ANCORIA BANK

banking redefined

ANNUAL FINANCIAL REPORT 2017

Contents

Board of Directors

Martin Eduard Philip Schenk (Chairman)
Charalambos Panayiotou (Vice Chairman)
Bo Sievert Larsson (Non-executive)
Charidemos Theocharides (Non-executive)
Odysseas Christodoulou (Non-executive) – resigned 6 June 2017
Athena Papadopoulou (Non-executive)
Evan Gavas (Non-executive) – appointed 8 March 2017
Marios Clerides (Non-executive) – appointed 11 April 2017
Evgenia Christodoulou (Executive)
Ioannis Loizou (Executive)

Secretary

Christos Papoutsas

Chief Executive Officer

Ioannis Loizou

Chief Financial Officer

Savvas Pashias

Registered Office

12 Demostheni Severi
1st floor
1080 Nicosia
Cyprus

Legal Advisors

Chryssafinis & Polyviou LLC

Independent Auditors

Deloitte Limited

Tax Advisors

KPMG Limited

The Board of Directors of Ancoria Bank Limited (the ‘Company’ or the ‘Bank’) submits to the shareholders its Management Report and the audited financial statements for the year ended 31 December 2017.

Incorporation

The Company was incorporated in Cyprus on 20 August 2013 as a limited liability company under the Cyprus Companies Law, Cap.113.

On 24 November 2014, the Company passed a special resolution to change its name from “Ancoria Holdings Limited” to “Ancoria Bank Limited”. The name change was approved by the Registrar of Companies on 30 April 2015.

Principal activity

The principal activity of the Company is the provision of banking services.

On 14 October 2013, the Company filed an application with the Central Bank of Cyprus for a banking licence to enable the Company to operate as a Credit Institution under the Business of Credit Institutions Laws of 1997 and all amendments thereafter.

On 3 November 2014, the banking licence was granted by the Central Bank of Cyprus, subject to certain conditions that needed to be fulfilled prior to the commencement of any banking operations. These conditions have been fulfilled during 2015, and the Company begun operations as a Credit Institution during the last quarter of 2015.

Operating environment of the Bank and future developments

The Board of Directors recognises the difficulties involved in predicting all developments which could have an impact on the Cyprus economy and consequently, what effect, if any, they could have on the future financial performance, cash flows and financial position of the Bank. The Board of Directors will closely monitor all future developments in the economic and political environment it operates and take appropriate measures.

Detailed information about the operating environment is set out in Note 32 to the financial statements.

Board of Directors

The members of the Company's Board of Directors as at 31 December 2017 and as of the date of this report are presented on page 2.

Other than the appointments of Messrs Evan Gavas and Marios Clerides and the resignation of Mr Odysseas Christodoulou, there were no significant changes in the composition, distribution of responsibilities or compensation of the Board of Directors during the year ended 31 December 2017.

In accordance with the Company's Articles of Association, all directors presently members of the Board continue in office.

Financial Results

The Bank's results for the year are set out on page 6.

The main financial highlights of the Bank for year 2017 are as follows:

	2017	2016
	€	€
Profit or Loss		
Net interest income	**832.845**	6.948
Operating income	**966.781**	28.342
Loss before provisions for impairment	**(5.355.605)**	(5.368.936)
Provisions for impairment of loans and advances and other credit facilities	**(312.568)**	(66.580)
Loss for the year before tax	**(5.668.173)**	(5.435.516)
Loss for the year after tax	**(5.668.201)**	(5.435.516)
Loss per ordinary share in issue (€)[1]	**56,12**	53,82

	2017	2016
	€	€
Key Financial Position figures and ratios		
Customer deposits	**59.609.942**	37.521.835
Loans and advances to customers (gross)	**63.586.819**	24.666.415
Loans and advances to customers (net)	**63.278.220**	24.599.835
Net loans to deposits ratio	**106%**	66%
Loans in arrears over 90 days	**-**	-
Common Equity Tier 1 Capital ratio	**82,9%**	188,4%
Total Capital ratio	**82,9%**	188,7%
Risk weighted assets	**41.944.258**	21.187.693

Dividends

In 2017, no dividends were paid or declared by the Bank (2016: €nil).

Business Centres

The Bank operates through three business centres located in Nicosia, Limassol and Larnaca.

[1] Loss per ordinary share is calculated by dividing the loss for the year after tax by the weighted average number of ordinary shares outstanding during the period.

Information relating to share capital

Authorised capital

Under its Memorandum, the Company fixed its authorised share capital at 1.000 ordinary shares of nominal value of €1 each. On 15 December 2014, the Company increased its authorised capital to 201.000 ordinary shares of nominal value of €1 each.

Issued capital

Upon incorporation on 20 August 2013, the Company issued to the subscribers of its Memorandum of Association 1.000 ordinary shares of €1 each at par.

On 15 December 2014, the Company issued 50.000 additional ordinary shares of €1 each, at a premium of €499 each. On 29 December 2014, the Company issued 38.493 additional ordinary shares of €1 each, at a premium of €499 each.

On 24 July 2015, the Bank issued 11.507 additional ordinary shares of €1 each, at a premium of €499 each.

As at 31 December 2017, the issued share capital of the Bank amounted to €50 million, through contributions from its immediate parent company. This threshold was a prerequisite for the validity of the banking licence.

There are no restrictions on the transfer of the Bank's ordinary shares other than the provisions of the Bank's Articles of Association and the Banking Law of Cyprus which requires the approval of the Central Bank of Cyprus prior to the acquiring of shares of the Bank in excess of certain thresholds.

Risk management

The Bank considers risk management to be a major process and a significant factor contributing towards the safeguarding of a stable return to its shareholders. The financial risks that the Bank is exposed to are mainly credit risk, operational risk, market risk and liquidity risk. Detailed information relating to risk management is set out in Note 29 to the financial statements.

Events after the reporting date

Any significant events that occurred after the reporting date are described in Note 34 to the financial statements.

Independent auditors

The independent auditors of the Bank, Deloitte Limited, have expressed their willingness to continue in office. A resolution for the election of the Bank's independent auditors and their remuneration will be proposed at the shareholders' Annual General Meeting.

By order of the Board of Directors

Christos Papoutsas
Secretary

24 April 2018

Statement of Profit or Loss and Other Comprehensive Income
for the year ended 31 December 2017

	Note	**2017 €**	2016 €
Interest income	*4*	**1.092.878**	205.921
Interest expense	*5*	**(260.033)**	(198.973)
Net interest income		**832.845**	6.948
Fee and commission income		**195.331**	51.678
Fee and commission expense		**(70.295)**	(51.508)
Net foreign exchange (losses) / gains		**(7.847)**	7.424
Other income		**16.747**	13.800
Operating income		**966.781**	28.342
Staff costs	*6*	**(2.940.868)**	(2.484.604)
Depreciation and amortisation of property, equipment and intangible assets	*17,18*	**(1.070.142)**	(939.749)
Other operating expenses	*7*	**(2.311.376)**	(1.972.925)
Loss before provisions for impairment		**(5.355.605)**	(5.368.936)
Provisions for impairment of loans and advances and other credit facilities	*8*	**(312.568)**	(66.580)
Loss before tax	*9*	**(5.668.173)**	(5.435.516)
Income tax	*10*	**(28)**	-
Loss for the year		**(5.668.201)**	(5.435.516)
Other comprehensive income			
Items that may subsequently be reclassified to profit or loss			
Profit / (loss) on revaluation of investments available-for-sale		**17.364**	(172)
Total comprehensive loss for the year		**(5.650.837)**	(5.435.688)

Statement of Financial Position
as at 31 December 2017

	Note	**2017** €	2016 €
ASSETS			
Cash and balances with Central Bank	*11*	**20.164.025**	34.798.717
Placements with banks	*12*	**2.615.172**	5.687.390
Loans and advances to customers	*13*	**63.278.220**	24.599.835
Investments available-for-sale	*14*	**2.212.743**	302.807
Investments held-to-maturity	*15*	**4.229.770**	8.398.240
Other assets	*16*	**1.424.749**	1.197.917
Property and equipment	*17*	**5.007.477**	3.121.056
Intangible assets	*18*	**886.146**	1.286.111
Total assets		**99.818.302**	79.392.073
LIABILITIES			
Customer deposits	*19*	**59.609.942**	37.521.835
Other borrowings	*20*	**3.004.737**	-
Other liabilities	*21*	**1.648.469**	664.247
Total liabilities		**64.263.148**	38.186.082
EQUITY			
Share capital	*22*	**101.000**	101.000
Share premium	*22*	**49.900.000**	49.900.000
Revaluation reserve	*23*	**17.192**	(172)
Accumulated losses	*24*	**(14.463.038)**	(8.794.837)
Total equity		**35.555.154**	41.205.991
Total liabilities and equity		**99.818.302**	79.392.073

On 24 April 2018, the Board of Directors of Ancoria Bank Limited authorised these financial statements for issue.

Charalambos Panayiotou
Vice Chairman of the Board ………………………………………………

Ioannis Loizou
Member of the Board and Chief Executive Officer ………………………………………………

Evgenia Christodoulou
Member of the Board and Deputy Chief Executive Officer ………………………………………………

Savvas Pashias
Chief Financial Officer ………………………………………………

Statement of Changes in Equity
for the year ended 31 December 2017

	Share capital *(Note 22)*	Share premium *(Note 22)*	Revaluation reserve *(Note 23)*	Accumulated losses *(Note 24)*	Total
	€	**€**	**€**	**€**	**€**
Balance at 1 January 2017	101.000	49.900.000	(172)	(8.794.837)	41.205.991
Comprehensive income					
Loss for the year	-	-	-	(5.668.201)	(5.668.201)
Other comprehensive profit for the year	-	-	17.364	-	17.364
Total comprehensive loss for the year	-	-	17.364	(5.668.201)	(5.650.837)
Balance as at 31 December 2017	**101.000**	**49.900.000**	**17.192**	**(14.463.038)**	**35.555.154**
Balance at 1 January 2016	101.000	49.900.000	-	(3.359.321)	46.641.679
Comprehensive income					
Loss for the year	-	-	-	(5.435.516)	(5.435.516)
Other comprehensive loss for the year	-	-	(172)	-	(172)
Total comprehensive loss for the year	-	-	(172)	(5.435.516)	(5.435.688)
Balance at 31 December 2016	**101.000**	**49.900.000**	**(172)**	**(8.794.837)**	**41.205.991**

Share premium is not available for distribution.

Statement of Cash Flows

for the year ended 31 December 2017

	Note	2017 €	2016 €
Net cash flow (used in) / from operating activities	*27*	**(17.350.197)**	3.228.536
Cash flow from investing activities			
Purchase of property, equipment and intangible assets	*17,18*	**(2.556.599)**	(1.170.215)
Purchase of held-to-maturity investments		**(18.408.454)**	(21.322.785)
Redemption of held-to maturity investments		**22.500.000**	16.000.000
Purchase of available-for-sale investments		**(1.891.660)**	(302.850)
Net cash flow used in investing activities		**(356.713)**	(6.795.850)
Net decrease in cash and cash equivalents		**(17.706.910)**	(3.567.314)
Cash and cash equivalents			
At 1 January		**40.486.107**	44.053.421
Net decrease in cash and cash equivalents		**(17.706.910)**	(3.567.314)
At 31 December	*28*	**22.779.197**	40.486.107

Significant non-cash transactions are disclosed in the notes to the financial statements.

1. Corporate information

The financial statements of Ancoria Bank Limited (the ‘Company’, or the ‘Bank’) for the year ended 31 December 2017 were authorised for issue in accordance with a resolution of the Board of Directors on 24 April 2017.

The Bank, which commenced operations in 2015, provides banking services in Cyprus. Its registered office is at 12 Demostheni Severi, 1st floor, 1080 Nicosia, Cyprus.

The Bank was incorporated in Cyprus on 20 August 2013 as a limited liability company under the Cyprus Companies Law, Cap.113.

On 14 October 2013, the Company filed an application with the Central Bank of Cyprus (‘CBC’) for a banking licence to enable the Company to operate as a Credit Institution under the Business of Credit Institutions Laws of 1997 and all amendments thereafter including No.4 of 2013.

On 3 November 2014, the banking licence was granted by the CBC subject to certain conditions that needed to be fulfilled prior to the commencement of any banking operations. These conditions were fulfilled during 2015 and the Company started its operations as a Credit Institution during the last quarter of the year.

On 24 November 2014, the Company passed a special resolution to change its name from ‘Ancoria Holdings Limited’ to ‘Ancoria Bank Limited’. The name change was approved by the Registrar of Companies on 30 April 2015.

The Company is a wholly owned subsidiary of Ancoria Investments Plc which is registered in Cyprus, and which prepares consolidated financial statements including the results, position and cash flows of the Company.

2. Significant accounting policies

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

2.1. Basis of preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (‘IFRSs’), as adopted by the European Union (‘EU’), and the requirements of the Cyprus Companies Law, Cap.113.

The financial statements are presented in Euro (€) and have been prepared under the historical cost convention, except as disclosed in the accounting policies below.

The Bank presents its statement of financial position in order of liquidity. An analysis regarding the expected recovery or settlement of any asset and liability within 12 months after the reporting date and more than 12 months after the reporting date is presented in Note 25.

The preparation of financial statements in conformity with IFRSs requires the use of certain critical accounting estimates and requires management to exercise its judgment in the process of applying the Bank's accounting policies. It also requires the use of assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of current events and actions, actual results may ultimately differ from those estimates.

2. Significant accounting policies (continued)

2.2. Adoption of new and revised IFRSs

In the current year, the Bank has adopted all the new and revised IFRSs that are relevant to its operations and are effective for accounting periods beginning on or after 1 January 2017. The adoption of these Standards did not have a material effect on the accounting policies of the Bank.

Standard / Interpretation	**Effective for annual periods beginning on or after**
Amendments to IAS 12 *Recognition of Deferred Tax Assets for Unrealised Losses*	1 January 2017
Amendments to IAS 7 *Disclosure Initiative*	1 January 2017
Annual Improvements to IFRS Standards 2014-2016 Cycle	1 January 2017

2.3. Standards, Interpretations and Amendments that are issued but not yet effective

Up to the date of approval of these financial statements, the following standards have been published by the International Accounting Standards Board ('IASB') but were not yet effective:

a) <u>Adopted by the EU</u>

Standard / Interpretation	**Effective for annual periods beginning on or after**
IFRS 15 *Revenue from Contracts with Customers*	1 January 2018
IFRS 9 *Financial Instruments*	1 January 2018
Clarification to IFRS 15 *Revenue from Contracts with Customers*	1 January 2018
Amendments to IFRS 4 *Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts*	1 January 2018
Annual Improvements to IFRS Standards 2014-2016 Cycle	1 January 2018
Amendments to IFRS 2 *Classification and Measurement of Share-based Payment Transactions*	1 January 2018
Amendments to IAS 40 *Transfers of Investment Property*	1 January 2018
IFRIC Interpretation 22 *Foreign Currency Transactions and Advance Consideration*	1 January 2018
IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments*	1 January 2019
IFRS 16 *Leases*	1 January 2019

b) <u>Not yet adopted by the EU</u>

Standard / Interpretation	**Effective for annual periods beginning on or after**
Amendments to IFRS 10 and IAS 28 *Sale or Contribution of Assets between an Investor and its Associate or Joint Venture*	Deferred indefinitely
Amendments to IFRS 9 *Prepayment Features with Negative Compensation*	1 January 2019

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

b) Not yet adopted by the EU (continued)

Standard / Interpretation	Effective for annual periods beginning on or after
Amendments to IAS 28 *Long-term Interests in Associates and Joint Ventures*	1 January 2019
Annual Improvements to IFRS Standards 2015-2017 Cycle	1 January 2019
Amendments to IAS 19 *Plan Amendment, Curtailment or Settlement*	1 January 2019
Amendments to References to the Conceptual Framework in IFRS Standards	1 January 2020
IFRS 17 *Insurance Contracts*	1 January 2021

The Bank is in the process of evaluating the effect that the adoption of the above standards will have on the financial statements of the Bank, and it does not intend to early adopt any of them. The Bank expects that the most significant impact will result from the below new standards that have been issued but are not yet effective:

- **IFRS 9 *Financial Instruments***

  IFRS 9 (as revised in 2014) will supersede IAS 39 *Financial Instruments: Recognition and Measurement* in its entirety. The completed IFRS 9 contains the requirements for a) classification and measurement of financial assets and financial liabilities, b) impairment methodology, and c) general hedge accounting.

- **IFRS 15 *Revenue from Contracts with Customers***

  IFRS 15 establishes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. Its core principle is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. IFRS 15 includes far more prescriptive guidance to deal with for specific scenarios and requires extensive disclosures in the financial statements.

- **IFRS 16 *Leases***

  IFRS 16 specifies how an IFRS reporter entity will recognise, measure, present and disclose leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. Lessors continue to classify leases as operating or finance, with IFRS 16's approach to lessor accounting substantially unchanged from its predecessor, IAS 17.

2.3.1. IFRS 9 framework and disclosures

Classification and measurement

From a classification and measurement perspective, the new standard will require all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories will be replaced by: fair value through profit or loss ('FVPL'), fair value through other comprehensive income ('FVOCI') and amortised cost. IFRS 9 will also allow entities to continue to irrevocably designate instruments that qualify for amortised cost or fair value through OCI instruments as FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Equity instruments that are not held for trading may be irrevocably designated as FVOCI, with no subsequent reclassification of gains or losses to the profit or loss.

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

2.3.1. IFRS 9 framework and disclosures (continued)

The accounting for financial liabilities will largely be the same as the requirements of IAS 39, except for the treatment of gains or losses arising from an entity's own credit risk relating to liabilities designated at FVPL. Such movements will be presented in OCI with no subsequent reclassification to profit or loss, unless an accounting mismatch in profit or loss would arise.

Having completed its initial assessment, the Bank has concluded that:

- Loans and advances to customers that are classified as loans and receivables under IAS 39 are expected to be measured at amortised cost under IFRS 9.
- Debt securities classified as available-for-sale under IAS 39 are expected to be measured at amortised cost or FVOCI. Some securities, might be classified as FVPL, either because of their contractual cash flow characteristics or the business model within which they are held.
- Debt securities classified as held to maturity are expected to continue to be measured at amortised cost.

Impairment of financial assets

IFRS 9 will also fundamentally change the loan loss impairment methodology. The standard will replace IAS 39's incurred loss approach with a forward-looking expected credit loss ('ECL') approach. The Bank will be required to record an allowance for expected losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination or the asset is considered credit-impaired or defaulted, in which case, the allowance is based on the probability of default over the life of the asset.

The Bank has established a policy to perform an assessment at the end of each reporting period of whether credit risk has increased significantly since initial recognition by considering the change in the risk of default occurring over the remaining life of the financial instrument.

To calculate lifetime ECL, the Bank will estimate the risk of a default occurring on the financial instrument during its remaining life. ECLs are estimated based on the present value of all cash shortfalls over the remaining expected life of the financial asset, i.e., the difference between the contractual cash flows that are due to the Bank under the contract and the cash flows that the Bank expects to receive, both discounted at the effective interest rate of the loan.

In comparison to IAS 39, the Bank expects the impairment charge under IFRS 9 to be more volatile than under IAS 39 due to the potential interchanges between stages throughout the lifetime of the facilities.

The Bank groups its loans into Stage 1, Stage 2 and Stage 3, based on the applied impairment methodology, as described below:

- **Stage 1 – Performing loans**: on initial recognition, the Bank recognises an allowance based on 12-month expected credit losses. Loans considered as of low credit risk and for which there was no significant increase in credit risk continue to be classified under Stage 1.
- **Stage 2 – Underperforming loans**: when a loan shows a significant increase in credit risk, the Bank records an allowance for the lifetime expected credit loss. A rebuttable assumption of 30 days past due holds (i.e. if a loan exceeds 30 days past due, it will remain under Stage 2).
- **Stage 3 – Impaired loans**: the Bank recognises the lifetime expected credit losses for these loans. For defaulted loans, the definition of default is in accordance with the relevant definition of the European Banking Authority ('EBA'). A rebuttable assumption of 90 days past due holds (i.e. if a loan exceeds 90 days past due it will remain under Stage 3). In addition, the Bank accrues interest income on the amortised cost of the loan net of allowances.

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

2.3.1. IFRS 9 framework and disclosures (continued)

The Bank will record impairment for FVOCI debt securities, depending on whether they are classified as Stage 1, 2, or 3, as explained above. However, the expected credit losses will not reduce the carrying amount of these financial assets in the statement of financial position, which will remain at fair value. Instead, an amount equal to the allowance that would arise if the asset were measured at amortised cost will be recognised in OCI as an accumulated impairment amount, with a corresponding charge to profit or loss.

For 'low risk' FVOCI debt securities, the Bank intends to apply a policy which assumes that the credit risk on the instrument has not increased significantly since initial recognition and will calculate ECL as explained in Stage 1 below. Such instruments will generally include traded, investment grade securities where the borrower has a strong capacity to meet its contractual cash flow obligations in the near term and adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil its contractual cash flow obligations. The Bank will not consider instruments to have low credit risk simply because of the value of collateral. Financial instruments are also not considered to have low credit risk simply because they have a lower risk of default than the Bank's other financial instruments.

<u>Stage 1</u>

Under IAS 39 the Bank has been recording an allowance for Incurred But Not Reported (IBNR) impairment losses. These are designed to reflect impairment losses that had been incurred in the performing portfolio but have not been identified. Under IFRS 9, the impairment of financial assets that are not considered to have suffered a significant increase in their credit risk will be measured on a 12-month ECL basis.

The estimation of ECL should be unbiased and probability weighted, taking into account all reasonable and supportable information, including forward looking economic assumptions and a range of possible outcomes. IFRS 9 has the effect of bringing forward recognition of impairment losses relative to IAS 39 which requires provisions to be recognised only when there is objective evidence of credit impairment.

Stage 1 impairment allowance is not considered to differ in comparison with IAS 39 as both apply a the 12-month ECL model. However, the introduction of changes in certain methodology parameters due to market observations, such as the assumed liquidation period of immovable property and credit conversion factors, will have both negative and positive impact on impairment allowances with an overall net decrease as exhibited in the table below.

For revolving facilities, the Bank measures 12-month ECL taking into account that such facilities are reviewed on an annual basis and, based on this review, adjustments in exposure amounts may take place. For financial guarantee contracts, a credit conversion factor in accordance with Capital Requirement Regulation ('CRR') 575/2013 / Capital Requirement Directive IV ('CRD IV') classification is applied to determine exposure at default when estimating ECLs.

<u>Stage 2</u>

IFRS 9 requires financial assets to be classified in Stage 2 when their credit risk has increased significantly since their initial recognition. For these assets, a loss allowance needs to be recognised based on their lifetime ECLs. Since this is a new concept compared to IAS 39, it will result in increased allowance as most such assets are not considered to be credit-impaired under IAS 39. If the new standard were applied as at 2017, this would result in an increase in the impairment allowance.

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

2.3.1. IFRS 9 framework and disclosures (continued)

The Bank considers whether there has been a significant increase in credit risk of an asset by comparing the probability of default upon initial recognition of the asset against the risk of a default occurring on the asset as at the end of each reporting period. In each case, this assessment is based on forward-looking assessment that takes into account a number of economic scenarios, in order to recognise the probability of higher losses associated with more negative economic outlooks.

In addition, a significant increase in credit risk is assumed if the borrower falls more than 30 days past due in making its contractual payments, or if the Bank expects to grant the borrower forbearance, or the facility is placed on the Bank's watch list. It is the Bank's policy to evaluate additional available reasonable and supportive forwarding-looking information as further additional drivers.

When estimating lifetime ECLs for undrawn loan commitments, the Bank will:

- Estimate the expected portion of the loan commitment that will be drawn down over the expected life of the loan commitment in accordance with the loan commitment's contractual arrangements, and
- Calculate the present value of cash shortfalls between the contractual cash flows that are due to the entity if the holder of the loan commitment draws down that expected portion of the loan and the cash flows that the entity expects to receive if that expected portion of the loan is drawn down.

For revolving facilities, the Bank measures 12-month ECL taking into account that such facilities are reviewed on an annual basis and, based on this review, adjustments in exposure amounts may take place. For financial guarantee contracts, a credit conversion factor in accordance with Capital Requirement Regulation ('CRR') 575/2013 / Capital Requirement Directive IV ('CRD IV') classification is applied to determine exposure at default when estimating ECLs.

<u>Stage 3</u>

Financial assets will be included in Stage 3 when there is objective evidence that the asset is credit-impaired or defaulted. The criteria of such objective evidence are the same as under the current IAS 39 methodology and the definition of default is in accordance with the relevant definition of EBA.

Loans in Stage 3, where the Bank calculated the IAS 39 impairment on an individual basis will continue to be calculated on the same basis, but collateral values will be adjusted to reflect the amounts that can be expected to be realised, giving consideration to the possibility that these will be lower in more adverse macroeconomic scenarios. The impairment calculation will be the same as for Stage 2 loans with the probability of default set to 100%.

When forbearance results in the derecognition of the original loan, the new loan will be classified as originated credit-impaired. Other than originated credit-impaired loans, loans will be transferred from out of Stage 3 if they no longer meet the criteria of credit-impaired.

<u>Forward-looking information</u>

The Bank will incorporate forward-looking information in the measurement of ECLs.

The Bank considers forward-looking information such as macroeconomic factors (e.g., unemployment, GDP growth, house prices) and economic forecasts. To evaluate a range of possible outcomes, the Bank intends to formulate three scenarios: a base case, a pessimistic case and an optimistic case. The base case scenario represents the more likely outcome resulting from the Bank's normal financial planning and budgeting process. Since the effort is to provide plausible scenarios, the optimistic and pessimistic scenarios represent slight variations of the base case. For each scenario, the Bank will derive an ECL and apply a probability weighted approach to determine the impairment allowance.

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

2.3.1. IFRS 9 framework and disclosures (continued)

The Bank will use published external information from government and private economic forecasting services to maintain independent input of information and assume cyclicality for the remaining maturity where forecasts are not available.

Limitation of estimation techniques

The models applied by the Bank may not always capture all characteristics of the market at a point in time as they cannot be recalibrated at the same pace as changes in market conditions. Interim adjustments are expected to need to be made until the base models are updated. Although the Bank will use latest available data wherever possible and available, models used to calculate ECLs may also include data that are not as current, for which adjustments will be made for significant events occurring prior to the reporting date.

Impact of IFRS 9

The Bank's loan portfolio has a short history of two years, based on which approximately 50% of the portfolio originated within 2017 with insignificant amounts in arrears and a distribution skewed towards lower risk bands. In addition, all but one debt investments are considered to be classified as investment grade with no significant changes in their overall risk profile since inception. Consequently, the implementation of IFRS 9 results in all debt investments being classified under Stage 1 and an insignificant percentage of assets being classified under Stage 2.

Impairment allowances on loans and advances calculated under Stage 2 are due to such loans and advances belonging in higher risk bands than the average portfolio and not a result of arrears. In transitioning to IFRS 9, the Bank has made enhancements to its impairment calculation methodology and respective parameters regarding years of liquidation for immovable property, cure rates, probabilities of default and Credit Conversion Factors ('CCFs'). For certain exposures, this has a transitional positive effect which may not have been incurred had these enhancements not been adopted. Loans and advances under Stage 2 have recorded an increase in impairment allowances compared to the respective ones under IAS 39.

The reconciliation of the net carrying value of loans and advances to customers, financial guarantees and commitments and debt investments all measured at amortised cost, as well as, debt investments measured at FVOCI under IAS 39 with their respective net carrying value after ECL remeasurement under IFRS 9 is disclosed below:

	Per IAS 39 31 December 2017	**ECL remeasurement**	**Per IFRS 9 1 January 2018**
Carrying value	**€**	**€**	**€**
Loans and advances to customers	63.278.220	(15.635)	63.262.585
Financial guarantees and loan commitments	20.610.351	28.172	20.638.523
Investments measured at amortised cost	4.229.770	(15.111)	4.214.659
Investments measured at FVOCI	2.212.743	(198)	2.212.545
	90.331.084	**(2.772)**	**90.328.312**

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

2.3.1. IFRS 9 framework and disclosures (continued)

The table below provides the analysis of the net carrying value under IFRS 9 as per above by stage as at 1 January 2018.

	€
Stage 1	89.312.776
Stage 2	1.015.536
Stage 3	-
	90.328.312

Further analysis on the impact of IFRS 9 implementation as at 1 January 2018 is disclosed below:

Loans and advances to customers

	Stage 1 12-month ECL		Stage 2 Lifetime ECL		Total		
	Gross value €	Allowances €	Gross value €	Allowances €	Gross value €	Allowances €	Carrying value €
Retail	46.689.550	(70.255)	412.320	(20.479)	47.101.870	(90.734)	47.011.918
Business	15.968.331	(207.791)	516.618	(25.709)	16.484.949	(233.500)	16.250.667
	62.657.881	**(278.046)**	**928.938**	**(46.188)**	**63.586.819**	**(324.234)**	**63.262.585**

Financial guarantees and loan commitments

	Stage 1 12-month ECL		Stage 2 Lifetime ECL		Total		
	Gross value €	Allowances €	Gross value €	Allowances €	Gross value €	Allowances €	Carrying value €
Retail	11.935.801	(12.892)	20.000	(616)	11.955.801	(13.508)	11.942.293
Business	8.610.550	(27.722)	114.549	(1.147)	8.725.099	(28.869)	8.696.230
	20.546.351	**(40.614)**	**134.549**	**(1.763)**	**20.680.900**	**(42.377)**	**20.638.523**

Investments

	Stage 1 12-month ECL		Stage 2 Lifetime ECL		Total		
	Gross value €	Allowances €	Gross value €	Allowances €	Gross value €	Allowances €	Carrying value €
At amortised cost	4.229.770	(15.111)	-	-	4.229.770	(15.111)	4.214.659
At FVOCI	2.212.743	(198)	-	-	2.212.743	(198)	2.212.545
	6.442.513	**(15.310)**	**-**	**-**	**6.442.513**	**(15.310)**	**6.427.204**
Total	**89.646.745**	**(333.970)**	**1.063.487**	**(47.951)**	**90.710.232**	**(381.921)**	**90.328.312**

2. Significant accounting policies (continued)

2.3. Standards, Interpretations and Amendments that are issued but not yet effective (continued)

2.3.1. IFRS 9 framework and disclosures (continued)

Capital management and transitional arrangements

The Bank uses the Standardised Approach for the capital treatment of credit risk as per the CRR. As a result and in accordance with EBA's opinion on transitional arrangements and credit risk adjustments due to the introduction of IFRS 9 (EBA/OP/2017/02), all provision amounts are considered as Specific Credit Risk Adjustments and therefore none qualifies as Tier 2 capital.

In accordance with EU transitional arrangements for regulatory capital purposes (EU Regulation 2017/2395), the Bank has the option to recognise the impact of the impairment amount from the initial application of IFRS 9 on the capital ratios under a gradual phase-in process over a five year period. Given the estimated minimal impact of IFRS 9 implementation on the Bank's regulatory capital, the Bank has elected not to apply this option.

Governance

The approval of provisions for impairment both in terms of methodology and calculations falls under the responsibility of the Board of Directors. The Risk Management Function is responsible for performing impairment calculations as per approved policies and methodologies by the Board of Directors, while recommendation for approval to the Board of Directors is provided by the Asset and Liability Committee.

2.4. Turnover

Turnover consists of interest income, fee and commission income, foreign exchange gains and other income.

2.5. Revenue recognition

Revenue is recognised when it is probable that future economic benefits will flow to the Bank and these can be reliably measured.

2.5.1. Interest income

For all financial assets measured at amortised cost and interest-bearing financial assets classified as available-for-sale investments or at fair value through profit or loss, interest income is recognised on an accruals basis using the effective interest rate method.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instruments, or where appropriate a shorter period, to the carrying amount of the financial instruments. When calculating the effective interest rate, the Bank shall estimate cash flows considering all contractual terms of the financial instrument (e.g. prepayment, call option, etc.) but shall not consider future credit losses. The calculation includes all fees that are an integral part to the contract, incremental transaction costs and all premiums or discounts.

Interest income is recognised on the recoverable portion of impaired loans applying the rate of interest used to discount the future cash flows for measuring the impairment loss.

The carrying amount of a financial asset or liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded in profit or loss.

2.5.2. Fee and commission income

Fee and commission income is generally recognised on the basis of work done so as to match the cost of providing the service, whereas fees and commissions in respect of loans and advances are recognised using the effective interest rate method as part of interest income.

2. Significant accounting policies (continued)

2.5.3. Dividend income

Dividend income is recognised in profit or loss when the right to receive payment is established.

2.6. Foreign currency translation

The functional and presentation currency of the Bank is the Euro (€).

Transactions in foreign currencies are recorded using the functional currency rate of exchange presiding at the date of each transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange presiding at the reporting date. All differences are recognised in profit or loss.

Non-monetary items that are measured at historic cost in a foreign currency are translated using the exchange rates presiding at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates presiding at the date when the fair value is determined.

2.7. Tax

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. Current tax also includes withholding tax on dividends.

Tax on income is provided in accordance with the fiscal regulations and rates applicable at every reporting date and is recognised as an expense in the period in which the income arises.

Deferred tax is provided using the liability method. Current income tax and deferred tax relating to items recognised directly in equity is recognised directly in equity.

Deferred tax liabilities are recognised for all taxable temporary differences between the tax basis of assets and liabilities and their carrying amounts at the reporting date, which will give rise to taxable amounts in future periods.

Deferred tax assets are recognised for all deductible temporary differences and carry-forward of unutilised tax losses to the extent that it is probable that taxable profit will be available, against which the deductible temporary differences and carry-forward of unutilised tax losses can be utilised. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to utilise all or part of the deductible temporary differences or tax losses. Unrecognised deferred tax assets are reassessed at each reporting date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the amount that is expected to be paid to or recovered from the tax authorities, after taking into account the tax rates and legislation that have been enacted or substantially enacted by the reporting date.

Current and deferred tax assets and liabilities are offset when they arise from the same tax reporting entity and relate to the same tax authority and when the legal right to offset exists.

2. Significant accounting policies (continued)

2.8. Financial Instruments

2.8.1. Initial recognition and measurement of financial instruments

The classification of financial instruments at initial recognition depends on the purpose for which the financial instruments were acquired and their characteristics. All financial instruments are measured initially at their fair value plus, in the case of financial assets and liabilities not measured at fair value through profit or loss, any directly attributable incremental costs of acquisition or issue.

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.

2.8.2. Derivative financial instruments

A derivative is a financial instrument or other contract with all three of the following characteristics:

- its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the ‘underlying’);
- it requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and
- it is settled at a future date.

Derivatives are recorded at fair value and classified as assets when their fair value is positive and as liabilities when their fair value is negative. Subsequently, derivatives are measured at fair value.

Revaluations of trading derivatives are included in profit or loss under *Net foreign exchange gains / losses* line in the case of currency derivatives and under *Financial instruments gains / losses* line in the case of all other derivatives.

Interest income and expense are recognised under their corresponding headings in profit or loss.

Derivatives embedded in other financial instruments, such as the conversion option in a convertible bond, are treated as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract and the host contract is not itself measured at fair value with revaluation recognised in profit or loss. The embedded derivatives separated from the host are carried at fair value, with any revaluation gains / losses recognised under *Financial instruments gains / losses* line in profit or loss.

2.8.3. Financial assets / liabilities held for trading

Financial assets or financial liabilities held for trading represent assets and liabilities acquired or incurred principally for the purpose of selling or repurchasing them in the near term and are recognised in the statement of financial position at fair value. Any revaluation gains / losses are recognised under *Financial instruments gains / losses* line in profit or loss, whilst interest income and expense are included in the corresponding heading in profit or loss according to the terms of the relevant contract. In the case of dividend income, this is recognised under *Other income* line when the right to receive the dividend has been established.

2. Significant accounting policies (continued)

2.8. Financial Instruments (continued)

2.8.4. Financial assets / liabilities designated upon initial recognition at fair value through profit or loss

Financial assets and financial liabilities classified in this category are designated by management on initial recognition when the following criteria are met:

- the designation eliminates or significantly reduces the inconsistency that would otherwise arise from the measurement of the assets or liabilities or the recognition of gains or losses on them on a different basis, or
- the assets and liabilities are part of a group of financial assets, financial liabilities or both which are managed and their performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy, or
- the financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows of the instrument or it is clear, with little or no analysis, that the embedded derivative could not be separated.

These assets do not form part of any trading portfolio because no recent pattern of short-term profit taking exists. They may include listed debt securities hedged by derivatives and not designated for hedge accounting, as well as, unlisted equities that are managed on a fair value basis.

Financial assets and financial liabilities designated upon initial recognition at fair value through profit or loss are recognised in the statement of financial position at fair value. Changes in fair value are recognised under *Financial instruments gains / losses* line in profit or loss. Interest income and expense are included under the corresponding headings in profit or loss according to the terms of the relevant contract, while any dividend income is recognised under *Other income* line when the right to receive the dividend has been established.

2.8.5. Held-to-maturity investments

Held-to-maturity investments are those non-derivative instruments with fixed or determinable payments and fixed maturities and which the Bank has the intention and ability to hold to maturity.

After initial measurement, held-to-maturity investments are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortisation is included under *Interest income* line and any losses arising from impairment of such investments are recognised in profit or loss. If as a result of a change in intention or ability it is no longer appropriate to classify an investment as held-to-maturity, it shall be reclassified as available-for-sale and re-measured at fair value, with any difference between its carrying amount and fair value accounted for accordingly.

2.8.6. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale and are not classified as investments held for trading, available-for-sale or at fair value through profit or loss.

After their initial recognition, loans and receivables are subsequently measured at amortised cost using the effective interest rate method, less any provision for impairment. The losses arising from impairment are recognised in profit or loss under *Provisions for impairment of loans and advances and other credit facilities* line in the case of loans and advances to customers and under *Impairment of other financial instruments* line for all other items.

2. Significant accounting policies (continued)

2.8. Financial Instruments (continued)

2.8.6. Loans and receivables (continued)

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. Loans subject to collective impairment assessment whose terms have been renegotiated are no longer considered past due, but are treated as up to date loans for measurement purposes. Such loans are taken into account in determining the inputs for collective impairment calculation. Loans subject to individual impairment assessment whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired. Any resulting difference is recognised in profit or loss. The carrying amounts of loans that have been classified as renegotiated retain this classification in accordance with the rules of the technical standard of the European Banking Authority ('EBA').

2.8.7. Available-for-sale investments

Available-for-sale investments are those which are designated as such or do not qualify for classification under investments at fair value through profit or loss, investments held-to-maturity or loans and receivables. These investments can be disposed in response to changes in market risks or liquidity requirements and include equity and debt securities.

After initial recognition, available-for-sale investments are measured at fair value. Unrealised gains and losses from changes in fair value are recognised directly in other comprehensive income. When the investment is disposed of, the cumulative gain or loss previously recognised in other comprehensive income is recognised in profit or loss under *Financial instruments gains / losses* line.

2.8.8. Other financial liabilities

Other financial liabilities refer mainly to customer deposits and funding from other banks. Financial liabilities are recognised when the Bank enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at fair value, which is net of directly attributable transaction costs incurred. Subsequent measurement of such financial liabilities is at amortised cost, using the effective interest rate method.

2.8.9. Amounts owed to depositors

Amounts owed to depositors are financial instruments where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder or other banks.

At initial recognition the amounts owed to depositors are recognised at fair value. After initial recognition, amounts owed to depositors are subsequently measured at amortised cost using the effective interest rate method. Amortised cost is calculated by taking into account any discount or premium on the face value and initial costs that are an integral part of the effective interest rate. The corresponding interest expense is recognised in profit or loss under *Interest expense* line.

2.8.10. Employee benefits

The Bank and its employees contribute to the Government Social Insurance Fund based on employees' salaries. The Bank's contributions are expensed as incurred and are included in *Staff costs* line.

The Bank operates a defined contribution scheme, which provides for employer contributions of 6% on the employee gross salary and employee contributions within a range of 4%-10% of their gross salary. The Bank has no legal or constructive obligations to pay further contributions if the scheme does not hold sufficient assets to pay all employee benefits relating to employee service in the current period. This scheme is in the form of a pension plan under Ancoria Insurance Public Ltd, an indirect shareholder of the Bank.

2. Significant accounting policies (continued)

2.8. Financial Instruments (continued)

2.8.11. General

Where the Bank holds more than one investment in the same security, they are deemed to be disposed of on a weighted average cost basis.

The following table summarises the treatment of each financial instrument category in terms of measurement methodology after initial recognition and the statement under which any gains or losses are recognised.

Category	Measurement	Recognition of gains & losses
Loans and receivables	Amortised cost using Effective Interest Rate method	Profit or loss
Held-to-maturity	Amortised cost using Effective Interest Rate method	Profit or loss
At fair value through profit or loss	Fair value	Profit or loss
Available-for-sale	Fair value	Other comprehensive income (except for interest, impairment and foreign exchange losses which are recognised in profit or loss). The cumulative gain or loss that was recognised in other comprehensive income is recognised in profit or loss.

2.9. Netting and derecognition of financial assets and liabilities

Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the rights to receive cash flows from the asset have expired,
- the Bank retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement, or
- the Bank has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

Financial liabilities

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, with the difference in the respective carrying amounts being recognised in profit or loss.

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. This is not generally the case with master netting agreements and the related assets and liabilities are presented gross in the statement of financial position.

2. Significant accounting policies (continued)

2.10. Impairment of financial assets

2.10.1. Loans and receivables

The Bank assesses at each reporting date whether there is any objective evidence that a financial asset is impaired. Such objective evidence of impairment is a result of one or more events that have occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

Objective evidence of impairment may include indications that the borrower is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that the borrower might be declared bankrupt or proceed with a financial restructuring and where observable data indicate that there is a measurable increase in credit risk. There is objective evidence that a loan is impaired when it is probable that the Bank will not be able to collect all amounts due, according to the original contract terms.

For loans and advances to customers carried at amortised cost, the Bank first assesses individually whether objective evidence of impairment exists for loans and advances that are individually significant. Furthermore, a collective impairment assessment is performed for loans and advances that are not individually significant. Collectively assessed facilities are grouped based on similar credit risk characteristics and evaluated for impairment. All facilities which are assessed on an individual basis but for which no impairment is recognised are included in the collective assessment according to the group with the most similar credit characteristics.

The Bank accounts for impairment provisions using a methodology consistent with IAS 39 and the Central Bank of Cyprus' Directive on Loan Impairment and Provisioning Procedures of 2014 to 2016.

Further, the Bank notes differences in impairment provisions under IFRS 9 and in an effort towards IFRS 9 compliance, the Bank has introduced the following stages in terms of categorising its facilities:

- **Stage 1** - As soon as facilities are originated

  Group exposures below a specific threshold are assessed under a collective basis using 12-month probability of default estimates. Group exposures above the specified threshold are assessed on an individual basis.

- **Stage 2** - When there is a significant increase in credit risk

  Group exposures are assessed on a collective basis by using a lifetime expected probability of default rather than a 12-month probability as per Stage 1.

- **Stage 3** - When there is evidence of impairment or credit losses have occurred

  This stage is assessed on an individual basis, without accounting for any specified exposure thresholds.

The above stage classification is currently used for internal monitoring purposes and will be applied to exposures, for the purpose of determining the impairment provisions, with the adoption of IFRS 9 in 2018. Currently all exposures lie within the Stage 1 classification.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan and the present value of the estimated future cash flows including the cash flows which may arise from guarantees and tangible collateral. The collectability of individually significant loans and advances is evaluated based on the customer's overall financial condition, resources and payment record, the prospect of support from creditworthy guarantors and the realisable value of any collateral.

The present value of the estimated future cash flows is calculated using the loan's original effective interest rate. If a loan bears a variable interest rate, the discount rate used for measuring any impairment loss is the current reference rate plus the margin specified in the initial contract.

2. Significant accounting policies (continued)

2.10. Impairment of financial assets (continued)

2.10.1. Loans and receivables (continued)

For the purposes of a collective evaluation of impairment, loans are grouped based on similar credit risk characteristics taking into account the type of the loan and the credit score of the customer.

Future cash flows for a group of loans and advances that are collectively evaluated for impairment are estimated on the basis of historical loss experience for loans with similar credit risk characteristics to those of the group. Historical loss experience is adjusted on the basis of current observable data due to the Bank's limited historical information availability to reflect both the impact of current conditions that did not affect the period on which the historical loss experience is based and to remove the impact of conditions in the historical period that do not currently apply. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The carrying amount of the loan is reduced using a provision account and the amount of the loss is recognised in profit or loss. Loans together with the associated provisions are written off when there is no realistic prospect of future recovery. If in a subsequent period, the amount of the estimated impairment loss decreases and the decrease is due to an event occurring after the impairment was recognised, when the creditworthiness of the customer has improved to such an extent that there is reasonable assurance that all or part of the principal and interest according to the original contract terms of the loan will be collected, the previously recognised impairment loss is reduced by adjusting the impairment provision account. If a previously written-off loan is subsequently recovered, any amounts previously charged are credited in profit or loss.

Collateral valuation

The Bank seeks to use collateral, where possible, to mitigate its risks on financial assets. The collateral comes in various forms, such as real estate, cash and other tangible assets. The fair value of collateral is generally assessed, at a minimum, at inception and based on the Bank's credit policy. To the extent possible, the Bank uses active market data for valuing any financial assets held as collateral. Other financial assets which do not have readily determinable market values are valued using models. Non-financial collateral, such as real estate, are valued on a frequent basis according to relevant directives, type and market fluctuations. Between formal valuations, value is projected based on property price indices by independent sources rectified by the Central Bank of Cyprus ('CBC').

2.10.2. Held-to-maturity investments

For held-to-maturity investments, the Bank assesses at each reporting date whether there is objective evidence of impairment. If this is the case, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses not yet incurred). The carrying amount of the asset is reduced and the amount of the loss is recognised under *Impairment of other financial instruments* line in profit or loss.

If, in a subsequent period, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, the impairment loss previously recognised is reversed and the reversal is credited to the same heading in profit or loss.

2. Significant accounting policies (continued)

2.10. Impairment of financial assets (continued)

2.10.3. Available-for-sale investments

For available-for-sale investments, the Bank assesses whether there is objective evidence of impairment at each reporting date.

In the case of equity securities classified as available-for-sale, objective evidence would include a significant or prolonged decrease, in the fair value of the investment below cost. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in profit or loss – is deducted from the respective revaluation reserve in other comprehensive income and recognised under *Impairment of other financial instruments* line in profit or loss. Impairment losses on equity securities are not reversed through profit or loss. Increases in their fair value after impairment are recognised in the respective revaluation reserve in other comprehensive income.

In the case of debt securities classified as available-for-sale, impairment is assessed based on the same criteria applicable to financial assets carried at amortised cost. If, in a subsequent period, the impairment loss decreases and the decrease can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss previously recognised is reversed through *Impairment of other financial instruments* line in profit or loss.

2.11. Hedge accounting

The Bank uses derivative financial instruments to hedge exposures to interest rate and foreign exchange risks. The Bank applies hedge accounting for transactions which meet the specified criteria.

At inception of the hedging relationship, the Bank formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk and the objective and strategy for undertaking the hedge, as well as the method that will be used to assess the effectiveness of the hedging relationship both at inception and at ongoing basis.

2.12. Property and equipment

2.12.1. Leasehold property

The cost of adapting / improving leasehold property is amortised on a straight-line basis over 5 to 10 years (or 10% to 20% depreciation per annum) or over the period of the lease if this does not exceed 10 years. Residual value is assumed to be nil.

2.12.2. Furniture and fittings

Furniture and fittings are measured at cost less accumulated depreciation. Depreciation of furniture and fittings is calculated on a straight-line basis over their estimated useful life of 5 to 10 years (or 10% to 20% depreciation per annum).

2.12.3. Computer hardware, security and operating systems and other equipment

Computer hardware, systems and equipment are measured at cost less accumulated depreciation. Depreciation is calculated on a straight-line basis over their estimated useful life of 5 to 10 years (or 10% to 20% depreciation per annum).

2. Significant accounting policies (continued)

2.13. Intangible assets

Intangible assets mainly consist of computer software and licences relating to usage of such software.

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses.

Amortisation is calculated on a straight-line basis over the estimated useful life of the assets which is 3 to 5 years for computer software (or 20% to 33% amortisation per annum). Intangible assets are reviewed for impairment when events relating to changes to circumstances indicate that the carrying value may not be recoverable. If the carrying amount exceeds the recoverable amount then the intangible assets are written down to their recoverable amount.

2.14. Impairment of tangible and intangible assets excluding goodwill

At each reporting date, the Bank reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Bank estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset or cash-generating unit is estimated to be less than its carrying amount, the carrying amount of the asset / cash-generating unit is reduced to its recoverable amount. An impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset / cash-generating unit is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset / cash-generating unit in prior years. A reversal of an impairment loss is recognised immediately in profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

2.15. Cash and cash equivalents

Cash and cash equivalents consist of cash, non-obligatory balances with central bank, placements with banks and other securities that are readily convertible into known amounts of cash or are repayable within three months of the date of their acquisition.

2.16. Leases

2.16.1 Finance Leases

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

2.16.2 Operating Leases

Leases that do not transfer to the Bank substantially all the risks and benefits incidental to ownership of the leased items are considered operating leases. Operating lease payments are recognised as an expense in profit or loss on a straight-line basis over the lease term.

2. Significant accounting policies (continued)

2.17. Provisions

Provisions for any claims against the Bank are calculated and recognised when:

- there is a present obligation (legal or constructive) arising from past events,
- the settlement of the obligation is expected to result in an outflow of resources embodying economic benefits, and
- a reliable estimate of the amount of the obligation can be made.

2.18. Share capital

Any difference between the issue price of share capital and the nominal value is recognised as share premium. The costs incurred attributable to the issue of share capital are deducted from equity.

2.19. Financial guarantees

The Bank issues financial guarantees to its customers, consisting of letters of credit, letters of guarantee and acceptances. Financial guarantees are initially recognised at fair value. Subsequently, the Bank's liability under each guarantee is measured at the higher of:

- the amount initially recognised reduced by the cumulative amortised premium which is periodically recognised in profit or loss under *Fee and commission income* line, in accordance with the terms of the guarantee, and
- the best estimate of the expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is recognised in profit or loss under *Provisions for impairment of loans and advances and other credit facilities* line. The remaining balance of the liability for financial guarantees is recognised under *Fee and commission income* line in profit or loss when the guarantee is fulfilled, cancelled or expired.

2.20. Comparatives

Where necessary, comparative figures have been adjusted to conform to changes in presentation in the current year.

3. Significant accounting estimates and judgments

The Bank makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. Estimates and judgments are continuously evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

3.1. Going concern

Despite recent developments in the economic environment of the Cyprus economy as mentioned in Note 32, the Bank's management has assessed the Bank's ability to continue as a going concern and is satisfied that the Bank has the financial resources to continue its business operations in the foreseeable future. Accordingly, the financial statements are prepared on the going concern basis.

3.2. Provisions for impairment of loans and advances

The Bank reviews loans and advances to assess whether a provision for impairment should be recorded in profit or loss.

For individually significant assets, impairment allowances are calculated on an individual basis and all relevant considerations that have a bearing on the expected future cash flows are taken into account. The level of the impairment allowance is the difference between the value of the expected future cash flows discounted at the loan's original effective interest rate and its carrying amount. Subjective judgements are made in the calculation of future cash flows.

Furthermore, judgements change with time as new information becomes available, resulting in revisions to the impairment allowance. Changes in these estimates would result in a change in the allowances and have a direct impact on the impairment charge.

In addition to provisions for impairment on an individual basis, the Bank also makes collective impairment provisions through the assignment of probabilities of default and loss given default for portfolios of loans with similar credit risk characteristics. This methodology is subject to estimation uncertainty, partly because it is not practicable to identify losses on an individual loan basis due to the large number of loans in each portfolio. Further, the absence of historical loss experience increases estimation uncertainty.

The methodology and the assumptions used in calculating impairment losses are reviewed regularly. It is possible that the actual results within the next financial year could be different from the assumptions made, resulting in a material adjustment to the carrying amount of loans and advances.

3.3. Tax

The Bank is subject to Cyprus income tax. Significant estimates are required in determining the provision for taxes at the reporting date, and therefore the tax determination is uncertain. Where the final tax is different from the amounts that were initially recorded, such differences will affect the income tax expense, the tax liabilities and deferred tax liabilities of the period in which the final tax is agreed with the tax authorities.

The Bank recognises a deferred tax asset in relation to tax losses, to the extent there may be future taxable profits against which the losses may be utilised. The determination of the amount of deferred tax assets that can be recognised is based on the timing and level of future taxable profits, in combination with future tax planning strategies. These variables are determined based on significant estimates and assumptions, and are by definition uncertain. It is possible that the actual conditions in the future will be different from the assumptions used, resulting in material adjustments to the carrying value of deferred tax assets.

No deferred tax asset has been recognised in the statement of financial position as at 31 December 2017 and 2016.

3.4. Fair value of financial assets and liabilities

Management estimates that the fair value of financial assets and liabilities approximates their carrying amounts as presented in the statement of financial position.

4. Interest income

	2017	2016
	€	€
Loans and advances to customers	**1.065.625**	165.042
Investments held-to-maturity	**23.672**	40.879
Investments available-for-sale	**3.367**	-
Placements with banks	**214**	-
	1.092.878	205.921

5. Interest expense

	2017	2016
	€	€
Customer deposits	**153.790**	80.035
Balances with Central Bank	**81.093**	91.477
Placements with banks	**17.147**	27.461
Other borrowings	**8.003**	-
	260.033	198.973

Balances held with the Central Bank and other banks carry negative interest, which averaged 0,40% as at 31 December 2017 (2016: 0,40%).

6. Staff costs

	2017	2016
	€	€
Staff salaries and other remuneration (net of any subsidies)	**2.508.682**	2.116.103
Pension plan contributions	**127.911**	93.651
Social insurance and other employer's contributions	**304.275**	274.850
	2.940.868	2.484.604

The number of persons employed by the Bank as at 31 December 2017 was 75 (2016: 65). Remuneration concerning Directors and key management personnel is disclosed in Note 31.

The Bank operates a defined contribution scheme, which provides for employer contributions of 6% on the employee gross salary and employee contributions within a range of 4%-10% of their gross salary. The Bank's contributions are expensed as incurred and are included under *Staff costs* line. The Bank has no legal or constructive obligations to pay further contributions if the scheme does not hold sufficient assets to pay all employee benefits relating to employee service in the current period. This scheme is in the form of a pension plan under Ancoria Insurance Public Ltd, an indirect shareholder of the Bank.

7. Other operating expenses

	2017	2016
	€	€
Rental of premises	**318.000**	310.932
Utilities and other premises expenses	**133.981**	142.441
Post and telecommunication expenses	**129.198**	89.117
Insurance expenses	**39.349**	50.659
Directors' remuneration and expenses	**114.237**	113.484
Travelling and training (net of any subsidies)	**53.191**	32.828
Auditors' remuneration for statutory audit	**48.195**	31.535
Auditors' remuneration for other assurance engagements	**-**	2.380
Legal and consultancy fees	**178.062**	168.513
Advertising and promotion	**245.836**	235.194
Special tax levy on deposits	**73.108**	40.618
Supervisory fees	**57.750**	54.602
Computer supplies, maintenance and related expenses	**697.625**	521.122
Other operating expenses	**222.844**	179.500
	2.311.376	1.972.925

8. Provisions for impairment of loans and advances and other credit facilities

	2017	2016
	€	€
Loans and advances to customers (*Note 13*)	**242.019**	66.580
Financial guarantees and commitments (*Note 21*)	**70.549**	-
	312.568	66.580

9. Loss before tax

Loss before tax is stated after charging the following items:

	2017	2016
	€	€
Directors' remuneration (*Note 31*)	**108.412**	107.459
Operating lease rentals for buildings and software	**369.349**	369.286
Auditors' remuneration for:		
- Statutory audit	**48.195**	31.535
- Other non-audit assurance engagements	**-**	2.380

All the above amounts are included under *Other operating expenses* line.

10. Income tax

The total tax charge for the year can be reconciled to the accounting profit or loss as follows:

	2017	2016
	€	€
Loss before tax	**(5.668.173)**	(5.435.516)
Corporation tax based on the applicable rates	**(708.522)**	(679.440)
Tax effect of:		
- Non-deductible expenses	**381.966**	283.526
- Allowances and income not subject to tax	**(368.053)**	(277.716)
- Tax losses for the year	**694.609**	673.630
	-	-
Withholding tax on dividend income	**(28)**	-
Tax charge	**(28)**	-

Corporation tax is calculated at the rate of 12,5% on taxable income.

As per the Income Tax law, a company may carry forward tax losses incurred during a tax year, over the next five years to be offset against taxable income. As at 31 December 2017, the Bank's tax losses (subject to assessment by the Tax Department) to be carried forward amounted to €14.018.136.

No deferred tax asset was recognised in respect of tax losses due to uncertainties pertaining the amount and timing of future taxable benefits.

Special Tax Levy on Credit Institutions

According to the Special Levy on Credit Institutions Law of 2011 passed on 14 April 2011, a special levy on credit institutions was imposed on qualifying deposits held by each credit institution at 31 December of the year preceding the year of taxation. Based on the latest amendment of the Law published in the official Gazette on the 26 July 2013, the annual special tax levy is calculated on a quarterly basis at the rate 0,0375% on the deposits of financial institutions at 31st March, 30th June, 30th September and 31st December of each year.

For the year ended 31 December 2017, the total Special Tax Levy imposed on the Bank's qualifying deposits amounted to €73.108 (2016: €40.618) and is included under *Other operating expenses* line.

11. Cash and balances with Central Bank

	2017	2016
	€	€
Cash	**3.394.380**	2.041.498
Balances with Central Bank of Cyprus	**16.769.645**	32.757.219
	20.164.025	34.798.717

As at 31 December 2017, the minimum reserve requirement with Central Bank of Cyprus ('CBC') was €460.316 (2016: €257.236).

The analysis of credit ratings for deposits with the CBC by independent rating agencies is presented in Note 29. Balances with CBC carry an interest charge for amounts in excess of calculated minimum reserves.

12. Placements with banks

The analysis of credit ratings of placements with banks by independent rating agencies is presented in Note 29. An analysis of placements between local and foreign banks is presented below:

	2017	2016
	€	€
Foreign Banks	**2.615.172**	5.601.874
Local Banks	**-**	85.516
	2.615.172	5.687.390

The majority of the total placements with foreign banks at the end of 2016 was kept with Skandinaviska Enskilda Banken AB ('SEB'), amounting to €3.407.808. As of 2017, the balance kept with SEB amounts to €398.261.

The rest of the placements with foreign banks as at 31 December 2017 and 2016 refer to current balances on nostro accounts with correspondent banks. The majority of these balances in 2017 was kept with KBC Bank NV for a total amount of €1.160.405. All placements with foreign banks carry an interest charge based on the interbank rate of the relevant term and currency.

13. Loans and advances to customers

	2017	2016
	€	€
Retail		
Housing	**43.912.611**	17.054.481
Consumer	**3.040.435**	1.007.191
Overdrafts	**148.824**	62.992
	47.101.870	18.124.664
Business		
Loans	**14.039.071**	6.178.902
Overdrafts	**2.445.878**	362.849
	16.484.949	6.541.751
Gross loans and advances to customers	**63.586.819**	24.666.415
Provisions for impairment of loans and advances to customers	**(308.599)**	(66.580)
	63.278.220	24.599.835

Movement of provisions for impairment of loans and advances

	2017	2016
	€	€
1 January	**(66.580)**	-
Provisions for impairment for the year (*Note 8*)	**(242.019)**	(66.580)
31 December	**(308.599)**	(66.580)

There was no interest suspended as at 31 December 2017.

13. Loans and advances to customers (continued)

<u>Non-performing exposures</u>

On 31 December 2017, no non-performing exposures were held by the Bank in accordance with the European Banking Authority's ('EBA') technical standards published in 2014.

According to the standards, the following exposures are considered as non-performing ('NPE'):

- Material exposures of more than ninety (90) days past due
- The debtor is assessed as unlikely to pay its credit obligations in full without realisation of collateral, regardless of the existence of any past due amount or of the number of days past due
- The exposure is impaired as per the applicable accounting framework
- Exposures considered as in default in accordance with EU Regulation 575/2013 Article 178
- Exposures where legal action has been taken by the Bank against them or exposures of which debtors are bankrupt
- Forborne exposures reclassified from NPE status that were NPE at forbearance or became NPE after forbearance and which are re-forborne while under probation
- Forborne exposures reclassified from NPE status that were NPE at forbearance or became NPE after forbearance that present arrears 30 days past due while under probation
- For debtors classified as retail as per the EU Regulation 575/2013, when the Bank has on-balance sheet exposures to a debtor that are material and are past due by more than 90 days and the gross carrying amount of which represents more than 20% of the gross carrying amount of all on-balance sheet exposures to that debtor, then all on and off-balance sheet exposures to that debtor shall be considered as NPE
- For debtors classified as non-retail as per the EU Regulation 575/2013, when the Bank has on-balance sheet exposures to a debtor classified as non-performing, then all on and off-balance sheet exposures to that debtor shall be considered as NPE

According to EU Regulation 575/2013 Article 178, reasonable materiality thresholds of credit obligations past due shall be defined by national competent authorities. The Central Bank of Cyprus ('CBC') has issued a Directive on Supervisory Reporting on Forbearance and Non-Performing Exposures of 2015 stating the following thresholds:

- For obligors of retail exposures, including exposures secured by mortgages of residential or commercial property, the higher of:
  a. A minimum limit of €500, i.e. if the amount in arrears of an obligor who has a retail exposure does not exceed €500, this exposure is not classified as defaulted exposure, or
  b. One loan instalment or an overdraft excess of 10% of the contractual limit, as applicable
- For other exposures, the higher of:
  a. A minimum limit of €1.000, i.e. if the total amount in arrears of the total exposure of an obligor does not exceed €1.000, this exposure is not classified as defaulted exposure, or
  b. The amount of arrears and excesses that in total exceed 10% of the total exposures to the obligor

13. Loans and advances to customers (continued)

Non-performing exposures (continued)

In October 2017, the European Commission published a delegated regulation supplementing EU Regulation 575/2013 with regard to regulatory technical standards for the materiality threshold for credit obligations past due which states the following thresholds:

- Absolute threshold cannot be higher than €100 for retail exposures or €500 for non-retail exposures
- Relative thresholds to be set at the level of 1% for both retail and non-retail exposures
- If a national competent authority considers that the 1% materiality threshold does not reflect a reasonable level of risk, it may set a relative threshold at a different level which in any case must be lower than or equal to 2,5%

Forborne exposures

On 31 December 2017, no forborne exposures were held by the Bank in accordance with EBA's technical standards published in 2014.

According to the standards, forborne exposures are debt contracts in respect of which forbearance measures have been extended. Forbearance measures consist of concessions towards a debtor facing or about to face difficulties in meeting its financial commitments ("financial difficulties").

Concession refers to either of the following actions:

- A modification of the previous terms and conditions of a contract the debtor is considered unable to comply with due to its financial difficulties to allow for sufficient debt service ability, that would not have been granted had the debtor not been in financial difficulties
- A total or partial refinancing of a troubled debt contract that would not have been granted had the debtor not been in financial difficulties.

Evidence of concession includes:

- A difference in favour of the debtor between the modified and the previous terms of the contract
- Cases where a modified contract includes more favourable terms than other debtors with a similar risk profile could have obtained from the same institution.

Bank's policy for specific and collective provisions

The Bank reviews the collectability of its loans and advances to customers and assesses whether a provision for impairment should be recorded in profit or loss. The procedure followed by the Bank for the provisioning exercise comprises of an individual assessment of the exposures for specific provision and assessment for collective impairment as per the Bank's provisioning policy.

The selection criteria for clients which are individually assessed for specific provision are the following:

- To groups of connected persons which exceed 1% of the Bank's share capital and reserves
- To shareholders with direct or indirect holdings in excess of 10% of the Bank's share capital and their connected persons
- To members of the Board of Directors and their connected persons
- Senior management of the Bank and their connected persons
- Facilities where evidence of impairment exists as outlined in Note 2.10.1.

13. Loans and advances to customers (continued)

Bank's policy for specific and collective provisions (continued)

For the exposures that are individually assessed for impairment, discounted cash flow calculations are performed. The amount of impairment is the difference between the exposure's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The estimated future cash flows include any expected cash flows from the borrowers operations, any other sources of funds and the proceeds from liquidation of collateral where applicable. Property collateral values are assessed in accordance to the CBC's Directive on Loan Impairment and Provisioning Procedures in terms of expected amount to be received and timing of cash realisation.

Collective provision

All exposures which are assessed on an individual basis but for which no impairment is recognised and all exposures not individually assessed are included in pools of exposures with similar credit characteristics and are assessed for collective impairment using the applicable Probability of Default and Loss Given Default rates that are set in the Bank's provisioning policy.

14. Investments available-for-sale

	2017	2016
	€	€
Bonds		
Banks and other organisations	**2.132.275**	302.807
Exchange-traded funds	**80.468**	-
	2.212.743	302.807
Listed in European stock exchanges	**2.132.275**	302.807
Listed in other stock exchanges	**80.468**	-
	2.212.743	302.807

Geographical breakdown based on region / country of issuer

	2017	2016
	€	€
Other European countries	**911.863**	-
Other non-European countries	**1.300.880**	302.807
	2.212.743	302.807

The Bank uses the following hierarchy for determining and disclosing fair value:

- **Level 1**: investments valued using quoted prices in active markets.
- **Level 2**: investments valued using models for which all inputs that have a significant effect on fair value are market observable.
- **Level 3**: investments valued using models for which inputs that have a significant effect on fair value are not based on observable market data.

All investments available-for-sale are classified as Level 1 for fair value disclosure purposes.

15. Investments held-to-maturity

	2017	2016
	€	€
Bonds		
Cyprus government	**530.033**	5.040.663
Other European governments	**1.337.394**	964.228
Banks and other organisations	**2.362.343**	2.393.349
	4.229.770	8.398.240
Listed in Cyprus Stock Exchange	**-**	4.498.972
Listed in other stock exchanges	**4.229.770**	3.899.268
	4.229.770	8.398.240

Geographical breakdown based on region / country of issuer

	2017	2016
	€	€
Cyprus	**530.033**	5.040.663
Other European countries	**3.396.713**	3.053.564
Other non-European countries	**303.024**	304.013
	4.229.770	8.398.240

The fair value of investments held-to-maturity as at 31 December 2017 was €4.236.441 (2016: €8.429.935), based on quoted market prices with the exception of short-term Treasury bills (i.e. with maturity less than 3 months) for which nominal value approximates fair value.

As a result, in accordance with the hierarchy followed for determining and disclosing fair value as mentioned in Note 14, all investments held-to-maturity are classified as Level 1 for fair value disclosure purposes, with the exception of Treasury bills which are classified as Level 2. As at 31 December 2017, the fair value of Treasury bills was €nil since all such positions had been redeemed prior to year end (2016: €4.500.000). The credit ratings applicable to investments held-to-maturity as at 31 December 2017 and 2016 are presented in Note 29.

The weighted average effective yield on investments held-to-maturity held at the year end was 0,57% (2016: 0,41%).

16. Other assets

	2017	2016
	€	€
Receivables from parent company (*Note 31*)	**88.745**	56.087
Deposits and prepayments	**377.541**	343.539
Other receivables	**958.463**	798.291
	1.424.749	1.197.917

Deposits and prepayments include an amount of €130.800 (2016: €130.550) relevant to premises lease agreements and related expenses.

Other receivables include an amount of €92.891 (2016: €102.499) that relates to receivables from suppliers in respect of VAT, which has already been remitted by the Bank to the VAT authorities during 2016. The remainder of other receivables mainly consist of cheques pending clearance and settlement accounts.

17. Property and equipment

Year 2017	Leasehold improvements €	Equipment €	Furniture and fittings €	Advances for premises €	Other tangible assets €	Total €
Cost						
1 January	2.147.824	877.013	531.771	-	-	**3.556.608**
Additions	1.837	180.619	11.588	2.131.071	-	**2.325.116**
31 December	**2.149.661**	**1.057.632**	**543.359**	**2.131.071**	**-**	**5.881.724**
Depreciation						
1 January	243.619	135.130	56.803	-	-	**435.552**
Charge for the year	214.913	170.111	53.671	**-**	**-**	**438.695**
31 December	**458.532**	**305.241**	**110.474**	**-**	**-**	**874.247**
Net Book Value	**1.691.129**	**752.391**	**432.885**	**2.131.071**	**-**	**5.007.477**

Year 2016	Leasehold improvements €	Equipment €	Furniture and fittings €	Advances for premises €	Other tangible assets €	Total €
Cost						
1 January	1.841.218	492.237	402.572	-	32.851	2.768.878
Additions	306.606	351.925	129.199	-	-	787.730
Transfers	-	32.851	-	-	(32.851)	-
31 December	2.147.824	877.013	531.771	-	-	3.556.608
Depreciation						
1 January	40.663	22.409	9.849	-	-	72.921
Charge for the year	202.956	112.721	46.954	-	-	362.631
31 December	243.619	135.130	56.803	-	-	435.552
Net Book Value	1.904.205	741.883	474.968	-	-	3.121.056

Leasehold improvements comprise of expenditure on the Bank's business centres and head office premises.

Advances for premises as at 31 December 2017 consist of a down payment made on 20 December 2017 in relation to the acquisition of the Bank's business centre premises in Limassol which are currently under leasehold arrangements. Further details on the mentioned transaction are provided in Note 31.

18. Intangible assets

Year 2017	Computer software and licences €	Intangibles under development €	Total €
Cost			
1 January	1.817.247	179.128	**1.996.375**
Additions	231.482	-	**231.482**
Transfers	162.135	(162.135)	**-**
31 December	**2.210.864**	**16.993**	**2.227.857**
Amortisation			
1 January	710.264	-	**710.264**
Charge for the year	631.447	-	**631.447**
31 December	**1.341.711**	**-**	**1.341.711**
Net Book Value	**869.153**	**16.993**	**886.146**

Year 2016	Computer software and licences €	Intangibles under development €	Total €
Cost			
1 January	1.613.890	-	1.613.890
Additions	203.357	179.128	382.485
31 December	1.817.247	179.128	1.996.375
Amortisation			
1 January	133.146	-	133.146
Charge for the year	577.118	-	577.118
31 December	710.264	-	710.264
Net Book Value	1.106.983	179.128	1.286.111

As at 1 January 2016, intangible assets mainly relate to software licences and banking systems that had been put in operation during 2015, on the commencement of banking operations. No amortisation had been charged prior to commencement of operations.

None of the intangibles under development are internally generated.

19. Customer deposits

	2017 €	2016 €
Current accounts	**34.177.710**	26.375.180
Savings accounts	**2.344.889**	1.101.950
Fixed term deposit accounts	**23.087.343**	10.044.705
	59.609.942	37.521.835

20. Other borrowings

On 16 May 2017, the Bank entered into a portfolio risk sharing loan agreement of €20 million with the European Investment Fund acting on behalf of the Cyprus Entrepreneurship Fund ('CYPEF'). CYPEF is a fund established by the Republic of Cyprus to implement a national scheme for facilitating access to finance and improving funding conditions for small and medium-sized enterprises (including self-employed entrepreneurs) active in Cyprus in collaboration with selected financial intermediaries.

In accordance with the terms of the agreement, CYPEF will contribute €10 million and the Bank an additional €10 million towards lending small and medium-sized enterprises ('SMEs') at lower interest rates than what would have been offered by the Bank in the absence of the agreement with CYPEF. The €10 million of CYPEF will be made available to the Bank in tranches to be decided by the Bank and subject to the satisfaction of certain covenants.

The commencement date of the agreement is considered to be the 1st of June 2017. The agreement carries a maximum maturity period of 15 years. The loan payable to CYPEF is charged with interest rate of 3-month Euribor + 1,00% and repayments of the loan are made quarterly depending on the amount of repayments made by SMEs with outstanding balances under the scheme. The agreement provides that the principal amount owed towards CYPEF will be reduced in case of a defaulted or restructured exposure under the scheme, subject to certain covenants.

Up to 31 December 2017, the Bank has only requested €3 million from CYPEF out of the total €10 million available under the agreement. As at the reporting date, the outstanding balance comprises of €3 million principal together with accrued interest for the relevant period.

21. Other liabilities

	2017	2016
	€	€
Taxes payable	**122.689**	84.036
Accrued expenses	**252.240**	239.749
VAT payable	**22.622**	11.799
Provisions for financial guarantees and commitments (*Note 8*)	**70.549**	-
Other creditors and liabilities	**1.180.369**	328.663
	1.648.469	664.247

Other creditors and liabilities mainly consist of issued cheques pending clearance and settlement accounts.

22. Share capital and share premium

	2017			2016		
	Number of shares	**Share capital €**	**Share premium €**	Number of shares	Share capital €	Share premium €
Authorised						
Ordinary shares of €1 each	**201.000**	**201.000**	**-**	201.000	201.000	-
Issued and fully paid						
1 January	**101.000**	**101.000**	**49.900.000**	101.000	101.000	49.900.000
31 December	**101.000**	**101.000**	**49.900.000**	101.000	101.000	49.900.000

Authorised capital

Under its Memorandum of Association, the Company fixed its authorised share capital at 1.000 ordinary shares of nominal value of €1 each.

On 15 December 2014, the Company increased its authorised capital to 201.000 ordinary shares of nominal value of €1 each.

Issued and fully paid capital

Upon incorporation on 20 August 2013, the Company issued to the subscribers of its Memorandum of Association 1.000 ordinary shares of €1 each at par.

On 15 December 2014, the Company issued 50.000 additional ordinary shares of €1 each, at a premium of €499 each.

On 29 December 2014, the Company issued 38.493 additional ordinary shares of €1 each, at a premium of €499 each.

On 24 July 2015, the Company issued 11.507 additional ordinary shares of €1 each, at a premium of €499 each.

Following the above, as at 31 December 2017 and 2016, the Bank had a total issued share capital of 101.000 ordinary shares of nominal value of €1 each, at a total premium of €49.900.000.

23. Revaluation reserve

	2017	2016
Investments fair value reserve	**€**	€
1 January	**(172)**	-
Revaluation of investments available-for-sale	**17.364**	(172)
31 December	**17.192**	(172)

The fair value reserve for investments represents accumulated gains and losses arising on the revaluation of available-for-sale financial assets that have been recognised in other comprehensive income, net of amounts reclassified to profit or loss when those assets have been disposed of or are determined to be impaired.

24. Accumulated losses

The only reserves available for distribution as dividend are retained earnings. In 2017 and 2016, no dividends were paid nor declared to be paid since the Bank had accumulated losses.

Companies which do not distribute 70% of their profits after tax, as defined by the Special Contribution for the Defence of the Republic Law, during the two years after the end of the year of assessment to which the profits refer, will be deemed to have distributed this amount as dividends. Special contribution for defence at 17% will be payable on such deemed dividends to the extent that the ultimate shareholders at the end of the period of two years from the end of the period of assessment to which the profits refer are both Cyprus tax residents and domiciled. The deemed distribution provisions do not apply if the ultimate shareholders are either non-Cyprus tax residents or non-Cyprus domiciled. The amount of deemed dividend distribution is reduced by any actual dividends paid out of the profits of the relevant year at any time. This special contribution for defence is payable by the Bank for the account of the shareholders.

The Bank incurred losses in 2015 and, as a result, no special defence contribution in relation to deemed dividend distribution was payable in the current year.

25. Analysis of assets and liabilities by expected maturity

	2017			2016		
	Less than one year	**Over one year**	**Total**	Less than one year	Over one year	Total
	€	**€**	**€**	€	€	€
Assets						
Cash and balances with Central Bank	**20.164.025**	**-**	**20.164.025**	34.798.717	-	34.798.717
Placements with banks	**2.615.172**	**-**	**2.615.172**	5.687.390	-	5.687.390
Loans and advances to customers	**4.270.917**	**59.007.303**	**63.278.220**	1.912.309	22.687.526	24.599.835
Investments available-for-sale	**-**	**2.212.743**	**2.212.743**	-	302.807	302.807
Investments held-to-maturity	**-**	**4.229.770**	**4.229.770**	4.498.972	3.899.268	8.398.240
Other assets	**1.424.749**	**-**	**1.424.749**	1.197.917	-	1.197.917
Property and equipment	**-**	**5.007.477**	**5.007.477**	-	3.121.056	3.121.056
Intangible assets	**415.509**	**470.637**	**886.146**	-	1.286.111	1.286.111
	28.890.372	**70.927.930**	**99.818.302**	48.095.305	31.296.768	79.392.073
Liabilities						
Customer deposits	**23.087.343**	**36.522.599**	**59.609.942**	10.044.705	27.477.130	37.521.835
Other borrowings	**67.162**	**2.937.575**	**3.004.737**	-	-	-
Other liabilities	**1.577.920**	**70.549**	**1.648.469**	664.247	-	664.247
	24.732.425	**39.530.723**	**64.263.148**	10.708.952	27.477.130	38.186.082

25. Analysis of assets and liabilities by expected maturity (continued)

The main assumptions used in determining the expected maturity of assets and liabilities are set out below:

- Loans and advances to customers are classified based on their expected repayment schedule. Overdraft accounts are classified in the over one year time band. Accumulated provisions for impairment on loans and advances are classified in the over one year time band.
- Investments held-to-maturity and investments available-for-sale are classified in the relevant time band based on expectations as to their realisation. In most cases, this is the maturity date, unless there is an indication that the maturity will be prolonged or there is an intention to sell, roll or replace the security with a similar one.
- Customer deposits are classified based on contractual maturity date. Current and savings accounts are classified in the over one year time band.
- Other borrowings are classified based on their expected repayment schedule.
- The expected maturity of all other assets and liabilities is the same as their contractual maturity. If they do not have a contractual maturity, the expected maturity is based on the timing the asset is expected to be realised and the liability is expected to be settled. Accumulated provisions for financial guarantees and commitments are classified in the over one year time band.

26. Operating leases

Commitments under operating leases are as follows:

Software licences

	2017	2016
	€	€
Within one year	**51.349**	51.349
Between two and five years	**51.349**	102.698
	102.698	154.047

Properties

	2017	2016
	€	€
Within one year	**332.300**	318.000
Between two and five years	**1.583.350**	1.478.450
Over five years	**1.187.850**	1.625.050
	3.103.500	3.421.500

The Bank's commitments for lease of properties and software licences depend on the provisions of the relevant operating lease agreements. These agreements contain provisions for future adjustments on the lease payments and allow the renewal of the agreements upon expiry. Agreements in respect of software licences are non-cancellable, while agreements in respect of properties are cancellable upon notice.

27. Net cash flow from operating activities

	2017	2016
	€	€
Loss before tax	**(5.668.173)**	(5.435.516)
Adjustments:		
Depreciation and amortisation of property, equipment and intangible assets	**1.070.142**	939.749
Provisions for impairment of loans and advances and other credit facilities	**312.568**	66.580
Income accrued but not received	**(132.005)**	(68.649)
Expenses accrued but not paid	**137.441**	45.888
	(4.280.027)	(4.451.948)
Increase in operating assets:		
Loans and advances to customers	**(38.920.404)**	(24.618.748)
Other assets	**(226.832)**	(695.046)
	(43.427.263)	(29.765.742)
Increase in operating liabilities:		
Customer deposits	**22.088.107**	32.934.156
Other borrowings	**3.004.737**	-
Other liabilities	**984.222**	60.122
Net cash flow (used in) / from operating activities	**(17.350.197)**	3.228.536

28. Cash and cash equivalents

	2017	2016
	€	€
Cash and balances with the Central Bank (*Note 11*)	**20.164.025**	34.798.717
Placements with banks (*Note 12*)	**2.615.172**	5.687.390
	22.779.197	40.486.107

At 31 December 2017, placements with the Central Bank amounted to €16.769.645 (2016: €32.757.219).

29. Risk management

In the ordinary course of the business, the Bank is exposed to various risks, which are managed and monitored through a continuous process of identification, measurement, and monitoring to prevent undue risk concentrations. The risk management policies employed by the Bank to manage these risks are discussed below.

Credit risk

Credit risk is the risk created primarily from credit facilities, trading and treasury management if one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

29. Risk management (continued)

Credit risk (continued)

The Risk Management department has the responsibility to identify, evaluate and assess the credit risk of the Bank and the responsibility to make proposals on the management of and controls on credit risk through various mechanisms on the basis of the strategic goals as determined by the Board of Directors. It recommends establishing and developing credit policies and procedures based on European and local directives and adjusts internal policies and procedures as appropriate.

The Risk Management department sets the procedure for granting of credit facilities to customers of the Bank according to the Bank's Risk Appetite Statement as set by the Board of Directors. Additionally, the Risk Management department sets limits and principles of financing and assesses the new banking products and new banking activities of the Bank.

The approval process of credit facilities aims in minimising credit risk by evaluating the creditworthiness of the counterparty, the collateral offered and the type of credit facility. Emphasis is given on the customer's repayment ability and any collaterals assigned act as a fall-back position in times of financial difficulties. Credit risks from connected customer accounts are consolidated and monitored on a single customer group basis.

Credit Granting and Review Processes

In March 2016, the Central Bank of Cyprus ('CBC') issued a Directive on Credit Granting and Review Processes. The provisions of this Directive are applicable to all Authorised Credit Institutions ('ACIs') and credit institutions that operate in the Republic of Cyprus under Section 10A of the Business of Credit Institutions Laws of 1997 to 2013.

The basic principle when assessing or reviewing a loan is that the value of collateral is not a decisive factor in the ACI's assessment of a loan application. Collateral could only serve as a secondary source of repayment, and as such it shall be assessed.

The decisive / overriding criterion for granting a credit facility is the borrower's ability to repay the credit facility within the approved time limit. It is noted that when assessing the borrower's repayment ability, any recourse to collateral or to guarantors' income shall not be taken into account.

Monitoring of the lending portfolio

The Bank's portfolio is continuously monitored in order to avoid undertaking high risks when granting credit facilities and in their subsequent duration. When granting loans and advances to customers, the Bank uses an internal evaluation and rating system, so as the customer's rating is representative of the credit risk involved.

The Bank's policy regarding the identification of impaired loans and advances and the methodology employed to determining the impairment provisions is set out in Note 2.

The Bank prepares all reports relating to the control of credit risk at fixed intervals. The Risk Management department communicates credit risk issues to the Board of Directors through its Risk Committee on a quarterly basis. Standardised reports to the Regulatory & Banking Supervision Department of the CBC are sent on a monthly and quarterly basis according to each report's requirements.

Arrears Management Process

In April of 2015, the CBC issued the Directive on Arrears Management and the Code of Conduct on the Handling of Borrowers in Financial Difficulties (the 'Code'), which set out the framework that all banks must use when dealing with customers in excesses/arrears or in pre-arrears. It requires ACIs to handle all such cases with the ultimate objective of reinstating, where possible, the sustainable ability of borrowers to meet their credit obligations.

29. Risk management (continued)

Arrears Management Process (continued)

The Code is intended to support and facilitate a meaningful interaction between ACIs and eligible borrowers, with the ultimate goal of achieving a fair and sustainable restructuring, where possible. The code of conduct applies to all borrowers, physical and legal persons, and for any kind of borrowing and the framework on arrears aims to support and find solution for the Bank's customers who are in arrears, or are at risk of going into arrears. To this effect, the Code clearly outlines, inter alia, the responsibilities of the ACIs in the arrears management process. It, also, makes a clear distinction between cooperative and non-cooperative borrowers with the focus on a consensual and voluntary restructuring.

According to the Directive on Arrears Management, ACIs shall lay down effective processes and mechanisms in order to enable timely reaction in the event that the restructuring conditions and / or milestones are not being met and / or the financial situation of the borrower has materially changed. ACIs shall cascade the processes including legal and other measures to be undertaken for cases where sustainable viability cannot be achieved or the borrower is no longer cooperating.

A "borrower in financial difficulties" means a borrower whose financial position has deteriorated to an extent that he / she is or may in the foreseeable future be unable to service his / her credit facilities, in accordance with the contractual repayment program. A borrower is defined as "non-cooperative" when a warning letter has been sent to the borrower and the borrower did not carry out the actions specified in that letter and any of the following conditions apply:

- the borrower does not fully and honestly disclose to the Bank relevant and material information that would have a significant impact on the assessment of the borrower's repayment ability, or
- the borrower does not provide the relevant information and / or documentation as requested by the Bank for the assessment of the financial position of the borrower, within a determined by the Bank time limit, or
- the duration of the contact between the Bank and borrower after the first communication of the Bank on its decision for a proposed solution or solutions exceeds the 14-day time limit due to the borrower's culpability, or
- 90 days elapse:
    a. where the borrower has failed to meet his / her contractual payments in full and has not entered into a workout arrangement, or
    b. where the borrower does not contact or does not respond to contacts and notifications initiated by the Bank, or the borrower does not take collaborative steps with the credit institution to develop a restructuring plan.

The effective management of arrears of viable borrowers in financial difficulties is an essential component of the credit institution's risk management, particularly in a distressed environment. The objective of arrears management is to reduce credit risk and avoid further deterioration of the financial position of the borrower, with the ultimate objective of reinstating, where possible, the sustainable ability of borrowers to meet their credit obligations.

The Risk Management department has the responsibility of ensuring that appropriate skills and systems are in place for the effective management of credit facilities in arrears and the conduct of feasible and sustainable debt restructuring in accordance with the European Commission's Implementing Regulation 2015/227.

29. Risk management (continued)

Maximum exposure to credit risk

The table below shows the maximum exposure to credit risk, without taking into account any collateral held, as well as any other credit enhancements.

	2017	2016
	€	€
Balances with the Central Bank (*Note 11*)	**16.769.645**	32.757.219
Placements with banks (*Note 12*)	**2.615.172**	5.687.390
Loans and advances to customers net of provisions for impairment (*Note 13*)	**63.278.220**	24.599.835
Investments available-for-sale (*Note 14*)	**2.212.743**	302.807
Investments held-to-maturity (*Note 15*)	**4.229.770**	8.398.240
Other assets (*Note 16*)	**1.424.749**	1.197.917
Total on statement of financial position	**90.530.299**	72.943.408
Undisbursed loan facilities	**12.655.496**	3.619.739
Undrawn overdraft facilities	**3.828.611**	1.292.910
Letters of guarantee	**1.858.333**	477.103
Unutilised trade finance limits	**2.338.460**	-
Total off-balance sheet position (*Note 33)*	**20.680.900**	5.389.752
Provisions for financial guarantees and commitments (*Note 21*)	**(70.549)**	-
Off-balance sheet position net of provisions for impairment	**20.610.351**	5.389.752
Total credit exposure	**111.140.650**	78.399.740

Credit risk concentration

According to the EU Regulation 575/2013, a large exposure is defined as the Bank's exposure to a client or group of connected clients which is equal or exceeds 10% of eligible capital. The Bank should not incur an exposure to a client or group of connected clients the value of which exceeds 25% of the Bank's eligible capital, after taking into account the effect of credit risk mitigation.

The Bank has not provided any credit facilities to Board of Directors and their connected persons or shareholders with direct or indirect ownership of more than 10% of the Bank and their connected persons for the reported financial year.

As eligible capital will be gradually allocated towards the Bank's operations as required, the Bank monitors allocations so that regulatory limits are not breached. The Bank exceeds the 25% threshold of eligible capital prior to credit risk mitigation with its exposure on its TARGET2 account kept with CBC. As these exposures take a 0% risk weight, there is no breach of the 25% threshold post credit risk mitigation.

Collateral and other credit enhancements

As at 31 December 2017, the main types of collateral obtained by the Bank consisted of property mortgages, cash, motor vehicles, as well as, life insurance policies, fixed and floating charges, assigned receivables and contracts of sale.

29. Risk management (continued)

Credit quality of loans and advances to customers

	2017	2016
Performing	**€**	€
Neither past due nor impaired	**63.253.591**	24.489.357
Past due but not impaired:		
- Up to 30 days	**323.904**	177.058
- 31 to 60 days	**-**	-
- 61 to 90 days	**9.324**	-
	63.586.819	24.666.415
Provisions for impairment of loans and advances (*Note 13*)	**(308.599)**	(66.580)
	63.278.220	24.599.835

Non-Performing

No loans have been assessed as non-performing loans as at 31 December 2017 (2016: €nil).

The credit quality of performing loans and advances to customers that were neither past due nor impaired is managed by the Bank using internal credit ratings.

The Bank has internally developed two credit rating systems, one for individuals and one for businesses. Both systems use qualitative (e.g. occupation, industry, etc.) and quantitative (e.g. days in arrears, length of credit history, etc.) information to calculate a score ranging from 1 to 10. The Bank uses five credit rating bands with Band 1 indicating a very low credit risk profile while Band 5 a very high risk profile for both individuals and businesses.

The Bank recognises the inherent limitations of the internal credit rating system due to its limited operational history. Thus, the Bank will continuously monitor the performance of the credit rating model along with actual performance of borrowers in order to continuously improve the model as new information becomes available.

Neither past due nor impaired performing loans and advances to customers

The table below shows the credit quality of performing loans and advances to customers that were neither past due nor impaired based on the Bank's credit rating system.

	2017	2016
	€	€
Band 1	**6.579.665**	6.044.971
Band 2	**31.510.668**	15.659.066
Band 3	**24.084.776**	2.775.427
Band 4	**1.078.482**	9.893
Band 5	**-**	-
	63.253.591	24.489.357
Provisions for impairment of loans and advances	**(306.734)**	(66.334)
	62.946.857	24.423.023

29. Risk management (continued)

Past due but not impaired performing loans and advances to customers

The table below shows the credit quality of performing loans and advances to customers that were past due but not impaired based on the Bank's credit rating system.

	2017	2016
	€	€
Band 1	85.212	174.684
Band 2	229.184	2.374
Band 3	18.832	-
Band 4	-	-
Band 5	-	-
	333.228	177.058
Provisions for impairment of loans and advances	(1.865)	(246)
	331.363	176.812

Facilities shown as past due but not impaired as at 31 December 2017 represent 9 facilities in total, with actual arrears amount of €5.426 which has been fully settled since (2016: 1 facility with 1 day in arrears).

Collateral on performing loans and advances

The fair value of collateral held by the Bank in respect of performing loans and advances to customers as at 31 December 2017 amounted to €167.335.766 (2016: €59.983.992).

Credit ratings from independent rating agencies

Balances with the CBC and placements with banks are analysed in accordance with Standard & Poor's ('S&P') rating agency as follows:

	2017	2016
	€	€
AAA to BBB	19.384.817	38.359.040
CCC+ to CCC-	-	85.569
	19.384.817	38.444.609

Bonds and other investments portfolios are analysed in accordance to S&P rating agency as follows:

	2017	2016
	€	€
AAA to BB	6.442.513	8.701.047

29. Risk management (continued)

Credit ratings from independent rating agencies (continued)

	2017	2016
	€	€
Issued by:		
Cyprus government	**530.033**	5.040.663
Other European governments	**1.337.394**	964.228
Financial corporations	**2.211.483**	606.820
Non-financial corporations	**2.363.603**	2.089.336
	6.442.513	8.701.047
Classified as:		
Investments available-for-sale	**2.212.743**	302.807
Investments held-to-maturity	**4.229.770**	8.398.240
	6.442.513	8.701.047

Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. Interest rate risk arises as a result of timing differences on the repricing interest rates of assets and liabilities.

Interest rate risk is measured, monitored and controlled using interest rate sensitivity gap analysis estimating the difference between assets and liabilities for which interest rates are repriced in each time band, separately for each currency. This difference is multiplied by the respective assumed change in interest rates for the period from the repricing date until twelve months from the date of the analysis, in order to estimate the impact on annual revenues of any changes in interest rates for the next twelve months for each currency.

Currency risk

Currency risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates. Currency risk arises when future commercial transactions and recognised assets and liabilities are denominated in a currency that is not the Bank's measurement currency. The Bank is exposed to foreign exchange risk arising from various currency exposures. Exchange rate fluctuations are managed by the Bank's Treasury department and monitored by the Risk Management department. The Bank's foreign exchange exposure is communicated to senior management on a monthly basis and to the Board of Directors through its Risk Committee.

There are no materially open positions in any foreign currency, and consequently the impact on net loss and equity of reasonably possible changes in exchange rates is not expected to be significant.

Liquidity risk

Liquidity risk is the risk that the Bank is unable to fully or promptly meet current and future payment obligations as and when they fall due. This risk includes the possibility that the Bank may have to raise funding at higher cost or sell assets at a discount.

It reflects the potential mismatch between incoming and outgoing payments, taking into account unexpected delays in repayment or unexpectedly high payment outflows. Liquidity risk involves both the risk of unexpected increases in the cost of funding of the portfolio of assets and the risk of being unable to liquidate a position in a timely manner on reasonable terms.

29. Risk management (continued)

Liquidity risk (continued)

The Bank has developed monitoring tools for treasury operations in order to manage, amongst others, liquidity risk and cash flows and will continue to improve such tools as its operations become more complex. In addition, the Bank has set a limit structure for treasury placements that promotes diversity of exposures and to assist in monitoring the Bank's risk profile against its risk appetite.

The Bank`s Treasury department is responsible for managing liquidity and to ensure compliance with internal and regulatory liquidity policies and provide direction as to the actions to be taken regarding liquidity availability. The Asset and Liability Committee reviews the liquidity position on a monthly basis and takes the necessary actions to enhance the Bank's liquidity position.

Monitoring Process

It is also important that Treasury monitors cash flows and highly liquid assets in addition to the supervisory liquidity ratios to ensure the uninterrupted operation of the Bank's activities. The Bank`s Treasury department submits a report to the CBC on a daily basis indicating the cash inflows and outflows observed in customer balances and other balances, as well as the opening and closing balances of cash (banknote balances, nostro balances and any overnight money market balances). Moreover, the Treasury department prepares a weekly report of Euro and foreign currency liquidity mismatch which is submitted to the CBC.

Main Refinancing Operations

For prudency and in order to have access to various liquidity sources, the Bank maintains an available credit line with CBC under the relevant Main Refinancing Operations framework. The amount of the credit line available to the Bank is linked / dependent to the value of assets declared by the Bank for such purpose. The Bank has declared assets with a nominal value of €2.100.000 as at 31 December 2017 (2016: €1.273.000), which will enable it, upon request, access to such facilities in line with the provisions of the aforementioned scheme.

As the credit line has not been utilized by 31 December 2017, such assets are not considered encumbered in any manner.

Liquidity ratios

The calculation of prudential liquidity in Euro and other currencies for supervisory purposes was a local regulatory liquidity requirement which was being submitted to the CBC on a quarterly basis, while additional information in relation to liquidity was submitted on a weekly basis. Until 15 September 2017, the minimum percentage of liquid assets was 20% of total Euro deposits while the respective percentage for foreign currencies was 70%. From 15 September until 31 December 2017, the minimum percentage of liquid assets was reduced to 18% of total Euro deposits while the respective percentage for foreign currencies was reduced to 50%.

The prudential liquidity ratio in Euro was as follows:

	2017	2016
	%	%
End of reporting period	**68,52**	123,75
Average for the year	**88,80**	190,28
Maximum ratio for the year	**122,04**	244,55
Minimum ratio for the year	**65,77**	123,75

29. Risk management (continued)

Liquidity risk (continued)

The prudential liquidity ratio in foreign currencies, which is calculated using data denominated in foreign currencies other than the Euro, was as follows:

	2017	2016
	%	%
End of reporting period	**180,57**	181,29
Average for the year	**201,54**	183,70
Maximum ratio for the year	**253,17**	303,02
Minimum ratio for the year	**173,46**	100,40

The Bank also calculates the Liquidity Coverage Ratio (LCR) based on the Delegated Regulation (EU) 2015/61 and submits it to the CBC on a monthly basis. The LCR is designed to establish a minimum level of high-quality liquid assets sufficient to meet an acute stress scenario lasting for 30 calendar days. During 2017 the minimum requirement was 80% (2016: 70%) and increased to 100% as of 1 January 2018.

The LCR ratio was as follows:

	2017	2016
	%	%
End of the reporting period	**387,97**	435,70
Average for the year	**350,14**	1.527,80
Maximum ratio for the year	**507,33**	2.586,64
Minimum ratio for the year	**272,31**	435,70

As at 31 December 2017, the Bank was in compliance with the above regulatory liquidity requirements.

The local prudential liquidity requirements in Euro and other currencies were abolished on 1 January 2018 as per Article 412(5) of EU Regulation No 575/2013. To this purpose, in December 2017, the CBC introduced a macroprudential measure in the form of a liquidity add-on that was imposed on top of the LCR and which became effective on 1 January 2018 and expected to apply until 31 December 2018. Despite the abolishment, the Bank continues to submit prudential liquidity data to CBC for informational purposes.

The objective of the measure is to ensure that there will be a gradual release of excess liquidity arising from the shift to a single liquidity requirement framework. The add-on applies stricter outflow and inflow rates on some of the parameters used in the calculation of the LCR than the ones defined in the Commission Delegated Regulation (EU) 2015/61, as well as, additional liquidity requirements in the form of outflow rates on other items that are not subject to any outflow rates as per the relevant Regulation.

The measure will be implemented in two stages. The first stage requires stricter outflow and inflow rates which are applicable from 1 January 2018 until 30 June 2018. The second stage, applicable from 1 July 2018 until 31 December 2018, requires more relaxed outflow and inflow rates compared to the initial ones through the reduction of 50% of the LCR add-on rates. The CBC may propose to modify or extend the period of application of this macroprudential measure depending on the results of the follow-up of the banks' actions on how the excess liquidity is utilised. As at 31 December 2017, the Bank was in compliance with the LCR add-on implemented on 1 January 2018.

29. Risk management (continued)

Liquidity risk (continued)

Additionally to the LCR, the Bank calculates and submits to CBC on a quarterly basis the Net Stable Funding Ratio (NSFR). NSFR, defined as the ratio of available stable funding relative to required stable funding, was not introduced as a regulatory requirement on 1 January 2018 as originally expected. The minimum requirement of NSFR will be 100%. At 31 December 2017 the Bank's NSFR was at 159% (2016: 294%).

Analysis of financial liabilities by remaining contractual maturity

	Carrying amount	Contractual cash flows	On demand and up to 1 month	Between 1 and 3 months	Between 3 months and 1 year	Between 1 and 5 years	More than 5 years
	€	€	€	€	€	€	€
Year 2017							
Customer deposits	59.609.942	59.734.447	37.471.498	3.988.738	18.274.211	-	-
Other borrowings	3.004.737	3.236.461	10.410	-	71.836	378.478	2.775.737
Other liabilities	1.648.469	1.648.469	1.455.751	24.733	58.212	-	109.773
	64.263.148	**64.619.377**	**38.937.659**	**4.013.471**	**18.404.259**	**378.478**	**2.885.510**
Year 2016							
Customer deposits	37.521.835	37.573.923	28.059.524	3.069.467	6.444.932	-	-
Other liabilities	664.247	664.247	392.219	-	272.028	-	-
	38.186.082	**38.238.170**	**28.451.743**	**3.069.467**	**6.716.960**	**-**	**-**

The table above presents the Bank's financial liabilities based on undiscounted cash flows, analysed in time bands according to the number of days remaining from 31 December until the contractual maturity date. Repayments for which notice should be given, have been placed in the relevant time bands, as if notice had been given on 31 December. The amounts in this table may not be equal to the amounts in the statement of financial position since the table above presents all cash flows (including interest) on an undiscounted basis.

29. Risk management (continued)

Liquidity risk (continued)

Analysis of contingent liabilities and commitments by remaining contractual maturity

	Contractual cash flows €	On demand and up to 1 month €	Between 1 and 3 months €	Between 3 months and 1 year €	Between 1 and 5 years €	More than 5 years €
Year 2017						
Letters of guarantee	1.858.333	109.000	105.219	364.680	1.206.456	72.978
Unutilised trade finance limits	2.338.460	-	-	-	2.338.460	-
Undisbursed loan facilities	12.655.496	-	-	1.294.698	11.360.798	-
Undrawn overdraft facilities	3.828.611	3.828.611	-	-	-	-
	20.680.900	**3.937.611**	**105.219**	**1.659.378**	**14.905.714**	**72.978**
Year 2016						
Letters of guarantee	477.103	-	4.801	433.756	23.935	14.611
Undisbursed loan facilities	3.619.739	-	-	11.800	3.607.939	-
Undrawn overdraft facilities	1.292.910	1.292.910	-	-	-	-
	5.389.752	**1.292.210**	**4.801**	**445.556**	**3.631.874**	**14.611**

The table above presents the Bank's contingent liabilities and commitments to lend based on undiscounted cash flows, analysed in time bands according to the number of days remaining from 31 December until the contractual maturity date or the date assumed to materialise into a liability for the Bank to pay. The main assumptions used in determining the appropriate time band for classification are set out below:

- Letters of guarantee are classified based on their contractual maturity date.
- Unutilised trade finance limits do not carry a contractual maturity date and are classified based on the date which the Bank intends to perform a review of the respective facilities.
- Undisbursed loan facilities are classified based on the maximum allowable period for the customer to withdraw the remaining balance in accordance with the contractual terms of the facility. The allowable period does not exceed 2 years. The Bank reserves the right to cancel any remaining balance after the elapsing of the allowable period by giving relevant notice to the customers.
- Undrawn overdraft facilities are classified as on demand given that there are no restrictions in respect of their utilisation.

Operational risk

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal, conduct and reputational risk.

Regulatory risk

The Bank's operations are supervised by the CBC and the European Central Bank ('ECB') as a supervisory body for all the banks in the Eurozone area (referred to as the Single Supervisory Mechanism, or SSM). The ECB exercises its supervisory responsibilities in cooperation with the national central banks. Future changes in the legal or regulatory obligations as a result of arrangements made by either ECB or CBC, may impact the Bank's operations.

29. Risk management (continued)

Intensity of competition

The operational environment of the Bank is highly competitive. Competition arises from commercial banks, cooperative credit institutions and international banking units. Any intensification of competition as a result of more competitive interest rates being offered on deposits and advances compared to those offered by the Bank, may create pressure on the Bank's profitability.

Litigation risk

Litigation risk is the risk of financial loss, interruption of the Bank's operations or any other undesirable situation that arises from the possibility of non-execution or violation of legal contracts and consequentially of lawsuits. The risk is restricted through the contracts used by the Bank to execute its operations.

Political and other risks

External factors which are beyond the control of the Bank, such as political developments and government actions (i.e. the ongoing unresolved political issue in Cyprus, political and social unrest or military conflict in neighbouring countries) may adversely affect the operations of the Bank, its strategy and prospects.

Given the above, the Bank recognises that unforeseen political events can have negative impact on Bank's activities, operating results and position.

Furthermore, the general economic environment prevailing in Cyprus and internationally may affect the Bank's operations to a great extent. Economic conditions such as inflation, unemployment, and development of the gross domestic product are directly linked to the economic course of every country and any variation in these and the economic environment in general may create chain reactions in all areas hence affecting the Bank.

Given the above, the Bank recognises that unforeseen political events can have negative effects on the fulfilment of contractual relationships and obligations of its customers and other counterparties which may result in a negative impact on Bank's activities, operating results and position.

30. Capital management

The main regulator that sets and monitors capital requirements for the Bank is the CBC.

As from 1 January 2014, the new Basel III Framework known as Capital Requirement Regulation ('CRR') 575/2013 / Capital Requirement Directive IV ('CRD IV') dated 26 June 2013 became effective. CRR establishes the prudential requirements for capital, liquidity and leverage that entities need to abide by. CRD IV governs access to deposit-taking activities, internal governance arrangements including remuneration, board composition and transparency.

In November 2016, the European Commission published its first proposals for revised rules to calibrate capital and liquidity requirements, in the form of a Directive and a Regulation known as CRD V and CRR II, as well as amendments to the Bank Recovery and Resolution Directive, to implement global standards for total loss absorbing capital.

Basel III Framework comprises of three Pillars:

- Pillar 1 – Minimum capital requirements
- Pillar 2 – Internal capital and liquidity assessment and supervisory review process
- Pillar 3 – Market discipline

30. Capital management (continued)

Pillar 1 – Minimum capital requirements

Pillar 1 sets forth the guidelines for calculating the minimum capital requirements to cover the credit risk, the market risk and the operational risk.

The Bank uses the Standardised Approach for the calculation of minimum capital requirements against credit risk and the financial collateral simple method for credit risk mitigation purposes. The Simplified Approach is used for the calculation of own fund requirements for commodity risk for each commodity exposure category. The Bank adopts the Basic Indicator Approach for the calculation of capital regarding operational risk.

Pillar 2 – Supervisory review process

Pillar 2 aims to enhance the link between an institution's risk profile, its risk management and risk mitigation systems, and its capital planning. The process can be divided into two major components:

- An internal assessment by the institution on internal governance, risk management, stress testing frameworks, business model and strategy, known as Internal Capital and Liquidity Adequacy Assessment Process ('ICAAP / ILAAP')
- A supervisory review and evaluation process ('SREP'), of which its key purpose is to ensure that institutions have adequate arrangements, strategies, processes and mechanisms, as well as capital and liquidity to ensure a sound management and coverage of their risks to which they are or might be exposed to. This includes risks arising from stress testing exercises and risks an institution may pose to the financial system.

The Bank has prepared and submitted its first ICAAP / ILAAP report in 2016 and has submitted its 2017 report in March 2018. Until the date of signing of these financial statements, the Bank has not received any notification or requirements regarding SREP.

Pillar 3 – Market discipline

Pillar 3 sets out required disclosures to allow market participants to assess key pieces of information relevant to the capital structure, risk exposures, risk assessment processes and hence the capital adequacy of the Bank.

Based on EU Regulation 575/2013, disclosures by banks include information relating to their risk management objectives and policies, the composition of own funds and original and supplementary funds, their compliance with minimum capital requirements and the internal capital adequacy assessment process.

The Bank closely monitors its capital adequacy both for compliance with the requirements of the supervisory authority as well as to maintain a base to support and develop its activities and safeguard the interests of its shareholders.

Pillar 3 disclosures are published on the Bank's website in conjunction with the financial statements.

30. Capital management (continued)

<u>Capital position as per CRR / CRD IV</u>

At 31 December 2017, the Bank fully meets the minimum capital requirements.

The information presented below represents the Bank's capital position under CRR / CRD IV, including the application of the transitional arrangements as set by the CBC.

	31 December 2017 €	31 December 2016 €
Common Equity Tier 1 capital	**34.790.122**	39.918.622
Additional Tier 1 capital	**-**	-
Tier 1 capital	**34.790.122**	39.918.622
Tier 2 capital	**-**	66.580
Total Regulatory Capital	**34.790.122**	39.985.202
Risk weighted assets - credit risk	**41.010.469**	19.632.693
Risk weighted assets - operational risk	**933.789**	1.555.000
Risk weighted assets - market risk	**-**	-
Total Risk Weighted Assets	**41.944.258**	21.187.693
Common Equity Tier 1 ratio	**82,94%**	188,40%
Tier 1 ratio	**82,94%**	188,40%
Total capital ratio	**82,94%**	188,72%
Minimum Ratios as per the CRR / CRD IV		
Common Equity Tier 1 ratio	**4,50%**	4,50%
Tier 1 ratio	**6,00%**	6,00%
Total capital ratio	**8,00%**	8,00%

Following the enactment of the amendments in the Cypriot Banking Law in February 2017 regarding the gradual phase-in of the Capital Conservation Buffer (CCB), the CCB as of 1 January 2017 was 1,25% (1 January 2016: 0,625%). As a result, the Bank's minimum Common Equity Tier 1 (CET1) ratio including CCB phase-in arrangements was 5,75% in 2017 (2016: 5,125%) and the overall Total Capital Ratio including CCB phase-in arrangements was 9,25% in 2017 (2016: 8,625%).

In accordance with the phase-in arrangements of CCB, the CET1 ratio will gradually reach 7,0% as of 1 January 2019, while the Total Capital Ratio will gradually reach 10,5% as of 1 January 2019, both including CCB on a fully loaded basis.

31. Related party transactions

In accordance with IAS 24 *Related Party Disclosures*, parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form. Related parties may enter into transactions which unrelated parties might not, and transactions between related parties may not be effected on the same terms, conditions and amounts as transactions between unrelated parties.

The Bank is a subsidiary of Ancoria Investments Plc, which is incorporated in Cyprus and holds 100% of the Bank's issued share capital. Ancoria Investments Plc is owned by several legal entities as well as natural persons, and has no other significant activity, assets or liabilities other than its holding in the Bank.

The shareholders of Ancoria Investments Plc as at the date of signing of these financial statements and as at 31 December 2017 and 2016 are listed below:

Name / relationship	**Percentage of Share Capital in the parent company**	
	Date of signing this report and 31 December 2017	**31 December 2016**
	%	**%**
Bo Sievert Larsson	41,00	40,40
Ancoria Insurance Ltd	20,00	20,00
Sievert Larsson Scholarship Foundation	19,18	19,20
Other shareholders	19,82	20,40
	100,00	**100,00**

Participation of directors in the Company's share capital

The percentage of share capital of the Bank held indirectly by each member of the Board of Directors (through ownership interest in the immediate parent company) and their connected persons, as at 31 December 2017 and 31 December 2016 were as follows:

Name	**31 December 2017**	**31 December 2016**
	%	**%**
Ioannis Loizou	3,40	3,40
Evgenia Christodoulou	0,08	0,08
Bo Sievert Larsson	41,00	40,40
Charidemos Theocharides	0,23	0,23
Odysseas Christodoulou (resigned 6 June 2017)	N/A	0,80

31. Related party transactions (continued)

Connected persons include (i) spouses, (ii) minor children and (iii) companies in which company directors / other key management personnel hold, directly or indirectly, at least 20% of the voting power at a general meeting, or act as executive director or exercise control over the entities, in any manner.

Further to the above shareholdings, the Sievert Larsson Scholarship Foundation, founded by Mr. Bo Sievert Larsson, indirectly holds 38,6% (2016: 38,6%) of the Company's issued share capital.

	2017	2016
	€	€
Deposits		
Members of the Board of Directors and key management personnel	**1.409.483**	1.688.180
Parent company	**40.954**	-
Entity with significant influence	**17.977**	3.982
Other related parties	**3.097.933**	13.327.262
	4.566.347	15.019.424
Interest expense	**26.541**	28.622

	2017	2016
	€	€
Loans and advances		
Other related parties	**28**	6.857
Interest income	**31**	56

The above table does not include balances for members of the Board of Directors and their connected persons who resigned during the year. Interest income and expense is disclosed for the period during which they were members of the Board of Directors.

The amount of deposits placed by other related parties includes deposits from Ancoria Insurance Public Ltd (indirect shareholder) in the amount of €759.007 (2016: €2.769.006), as well as, deposits by members of the Board of Directors of Ancoria Insurance Public Ltd.

In addition to loans and advances, there were contingent liabilities and commitments in respect of members of the Board of Directors and their connected persons, mainly in the form of guarantees and commitments to lend amounting to €21.000 (2016: €23.143).

During 2017, the Bank recognised a total income amounting to €16.560 (2016: €13.800) as a result of a use of space agreement with Ancoria Insurance Public Ltd. This amount is shown under *Other income* line.

All transactions with non-executive members of the Board of Directors, the Bank’s shareholders and their connected persons are made on normal business terms as for comparable transactions with customers of a similar credit standing.

31. Related party transactions (continued)

Fees and emoluments of Directors and key management personnel

	2017	2016
	€	€
Non-executives		
Membership fees	**108.412**	107.459
Executives		
Salaries and other short-term benefits	**417.000**	321.000
Employer's contributions	**39.195**	40.455
	456.195	361.455
	564.607	468.914

The Bank considers only the two Executive directors as key management personnel.

Receivables from parent company (*Note 16*)

		2017	2016
Name	**Nature of transactions**	**€**	€
Ancoria Investments Plc	Current account balance	**88.745**	56.087
		88.745	56.087

The balance due from the parent company is interest free and does not have a specified repayment date. It concerns amounts paid on behalf of the parent company.

Rental of premises

On 2 December 2016, an entity controlled by directors of the Bank acquired the rented premises of the Bank in Limassol. The Bank consented to the sale agreement on the condition that its rights and obligations for the remaining term of its rental agreement, as well as any other rights and obligations of the Bank are retained and that a new agreement will be signed between the Bank, the previous and the current owners of the property by virtue of which the new owner will be bound by the existing rental terms towards the Bank. The said agreement was also signed on 2 December 2016.

The current rental agreement runs until June 2025 and the Bank has the obligation to pay rentals one year in advance, payable in July of each year. The monthly rentals stipulated in the agreement are as follows:

	€
Until 30 June 2018	10.000
From 1 July 2018 until 30 June 2019	12.000
From 1 July 2019 until 30 June 2021	14.000
From 1 July 2021 until 30 June 2025	18.000

The rental up to 30 June 2018 has been paid in advance. As at 31 December 2017, the prepaid rents to the current owner of the premises in Limassol amounted to €60.000.

On 20 December 2017, the Bank entered into an agreement to acquire its rented premises in Limassol. In accordance with the terms of the agreement, the Bank will pay a sum of €4.100.000 to the current owner in tranches. The consideration is considered to be at an arm's length based on supporting valuation reports provided by independent valuators.

31. Related party transactions (continued)

The first payment of €2.122.959 was made on 20 December 2017 and has been recognised under property and equipment along with the relevant stamp duty paid (Note 17). A second payment of €1.577.041 will follow as soon as the transfer of ownership of the premises to the Bank is completed, currently subject to the approval of the Land Registry. The residual amount of €400.000 will become payable upon issuance of the Certificate of Final Approval by the competent authorities and the transfer of the title deed in the name of the Bank.

32. Operating environment

During the last years, the Cyprus economy has been adversely affected by the crisis in the Cyprus banking system and the inability of the Republic of Cyprus to secure financing from international markets. As a result, the Republic of Cyprus entered into negotiations with the European Commission, the European Central Bank and the International Monetary Fund (the 'Troika'), for financial support of €10 billion, which resulted into an agreement and the Eurogroup decision of 25 March 2013. The decision included the restructuring of the two largest banks in Cyprus through bail-in, safeguarding deposits below €100.000.

Since March 2013, Troika performed several reviews of the Cyprus' economic program with very positive outcomes which resulted in the disbursement of all scheduled tranches of financial assistance to Cyprus. The final review by the Troika was successfully completed in March 2015 which signified the finalisation of the Memorandum of Understanding. Since the successful completion of the Memorandum, the three major credit rating agencies have upgraded Cyprus' sovereign at least two times each, signifying the positive developments in the Cypriot economy. In 2017, inflation returned to a positive figure of 0,5% after two consecutive years of deflation, which constitutes another sign of the stabilisation of the economy.

Despite the achieved growth rate of 3,9% of GDP in 2017, the economic conditions in Cyprus remain uncertain (unavailability of financing, high percentage of non-performing bank loans, high unemployment rates) and the full extent of the impact of the on-going financial crisis is proving to be difficult to anticipate or completely guard against. The political tensions in the eastern Mediterranean and Syria, as well as, the developments in the ongoing negotiations of the national problem provide additional elements of uncertainty.

Effects of developments

The Bank's management recognises the difficulties involved in predicting all developments which could have an impact on the Cyprus economy and consequently, what effect, if any, they could have on the future financial performance, cash flows and financial position of the Bank. The Bank's management will closely monitor all future developments in the economic and political environment it operates and take appropriate measures.

33. Contingent liabilities, capital commitments and off-balance sheet financing

Commitments and contingent liabilities consist of financial guarantees, letters of credit and other undrawn commitments to lend. Even though these obligations may not be recognised on-balance sheet, they do contain credit risk and are therefore part of the overall credit risk exposure of the Bank (Note 29).

An analysis of the Bank's off-balance sheet items is provided below:

	2017	2016
	€	€
Contingent liabilities		
Letters of guarantee	**1.858.333**	477.103
Unutilised trade finance limits	**2.338.460**	-
	4.196.793	477.103
Commitments		
Undisbursed loan facilities	**12.655.496**	3.619.739
Undrawn overdraft facilities	**3.828.611**	1.292.910
	16.484.107	4.912.649
	20.680.900	5.389.752

The Bank's commitments in respect of operating leases are presented in Note 26.

Capital commitments

As at 31 December 2017, there were no significant commitments for contracted capital expenditures of the Bank other than the residual amounts owed in accordance with the agreement for the acquisition of the rented premises in Limassol as mentioned in Note 31.

As a result, the total capital commitments of the Bank as at 31 December 2017 are €1.977.041 (2016: €nil).

Legal proceedings

As at 31 December 2017 and 2016, there were no pending litigation, claims or assessments against the Bank.

34. Events after the reporting date

There were no significant events after the end of the financial year which have a bearing on the understanding of the financial statements.

Independent auditor's report on pages 63 to 68.

Deloitte Limited
24 Spyrou Kyprianou Avenue
CY-1075 Nicosia, Cyprus
Mail: P.O.Box 21675
CY-1512 Nicosia, Cyprus

Tel: +357 22 360 300
Fax: +357 22 360 400
infonicosia@deloitte.com
www.deloitte.com/cy

Independent Auditor's report

To the Members of ANCORIA BANK LIMITED

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of **Ancoria Bank Limited** (the 'Bank'), which are presented in pages 6 to 62 and comprise the statement of financial position as at 31 December 2017, and the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Bank as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and the requirements of the Cyprus Companies Law, Cap. 113.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We remained independent of the Bank throughout the period of our appointment in accordance with the *International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code)* together with the ethical requirements that are relevant to our audit of the financial statements in Cyprus, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters incorporating the most significant risks of material misstatements, including assessed risk of material misstatements due to fraud

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

Independent Auditor's report (continued)

<table>
<tr><th>Key audit matter</th><th>How we examined the key audit matter</th></tr>
<tr><th colspan="2">Provisions for impairment of loans and advances to customers</th></tr>
<tr><td>
Loans and advances to customers amounted to €63.278.220 as at 31 December 2017 compared to €24.599.835 as at 31 December 2016, net of provisions for impairment of loans and advances to customers amounting to €308.599 as at 31 December 2017, compared to €66.580 as at 31 December 2016. Provisions for impairment of loans and advances to customers is an area which involves a high level of critical judgment by the Management of the Bank.
The measurement of the provisions for impairment of loans and advances to customers is considered a key audit matter as the determination of the assumptions used by Management in estimating the provisions is highly subjective due to the high degree of judgment applied by Management.
The Bank establishes an allowance for provisions for impairment of loans and advances to customers for incurred credit losses on both an individual and on a collective basis. The most significant judgements are:

Methodologies and policies selected by Management, valuation of collaterals and underlying assumptions in the discounted cash flows used for the individually assessed loans.
Methodologies and policies selected by Management as well as assumptions made to support the calculation of the collectively assessed loans including segmentation, the Probability of Default, Loss Given Default and Loss Emergence Period.

The disclosures regarding the provisions are included in notes 13 and 29 to the financial statements.
With effect from 1 January 2018, the Bank has adopted IFRS 9, resulting in credit losses being recognised when they are expected rather than when they have been incurred. Management has disclosed information regarding the estimated impact of IFRS 9 in Note 2.3.1.
</td><td>
Our audit procedures included the following:

The credit granting process of the Bank was compared with the Central Bank of Cyprus' requirements (based on applicable regulations and directives) to identify and assess the impact of any discrepancies.
The controls in place for the credit granting process were reviewed and their adequacy, in terms of design and implementation and operating effectiveness, was assessed.
We evaluated the appropriateness of the methodologies and policies chosen by Management in relation to the provisions for impairment of loans and advances to customers.
Based on our risk assessment we selected a sample of loans and advances to customers that had been individually assessed by the Bank for provisioning purposes and independently assessed the appropriateness of the results of the process followed by Management. In particular, we tested the reasonableness of significant assumptions used, and re-performed the discounted cash flow calculations, comparing our results with those arrived at by Management and investigated any differences arising.
In respect of collective assessment, through our credit risk specialists, we tested the arithmetical accuracy of the calculation performed by Management. As part of our testing, we reviewed and assessed the appropriateness of key assumptions and risk inputs used.
We assessed the completeness and accuracy of disclosures against the relevant accounting standards.

<u>Estimated impact of IFRS 9</u>
We have assessed the estimated impact of IFRS 9 with particular focus on the methodology, policies and assumptions used by Management to determine the expected future credit losses, with the assistance of our credit risk specialists. We also assessed the completeness and accuracy of IFRS 9 transitional disclosures.
</td></tr>
</table>

Deloitte.

Independent Auditor's report (continued)

Reporting on other information

The Board of Directors is responsible for the other information. The other information comprises the information included in the Management Report but does not include the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Board of Directors and those charged with governance for the Financial Statements

The Board of Directors is responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union and the requirements of the Cyprus Companies Law, Cap. 113, and for such internal control as the Board of Directors determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

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

Deloitte.

Independent Auditor's report (continued)

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

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

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

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

Independent Auditor's report (continued)

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters.

Report on Other Legal and Regulatory Requirements

Pursuant to the requirements of Article 10(2) of the EU Regulation 537/2014 we provide the following information in our Independent Auditor's Report, which is required in addition to the requirements of International Standards on Auditing.

Appointment of the Auditor and Period of Engagement

We were first appointed as auditors of the Bank on 20 February 2015 by the Bank's Board of Directors. Our appointment has been renewed annually by shareholders' resolution representing a total period of uninterrupted engagement appointment of 3 years.

Consistency of the Additional Report to the Audit Committee

We confirm that our audit opinion on the financial statements expressed in this report is consistent with the additional report to the Audit Committee of the Bank, which we issued on 23 April 2018 in accordance with Article 11 of the EU Regulation 537/2014.

Provision of Non-Audit Services

We declare that no prohibited non-audit services referred to in Article 5 of the EU Regulation 537/2014 and Section 72 of the Auditors Law of 2017 were provided. In addition, there are no non-audit services which were provided by us to the Bank and which have not been disclosed in the financial statements or the management report.

Other Legal Requirements

Pursuant to the additional requirements of the Auditors Law of 2017, we report the following:

- In our opinion, based on the work undertaken in the course of our audit, the management report has been prepared in accordance with the requirements of the Cyprus Companies Law, Cap. 113, and the information given is consistent with the financial statements.
- In light of the knowledge and understanding of the Bank and its environment obtained in the course of the audit, we are required to report if we have identified material misstatements in the management report. We have nothing to report in this respect.

Independent Auditor's report (continued)

Other Matter

This report, including the opinion, has been prepared for and only for the Bank's members as a body in accordance with Article 10(1) of the EU Regulation 537/2014 and Section 69 of the Auditors Law of 2017 and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whose knowledge this report may come to.

The engagement partner on the audit resulting in this independent auditor's report is Alexis Agathocleous.

Alexis Agathocleous
Certified Public Accountant and Registered Auditor
for and on behalf of
Deloitte Limited
Certified Public Accountants and Registered Auditors

Nicosia, 24 April 2018

Credit risk

In February 2014, the CBC issued to credit institutions the Directive on Loan Impairment and Provisioning Procedures of 2014 to 2016, which provides guidance to banks for loan impairment policy and procedures for provisions. The purpose of this Directive is to ensure that credit institutions have in place adequate provisioning policies and procedures for the identification of credit losses and prudent application of IFRSs in the preparation of their financial statements.

The Directive requires certain disclosures in relation to the loan portfolio quality, provisioning policy and levels of provision. The disclosures required by the Directive, in addition to those presented in the financial statements, are set out in the following tables.

Credit Risk (continued)

TABLE A: Analysis of the credit portfolio according to performance status for balances

As at 31 December 2017

	Gross carrying amount				Accumulated impairment			
		Of which non-performing exposures	Of which exposures with forbearance measures			Of which non-performing exposures	Of which exposures with forbearance measures	
				Of which non-performing exposures				Of which non-performing exposures
	€000	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Loans and advances	**63,587**				**309**			
General governments								
Other financial corporations								
Non-financial corporations	**16,485**				**168**			
Of which: Small and Medium-sized Enterprises	15,170				138			
Of which: Commercial real estate	10,586				111			
By sector								
Construction	2,242				30			
Wholesale and retail trade	3,040				24			
Real estate activities	3,839				52			
Accommodation and food service activities	310				5			
Transportation and storage	2,051				37			
Other sectors	5,003				20			
Households	**47,102**				**141**			
Of which: Residential mortgage loans	43.913				128			
Of which: Credit for consumption	3.189				13			

Credit Risk (continued)

TABLE A: Analysis of the credit portfolio according to performance status for balances (continued)

As at 31 December 2016

	Gross carrying amount				Accumulated impairment			
		Of which non-performing exposures	Of which exposures with forbearance measures			Of which non-performing exposures	Of which exposures with forbearance measures	
				Of which non-performing exposures				Of which non-performing exposures
	€000	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Loans and advances	**24,666**				**67**			
General governments								
Other financial corporations								
Non-financial corporations	**6,542**				**36**			
Of which: Small and Medium-sized Enterprises	6,538				32			
Of which: Commercial real estate	3,136							
By sector								
Construction	1							
Wholesale and retail trade	876				6			
Real estate activities	2,192							
Accommodation and food service activities	49							
Transportation and storage	470				1			
Other sectors	2,954				29			
Households	**18,124**				**31**			
Of which: Residential mortgage loans	17,054				15			
Of which: Credit for consumption	1,070				16			

Credit Risk (continued)

TABLE B: Analysis of the credit portfolio on the basis of their origination date* for balances

As at 31 December 2017

Total loans granted	Gross carrying amount of total loans			Loans to non-financial corporations			Loans to other financial corporations			Loans to households		
	Total	Non-performing	Accumulated impairment	Total	Non-performing	Accumulated impairment	Total	Non-performing	Accumulated impairment	Total	Non-performing	Accumulated impairment
	€000	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Within 1 year	36,894		159	9,255		91				27,639		68
1 - 2 years	26,688		150	7,230		77				19,458		73
2 - 3 years	5									5		
3 - 5 years												
5 - 7 years												
7 - 10 years												
More than 10 years												
Total	**63,587**		**309**	**16,485**		**168**				**47,102**		**141**

* The origination date of new or restructured credit facilities is defined as the date of loan agreement i.e. the contract date.

Credit Risk (continued)

<u>TABLE B: Analysis of the credit portfolio on the basis of their origination date* for balances (continued)</u>

As at 31 December 2016

Total loans granted	Gross carrying amount of total loans			Loans to non-financial corporations			Loans to other financial corporations			Loans to households		
	Total	Non-performing	Accumulated impairment	Total	Non-performing	Accumulated impairment	Total	Non-performing	Accumulated impairment	Total	Non-performing	Accumulated impairment
	€000	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**	**€000**
Within 1 year	24,628		67	6,542		36				18,086		31
1 - 2 years	38									38		
2 - 3 years												
3 - 5 years												
5 - 7 years												
7 - 10 years												
More than 10 years												
Total	**24,666**		**67**	**6,542**		**36**				**18,124**		**31**

* The origination date of new or restructured credit facilities is defined as the date of loan agreement i.e. the contract date.