HABIBSONS BANK LIMITED
COMPANY REGISTRATION NO: 1719649

FINANCIAL STATEMENTS

FOR THE YEAR ENDED
31 DECEMBER 2013

Strategic Report 2013

The Bank is an authorised institution under the Financial Services and Markets Act 2000 (as amended 2012) and regulated by the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA) It provides a range of banking products and services including Trade Finance, Funds Transfers (including electronic remittances), Foreign Exchange & Money Market dealings, Depository Products and Fiduciary Products (Deposits and investments) The Bank is a subsidiary of Habib Allied International Bank Plc together the "Group"

__Business Review__

2013 was a challenging year for the Bank as the Group was consolidating its operations in an effort to derive synergies through moving into a one bank model subsequent to its acquisition of this bank At the same time the Bank is adapting a more rigorous and robust risk monitoring system and credit policies As a niche market player, we are re-shaping our business in line with the Group's Business model and objectives

There are three primary business models that define our path to achieving our objectives

First is our business with the South Asian community Continuing our focus on the customized but vanilla products with enhanced personalised service, leveraging our strength through our extensive presence in South Asian market. Second is to focus on the financing of trade, both funded and non-funded, which is the core strength of the Group based on its cross border relationships as well as an extensive distribution channel for down-selling The third is concentrating on a niche within our target market i.e segmenting our customer base for enhanced focus on the high net-worth customers seeking Wealth Management

The Bank, as per the business model of the Group, continued to focus on the Deposit Franchise, Customer Loans & Advances, Trade Finance and Private Banking During the year, the Risk Management infrastructure was strengthened through a comprehensive review of the process and seeks to follow best market practice This resulted in rigorous portfolio monitoring, strict controls and remedial management of impaired accounts

On the Deposit Franchise front, average customer deposits decreased by 4% to £191M This decline was a result of an 8% attrition in term deposits while the CASA improved by 2% to £82M

During the year, the Bank was able to double the size of its investment portfolio consisting of Sovereign, Corporate, and FI exposures This portfolio increased to £135M with a yield of 1 32% which was slightly lower than the targeted yield, however, the positive variance in volume mitigated the shortfall in yield. Average Customer advances decreased over the year to £55M, a decrease of 12% as compared to target The yield on advances of 3 54% remained slightly under budget of 3 82%

The net interest income of the Bank remained exactly as per budget at £3.3M, The non fund based income remained at the same level at £3 1M although slightly behind the budget target due to a shortfall in Private Banking income

Despite all the premerger challenges, the Bank was able to reduce its expenses by 3% to £5 9M and ended with a pretax profit of £359,000

Key Performance Indicators

Directors used certain key performance indicators (KPIs) to monitor the business, these indicators are used to measure profitability, capital and liquidity of the Group

Future Outlook

Overall 2013 remained a year of consolidation for the bank, adapting itself to the new structure while merging into a one bank model The UK economy grew by 1 90% in 2013, the strongest annual growth rate in six years, brightening the economic environment in which we operate and after some revival in the housing market, the business investment sector is likely to gather pace this year

The Group is presently in the process of completing the legal merger of the two entities which will provide further consolidation of the operating model through convergence to a single IT platform Going forward, the Group's strategy will be to focus on leveraging an enhanced network and experience through synergizing the merged operations and relationships with existing customers and partners The Group will be concentrating its efforts on the steady growth of the Deposit Franchise, Remittances, Investments, Private Banking and Trade business which should lead to an improvement in both the Fund based and Non Fund based Income

Principal Risks and Risk Management

Principal risks: Banks are, by their very nature, in the risk business and managing risk is an integral part of banking The Bank is primarily exposed to credit risk, market risk (including interest, FX and liquidity risks), operational risk (including risk of non-compliance with regulatory requirements) and reputational risk All these risks are managed through adherence to documented policies and procedures together with a high level managerial oversight of the Bank's operations

Given the conditions in the financial markets, the Bank has consciously adopted a strategy to maintain adequate liquidity at all times, both in terms of amount and quality, to ensure that it continues to meet its obligations as they fall due The Bank regularly reviews its asset / liability maturity mismatches and maintains liquidity gaps within prescribed limits

Risk Management: Risk management involves the identification, analysis, evaluation, acceptance and mitigation of all financial and non financial risks that could have a negative impact on the Bank's performance and reputation The Board of Directors has overall responsibility for the establishment and oversight of risk management and continues to maintain a "Risk Averse" policy The Bank has established Risk Management systems and controls to ensure that all of its principal risks are identified and that policies and monitoring processes are in place to mitigate them The Bank's risks are managed taking into account several main principles including responsibilities for their management and control, assessment and measurement of all identified risks with a balance between risk versus return and undertaking periodical review of risk policies and the control framework to ensure optimal capital allocation and utilisation

Those risks identified in the Bank's risk registers are at a level commensurate with current business operations and the proposed Business Plan With regard to credit risk, given the unprecedented conditions in the market and economy, the controls in this area have been strengthened with additional oversight to ensure regular stress testing of the portfolio and a focused strategy is adopted for managing stressed borrowers.

With a view to maximizing shareholder value, the risk management systems seek to ensure that the Bank's risk profiles are aligned to available financial and non-financial resources To ensure this, the Board of Directors has established

- Defined, clear and coherent Risk Management systems and controls covering various types of risks to the Bank to ensure that all of its principal risks are identified and that internal monitoring processes, procedures and controls are in place to mitigate them,

- Group Risk Appetite Statement sets defined risk limits and tolerance levels for each underlying risk in relation to Regulatory Limits, Credit and Market risk and in accordance with the underlying financial resources,

- Enhanced systems and controls / Risk Reporting System to manage and monitor the core risk related to Capital, liquidity and Credit,

- Suitable forums for discussing, monitoring and managing these risks All key decisions are subject to the "four eyes" principle,

- A Risk Management Framework which sets out the constitution, roles and responsibilities of the Board of Directors, Non Executive Directors, all the Committees, Chief Executive Officer, and Management

To enable a better and more focused attention to the affairs of HBL UK, including the oversight of its subsidiary, Habibsons Bank, the Board has established a number of Committees, each with defined terms of reference, scope of work, roles and responsibilities to prepare the ground work for decision making and to assist the Board in monitoring the implementation of the policies, processes and procedures

All significant matters discussed and decided at each meeting of the Board Committees are reported to the Board by the Chairmen of the respective Committees·

- Audit and Compliance Committee
- Group Risk Management Committee
- Group Human Resources Committee

The Risk management disclosures as required under Pillar III are available on the HBL UK's website www habibbankuk com These disclosures under Pillar III include a detailed risk management analysis, Capital Management and details of overdue and impairment exposures

Basel II Capital Resource Requirement: Under the Capital Requirement Directive, the Group has adopted the Standardized Approach to credit risk and the Basic Indicator Approach to operational risk. The Bank has implemented the Basel II Capital Resource Requirement and maintains its capital adequacy within the Individual Capital Guidance (ICG) received from the Regulator after a supervisory review of the Statutory Liquidity Review Process (SLRP) The Bank has remained in compliance with its ICG requirements that include maintaining a Capital Planning Buffer (CPB) during the year

Capital Requirement Directive and Capital Requirement Regulation (CRD IV) The Bank is fully geared to adopt the requirements and guidelines in relation to the Basel III CRD IV The new directive apart from other things primarily focuses on enhancing the quality of capital, emphasis on core tier 1 capital, strengthening capital requirements for counterparty credit risk resulting in higher Pillar1 requirements and introducing new capital buffers i e. capital conservation and countercyclical buffers

Liquidity Management: Under the liquidity regulations, the Bank has implemented the regulatory requirements for liquidity risk management including embedding systems and controls overseen by the Group Asset and Liability Committee (ALCO)

The Bank maintained adequate liquidity during 2013 and placed surplus liquidity in high quality investments

Money Laundering and Terrorist Financing: The Bank has adopted a risk based approach to prevent financial crime Documented policies and procedures are in place to combat money laundering and terrorist financing which are independently monitored by the respective MLROs of the two banks and the Group's Compliance Department. All employees at regular intervals and new employees at the time of joining the service of the Bank receive Anti-Money Laundering training to ensure that they remain aware of the risk of money laundering and terrorist financing while conducting business activities.

The Bank maintains appropriate customer screening, monitoring of transactions and related due diligence procedures that are designed to prevent the Bank from doing business with entities on sanctions lists To check funds transfers to or from a person / entity on any of the various sanctions list, all transactions are monitored and filtered on a real time basis through a robust automated software solution

Internal Controls: The system of internal control is based on an ongoing process designed to identify the principal risks which are inherent in the Bank's business, to evaluate the nature and extent of those risks and to manage them efficiently and effectively.

The Bank's system of internal control includes appropriate levels of authorisation, segregation of duties and limits for each aspect of business There are established procedures and MIS for regular reporting of financial information Financial reports are presented to the Board in each of its meetings detailing results and other performance data

Management assumes the responsibility of establishing and maintaining adequate internal controls and procedures while the Board of Directors is ultimately responsible for the internal control systems For this purpose the Bank has developed Procedure Manuals that are followed when conducting the various banking transactions These Procedure Manuals are revised and updated as and when appropriate

The Internal Audit function of the Bank reviews the adequacy and implementation of internal controls on a regular basis and deficiencies, if any, are followed up until they are rectified. Status of the unresolved significant issues is reviewed by the Audit and Compliance Committee (ACC) in each of its meetings An audit programme is agreed annually with the ACC and the Bank's Head of Audit presents a summary of audit reports completed during the period and provides any explanation required by the Committee

Treating Customers Fairly: The Bank fully supports the Regulators initiative on 'Treating Customers Fairly' (TCF), and has adopted a proactive approach to ensuring compliance with Principle 6 of the Financial Conduct Authority (FCA) 'Principles for Businesses', which states *"a firm must pay due regard to the interests of its customers and treat them fairly"* The Board and senior management continues to ensure that the concept of TCF is fully embedded into the culture of the Bank at all levels Policies are in place to guide employees in understanding how they can help the Bank deliver on the commitment

The Bank has a complaints handling procedure and encourages customers to report instances where the Bank's service falls short of the expected high standards This commitment remains a priority for the Bank

Anti-Bribery Policy: The Bank places great value on all of its assets Among those assets, reputation of the Bank is at the core of its priorities The Board, senior management and every employee has a significant role to play in preserving and nurturing the Bank's reputation for honesty, integrity, and fair play in dealing with fellow employees, customers, regulators, suppliers and the general public The Bank expects all employees to conduct themselves in accordance with the highest standards of personal and professional integrity and to comply with all laws, regulations, corporate policies and procedures

The Bank has adopted a formal Anti-Bribery Policy for the prevention of bribery and has zero-tolerance towards any type of bribery Staff members are required to report any bribery that comes to their attention The Policy clearly states that any person found in breach of this Policy will expose themselves to disciplinary proceedings and possible prosecution

By order of the Board of Directors

Bande Hasan
Chief Executive Officer
9 Portman Street, London

Dated 04 March 2014

Directors' Report

The Directors are pleased to present their Annual Report and Audited Financial Statements together with the Auditors' Report for the year ended 31st December 2013

Management

The management team of the Bank consists of seasoned professionals with diverse and complementary skills in various backgrounds as well as depth of experience in their area of operations Over the years, these executives have brought their knowledge, experience and leadership to bear in the development and delivery of solutions to meet the needs of the customers, and in the process contributing to sustaining the performance of the Bank

Financial Performance - Results

The financial statements for the year ended 31st December 2013 are set out in detail on pages 11 to 27 The profit on ordinary activities before tax for the financial year amounted to £359,000

The Directors do not propose the payment of a dividend for the year (2012 Nil)

The Bank's financial statements have been prepared on the going concern basis which the Directors consider to be appropriate as there are no material uncertainties that may cast significant doubt about the bank's ability to continue as a going concern This conclusion is based on the following

- Review of the financial performance, outlook, principal risks and risk management as discussed in the Directors' report
- Detailed assessments carried out by the management in respect of key areas of the Bank such as the liquidity, capital management, profit projections and litigation covering a period of twelve months from the date of signing the balance sheet

The Group Risk management disclosures as required under Pillar III are available on the parent bank's website www habibbankuk com The disclosures under Pillar III include a detailed risk management analysis, Capital Management and details of overdue and impaired exposures

BOARD OF DIRECTORS

Current members of the Board are given below

Nauman K Dar	Chairman
H D Habib	Vice Chairman
Bande Hasan	Chief Executive Officer
Anwar Zaidi	Non-Executive Director
Michael D Bendon	Non-Executive Director
Patrick Quinn	Non-Executive Director
David J Blatchford	Non-Executive Director

Directors Interests

None of the Directors who held office at the end of the financial year under review had any disclosable interest in the shares of the Bank No contract of significance in relation to the Bank's business in which a Director of the Bank has a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year other than contracts entered in the normal course of business on an arms length basis or under a service contract.

Corporate Governance

The Board has ultimate responsibility for the proper stewardship of the Bank It meets regularly to discharge its responsibilities for all important aspects of the Bank s affairs, including monitoring performance, considering major strategic issues, approving budgets and business plans

The Board is firmly committed to the highest standards of corporate governance The Bank's corporate governance is closely directed towards regulatory and legal requirements alongside adherence to sound business practices, transparency and disclosures to shareholders The Bank within its relationship with its borrowers, depositors, shareholders and other stakeholders has always maintained its fundamental principles of corporate governance – that of integrity, transparency and fairness, seeking to provide an enabling environment to harmonise the goals of maximising shareholder value and maintaining focus on customer confidence in the Bank

The corporate governance framework of the Bank is based on an effective and independent Board which is not involved in the day-to-day management of the Bank The position of the Chairman of the Board and CEO are held by separate individuals The Board of Directors is entrusted with the formulation of policy guidelines, objective setting, strategic planning, organisational structure, supervising business activities, reviewing performance of management, ensuring regulatory compliance and safeguarding interests of the shareholders Management seeks to realise the Bank's strategic goals which are to maximise long-term shareholder value and to maintain the required standards of integrity and transparency

Board meetings are held at least three times a year. If required, additional meetings can be held to discuss any specific item of critical importance The Company Secretary in consultation with the CEO and Chairman prepares a detailed agenda for the meetings Agenda papers and other explanatory notes are circulated to the Directors in advance The Directors have complete access to all information of the Bank, and are free to recommend inclusion of any matter in the agenda for discussion Senior management is also invited to attend the Board meetings as and when required, so as to provide additional input to the items or issues being reviewed or discussed by the Board. This also keeps them informed of the Board's views

For smooth operation, risk management and monitoring purposes, the Board has formed various committees. These Board Committees conduct detailed analysis and reviews of various policies and critical issues and ensure that the activities of the Bank are always conducted in accordance with appropriate ethical standards. All the significant matters discussed and decided at each meeting are reported to the Board by the Chairman of the respective Committees

The Bank has an independent Audit and Compliance function The Group Head of Audit reports directly to the Chairman of the Audit and Compliance Committee of the Bank who is an Independent

Non-Executive Director The Committee reviews the Bank's internal controls, Risk Management Systems, statutory and regulatory compliance After detailed discussions on the findings of Internal Audit as well as the statutory auditor's reports, the Committee initiates necessary corrective actions The Committee apprises the Board of Directors of any significant issues and the corrective measures initiated The Committee also follows-up implementation of its various suggestions/recommendations on a regular basis

The Chief Executive Officer, who reports to the Chairman and the Board, is empowered by the Board of Directors for all operational issues and day-to-day management of the Bank In carrying out his duties he is assisted by senior management and the following committees

- Group Asset and Liability Committee
- Management Committee
- Credit Risk Committee

Code of Ethics

Every employee of the Bank has a significant role to play in preserving and nurturing the Bank's reputation for honesty, integrity and fair play in dealing with fellow employees, customers, regulators, suppliers and the general public The Bank expects all employees to conduct themselves in accordance with the appropriate standards of personal and professional integrity and to comply with all laws, regulations, corporate policies and procedures

Acknowledgement

The Board of Directors takes the opportunity to express its thanks and gratitude to all stakeholders including its customers for their continued support and cooperation without which the business growth of the Bank would not have been possible

The Board of Directors also records its appreciation to the Management and Staff for their dedication, commitment and team work

Directors Representation

The Directors who held office at the date of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Bank's auditors are unaware, and each Director has taken all steps that he ought to have taken as a Director in order to make himself aware of any relevant audit information and to establish that the Bank's auditors are aware of that information

The Directors are unaware of any material events that have occurred since the end of the financial year to the date of signing this report that could impact the financial health of the Bank

By order of the Board of Directors

Bande Hasan
Chief Executive Officer
9 Portman Street, London

Dated 04 March 2014

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

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

Company law requires the directors to prepare financial statements for each financial year Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice)

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

- select suitable accounting policies and then apply them consistently;
- make judgments and estimates that are reasonable and prudent,
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements, and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the bank will continue in business

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the bank's transactions and disclose with reasonable accuracy at any time the financial position of the bank and enable them to ensure that its financial statements comply with the Companies Act 2006 They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the bank and to prevent and detect fraud and other irregularities

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

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF HABIBSONS BANK LIMITED

We have audited the financial statements of Habibsons Bank Limited for the year ended 31 December 2013 set out on pages 11 to 27 The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice)

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

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement set out on page 8, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view Our responsibility is to audit, and express an opinion on, the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors

Scope of the audit of the financial statements

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www frc.org.uk/auditscopeukprivate

Opinion on financial statements

In our opinion the financial statements

- give a true and fair view of the state of the company's affairs as at 31 December 2013 and of its profit for the year then ended,
- have been properly prepared in accordance with UK Generally Accepted Accounting Practice, and
- have been prepared in accordance with the requirements of the Companies Act 2006

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion

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

Samer Hijazi (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
15 Canada Square, London
04 March 2014

Profit and loss account	Note	**Year ended 31 December 2013 £'000**	Year ended 31 December 2012 £'000
Interest receivable			
Interest receivable and similar income arising from debt securities		1,448	859
Other interest receivable and similar income	2	2,906	3,813
		4,354	4,672
Interest payable		(1,010)	(747)
Net interest income		3,344	3,925
Fees and commissions receivable		1,983	2,204
Foreign exchange dealing profits		366	394
Other operating income		761	498
Total operating income		6,454	7,021
Administrative expenses	3	(5,766)	(6,023)
Depreciation	10	(139)	(135)
Total operating expenditure		(5,905)	(6,158)
		549	863
Provision for loan losses	8	(190)	(140)
Profit on ordinary activities before tax		359	723
Tax on profit on ordinary activities	5	(71)	(162)
Profit on ordinary activities after tax	15	288	561

There are no recognised gains and losses other than the profit for the year, except as reported in note 15
The result for the year is derived entirely from continuing activities
The notes on pages 13 to 27 form part of these financial statements

Balance sheet
as at 31 December

	Note	2013 £'000	2012 £'000
Assets			
Cash and balances at central banks		**409**	358
Loans and advances to banks		**75,568**	135,675
Loans and advances to customers	7	**50,806**	50,793
Debt securities	9	**135,200**	63,855
Other assets	11	**85**	284
Prepayments and accrued income		**2,308**	1,207
Tangible fixed assets	10	**649**	642
Total assets		**265,025**	252,814
Liabilities			
Deposits by banks		**10,628**	19,262
Customer accounts		**225,984**	207,446
Other liabilities	12	**727**	786
Accruals and deferred income		**525**	708
Subordinated liabilities	14	**6,050**	3,713
Total liabilities		**243,914**	231,915
Shareholders' funds			
Called up share capital	13	**14,000**	14,000
Profit and loss account	15	**7,196**	6,908
Other reserves	15	**(85)**	(9)
Total Equity		**21,111**	**20,899**
Total liabilities & Equity		**265,025**	**252,814**

The notes on pages 13 to 27 form part of these financial statements

These financial statements were approved by the board of directors on 20 February 2014 and signed on its behalf by

Bande Hasan
Chief Executive Officer

Notes to the Accounts
Year ended 31 December 2013

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Bank's financial statements

Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost accounting rules

Under FRS 1 the Bank is exempt from the requirement to prepare a cash flow statement on the grounds that a parent undertaking includes the Bank in its own consolidated financial statements

As the Bank is a wholly owned subsidiary of Habib Allied International Bank PLC, the bank has taken advantage of the exemption contained in FRS 8 and has therefore not disclosed transactions or balances with its related parties

The preparation of these financial statements requires management to make estimates and judgements This is particularly so in the assessment of provisions for bad and doubtful debts and in assessing impairment of debt securities Making reliable estimates of the ability of customers and other counterparties to repay is often difficult even in periods of economic stability and becomes more difficult in periods of economic volatility Therefore while management believes it has utilised all available information to estimate adequate allowances for all identifiable risks in the current portfolios, there can be no assurance that the provisions for bad and doubtful debts or other impairment provisions will prove adequate for all losses ultimately realised

The Bank's financial statements have been prepared on the going concern basis which the directors believe to be appropriate as there are no material uncertainties that may cast significant doubt about the bank's ability to continue as a going concern This conclusion is based on the following

(i) Review of the financial performance, outlook, principal risks and risk management as discussed in the Director's report

(ii) Detailed assessments carried out by the management in respect to the key areas of the Bank such as the liquidity, capital management, profit projections and litigation covering a period of twelve months from the date of signing the balance sheet

The Group Risk management disclosures as required under Pillar III are available on the parent bank's website www habibbankuk com. The disclosures under Pillar III include a detailed risk management analysis Capital Management and details of overdue and impairment exposures

Revenue recognition

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate Interest on impaired accounts is credited to suspense and excluded from interest income

Fees receivable which represent a return for services provided or risk borne or which are in the nature of interest are credited to income when the related service is performed or over the period of the transaction, depending on the nature of the income.

Dealing profits represent profits or losses on foreign exchange transactions

Financial assets and liabilities

The Bank classifies its financial assets into the following measurement categories a) loans and receivables, b) held-to-maturity investments, and c) available-for sale financial assets Financial liabilities are classified as either held at fair value through profit or loss, or at amortised cost Management determines the classification of its financial assets and liabilities at initial recognition or, where appropriate at the time of reclassification

(a) Loans & receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and it is expected that substantially all of the initial investment will be recovered other than because of credit deterioration.

(b) Held-to-maturity

Held to-maturity assets are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity

(c) Available-for-sale

Available-for-sale assets are those non-derivative financial assets intended to be held for an indefinite period of time, which may be sold in response to liquidity requirements or changes in interest rates, exchange rates, commodity prices or equity prices

Initial recognition

Purchases and sales of financial assets which are held-to-maturity and available-for-sale are initially recognised on trade-date (the date on which the Bank commits to purchase or sell the asset) Loans are recognised when cash is advanced to the borrowers.

Derecognition

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership If substantially all the risks and rewards have been neither retained nor transferred and the Bank has retained control, the assets continue to be recognised to the extent of the Bank's continuing involvement Financial liabilities are derecognised when they are extinguished

Subsequent measurement

Available-for-sale financial assets are carried at fair value, with gains and losses arising from changes in fair value taken to a separate component of equity until the asset is sold, or is impaired, when the cumulative gain or loss is transferred to the income statement

Loans and receivables and held-to-maturity financial assets are subsequently carried at amortised cost using the effective interest method

Leases

The Bank enters into operating leases as referred to in note 4 Rentals under operating leases are charged on a straight line basis over the lease term The Bank has not entered into any finance leases

Impairment of financial assets
Specific provisions are made for advances which are recognised to be impaired A loan is impaired when, based on current information and events, the Bank considers that the creditworthiness of the borrower has undergone a deterioration such that it no longer expects to recover the advance in full Provisions made during the year are charged to revenue, net of recoveries When there is no further likelihood of recovery the remaining balance is written off

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through profit or loss to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised

Collective impairments arise in respect of groups of exposures with similar risk characteristics for which previous experience indicates that impairment has taken place at the balance sheet date, but whose existence has yet to emerge While assessing collective impairment allowances, management considers factors such as historical loss trends, concentrations, collaterals, emergence period, and inherent credit risk The aggregate amount of specific and collective provisions is intended to be sufficient to absorb estimated credit losses generated in the loan portfolio

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

Offsetting financial assets and financial liabilities
Financial assets and liabilities are offset and the net amount reported in the Balance Sheet when, in the event of default, the Bank has a legal right to set off the recognised amounts and intends to settle on a net basis

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains or losses arising from a group of similar transactions

Derivatives
Derivative instruments used by the bank are forward exchange contracts The bank does not enter into speculative derivative contracts All such contracts are generally executed on behalf of customers.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re measured to their fair value at each balance sheet date The resulting gain or loss is recognised in profit or loss immediately based on market observable parameters

Foreign currency
Transactions in foreign currencies are recorded at the rate of exchange at the date of the transaction, or if hedged at the forward contract rate Monetary assets and liabilities denominated in a currency other than sterling are translated at exchange rates prevailing at the year end and exchange gains and losses are included in the profit and loss account

Fiduciary Activities
The Bank commonly acts as trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals and other institutions Assets held in trust and fiduciary accounts do not become assets or liabilities of the bank and are segregated from the bank's assets

Pensions
The company operates a defined contribution scheme. The assets of the scheme are held separate from those of the company in independently administered funds Amounts charged to the profit and loss account represent the contributions payable to the schemes in respect of the accounting period Differences between contributions payable in the year and contributions actually paid are shown as either prepayments or accruals in the balance sheet.

Tangible fixed assets
Tangible fixed assets are stated at cost net of accumulated depreciation and impairment in value Depreciation is provided by the company to write-off equipment by equal installments over its estimated useful economic life. Rates applicable are as follows

Nature of	Rate of depreciation
Leasehold improvements	10%
Furniture, fixtures and office equipment	10%
Computer software and hardware	20%

Taxation
The charge for taxation is based on the profit for the year and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes

Deferred taxation is recognised in accordance with FRS 19 "Deferred Tax" and in respect of timing differences that have originated but not reversed at the balance sheet date where transactions or events that result in an obligation to pay more tax in the future or a right to pay less tax in the future have occurred at the balance sheet date

Deferred tax assets are regarded as recoverable and recognised in the financial statements to the extent that, on the basis of available evidence, it is more likely than not that there will be suitable taxable profits from which the future reversal of the timing difference can be deducted

Claims and litigation
Provisions for restructuring costs and legal claims are recognised when the Bank has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated

2 Other interest receivable and similar income

	Year ended 31 December 2013 £'000	Year ended 31 December 2012 £'000
Interest on loans and advances		
Banks	959	1,486
Customers	1,947	2,327
	2,906	3,813

3 Administrative expenses

	Year ended 31 December 2013 £'000	Year ended 31 December 2012 £'000
Staff costs		
Wages, salaries and allowances	2,808	3,137
Social security costs	331	317
Other pension costs	140	147
Other administrative expenses	2,487	2,422
	5,766	6,023

The average number of persons (including part-time employees) employed by the Bank during the period was 59 (2012 62) The total number of persons employed at 31 December 2013 was 59 (2012 60)

The Bank operates a defined contribution pension scheme The pension cost charge for the period represents contributions payable by the Bank to the scheme and amounted to £139,909 (2012 146,532) There were no outstanding or prepaid contributions at either the beginning or end of the financial year

4 Profit on ordinary activities before tax

	Year ended 31 December 2013 £'000	Year ended 31 December 2012 £'000
(a) Is stated after		
Charging		
Auditors' Remuneration		
Fees payable to the Banks' auditors for the audit of the Banks' financial statements	50	45
Fees payable to the Banks' auditors for other services		
All other services	2	18
Operating lease rentals		
Land and buildings	232	592
Depreciation	139	135

5 Taxation

	Year ended 31 December 2013 £'000	Year ended 31 December 2012 £'000
(a) Analysis of charge for the year		
Current tax		
UK corporation tax for the year at 23 25% (2012 24 50%)	81	217
Less relief for foreign tax suffered	(57)	(28)
Underprovision in respect of prior years	(16)	5
Total current tax	8	194
Effects of double tax relief		
Foreign tax for current year	57	28
Total current tax	65	222
Deferred tax		
Reversal in respect of timing differences	(2)	(59)
Prior year adjustment in respect of timing differences	9	3
Effect of change in tax rate	(1)	(4)
Total deferred tax	6	(60)
Tax charge	71	162

	Year ended 31 December 2013 £'000	Year ended 31 December 2012 £'000
(b) Factors affecting tax charge for the year		
Profit on ordinary activities before tax	359	723
Profit multiplied by standard tax rate of 23 25% (2012 24 50%)	83	177
Effects of		
Expenses not deductible for tax purposes	6	34
Depreciation for the period in excess of capital allowances	(8)	6
Adjustments in respect of prior periods	(16)	5
Current tax charge for the year	65	222

(c) The main rate of corporation tax reduced from 24% to 23% on 01 April 2013 A reduction in the main rate of corporation tax from 23% to 21% effective from 01 April 2014 and from 21% to 20% effective from 01 April 2015 was substantively enacted in July 2013 These changes will reduce the Bank's future current tax charge accordingly The deferred tax asset at 31 December 2013 has been calculated based on the rate of 20% substantively enacted at the balance sheet date

It has not yet been possible to quantify the full anticipated effect of the announced further 1% rate reduction, although this will further reduce the Bank's future current tax charge and reduce the Bank's deferred tax asset accordingly

6 Emoluments of directors

	31 December 2013 £'000	31 December 2012 £'000
Directors' fees and emoluments	271	270
The total remuneration and benefits of the highest paid director were	181	190

7 Loans and advances to customers

	2013 £'000	2012 £'000
Advances	51,640	51,453
Less Provision	(834)	(660)
	50,806	50,793

8 Provision for loan losses

Provisions	Loans & Advances Specific £'000	Collective £'000	2013 Total £'000	2012 Total £'000
At 31 December 2012	570	90	660	874
Provisions for the year	144	46	190	140
Reversals	-			(273)
Amounts written off	(16)		(16)	(81)
At 31 December 2013	698	136	834	660

9 Debt securities

	2013 £'000	2012 £'000
Investment securities - Held to maturity		
Listed		
Government securities	33,614	53,268
Others	17,412	5,374
	51,026	58,642
Investment securities - Available for sale		
Listed		
Government securities	45,277	
Others	38,897	5,213
	84,174	5,213
	135,200	63,855

(a) Market Value

Market value of held to maturity investments as at 31 December 2013 is £51,099,444 (2012 £58,943,110) All debt securities as at 31 December 2013 and 2012 are quoted in active markets (Level 1)

Level 1 Investments are valued using quoted prices in active markets for identical assets

(b) Debt securities movement

	(Discount)/ Premium £'000	Carrying value £'000
At 31 December 2012	470	63,855
New investments	5,399	114,347
Exchange adjustments	(165)	(3,711)
Amortised during the year	(2,038)	(2,038)
Revaluation loss on debt securities - available for sale	-	(85)
Matured / disposed of during the year	350	(37,168)
At 31 December 2013	4,016	135,200

10 Tangible fixed assets

	Leasehold Improvements £'000	Computer Furniture Fixtures & Equipment £'000	Total £'000
Cost			
At 31 December 2012	462	2,693	**3,155**
Additions	-	147	**147**
Exchange Impact	-	(10)	**(10)**
Disposals	-	(52)	**(52)**
At 31 December 2013	462	2,778	**3,240**
Accumulated depreciation			
At 31 December 2012	126	2,387	**2,513**
Charge for the year	28	111	**139**
Exchange Impact	-	(9)	**(9)**
Depreciation on disposal	-	(52)	**(52)**
At 31 December 2013	154	2,437	**2,591**
Net book value as at 31 December 2013	308	341	**649**
Net book value as at 31 December 2012	336	306	**642**

11 Other assets

	2013 £'000	2012 £'000
Deferred tax	5	11
Unrealised gain on forward contracts	5	3
Other assets	75	270
	85	284

12 Other liabilities

	2013 £'000	2012 £'000
Corporation tax	13	131
Bills payable	22	252
Other liabilities	692	403
	727	786

13 Share capital

	2013 £'000	2012 £'000
Authorised		
5,000,000 Ordinary shares of £5 each	25,000	25,000
Allotted, called up and fully paid		
2,800,000 Ordinary shares of £5 each	14,000	14 000

14 Subordinated liabilities

	2013 £'000	2012 £'000
Subordinated loan	6,050	3,713
	6,050	3,713

During the year the Bank has issued subordinated debt of $10,000,000 (equivalent to £6,050,000) to the Habib Bank Limited, Bahrain These notes are perpetual and are repayable at the option of the Bank after five years have passed from the date of issuance The loan is subordinated to the claims of depositors and other creditors The Prudential Regulation Authority (PRA) classify this as upper Tier II capital and approval from them is required prior to any repayment. Interest is payable on a six monthly basis at the rate of 5 75% above six month LIBOR

The subordinated debt of $6,000,000 outstanding as at 31 December 2012 was repaid

15 Movement in Shareholders' funds

	2013			
	Share capital £'000	Profit and loss £'000	Other Reserves £'000	Total £'000
At 1 January 2013	14,000	6,908	(9)	20,899
Retained profit for the year	-	288	-	288
Revaluation loss on debt securities - available for sale	-	-	(76)	(76)
	14,000	7,196	(85)	21,111

	2012			
	Share capital £'000	Profit and loss £'000	Other Reserves £'000	Total £'000
At 1 January 2012	14,000	6,347	-	20,347
Retained profit for the year	-	561	-	561
Realised during the year	-	-	(9)	(9)
	14,000	6,908	(9)	20,899

16 Contingencies and commitments

	Year ended 31 December 2013 £'000	Year ended 31 December 2012 £'000
(a) Contingencies		
Acceptances and endorsements	1,849	9,692
Guarantees	10,560	7,607
(b) Commitments		
(i) Annual commitments under non-cancellable operating leases on land and buildings are as follows		
Lease of premises		
Within one year	-	-
In the second to fifth years	57	59
Over five years	567	565
(ii) In respect of forward foreign exchange contracts		
Purchase	30,984	27,045
Sale	31,014	27,052
(iii) In respect of undrawn credit facilities	1,549	2,470

(c) Contingent liabilities and commitments to extend credit are mainly credit exposures which represent the amounts at risk should contracts be fully drawn upon and clients default Since a significant portion of contingent exposures and commitments are expected to expire without being drawn fully upon or be covered by cash lien, the total of the contractual amounts is not representative of future liquidity requirements

17 Assets and liabilities denominated by currency

2013	Assets	Liabilities	Forward exchange contracts	Shareholders funds & Reserves	Net Exposure
					£'000
GBP	98,123	77,323	30	20,966	(136)
USD	138,734	141,159	(194)	-	(2,619)
EURO	16,865	17,140	105	-	(170)
Other currencies	11,303	8,292	59	145	2,925
	265,025	243,914	-	21,111	-
	-	-	-	-	-

2012	Assets	Liabilities	Forward exchange contracts	Shareholders funds & Reserves	Net Exposure
					£'000
GBP	97,898	77,062	7	20,826	17
USD	130,459	130,146	(96)		217
EURO	15,773	15,892	40	-	(79)
Other currencies	8,684	8,815	49	73	(155)
	252,814	231,915	-	20,899	-

18 Concentration of credit risk

	2013				
	Loans to customers	Loans to banks	Debt securities	Contingencies	**Total £'000**
Sectoral concentration					
Textile	977		-	404	**1,381**
Financial	-	75,568	31,268	876	**107,712**
Government	-		79,026	-	**79,026**
Property investments	11,699	-	-	1,500	**13,199**
Foods, tobacco and beverages	541	-	-	2,105	**2,646**
General traders	3,106	-	-	108	**3,214**
Individuals	18,434	-	-	5,561	**23,995**
Others	16,049	-	24,906	1,855	**42,810**
	50,806	75,568	135,200	12,409	

	2013				
	Loans to customers	Loans to banks	Debt securities	Contingencies	**Total £'000**
Geographical concentration					
Europe	26,645	55,973	87,600	8,113	**178,331**
North America	-	9,047	4,550	-	**13,597**
South America	4,106	-	3,120	73	**7,299**
Asia Pacific (including South Asia)	9,484	8,018	17,555	2,310	**37,367**
Africa	10,120	2,259	3,099	1,913	**17,391**
Middle East	3	143	16,244	-	**16,390**
Australia	448	128	3,032	-	**3,608**
	50,806	75,568	135,200	12,409	

	2012				
	Loans to customers	Loans to banks	Debt securities	Contingencies	Total £'000
Sectoral concentration					
Textile	-	-	-	1,158	1,158
Financial	-	135,675	5,374	5,573	146,622
Government	-	-	53,268		53,268
Property investments	11,563	-		-	11,563
Foods, tobacco and beverages	1,308	-	-	-	1,308
General traders	4,207	-	-	2,634	6,841
Individuals	16,264	-	-	6,215	22,479
Others	17,451	-	5,213	1,719	24,383
	50,793	135,675	63,855	17,299	

	2012				
	Loans to customers	Loans to banks	Debt securities	Contingencies	Total £'000
Geographical concentration					
Europe	27,042	98,732	47,618	1,836	175,228
North America	31	2,167	6,086	-	8,284
South America	1,684	-	-	74	1,758
Asia Pacific (including South Asia)	10,611	30,909	3,883	9,048	54,451
Africa	10,412	3,453	1,550	3,866	19,281
Middle East	130	388	1,603	2,475	4,596
Australia	883	26	3,115	-	4,024
	50,793	135,675	63,855	17,299	

European exposure primarily pertains to UK, direct and in-direct exposure of £11,151,439 (2012 £12,173,619) and £73,993,245 (2012 £124,011,587) respectively The Bank does not have any direct exposure to Portugal, Ireland, Italy, Greece and Spain Indirect exposure to these countries amounts to nil Direct exposure is the direct investment by the Bank in sovereign papers or debt instruments guaranteed by sovereigns

19 Maturity of Loans, Debt securities and Deposits

Maturity of loans, debt securities and deposits at the end of the year were

	2013					
	On Demand	**3 months or less but not on demand**	**Over 3 months but less than 1 year**	**Over 1year but less than 5 years**	**Greater than 5 years**	**Total**
	£'000	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Loans and advances to						
banks,						
- Parent and connected counterparties	915	3,000	-	-	-	3,915
- Others	21,886	46,418	1,055	2,294	-	71,653
customers	4,450	22,744	8,137	15,475	-	50,806
Debt securities	-	20,421	29,133	85,646	-	135,200
Other assets	409	80	2,313		-	2,802
Tangible fixed assets	-	-	-	-	649	649
	27,660	92,663	40,638	103,415	649	265,025
Deposits by						
banks,						
- Parent	2	5,415	-	-	-	5,417
- Others	4,529	667	15	-	-	5,211
customers	79,257	138,451	8,276		-	225,984
Subordinated liabilities	-	-	-	-	6,050	6,050
Other liabilities	-	714	538	-	-	1,252
	83,788	145,247	8,829	-	6,050	243,914
Net gap	(56,128)	(52,584)	31,809	103,415	(5,401)	21,111
Shareholders' funds						21,111

	2012					
	On Demand	3 months or less but not on demand	Over 3 months but less than 1 year	Over 1year but less than 5 years	Greater than 5 years	Total
	£'000	£'000	£'000	£'000	£'000	£'000
Loans and advances to						
banks,						
- Parent and connected counterparties	205	10,000	11,238	-	-	21,443
- Others	7,968	102,629	3,635	-	-	114,232
customers	5,310	26,009	8,101	11,373	-	50,793
Debt securities	-	8,386	20,864	34,605	-	63,855
Other assets	358	273	1,218	-	-	1,849
Tangible fixed assets	-	-		-	642	642
	13,841	147,297	45,056	45,978	642	252,814
Deposits by						
banks,						
- Parent	-	12,376	-		-	12,376
- Others	4,220	2,500	166		-	6,886
customers	78,996	120,412	8,038		-	207,446
Subordinated liabilities	-		-	-	3,713	3,713
Other liabilities	-	864	630	-	-	1,494
	83,216	136,152	8,834	-	3,713	231,915
Net gap	(69,375)	11,145	36,222	45,978	(3,071)	20,899
Shareholders' funds						20,899

The maturity of loans, debt securities and deposits have been shown according to their contractual maturities except for deposits held under lien which have been classified as per the maturities of the underlying exposure and impaired assets which have been classified in greater than 5 years net of their provision and interest in suspense

Expected maturity dates do not differ significantly from the contract dates except for the maturity of £178,056,000 (2012 £146,163,000) of deposits representing retail deposit accounts considered by the Bank as a stable source of funding of its operations

The connected counterparties include the Bank's subsidiary, parent, ultimate parent, subsidiaries of the parent and ultimate parent and any entity where the parent or ultimate parent holds singly or jointly more than 20% of the controlling interest.

20 Interest rate sensitivity gaps

Interest rate risk primarily arises on the mis-matching of the Bank's assets with its funding Interest rate sensitivity gaps in the Bank at the end of the year were

2013	Not more than three months £'000	More than three months but not more than 6 months £'000	More than six months but not more than 1 year £'000	More than 1 year but not more than 5 years £'000	Greater than 5 years £'000	Non interest bearing £'000	Total £'000
Loans and advances to							
banks	72,219	1,055	-	2,294	-	-	75,568
customers	49,298	-	-	-	-	1,508	50,806
Debt securities	33,972	7,124	17,425	76,652	-	27	135,200
Other assets	-	-	-	-	-	3,451	3,451
	155,489	8,179	17,425	78,946	-	4,986	265,025
Deposits by							
banks	10,613	15	-	-	-	-	10,628
customers	217,709	8,241	34	-	-	-	225,984
Subordinated liabilities	6,050	-	-	-	-	-	6,050
Other liabilities	-	-	-	-	-	1,252	1,252
Shareholders' funds	-	-	-	-	-	21,111	21,111
	234,372	8,256	34	-	-	22,363	265,025
Overall gap	(78,883)	(77)	17,391	78,946	-	(17,377)	-
Cumulative gap	(78,883)	(78,960)	(61,569)	17,377	17,377	-	-

2012	Not more than three months £'000	More than three months but not more than 6 months £'000	More than six months but not more than 1 year £'000	More than 1 year but not more than 5 years £'000	Greater than 5 years £'000	Non interest bearing £'000	Total £'000
Loans and advances to							
banks	120,802	12,318	2,555	-	-	-	135,675
customers	49,350	-	-	-	-	1,443	50,793
Debt securities	21,086	3,135	16,216	23,390	-	28	63,855
Other assets	-	-	-	-	-	2,491	2,491
	191,238	15,453	18,771	23,390	-	3,962	252,814
Deposits by							
banks	19,096	16	150	-	-	-	19,262
customers	199,408	7,873	165	-	-	-	207,446
Subordinated liabilities	3,713	-	-	-	-	-	3,713
Other liabilities	-	-	-	-	-	1,494	1,494
Shareholders' funds	-	-	-	-	-	20,899	20,899
	222,217	7,889	315	-	-	22,393	252,814
Overall gap	(30,979)	7,564	18,456	23,390	-	(18,431)	-
Cumulative gap	(30,979)	(23,415)	(4,959)	18,431	18,431	-	-

Non interest bearing items comprise shareholders funds, provisions, fixed assets, impaired assets and other assets and liabilities not subject to interest

21 Fair value of financial instruments

The fair values of traded investments are based on quoted market prices Fair value of these investments has been disclosed in note 9

In the opinion of management, the fair value of the remaining financial assets and liabilities are not significantly different from their carrying values since assets and liabilities are either short-term in nature or in the case of customer loans and deposits are frequently repriced

22 Ultimate parent undertaking and parent undertaking of larger group of which the Bank is a member

In the year 2011 the Bank was 100% acquired by Habib Allied International Bank Plc, registered in UK, which is in turn a subsidiary of Habib Bank Limited, registered in Pakistan, the ultimate parent undertaking The smallest and largest group in which the results of the Bank are consolidated is that headed by Habib Allied International Bank Plc and Habib Bank Limited, respectively Copies of the group accounts for Habib Allied International Bank Plc can be obtained from its website www habibbankuk com

23 Risk management framework

The Bank has adopted the parent's Risk Management Framework (RMF) Salient features of the RMF are summarised below

Credit Risk

Credit risk is the risk of loss due to the failure of a counterparty to meet their credit obligations in accordance with agreed contract terms

Credit risk makes up the largest part of the Bank's risk exposures The Credit risk policies are established by the Group Risk Management Committee (GRMC) and are approved by the Board The GRMC is responsible for ensuring appropriate governance and oversight in relation to all the risks in the Bank i e credit risk market risk, operational risk, and reputational risk In terms of credit risk the GRMC's responsibilities include

- to determine the policies and processes for credit approval, large exposures, country risk exposures and provisioning,
- to establish overall lending policies and guidelines,
- to monitor effective implementation of policies and consider any desirable amendments in the light of market conditions,
- to ensure the credit exposures of the Bank are at all times in compliance with any legal or regulatory requirements or restrictions,
- to ensure portfolio performance is in line with the set benchmarks and determine that overall provisions remain at required levels and
- to review the Large Exposures portfolio

The Bank's strategy for managing its different type of credits is as per the parent's asset underwriting strategy

Credit risk on financial instruments

31 December 2013	Neither past due nor impaired	Past due not impaired	Impaired	Impairment allowances	Total
	£(000)	£(000)	£(000)	£(000)	£(000)
Cash and balances at central banks	409	-			409
Loans and advances to banks	75,568		-		75,568
Loans and advances to customers	45,219	4 041	2,380	(834)	50,806
Debt securities	135,200	-		-	135,200
Total financial instruments	256,396	4,041	2,380	(834)	261,983

31 December 2012	Neither past due nor impaired	Past due not impaired	Impaired	Impairment allowances	Total
	£(000)	£(000)	£(000)	£(000)	£(000)
Cash and balances at central banks	358	-	-	-	358
Loans and advances to banks	135 675	-		-	135,675
Loans and advances to customers	41,134	8,306	2,013	(660)	50,793
Debt securities	63,855	-			63,855
Total financial instruments	241,022	8,306	2,013	(660)	250,681

Credit quality of loans and advances portfolio

The definition of internal risk rating for the loans and advances are given below

Grade 1-6	Performing
Grade 7	Watch-list
Grade 8	Impaired accounts
Grade 9	Staff loans

The Bank s internal risk rating scale is a measure of relative credit worthiness and does not map exactly with that of external rating agencies

Internal risk rating of loans and advances to customers

Rating	2013 £'000	2012 £'000
Grade 1 to 6	45,042	40,959
Grade 7	4,041	8 306
Grade 8	2,380	2,013
Grade 9	177	175
Total Gross Amount	51,640	51,453
Allowance for impairment (individual and collective)	(834)	(660)
Total	50,806	50,793

Concentration of past due exposure	2013 £'000	2012 £'000
UK	2 581	6,601
ASIA	880	983
AFRICA	2,960	2,734
	6,421	10,319

The table below provides the value of collateral/collaterals held by the Bank	2013 £'000	2012 £'000
Collateral Value	46,363	43,030
Gross loans and advances to customers	51,640	51,453

As at 31 December 2013 Bank's maximum exposure towards credit risk is approximately £277 million (2012 £270 million) This represents funded and non funded exposures towards sovergin banks financial institutions and other customers

The collateral value in the above table excludes the value of such collateral which the Bank may accept to manage its risks more effectively such as personal guarantees The Bank has applied appropriate haircuts as per its credit policy, while calculating the collateral value detailed above

Debt securities

An analysis of the Bank's debt securities portfolio based on credit ratings provided by external rating agencies is as follows

Rating	2013 £'000	2012 £ 000
Aaa to Aa3	69,251	54,756
A1 to A3	27,232	1,241
Baa1 to Baa3	29,169	5,213
Ba1 to Ba3	9,521	2 618
Non rated	27	28
	135,200	63,855

Liquidity Risk

This is the risk arising from the maturity profile, and type and nature of the Bank s assets and liability mix If not satisfactorily controlled the Bank could be faced with being unable to meet customer demands for repayment of deposits which can lead to a run on Bank deposits

The new liquidity regime introduced by the FSA has meant that the Bank has revised its liquidity management to be in compliance with the new rule set out in BIPRU 12 The new requirements include the overall liquidity rules risk tolerances, thresholds, systems and controls, stress testing scenarios, contingency funding plan, quantitative reporting and the documentation of the internal liquidity adequacy assessment (ILAA).

The Bank's liquidity policy is to ensure the Bank at all times maintains solvency through a prudent funding profile and appropriate mix of assets to ensure compliance with the overall liquidity adequacy principle as defined in BIPRU 12 2 1 The Bank s solvency has to be achieved on a self-sufficiency basis

The policy document sets out the Bank s liquidity management framework and sets out the overall liquidity policy, liquidity risk appetite, thresholds and tolerance levels, and systems and controls Senior management is responsible for regularly reviewing this policy document and for recommending changes, if any to the Board in a timely manner

The Bank will continue to evolve its liquidity risk management arrangements based on feedback from the FCA/PRA experience, and from developments in market and industry best practices

The Group Assets and Liabilities Committee (GALCO) has responsibility for the formulation of the overall strategy and oversight of the asset liability management function Roles and responsibilities of GALCO include but are not limited to -

Establishing the Bank's Liquidity and Interest Rate policies including changes in the Bank's Base Rate and deposit interest rates
- Monitoring liquidity and market exposure limits;
- Review of the Treasury market trends and forecasts on interest rates and FX rates and to decide on the Bank s strategy,
Developing the sterling and currency interest rate forecasts to be used for planning and budgeting purposes,
- Review of the breaches if any of the FCA/PRA guidelines on the liquidity position of the Bank and deciding on the action to restore/bring the position within the mismatch guidelines agreed with the FCA/PRA,
- To review market valuations of the Bank's portfolio of Floating Rate Notes and Fixed Income Securities and to approve further courses of action if any investment individually fell by 5% or more or is downgraded in its external rating to below the investment grade,
- Review of exchange profits and FX income trends of the Bank and plan for the future,
- Review of the Bank's liquidity position in the sight to 1 month band and Capital Adequacy Ratio,
- Management of Liquidity during stringent conditions and abnormal circumstances;
- Review and monitor warning indicators and funding sources,
Providing a forum for the exchange of views on liquidity related matters,
Management of thresholds and compliance with the liquidity policy;
- Review of stress testing results and consideration of the impact of stress results on the appropriateness of assumptions relating to the
    Effectiveness of diversification across the Bank's chosen sources of funding,
    - Estimates of future balance sheet growth,
    - Ability to access unsecured funding,
    Ability to convert currencies through use of foreign exchange swap markets,
Regular review of the Bank's contingency funding plan (CFP) and to incorporate changes if any required based on experience,
- Review of large exposures; and
- Review of liquidity reports

Market risk

Market risk is the risk of loss due to adverse movements in market rates or prices, such as foreign exchange rates interest rates and equity prices The Bank does not maintain an active trading book and hence carries limited market risk which emanates from mismatches in structural assets and liabilities positions

(i) Interest rate risk

Interest rate risk arises when there is a mismatch between positions which are subject to interest rate adjustments within a specific period A substantial part of the Bank s assets and liabilities are subject to floating rates and hence are re-priced simultaneously However, the Bank is exposed to interest rate risk as a result of mismatches on a relatively small portion of its assets and liabilities and assets funded through equity The major portion related to this risk is reflected in the banking book

The Bank manages its interest rate exposure through an interest rate gap report whereby assets and liabilities are allocated into an appropriate time band, based on the next interest re fix date.

The interest risk is then calculated as a 2% impact on earnings of the resulting net position for each time band, in line with the Basel Committee's recommendation

Interest sensitivity

The impact of an increase in interest rates has an impact on an entity s interest earnings An increase of 100bps in interest rates results would have had a positive impact of £112 000 on net interest income for the year ended 31 December 2013 (2012 £648,000)

(ii) Foreign exchange risk

The Bank's assets are typically funded in the same currency as that of the business transacted in order to eliminate foreign exchange exposure Foreign currency transactions are undertaken only on behalf of customers who are covered from the market on the same day

The Bank's foreign exchange risk appetite is defined by GALCO and monitored on a daily basis

The foreign exchange position risk is calculated as 8% higher of the net overbought or oversold position in foreign currencies

Operational risk

Operational risk is the risk of loss resulting from weaknesses in systems, procedures and people or from external events The Bank has adopted the 'Basic Indicator Approach', which as the BIPRU sourcebook states is 'The Operational Risk Capital Requirement' (ORCR) under the Basic Indicator Approach equal to 15% of the three-year average of the sum of (a) A firm's net interest income, and (b) A firm's net non-interest income

The RMF will reduce any operational risk to a minimum, although in view of the number of unknown external factors, the framework is regularly reviewed and overall risk management is kept at a high profile within the business to ensure any unmitigated operational risk is identified at an early stage

The data available to the bank since its inception shows that the bank has made insignificant operational losses during the period to date The level of complaints received are minimal and insufficient to identify any particular trends or weaknesses

Counterparty risk

Counterparty credit risk (CCR) is the risk to the Bank that a counterparty to a transaction could default before the final settlement of the transaction's cash flows In the normal course of business the Bank enters into foreign exchange contracts on behalf of its customers which are generally covered by entering into reciprocal transactions with other banks in the market on a daily basis to avoid position risk Counterparty credit risk emanating from these transactions is managed by maintaining appropriate collateral from customers to mitigate customer default exposure at the time of settlement. Exposures on Banks which are other counterparties to these transactions are managed within overall limit allocations determined as part of the Bank's credit assessment of such institutions

Capital management

The Bank is managing and monitoring its capital resources as per the Individual Capital Guidance (ICG) as set out by the FSA The Bank's capital resources consist of paid-up capital, retained earnings and lower Tier II capital There are no terms and conditions attached to the Bank's Tier I capital resources except for the capital gearing rules prescribed by the FCA/PRA

The firms own assessment of the capital required to hold against its risks is known as ICAAP (Internal Capital Adequacy Assessment Process) and the SREP (Supervisory Review and Evaluation Process) is the assessment conducted alongside the ARROW review to assess the overall risks of the firm The SREP also includes a qualitative and a quantitative assessment of the ICAAP