19,230)**
At 31 December 2014		**97,281**	**42,510**	**305,314**	**445,105**
At 1 January 2013		87,552	37,637	275,409	400,598
Profit for the year		–	–	58,717	58,717
Other comprehensive income					
Available-for-sale investments:					
– fair value gains, net of tax		–	198	–	198
– fair value gains transferred to profit or loss on disposal, net of tax		–	(2,792)	–	(2,792)
Properties:					
– revaluation of properties, net of tax		–	64	–	64
Total other comprehensive income		–	(2,530)	–	(2,530)
Total comprehensive income for the year		–	(2,530)	58,717	56,187
Transactions with owners, recognised directly in equity					
Contributions by and distributions to owners:					
– share-based payments		–	–	155	155
– dividends	*48*	–	–	(33,956)	(33,956)
Total contributions by and distributions to owners		–	–	(33,801)	(33,801)
At 31 December 2013		87,552	35,107	300,325	422,984

The notes on pages 49 to 119 are an integral part of these financial statements.

	Note	Share capital €000	Revaluation reserve €000	Retained earnings €000	Total equity €000
Bank					
At 1 January 2014		**87,552**	**34,636**	**244,094**	**366,282**
Profit for the year		**–**	**–**	**40,382**	**40,382**
Other comprehensive income					
Available-for-sale investments:					
– fair value gains, net of tax		**–**	**8,977**	**–**	**8,977**
– fair value gains transferred to profit or loss on disposal, net of tax		**–**	**(1,118)**	**–**	**(1,118)**
Properties:					
– release of revaluation reserve on disposal, net of tax		**–**	**(331)**	**331**	**–**
– revaluation of properties, net of tax		**–**	**(25)**	**–**	**(25)**
Total other comprehensive income		**–**	**7,503**	**331**	**7,834**
Total comprehensive income for the year		**–**	**7,503**	**40,713**	**48,216**
Transactions with owners, recognised directly in equity					
Contributions by and distributions to owners:					
– share-based payments		**–**	**–**	**108**	**108**
– dividends	*48*	**–**	**–**	**(19,349)**	**(19,349)**
– bonus issue	*43*	**9,729**	**–**	**(9,729)**	**–**
Total contributions by and distributions to owners		**9,729**	**–**	**(28,970)**	**(19,241)**
At 31 December 2014		**97,281**	**42,139**	**255,837**	**395,257**
At 1 January 2013		87,552	36,975	221,494	346,021
Profit for the year		–	–	56,415	56,415
Other comprehensive income					
Available-for-sale investments:					
– fair value gains, net of tax		–	426	–	426
– fair value gains transferred to profit or loss on disposal, net of tax		–	(2,829)	–	(2,829)
Properties:					
– revaluation of properties, net of tax		–	64	–	64
Total other comprehensive income		–	(2,339)	–	(2,339)
Total comprehensive income for the year		–	(2,339)	56,415	54,076
Transactions with owners, recognised directly in equity					
Contributions by and distributions to owners:					
– share-based payments		–	–	141	141
– dividends	*48*	–	–	(33,956)	(33,956)
Total contributions by and distributions to owners		–	–	(33,815)	(33,815)
At 31 December 2013		87,552	34,636	244,094	366,282

The notes on pages 49 to 119 are an integral part of these financial statements.

Statements of Cash Flows for the year 1 January 2014 to 31 December 2014

		Group		*Bank*	
		2014	2013	**2014**	2013
	Note	**€000**	€000	**€000**	€000
Cash flows from operating activities					
Interest, commission and premium receipts		**241,480**	256,793	**172,609**	182,462
Interest, commission and claims payments		**(87,678)**	(89,324)	**(37,839)**	(42,640)
Payments to employees and suppliers		**(89,873)**	(86,291)	**(85,113)**	(83,616)
Operating profit before changes in operating assets/liabilities		**63,929**	81,178	**49,657**	56,206
Decrease/(increase) in operating assets:					
Financial assets designated at fair value		**14,835**	171	**–**	–
Reserve deposit with Central Bank of Malta		**(3,358)**	1,242	**(3,358)**	1,242
Loans and advances to customers and banks		**1,262**	42,900	**3,870**	42,900
Treasury Bills		**44,227**	(46,845)	**44,227**	(46,845)
Other receivables		**(40,824)**	(8,861)	**(576)**	(3,085)
Increase/(decrease) in operating liabilities:					
Customer accounts and deposits by banks		**315,261**	6,906	**343,507**	22,674
Other payables		**35,343**	7,330	**(3,583)**	6,455
Net cash from operating activities before tax		**430,675**	84,021	**433,744**	79,547
Tax paid		**(21,529)**	(32,682)	**(20,875)**	(26,446)
Net cash from operating activities		**409,146**	51,339	**412,869**	53,101
Cash flows from investing activities					
Dividends received		**–**	21	**14,370**	8,000
Interest received from financial investments		**39,435**	30,255	**23,792**	26,719
Purchase of financial investments		**(413,566)**	(277,694)	**(413,566)**	(275,655)
Proceeds from sale and maturity of financial investments		**217,133**	334,396	**212,926**	328,537
Purchase of property, plant and equipment, investment property and intangible assets		**(5,264)**	(12,087)	**(3,546)**	(12,000)
Proceeds on sale of property, plant and equipment, intangible assets and liquidation of subsidiary company		**81**	476	**56**	476
Net cash flows (used in)/from investing activities		**(162,181)**	75,367	**(165,968)**	76,077
Cash flows from financing activities					
Dividends paid		**(19,349)**	(33,956)	**(19,349)**	(33,956)
Cash used in financing activities		**(19,349)**	(33,956)	**(19,349)**	(33,956)
Increase in cash and cash equivalents		**227,616**	92,750	**227,552**	95,222
Effect of exchange rate changes on cash and cash equivalents		**(31,354)**	(33,029)	**(31,354)**	(33,029)
Net increase in cash and cash equivalents		**258,970**	125,779	**258,906**	128,251
		227,616	92,750	**227,552**	95,222
Cash and cash equivalents at beginning of year		**521,411**	428,661	**521,295**	426,073
		749,027	521,411	**748,847**	521,295
Cash balance on portfolio transfer by subsidiary company		**78,658**	–	**–**	–
Cash and cash equivalents at end of year	*49*	**827,685**	521,411	**748,847**	521,295

The notes on pages 49 to 119 are an integral part of these 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 local group as at and for the year ended 31 December 2014 comprise the bank and its subsidiaries.

2 Basis of preparation

a *Statement of compliance*

These financial statements have been prepared and presented in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU.

All references in these financial statements to IAS, IFRS or SIC/IFRIC interpretations refer to those adopted by the EU.

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

During 2014 the local group adopted the following amendments to standards and interpretations for the first time for the financial year beginning on or after 1 January 2014:

– Amendment to IAS 32, 'Financial instruments: Presentation' on offsetting financial assets and financial liabilities. This amendment clarifies that the right of set-off must not be contingent on a future event. It must also be legally enforceable for all counterparties in the normal course of business, as well as in the event of default, insolvency or bankruptcy. The amendment also considers settlement mechanisms.

– Amendments to IAS 36, 'Impairment of assets', on the recoverable amount disclosures for non-financial assets. This amendment removed certain disclosures of the recoverable amount of CGUs which had been included in IAS 36 by the issue of IFRS 13.

– Amendment to IAS 39, 'Financial instruments: Recognition and measurement' on the novation of derivatives and the continuation of hedge accounting. This amendment considers legislative changes to 'over-the-counter' derivatives and the establishment of central counterparties. The amendment provides relief from discontinuing hedge accounting when novation of a hedging instrument meets specified criteria. Under IAS 39 novation of derivatives to central counterparties would result in discontinuance of hedge accounting.

– IFRIC 21, 'Levies', sets out the accounting for an obligation to pay a levy if that liability is within the scope of IAS 37 'Provisions'. The interpretation addresses what the obligating event is that gives rise to pay a levy and when a liability should be recognised. The local group is not currently subject to significant levies so the impact on the financial statements is not material.

The above amendments did not have a significant effect on the local group's financial statements.

Other standards, amendments and interpretations which are effective for the financial year beginning on 1 January 2014 are not material to the local group.

b *Basis of measurement*

Assets and liabilities are measured at historical cost except for 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 assets designated at fair value;

– Financial investments;

– Property; and

– Liabilities under investment contracts.

2 Basis of preparation *(continued)*

c *Functional and presentation currency*

The financial statements are presented in euro, which is the local group's functional currency. All amounts have been rounded to the nearest thousand, unless otherwise stated.

d *Use of estimates and assumptions*

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

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

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment and judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the financial statements are included in notes 4, 16 and 56.

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 local group entities.

a *Basis of consolidation*

i Consolidation

HSBC Bank Malta p.l.c. controls and consequently consolidates an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The local group is considered to have power over an entity when it has existing rights that give it the current ability to direct the relevant activities. For the local group to have power over an entity, it must have the practical ability to exercise those rights. In the rare situations where potential voting rights exist, these are taken into account if the local group has the practical ability to exercise those rights.

Where voting rights are not relevant in deciding whether the local group has power over an entity, the assessment of control is based on all facts and circumstances. The local group may have power over an entity even though it holds less than a majority of the voting rights, if it holds additional rights arising through other contractual arrangements or substantive potential voting rights which give it power.

When assessing whether to consolidate investment funds, the local group reviews all facts and circumstances to determine whether the local group, as fund manager, is acting as agent or principal, the local group may be deemed to be a principal, and hence controls and consolidates the funds, when it acts as fund manager and cannot be removed without cause, has variable returns through significant unit holdings and/or a guarantee, and is able to influence the returns of the funds by exercising its power.

The acquisition method of accounting is used when subsidiaries are acquired by the local group. The cost of an acquisition is measured at the fair value of the consideration, including contingent consideration, given at the date of exchange. Acquisition-related costs are recognised as an expense in the profit or loss in the period in which they are incurred. The acquired identifiable assets, liabilities and contingent liabilities are generally measured at their fair values at the date of acquisition. Goodwill is measured as the excess of the aggregate of the consideration transferred, the amount of non-controlling interest and the fair value of the local group's previously held equity interest, if any, over the net of the amounts of the identifiable assets acquired and the liabilities assumed.

Changes in a parent's ownership interest in a subsidiary that do not result in a loss of control are treated as transactions between equity holders and are reported in equity.

Entities that are controlled by the local group are consolidated from the date the local group gains controls and cease until the date the bank loses control of the entities.

The bank performs a re-assessment of consolidation whenever there is a change in the facts and circumstances of determining the control of all entities.

3 Significant accounting policies *(continued)*

a *Basis of consolidation (continued)*

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.

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b *Financial instruments*

i Non-derivative financial instruments

Non-derivative financial instruments are recognised on trade date when the local group enters into contractual arrangements with counterparties. These financial instruments are recognised initially at fair value adjusted with, 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, highly liquid investments and deposits with contractual maturity of three months or less. 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 local group's cash management are included as a component of cash and cash equivalents for the purpose of the Statements of Cash Flows. Subsequent to initial recognition, cash and cash equivalents are measured at amortised cost using the effective interest method.

Financial instruments designated at fair value through profit or loss

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 local group designates insurance 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 local group is financial assets under insurance and investment contracts and financial liabilities under investment contracts.

  Liabilities 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 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 local 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/(expense) from insurance financial instruments designated at fair value.

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 re-measured 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, the cumulative gains or losses previously recognised in other comprehensive income are recognised in profit or loss as Net gains on sale of available-for-sale financial investments.

Unquoted equity securities, the fair value of which cannot be reliably measured, are carried at cost less impairment.

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 and that the local group does not intend to sell immediately or in the near term. Loans and advances are recognised either when the cash is advanced to the borrowers or when funds are placed with other banks. They are subsequently measured at amortised cost using the effective interest method, less impairment losses.

Loans and advances to banks and customers are classified as loans and receivables.

Subordinated liabilities, deposits by banks and customer accounts

Financial liabilities are recognised when the local group enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at fair value, which is normally the consideration received, net of directly attributable transaction costs incurred. Subsequent measurement of financial liabilities, other than those measured at fair value through profit or loss and financial guarantees, is at amortised cost, using the effective interest rate method to amortise the difference between proceeds received, net of directly attributable transaction costs incurred, and the redemption amount over the expected life of the instrument.

ii Derivative financial instruments

Derivatives are recognised initially and are subsequently re-measured 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 in 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/(expense) from insurance financial instruments designated at fair value. Derivatives that do not qualify for hedge accounting include non-qualifying hedges entered into as part of documented interest rate management strategies for which hedge accounting was not, or could not be applied.

3 Significant accounting policies *(continued)*

b *Financial instruments (continued)*

ii Derivative financial instruments (continued)

Hedge accounting

When derivatives are designated as hedges, the local group 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 local group documents the relationship between the hedging instruments and the hedged items, its risk management objective and its strategy for undertaking the hedge. The local group 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 or cash flows of the hedged items. Interest on designated qualifying hedges is included in Net interest income.

Fair value hedge

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.

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.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income. Any gain or loss in fair value relating to an ineffective portion is recognised immediately in profit or loss.

The accumulated gains and losses recognised in other comprehensive income are reclassified to profit or loss in the periods in which the hedged item will affect profit or loss. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains or losses previously recognised in other comprehensive income are removed from equity and included in the initial measurement of the cost of the asset or liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised in other comprehensive income at that time remains in equity until the forecast transaction is eventually recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in other comprehensive income is immediately reclassified to profit or loss.

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 local 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% to 125%.

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

3 Significant accounting policies *(continued)*

b *Financial instruments (continued)*

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 local 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 expired.

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 local 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 net interest income.

c *Investment in subsidiaries*

HSBC Bank Malta p.l.c. classifies investments in entities which it controls as investments in subsidiaries.

The bank's investments in subsidiaries are stated at cost less any impairment losses.

Impairment losses recognised in prior periods are reversed through profit or loss if, and only if, there has been a change in the estimates used to determine the recoverable amount of the investment in subsidiary since the last impairment loss was recognised.

d *Intangible assets*

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

Software acquired by the local 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.

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. Estimated useful life is the lower of legal duration and expected useful life. 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, plant and equipment*

i Owned assets

Property, plant and equipment are initially measured at cost. Freehold and long leasehold properties are re-measured to fair value on the basis of their existing use. Revaluations are performed by a professionally qualified and independent 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.

3 Significant accounting policies *(continued)*

e *Property, plant and equipment (continued)*

i Owned assets (continued)

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

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

ii Operating leases

All leases which the local group enters into are classified as operating leases. When the local 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 respectively.

iii Subsequent costs

The cost of replacing a component of an item of property, plant 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 local 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, plant 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, plant 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.

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f *Investment property*

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

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 independent valuers who apply recognised valuation techniques. The bank has in place set benchmarks to ensure that these valuers hold the necessary recognised and relevant professional qualifications as well as the knowledge and experience to value this type of properties. Any gain or loss on the disposal of an investment property is recognised in profit or loss. When the use of property changes such that it is reclassified as property, plant and equipment, its fair value at the date of reclassification becomes its cost for subsequent accounting.

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g *Impairment*

i Financial investments: available-for-sale securities

At each reporting date an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset. Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the financial asset (a ‘loss event’) and that loss event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

If the available-for-sale financial asset is impaired, the difference between the financial asset’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, is removed from other comprehensive income and recognised in profit or loss.

3 Significant accounting policies *(continued)*

g *Impairment (continued)*

i Financial investments: available-for-sale securities (continued)

When assessing available-for-sale debt securities for objective evidence of impairment at the reporting date, the local group considers all available evidence, including observable data or information about events specifically relating to the securities which may result in a shortfall in recovery of future cash flows. These events may include a significant financial difficulty of the issuer, a breach of contract such as a default, bankruptcy or other financial reorganisation, or the disappearance of an active market for the debt security because of financial difficulties relating to the issuer.

These types of specific events and other factors such as information about the issuers' liquidity, business and financial risk exposures, levels of and trends in default for similar financial assets, national and local economic trends and conditions, and the fair value of collateral and guarantees may be considered individually, or in combination, to determine if there is objective evidence of impairment of a debt security.

Objective evidence of impairment for available-for-sale equity securities may include specific information about the issuer as detailed above, but may also include information about significant changes in technology, markets, economics or the law that provides evidence that the cost of the equity securities may not be recovered.

A significant or prolonged decline in the fair value of the equity securities classified as available-for-sale below its cost is also objective evidence of impairment. In assessing whether it is significant, the decline in fair value is evaluated against the original cost of the asset at initial recognition. In assessing whether it is prolonged, the decline is evaluated against the period in which the fair value of the asset has been below its original cost at initial recognition.

Once an impairment loss has been recognised on an available-for-sale financial asset, the subsequent accounting treatment for changes in the fair value of that asset differs depending on the nature of the available-for-sale financial asset concerned:

- for an available-for-sale debt security, a subsequent decline in the fair value of the instrument is recognised in profit or loss when there is further objective evidence of impairment as a result of further decreases in the estimated future cash flows of the financial asset. Where there is no further objective evidence of impairment, the decline in the fair value of the financial asset is recognised in other comprehensive income.
- for an available-for-sale equity security, subsequent decreases in the fair value of the available-for-sale equity security are recognised in profit or loss, to the extent that further cumulative impairment losses have been incurred in relation to the acquisition cost of the equity security.

ii Loans and receivables

Losses for impaired loans are recognised promptly when there is objective evidence that impairment of a loan or portfolio of loans has occurred. Impairment allowances are calculated on individual loans and on groups of loans assessed collectively. Impairment losses are recognised in profit or loss. The carrying amount of impaired loans as at the reporting date is reduced through the use of impairment allowance accounts. Losses which may arise from future events are not recognised.

Individually assessed loans and advances

The factors considered in determining whether a loan is individually significant for the purposes of assessing impairment include:

- the size of the loan;
- the number of loans in the portfolio; and
- the importance of the individual loan relationship, and how this is managed.

Loans that meet the above criteria will be individually assessed for impairment, except when volumes of defaults and losses are sufficient to justify treatment under a collective assessment methodology.

3 Significant accounting policies *(continued)*

g *Impairment (continued)*

ii Loans and receivables (continued)

For all loans that are considered individually significant, the local group assesses on a case-by-case basis at each reporting date whether there is any objective evidence that a loan is impaired. The criteria used by the local group to determine that there is such objective evidence include:

– known cash flow difficulties experienced by the borrower;
– contractual payments of either principal or interest being past due for more than 90 days;
– the probability that the borrower will enter bankruptcy or other financial realisation;
– a concession granted to the borrower for economic or legal reasons relating to the borrower's financial difficulty that results in forgiveness or postponement of principal, interest or fees, where the concession is not insignificant; and
– there has been deterioration in the financial condition or outlook of the borrower such that its ability to repay is considered doubtful.

For those loans where objective evidence of impairment exists, impaired losses are determined considering the following factors:

– the local 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 likely dividend available on liquidation or bankruptcy;
– the extent of other creditors' commitments ranking ahead of, or pari passu with, the local 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.

The realisable value of security is determined based on the current market value when the impairment assessment is performed. The value is not adjusted for expected future changes in market prices; however, adjustments are made to reflect local conditions, such as forced sale discounts.

Impairment losses are calculated by discounting the expected future cash flows of a loan, which includes expected future receipts of contractual interest at the loan's original effective interest rate and comparing the resultant present value with the loan's current carrying amount. The impairment allowances on individually significant accounts are reviewed at least annually and more regularly when circumstances require. This normally encompasses re-assessment of the enforceability of any collateral held and the timing and amount of actual and anticipated receipts. Individually assessed impairment allowances are only released when there is reasonable and objective evidence of a reduction in the established loss estimate.

Collectively assessed loans and advances

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 impairment. These credit risk characteristics may include type of business involved, type of products offered, security obtained or other relevant factors. This reflects impairment losses that the local group has incurred as a result of events occurring before the reporting date, which the local group is not able to identify on an individual loan basis, and that can be reliably estimated. These losses will only be individually identified in the future. As soon as information becomes available which identifies losses on individual loans within the group, those loans are removed from the group and assessed on an individual basis for impairment.

3 Significant accounting policies *(continued)*

g *Impairment (continued)*

ii Loans and receivables (continued)

Collectively assessed loans and advances (continued)

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);
– 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 estimated by local management for each identified portfolio. The factors that may influence this estimation include economic and market conditions, customer behaviour, portfolio management information, credit management techniques and collection and recovery experiences in the market. As it is assessed empirically on a periodic basis the estimated period between a loss occurring and its identification may vary over time as these factors change.

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 local group utilises roll rate methodology. This methodology employs a statistical analyses of historical data and experience 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.
– When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll rate methodology, the local group adopts a formulaic approach based on historical loss rate experience. Loss rates are calculated from the discounted expected future cash flows from a portfolio.

  The inherent loss within each portfolio is assessed on the basis of statistical analysis using historical data observations, which are updated periodically to reflect recent portfolio and economic trends. When the most recent trends arising from changes in economic, regulatory or behavioural conditions are not fully reflected in the statistical analysis, they are taken into account by adjusting the impairment allowances derived solely from the statistical analysis to reflect these changes as at the reporting date.

  These additional portfolio risk factors may include recent loan portfolio growth and product mix, unemployment rates, bankruptcy trends, loan product features (such as the ability of borrowers to repay adjustable-rate loans where reset interest rates give rise to increases in interest charges), economic conditions such as national and local trends in housing markets and interest rates, portfolio seasoning, account management policies and practices, current levels of write-offs, changes in laws and regulations and other factors which can affect customer payment patterns on outstanding loans, such as natural disasters. These risk factors, where relevant, 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 local 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.

3 Significant accounting policies *(continued)*

g *Impairment (continued)*

iii Non-financial assets (continued)

The recoverable amount of non-financial assets is the greater of their fair value less cost to sell. 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 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.

An impairment loss on non-financial assets 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.

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h *Non-current assets held for sale*

Non-current assets are classified as held for sale when their carrying amounts will be recovered principally through sale, they are available for sale in their present condition and their sale is highly probable. Immediately before classification as held for sale, the assets are re-measured in accordance with the local 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 re-measurement are recognised in profit or loss. Gains are not recognised in excess of any cumulative impairment loss.

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i *Insurance and investment contracts*

Through its insurance subsidiary, the local group issues contracts to customers that contain insurance risk, financial risk or a combination thereof. A contract under which the local 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.

3 Significant accounting policies *(continued)*

i *Insurance and investment contracts (continued)*

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.

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/(expense) from insurance financial instruments designated at fair value.

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.

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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 which has arisen as a result of past events, and for which a reliable estimate can be made of the amount of the obligation.

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security, are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of the local group; or are present obligations that have arisen from past events but are not recognised because it is not probable that settlement will require the outflow of economic benefits, or because the amount of the obligations cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

Restructuring

A provision for restructuring is recognised when the local 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.

3 Significant accounting policies *(continued)*

k *Financial guarantee contracts*

Financial guarantees are contracts that require the local 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 the initial fair value less cumulative amortisation and the best estimate of the expenditure required to settle the obligations.

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.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the local group estimates cash flows considering all contractual terms of the financial instrument but excluding future credit losses. The calculation includes all amounts paid or received by the local group that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts.

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 local 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.

3 Significant accounting policies *(continued)*

n *Employee benefits (continued)*

ii Termination benefits

Termination benefits are recognised as an expense when the local 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 local group has made an offer of 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 local 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 become unconditionally 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 performance 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.

o *Foreign currencies*

Transactions in foreign currencies are recorded in the functional currency at the 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. Foreign currency differences on monetary assets and liabilities are recognised in profit or loss except for foreign currency exchange differences arising on available-for-sale equity instruments, which are recognised in other comprehensive income. 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 at historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Any exchange component of a gain or loss on a non-monetary item is recognised in other comprehensive income if the gain or loss on the non-monetary item is recognised in other comprehensive income. Any exchange component of a gain or loss on a non-monetary item is recognised in profit or loss if the gain or loss on the non-monetary item is recognised in profit or loss.

p *Income tax*

Income tax expense comprises current and deferred tax. Income tax is 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*

Measurement of segment assets, liabilities, income and expenses is based on the local 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.

4 Financial instruments and risk management

a *Use of financial instruments*

The nature of the local group's core banking operations implies that financial instruments are extensively used in the course of its routine business. The local 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 local 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 local 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).

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii)*

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 local group's holdings of these assets fall. The local group has standards, policies and procedures dedicated to control and monitor the risk arising from all such activities.

Within the overall framework of the local group policy, the local 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 local 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 local 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 local 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.

The table below sets out the principal types of collateral held against different types of financial assets:

Type of credit exposure		*Percentage of collateralised exposure*	
	Principal type of security held for secured lending	**31 December 2014**	31 December 2013
		%	%
Loans and advances to retail customers			
Mortgage lending	Residential property	**100**	100
Personal lending	Residential property	**15**	20
Credit cards	None	**–**	–
Loans and advances to corporate customers			
Government and public sectors	Government guarantees	**87**	86
Other	Commercial property	**40**	47

The local group typically does not hold collateral against financial assets designated at fair value, financial investments and loans to banks, and no such collateral was held at 31 December 2014 and 2013.

4 Financial instruments and risk management *(continued)*

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii) (continued)*

i Credit risk management (continued)

a Collateral and other credit enhancements *(continued)*

Residential mortgage lending

The table below stratifies credit exposures from mortgage loans and advances to retail customers by ranges of loan-to-value ('LTV'). LTV is calculated as the ratio of the gross amount of loan or the amount committed for loan commitments to the value of the collateral. The gross amounts exclude any impairment allowances. The valuation of the collateral excludes any adjustments for obtaining and selling the collateral. The value of the collateral for residential mortgage loans is based on the collateral value at origination updated based on changes in house price indices.

Residential mortgage lending and commitments for mortgage lending

	31 December 2014	31 December 2013
	€000	€000
Loan-to-value (LTV) ratio		
Less than 25%	**260,712**	291,207
25% to 50%	**491,526**	433,767
51% to 75%	**552,591**	500,632
76% to 90%	**334,477**	281,165
91% to 100%	**43,973**	117,350
Greater than 100%	**12,983**	17,498
	1,696,262	1,641,619

ii Credit exposure and risk concentrations

The local 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 designated at fair value, 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 local 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.

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 the same conditions.

4 Financial instruments and risk management *(continued)*

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii) (continued)*

ii *Credit exposure and risk concentrations (continued)*

An industry sector analysis of the bank's loans and advances to customers, before and after taking into account collateral held or other credit enhancements, is as follows:

	Gross maximum exposure	*Net maximum exposure*	*Gross maximum exposure*	*Net maximum exposure*
	2014	**2014**	2013	2013
	€000	**€000**	€000	€000
Agriculture	**3,202**	**1,321**	4,081	1,083
Fishing	**2,310**	**119**	4,520	459
Mining and quarrying	**66**	**–**	37	–
Manufacturing	**96,673**	**52,571**	98,970	51,444
Electricity, gas and water supply	**101,902**	**16,198**	106,217	15,829
Water supply, sewerage waste management and remediation activities	**26,921**	**1,169**	32,966	–
Construction	**300,569**	**113,559**	360,517	122,682
Wholesale and retail trade and repairs	**358,501**	**190,802**	295,597	97,635
Transport, storage and communication	**40,129**	**22,063**	44,027	22,850
Accommodation and food service activities	**142,959**	**72,274**	150,404	48,256
Information and communication	**56,681**	**34,948**	69,559	40,747
Financial and insurance activities	**84,899**	**49,746**	59,622	29,849
Real estate activities	**75,138**	**29,863**	103,964	28,148
Professional, scientific and technical activities	**5,001**	**2,657**	10,037	5,713
Administrative and support service activities	**20,156**	**16,137**	14,694	8,856
Public administration and defence and compulsory social security	**129,463**	**56,379**	122,885	56,382
Education	**2,183**	**733**	2,613	2,140
Human health and social work activities	**35,440**	**8,603**	33,378	13,807
Arts, entertainment and recreation	**8,624**	**6,359**	7,513	4,737
Other services activities	**9,471**	**6,681**	9,030	4,671
Household and individuals	**1,875,105**	**152,196**	1,843,750	166,192
	3,375,393	**834,378**	3,374,381	721,480

iii *Credit quality of financial assets*

The local 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 local group's standard credit rating system.

4 Financial instruments and risk management *(continued)*

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii) (continued)*

iii Credit quality of financial assets (continued)

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

a Distribution of gross loans and advances by credit quality

	Loans and advances to customers			
	Total	*of which forborne*	*Total*	*of which forborne*
	2014	**2014**	2013	2013
	€000	**€000**	**€000**	**€000**
Gross loans and advances:				
Performing				
– neither past due nor impaired	**2,969,162**	**80,411**	2,921,534	38,974
– past due by less than 90 days, but not impaired	**103,720**	**18,078**	145,167	14,597
	3,072,882	**98,489**	3,066,701	53,571
Non-Performing				
– past due by more than 90 days, but not impaired	**2,849**	**1,515**	4,557	418
– impaired	**299,662**	**143,145**	303,123	154,912
	302,511	**144,660**	307,680	155,330
	3,375,393	**243,149**	3,374,381	208,901

Loans and advances to banks 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 local group's standard credit grading system. The following information is based on that system:

	Loans and advances to customers	
	2014	2013
	€000	€000
Satisfactory risk	**2,799,651**	2,731,457
Watch list and special attention	**142,220**	128,055
Sub-standard but not impaired	**27,291**	62,022
	2,969,162	2,921,534

Loans and advances to banks 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 €103,721,000 (2013: €145,167,000).

	Loans and advances to customers	
	2014	2013
	€000	€000
Past due up to 29 days	**63,262**	109,326
Past due 30 – 59 days	**28,138**	22,334
Past due 60 – 89 days	**12,320**	13,507
Past due 90 – 179 days	**1,320**	4,502
Past due over 180 days	**1,529**	55
	106,569	149,724

4 Financial instruments and risk management *(continued)*

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii) (continued)*

iii Credit quality of financial assets (continued)

d Individually impaired gross loans by segment

	Loans and advances to customers	
	2014	2013
	€000	€000
Personal banking	**62,978**	59,427
Commercial and corporate	**236,684**	243,696
	299,662	303,123

e Renegotiated loans and forbearance

The contractual terms of a loan may be modified for a number of reasons including changing market conditions, customer retention and other factors not related to the current or potential credit deterioration of a customer. Under certain circumstances, the local group may renegotiate the terms and conditions of a loan in response to actual or perceived financial difficulties of a customer. This practice of renegotiation for credit purposes is known as loan forbearance. When the contractual payment terms of a loan have been modified because the bank has significant concerns about the borrower's ability to meet contractual payments when due, these loans are classified as 'renegotiated loans'. For the purposes of this disclosure the term 'forbearance' is synonymous with the renegotiation of loans.

A range of forbearance strategies is employed in order to improve the management of customer relationships, maximize collection opportunities and, if possible, avoid default, foreclosure or repossession. They include extended payment terms, a reduction in interest or principal repayments, approved external debt management plans, debt consolidations, the deferral of foreclosures, and other forms of loan modifications and re-ageing.

Our policies and practices are based on criteria which enable management to judge whether repayment is likely to continue. These typically provide a customer with terms and conditions that are more favourable than those provided initially. Loan forbearance is only granted in situations where the customer has showed a willingness to repay the borrowing and is expected to be able to meet the revised obligations.

For retail lending the bank's credit risk management policy sets out restrictions on the number and frequency of renegotiations, the minimum period an account must have been opened before any renegotiation can be considered and the number of qualifying payments that must be received. Where the customer is not meeting contractual repayments or it is evident that they will be unable to do so without the renegotiation, there will be a significant concern regarding their ability to meet contractual payments, and the loan will be disclosed as impaired, unless the concession granted is insignificant.

When the bank grants a concession to a customer that the bank would not otherwise consider, as a result of their financial difficulty, this is objective evidence of impairment and impairment losses are measured accordingly. A renegotiated loan is presented as impaired when there has been a change in contractual cash flows as a result of a concession which the lender would otherwise not consider; and it is probable that without the concession, the borrower would be unable to meet contractual payment obligations in full.

Renegotiated loans are classified as unimpaired where the renegotiation has resulted from significant concern about a borrower's ability to meet their contractual payment terms but the renegotiated terms are based on current market rates and contractual cash flows are expected to be collected in full following the renegotiation.

Loans that have been identified as renegotiated retain this designation until maturity or derecognition. When a loan is restructured as part of a forbearance strategy and the restructuring results in a derecognition of the existing loan, the new loan is disclosed as renegotiated. A loan that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement made on substantially different terms, or if the terms of an existing agreement are modified, such that the renegotiated loan is substantially a different financial instrument.

4 Financial instruments and risk management *(continued)*

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii) (continued)*

iii Credit quality of financial assets (continued)

e Renegotiated loans and forbearance *(continued)*

The following tables show the gross carrying amounts of the bank's holdings of renegotiated loans and advances to customers by industry sector and credit quality classification:

	Neither past due nor impaired	*Past due but not impaired*	*Impaired*	*Total*
	€000	**€000**	**€000**	**€000**
At 31 December 2014				
Personal				
– first lien residential mortgages	**25,848**	**13,921**	**6,449**	**46,218**
– other personal	**3,000**	**613**	**5,102**	**8,715**
Corporate and commercial				
– commercial real estate and other property-related	**4,062**	**1,748**	**60,768**	**66,578**
– other commercial	**47,501**	**3,311**	**70,471**	**121,283**
Financial institutions	**–**	**–**	**355**	**355**
	80,411	**19,593**	**143,145**	**243,149**
Total impaired allowances renegotiated loans				
– individually assessed	**–**	**–**	**41,079**	**41,079**
– collectively assessed	**146**	**989**	**1,031**	**2,166**
	146	**989**	**42,110**	**43,245**
Collateral held	**41,796**	**17,163**	**88,327**	**147,286**
At 31 December 2013				
Personal				
– first lien residential mortgages	27,989	6,065	4,592	38,646
– other personal	675	400	25,929	27,004
Corporate and commercial				
– commercial real estate and other property-related	2,364	2,415	74,101	78,880
– other commercial	7,946	6,135	49,483	63,564
Financial institutions	–	–	807	807
	38,974	15,015	154,912	208,901
Total impaired allowances renegotiated loans				
– individually assessed	–	–	48,652	48,652
– collectively assessed	99	74	3,197	3,370
	99	74	51,849	52,022
Collateral held	45,315	14,674	117,823	177,812
Total renegotiated loans and advances to customers as a percentage of total gross loans and advances to customers at 31 December 2014				**7.2%**

Interest income recognised during 2014 in respect to forborne assets amounts to €6,988,000.

4 Financial instruments and risk management *(continued)*

b *Credit risk excluding Insurance credit risk which is reported under 4(e)(ii) (continued)*

iii Credit quality of financial assets (continued)

e Renegotiated loans and forbearance *(continued)*

Movement in forbearance activity during the year:	
1 January 2014	208,901
Additions	62,839
Retired from forborne	(28,591)
31 December 2014	**243,149**

f Treasury Bills and debt securities

Debt securities and other bills by rating agency (S&P Rating Agency) designation of the local group excluding HSBC Life Assurance (Malta) Limited, are reported in the table below. Information relating to the HSBC Life insurance business is disclosed in note 4(e)ii.

	Treasury Bills	*Debt securities*	*Total*
	€000	**€000**	**€000**
At 31 December 2014			
AAA	**–**	**509,039**	**509,039**
AA- to AA+	**–**	**63,991**	**63,991**
Lower than A-	**31,496**	**564,680**	**596,176**
	31,496	**1,137,710**	**1,169,206**
At 31 December 2013			
AAA	–	171,739	171,739
AA- to AA+	4,999	201,507	206,506
Lower than A-	43,938	524,510	568,448
	48,937	897,756	946,693

iv Movement in allowance accounts for loans and advances to customers

	Individually assessed allowances	*Collective allowances*	*Individually assessed allowances*	*Collective allowances*
	2014	**2014**	2013	2013
	€000	**€000**	€000	€000
Group				
Change in allowances for uncollectibility:				
At 1 January	**60,180**	**13,219**	52,904	13,276
Additions	**30,352**	**–**	12,791	–
Reversals	**(5,143)**	**(5,673)**	(3,321)	(57)
Discount unwind	**(2,515)**	**–**	(2,164)	–
Exchange	**92**	**–**	(30)	–
At 31 December	**82,966**	**7,546**	60,180	13,219

v Settlement risk

The local 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 local 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.

4 Financial instruments and risk management *(continued)*

c *Liquidity risk*

Liquidity risk is the risk that the local 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 local 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 local group's objective to maintain a diversified and stable funding base with the objective of enabling the local group to respond quickly and smoothly to unforeseen liquidity requirements.

The local 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 local group's funding. The local group places considerable importance on maintaining the stability of these deposits.

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

	Due within 3 months	*Due between 3 and 12 months*	*Due between 1 and 5 years*	*Due after 5 years*	*Gross nominal outflow*	*Carrying amount*
	€000	**€000**	**€000**	**€000**	**€000**	**€000**
Group						
At 31 December 2014						
Deposits by banks	**60,232**	**128**	**442**	**–**	**60,802**	**59,848**
Customer accounts	**3,915,065**	**855,884**	**108,861**	**–**	**4,879,810**	**4,867,124**
Subordinated liabilities	**1,339**	**3,109**	**97,562**	**–**	**102,010**	**87,284**
Other financial liabilities	**33,567**	**377**	**–**	**–**	**33,944**	**33,944**
	4,010,203	**859,498**	**206,865**	**–**	**5,076,566**	**5,048,200**
Commitments	**921,653**	**100,211**	**269,361**	**–**	**1,291,225**	
At 31 December 2013						
Deposits by banks	41,534	48	221	–	41,803	41,794
Customer accounts	3,529,883	940,940	65,091	–	4,535,914	4,517,862
Subordinated liabilities	1,339	3,064	103,741	–	108,144	87,273
Other financial liabilities	32,249	5,310	111	–	37,670	37,670
	3,605,005	949,362	169,164	–	4,723,531	4,684,599
Commitments	937,455	107,283	224,306	178	1,269,222	

4 Financial instruments and risk management *(continued)*

c *Liquidity risk (continued)*

i Cash flows payable by the local group under financial liabilities by remaining maturities (continued)

Bank

At 31 December 2014						
Deposits by banks	**60,232**	**128**	**442**	**–**	**60,802**	**59,848**
Customer accounts	**3,979,565**	**855,884**	**108,861**	**–**	**4,944,310**	**4,931,485**
Subordinated liabilities	**1,339**	**3,109**	**97,562**	**–**	**102,010**	**88,093**
Other financial liabilities	**28,882**	**377**	**–**	**–**	**29,259**	**29,259**
	4,070,018	**859,498**	**206,865**	**–**	**5,136,381**	**5,108,685**
Commitments	**925,703**	**100,211**	**269,361**	**–**	**1,295,275**	
At 31 December 2013						
Deposits by banks	41,534	48	221	–	41,803	41,794
Customer accounts	3,566,203	940,940	65,091	–	4,572,234	4,554,104
Subordinated liabilities	1,339	3,109	104,689	–	109,137	88,040
Other financial liabilities	24,682	5,310	111	–	30,103	30,103
	3,633,758	949,407	170,112	–	4,753,277	4,714,041
Commitments	941,429	107,283	224,306	178	1,273,196	

Cash flows payable by the local 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.

The balances in the above table will not agree directly to the balances in the statement of financial position as the table incorporates 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, included balances with Central Bank of Malta, Treasury Bills and cash, cheques in course of collection, loans to banks and to customers and marketable debt securities.

The local 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.

ii Asset encumbrance

The disclosure on asset encumbrance is a new requirement introduced in Banking Rule 07 transposing the provisions of the EBA Guidelines on Disclosure of Encumbered and Unencumbered Assets (EBA/GL/2014/03).

The objective of this disclosure is to facilitate an understanding of available and unrestricted assets that could be used to support potential future funding and collateral needs. An asset is defined as encumbered if it has been pledged as collateral against an existing liability, and as a result is no longer available to the group to secure funding, satisfy collateral needs or be sold to reduce the funding requirement.

The disclosure is not designed to identify assets which would be available to meet the claims of creditors or to predict assets that would be available to creditors in the event of a resolution or bankruptcy.

4 Financial instruments and risk management *(continued)*

c *Liquidity risk (continued)*

ii Asset encumbrance (continued)

Encumbered and unencumbered assets

	Carrying amount of encumbered gross assets	*Fair value of encumbered gross assets*	*Carrying amount of unencumbered gross assets*	*Fair value of unencumbered gross assets*
	€000	**€000**	**€000**	**€000**
Group				
At 31 December 2014				
Equity instruments	**–**	**–**	**22**	**–**
Debt securities	**91,018**	**91,018**	**1,062,844**	**1,062,844**
Loan and advances to customers	**103,438**	**103,438**	**3,260,455**	**3,260,455**
Other assets	**8,000**	**8,000**	**2,763,722**	**2,763,722**
	202,456	**202,456**	**7,087,043**	**7,087,021**
At 31 December 2013				
Equity instruments	–	–	73	–
Debt securities	109,944	109,944	808,275	808,275
Loan and advances to customers	106,379	106,379	3,268,002	3,268,002
Other assets	8,000	8,000	1,494,256	1,494,256
	224,323	224,323	5,570,606	5,570,533
Bank				
At 31 December 2014				
Equity instruments	**–**	**–**	**19**	**–**
Debt securities	**91,018**	**91,018**	**1,046,660**	**1,046,660**
Loan and advances to customers	**103,438**	**103,438**	**3,271,955**	**3,271,955**
Other assets	**8,000**	**8,000**	**1,116,149**	**1,116,149**
	202,456	**202,456**	**5,434,783**	**5,434,764**
At 31 December 2013				
Equity instruments	–	–	70	70
Debt securities	109,944	109,944	787,780	787,780
Loan and advances to customers	106,379	106,379	3,268,002	3,268,002
Other assets	8,000	8,000	919,648	919,648
	224,323	224,323	4,975,500	4,975,500

The local group does not encumber any of the collateral received or any of its own debt securities issued.

As at 31 December 2014, the local group did not have any outstanding liabilities associated with encumbered assets and collateral received.

The bank undertakes the following types of encumbrance:

i Pledging of loans and advances to customers and debt securities against the provision of credit lines by the Central Bank of Malta.

ii Pledging of balances held with the Central Bank of Malta and debt securities in favour of the Depositor Compensation Scheme.

4 Financial instruments and risk management *(continued)*

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 local group's income or the value of its portfolios.

The objective of the local 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 local group's status as a premier provider of financial products and services.

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

Each line of business is requested to assess the market risks which arise on each product in the business and, where their is a risk that can be hedged in the markets, this is transferred to the local Global Banking and Markets Unit for management. Where market risk is identified but there is no viable hedge in the market then the risk is managed under the local ALCO.

i Credit valuation adjustment methodology

The local 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 local 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 local group uses a simulation methodology to calculate the expected positive exposure. The methodology simulates the range of potential exposures of the local 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 local group considers that an appropriate spread to reflect its own probability of default within the credit risk adjustment calculation is currently zero. Consequently, the local group 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.

ii Value at risk ('VAR')

One of the principal tools used by the local 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 local 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 bank 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, commodity prices, interest rates, equity prices and the associated volatilities;
- VAR is calculated to a 99% confidence level; and
- VAR is calculated for a one-day holding period.

4 Financial instruments and risk management *(continued)*

d *Market risk (continued)*

ii Value at risk ('VAR') (continued)

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

The VAR for the bank was as follows:

	2014	2013
	€000	€000
At 31 December	**590**	1,059
Average	**656**	925
Minimum	**581**	779
Maximum	**819**	1,292

The reduction in VAR as at 31 December 2014 compared with 31 December 2013 was mainly due to more benign periods included in the VAR model.

iii 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 uses 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 15 basis points parallel fall or rise in all yield curves worldwide on the first day of the following year based on current financial position/risk profiles and current managed interest rate policy. This calculation is taking into account the bank's strategy that negative rates are never passed through to customers.

	Impact on profit for the year	*Impact on net assets*	*Impact on profit for the year*	*Impact on net assets*
	2014	**2014**	2013	2013
	€000	**€000**	€000	€000
Group/Bank				
+ 15 basis points	**(528)**	**(5,178)**	(200)	(6,599)
- 15 basis points	**(1,245)**	**3,405**	200	6,599

4 Financial instruments and risk management *(continued)*

d *Market risk (continued)*

iv Currency concentration

	Reporting currency	*Other currencies*	*Total*	*Reporting currency*	*Other currencies*	*Total*
	2014	**2014**	**2014**	2013	2013	2013
	€000	**€000**	**€000**	€000	€000	€000
Group						
Assets						
Balances with Central Bank of Malta, Treasury Bills and cash	**115,895**	**2,138**	**118,033**	149,678	1,780	151,458
Cheques in course of collection	**10,755**	**235**	**10,990**	9,441	262	9,703
Derivatives	**6,886**	**6,284**	**13,170**	9,724	2,942	12,666
Financial assets designated at fair value	**637,843**	**783,737**	**1,421,580**	386,261	91,084	477,345
Financial investments	**777,085**	**376,799**	**1,153,884**	686,414	231,878	918,292
Loans and advances to banks	**437,108**	**437,987**	**875,095**	97,510	467,280	564,790
Loans and advances to customers	**3,240,543**	**32,838**	**3,273,381**	3,261,466	39,516	3,300,982
Other assets	**329,999**	**2,855**	**332,854**	284,703	1,591	286,294
Total assets	**5,556,114**	**1,642,873**	**7,198,987**	4,885,197	836,333	5,721,530
Liabilities and equity						
Derivatives	**6,864**	**7,006**	**13,870**	9,996	2,933	12,929
Deposits by banks	**16,632**	**43,216**	**59,848**	8,892	32,902	41,794
Customer accounts	**4,113,761**	**753,363**	**4,867,124**	3,822,843	695,019	4,517,862
Liabilities to customers under investment contracts	**418,746**	**601,848**	**1,020,594**	16,763	–	16,763
Liabilities under insurance contracts issued	**602,712**	**–**	**602,712**	524,999	–	524,999
Subordinated liabilities	**87,284**	**–**	**87,284**	87,273	–	87,273
Other liabilities	**96,606**	**5,844**	**102,450**	91,950	4,976	96,926
Total equity	**445,105**	**–**	**445,105**	422,984	–	422,984
Total liabilities and equity	**5,787,710**	**1,411,277**	**7,198,987**	4,985,700	735,830	5,721,530

4 Financial instruments and risk management *(continued)*

d *Market risk (continued)*

iv Currency concentration (continued)

	currency	*Reporting currencies*	*Other Total*	*currency*	*Reporting currencies*	*Other Total*
	2014	**2014**	**2014**	2013	2013	2013
	€000	**€000**	**€000**	€000	€000	€000
Bank						
Assets						
Balances with Central Bank of Malta, Treasury Bills and cash	**115,895**	**2,138**	**118,033**	149,677	1,780	151,457
Cheques in course of collection	**10,755**	**235**	**10,990**	9,441	262	9,703
Derivatives	**6,882**	**6,216**	**13,098**	9,724	2,942	12,666
Financial investments	**760,934**	**376,763**	**1,137,697**	665,916	231,878	897,794
Loans and advances to banks	**401,874**	**394,383**	**796,257**	97,395	467,280	564,675
Loans and advances to customers	**3,252,043**	**32,838**	**3,284,881**	3,261,466	39,516	3,300,982
Other assets	**182,916**	**2,855**	**185,771**	187,556	1,591	189,147
Total assets	**4,731,299**	**815,428**	**5,546,727**	4,381,175	745,249	5,126,424
Liabilities and equity						
Derivatives	**6,845**	**6,574**	**13,419**	9,996	2,933	12,929
Deposits by banks	**16,632**	**43,216**	**59,848**	8,892	32,902	41,794
Customer accounts	**4,178,122**	**753,363**	**4,931,485**	3,859,085	695,019	4,554,104
Subordinated liabilities	**88,093**	**–**	**88,093**	88,040	–	88,040
Other liabilities	**52,781**	**5,844**	**58,625**	58,299	4,976	63,275
Total equity	**395,257**	**–**	**395,257**	366,282	–	366,282
Total liabilities and equity	**4,737,730**	**808,997**	**5,546,727**	4,390,594	735,830	5,126,424

e *Insurance risk*

The insurance risk of the local 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 local 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:

	Group	
	2014	2013
	€000	€000
Life insurance (non-linked)		
Insurance contracts with discretionary participation feature	**414,410**	348,206
Term assurance and other long-term contracts	**1,977**	2,568
Total non-linked	**416,387**	350,774
Life insurance (linked)	**186,325**	174,225
Liabilities under insurance contracts	**602,712**	524,999
Liabilities under investment contracts	**1,020,594**	16,763
Total insurance liabilities	**1,623,306**	541,762

4 **Financial instruments and risk management** *(continued)*

e *Insurance risk (continued)*

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

	2014	2013
	%	%
Risk free rate	**Euro Swap Curve**	Euro Swap Curve
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 following table shows the effect on the PVIF of reasonably possible changes in the main economic assumptions across the life insurance business:

		PVIF Impact	
		2014	2013
Assumptions	**Movement**	**€000**	€000
As published			
Risk free rate	+100 basis points	**9,186**	10,298
Risk free rate	-100 basis points	**4,141**	(10,238)
Expenses inflation	+10%	**(670)**	(662)
Expenses inflation	-10%	**747**	717
Lapse rate	+100 basis points	**951**	(495)
Lapse rate	-100 basis points	**(1,642)**	252

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

Interest rate risk and equity 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 local 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.

The local 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:

4 Financial instruments and risk management *(continued)*

e *Insurance risk (continued)*

i Market risk (continued)

Interest rate risk and equity risk *(continued)*

	2014	2013
	€000	€000
+100 basis points shift in yield curves	**54**	(559)
-100 basis points shift in yield curves	**(31)**	539
+10 per cent increase in equity prices	**203**	233
-10 per cent increase in equity prices	**(204)**	(234)

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):

	Debt securities – Unit linked		*Debt securities – Others*		*Total*	
	2014	2013	**2014**	2013	**2014**	2013
	€000	€000	**€000**	€000	**€000**	€000
AAA	**17,430**	–	**26,515**	43,011	**43,945**	43,011
AA+ to AA-	**12,959**	–	**71,979**	60,326	**84,938**	60,326
A- to A+	**24,212**	–	**54,446**	49,575	**78,658**	49,575
Lower than A-	**237,545**	–	**94,009**	104,372	**331,554**	104,372
Unrated	**130,400**	–	**12,445**	14,484	**142,845**	14,484
Total	**422,546**	–	**259,394**	271,768	**681,940**	271,768

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:

	Due within 3 months	*Due between 3 and 12 months*	*Due between 1 and 5 years*	*Due after 5 years*	*Gross nominal outflow*
	€000	**€000**	**€000**	**€000**	**€000**
At 31 December 2014					
Liabilities under investment contracts	**332**	**975**	**3,261**	**1,001,839**	**1,006,407**
Liabilities under insurance contracts	**20,121**	**41,309**	**197,323**	**328,347**	**587,100**
At 31 December 2013					
Liabilities under investment contracts	136	336	3,244	20,457	24,173
Liabilities under insurance contracts	13,967	34,849	172,738	293,288	514,842

4 Financial instruments and risk management *(continued)*

e *Insurance risk (continued)*

iii Liquidity risk (continued)

The methodology used for estimating liquidity risk is as follows:

– 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 Reserves 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 Fair value of financial and non-financial instruments

i *Valuation of financial instruments*

All financial instruments are recognised initially at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of a financial instrument on initial recognition is generally its transaction price (that is, the fair value of the consideration given or received). However, sometimes the fair value will be based on other observable current market transactions in the same instrument, without modification or repackaging, or on a valuation technique whose variables include only data from observable markets, such as interest rate yield curves, option volatilities and currency rates. When such evidence exists, the local group recognises a trading gain or loss on day 1, being the difference between the transaction price and the fair value. When significant unobservable parameters are used, the entire day 1 gain or loss is deferred and is recognised in the income statement over the life of the transaction until the transaction matures, is closed out, the valuation inputs become observable, or when the bank enters into an offsetting transaction.

The fair value of financial instruments is generally measured on an individual basis. However, in cases where HSBC manages a group of financial assets and liabilities according to its net market or credit risk exposure, the local group measures the fair value of the group of financial instruments on a net basis but presents the underlying financial assets and liabilities separately in the financial statements, unless they satisfy the IFRS offsetting criteria.

The best evidence of fair value is a quoted price in an actively traded principal market. In the event that the market for a financial instrument is not active, and the valuation technique uses only observable market data, the reliability of the fair value measurement is high. However, when valuation techniques include one or more significant unobservable inputs, they rely to a greater extent on management judgement and the fair value derived becomes less reliable. In absence of observable valuation inputs, due to lack of or a reduced volume of similar transactions, management judgement is required to assess the price at which an arm's length transaction would occur under normal business conditions, in which case management may rely on historical prices for that particular financial instrument or on recent prices for similar instruments.

The main assumptions and estimates which management consider when applying a model with valuation techniques are:

– the likelihood and expected timing of future cash flows on the instrument; judgement may be required to assess the counterparty's ability to service the instrument in accordance with its contractual terms. Future cash flows may be sensitive to changes in market rates;

– selecting an appropriate discount rate for the instrument: Judgement is required to assess what a market participant would regard as the appropriate spread of the rate for an instrument over the appropriate risk-free rate;

– judgement to determine what model to use to calculate fair value in areas where the choice of valuation model is particularly subjective, for example, when valuing complex derivative products.

When applying a model with unobservable inputs, estimates are made to reflect uncertainties in fair values resulting from a lack of market data inputs, for example, as a result of illiquidity in the market. For these instruments, the fair value measurement is less reliable. Inputs into valuations based on unobservable data are inherently uncertain because there is little or no current market data available from which to determine the level at which an arm's length transaction would occur under normal business conditions. However, in most cases there is some market data available on which to base a determination of fair value, for example historical data, and the fair values of most financial instruments are based on some market observable inputs even when unobservable inputs are significant.

5 Fair value of financial and non-financial instruments *(continued)*

ii Control framework

Fair values are subject to a control framework designed to ensure that they are either determined, or validated, by a function independent of the risk-taker.

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, the local group 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. The factors that are considered in this regard are, inter alia:

- the extent to which prices may be expected to represent genuine traded or tradable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the reporting date; and
- the manner in which the data was sourced.

For fair values determined using a valuation model, the control framework may include, as applicable, development or validation by independent support functions of (i) the logic within valuation models; (ii) the inputs to those models; (iii) any adjustments required outside the valuation models; and, where possible, (iv) model outputs. Valuation models are subject to a process of due diligence and calibration before becoming operational and are calibrated against external market data on an ongoing basis.

iii Determination of fair value

Fair values are determined according to the following hierarchy:

a *Level 1 – quoted market price:* financial instruments with quoted prices for identical instruments in active markets.

b *Level 2 – valuation technique using observable inputs:* financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

c *Level 3 – valuation technique with significant unobservable inputs:* financial instruments valued using models where one or more significant inputs are unobservable.

The best evidence of fair value is a quoted price in an actively traded market. The fair values of financial instruments that are quoted in active markets are based on bid prices for assets held and offer prices for liabilities issued. Where a financial instrument has a quoted price in an active market, the fair value of the total holding of the financial instrument is calculated as the product of the number of units and quoted price. In the event that the market for a financial instrument is not active, a valuation technique is used.

The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices that are necessary to measure the fair value of the instrument requires additional work during the valuation process.

iv Valuation techniques

Valuation techniques incorporate assumptions about factors that other market participants would use in their valuations. A range of valuation techniques is employed, dependent on the instrument type and available market data. Most valuation techniques are based upon discounted cash flow analyses, in which expected future cash flows are calculated and discounted to present value using a discounting curve. Prior to considering credit risk, the expected future cash flows may be known, as would be the case for the fixed leg of an interest rate swap, or may be uncertain and require projection, as would be the case for the floating leg of an interest rate swap. 'Projection' utilises market forward curves, if available. In option models, the probability of different potential future outcomes must be considered. In addition, the value of some products are dependent on more than one market factor, and in these cases it will typically be necessary to consider how movements in one market factor may affect the other market factors.

5 Fair value of financial and non-financial instruments *(continued)*

iv Valuation techniques (continued)

The model inputs necessary to perform such calculations include interest rate yield curves, exchange rates, volatilities, correlations, prepayment and default rates. For interest rate derivatives with collateralised counterparties and in significant currencies, HSBC uses a discounting curve that reflects the overnight interest rate ('OIS discounting').

The majority of valuation techniques employ only observable market data. However certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, and for them the derivation of fair value is more judgemental. An instrument in its entirety is classified as valued using significant unobservable inputs if, in the opinion of management, a significant proportion of the instrument's inception profit ('day 1 gain or loss') or greater than 5% of the instrument's carrying value is driven by unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the price at which an arm's length transaction would be likely to occur. It generally does not mean that there is no data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used). All fair value adjustments are included within the levelling determination.

Structured notes issued and certain other hybrid instrument liabilities are included within trading liabilities and are measured at fair value. The credit spread applied to these instruments is derived from the spreads at which the local group issues structured notes.

Gains and losses arising from changes in the credit spread of liabilities issued by the local group reverse over the contractual life of the debt, provided that the debt is not repaid at a premium or a discount.

Changes in fair value are generally subject to a profit and loss analysis process. This process disaggregates changes in fair value into three high level categories; (i) portfolio changes, such as new transactions or maturing transactions, (ii) market movements, such as changes in foreign exchange rates or equity prices, and (iii) other, such as changes in fair value adjustments, discussed below.

v Basis of valuing 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, the local group 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.

	Valuation techniques			
	Quoted market price	*Using observable inputs*	*With significant unobservable inputs*	
	Level 1	Level 2	Level 3	Total
	€000	**€000**	**€000**	**€000**
Group				
At 31 December 2014				
Assets				
Treasury bills	**–**	**31,496**	**–**	**31,496**
Derivatives	**–**	**13,170**	**–**	**13,170**
Financial assets designated at fair value	**1,207,613**	**207,414**	**6,553**	**1,421,580**
Financial investments: available-for-sale	**1,153,862**	**–**	**–**	**1,153,862**
Liabilities				
Derivatives	**–**	**13,870**	**–**	**13,870**
Liabilities to customers under investment contracts	**807,006**	**207,035**	**6,553**	**1,020,594**
At 31 December 2013				
Assets				
Treasury bills	–	48,937	–	48,937
Derivatives	–	12,666	–	12,666
Financial assets designated at fair value	477,345	–	–	477,345
Financial investments: available-for-sale	918,219	–	–	918,219

5 Fair value of financial and non-financial instruments *(continued)*

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

	Valuation techniques			
	Quoted market price	*Using observable inputs*	*With significant unobservable inputs*	
	Level 1	Level 2	Level 3	Total
	€000	**€000**	**€000**	**€000**
Group				
At 31 December 2013				
Liabilities				
Derivatives	–	12,929	–	12,929
Liabilities to customers under investment contracts	16,763	–	–	16,763
Bank				
At 31 December 2014				
Assets				
Treasury bills	**–**	**31,496**	**–**	**31,496**
Derivatives	**–**	**13,098**	**–**	**13,098**
Financial investments: available-for-sale	**1,137,678**	**–**	**–**	**1,137,678**
Liabilities				
Derivatives	**–**	**13,419**	**–**	**13,419**
At 31 December 2013				
Assets				
Treasury bills	–	48,937	–	48,937
Derivatives	–	12,666	–	12,666
Financial investments: available-for-sale	897,724	–	–	897,724
Liabilities				
Derivatives	–	12,929	–	12,929

The following table shows a reconciliation of the fair value Level 3 movement:

	2014
	€000
Level 3	
Financial assets designated at fair value through profit or loss	
Acquired on portfolio transfer	**6,536**
Gains recognised in profit or loss	**17**
At 31 December 2014	**6,553**

The collective investment schemes categorised in Level 3, were acquired by HSBC Life Assurance (Malta) Limited (‘the company’) as part of the portfolio transfer of unit linked investment contracts from HSBC Life (Europe) Limited, effective on 30 November 2014.

The company’s collective investment schemes, categorised in Level 3, consist of shares in alternative funds which are unlisted and have illiquid price sources. In view of no quoted market prices or observable inputs for modelling their value, the fair value of the shares held is derived using the net asset value as sourced from the respective custodians. The uncertainty in utilising the net asset value lies in the availability of the financial statements of the alternative funds as at 31 December 2014 and their respective audit opinion. The latest available financial statements of the alternative funds are accompanied by an unqualified audit opinion.

5 Fair value of financial and non-financial instruments *(continued)*

v *Basis of valuing assets and liabilities measured at fair value (continued)*

The collective investment schemes categorised in Level 3 are financial assets held to cover linked liabilities. The corresponding liabilities to customers under investment contracts in relation to these investments are also categorised in Level 3. Investment risk on these Level 3 assets is borne by the policyholder as it was the decision of the policyholder to invest in these assets.

The following non-financial assets are also measured at fair value. Freehold and long leasehold properties including investment properties are remeasured to fair value on the basis of their existing use. Revaluations are carried out by professionally qualified architects 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.

	Group		*Bank*	
	2014	2013	**2014**	2013
Assets	**€000**	€000	**€000**	€000
Property	**42,513**	42,747	**42,611**	42,852
Investment property	**16,326**	14,529	**11,667**	11,660
	58,839	57,276	**54,278**	54,512

The fair values of these assets are determined under Level 3 of the fair value hierarchy. The unobservable inputs used to determine the fair value of property and investment property are the rental market going rates. A discount factor is added to cover property, depreciation and tenant risk where applicable. An analysis of the fair value movement is included in note 29 for property and note 30 for investment property, if any.

vi *Basis of valuing financial instruments not measured at fair value*

Certain financial assets and liabilities are either carried at amortised cost or cost less impairment. The fair values of these financial assets and liabilities are not disclosed given that the carrying amount is a reasonable approximation of fair value because these are either re-priced to current market rates frequently or are short-term in nature.

The following table sets out the carrying amounts of these financial assets and liabilities:

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Assets				
Balances with Central Bank of Malta and cash	**86,537**	102,521	**86,537**	102,520
Cheques in course of collection	**10,990**	9,703	**10,990**	9,703
Loans and advance to banks	**875,095**	564,790	**796,257**	564,675
Loans and advance to customers	**3,273,381**	3,300,982	**3,284,881**	3,300,982
Financial investments (note i)	**22**	73	**19**	70
Accrued interest	**40,824**	36,011	**31,704**	31,193
	4,286,849	4,014,080	**4,210,388**	4,009,143
Liabilities				
Deposits by banks	**59,848**	41,794	**59,848**	41,794
Customer accounts	**4,867,124**	4,517,862	**4,931,485**	4,554,104
Subordinated liabilities (note ii)	**87,284**	87,273	**88,093**	88,040
Accrued interest	**10,807**	13,635	**10,808**	13,662
	5,025,063	4,660,564	**5,090,234**	4,697,600

Note i

Certain unlisted equity investments are carried at cost less impairment. 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.

Note ii

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 €93,717,122 as at 31 December 2014 (2013: €94,095,000). The fair value is determined under Level 1 of the fair value hierarchy.

6 Capital management and allocation

The local group's approach to capital management is driven by its strategic and organisational requirements, 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 risks inherent in its business and to meet regulatory capital requirements at all times.

Capital management policy falls under the direct oversight of the Asset and Liability Committee (ALCO). As part of its capital management process, an annual capital plan is drawn up and approved by the Board with the objective of maintaining the optimal amount and composition of regulatory capital. The impact on shareholder returns is recognised 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.

The wave of unprecedented regulatory change continued relentlessly during 2014. The Basel III has been implemented in the EU through a Directive and a Regulation, referred to as 'CRD IV', with legal effect from 1 January 2014. The significant matters within the scope of CRD IV include quality and quantity of regulatory capital, calculation of capital requirements for major risk types, liquidity and funding, capital buffers, introduction of a leverage ratio, and disclosure requirements. Furthermore, the transition towards a full implementation of the Single Supervisory Mechanism (SSM) began in November 2014. The SSM is composed of the European Central Bank (ECB) and "National Competent Authorities" (NCAs), MFSA in the case of Malta, and is guided by the single rulebook approach. This is a significant step towards harmonisation of financial supervision within the EU aimed at promoting a commonly agreed approach to prudential supervision of credit institutions to ensure the robustness of the euro area banking system. In this regard, the ECB published the "Guide to Banking Supervision" document in November 2014, which introduced the concept of "significant institutions" and "less significant institutions", and each of these set out distinct processes for the conduct of supervision within SSM.

HSBC Bank Malta p.l.c. has been designated as a significant institution, since it is clearly a systemically important bank within the context of the domestic economy, and therefore in scope for dual supervision by the ECB and MFSA. As part of the transition process, HSBC took part in a "Comprehensive Assessment" conducted by the ECB on 130 systemically important credit institutions in Europe. The assessment was designed to test the financial resilience of such banks before ECB took on responsibility for their supervision, and was structured into two main parts: an Asset Quality Review (AQR) that is a quality test of the loan book and a Stress Test (ST) that is a forward-looking stress test that examined the resilience of banks' balance sheets in adverse scenarios.

The bank has performed strongly in both the Asset Quality Review and Stress Test, confirming that the bank remains in a well capitalised and liquid position to support continuing growth in Malta.

The local group's capital base is composed of Common Equity Tier 1 (CET1) and Tier 2, as defined in Part Two of the Capital Requirements Regulation (CRR). This regulation places higher importance on CET1 being the highest form of quality capital thus providing the greatest level of protection against losses, with the regulatory minimum CET1 of 4.0% and Tier 1 of 5.5% as of 1 January 2014 as per CRR Articles 465(1a) and 465(1b) respectively.

- Common Equity Tier 1 is composed of called-up share capital and distributable retained earnings, net of depositor compensation scheme reserve (see note 44), proposed dividend, proposed bonus share issue and general banking risk reserve as required by MFSA Banking Rule 09 (refer to note 44). Intangible assets are deduced from CET1 in accordance with CRR Article 37.
- Tier 2 is composed of:
  - Subordinated loan capital qualifying for inclusion as per CRR Article 63(a) and application of CRR Article (64) to recognise at amortised value (nominal amount multiplied by number of remaining calendar days of contractual maturity) on the basis of remaining maturity less than five years.
  - Unrealised gains arising on the fair valuation of financial investments designated as available-for-sale and revaluation of properties qualify for full inclusion as per CRR Article 468(2).

On the basis of CRR Article 43(a), the investment in HSBC Life Assurance (Malta) Limited is deemed to be significant for the purposes of capital requirements.

The investment in HSBC Life Assurance (Malta) Limited and Deferred Taxation are subject to provisions in CRR Article 36(1c) and 36(1i) respectively, and therefore in scope for deduction from CET1. However, CRR Article 48(1) provides an exemption from the deduction if the aggregate amount of the aforementioned is equal to or less than the threshold referred to in CRR Article 48(2), i.e. result of Tier 1 after deductions multiplied by 17.65%. Since the aggregate amount is effectively below the threshold, both the investment in HSBC Life Assurance (Malta) Limited and Deferred Taxation amounts are risk weighted at 250% as per Article 48(4), and are not deducted from CET1.

The subordinated loan granted to HSBC Life Assurance (Malta) Limited is fully deducted from Tier 2 in line with CRR Articles 66(d) and 69.

6 Capital management and allocation *(continued)*

In line with EU Regulation No 1423/2013 (disclosure of own funds requirements for institutions), which introduced standards for disclosure of capital instruments qualifying for own funds, the following table discloses the main features, and the main terms and conditions, of the ordinary share capital and subordinated bonds issued, included as capital instruments in the Tier 1 and Tier 2 regulatory capital.

Capital Instruments Main Features	*HSBC Ordinary shares @ par*	*4.6% HSBC Bank Malta p.l.c. Subordinated Bonds 2017 @ par*	*5.9% HSBC Bank Malta p.l.c. Subordinated Bonds 2018 @ par*
Unique identifier	MT0000030107	MT0000031220	MT0000031238
Governing Law(s) of the instrument	Maltese Law	Maltese Law	Maltese Law
Regulatory Treatment			
Transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2
Post-transitional CRR rules	Common Equity Tier 1	Tier 2	Tier 2
Eligible at solo/(sub)consolidated /solo & (sub)consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated	Solo & (Sub) consolidated
Amount recognised in regulatory capital	97,281,414	30,552,610	15,288,390
Nominal amount of instrument	97,281,414	58,234,390	30,000,000
Issue Price	N/A	At par (€100 per bond)	At par (€100 per bond)
Redemption Price	N/A	At €100	At €100
Accounting classification	Share Equity	Liability – amortised cost	Liability – amortised cost
Original date of issuance	27 January 1993*	12 February 2007	16 October 2008
Perpetual or dated	N/A	Dated	Dated
Original maturity date	No	01 February 2017	07 August 2018
Issuer call subject to prior supervisory approval	No	No	No
Coupons/dividends			
Fixed or floating dividend coupon	Floating	Fixed	Fixed
Coupon rate and any related index	N/A	4.60%	5.90%
Existence of dividend stopper	No	No	No
Fully discretionary, partially discretionary or mandatory (in terms of timing)	Fully discretionary	Mandatory	Mandatory
Fully discretionary, partially discretionary or mandatory (in terms of amount)	Partially discretionary	Mandatory	Mandatory
Existence of step up or other incentive to redeem	N/A	No	No
Non-cumulative or cumulative	Non-cumulative	Non-cumulative	Non-cumulative
Convertible or non-convertible	Non-convertible	Non-convertible	Non-convertible
Write-down features	No	No	No
Position in subordination hierarchy in liquidation	Subordinated to HSBC Subordinated Bonds	Subordinated to senior creditors and depositors	Subordinated to senior creditors and depositors
Non-compliant transitional features	No	No	No

* Date when the bank was initially listed on the Malta Stock Exchange

6 Capital management and allocation *(continued)*

The regulatory framework underpinning the local group's capital risk management policy is the Capital Requirements Regulation (EU Regulation 575/2013), principally in respect of the own funds requirements as defined in Parts 2 & 3 of CRR and disclosure requirements as defined in Part 8 of CRR.

– Own Funds Requirements defines the minimum capital requirement that a credit institution should maintain to cover for its credit, market and operational risks of Common Equity Tier 1 at 4%, Tier 1 at 5.5% and Total Capital at 8%. The CRR also specifies strict criteria of what qualifies for inclusion in the 3 categories of Own Funds to ensure that own funds is of the highest quality.

The local group's capital requirement is based on the risk weighting methodology as defined in CRR. The Group adopts the Standardised Approach to calculate risk weighted assets in relation to the banking book by assigning the appropriate risk weight according to the nature of the asset and counterparty and taking into account any eligible collateral and value adjustments, in order to calculate the exposure at default.

The risk-weighted assets for the trading book are determined by taking into consideration the market related risks such as foreign exchange, interest rate and equity position risks and counterparty risk.

The operational risk capital requirement is calculated using the Basic Indicator Approach.

– As stipulated in Section 1 of Chapter 2 of the CRD IV (EU Directive 2013/36), the Group is required to have in place an internal process to assess the adequacy of capital levels in relation to its overall risk profile. The outcome of this process is enshrined in a document known as Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP process encompasses the adequacy of capital requirements for Pillar 1 risks (credit, market and operational), and other material residual risks not fully captured under Pillar 1, including concentration, liquidity, reputational and strategic risks, and interest rate risk in the banking book and risks arising from the macroeconomic environment.

Credit risk is assessed by utilising the embedded operational process for the Pillar 1 capital calculation, supported by a suite of internal models that take into account the internal assessment of diversification of risks, within the portfolios and similarly, any concentrations of risk that arise. The bank maintains a prudent 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 non-trading products over one year to a 99% level of confidence.

The ICAAP was last updated and approved by ALCO and the senior management in January 2015, and subsequently presented to the Joint Supervisory Team ('JST') for review. Typically, this would then lead to a discussion between the local group and JST on the appropriate level of capital adequacy to cover Pillar 2 risks.

Stress testing forms an integral part of the risk and capital management framework and is an important component of ICAAP. Its main purpose is to highlight to senior management potential adverse unexpected outcomes that could arise under hypothetical scenarios, and provides a quantitative indication of how much capital might be required to absorb the losses, should such adverse scenarios occur. Stress testing is used to assess risk concentrations, estimate the impact on revenue, impairments, write-downs and the resultant capital adequacy under a variety of adverse scenarios.

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

The stress testing framework brings manifold benefits to risk management, including: understanding the impact of recessionary scenarios; assessing material risk concentrations; impact of market price movements; and, forecasting of the balance sheet management and liquidity.

A series of stress events are run on a regular basis to assess the potential impact of an extreme yet plausible event on the local group. In an adverse scenario, a range of mitigating actions is ready to be implemented whenever the need arises. The latter also forms part of the ICAAP document.

This note has been prepared in accordance with MFSA Banking Rule 07/2014 (Publication of Annual Report and Audited Financial Statements of Credit Institutions Authorised under the Banking Act 1994). This requires credit institutions to disclose annually information on risk and capital management under the CRR. The local group is designated as a significant subsidiary of HSBC Holdings plc and is therefore exempt in terms of Article 24 of BR/07 from full risk disclosure requirements under CRR Article 13. HSBC Holdings plc publishes Pillar 3 disclosures as a separate document on the Group Investor Relations website.

6 Capital management and allocation *(continued)*

Full reconciliation of own funds items to audited financial statements as at 31 December 2014

	Group	*Bank*
	2014	**2014**
	€000	**€000**
Common Equity Tier 1		
As per statement of Financial Position		
– Called up share capital	**97,281**	**97,281**
– Retained earnings	**305,314**	**255,837**
	402,595	**353,118**
Less: Own Funds adjustments		
– Expected final dividend	**(5,446)**	**(5,446)**
– Retained earnings – HSBC Life Assurance (Malta) Limited	**(50,211)**	**–**
– Depositor Compensation Scheme Reserve	**(28,551)**	**(28,551)**
– Intangible assets	**(8,989)**	**(8,989)**
– Investment property revaluation reserve	**(3,360)**	**(3,360)**
– Other	**(352)**	**(362)**
Sub-total Tier 1	**305,686**	**306,410**
Tier 2		
As per statement of Financial Position		
Revaluation reserve	**42,510**	**42,139**
Less: Own Funds adjustments		
– Property revaluation reserve	**(4,715)**	**(4,715)**
– Unrealised gains and losses	**(4,084)**	**(3,713)**
– Investment property revaluation reserve	**2,684**	**2,684**
– Subordinated loan to HSBC Life Assurance (Malta) Limited	**(11,500)**	**(11,500)**
	24,895	**24,895**
As per statement of Financial Position		
Subordinated liabilities	**87,284**	**88,093**
Less: Own Funds adjustments		
– HSBC Life Assurance (Malta) Limited – holding in banks subordinated loan capital	**809**	**–**
– Amortisation of subordinated loan capital	**(42,252)**	**(42,252)**
Subtotal of subordinated liabilities	**45,841**	**45,841**
Subtotal Tier 2	**70,736**	**70,736**
Total Own Funds	**376,422**	**377,146**

6 Capital management and allocation *(continued)*

Capital adequacy calculation

	Group			*Bank*		
	Exposure value	*RWA*	*Capital Required*	*Exposure value*	*RWA*	*Capital Required*
	2014	**2014**	**2014**	**2014**	**2014**	**2014**
	€000	**€000**	**€000**	**€000**	**€000**	**€000**
Exposures under the standardised approach						
Credit risk						
Sovereign	**1,087,718**	**–**	**–**	**1,087,718**	**–**	**–**
Institutions	**1,025,526**	**184,557**	**14,765**	**1,025,518**	**184,556**	**14,764**
Corporates	**197,040**	**192,843**	**15,427**	**197,040**	**192,843**	**15,427**
Public sector	**209,360**	**1,032**	**83**	**209,360**	**1,032**	**83**
Retail	**183,744**	**132,327**	**10,586**	**183,744**	**132,327**	**10,586**
Secured on real estate property	**2,576,213**	**1,482,941**	**118,635**	**2,576,213**	**1,482,941**	**118,635**
Past due items	**302,590**	**302,590**	**24,207**	**302,590**	**302,590**	**24,207**
Other items	**323,599**	**248,080**	**19,846**	**329,995**	**253,570**	**20,286**
	5,905,790	**2,544,370**	**203,549**	**5,912,178**	**2,549,859**	**203,988**
Operational risk		**339,860**	**27,189**		**339,860**	**27,189**
Market risk		**4,443**	**355**		**4,443**	**355**
		2,888,673	**231,093**		**2,894,162**	**231,532**

	Group		*Bank*	
	Nominal amount	*Risk-weighted amount*	*Nominal amount*	*Risk-weighted amount*
	2014	**2014**	**2014**	**2014**
Assets	**€000**	**€000**	**€000**	**€000**
Balances with Central Bank of Malta, Treasury Bills and cash	**118,033**	**–**	**118,033**	**–**
Cheques in course of collection	**10,990**	**2,198**	**10,990**	**2,198**
Financial investments	**1,137,710**	**38**	**1,137,697**	**32**
Loans and advances to banks	**796,263**	**142,345**	**796,257**	**142,340**
Loans and advances to customers	**3,363,893**	**1,986,889**	**3,363,893**	**1,986,888**
Shares in subsidiary companies	**–**	**–**	**5,963**	**5,963**
Property, plant and equipment and investment property	**71,142**	**71,142**	**71,240**	**71,240**
Other assets	**64,167**	**100,932**	**63,739**	**100,920**
Prepayments and accrued income	**35,944**	**35,944**	**35,384**	**35,384**
	5,598,142	**2,339,488**	**5,603,196**	**2,344,965**
Off-balance sheet items				
Contingent liabilities, commitments and other	**1,668,449**	**204,882**	**1,668,471**	**204,894**
Total adjusted assets and off-balance sheet items		**2,544,370**		**2,549,859**
Operational risk		**339,860**		**339,860**
Market risk		**4,443**		**4,443**
Total risk weighted assets		**2,888,673**		**2,894,162**

6 Capital management and allocation *(continued)*

	Group	*Bank*
	2014	**2014**
	€000	**€000**
Total own funds		
Tier 1		
Called up share capital	**97,281**	**97,281**
Retained earnings	**251,391**	**252,115**
Exclusions/deductions:		
– Depositor compensation scheme reserve	**(28,551)**	**(28,551)**
– Final dividend	**(5,446)**	**(5,446)**
– Intangible assets	**(8,989)**	**(8,989)**
	305,686	**306,410**
Tier 2		
Available-for-sale reserve	**14,851**	**14,851**
Property revaluation reserve	**21,544**	**21,544**
Subordinated liabilities	**45,841**	**45,841**
Deductions:		
– Subordinated loan to HSBC Life Assurance (Malta) Limited	**(11,500)**	**(11,500)**
	70,736	**70,736**
Total own funds	**376,422**	**377,146**
Capital adequacy ratio at 31 December 2014		
Tier 1 Ratio	**10.6%**	**10.6%**
Total capital ratio	**13.0%**	**13.0%**
Capital adequacy ratio at 31 December 2013		
Tier 1 Ratio	9.4%	9.4%
Total capital ratio	12.9%	12.9%

Risk Weighted Assets and Own Funds computation as at 2014 is based on the Capital Requirements Regulation whereas 2013 is based on MFSA Banking Rule 04.

Leverage ratio

The leverage ratio is a new regulatory and supervisory tool introduced in CRR Article 429 and 431. It is intended to provide a transparent and non-risk based measurement of institutions to supplement the risk-based capital requirements, and is the result of Tier 1 divided by the total of unweighted exposures, including on and off balance sheet assets adjusted for deductions.

HSBC Bank Malta p.l.c. complies with the reporting requirement of the leverage ratio as prescribed in CRR and ALCO monitors the leverage ratio on an ongoing basis.

	Group	*Bank*
	2014	**2014**
	€000	**€000**
Tier 1 capital	**305,686**	**306,410**
Total on/off balance sheet assets adjusted for deductions	**5,905,790**	**5,912,178**
Leverage ratio	**5.18%**	**5.18%**

7 Interest and similar income

	Group		Bank	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
On loans and advances to banks	**1,488**	1,914	**1,476**	1,891
On loans and advances to customers	**134,349**	140,979	**134,451**	140,994
On balances with Central Bank of Malta	**97**	322	**97**	322
On Treasury Bills	**300**	99	**300**	99
	136,234	143,314	**136,324**	143,306
On debt and other fixed income instruments	**24,863**	26,433	**24,334**	25,659
Amortisation of net premiums	**(7,708)**	(7,641)	**(7,688)**	(7,590)
	17,155	18,792	**16,646**	18,069
	153,389	162,106	**152,970**	161,375
Interest and similar income from:				
– Group companies	**1,493**	1,886	**1,473**	1,886
– subsidiary companies	**–**	–	**102**	15

Discount unwind on impaired loans and advances to customers included in interest receivable on loans and advances to customers amounted to €2,515,000 (2013: €2,164,000).

8 Interest expense

	Group		Bank	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
On deposits by banks	**39**	119	**39**	119
On customer accounts	**28,739**	32,827	**28,863**	32,935
On subordinated liabilities	**4,449**	4,449	**4,449**	4,449
	33,227	37,395	**33,351**	37,503
Interest payable to:				
– Group companies	**19**	93	**19**	93
– subsidiary companies	**–**	–	**124**	108

9 Net fee and commission income

	Group		Bank	
	2014	2013	**2014**	2013
	€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	**17,187**	17,594	**17,187**	17,594
– trust and other fiduciary activities that result in the holding or investing of assets on behalf of individuals and other institutions	**8,356**	9,350	**4,663**	4,764
– other	**2,908**	2,593	**4,445**	4,385
	28,451	29,537	**26,295**	26,743
Net fee and commission income from:				
– Group companies	**1,192**	1,248	**514**	699
– subsidiary companies	**–**	–	**3,320**	3,913

Net fee and commission income for the bank include €2,945,000 (2013: €2,649,000) derived from investment services activities.

10 Dividend income

Dividend income for the bank amounts to €20,462,000 (2013: €12,308,000) and represents dividend received from subsidiary companies.

11 Trading profits

	2014	2013
	€000	€000
Group/Bank		
Profit on foreign exchange activities	**8,741**	9,213
Net profits on financial instruments at fair value through profit or loss	**44**	310
	8,785	9,523

12 Net gains on sale of available-for-sale financial investments

Net gains represent revaluation amounts which were transferred from equity following the sale of available-for-sale investments.

13 Net other operating income

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Operating income				
Rental income	**927**	909	**819**	783
Services rendered	**805**	530	**446**	277
Profit arising from liquidation of subsidiary	**–**	–	**559**	–
Other income	**–**	373	**–**	45
	1,732	1,812	**1,824**	1,105
Operating expense				
Other expenses	**(148)**	(136)	**(135)**	(136)
	(148)	(136)	**(135)**	(136)
	1,584	1,676	**1,689**	969
Operating income from:				
– Group companies	**1,595**	1,295	**1,192**	956
– Subsidiary companies	**–**	–	**603**	86

14 Net earned insurance premiums

	Group	
	2014	2013
	€000	€000
Life insurance		
Gross premium written	**64,722**	70,702
Outward reinsurance premiums	**(4,691)**	(4,629)
	60,031	66,073

15 Net insurance claims incurred and movement in policyholders' liabilities

	Group					
	Gross	*Reinsurance*	*Net*	*Gross*	*Reinsurance*	*Net*
	2014	**2014**	**2014**	2013	2013	2013
	€000	**€000**	**€000**	€000	€000	€000
Life insurance						
Claims paid	**51,220**	**(1,551)**	**49,669**	44,523	(1,096)	43,427
Change in technical provision	**67,602**	**(33,108)**	**34,494**	31,575	(5,049)	26,526
Change in claims provision	**809**	**(344)**	**465**	1,561	(313)	1,248
	119,631	**(35,003)**	**84,628**	77,659	(6,458)	71,201

16 Employee compensation and benefits

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Wages, salaries and allowances	**46,843**	45,197	**44,374**	41,790
Defined contribution social security costs	**2,631**	2,122	**2,500**	2,353
Retirement benefits	**1,943**	844	**1,943**	830
Share-based payments	**327**	376	**306**	362
	51,744	48,539	**49,123**	45,335
	Number	*Number*	***Number***	*Number*
Average number of employees				
– executive and senior managerial	**284**	256	**266**	235
– other managerial, supervisory and clerical	**1,077**	1,051	**1,029**	986
– others	**28**	31	**28**	31
	1,389	1,338	**1,323**	1,252

The charge for the year in respect of Retirement benefits consists of early voluntary retirement charges of €1,674,000 (2013: €380,000) for the local group and the bank and pension costs of €269,000 (2013: €450,000) for the bank and €269,000 (2013: €464,000) for the local group. €352,000 out of the €1,674,000 represents early voluntary retirement charges effected directly through profit or loss.

Share-based payments

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 local group employees under all-employee share plans and achievement shares awarded to local group senior management under discretionary incentive plans. The local group offers the following types of share option schemes to its employees.

Main Plans	**Policy**	**Purpose**
Savings related share options plans	• Exercisable within three months following the first anniversary of the commencement of a one-year savings contract or within six months following either the third or fifth anniversaries of the commencement of three-year or five-year contracts, respectively • The exercise price is set at a 20% (2013: 20%) discount to the market value immediately preceding the date of invitation	• Eligible employees save up to £250 per month (or its equivalent in euros), with the option to use the savings to acquire shares • To align the interests of all employees with the creation of shareholder value
HSBC Holdings Group share option plan	• Plan ceased in May 2005 • Exercisable between third and tenth anniversaries of the date of grant	• Long-term incentive plan between 2000 and 2005 during which certain HSBC employees were awarded share options

16 Employee compensation and benefits *(continued)*

	Group			
	Options	*Weighted average exercise price (€)*	*Options*	*Weighted average exercise price (€)*
	2014	**2014**	2013	2013
Savings related Share Option Plans				
Outstanding at 1 January	**517,810**	**4.45**	677,764	4.61
Granted during the year	**4,945**	**5.89**	–	–
Exercised during the year	**(305,197)**	**3.42**	(96,990)	5.25
Closed during the year	**(15,452)**	**5.17**	(62,964)	4.86
Outstanding at 31 December	**202,106**	**5.35**	517,810	4.45
Exercisable at 31 December	**29,177**	**5.06**	3,413	6.43
Group Share Option Plans				
Outstanding at 1 January	**288,038**	**9.11**	479,663	8.35
Exercised during the year	**–**	**–**	(126,230)	7.66
Released during the year	**(288,038)**	**9.11**	(65,395)	7.23
Outstanding at 31 December	**–**	**–**	288,038	9.11
Exercisable at 31 December	**–**	**–**	288,038	9.11

The options outstanding at the 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 dates.

Fair value of share option schemes

Fair values of share options awarded under all-employee share option plans, 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 risk-free interest rate is 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.

The local group also grants the following type of award to its employees:

Award	**Policy**	**Purpose**
Restricted share awards (including Group Performance Share Plans 'GPSP')	• Vesting of awards generally subject to continued employment with the local group • Vesting often staggered over three years. GPSP awards vest after five years • Certain shares subject to a retention requirement post vesting • In the case of GPSP awards retention applies until cessation of employment • Awards generally not subject to performance conditions • Awards granted from 2010 onwards are subject to clawback provision prior to vesting	• Rewards employee performance and potential and retention of key employees • To defer variable pay

These awards are generally granted to employees early in the year following the year to which the award relates. The charge for these awards is recognised from the start of the period to which the service relates to the end of the vesting period. The vesting period is the period over which the employee satisfies certain service conditions in order to become entitled to the award. Due to the staggered vesting profile of certain deferred share awards, the employee becomes entitled to a portion of the award at the end of each year during the vesting period.

17 Net impairment

	Group		Bank	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Write-downs				
Loans and advances to customers				
– individual allowances	**(25,321)**	(5,864)	**(25,321)**	(5,864)
– bad debts written off	**(8,288)**	(883)	**(8,288)**	(883)
	(33,609)	(6,747)	**(33,609)**	(6,747)
Other assets				
– individual allowances	**(260)**	–	**(260)**	–
Reversals of write-downs				
Loans and advances to customers				
– individual allowances	**5,143**	3,321	**5,143**	3,321
– collective allowances	**5,673**	57	**5,673**	57
– bad debts recovered	**508**	97	**508**	97
	11,324	3,475	**11,324**	3,475
	(22,545)	(3,272)	**(22,545)**	(3,272)

18 Profit before tax

	2014	2013
	€000	€000
Group/Bank		
Profit before tax is stated after charging:		
Directors' emoluments		
– fees	**178**	169
– other emoluments	**958**	1,475
	1,136	1,644
Profit before tax for the local group is also stated after charging the following fees (excluding VAT) in relation to services provided by the external auditors of the local group:		
– auditors' fees	**180**	172
– other assurance services fees	**27**	33
– tax advisory services fees	**12**	23
– other non-audit services fees	**34**	13
	253	241

19 Tax expense

	Group		Bank	
	2014	2013	**2014**	2013
	€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	**20,733**	30,869	**28,083**	30,761
– deferred	**(2,229)**	891	**(5,342)**	(57)
	18,504	31,760	**22,741**	30,704

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

	Group		Bank	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Profit before tax	**52,121**	90,477	**63,123**	87,119
Tax at the applicable rate of 35%	**18,242**	31,667	**22,093**	30,492
Tax effect of profits taxed at different rates	**(7)**	(11)	**–**	–
Tax effect of non-deductible expenses	**66**	61	**502**	60
Tax effect of depreciation charges not deductible by way of capital allowances	**199**	221	**199**	221
Tax effect of property sales tax consequences	**10**	(13)	**–**	–
Tax effect of additional deductions	**(55)**	(53)	**(55)**	(55)
Tax effect of taxable temporary differences not previously recognised	**49**	(112)	**2**	(14)
Tax on profit on ordinary activities	**18,504**	31,760	**22,741**	30,704

20 Earnings per share

The calculation of earnings per share of the local 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 2014. For the purposes of calculating the earnings per share for the comparative year ended 31 December 2013, the number of shares in issue was adjusted to reflect the bonus issue of 1 share for every 9 shares held as of 29 April 2014 made by way of capitalisation of reserves. The number of shares following the bonus issue amounted to 324,271,380.

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

	Group		Bank	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Balances with Central Bank of Malta	**54,604**	71,998	**54,604**	71,998
Malta Government Treasury Bills	**31,496**	48,937	**31,496**	48,937
Cash	**31,933**	30,523	**31,933**	30,522
	118,033	151,458	**118,033**	151,457

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 year end was €46,492,601 (2013: €43,854,000) in respect of the local group and the bank. Balances with Central Bank of Malta amounting to €8,000,000 (2013: €8,000,000) have been pledged in favour of the Depositor Compensation Scheme (refer to note 44).

22 Derivatives

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Derivative assets				
Held for trading	**13,170**	12,666	**13,098**	12,666
Held for trading instruments held with:				
– Group companies	**5,207**	3,259	**5,205**	3,259
Derivative liabilities				
Held for trading	**13,870**	12,929	**13,419**	12,929
Held for trading instruments held with:				
– Group companies	**8,226**	9,206	**8,226**	9,206

Derivatives held for trading

	Notional	*Fair value assets*	*Fair value liabilities*	*Notional*	*Fair value assets*	*Fair value liabilities*
	2014	**2014**	**2014**	2013	2013	2013
	€000	**€000**	**€000**	€000	€000	€000
Group						
Interest rate derivatives						
– interest rate swaps purchased	**74,797**	**5,516**	**–**	158,736	7,242	–
– interest rate swaps written	**74,797**	**–**	**5,760**	158,736	–	7,561
Currency derivatives						
– foreign exchange contracts	**497,335**	**5,269**	**5,328**	162,208	2,448	2,390
– foreign exchange options purchased	**28,074**	**1,246**	**3**	13,303	353	249
– foreign exchange options written	**27,909**	**–**	**1,246**	13,303	247	353
Equity derivatives						
– equity index options purchased	**39,391**	**1,139**	**20**	64,657	2,376	–
– equity index options written	**39,392**	**–**	**1,513**	64,657	–	2,376
		13,170	**13,870**		12,666	12,929
Bank						
Interest rate derivatives						
– interest rate swaps purchased	**74,797**	**5,516**	**–**	158,736	7,242	–
– interest rate swaps written	**74,797**	**–**	**5,760**	158,736	–	7,561
Currency derivatives						
– foreign exchange contracts	**141,140**	**5,198**	**5,275**	162,208	2,448	2,390
– foreign exchange options purchased	**27,909**	**1,246**	**–**	13,303	353	249
– foreign exchange options written	**27,909**	**–**	**1,246**	13,303	247	353
Equity derivatives						
– equity index options purchased	**39,390**	**1,138**	**–**	64,657	2,376	–
– equity index options written	**39,390**	**–**	**1,138**	64,657	–	2,376
		13,098	**13,419**		12,666	12,929

All derivatives are over the counter products.

23 Financial assets designated at fair value through profit or loss

	Group	
	2014	2013
	€000	€000
Debt, Treasury Bills and other fixed income instruments	**664,981**	251,305
Equity and other non-fixed income instruments	**770,440**	226,040
Policy loans	**(13,841)**	–
	1,421,580	477,345

a *Debt, Treasury Bills and other fixed income instruments*

	Group	
	2014	2013
	€000	€000
Issued by public bodies		
– local government	**85,094**	80,255
– foreign government	**153,843**	101,272
Issued by other issuers		
– local banks	**3,551**	3,448
– foreign banks	**200,523**	6,993
– others local	**5,400**	3,377
– others foreign	**216,570**	55,960
	664,981	251,305
Listing status		
– listed on the Malta Stock Exchange	**94,045**	87,080
– listed elsewhere	**478,230**	164,225
– foreign unlisted	**92,706**	–
	664,981	251,305
At 1 January	**251,305**	255,183
Acquisitions	**449,875**	36,485
Disposals	**(62,843)**	(36,403)
Changes in fair value	**26,644**	(3,960)
At 31 December	**664,981**	251,305

23 Financial assets designated at fair value through profit or loss *(continued)*

b *Equity and other non-fixed income instruments*

	Group	
	2014	2013
	€000	€000
Issued by other issuers		
– local banks	**139**	–
– foreign banks	**14,158**	–
– others local	**70,687**	43,155
– others foreign	**685,456**	182,885
	770,440	226,040
Listing status		
– listed on the Malta Stock Exchange	**9,930**	8,396
– listed elsewhere	**700,190**	217,644
– foreign unlisted	**60,320**	–
	770,440	226,040
At 1 January	**226,040**	199,408
Acquisitions	**588,699**	23,866
Disposals	**(53,029)**	(16,095)
Changes in fair value	**8,730**	18,861
At 31 December	**770,440**	226,040

The bank has no financial assets designated at fair value through profit or loss.

24 Financial investments

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Debt and other fixed income instruments				
– available-for-sale	**1,153,862**	918,219	**1,137,678**	897,724
Equity and other non-fixed income instruments				
– available-for-sale	**22**	73	**19**	70
	1,153,884	918,292	**1,137,697**	897,794

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

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Issued by public bodies				
– local government	**575,780**	539,424	**564,648**	524,510
– foreign government	**90,871**	96,520	**88,399**	94,046
Issued by other issuers				
– foreign banks	**189,403**	49,115	**189,371**	46,503
– local others	**–**	495	**–**	–
– foreign others	**297,808**	232,665	**295,260**	232,665
	1,153,862	918,219	**1,137,678**	897,724
Amounts include:				
– issued by Group companies	**32**	32	**–**	–

24 Financial investments *(continued)*

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

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Listing status				
– listed on the Malta Stock Exchange	**575,780**	539,919	**564,648**	524,510
– listed elsewhere	**578,082**	378,300	**573,030**	373,214
	1,153,862	918,219	**1,137,678**	897,724
At 1 January	**918,219**	987,398	**897,724**	962,651
Exchange adjustments	**33,209**	(5,148)	**33,139**	(5,117)
Amortisation	**(7,708)**	(7,641)	**(7,688)**	(7,590)
Additions	**413,638**	277,694	**413,638**	275,655
Disposals/Redemptions	**(217,137)**	(334,396)	**(212,930)**	(328,537)
Changes in fair value	**13,641**	312	**13,795**	662
At 31 December	**1,153,862**	918,219	**1,137,678**	897,724

Debt instruments with a carrying amount of €69,486,287 (2013: €89,150,000) have been pledged against the provision of credit lines by the Central Bank of Malta. At 31 December 2014, no balances were outstanding against these credit lines. In addition debt securities with a carrying amount of €21,531,900 (2013: €20,794,000) have been pledged in favour of the Depositors' Compensation Scheme (refer to note 44).

The financial investments which are denominated in currencies other than the reporting currency are economically hedged through balances in corresponding currencies mainly forming part of Customer accounts and Deposits by banks. Thus, the exchange adjustment reflected above does not result in an exchange gain recognised in profit or loss.

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

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Issued by issuers other than public bodies and banks				
– local others	**8**	59	**5**	56
– foreign others	**14**	14	**14**	14
	22	73	**19**	70
Listing status				
– local unlisted	**8**	59	**5**	56
– foreign unlisted	**14**	14	**14**	14
	22	73	**19**	70
At 1 January	**73**	73	**70**	70
Disposals	**(347)**	–	**(347)**	–
Impairment reversal	**300**	–	**300**	**–**
Other movement	**(4)**	–	**(4)**	**–**
At 31 December	**22**	73	**19**	70

As at the reporting date, impairment loss on the local group's equity and other non-fixed income instruments available-for-sale amounted to €47,000 (2013: €347,000).

25 Loans and advances to banks

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Repayable on call and at short notice	**647,388**	467,192	**568,550**	467,077
Term loans and advances	**227,707**	97,598	**227,707**	97,598
	875,095	564,790	**796,257**	564,675
Amounts include:				
– due from Group companies	**787,517**	562,066	**775,156**	562,066

26 Loans and advances to customers

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Repayable on call and at short notice	**351,022**	384,340	**351,021**	384,340
Term loans and advances	**3,012,871**	2,990,041	**3,024,372**	2,990,041
Gross loans and advances to customers	**3,363,893**	3,374,381	**3,375,393**	3,374,381
Allowances for uncollectibility	**(90,512)**	(73,399)	**(90,512)**	(73,399)
Net loans and advances to customers	**3,273,381**	3,300,982	**3,284,881**	3,300,982
Allowances for uncollectibility				
– individually assessed allowances	**82,966**	60,180	**82,966**	60,180
– collectively assessed allowances	**7,546**	13,219	**7,546**	13,219
	90,512	73,399	**90,512**	73,399
Amounts include				
– due from subsidiary companies	**–**	–	**11,500**	–

The balance of individually assessed allowances at reporting date includes €43,634,000 (2013: €38,603,000) in respect of interest in suspense which has been netted off against interest receivable. Loans with a carrying amount of €103,438,000 (2013: €106,379,000) have been pledged against the provision of credit lines by Central Bank of Malta. At 31 December 2014, no balances were outstanding against these credit lines.

27 Shares in subsidiary companies

Bank *Name of company*	*Nature of business*	*Equity interest*	**2014**	2013
		%	**€000**	€000
HSBC Life Assurance (Malta) Limited	Life insurance	**99.99**	**28,578**	28,578
HSBC Global Asset Management (Malta) Limited	Portfolio management services	**99.99**	**5,940**	5,940
HSBC Securities Services (Malta) Limited	Fund administration services	**99.99**	**–**	1,166
HSBC Stockbrokers (Malta) Limited	Stockbroking services	**99.99**	**23**	23
			34,541	35,707

27 Shares in subsidiary companies *(continued)*

HSBC Stockbrokers (Malta) Limited and HSBC Securities Services (Malta) Limited are undergoing a voluntary winding up process. HSBC Life Assurance (Malta) Limited holds investment in the following subsidiary:

Name of company	*Nature of business*	*Equity interest*	**2014**	2013
		%	**€000**	€000
HSBC Insurance Management Services (Europe) Limited	Insurance management services	**99.99**	**25**	25

All subsidiaries are incorporated in Malta.

28 Intangible assets

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Software	**9,094**	10,255	**8,989**	10,093
Present value of in-force long-term insurance business	**64,877**	76,363	**–**	–
	73,971	86,618	**8,989**	10,093

a *Software*

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Cost				
At 1 January	**25,825**	26,056	**24,407**	24,719
Additions	**1,939**	1,358	**1,932**	1,277
Disposals	**–**	(1,589)	**–**	(1,589)
Write-offs	**(207)**	–	–	–
At 31 December	**27,557**	25,825	**26,339**	24,407
Amortisation and impairment losses				
At 1 January	**15,570**	14,012	**14,314**	12,776
Charge for the year	**3,092**	2,844	**3,036**	2,824
Reversal of impairment losses	**–**	(622)	**–**	(622)
Write-offs	**(199)**	597	–	597
Disposals	**–**	(1,261)	**–**	(1,261)
At 31 December	**18,463**	15,570	**17,350**	14,314
Carrying amount at 1 January	**10,255**	12,044	**10,093**	11,943
Carrying amount at 31 December	**9,094**	10,255	**8,989**	10,093

Impairment losses, reversal of impairment losses and write-offs are recognised in General and administrative expenses.

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

	Group	
	2014	2013
	€000	€000
At 1 January	**76,363**	79,166
Addition from new business	**7,624**	5,459
Movement in in-force business	**(19,110)**	(8,262)
At 31 December	**64,877**	76,363

29 Property, plant and equipment

	Land and buildings	*Computer equipment*	*Others*	*Total*
	€000	**€000**	**€000**	**€000**
Group				
Cost/revaluation				
At 1 January 2014	**43,665**	**19,700**	**45,652**	**109,017**
Acquisitions	**162**	**35**	**1,427**	**1,624**
Disposals	**–**	**(538)**	**(2,078)**	**(2,616)**
At 31 December 2014	**43,827**	**19,197**	**45,001**	**108,025**
Depreciation and impairment losses				
At 1 January 2014	**918**	**14,218**	**32,390**	**47,526**
Charge for the year	**396**	**1,162**	**1,902**	**3,460**
Revaluation	**–**	**–**	**–**	**–**
Disposals	**–**	**(546)**	**(1,896)**	**(2,442)**
At 31 December 2014	**1,314**	**14,834**	**32,396**	**48,544**
Carrying amount at 1 January 2014	**42,747**	**5,482**	**13,262**	**61,491**
Carrying amount at 31 December 2014	**42,513**	**4,363**	**12,605**	**59,481**
Cost/revaluation				
At 1 January 2013	39,372	17,613	44,108	101,093
Acquisitions	4,648	3,386	2,695	10,729
Revaluation	81	–	–	81
Transfer to Non-current assets held for sale (note 31)	(436)	–	–	(436)
Disposals	–	(1,299)	(1,151)	(2,450)
At 31 December 2013	43,665	19,700	45,652	109,017
Depreciation and impairment losses				
At 1 January 2013	525	14,390	31,306	46,221
Charge for the year	396	900	2,153	3,449
Revaluation	(3)	–	–	(3)
Disposals	–	(1,072)	(1,069)	(2,141)
At 31 December 2013	918	14,218	32,390	47,526
Carrying amount at 1 January 2013	38,847	3,223	12,802	54,872
Carrying amount at 31 December 2013	42,747	5,482	13,262	61,491

29 Property, plant and equipment *(continued)*

	Land and buildings	*Computer equipment*	*Others*	*Total*
	€000	**€000**	**€000**	**€000**
Bank				
Cost/revaluation				
At 1 January 2014	**43,770**	**19,446**	**45,430**	**108,646**
Acquisitions	**155**	**32**	**1,427**	**1,614**
Revaluation	**–**	**–**	**–**	**–**
Disposals	**–**	**(504)**	**(2,059)**	**(2,563)**
At 31 December 2014	**43,925**	**18,974**	**44,798**	**107,697**
Depreciation and impairment losses				
At 1 January 2014	**918**	**13,967**	**32,186**	**47,071**
Charge for the year	**396**	**1,151**	**1,902**	**3,449**
Revaluation	**–**	**–**	**–**	**–**
Disposals	**–**	**(504)**	**(1,892)**	**(2,396)**
At 31 December 2014	**1,314**	**14,614**	**32,196**	**48,124**
Carrying amount at 1 January 2014	**42,852**	**5,479**	**13,244**	**61,575**
Carrying amount at 31 December 2014	**42,611**	**4,360**	**12,602**	**59,573**
Cost/revaluation				
At 1 January 2013	39,477	17,364	43,887	100,728
Acquisitions	4,648	3,381	2,694	10,723
Revaluation	81	–	–	81
Transfer to Non-current assets held for sale (note 31)	(436)	–	–	(436)
Disposals	–	(1,299)	(1,151)	(2,450)
At 31 December 2013	43,770	19,446	45,430	108,646
Depreciation and impairment losses				
At 1 January 2013	525	14,141	31,109	45,775
Charge for the year	396	898	2,146	3,440
Revaluation	(3)	–	–	(3)
Disposals	–	(1,072)	(1,069)	(2,141)
At 31 December 2013	918	13,967	32,186	47,071
Carrying amount at 1 January 2013	38,952	3,223	12,778	54,953
Carrying amount at 31 December 2013	42,852	5,479	13,244	61,575

Land and buildings reported above are all utilised for own activities.

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 €18,938,000 (2013: €18,675,000) for the local group and the bank.

A full revaluation on all land and buildings is carried out every three years. The last revaluation was carried out in 2012. On an annual basis, a desktop review is carried out to capture any significant year-on-year fluctuations.

30 Investment property

	Fair Value	*Cost*	*Fair Value*	*Cost*
	2014	**2014**	2013	2013
	€000	**€000**	€000	€000
Group				
Freehold land and buildings				
As at 1 January	**14,529**	**8,615**	14,471	8,615
Additions	**1,679**	**1,679**	–	–
Fair value adjustments	**118**	**–**	58	–
At 31 December	**16,326**	**10,294**	14,529	8,615
Bank				
Freehold land and buildings				
As at 1 January	**11,660**	**6,498**	11,660	6,498
Additions	**–**	**–**	–	–
Fair value adjustments	**7**	**–**	–	–
At 31 December	**11,667**	**6,498**	11,660	6,498

During the year ended 31 December 2014, €898,000 (2013: €891,000) was recognised as rental income in profit or loss relating to investment property of the local group. The bank recognised €790,000 (2013: €765,000) as rental income, which was received from a Group company. Related repair and maintenance expenses incurred by the bank and the local group on these properties are reimbursed by the tenants.

Fair values are determined by professional valuers who apply recognised valuation techniques. The bank has in place set benchmarks to ensure that these valuers are independent, hold the necessary recognised and relevant professional qualifications as well as the knowledge and experience depending on the location and category of the investment property being valued. Further disclosures on fair value are included in note 5(v).

31 Non-current assets held for sale

	Group/Bank	
	2014	2013
	€000	€000
Assets acquired in satisfaction of debt	**9,297**	11,347
Other	**–**	436
	9,297	11,783

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

32 Other assets

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Acceptances and endorsements	**2,281**	1,796	**2,281**	1,796
Reinsurance assets	**86,691**	41,102	**–**	–
Other	**17,632**	9,837	**6,665**	7,636
	106,604	52,735	**8,946**	9,432
Amounts include:				
– due from Group companies	**1,403**	1,442	**1,403**	1,442

Other assets are stated net of an individual allowance for uncollectibility of €260,000 (refer to note 17). The local group's Other assets includes €9,344,000 (2013: €89,000) deferred acquisition costs related to investment contracts.

33 Prepayments and accrued income

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Accrued income	**43,093**	37,313	**32,988**	32,564
Dividend income	**–**	–	**1,300**	–
Prepayments	**1,637**	1,364	**1,610**	1,109
	44,730	38,677	**35,898**	33,673
Amounts include:				
– due from Group companies	**708**	204	**164**	61
– due from subsidiary companies	**–**	–	**1,650**	303

34 Deposits by banks

	2014	2013
	€000	€000
Group/Bank		
Term deposits	**25,952**	766
Repayable on demand	**33,896**	41,028
	59,848	41,794
Amounts include:		
– due to Group companies	**28,133**	9,498

35 Customer accounts

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Term deposits	**1,561,422**	1,686,355	**1,561,422**	1,687,390
Repayable on demand	**3,305,702**	2,831,507	**3,370,063**	2,866,714
	4,867,124	4,517,862	**4,931,485**	4,554,104
Amounts include:				
– due to subsidiary companies	**–**	–	**64,361**	36,242

36 Deferred tax

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Deferred tax (liabilities)/assets are attributable to the following:				
– excess of capital allowances over depreciation	**(1,825)**	(1,664)	**(2,125)**	(1,659)
– allowances for uncollectibility	**30,210**	24,112	**30,210**	24,112
– property sales tax consequences	**(6,388)**	(6,371)	**(5,995)**	(6,027)
– fair value movements on investments	**(10,148)**	(5,970)	**(9,953)**	(5,721)
– value of in-force life insurance business	**(22,707)**	(26,727)	**–**	–
– fair value movement on policyholders' investments	**(5,041)**	2,303	**–**	–
– retirement benefits	**435**	696	**435**	674
– other	**832**	948	**1,030**	1,125
	(14,632)	(12,673)	**13,602**	12,504

36 Deferred tax *(continued)*

	Group			
	At 1 January 2014	*Recognised in profit or loss*	*Recognised in equity*	*At 31 December 2014*
	€000	**€000**	**€000**	**€000**
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	**(1,664)**	**(161)**	**–**	**(1,825)**
– allowances for uncollectibility	**24,112**	**6,098**	**–**	**30,210**
– property sales tax consequences	**(6,371)**	**(50)**	**3**	**(6,418)**
– fair value movements on investments	**(5,970)**	**–**	**(4,178)**	**(10,148)**
– value of in-force life insurance business	**(26,727)**	**4,020**	**–**	**(22,707)**
– fair value movement on policyholders’ investments	**2,303**	**(7,344)**	**–**	**(5,041)**
– retirement benefits	**696**	**(261)**	**–**	**435**
– other	**948**	**(73)**	**(13)**	**862**
	(12,673)	**2,229**	**(4,188)**	**(14,632)**

	Group			
	At 1 January 2013	*Recognised in profit or loss*	*Recognised in equity*	*At 31 December 2013*
	€000	€000	€000	€000
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	(1,410)	(254)	–	(1,664)
– allowances for uncollectibility	22,110	2,002	–	24,112
– property sales tax consequences	(6,347)	(4)	(20)	(6,371)
– fair value movements on investments	(7,366)	–	1,396	(5,970)
– value of in-force life insurance business	(27,708)	981	–	(26,727)
– fair value movement on policyholders’ investments	2,086	217	–	2,303
– retirement benefits	2,115	(1,419)	–	696
– unutilised tax losses	2,039	(2,039)	–	–
– other	1,391	(375)	(68)	948
	(13,090)	(891)	1,308	(12,673)

	Bank			
	At 1 January 2014	*Recognised in profit or loss*	*Recognised in equity*	*At 31 December 2014*
	€000	**€000**	**€000**	**€000**
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	**(1,659)**	**(466)**	**–**	**(2,125)**
– allowances for uncollectibility	**24,112**	**6,098**	**–**	**30,210**
– property sales tax consequences	**(6,027)**	**(1)**	**3**	**(6,025)**
– fair value movements on investments	**(5,721)**	**–**	**(4,232)**	**(9,953)**
– retirement benefits	**674**	**(239)**	**–**	**435**
– other	**1,125**	**(50)**	**(15)**	**1,060**
	12,504	**5,342**	**(4,244)**	**13,602**

36 Deferred tax *(continued)*

	Bank			
	At 1 January 2013	*Recognised in profit or loss*	*Recognised in equity*	*At 31 December 2013*
	€000	€000	€000	€000
Movement in temporary differences relating to:				
– excess of capital allowances over depreciation	(1,413)	(246)	–	(1,659)
– allowances for uncollectibility	22,110	2,002	–	24,112
– property sales tax consequences	(6,007)	–	(20)	(6,027)
– fair value movements on investments	(7,015)	–	1,294	(5,721)
– retirement benefits	2,092	(1,418)	–	674
– other	1,486	(281)	(80)	1,125
	11,253	57	1,194	12,504

The local 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.

In the Budget 2015 Document presented by the Minister of Finance in November 2014 the taxation rules on capital gains upon transfer of immovable property have been amended to include a reduction of the property sales tax from 12% to either 8% or 10% depending on the type of property. The local group estimates that the effect of this change as at the reporting date is a reduction in the deferred tax liability of €2 million.

37 Liabilities under investment contracts

	Group	
	2014	2013
	€000	€000
At 1 January	**16,763**	17,254
Fair value of assets acquired during the year	**993,324**	–
Premiums received	**5,459**	285
Amounts paid on surrender and other termination during the year	**(2,796)**	(2,413)
Changes in unit prices and other movements	**7,844**	1,637
At 31 December	**1,020,594**	16,763

38 Liabilities under insurance contracts

	Group	
	Gross	*Gross*
	2014	2013
	€000	€000
Life insurance (non-linked)		
Provisions for policyholders	**414,410**	348,206
Outstanding claims	**1,977**	2,568
Total non-linked	**416,387**	350,774
Life insurance (linked)		
Provisions for policyholders	**185,899**	174,035
Outstanding claims	**426**	190
Total linked	**186,325**	174,225
Total liabilities under insurance contracts	**602,712**	524,999

38 Liabilities under insurance contracts *(continued)*

	Group			
	Non-linked business	*Linked business*	*All business*	
	Provisions for policy-holders	*Provisions for policy-holders*	*Outstanding claims*	*Total*
	2014	**2014**	**2014**	**2014**
	€000	**€000**	**€000**	**€000**
At 1 January	**348,206**	**174,035**	**2,758**	**524,999**
Claims in respect of new business	**–**	**26,111**	**3,437**	**29,548**
Movement for the year	**66,204**	**(14,247)**	**(2,302)**	**49,655**
Previous year's claims paid	**–**	**–**	**(1,490)**	**(1,490)**
At 31 December	**414,410**	**185,899**	**2,403**	**602,712**
	2013	2013	2013	2013
	€000	€000	€000	€000
At 1 January	341,956	148,609	2,689	493,254
Claims in respect of new business	–	29,472	4,347	33,819
Movement for the year	6,250	(4,046)	(2,102)	102
Previous year's claims paid	–	–	(2,176)	(2,176)
At 31 December	348,206	174,035	2,758	524,999

39 Other liabilities

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Bills payable	**13,947**	11,718	**13,947**	11,718
Cash collateral for commitments	**146**	225	**146**	225
Acceptances and endorsements	**2,281**	1,796	**2,281**	1,796
Other	**27,729**	24,535	**13,764**	16,968
	44,103	38,274	**30,138**	30,707

40 Accruals and deferred income

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Accrued interest	**10,807**	13,635	**10,808**	13,662
Other	**16,707**	16,595	**15,262**	15,757
	27,514	30,230	**26,070**	29,419
Amounts include:				
– due to Group companies	**3,198**	3,445	**2,411**	3,110
– due to subsidiary companies	**–**	–	**1**	27

41 Provisions for liabilities and other charges

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
At 1 January	**3,211**	7,493	**3,149**	7,423
Provisions made during the year	**1,445**	552	**1,445**	552
Provisions reversed during the year	**–**	(52)	**–**	(52)
Provisions utilised during the year	**(2,239)**	(4,782)	**(2,177)**	(4,774)
At 31 December	**2,417**	3,211	**2,417**	3,149

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

Litigation provision as at 31 December 2014 amounted to €794,000 (2013: €671,000) for both bank and local group. This provision is expected to be settled after more than one year from the reporting date. The impact of discounting is not considered to be material. Movement for 2014 of €123,000 is reported in the profit or loss under 'Net provisions for liabilities and other charges'. Movement for 2013 is reported in the profit or loss as follows: (€52,000) under 'Net provisions for liabilities and other charges' and €172,000 under 'General and administrative expenses'.

The bank is a party to legal actions arising from normal business operations. Based on legal advice, management believes that adequate provisions have been made, taking into consideration the timing and amount of the probable economic outflows required against these litigations.

Early voluntary retirement scheme provision as at 31 December 2014 amounted to €1,623,000 (2013: €2,540,000) for the local group and €1,623,000 (2013: €2,478,000) for the bank. New provisions for 2014 of €1,322,000 for bank and local group are reported in note 16 Employee Compensation and Benefits under 'Retirement benefits'. The total amount of this provision is expected to be settled within a year from reporting date.

42 Subordinated liabilities

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
4.60% subordinated unsecured loan stock 2017	**58,174**	58,143	**58,174**	58,143
5.90% subordinated unsecured loan stock 2018	**29,110**	29,130	**29,919**	29,897
	87,284	87,273	**88,093**	88,040
Subordinated loan liabilities held by:				
– subsidiary companies	**–**	–	**809**	767

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

43 Called up share capital

	2014	2013
	€000	€000
Authorised		
470,000,000 Ordinary shares of 30 cent each	**141,000**	141,000
Issued and fully paid up		
324,271,000 (2013: 291,840,000) Ordinary shares of 30 cent each	**97,281**	87,552

The number of shares in issue have increased as a result of the bonus issue of 1 share for every 9 shares held as on 29 April 2014.

44 Reserves

a *Revaluation reserve*

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

b *Retained earnings*

Retained earnings include the Depositor Compensation Scheme reserve which is excluded for the purposes of the Own Funds calculations (refer to note 6) and the General Banking Risk reserve which is held as a capital buffer for regulatory purposes.

Depositor Compensation Scheme reserve

The Depositor Compensation Scheme reserve amounts to €28,551,000.

As at 31 December 2014, debt securities with a carrying amount of €21,531,900 had been pledged in terms of the Depositor Compensation Scheme (refer to note 24a). Central Bank balances amounting to €8,000,000 have also been pledged in favour of the scheme (refer to note 21).

General Banking Risk reserve

The revised Banking Rule 09 requires banks in Malta to hold additional reserves for general banking risks against non-performing loans. This reserve is required to be funded from planned dividend. As at the reporting date, under the three year transitional rules, this reserve amounted to €7,012,000 (85% of the total estimated amount). The increase during the year under review amounted to €3,493,000.

45 Contingent liabilities

	Group *Contract amount*		*Bank* *Contract amount*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Guarantees and assets pledged as collateral security				
– guarantees	**102,163**	81,432	**103,866**	83,135
– standby letters of credit	**30,216**	29,735	**30,216**	29,735
– other	**1,069**	685	**1,069**	685
	133,448	111,852	**135,151**	113,555
Amounts include:				
– in favour of Group companies	**1,413**	1,849	**1,413**	1,849
– in favour of subsidiary companies	**–**	–	**1,703**	1,703

Other contingent liabilities relate to legal claims against the bank. The timing and amount of the possible economic outflow of the local group against these amounts, based on legal advice, was determined to be remote.

46 Commitments

	Group *Contract amount*		*Bank* *Contract amount*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Documentary credits	**24,585**	22,151	**24,585**	22,151
Undrawn formal standby facilities, credit facilities and other commitments to lend	**1,266,640**	1,247,071	**1,270,690**	1,251,045
	1,291,225	1,269,222	**1,295,275**	1,273,196
Amounts include:				
– in favour of Group companies	**178,395**	185,194	**178,395**	185,194
– in favour of subsidiary companies	**–**	–	**4,050**	3,974

47 Capital and lease commitments

a *Capital commitments*

Capital commitments are made up of:

	2014	2013
	€000	€000
Group/Bank		
Intangible assets	**27**	152
Property, plant and equipment	**3,584**	2,733
Investment property	**84**	–
	3,695	2,885

b *Operating leases*

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

	2014	2013
	€000	€000
Group/Bank		
Less than one year	**1,035**	1,256
Between one year and five years	**671**	1,288
More than five years	**2,022**	2,080
	3,728	4,624

Lease payments recognised in profit or loss under 'General administrative expenses' amounted to €1,222,000 (2013: €1,111,000). This amount includes a payment of €78,000 (2013: €69,000) in respect of rent paid on one property which is subject to a sub-lease agreement for the same amount.

48 Dividends

	Bank			
	2014	2013	**2014**	2013
	% per share	% per share	**€000**	€000
Gross of income tax				
% per 30 cent share				
– prior year's final	**17**	26	**15,176**	23,055
– interim	**15**	33	**14,592**	29,184
	32	59	**29,768**	52,239
	Cent per share	Cent per share	**€000**	€000
Net of income tax				
cent per 30 cent share				
– prior year's final	**3.38**	5.13	**9,864**	14,986
– interim	**2.92**	6.50	**9,485**	18,970
	6.30	11.63	**19,349**	33,956

The Directors propose a final gross ordinary dividend of 2.6 cent (2013: 5.2 cent) per share. The final dividend will be payable to shareholders on the bank's register as at 23 March 2015.

48 Dividends *(continued)*

	Bank	
	2014	2013
	€000	€000
Proposed dividend		
Profit for the year	**33,617**	58,717
Available for distribution as per dividend policy	**18,489**	32,353
Less: interim dividend paid	**(9,485)**	(18,970)
Available for distribution at year end	**9,004**	13,383
Allocation to General Banking Risk Reserve (note 44)	**(3,493)**	(3,519)
Proposed final dividend	**5,511**	9,864
Issued and fully paid up shares (note 43)	**324,271**	291,840

	Cent per share	Cent per share
Proposed final dividend		
– gross of income tax per share	**2.6**	5.2
– net of income tax per share	**1.7**	3.4

49 Cash and cash equivalents

	Group		*Bank*	
	2014	2013	**2014**	2013
	€000	€000	**€000**	€000
Balances of cash and cash equivalents are analysed below:				
Cash	**31,933**	30,523	**31,933**	30,522
Balances with Central Bank of Malta (excluding reserve deposit)	**8,111**	28,863	**8,111**	28,863
Treasury Bills	**28,497**	2,000	**28,497**	2,000
Loans and advances to banks	**817,739**	499,866	**738,901**	499,751
Deposits by banks	**(58,595)**	(39,841)	**(58,595)**	(39,841)
Per Statements of Cash Flows	**827,685**	521,411	**748,847**	521,295
Adjustment to reflect balances with contractual maturity of more than three months	**105,595**	153,043	**105,595**	153,043
Per Statements of Financial Position	**933,280**	674,454	**854,442**	674,338
Analysed as follows:				
Cash and balances with Central Bank of Malta (excluding reserve deposit)	**86,537**	102,521	**86,537**	102,520
Malta Government Treasury Bills	**31,496**	48,937	**31,496**	48,937
Loans and advances to banks	**875,095**	564,790	**796,257**	564,675
Deposits by banks	**(59,848)**	(41,794)	**(59,848)**	(41,794)
	933,280	674,454	**854,442**	674,338

50 Segmental information

a *Class of business*

The local group's segments are organised into three global businesses: Retail Banking and Wealth Management, Commercial Banking and Global Banking and Markets. The global businesses reflect the way the Chief Executive Officer, as chief operating decision-maker, reviews financial information in order to make decisions about allocating resources and assessing performance. Information provided to the chief operating decision-maker is measured in accordance with IFRSs.

	Retail Banking and Wealth Management	*Commercial Banking*	*Global Banking and Markets*	*Intersegment*	*Group Total*
	2014	**2014**	**2014**	**2014**	**2014**
	€000	**€000**	**€000**	**€000**	**€000**
Group					
Net interest income					
– External	**44,980**	**61,241**	**13,941**	**–**	**120,162**
– Inter-segment	**12,602**	**(16,685)**	**4,083**	**–**	**–**
	57,582	**44,556**	**18,024**	**–**	**120,162**
Net non-interest income					
– External	**31,258**	**14,536**	**7,304**	**–**	**53,098**
– Inter-segment	**508**	**39**	**–**	**(547)**	**–**
	31,766	**14,575**	**7,304**	**(547)**	**53,098**
External employee compensation and benefits	**(35,331)**	**(13,966)**	**(2,447)**	**–**	**(51,744)**
General and administrative expenses					
– External	**(27,588)**	**(10,715)**	**(1,872)**	**–**	**(40,175)**
– Inter-segment	**(547)**	**–**	**–**	**547**	**–**
	(28,135)	**(10,715)**	**(1,872)**	**547**	**(40,175)**
External Depreciation	**(2,260)**	**(1,048)**	**(152)**	**–**	**(3,460)**
External Amortisation	**(2,075)**	**(928)**	**(89)**	**–**	**(3,092)**
External Net impairment	**(2,319)**	**(20,196)**	**(30)**	**–**	**(22,545)**
External Net provisions for liabilities and other charges	**(58)**	**(65)**	**–**	**–**	**(123)**
Profit before tax	**19,170**	**12,213**	**20,738**	**–**	**52,121**
Assets					
Segment total assets	**3,667,153**	**1,480,420**	**2,051,414**	**–**	**7,198,987**
Total Equity	**216,707**	**166,931**	**61,467**	**–**	**445,105**

50 Segmental information *(continued)*

a *Class of business (continued)*

	Retail Banking and Wealth Management	*Commercial Banking*	*Global Banking and Markets*	*Group Intersegment*	*Total*
	2013	2013	2013	2013	2013
	€000	€000	€000	€000	€000
Group					
Net interest income					
– External	42,444	66,560	15,707	–	124,711
– Inter-segment	15,731	(18,489)	2,758	–	–
	58,175	48,071	18,465	–	124,711
Net non-interest income					
– External	36,554	13,888	11,859	–	62,301
– Inter-segment	(822)	460	956	(594)	–
	35,732	14,348	12,815	(594)	62,301
External employee compensation and benefits	(32,594)	(12,669)	(3,276)	–	(48,539)
General and administrative expenses					
– External	(28,401)	(8,333)	(1,749)	–	(38,483)
– Inter-segment	(594)	–	–	594	–
	(28,995)	(8,333)	(1,749)	594	(38,483)
External Depreciation	(2,724)	(623)	(102)	–	(3,449)
External Amortisation	(1,852)	(909)	(83)	–	(2,844)
External Net impairment	(2,050)	(1,222)	–	–	(3,272)
External Net provisions for liabilities and other charges	–	52	–	–	52
Profit before tax	25,692	38,715	26,070	–	90,477
Assets					
Segment total assets	2,589,326	1,525,675	1,606,529	–	5,721,530
Total Equity	212,422	168,950	41,612	–	422,984

b *Geographical segments*

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

c *Products and services*

HSBC Bank Malta p.l.c. provides a comprehensive range of banking and related financial services to its customers. The products and services offered to customers are organised by global business.

- Retail Banking and Wealth Management ('RBWM') offers a broad range of products and services to meet the personal banking and wealth management needs of individual customers. Typically, customer offerings include personal banking products (current and savings accounts, mortgages and personal loans, credit cards, debit cards and local and international payment services) and wealth management services (insurance and investment products, global asset management services and financial planning services).
- Commercial Banking ('CMB') offers a broad range of products and services to serve the needs of our commercial customers, including small and medium sized enterprises, mid-market enterprises and corporates. These include credit and lending, international trade and receivables finance, treasury management and liquidity solutions (payments and cash management and commercial cards) and commercial insurance. We also offer our customers access to products and services offered by other global businesses, for example Global Banking & Markets ('GB&M') which include foreign exchange products, raising capital on debt and equity markets and advisory services.

50 Segmental information *(continued)*

c *Products and services (continued)*

- Global Banking and Markets ('GB&M') provides tailored financial solutions to corporate and institutional clients. The client-focused business line delivers a full range of banking capabilities including financing, advisory and transaction services, a markets business that provides services in rates, foreign exchange, money markets and securities services, and principal investment activities.

51 Related party transactions

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

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of HSBC Bank Malta p.l.c. and the local group and includes members of the Boards of Directors of HSBC Bank Malta p.l.c. and the bank's Executive Committee.

a *Transactions, arrangements and agreements involving Directors and key management personnel*

Particulars of transactions, arrangements and agreements entered into with Directors and key management personnel, connected persons and companies controlled by them:

	Balance at end of year	*Balance at end of year*
	2014	2013
	€000	€000
Loans	**676**	655
Credit card transactions	**33**	24
Guarantees	**31**	34
Commitments to lend	**404**	261

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 other key management personnel*

	2014	2013
	€000	€000
Short-term employee benefits	**2,953**	3,055
Retirement benefits	**199**	594
Share-based payments	**117**	220
	3,269	3,869

Details of Directors' fees and emoluments are stated in note 18.

51 Related party transactions *(continued)*

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 7 – Interest and similar income
Note 8 – Interest expense
Note 9 – Net fee and commission income
Note 10 – Dividend income
Note 13 – Net other operating income
Note 16 – Employee compensation and benefits
Note 22 – Derivatives
Note 25 – Loans and advances to banks
Note 26 – Loans and advances to customers
Note 30 – Investment property
Note 32 – Other assets
Note 33 – Prepayments and accrued income
Note 34 – Deposits by banks
Note 35 – Customer accounts
Note 40 – Accruals and deferred income
Note 42 – Subordinated liabilities
Note 45 – Contingent liabilities
Note 46 – Commitments

Included in Interest and similar income (refer to note 7) and in Interest expense (refer to note 8), the local group recognised interest amounting to €824,000 (2013: €976,000) and €1,000 (2013: €5,000) respectively, on advances and deposits placed with intermediate parents.

Included in Net fee and commission income (refer to note 9), the local group recognised commission amounting to €278,000 (2013: €588,000).

Furthermore, expenditure relating to transactions with HSBC Holdings plc and its subsidiaries amounting to €3,280,000 (2013: €3,885,000) for the local group and €2,932,000 (2013: €2,915,000) for the bank is included in Employee compensation and benefits and €12,768,000 (2013: €12,966,000) for the local group and €10,833,000 (2013: €11,652,000) for the bank is included within General and administrative expenses.

On 30 November 2014, a portfolio of unit-linked investment products and non-linked insurance products was transferred from HSBC Life (Europe) Limited to HSBC Life Assurance (Malta) Limited at nil consideration.

The following assets and liabilities were acquired:

	2014
	€000
Assets	
Financial assets designated at fair value	**910,205**
Loans and advances to banks	**78,658**
Other assets	**28,193**
	1,017,056
Liabilities	
Liabilities under investment contracts	**993,324**
Other liabilities	**23,732**
	1,017,056

52 Unconsolidated structured entities

HSBC Bank Malta p.l.c. has established and manages investment funds to provide customers with investment opportunities. The table below describes the types of structured entities that the local group does not consolidate but in which it holds an interest.

Type of structured entity	Nature and purpose	Interest held by the group
Investment funds	To generate fees from managing assets on behalf of third party investors.	Investments in units issued by the fund
	These vehicles are financed through the issue of units to investors.	Management fees

The local group, as fund manager, may be entitled to receive a management fee based on the assets under management. The total management fees earned during the year were €3,677,000 (2013: €3,979,000).

The carrying amounts of interests held by the local group in unconsolidated structured entities at 31 December 2014 was as follows:

	2014	2013
	€000	€000
Investment funds	**56,186**	46,100

The maximum exposure to loss is the carrying amount of the assets held.

53 Trust and custody activities

The local group provides custody services to individuals and retirement benefit plans, whereby it holds and manages assets or invests funds received in various financial instruments at the discretion of the customer. In line with Group strategy, during 2014, the bank exited from the fund administration business and has also started the process of exiting the trust business.

The local group receives fee income for providing these services. Trust assets and assets held in custody are not assets of the local group and are not recognised in the statements of financial position. The local group is not exposed to any credit risk relating to such placements, as it does not guarantee these investments.

At 31 December 2014, the total assets held by the local group on behalf of customers were €2,374,340,000 (2013: €3,476,136,000).

54 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, and the immediate parent company is HSBC Europe B.V., which are incorporated and registered in the United Kingdom and the Netherlands respectively. The registered address of both companies is 8 Canada Square, London E14 5HQ, United Kingdom. Copies of the HSBC Holdings plc Annual Review 2014, Strategic Report 2014, and Annual Report and Accounts 2014 may be obtained from its registered office or viewed on www.hsbc.com.

55 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. has elected to pay the amount of the variable contribution directly to the Scheme.

56 Accounting estimates and judgements

In addition to disclosures set out in notes 4 and 16, the Directors considered the development, selection and disclosure of the local 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 local 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)(ii)). As a result, the local 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 local group. Estimates are made as to the expected number of deaths for each of the years in which the local group is exposed to risk. The local group bases these estimates on Industry standard mortality tables that reflect recent historical mortality experience, adjusted where appropriate to reflect the local 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 local 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. Interest rate assumptions on liabilities as at reporting date are based on the euro swap rates curve. Appropriate margins were taken for bond portfolio and equities/property portfolio.

If the average future investment returns differs by +/-1% from management's estimates, the insurance liability would decrease by €6,788,000 or increase by €22,586,000. In this case there is no relief arising from reinsurance contracts held.

If the number of deaths in future years differs by +/-10% from management's estimate, the liability would increase by €1,175,000 or decrease by €1,112,000.

For long-term insurance contracts with fixed and guaranteed terms and with discretionary participation features, estimates of future deaths, investment returns and administration 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.

56 Accounting estimates and judgements *(continued)*

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 local 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 local 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 43 to 119, which comprise the statements of financial position as at 31 December 2014 and the statements of profit or loss, profit or loss and other 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 42, the directors are responsible for the preparation of financial statements that (a) give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU, and (b) are properly prepared in accordance with the provisions of the Companies Act, 1995 (Chapter 386, Laws of Malta) (the "Act"), the Banking Act, 1994 (Chapter 371, Laws of Malta), and, as regards the financial statements of the group, Article 4 of the IAS Regulation. They are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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 bank'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 2014 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 2014, 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.

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 bank 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 28 to 36.

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 bank’s corporate governance procedures or its risks and control procedures, nor on the ability of the bank to continue in operational existence.

In our opinion, the Directors’ Statement of Compliance set out on pages 28 to 36 provides the disclosures required by Listing Rule 5.97 issued by the Listing Authority of Malta.

Hilary Galea-Lauri (Partner) for and on behalf of

KPMG
Registered Auditors
Portico Building
Marina Street
Pietà PTA 9044
Malta

23 February 2015

Statements of Profit or Loss and Statements of Profit or Loss and Other Comprehensive Income: Five-Year Comparison

Group Statements of Profit or Loss

	2014	2013	2012	2011	2010
	€000	€000	€000	€000	€000
Interest receivable and similar income	**153,389**	162,106	174,637	175,962	169,012
Interest expense	**(33,227)**	(37,395)	(41,537)	(46,703)	(46,170)
Net interest income	**120,162**	124,711	133,100	129,259	122,842
Net non-interest income	**53,098**	62,301	64,576	65,606	53,346
Operating expenses	**(98,471)**	(93,315)	(96,779)	(98,200)	(87,605)
Net impairment	**(22,545)**	(3,272)	(5,115)	(8,250)	(5,496)
Net provisions for liabilities and other charges	**(123)**	52	(447)	(110)	1
Profit before tax	**52,121**	90,477	95,335	88,305	83,088
Tax expense	**(18,504)**	(31,760)	(33,733)	(30,738)	(29,327)
Profit for the year	**33,617**	58,717	61,602	57,567	53,761
Profit attributable to shareholders	**33,617**	58,717	61,602	57,567	53,761
Earnings per share	**10.4c**	18.1c	19.0c	17.8c	16.6c

Group Statements of Profit or Loss and Other Comprehensive Income

	2014	2013	2012	2011	2010
	€000	€000	€000	€000	€000
Profit for the year	**33,617**	58,717	61,602	57,567	53,761
Other comprehensive income					
Items that may be reclassified to Profit or Loss:					
Available-for-sale investments:					
– fair value gains	**13,656**	305	16,671	1,193	1,178
– fair value (gains)/losses transferred to profit or loss on disposal	**(1,719)**	(4,295)	(4,049)	2,107	369
– amounts transferred to profit or loss on impairment	**–**	–	–	4,179	198
– income taxes	**(4,178)**	1,396	(4,418)	(2,580)	(610)
	7,759	(2,594)	8,204	4,899	1,135
Items that will not be reclassified to Profit or Loss:					
Properties:					
– revaluation	**(28)**	84	(4,022)	–	2,117
– income taxes	**3**	(20)	583	–	(89)
	(25)	64	(3,439)	–	2,028
Other comprehensive income for the year, net of tax	**7,734**	(2,530)	4,765	4,899	3,163
Total comprehensive income	**41,351**	56,187	66,367	62,466	56,924

Statements of Financial Position: Five-Year Comparison

	2014	2013	2012	2011	2010
	€000	€000	€000	€000	€000
Assets					
Balances with Central Bank of Malta, Treasury Bills and cash	**118,033**	151,458	106,991	233,388	379,985
Cheques in course of collection	**10,990**	9,703	7,211	22,685	9,011
Derivatives	**13,170**	12,666	17,615	17,136	11,489
Financial assets designated at fair value	**1,421,580**	477,345	454,591	370,080	305,569
Financial investments	**1,153,884**	918,292	987,471	936,830	690,606
Loans and advances to banks	**875,095**	564,790	681,352	637,956	714,901
Loans and advances to customers	**3,273,381**	3,300,982	3,354,413	3,344,290	3,290,435
Intangible assets	**73,971**	86,618	91,210	89,011	70,655
Property, plant and equipment	**59,481**	61,491	54,872	60,113	65,487
Investment property	**16,326**	14,529	14,471	14,598	14,591
Non-current assets held for sale	**9,297**	11,783	11,240	12,978	9,674
Current tax assets	**8,833**	7,939	6,134	–	4,712
Deferred tax assets	**13,612**	12,522	11,273	14,158	10,181
Other assets	**106,604**	52,735	46,509	31,209	34,425
Prepayments and accrued income	**44,730**	38,677	41,121	40,629	38,710
Total assets	**7,198,987**	5,721,530	5,886,474	5,825,061	5,650,431
Liabilities					
Derivatives	**13,870**	12,929	17,857	17,810	12,311
Deposits by banks	**59,848**	41,794	258,611	389,170	232,790
Customer accounts	**4,867,124**	4,517,862	4,516,999	4,402,975	4,462,861
Current tax liabilities	**172**	16	24	4,287	2,603
Deferred tax liabilities	**28,244**	25,195	24,363	18,113	19,604
Liabilities under investment contracts	**1,020,594**	16,763	17,254	16,920	18,962
Liabilities under insurance contracts	**602,712**	524,999	493,254	436,672	410,461
Other liabilities	**44,103**	38,274	29,222	38,145	33,024
Accruals and deferred income	**27,514**	30,230	33,559	36,045	34,287
Provisions for liabilities and other charges	**2,417**	3,211	7,493	11,251	2,548
Subordinated liabilities	**87,284**	87,273	87,240	87,208	87,150
Total liabilities	**6,753,882**	5,298,546	5,485,876	5,458,596	5,316,601
Total equity	**445,105**	422,984	400,598	366,465	333,830
Total liabilities and equity	**7,198,987**	5,721,530	5,886,474	5,825,061	5,650,431
Memorandum items					
Contingent liabilities	**133,448**	111,852	104,569	130,763	128,947
Commitments	**1,291,225**	1,269,222	1,073,831	1,118,779	977,718

Statements of Cash Flows: Five-Year Comparison

	2014	2013	2012	2011	2010
	€000	€000	€000	€000	€000
Net cash from operating activities	**409,146**	51,339	258,354	29,772	103,151
Cash flows from investing activities					
Dividends received	**–**	21	26	785	281
Interest received from financial investments	**39,435**	30,255	41,356	34,624	25,575
Purchase of financial investments	**(413,566)**	(277,694)	(375,638)	(599,079)	(307,715)
Proceeds from sale and maturity of financial investments	**217,133**	334,396	335,059	344,079	94,246
Purchase of property, plant and equipment, investment property and intangible assets	**(5,264)**	(12,087)	(6,133)	(9,031)	(11,038)
Proceeds on sale of property, plant and equipment, intangible assets and liquidation of subsidiary company	**81**	476	502	2,094	453
Proceeds on disposal of card acquiring business	**–**	–	–	11,075	–
Net cash flows (used in)/from investing activities	**(162,181)**	75,367	(4,828)	(215,453)	(198,198)
Cash flows from financing activities					
Dividends paid	**(19,349)**	(33,956)	(32,628)	(30,162)	(30,162)
Net cash used in financing activities	**(19,349)**	(33,956)	(32,628)	(30,162)	(30,162)
Increase/(decrease) in cash and cash equivalents	**227,616**	92,750	220,898	(215,843)	(125,209)

Accounting Ratios: Five-Year Comparison

	2014	2013	2012	2011	2010
	%	%	%	%	%
Net operating income to total assets	**2.4**	3.3	3.4	3.3	3.1
Operating expenses to total assets	**1.4**	1.6	1.6	1.7	1.5
Cost efficiency ratio	**56.8**	49.9	49.0	50.4	49.7
Profit before tax to total assets	**0.7**	1.6	1.6	1.5	1.5
Profit before tax on equity	**11.7**	21.4	23.8	24.1	24.9
Profit after tax to equity	**7.7**	13.9	15.4	15.7	16.1

	2014	**2013**	2012	2011	2010
Shares in issue (millions)	**324.3**	291.8	291.8	291.8	291.8
Net assets per 30 cent share (cent)	**137.3**	130.4	123.5	113.0	102.9
Earnings per 30 cent share (cent)	**10.4**	18.1	19.0	17.8	16.6
Dividend per 30 cent share (cent)					
– gross	**9.7**	17.8	17.2	15.9	15.9
– net	**6.3**	11.6	11.2	10.3	10.3
Dividend cover	**1.7**	1.7	1.9	1.9	1.8

Financial Highlights in US dollars

	2014	2013
	US$000	US$000
Statements of Profit or Loss		
Net operating income	**210,468**	227,173
Operating expenses	**(119,618)**	(113,354)
Net impairment	**(27,387)**	(3,975)
Net provisions for liabilities and other charges	**(149)**	63
Profit before tax	**63,314**	109,907
Tax expense	**(22,478)**	(38,580)
Profit for the year	**40,836**	71,327
Profit attributable to shareholders	**40,836**	71,327
Statements of Financial Position		
Assets		
Balances with Central Bank of Malta, Treasury Bills and cash	**143,380**	183,984
Cheques in course of collection	**13,350**	11,787
Derivatives	**15,998**	15,386
Financial assets designated at fair value through profit or loss	**1,726,864**	579,855
Financial investments	**1,401,681**	1,115,495
Loans and advances to banks	**1,063,022**	686,079
Loans and advances to customers	**3,976,340**	4,009,868
Intangible assets	**89,856**	105,219
Property, plant and equipment	**72,225**	74,696
Investment property	**19,832**	17,649
Non-current assets held for sale	**11,293**	14,313
Current tax assets	**10,730**	9,644
Deferred tax assets	**16,535**	15,211
Other assets	**129,497**	64,060
Prepayments and accrued income	**54,336**	46,983
Total assets	**8,744,969**	6,950,229
Liabilities and equity		
Derivatives	**16,849**	15,705
Deposits by banks	**72,700**	50,769
Customer accounts	**5,912,339**	5,488,073
Current tax liabilities	**209**	19
Deferred tax liabilities	**34,309**	30,606
Liabilities under investment contracts	**1,239,767**	20,363
Liabilities under insurance contracts	**732,144**	637,743
Other liabilities	**53,574**	46,493
Accruals and deferred income	**33,423**	36,722
Provisions for liabilities and other charges	**2,936**	3,901
Subordinated liabilities	**106,028**	106,015
Called up share capital	**118,172**	106,354
Revaluation reserve	**51,639**	42,646
Retained earnings	**370,880**	364,820
Total liabilities and equity	**8,744,969**	6,950,229

The US Dollar Exchange as at 31 December 2014 was €1 = US$1.21475. 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 Operations
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

Inheritance Unit
80 Mill Street, Qormi QRM 3101
Tel: 2380 3360/1/2/3/4
Fax: 2380 5190

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

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

Birkirkara
1 Naxxar Road BKR 9049
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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
Żabbar Road FGR 1254
Tel: 2380 2380 Fax: 2361 8790

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

Ħamrun
121 St Joseph Road HMR 1017
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Marsascala
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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 *(Agency)*
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Humanities Building MSD 2080
Tel: 2380 2380 Fax: 2133 1377

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12 Antoine De Paule Square PLA 1261
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Qormi
38 St Sebastian Street QRM 2331
Tel: 2380 2380 Fax: 2380 5490

Rabat
12 Saqqajja Square RBT 1190
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San Ġwann
198 Naxxar Road SGN 9030
Tel: 2380 2380 Fax: 2324 7590

St Julian's
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

Swieqi
St Andrew's 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

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

SUBSIDIARY COMPANIES

HSBC Global Asset Management (Malta) Limited
Operations Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 5128 Fax: 2380 5191

HSBC Life Assurance (Malta) Limited
Business Banking Centre
80 Mill Street Qormi QRM 3101
Tel: 2380 8699 Fax: 2380 8690

HSBC Securities Services (Malta) Limited
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

HSBC Stockbrokers (Malta) Limited
Business Banking Centre
80 Mill Street Qormi QRM 3101
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