Habib Bank Zurich plc

Annual Report 2020

Canada
United Kingdom
Switzerland
UAE
Kenya
South Africa

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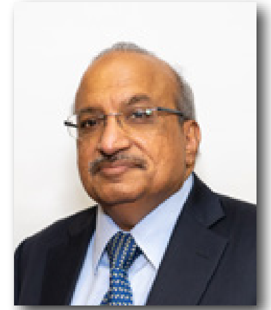
Corporate Information

Board of Directors	Mr Muhammad H. Habib (Chairman)		Non-Executive Director	
	Mr Carey Leonard		Independent Non-Executive Director	
	Mr Gerald Arthur Gregory		Independent Non-Executive Director	
	Mr Anjum Iqbal		Non-Executive Director	
	Mr Rajat Garg		Non-Executive Director	
	Mr Satyajeet Roy (CEO)		Executive Director	
	Mr Masum Billah (resigned 31 May 2021)		COO / Executive Director	
Board Committees	**Risk Committee**		**Audit & Compliance Committee**	
	Mr Carey Leonard	Chairman	Mr Gerald Arthur Gregory	Chairman
	Mr Gerald Arthur Gregory	Member	Mr Carey Leonard	Member
	Mr Anjum Iqbal	Member	Mr Anjum Iqbal	Member
	Mr Rajat Garg	Member	Mr Rajat Garg	Member
Management Committees	Executive Committee (EXCO)			
	Asset and Liability Committee (ALCO)			
	Audit, Risk and Compliance Committee (ARCC)			
	Country Credit Committee (CCC)			
	Operations and Technology Committee (OTCO)			
	Human Resources Committee (HRC)			
	Business Development Committee (BC)			
Company Secretary	Taylor Wessing			
	5 New Street Square			
	London EC4A 3TW			
Registered Office	Habib Bank Zurich plc			
	Habib House			
	42 Moorgate			
	London EC2R 6JJ			
Auditors	Mazars LLP, Statutory Auditor			
	Chartered Accountants			
	Tower Bridge House			
	St Katharine's Way			
	London E1W 1DD			
Legal Advisors	Saleem Malik			
	40 Eagle Lane			
	Snaresbrook			
	London E11 1PF			

Chairman's Message



On behalf of the Board of Directors of Habib Bank Zurich plc, I am pleased to share with you the 2020 Annual Report and Financial Statements.

In last year's message, I had briefly spoken on the uncertainty prevalent at the start of the global health crisis. This year's report documents the way our Bank responded to the onslaught of Covid 19, both social and financial. 2020 was a year of unprecedented challenges and left devastating consequences for millions around the globe and the UK. Our priorities were clear, to meet customers' needs, safeguard our colleagues and customers and work in tandem with the government/regulatory guidelines. The pages in this report tell the story of how our Bank came together in new ways to deliver for our team members, customers, communities and to play our part in addressing one of the world's biggest challenges.

By the grace of God, we navigated the difficulties in a resilient manner and with compassion in line with our ethos. During the year we supported our customers by taking several measures. These included increased engagement, underwriting new credit, reducing fees, deferring repayment obligations, keeping our 8 branch network open and ensuring there was little disruption to our services.

Despite the impact of the global health crisis, which resulted in a historically low interest rate environment, and a long period of uncertainty, our Bank remained profitable. We grew the balance sheet by 12%, increased customer deposits and advances and maintained a good liquidity profile. Net new disbursements however reduced due to lockdowns and market volatility, with an overall decline in revenue due to low interest rate environment felt specifically on our Investment book. Notwithstanding the challenges, our core customer revenue saw marginal growth, and as fears moderated, our Trade and FI business recorded its largest growth and was well supported by the newly launched Islamic Banking initiative under the 'Sirat' banner. We maintained a strong Capital Ratio alongside Non-Performing Loans to Total Advances ratio of 3%, which is a reflection of our robust underwriting standards and credit management. Under the circumstances, I find these results satisfactory and in line with our focus on responsible growth and financial soundness.

We place great emphasis on good governance as a vital foundation for a successful organisation. The Board worked closely with the CEO and the executive team to ensure that the Bank remained aligned with the business strategy and regulatory expectations. The Board also held additional meetings periodically during the pandemic to maintain oversight. Through its oversight, the Board takes comfort that the executive team delivered an efficient response whilst maintaining a robust control framework.

The country has made admirable progress through the vaccination programme rollout and government support for the people and businesses. There is no doubt that the effects of the pandemic will continue to impact our daily lives for some time. However, we are cautiously optimistic in the resilience of the British economy and take comfort from the predictions of steady economic recovery during 2021/22.

I would like to conclude by extending my appreciation to our colleagues in the UK for their tireless, steadfast commitment and the senior leadership for their professionalism and hard work. I was ably supported by the Board members, specifically the independent directors, during the year and would like to thank them for their guidance and support. Above all, I would like to thank our customers for their loyalty and patronage – I wish them well for 2021.

Muhammad H. Habib
Chairman

CEO Statement

Early March last year, UK's total Covid 19 infections were less than a 100, who would have guessed that in the next 12 months, this number will exceed 4 million, and in excess of 125 thousand people in the UK will lose their lives. This unprecedented year, which saw human life in peril, government borrowing crossing £350B, where everyone has had to adapt and evolve – to merely survive, was not only unsettling but extremely arduous.

In the previous Annual Report, we had noted that the Covid 19 pandemic will have a serious impact to the economy. It did, not just serious but a devastating once in a lifetime experience, which inflicted extraordinary damage. Despite this inexplicable calamity, the precipitous grit of the team, loyalty of our customers and support from the Board including shareholders, helped us manage its harsh effect. The Bank navigated well through the severity on interest rates, credit portfolios and volatility. Inspired from our core values of commitment and teamwork, we held numerous team meetings mostly daily, engaged continuously with our clients and innovated every day to preserve the financial and operational integrity of the Bank. The Bank remained operational at all times during the crisis, providing high level of customer service underpinning the duty of care and commitment to the community, at a time when needed most.

Like any other manager, my biggest challenge was to ensure people's safety and operational continuity. It is with great admiration that I can say that in the last 14 months, we have succeeded in achieving this, collectively, as a team. I can acknowledge with humility and pride that neither our energy levels were jeopardised throughout national lockdowns nor did we flinch in our steadfast resolve to serve our customers. As is evident through the balance sheet which grew 12% in the year, the Bank continued to accelerate investment in new products, services, technology and human capital. One of the key achievements made in 2020 was the successful launch of our two Islamic Financing products; Diminishing Musharika and Commodity Murabaha under the existing brand "Sirat". The Bank now offers a full range of Islamic deposits and financing products in the UK through its network of 8 branches. Covid 19 affected both International trade and domestic consumption and globally the merchandise trade had declined. We needed to adapt and shift our gears which could fill this gap. We continued with our direct beneficiary marketing strategy with the origination of the LC business from our FI network. We focussed on Trade corridors where we had a credit appetite and capitalised on the gap – mainly driven by exceeding service expectations – in the market. This simple yet impactful approach helped us double our Trade and FI business this year and perform better than the planned budget. Outsourcing Trade services, enhancements in Web banking / Visa debit card and introduction of Islamic e-Deposits are few other successes we achieved during this difficult period.

The Bank also capitalised on initiatives taken in recent years of good corporate governance, efficient use of resources and vigilant lending alongside strong client engagement. Trust, Integrity and Respect were the most valuable features – integral to our vision that we had on offer to our customers and they played out well for us.

My thoughts remain with the families of our employees and clients, who have either lost a member or a friend. And to that end, of the dear colleague we lost and family who has been affected. For most people, the defining memory of 2020 will be the Covid 19 pandemic, which is still with us and has had such devastating consequences for the lives and livelihoods of millions around the world.

The Silver lining

Similar to the experience of many organisations, 2020 offered us the opportunity to explore and capitalise on creativity and productivity to hold or even at times ramp up services level through introduction of new technology.

We maintained our 'high touch client relationship-based model' making use of video conferencing channels, which allowed us to reach larger customer base across many jurisdictions more frequently. It was really motivating to see the team jell together by standing up to do whatever was required to keep the business running in a normal way. Collective wisdom was the key to faster and better decision-making, a capability we crave to sustain going forward.

During this challenging time empathy was another key factor which kept the advancement going. When difficulties closed doors, new avenues and opportunities emerged. During the lockdowns, through various credit, moratorium related meetings, as managers and team leaders we got an opportunity to better understand the challenges our teams and customers faced. We became more self-aware of relationships, time, and the worth of a normal life. I am happy to say that as a team we were able to create an environment where the frontline was able to focus on customer well-being, understanding the challenges and meeting their requirements taking into account the market pulse and regulatory guidance. Investment made in an effective risk management process over the years allowed the Bank to stay on course through a balanced approach. We remained engaged with the BoE, the PRA and the FCA and their guidance relating to moratorium and tailored support, including keeping the Bank a viable business.

Regular communication with customers and employees also played a pivotal role in keeping them abreast with the measures and processes introduced to manage the risks posed by the pandemic. We aspire to keep this channel open in future.

Working together and meeting expectations

Covid 19 has been an ultimate test of our commitment to service, we always knew that it is vital, but in the year, we continued to develop our expertise using a wide range of resources. As part of our transformation, we increased our use of technology to improve our services and make it more efficient and reliable for our customers and employees. The Bank extended wide-ranging suite of its services onto a secure online platform without compromising its rigorous compliance and security standards to ensure that our customers have the flexibility to manage their primary banking needs online. Web banking remains fundamental to our strategy – and we will continue to develop our offering by utilising technology to create excellent customer outcomes.

The continuity of services could only be achieved with the ability to operate remotely in pandemic environment. Facilities were put in place within a short period of time and processes were set up accordingly to ensure that our employees can provide uninterrupted services to customers. This also allowed the Bank to work in accordance with government guidance to stay at home and protect lives thus putting less pressure on NHS. As a team we also reacted fast in making our offices a secured working place by introducing social distancing measures such as restricting number of staff in office premises, using multiple locations and staggered working hours.

Our staff and customers joined forces to help those working across the NHS and Care services to support them in their heroic efforts in these unprecedented times by donating through JustGiving page. A big thank you from HBZ Team to all those who supported us in this cause.

During the peak of the pandemic, the Bank successfully outsourced its trade finance operations to its Group Outsourcing centre based in UAE. It has been a few months since the migration of responsibility has taken place and the experience so far has been very positive. As mentioned earlier, we really feel proud – in securing a 100% plus growth in trade finance business in 2020, which was not possible without this strategic shift.

When normal services face severe challenges, other important issues such as climate change and social inequality, can be at risk of being exacerbated or put on the back burner as a result of the pandemic. We kept a focus on the aforementioned issues and regulatory priorities including LIBOR transition, negative interest rate to make progress under Board oversight.

Specifically on climate change – the Bank has put in place a high-level implementation plan to manage financial risks arising from it. The approach to managing this risk will entail review of business strategy, risk management and decision-making process. As part of developing a comprehensive framework and risk appetite, a materiality assessment has been undertaken by the Bank to establish existing/foreseeable exposure and segments/geographies susceptible to climate change in which the Bank operates. The three board risk categories considered by the Bank includes credit risk, financial/market risk and operational risk identified across all sectors. By continuing to make progress in this area, the Bank is enhancing its understanding of the long and short-term financial risks in relation to climate change. This should be strengthened through the use of scenario testing and forward-looking catastrophe modelling. With management focus and Board oversight, we will ensure that consideration for this emerging risk is embedded in our risk management and governance framework.

Performance Highlights

Early in the 2nd quarter we became acutely aware of what was on the horizon – whilst some of it can be ascribed to a fractured economic system due to the lockdown, it is also driven by changing customer behaviour. Over the last year we raised a positive thrust that was gained by executing our strategy for driving sustainable growth even in a difficult macroeconomic period. The Bank managed an improved lending performance during the period, resulting in 6% increase in the lending portfolio. Our cautious and prudent credit underwriting process ensured that the lending portfolio largely remained protected despite severe economic stress observed in 2020. The Bank supported its customers wherever they required assistance by understanding their business and financial needs. Range of measures were implemented such as payment holidays, waiver of penal interest and tailored support, which will continue in line with regulatory guidance. It is reflection of lending portfolio quality that the moratorium or tailored support trend has declined as the impact of pandemic softens with widespread vaccination and return of consumer confidence.

Our customers deposit base continued to maintain its growth as seen in recent years. We remained in close contact with our customers assuring them of continuous support and managed their expectations by allowing access to funds to meet their unanticipated commitments arising from Covid 19. Internet deposits played an important part in overall liquidity management as the Bank offered competitive rates in second quarter of 2020 to strengthen its funding base. Introduction of Sirat e-Deposits positioned the Bank in a unique space by offering both shariah compliant and conventional deposit products available through both branch network and online access.

While the balance sheet depicted sustained growth, the revenues took the brunt of pandemic impact. Interest rate cut by central banks with a consequent impact on LIBOR resulted in significant decline in return on money market and investments income. In addition, the Bank passed on the benefit of decrease in interest rate to its customers by reducing the HBZ Base Rate in April 2020. The decrease in interest income was partially offset by increase in fee and commission revenue mainly due to better performance from trade finance activities by 97%. The Bank also implemented cost optimisation measures to sustain the impact of sharp decline in revenues. Our regulatory capital position remains solid as a result of strong capitalisation and profit retention which demonstrate high level of commitment from our shareholders to the UK franchise.

The Future outlook

The successful rollout of vaccination program by the UK Government has provided the country a reason for hope and optimism. The extraordinary support extended to individuals and businesses by the Chancellors and Bank of England kept the economy running despite challenges never seen or encountered before. As I meet clients over Google and Zoom meetings, I constantly hear that the 4-phase approach of returning back to normality by June 2021 announced by the Government has inspired them and the business community at large in preparing itself to meet the pent-up demand.

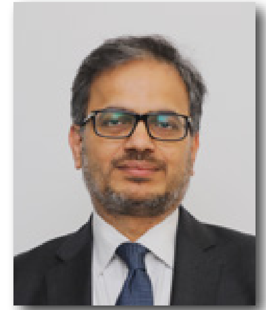
I am extremely honoured and privileged to have the strong team who has maintained our commitment by serving the clients and customers even in the very difficult circumstances. I am truly proud and inspired by the way our Bank has risen to this challenge – it epitomises the spirit of collaboration – with flexibility, resilience, responsibility and a caring heart. Despite uncertainties, we look forward to delivering our goals to our stakeholders in 2021. Together, we will ensure that a strong ethical and inclusive culture defines the way we do business at Habib Bank AG Zurich.

What we have done has mattered. What we will do in the coming months – which may be still replete with challenges, and there is no 'prescription' available – will be supported by our battle-tested commitment, confidence in knowing that we have the know-how, people, the purpose and what it takes to take care of clients' interest.

I will like to thank my staff, UK Board, group office and shareholders who provided unparalleled support and guidance to me and my team throughout 2020.

Satyajeet Roy
Chief Executive Officer

Strategic Report



The Board of Directors have the pleasure in presenting the Strategic Report for the year ended 31st December 2020 for Habib Bank Zurich plc (the "Bank"). The Strategic Report forms part of the Bank's Annual Report and Financial Statements. Habib Bank Zurich plc is the wholly owned UK incorporated subsidiary of Habib Bank AG Zurich, Switzerland.

Overview

The Strategic Report is provided to enable readers to assess Bank's financial position and results for the year 2020. This report also delivers a holistic picture of the Business model, Bank's strategic objectives, governance and significant developments which is useful to the stakeholders in assessing the performance and future prospects. This report includes a description of the evolving internal / external risks and uncertainties the Bank is currently facing with an analysis of its overall business and financial performance using key performance indicators.

The Covid 19 pandemic has had a damaging impact on economies around the world, causing a crisis that could never have been predicted earlier. The events arising from the pandemic have altered the outlook for the UK economy, and consequently the Bank plans set for 2020. The Bank, like many other organisations diverted its resources and efforts towards well-being and safety of its staff and customers. It tested the operational resilience and financially stability to ensure that the strength of capital and liquidity levels are sufficient to absorb the economic shocks and keep it serving the customers during this time of need.

One year since the announcement of first lockdown the Bank has emerged as a fighting unit showing its strength and strong bonding with customers. Despite strong headwinds, the Bank's business and financial performance remained resilient exhibiting growth in both customer lending and deposits.

Principal activity

The Bank's target market in the UK is frequently geared towards real estate investments, trading activities, services and small-scale manufacturing. Our customers' banking needs are catered by conventional and Islamic retail and commercial banking products.

Customers mainly engage with the branch relationship team and takes comfort in continuity with a relationship manager and quick turnaround on their requests as well as continued access to the decision makers at the Bank.

The business lines offered by the Bank to its customers include retail banking comprising current and savings accounts and commercial banking which offers real estate finance, trade finance, cash management and treasury services across various currencies. Our latest offerings are a range of Islamic personal and business banking products under the brand name "Sirat".

We continued to support our customers and small businesses by delivering against commitments associated with our long-term strategy. The services are provided through a network of eight branches across the UK.

We are focussed on building long-term value for our customers, employees, suppliers, communities we serve and our shareholders.

Strategy and objectives

The Bank's strategy has been developed with main objective to meet customers and clients' end-to-end needs. The Bank's core value is grounded in 'Service with Security' by placing customers at the heart of our decisions.

Our approach as a community Bank is to focus on delivering personalised services with security to a wide spectrum of business and personal customers from our niche markets. This means listening to our customers, understanding their priorities and adapting our products and services to ensure we have the capabilities to support their evolving needs.

The Bank's primary customer base and target market are often family-owned and managed businesses from the South Asian Diaspora owned by SMEs or high net worth individuals. These traditionally mercantile communities are known for their business and entrepreneurial traits. The key attribute of this segment is generational continuation and expansion of their business interests across generations. This is a substantial and growing segment, which provides an opportunity for the Bank to build a sustainable business model.

2020 was a highly varied and challenging year for the Bank, which required immediate actions to support our customers impacted by the pandemic. There were some immediate actions taken to manage the impact of Covid 19, however, the strategic direction remained unchanged. We continued to grow our real estate lending business. Initiatives planned for 2020 to launch Islamic lending products and increase Trade Finance activities were achieved. Daily senior management committee meetings were held covering all key business and risk areas along with frequent oversight by the Board. Continuous improvement in governance, risk management and controls over processing was considered as part of business as usual.

Technology remained at the forefront in delivering efficient customer services. Our capability in technology solutions was ably demonstrated by the IT leadership team by providing a secure remote working solution in a short span of time. Creative technology solutions combined with the Bank's set of digital offerings and strong remote working framework ensured service and operational continuity for internal and external stakeholders via secure and robust channels. As part of our transformation, we are using technology to improve our services and make it more efficient for our customers. We are continuously improving our transactional services through various enhancements such as alerts, improved FPS arrangements, contactless debit card etc. We are committed to convert technology experience for our customers parallel to their needs and expectations.

The Bank adopted the guidance provided by the Prudential Regulation Authority (PRA) to the banks on the exceptional circumstances arising out of the coronavirus pandemic and its impact on the financial situation of borrowing customers. The guidance entails for consistent and robust application of IFRS 9 and the regulatory capital requirements to Covid 19 related payment deferrals. In particular, the guidance in the PRA's March and June 2020 letters on the treatment of borrowers that breach covenants due to Covid 19, on IFRS 9 expected credit loss (ECL) model risk, and on the need for post-core ECL model adjustments, which were part of the Bank's ECL calculation methodology.

Following the guidance, a comprehensive risk assessment process was followed by the Bank in evaluating the moratorium needs of customers, which included discussion with the customers, understanding their cash flow and liquidity needs and making available the support they needed to continue their businesses. We continue to support our customers as they navigate through the pandemic in the form of tailored support wherever required. It is very encouraging to observe that most of the impacted customers have successfully managed the pandemic impact with only a small number requiring ongoing support.

We are confident that our strategy will deliver better results in the future. Although the pandemic is not over yet we are beginning to see some positive signs. The UK vaccination program is progressing smoothly through hard work of our NHS and volunteers, which is a cause for optimism.

Business Model

The Bank's business model is built upon delivering high quality service and taking a long-term view on building customer relationships. The model is geared towards focusing on selected segments to deliver on strategic objectives. The Bank's core value of 'Service with security' has led to a natural longevity in customer relationships, which are cross-generational and cross-border, strengthening the Bank's reputation as a businessman's bank. Owing to its history from the Indian subcontinent and based on the intrinsic value of the Bank as a family-owned conservative financial institution, customers identify the brand with security and trust.

The Bank offers two main services; real estate finance and commercial banking services. The Bank also offers regular cash management, trade finance and retail banking in line with the customer needs. It remained focused on the strategic areas that include customer, financial planning, processes, people, regulatory and treasury. The Bank's product and service offering is comprised of buy-to-let finance, commercial loans, working capital finance, current accounts, savings accounts, notice accounts, fixed term deposits and treasury services. It also offers fixed term bonds accessible directly through the web-based channel.

The Bank had introduced an Islamic Banking Window branded as 'Sirat' aligned to the Bank's customer-centric approach and vision. In 2019 'Sirat' offered selected Shariah-compliant deposits products to existing and new clients. In 2020, in line with its commitment and despite Covid 19 outbreak, the Bank launched its 'Sirat' financing products of Diminishing Musharika and Commodity Murabaha managed by a dedicated Sirat team, which has a UK-wide mandate. The Bank also successfully launched 'Sirat' e-Deposits in the summer of 2020 thus completing its full range of Islamic banking offering.

Another area of business in which the Bank excelled in 2020 was Trade Finance. The Bank revived its position as an active trade finance bank in the UK and now captures complete value chain of export business with focused marketing across a broad geography spanning Africa, China, Turkey in addition to the South Asian countries. We anticipate that this business will grow into larger value and a higher volume of transactions in the next year as we are winning business from large corporates in the UK with a client-centric proposition with efficient product delivery. The positive impact on our export LC business would have not been possible without the support of Group FI. To enhance operational capacity the Bank outsourced its trade service and finance transactions processing activity to Group Outsourcing centre based in the UAE in 2020.

The intermediary channel continues to remain a source of lending, customer referrals and also provides diversification in our business acquisition channels. We envisage a deeper role of Intermediaries in expansion of lending, business base through introduction of new to business customers. The Bank customer onboarding from intermediaries is similar to introductions made through relationship managers, which includes full control of client relationships from on-boarding to credit underwriting and service delivery. This enables products to be offered through intermediaries comprising of commercial lending, residential and commercial buy-to-let and mixed use buy-to-let mortgages and are designed to be flexible and collaborative so that the Bank can adopt the most appropriate strategy for intermediaries and their clients.

The Bank during the year became member of the Discount Window Facility (DWF) of the Bank of England (BoE) which operates under the Sterling Market Framework (SMF). This is a significant change which allows the Bank to borrow from the BoE by pledging eligible collateral. It is a tool which can be used in the event of any stress on liquidity without having to sell available eligible securities.

The Bank also became a member of Term Funding Scheme with additional incentives for SME (TFSME) introduced by Bank of England as a measure to incentivise eligible participants to provide credit to businesses and households to bridge through the current period of economic disruption caused by the outbreak of Covid 19.

Business Review

We continue to make progress on our sustainable business model through practical risk management measures, effective liquidity and capital management and meeting the requirements of the changing regulatory environment.

The Bank deployed a cautious approach towards lending business taking into account market conditions. All lending proposals were dealt on a risk-based approach, which allowed the Bank to continue serving its customers without impacting the quality of the credit portfolio. The Bank disbursed £67m of loans to new and existing customers. Net growth in lending business of £26m was mainly driven by Sirat and increase in Trade Finance funded exposure. Recognising the support expected by customers in the time of real uncertainty, the Bank ensured that relationship managers remained in close contact with customers to understand their circumstances and managing their needs. Throughout this process we were guided by our core values of trust and commitment.

The Bank witnessed an impressive start to its Sirat business in 2020 which is expected to grow further in 2021 as the market has substantial demand with few banks in place to offer such services. The Bank has a dedicated team supported by network of branches to build on this new initiative.

Another key area of business focus in 2020 was deposit growth. After going through a challenging second quarter where the Bank supported its customers by allowing them access to funding, it witnessed a strong growth in deposit base in the second half of 2020. The Bank made an effective use of Internet deposit channel by building up a base, which supported the liquidity and funding needs.

The Bank recognises that Covid 19 had a significant negative impact on the UK economy, which will take some time to recover. Various lock-downs impacted many businesses which will find it hard to survive in these depressed economic conditions. The UK government is continuously supporting businesses and individuals to keep the economy running. However, any meaningful recovery is likely to come towards the end of 2021 when a large part of the population has been vaccinated. The Bank is ready to navigate the tide as it has a strong capital and funding base supported by an effective risk management process.

The Bank has started work on renovating its landmark building, Habib House, situated at Moorgate which is at the heart of the City of London. The project involves complete change of the mechanical and electrical plant with a contemporary looking branch, which will reflect our culture and core values. The renovation project is expected to complete by the mid of 2022.

Financial Review

Balance sheet depicted a double-digit growth of 12% from the last year, which is a testimony to the Bank's resilience in uncertain conditions. The considerable growth is evident by the Bank's continued progress towards its strategic objectives. Loans and advances to customers increased by 6% to £455.95m reflecting positive growth in lending despite the economic uncertainties seen in 2020 related to Covid 19 mainly contributed by 'Sirat' an initiative taken in 2020.

Total Investment increased by 23% due to an increase in the size of Bond portfolio as the Bank invested some of the surplus liquidity it generated.

This year saw a significant increase in the trade finance business through expansion and strengthening of correspondent banking relationships with FIs, establishing account relationship with the beneficiaries and delivering on business growth through larger value/higher volume of transactions.

Customer deposits showed a growth of 8% as compared to 2019 due to a well-managed liability strategy. Internet deposits continue to remain a key part of Bank's overall liability strategy, which also serves the diversification objective and Bank's brand awareness to a wider market audience.

The Bank continues to monitor various models which are being used in the calculation of Expected credit losses (ECL) as required by IFRS 9. No changes were made in the ECL models during the year as they were considered to be appropriate by the Bank. The Bank decided to apply Post Model Adjustments (PMA) on the ECL outcome determined through a refresh of the macroeconomic model. A detailed analysis was carried out by the Bank by comparing the results from macroeconomic refresh and actual performance of the portfolio during the pandemic. The Bank has used unemployment rate and Government debt to GDP ratio as Macroeconomic Variables (MEV), which significantly deteriorated from 2019 when the MEV were last updated.

The Bank is in the process of updating its ECL models as part of group wide exercise with the help of market leading consultants. The exercise is expected to be completed by mid of 2021.

Balance sheet analysis

	2020 (£ 000')	2019 (£ 000')
Assets		
Loans and advances to customers	455,954	430,233
Balances with banks	191,267	157,262
Financial investments	104,357	84,586
Other	10,555	11,195
Total Assets	**762,133**	**683,276**
Liabilities and Equity		
Due to customers	623,644	577,013
Due to Banks	40,091	6,722
Subordinated liabilities	20,063	20,098
Tier 1 Capital / Equity	72,182	71,474
Other	6,153	7,969
Total Liabilities and Equity	**762,133**	**683,276**

Profit and Loss Analysis

The Bank remained profitable during 2020 with a net profit after taxation of £0.60 million in 2020 (2019: £3.48 million). The net operating income of the Bank decreased by 8% in 2020 (£17.97 million compared to £19.61 million in 2019). The decrease was mainly driven by the drop in interest rates and lower lending as the customers postponed investment decisions due to severe economic uncertainty resulting from series of lock-downs. Net fee and commission income increased which was mainly attributed to trade finance Export LC business.

The financial highlights for 2020 are provided below

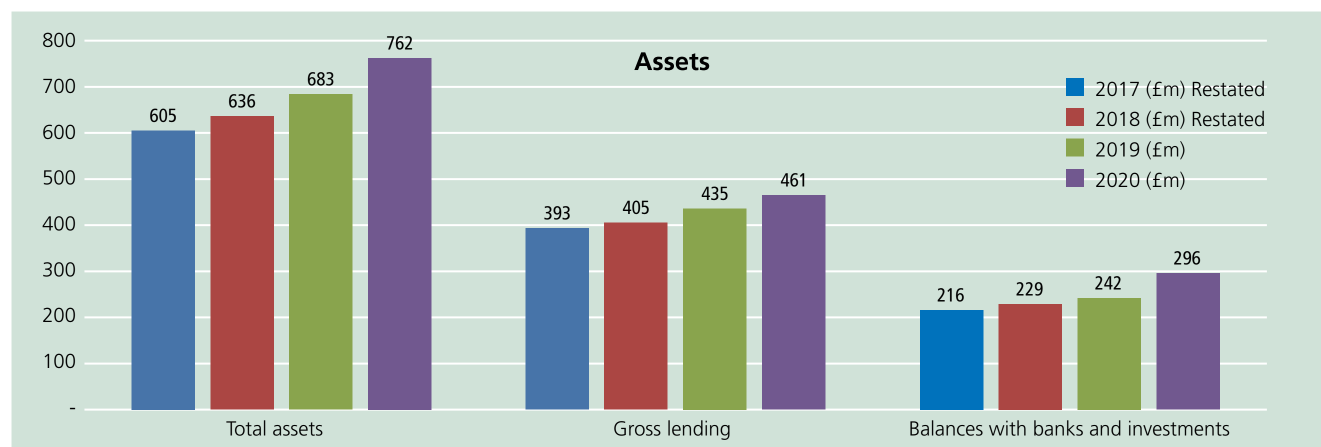
	2020 (£ 000')	2019 (£ 000')
Operating Profit		
Net interest income	15,989	17,395
Net fee and Commission income	1,490	1,310
Net other income	486	908
Net operating income	**17,965**	**19,613**
Total operating expenses	(16,688)	(16,176)
Operating profit before impairment losses on loans and advances and tax expenses	**1,277**	**3,437**
Credit impairment losses / reversals on financial assets	(588)	303
Profit before tax	**689**	**3,740**
Taxation	(89)	(256)
Profit after Tax	**600**	**3,484**

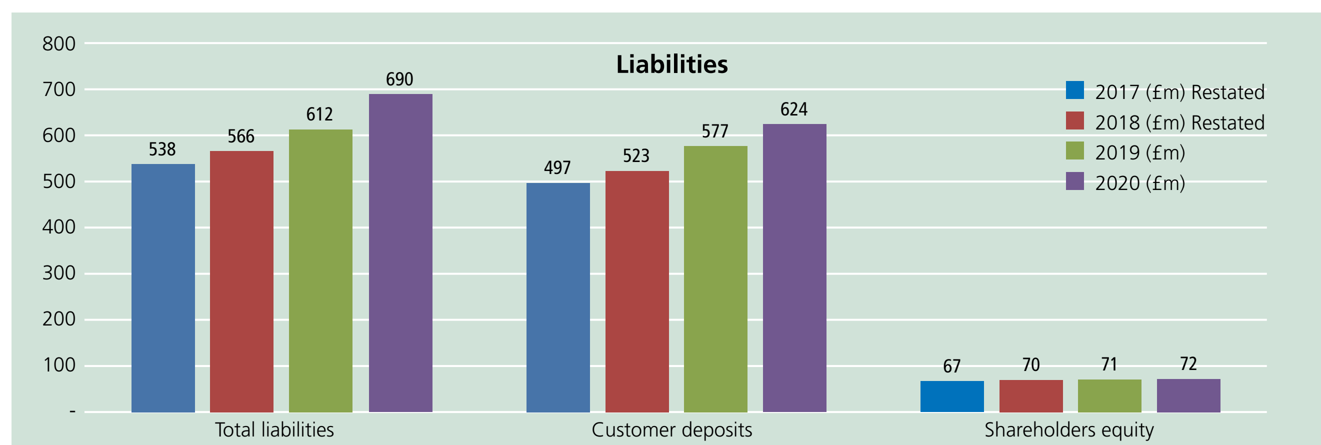
Net interest income of £15.99 million (2019: £17.40 million) including the interest received from customer loans, return from investment portfolio and interest on placement with banks. The financial markets in 2020 were challenging, with continuing pressure on margins. As a result of significant rate cut by the Bank of England and Federal Reserve the LIBOR dropped significantly across all tenor. This significantly impacted the investments income and return from money market placements.

Operating expenditure mainly represents staff and other operating expenses incurred during the year for the Bank's operations. Total Operating expenses of £16.69m include total staff costs of £10.81m and other operating costs £4.91m. Group direct costs paid by the Bank during 2020 are also included in operating expenses.

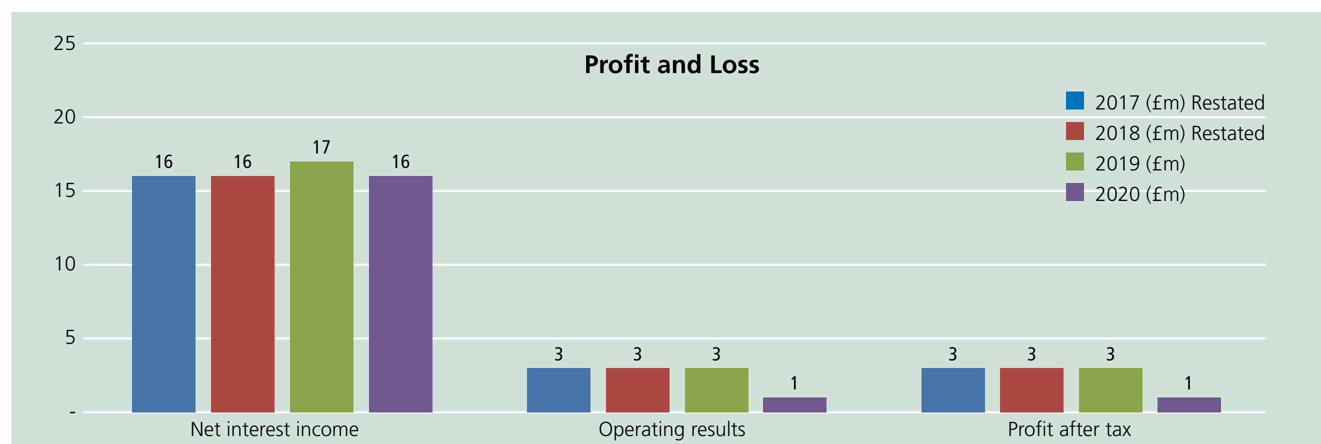
The following charts provide the key financial highlights of the Bank from the year 2017.

Assets and Liabilities





Profit and loss



* 2017 results exclude receipt of insurance claim

Capital structure

The Bank has a strong capital base with net equity of £72 million (2019: £71 million) and a five-year subordinated loan of £20 million (2019: £20 million) to support long-term asset growth and cover risks inherent to the business. Such strength in capital allows the Bank to deploy funds in areas that provide sustainable returns in line with the set objectives. The subordinated loan of £20m was renewed by the parent bank for another period of 5 years in March 2021 meeting the regulatory requirement to be classified as Tier 2 capital.

The regulatory capital base differs slightly from the amount reported above due to the different treatment of certain reserves. The Bank's regulatory capital and risk-weighted assets are summarised below:

		£ in million
Description	2020	2019
Share capital – Tier 1	60.00	60.00
Retained earnings – Tier 1	11.83	11.23
Subordinated loan – Tier 2	20.54	20.43
Risk-weighted assets	513.95	442.49

The Bank's total capital requirement (TCR) is calculated as follows:

		£ in million
	2020	2019
Risk weighted assets (£ million)	513.95	442.49
Total capital requirement – TCR (£ million)	71.03	61.15
Capital		
Share capital – Tier 1 (£ million)	60.00	60.00
Retained earnings	11.83	11.23
Subordinated liabilities – Tier 2 (£ million)	20.54	20.43
	92.37	91.66
Excess capital over requirement (£ million)	**21.34**	**30.51**

The capital adequacy ratio as of 31 December 2020 was 17.85% (2019: 19.93%), which was in surplus of the regulatory requirements. The Bank has already performed various stress tests in its Individual Capital Adequacy Assessment Process (ICAAP) and find the capital quite adequate to meet unforeseen shocks. The Bank also believes that the current strength of its capital would mitigate the current stress of Coronavirus outbreak.

Other Key regulatory ratios

The Bank maintained sufficient high-quality liquid assets ("HQLA") against the net cash outflows over a 30-day horizon on a daily basis. The Bank maintains its liquidity coverage ratio ("LCR") above the regulatory threshold at all times as set out by the Prudential Regulation Authority ("PRA"). The Bank maintained LCR of 227% as at 31 December 2020 (2019: 160%) as compared to a 100% regulatory threshold. Increase in LCR was mainly due to maintaining the high liquidity to meet any urgent and unforeseen funding requirements.

The Bank continues to monitor its liquidity position by taking into consideration impact of large outflows by customers due to Covid 19. Keeping in view strong liquidity position, vigorous monitoring process and the pattern observed during the peak of the covid pandemic, the Bank believes that it will be able to meet any plausible stress on its liquidity due to Coronavirus outbreak.

The Bank's leverage ratio as of 31 December 2020 was 8.9% (2019: 9.5%) as against the regulatory threshold of 3%.

Customer related contingent liabilities largely comprise trade finance business including letters of credit, guarantees and undrawn commitments.

Key performance Indicators (“KPIs”)

The Bank uses a broad range of financial and non-financial measures to evaluate the performance and trends against the strategic objectives. These quantifiable measures remained helpful not only to evaluate the Bank’s performance but also keep the management well aware of any anticipated issues specifically during the time of pandemic.

Monitoring the right vital signs has always been essential for informing key decisions. The coronavirus pandemic hasn’t changed that, but many businesses have changed what they consider a vital sign and how to measure it. To deal with the ongoing health and economic impacts of the pandemic, the Bank revisited the originally set KPIs, added new ones, and changed where required.

To assess our performance, we use a number of sources including regular management reporting of our key metrics; as well as balanced scorecard to look at the business from customer, commercial, colleague and control aspects for continuous improvement. The process allows the branch managers to self-evaluate their performance against given targets and the management to keep an oversight on business performance against targets.

We consider a range of metrics across all stakeholder groups and continuously assess whether new measures should be added or removed from our dashboards, in order to ensure these remains relevant and appropriate to our strategy.

Keeping in view the Bank’s business activities, performance of customer loans and deposits, profitability, capital adequacy, liquidity monitoring and operations and technology risks have been considered more important by the Directors than to other risks and considered by the management as part of its KPI.

Some of the key KPIs’ monitored by the Bank includes:

KPI	2020	2019
Percentage increase in customer loans	6%	8%
Percentage increase in customers deposits	8%	10%
Non-performing loan as a % of loan book	3%	2%
Percentage of non-interest revenue to total revenue	11%	11%
Loan to deposit ratio	73%	75%
Return on Assets	0.1%	0.5%
Return on Equity	0.8%	4.9%
Capital adequacy ratio	17.85%	19.93%
Common equity tier 1 ratio	13.86%	15.32%

As mentioned above in the financial review section, the Bank's revenue was impacted by reduction in net interest margin which is reflected in the reduction in return on assets and equity. Capital adequacy reduced mainly due to increase in risk weighted assets reflected through increase in customer loans, investments and banks placements. The Bank's overall financial performance continues to remain structurally strong.

Capital adequacy measures the Bank's capital strength, expressed as a ratio of total capital to risk-weighted assets. By having a mix of high-quality assets and capital free of deductions, the Bank maintained a capital adequacy ratio above the required regulatory requirement. The available capital resources of £92.37 million are considered sufficient with a view to support the business over a five-year period, which is demonstrated through the individual capital adequacy and assessment process ("ICAAP").

The ICAAP document summarises and demonstrates to the Board and to senior management that the Bank has adequate financial and capital resources to support its business and the risks attached to its business plan and model. The ICAAP also demonstrates the adequacy of non-financial resources (in the form of people, systems, policies and procedures) to manage the adequacy of these financial resources on an ongoing basis.

The Bank maintains a liquid balance sheet in the form of HQLA and non HQLA assets and placements with banks with a tenor of up to 12 months. The customer deposit base is sticky and stable with a mix of relationship-based retail depositors and business owners. Fixed rate bonds act as a source of well diversified deposit base, which continues when priced in line with market offering. The Bank's liquidity risk is managed by the Treasury function with oversight from the ALCO and the BRC.

Operation and technology risks have emerged as a major risk for the banking sector in the past few years on the risk matrix. This refers to the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. To mitigate the risk, the Bank has put in place a robust risk event reporting process alongside self-assessment of an internal control system ("ICS") and risk control self-assessment ("RCSA") process. The Operations and Technology Committee ("OTCO") is responsible for monitoring of the risk with oversight from BRC. All operational risk events are analysed in detail in OTCO with appropriate control measures put in place through root cause analysis. The operational risk profile of the Bank remains stable.

Principal risks and uncertainty and mitigation plan

Bank confronts number of financial and non-financial risks arising both from external and internal factors. These risks are addressed through a comprehensive risk management framework centred around the embedding of a strong risk culture.

The management of risk is a critical underpinning to the execution of the Banks strategy. The Bank's risk appetite is set by the Board of Directors and takes into account the Bank's Strategic Intent. The executive management of the Bank is responsible for implementation of the risk appetite throughout the Bank's operations and business. The Board Risk Committee (BRC) maintains oversight of the business performance against the risk appetite. The material risks and uncertainties the Bank faces across its business and portfolios are key areas of management focus.

The Bank's approach to Risk Management is built on the principle of low to medium risk appetite and investment return horizon, which is medium to long term. In order to achieve this, the Bank's business strategy is built on:

- A clearly defined target market (selected customer and industry segments).
- Relationship-based banking service.
- Comprehensive governance and control framework.

The key elements of the Bank's risk management framework are as follows:

- Governance at the Board and Management level.
- Risk oversight.
- Risk management controls.
- The Bank's risk management strategy and risk appetite are aligned with its motto 'Service with security', core values and strategic intent of delivering sustainable growth.

The Bank's risk appetite is articulated in the Risk Appetite Statements set by the Board of Directors. The Bank takes a conservative view on the inherent risks and has zero tolerance for financial crime, compliance and regulatory risks. All risk types are measured and monitored through identification, measurement, mitigation and escalation processes from management to the Board level.

The table below highlights the key risks that the Bank is exposed to and provides details of the measures taken to mitigate these risks.

Risk type	Tolerance and mitigation
Credit risk	The Bank's mitigation of credit risk is based on a combination of focused strategy, defined target market, secured lending and quality of underwriting, ongoing monitoring and pre-set thresholds for single party exposure, industry concentration and type of collateral. The Bank has a well-defined and articulated credit risk management framework ("CRMF"), which comprises its credit risk appetite, credit policies, terms of reference of management and board level committees, target market analysis, collateral management, credit monitoring and other credit related policies. The Board Risk Committee ("BRC") has oversight responsibilities of the CRMF. The Country Credit Committee ("CCC") and Board Risk Committee review and approve credit exposures based on delegated authorities. The Bank has put in place detailed policies and guidance for the business and credit team to deal with impact of IFRS 9. Regular monitoring of credit portfolio is carried out by analytics team which provides early warning to business team where customers start showing irregular repayments. Regular interaction between customers and relationship managers also helps in identifying any issues which might lead to significant increase in credit risk. Indicators if any, identified are closely monitored through a well-established watch list process in place. One of the key focus areas of the Bank during the pandemic was effective credit risk management. The credit team carried out frequent rapid reviews of the portfolio covering industries and sectors more severely affected by Covid 19 such as hospitality and travel. Frequency of CCC meetings was also increased along with increase in number of BRC meetings where the members met on monthly basis during the height of the pandemic. Business was at the forefront of managing customers who requested for moratorium, which were evaluated by credit risk function prior to being discussed and approved in the CCC meetings. System changes were introduced to manage deferred principal and interest payments to ensure that the customers receive timely and accurate information.

Risk type	Tolerance and mitigation
Concentration risk	The Bank has clearly articulated its risk appetite with respect to concentration risk. This is determined by taking into consideration concentration risk arising from single name, industry, product and geographical concentration. Concentration risk is discussed and managed at CCC, ALCO and BRC level. The Bank has put in place strong underwriting standards, portfolio monitoring process and early warning triggers to manage this risk.
Operational risk	The Bank manages operational risk through an articulated risk appetite and ongoing monitoring with oversight at management and board level committees. The Bank has a fully operational risk control function, which monitors various operational risks. The Bank sets various tolerance trigger points in accordance with regulation and guidance from the UK Financial Conduct Authority ("FCA") and Prudential Regulation Authority ("PRA"). In the event of these tolerances being breached, reporting to the Operations and Technology Committee ("OTCO") is made. OTCO reviews the breaches and considers whether further escalation to Audit, Risk and Compliance Committee ("ARCC") and Executive Committee is required. Reporting is made together with confirmation of remediation plans.
Financial crime risk	The Bank has in place a robust anti-money laundering ("AML") governance process supported by three lines of defence. The Board Audit and Compliance Committee is primarily responsible for oversight of financial crime risk supported by the Executive Committee of the Bank. A compliance dashboard, which incorporates risk events and regulatory updates, is reviewed and reported to the committees for oversight. The Bank has a zero tolerance for financial crime and is vigilant to identify, report and take appropriate action to mitigate the inherent risk associated with financial crime. Risk identification and mitigation is undertaken through risk assessment, effective implementation of customers due diligence requirements and ongoing account and transaction monitoring process. The Bank has comprehensive AML policies and procedures in place, which are reviewed and up dated regularly. The Bank provides continuous training to its staff in the areas of AML and compliance.
Conduct risk	The Bank is a service-oriented institution and therefore managing customer outcomes is central to the Bank's philosophy, business strategy and operations. The Bank has in place robust controls, adequate skill sets and appropriate decision-making arrangements to deliver its objectives of understanding customer needs, ensuring fair treatment and pro-actively preventing poor outcomes for its customers. The Bank has an articulated conduct risk appetite, which is driven by best customer outcome. The Audit, Risk and Compliance Committee and Board Audit and Compliance Committee monitor business performance against the risk appetite at management and board level respectively. The Bank has implemented the requirements under a Senior Managers and Certification Regime, assigning prescribed responsibilities and application of certification and conduct regime requirements. The Bank arranged adequate training for its employees, including senior management and members of the board, to ensure awareness and assist in implementing the requirements. Staff members meeting the certification requirements are identified through a robust process and undergo relevant training on an ongoing basis.

Risk type	Tolerance and mitigation
Capital risk	The Bank's capital structure has been built up to support the business over a long-term horizon and meet regulatory requirements. These include capital resources to cover Pillar 1, Pillar 2, Capital Requirement Directives ("CRD") Buffers and PRA Buffer. The Bank also maintains internal capital buffers over and above the minimum regulatory capital requirement. ALCO and Executive Committee monitor adequacy of capital with oversight from the Board Risk Committee.
Liquidity and funding risk	The Bank manages the maturities of its assets and liabilities and its cash flows on a daily basis. The Bank maintains substantial liquidity in the Bank of England Reserve account, high quality liquid assets and in short-term deposits. The Bank has early warning indicators in place, which are monitored at operational and management committee levels. The Bank's customer deposit base is stable and considered sticky based on long-term relationships. The Bank's depositor base mainly comprises relationship-based retail and SME deposits. The Bank also offers 6 and 12 months fixed-rate web-based deposits, which are mainly a rate-driven source of funding. To ensure the Bank has access to funding sources various measures were taken by the bank including access to BoE facilities under Sterling Monitory Framework, which includes Indexed Long Term Repo facility, Discount Window facility and Term funding for SMEs. In addition, the Bank has also entered into bilateral repo arrangements with other counterparty to gain access to funding by utilising its stock of investments as collateral.
Interest rate risk	Interest rate risk at the Bank is well managed and contained under oversight from ALCO and BRC. The Bank has no significant or complex long-term interest rate positions. The Bank effectively monitors interest rate risk in the banking book ("IRRBB"), through range of stress scenarios on economic value of equity and net interest margin. The Bank is also working actively to ensure its capability of implementing negative interest rate as communicated by the PRA.
Cyber risk	The Bank recognises risk associated with cyber threats and is constantly taking proactive measures to strengthen its operating environment to provide a secure banking experience to internal as well as external stakeholders. The Bank takes risks associated with cyber security extremely seriously and is constantly engaged in not only improving and strengthening its transactional gateways but also its internal operating environment.
Regulatory and legal	Regulations are constantly evolving and could adversely impact the Bank including capital, liquidity and funding requirements, enhanced data privacy requirements and the management of financial crime. The Bank implements new and updated regulatory requirements, where applicable, and incorporates the implications of related changes in its strategic and financial plans.
Foreign exchange risk	As the Bank does not maintain a trading book, it has minimal foreign exchange exposure risk. The foreign exchange exposures are managed by the treasury front office with defined levels of maximum allowable net open position in a single currency.

Emerging risks

Together with a strong governance process, the BRC receives regular information in respect of the risk profile of the Bank. Information received includes measures of risk profile against risk appetite as well as identification of new and emerging risks. We believe that our structure and governance support us in managing risk in the changing economic, political and market environments.

The Bank considers the following as emerging risks:

Risk type	Tolerance and mitigation
Climate change	Climate Change is a much-discussed topic in recent times at a global level. Risks highlighted by scientific research and changes in natural phenomenon have played a significant role is attracting focus at governmental level across the globe. Various initiatives have been introduced in the UK including legislation and regulatory requirements. As per the regulatory guidance the two risk factors that drive financials risks from climate change are Physical Risk and Transition Risk. Banks are expected to have an implementation plan which includes: **Governance** – embed the consideration of the financial risks from climate change in their governance arrangements; **Financial Risk Management Practice** – incorporate the financial risks from climate change into existing financial risk management practice; **Scenario Analysis** – use (long term) scenario analysis to inform strategy setting and risk assessment and identification; and **Disclosure** – develop an approach to disclosure on the financial risks from climate change. The approach set by the Bank to manage financial risks arising from climate change has consideration relating to: • Business Strategy • Risk Management • Decision making process Keeping the above in consideration the Bank is in the process of establishing a framework and risk appetite through a process which will involve: • Risk assessment • Identification of impact areas • Approach to setting tentative risk appetite • Risk indicators to be embedded in decision making process The Bank has undertaken a materiality assessment to establish existing/foreseeable exposure and segments/geographies susceptible to climate change from the Bank's perspective. Following this, existing risk types impacted by climate change risk are identified. As a natural outcome of materiality assessment and identification of existing risk types, a direction is proposed to: a) Establish a risk appetite including metrics for monitoring purposes b) Rating mechanism to be embedded in the decision-making process Given that the climate change risks are evolving, and the legal/regulatory approach is relatively at an early stage, regulatory expectation is that "firm's response to the financial risks from climate change to be proportionate to the nature, scale, and complexity of its business" and to mature over time.

Risk type	Tolerance and mitigation
Outsourcing and third-party risk management	The PRA published Supervisory Statement (SS) 2/21 in March 2021 which sets out expectations of how PRA-regulated firms should comply with regulatory requirements and expectations relating to outsourcing and third-party risk management. The statements cover PRA expectations relating to governance, pre outsourcing process such as risk assessment arrangements, due diligence of third parties, written agreements covering data security, access, audit and information rights, business continuity and exit strategies and record keeping. Banks are required to ensure implementation of the SS by March 2022. The Bank had taken into account PRA's consultation paper which predated the supervisory statement whilst revising or establishing new outsourcing arrangements in 2019-2020. The supervisory statement will inform the Bank's control framework for third party risk management.

The notes to the financial statements and Pillar 3 Disclosures provide further information about most of these risks; the committees that have the relevant responsibility for these risks; and the policies to manage the key risks. The Directors are confident that the current risk management structure is sufficient for identification, monitoring and management of significant financial risks to the business.

UNCERTAINTY

Impact of Coronavirus (Covid 19)

Coronavirus has seriously impacted the global economy. Like other governments, the UK government also took significant steps that included strict lockdown across the country covering hospitality sector, non-essential shops, shopping centres and services. All these had a serious impact on business across the country which resulted in one of the largest ever reductions in the GDP and worst economic recession seen since the great depression.

The Covid 19 pandemic no doubt is the most serious challenge to banks in nearly a century. It has generated significant instability and high volatility in global financial markets. While the full impact is yet to be determined, it's expected that the adverse impacts are likely to continue from the virus' knock-on effects. Banks have kept their distribution channels open through remote working solutions. At work locations, social distancing advice and staggered working hours have been implemented to avoid risk of infection.

The Bank focussed on providing support to customers, colleagues and wider community through the unprecedented times of the coronavirus pandemic.

It focussed on the following key areas to manage Covid 19 impact:

- HR risk – ensuring appropriate measures were taken to safeguard health and safety of employees and providing them with necessary support to manage their work with minimum disruption
- Liquidity and funding risk – ensuring the Bank has access to sufficient liquidity to manage its liabilities under stress conditions
- Credit risk – to identify, assess and manage risk arising from impact of economic downturn on industry segments and customers. Additionally, looking into staging criteria and impact of moratoriums, its trend and coverage of provisioning

- Operational risk – focus on information security, operational continuity and control framework for remote working arrangements
- Profitability and the wider business model framework
- Governance arrangements – swift alignment of strategies, tactical decision making, related procedures and the management's ability to ensure prompt implementation

The Bank formed a crisis management team comprising of senior management staff to monitor and address various challenges and took the following measures:

- Kept employees and customers informed about Government advice and Bank's own arrangements through various communications
- Implemented contingency measures for operational continuity by invoking business continuity plans and making additional arrangements to ensure minimum service disruption
- Assessed business and financial impact of Covid 19 on Bank's overall performance through review of lending portfolio and customers deposits in specially convened Country Credit Committee and ALCO meetings
- Daily meetings held to discuss areas of concern posed by the pandemic and measures put in place to mitigate impact

The executive management team will continue its tried and tested approach to monitor the situation to assess potential risks to its customers, employees and suppliers to manage the impact in line with the Government guidance.

Negative Interest Rate

The Bank performed a high-level assessment on its operational readiness for implementation of a (1) near zero Base Rate, (2) Zero Base Rate or a (3) Negative Base Rate as required by the PRA in its Dear CEO letter issued in October. The assessment highlighted that whilst the Bank was prepared for near zero and zero interest scenarios, further changes were required to its core banking platform to manage the impact of negative interest rates on some products offered by the Bank.

Detailed assessment has been carried out by the Bank as required by the PRA letter published on 4 February 2021. The Bank is confident that it is in a position to implement a tactical solution before August 2021 and a strategic solution before the end of 2021. The Bank's management has drawn up plans to make the required changes in the core banking platform to achieve this key change.

OTHER AREA OF KEY ATTENTION IN 2020

LIBOR change

The London Interbank Offered Rate (LIBOR) is the reference interest rate for tens of millions of contracts, ranging from complex derivatives to residential mortgages. LIBOR is also hardwired into all manner of financial activity, such as risk, valuation, performance modelling and commercial contracts. The UK's Financial Conduct Authority (FCA) announced in 2017 that it no longer intends to support the LIBOR benchmark interest rate from 2021 onwards. Alternative reference rates are therefore currently being discussed around the world.

The Bank continued its preparations for the transition from the LIBOR to other interest-based benchmarks by the end of 2021. The Bank participated in a group-wide Change Risk Assessment (CRA) in 2019 to assess the potential risks related to LIBOR replacement faced by the Bank. As an outcome of such assessment certain action items were

identified, which included fact-finding exercise to determine the facts on the ground, e.g., which products are LIBOR based, what is the number / volume of products with maturities > 2021. As an outcome of the exercise, it was concluded that the Bank will not face any significant impact on its product profile due to LIBOR transition.

The Bank main lending products use Bank's own reference rate – HBZ Base Rate – which is not linked to LIBOR. Similarly, customer deposits are fixed rate products. The Bank holds a few LIBOR linked debt securities as part of its investment portfolio which will mature after December 2021. This does not have a material impact as the Bank will only be required to put in place a process to verify accuracy of income received on such investments. Trade finance products, which currently constitute a small proportion of Bank's revenue are priced using LIBOR. The Bank is currently working as part of a Group wide project to put in place a mechanism for using alternate reference rates for pricing trade finance products, which will be available in time before LIBOR transition.

The Bank transacts derivatives to hedge its own foreign exchange rate risk and that of its customers. As per the current practice being followed by the Bank, the LIBOR is not connected in FX swap and hedge transactions. The LIBOR / IBOR transformation risk is not considered material.

Operational Resilience

A key priority for the Bank of England, Prudential Regulation Authority (PRA) and Financial Conduct Authority (FCA) is to put in place a stronger regulatory framework to promote operational resilience of firms and financial market infrastructures (FMIs). To this end, they published a joint Discussion Paper on Operational Resilience 2018 to start a dialogue with the financial services industry. Based on responses received the supervisory authorities issued consultation papers related to important business services, outsourcing and third-party risk management which are considered as key part of operational resilience. Consultation papers also refers to operational capacity, technology infrastructure, data centres and cyber security as elements of overall operational resilience. The FCA and PRA policy statement was published in March 2021 with an effective date of March 2022.

The Bank has considered five main areas in its business services:

1. Deposits, Lending and Transaction Banking
2. Payments, Clearing and Settlement
3. Wholesale Funding
4. Investments
5. Money Markets

In line with its size and business model and share of the market, the Bank considers three elements of the business services – (1) Deposits (2) Lending & loan servicing (3) Payments – to be of critical importance in the context of potential disruption impact on its own customers.

The operational resilience framework in the Bank is subject to continuous improvements, process re-engineering and changes to business model & operational design to increase effectiveness and robustness while maintaining secure and efficient service delivery to customers through minimising adverse impact due to operational disruption.

Employee remuneration policy

The Bank's remuneration policy is in line with market practice and is weighted towards a performance-based compensation plan. The Bank does not have an incentivised compensation scheme for its staff. However, all staff members are considered under a performance-based bonus scheme, which is paid out once a year.

The Bank's objectives, organisation structure and HR policies are integrated for best results. This works within an effective control framework and customer focus in order to implement the Bank's business strategy.

Performance is reviewed annually against pre-defined measures and efforts are recognised through a combination of monetary and non-monetary benefits. The performance management framework is managed through the Bank's HR and senior executive teams. The Board is responsible for annual reviews to determine the remuneration of senior management with Senior Management Function ("SMF") roles.

Annual performance is a self-assessment process where employees assess their own performance against their job profile. It is an important time for an employee and their line manager to meet and share feedback, provide coaching, assess the goals, contributions and behaviours, and identify learning and development needs. It is also a time when future goals and clear expectations are set based on the SMART objectives. Compliance also provides its input on adherence to certification regime staff and their required competencies.

Section 172 Statement

This section of the Strategic Report describes how the Directors have performed their duty to promote the success of the Bank, including how they have considered and engaged with other stakeholders and, in particular, how they have taken account of the matters set out in section 172(1)(a) to (f) of the Companies Act 2006.

The Directors consider prudently that they have acted in the way for the success of the Bank, both individually and collectively for the benefit of its shareholder and all its stakeholders. In discharging its duties under s172 the Board:

- annually reviews the strategic plan keeping in view the changes in the business and operating circumstances and approves the annual budget taking into account impact of such changes;
- recognises that employees are central to the success of the Bank. The interests of the employees are considered in a proper way while keeping safety, and well-being as the key considerations for the way in which the Bank conducts its business;
- recognises the need to develop successful relationships with all stakeholders for the success and viability of the Bank. The Board taken into the account the interests of and impact on the stakeholders while taking business decisions;
- considers the impact of the Bank's business and operations on the community and the environment;
- ensures maintaining a reputation for high standards of business conduct; and
- ensures that the matters are referred to the parent in line with relevant statutory requirements.

The Directors recognise that effective stakeholder engagement is crucial in working towards shared goals which delivers long-term sustainable success. The Board reflects the priorities of the Bank's various stakeholders by considering the long-term implications of its decisions. The Board engages directly with stakeholders, and also indirectly through reporting from the Executive team.

The Board also gives due regard to presence of an effective governance and risk management and clear distinction of responsibilities between the Board and management in discharging responsibilities under s172 detail of which are included in the Corporate Governance Report on Page 32.

Future outlook

2020 was a year of significant calamities caused by the pandemic. The Covid 19 forced people around the world into lockdown, significantly impacted economies and tested the limits of health systems around the globe. Although recent vaccination programs have raised hopes of a turnaround in the pandemic later this year, renewed waves and new variants of the virus pose concerns for the outlook. The pandemic has taught us some valuable lessons and underlined the importance of purpose in everything we do. Our strategy and business model are intact and we are confident that the Bank is in a strong position for the challenges and opportunities ahead.

We expect 2021 is likely to bring stability and a reset to normality as majority of the population will be vaccinated and social distance restrictions will be lifted. We hope the Bank to experience a steady growth in its real estate lending and commercial banking activities. We are determined that the Bank will come out stronger and will seek to ensure we serve our customers to the best of our abilities.

Approved by the Board and signed on its behalf by:

Kamran Qazi
Chief Financial Officer

Cambridge University

Directors' Report

On behalf of the Board of Directors of Habib Bank Zurich plc ("the Bank"), I am pleased to present the Directors Report on the Financial Statements of the Bank for the year ended 31 December 2020. The Bank is registered in England and Wales with number 08864609 and is authorised by the PRA and regulated by the FCA and PRA. The Bank is a wholly owned subsidiary of Habib Bank AG Zurich.

Results

In 2020, the Bank posted a profit after taxation of £0.60 million (2019 £3.48 million). I am pleased with the way we have demonstrated our financial resilience throughout the year despite unprecedented business challenges due to Covid 19 related lockdowns. We have delivered a good performance, despite extreme contraction in the global economy with a sturdy balance sheet growth. Our business model has demonstrated its capacity to deliver high performance, driven by the Bank's core business activities, real estate finance and commercial banking services. Islamic banking under the brand name "Sirat" and Trade finance business volumes boosted during the year as the Bank deployed resources to grow these areas to diversify its revenue base. The Bank remained cautious and prudently managed its investment and money market portfolio as a result of growing uncertainties about interest rate direction.

Share capital and dividend

The Directors do not propose any dividend on ordinary shares to be paid in respect of the year. (2019: Nil).

The share capital of the Bank remained unchanged at £60 million, which is divided into 60 million ordinary shares of £1 each.

Board of Directors

The following directors have been appointed to serve on the Board of the Bank:

Mr Muhammad H. Habib	Non-Executive Director (NED) and Chairman
Mr Carey Leonard	Independent NED
Mr Gerald Arthur Gregory	Independent NED
Mr Anjum Iqbal	Non-Executive Director
Mr Rajat Garg	Non-Executive Director
Mr Satyajeet Roy	CEO / Executive Director
Mr Masum Billah (resigned 31 May 2021)	COO / Executive Director

The Bank's Board membership represents a suitable mix of experience and knowledge relevant to the services offered.

Board meetings are held at least four times a year and additional meetings can be held at any time to discuss urgent issues.

Directors' representation

In the case of each of the persons who are Directors at the time the report is approved, so far as the director is aware, there is no relevant audit information of which the Bank's auditor is unaware, and the director has taken all the 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 auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418 of the Companies Act 2006.

Independent Auditor

Mazars LLP conducted their first audit of the Bank as appointed in place of KPMG LLP in 2020. Mazars has expressed an unqualified opinion on the 2020 financial statements.

Mazars LLP has expressed its willingness to continue in office as Auditors and a resolution to reappoint the firm was considered and approved at the annual general meeting.

Senior Management and Certification Regime

The Bank has established adequate documented processes over monitoring and governance of the Senior Management and Certification Regime ("SM&CR"), including the certified population. This includes adequate governance and oversight exercised by the Board, updating management responsibility and related business activities, and training staff in particular with Senior Management Function ("SMF") roles, as well as assessing the fitness and propriety of SM&CR staff.

Going concern

The Bank's operating model is simple, offering core lending and deposits products to its customers, who have a strong loyalty to the franchise. This is the foundation of the value proposition for the Bank. Service is delivered through dedicated branch and relationship managers. The customer takes comfort in continuity with a relationship manager and quick turnaround on their requests as well as access to the decision makers at the Bank. The expertise of the Bank in understanding and dealing with SME customers and business owners has positioned the Bank very strongly among its peer banks. This has enabled longevity of customers relationships spreading over two to three generations.

The Bank has prepared these financial statements taking into account that it operates on a self-sufficient basis with minimum dependency on Habib Bank AG Zurich (the "Parent Bank"). The Bank also expects to grow its lending book in line with its strategy and improve its credit quality, which provides a steady stream of interest income from customers. Introduction of Islamic lending facilities during the year was a big step towards accelerating our lending book growth. In addition to net interest income the Bank has a flow of revenue from fees and commissions, which is likely to increase with the positive momentum from Trade finance income seen in 2020, which is expected to gain further momentum into 2021 through introduction of new products and diversified customer base. The strength in our model and strategies gives us hope as we aim to increase inflow of income from investments, helping drive economic growth.

The Bank has a sound governance structure in place, which comprises the Board of Directors, Committees of the Directors and Management Committees covering all key risk areas such as credit risk, liquidity risk, anti-money laundering, compliance risk and operational risk. The capital base of the Bank is sound with more than the required capital invested by the Parent Bank. The Bank's liquidity position is also very strong with more than adequate liquid assets to cover a stress over a 90-day survivability period. Introduction of Sirat eDeposits in 2020 has increased the capacity to expand its deposit base.

The Board is fully conscious of the unprecedented economic compressions brought in by the Covid 19 pandemic that effected the whole World during 2020. There is some contraction expected in UK GDP in the 1st quarter of 2021 owing to the impact on activity restrictions needed to contain the Covid 19. While the impact of Covid 19 on daily lives is huge, given continued support by the UK government through various financial schemes, the economy continues to pull itself through these distressed times. The 4-stage plan of the government to open the economy on the back of an effective vaccination program has ignited the hopes of speedy recovery. The UK economy is anticipated to rebound strongly in the second half of 2021. The Bank is geared up to deal with the pent-up demand, sign of which are already visible through increase in number of new business inquiries.

2020 is the clear indicator of Bank's financial and operational strength where despite of big calamities we posted after tax profit. Our part history is clear indicative of the Bank's high touch relationship-based business models, which allows it to keep in close contact with customers. It not only provides them the needed confidence on Bank's financial health but also addresses their business needs in the time of real crisis like the one which we are in at the moment.

As explained in more detail in the Strategic Report the Bank has a strong capital base and liquidity position, which has gained strength during Covid 19. The Bank's overall capital resources remained intact during the year with head room to support future growth. The Bank has recently renewed the 5 years £20 million subordinated loan with its parent bank, which meets the Tier 2 capital requirement.

Based on the above, the Directors are confident that the Bank has adequate resources to continue and grow the franchise for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and financial statements.

Post-balance sheet events

There have been no other reportable events subsequent to the balance sheet date except for renewal of subordinated loan on 01 April 2021 as disclosed in note 33.

Acknowledgement

The Board of Directors takes the opportunity to express its gratitude to all stakeholders for their continued support.

The Board of Directors also records its appreciation to the Executive Committee and staff for their efforts, dedication, commitment and teamwork during 2020.

Approved by the Board and signed on its behalf by:

Satyajeet Roy
Chief Executive Officer

Directors' Responsibilities Statement

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

Company law requires the Directors to prepare the Bank's financial statements for each financial year. Under that law they have elected to prepare the Bank's financial statements in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006 and applicable law.

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

- Select suitable accounting policies and then apply them consistently.
- Make judgements and estimates that are reasonable and prudent.
- State whether they have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006.
- 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 it to ensure that its financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as is 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.

Satyajeet Roy
Chief Executive Officer

Corporate Governance Report

THE BOARD OF DIRECTORS

The Board of Directors ("the Board") is committed to follow best practice in Corporate Governance.
The Board approved and adopted a substantially updated revision of the Corporate Governance Code incorporating the Principles set out in the latest revision of the UK Corporate Governance Code (the 'UK Code'), modified as considered appropriate for an organisation of the Bank's size and type. Whilst the Code does not apply directly to the Bank, the Board agrees with and supports its general principles. This report sets out how the Bank has regard to the principles of the Code.

Board profile

Board of Directors
From left to right: Carey Leonard, Anjum Iqbal, Rajat Garg, Muhammad H. Habib, Masum Billah (resigned 31 May 2021), Satyajeet Roy and Gerald Arthur Gregory.

Muhammad H. Habib

Chairman

Roles & Committees

Chairman & Non-Executive Director

Skills & Experience

Muhammad H. Habib became a member of the General Management in 1992 (Habib Bank AG Zurich Group, Switzerland).

He was appointed as the President & Chief Executive Officer of Habib Bank AG Zurich Group, in 2011.

His banking journey, spanning over 40 years, started in 1981 from Dubai, UAE where he went through extensive training and manager level positions, in all aspects of banking over the next 11 years.

After entering General Management in 1992, his remit and responsibilities took him across Africa, UK, North America and Switzerland. Under his leadership, the Group ventured into newer geographies, inclusive of but not limited to South Africa (1995) and Canada (2001). During this period, he was elevated to the rank of Joint President in 1996.

He is currently a member of the General Management and President of Habib Bank AG Zurich Group.

Principal external appointments

- Chairman, Habib Canadian Bank, Canada
- Director, Habib Metropolitan Bank, Pakistan
- Chairman, HBZ Bank Limited, South Africa
- Vice Chairman, Gefan Finanz AG Zug, Switzerland
- Member Board of Trustees, Habib University Foundation
- Member Board of Trustees, Habib Public School, Karachi (Pakistan)
- Member Global Advisory Board, Babson College

Carey Leonard

Independent
Non-Executive Director

Roles & Committees

- Independent Non-Executive Director
- Chair of the Board Risk Committee
- Member of the Board Audit and Compliance Committee

Skills and experience

Carey Leonard has many years of banking experience in Asia, the Middle East, Africa and the UK. He has strong commercial banking disciplines in the areas of governance, strategy, business development, wholesale banking and risk management as well as proven leadership skills.

Principal external appointments

- Trustee and Treasurer to the Council, Malvern College
- Chairman, The Downs Malvern Preparatory School
- Chairman, Abberley Hall School
- Justice of the Peace Worcestershire branch

Former appointments

Standard Chartered Bank

- Regional Head, Special Assets Management Africa
- Chief Executive Officer, South Africa
- Managing Director and CEO, Nigeria
- Chief Executive Officer, Sri Lanka
- Member of Business Leadership Team

Gerald Arthur Gregory

Independent
Non-Executive Director

Roles & Committees

- Independent Non-Executive Director
- Chair of the Board Audit and Compliance Committee
- Member of the Board Risk Committee

Skills and experience

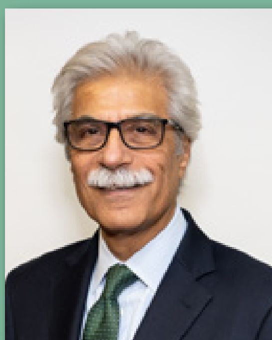
Gerald Gregory brings extensive experience both in practice and in independent non-executive functions. His experience covers treasury, lending, strategy, marketing and risk management.

Principal external appointments

- Deputy Chairman and Senior Independent Non-Executive Director, Chair of Risk Committee and member of Audit Committee, Gatehouse Bank Plc
- Chairman and Independent Non-Executive Director, Chair of Nomination Committee, member of Remuneration Committee, member of Audit committee and Risk Committee, Northern Bank Limited (t/a Danske Bank)

Former appointments

- Managing Director, Britannia Capital Investment Group
- Executive Director, Britannia Building Society
- Sales and Marketing Director, Britannia Building Society



Anjum Iqbal

Non-Executive Director

Roles & Committees

- Non-Executive Director
- Member of the Board Risk Committee
- Member of the Board Audit and Compliance Committee

Skills and experience

Anjum Iqbal has extensive management experience in various parts of the world in corporate and commercial banking. He has worked in several regions including Latin America, Europe, the Middle East, Africa and South Asia.

Principal external appointments

- Member of General Management and Regional CEO (Developing markets), Habib Bank AG Zurich (Switzerland)
- Non-Executive Director and member of Board Audit Committee, Board Risk Committee, HBZ Bank Ltd (South Africa)
- Chair of Risk and Compliance Committee, Chair of Board IT Committee, member of Board Audit Committee and Board Credit Committee, Habib Metropolitan Bank (Pakistan)

Former appointments

Habib Bank AG Zurich Group

- Chief Executive Officer, Habib Bank Zurich plc, UK
- President and Chief Executive Officer, Habib Metropolitan Bank, Pakistan

Citigroup

- Managing Director Commercial Banking Group (EMEA)
- Head of Corporate and Financial Institutions Group (CEEMEA)
- CEO Africa Division
- Regional CEO, Turkey and Central Asia

Rajat Garg

Non-Executive Director

Roles & Committees

- Non-Executive Director
- Member of the Board Risk Committee
- Member of the Board Audit & Compliance Committee
- Group Entity Senior Manager for Habib Bank Zurich plc

Skills and experience

Rajat Garg possesses over 31 years of experience in senior banking positions across Asia, Europe and Middle East. His professional background includes extensive experience in managing commercial banking and wealth management business.

Principal external appointments

- Member of General Management and Regional CEO (Developed markets), Habib Bank AG Zurich (Switzerland)
- Non-Executive Director, HBZ Bank (Hong Kong) Ltd
- Non-Executive Director, Habib Canadian Bank

Former appointments

Citigroup

- Head of Retail Banking and Wealth Management, EMEA
- Country Business Manager, Turkey
- Cards Business Manager, Saudi Arabia
- Regional CFO – Asia Pacific Cards, Singapore
- NRI Wealth Management Head, Singapore
- Financial Controller and Business Planning Head, India

Satyajeet Roy

Chief Executive Officer

Roles & Committees	· Executive Director · Chief Executive Officer
Skills and experience	Satyajeet Roy is a seasoned executive with 26 years of international banking experience across the Middle East, UK, Europe and India spread over commercial, SME and retail segments. He brings cross-functional experience covering business strategy, risk, audit and operations. His leadership experience in diverse locations is an added advantage for the Bank.
Principal external appointments	none
Former appointments	Commercial Bank International, UAE · Head of Business Banking Citigroup · Head of Commercial Banking for UAE & Bahrain (Dubai, UAE) · EMEA Head of Business Development, Business Banking (London UK) · EMEA Audit and Risk Review, Lead Auditor, UK

Masum Billah

Chief Operations Officer (resigned 31 May 2021)

Roles & Committees	· Executive Director · Chief Operations Officer
Skills and experience	Masum Billah (resigned 31 May 2021) has over 26 years of experience in financial services spread across operations, technology, operational risk, business development, compliance and risk management. During his various roles he has been based in Bangladesh and UK with coverage for Europe, Middle East and Africa markets.
Principal external appointments	none
Former appointments	Bank of America Merrill Lynch (London, UK) · Director, Global Trade Service EMEA Compliance Citigroup · Senior Compliance Officer, TTS EMEA Compliance (London, UK) · Risk and Control Programs Lead, TTS Global Operations (London, UK) · EMEA Trade Deal Facilitation and FI Training Head (London, UK) · Head of Operations and Technology (Dhaka, Bangladesh)

Oxford University

Executive Committee

Satyajeet Roy	CEO and Executive Director
Kamran Qazi	Chief Financial Officer
Kausar Kazmi	Head of Commercial Banking
Nadia Saleem	Head of Compliance and MLRO
Masum Billah (resigned 31 May 2021)	Chief Operations Officer
Asim Imtiaz Basraa	Head of Credit
Waqar Haider	Head of Governance and Risk Control and Board Secretary
Monika Poznar	Head of Human Resources

Executive Committee
From left to right: Waqar Haider, Nadia Saleem, Asim Imtiaz Basraa, Satyajeet Roy, Kausar Kazmi, Kamran Qazi and Monika Poznar.

LEADERSHIP

The role of the Board

The primary role of the Board is to set the overall strategy for the Bank and to protect and enhance its long-term strategic value. The Board ensures that the business of the Bank is conducted in an efficient and effective manner to promote the success of the Bank within an established framework of effective systems of internal control, robust risk management process and compliance with regulatory requirements. The Board also ensures that good corporate governance policies and practices are implemented within the Bank. In the course of discharging its responsibilities, the Board acts in good faith, with due diligence and care, and in the best interests of the Bank and its shareholders.

The primary responsibilities, which the Board undertakes in this respect, are to:

- Consider changes to the structure, size and composition of the Board and its committees and approve terms of reference.
- Define, oversee and be accountable for the implementation of governance arrangements that ensure effective and prudent management of the Bank, including the segregation of duties in the organisation and the prevention of conflicts of interest.
- Set the Bank's strategic objectives and goals and reviewing the performance of the executive team.
- Review and approve the risk appetite statements of the Bank.
- Establish and maintain a framework for the overall sound and proper internal control and risk management processes.
- Review and challenge the business performance of the Bank, set the budget and financial forecasts, and ensure that the business of the Bank is managed to balance risk and reward.
- Ensure that adequate succession planning arrangements are in place related to senior management so as to maintain an appropriate balance of skills and experience within the Bank.
- Consider and make recommendations to the Board regarding the remuneration including increment and bonus of employees with SMF responsibilities with the exception of Directors.

The responsibilities of the Board are clearly set out in its Terms of Reference ("TORs"), which is reviewed and approved periodically by the members of the Board. The schedule of Board meetings along with recurring items is approved in advance with the permission of the Chair and circulated to all members. The responsibilities of the Board are clearly set out in its Terms of Reference ("TORs"), which is reviewed and approved annually by the members of the Board. The schedule of Board meetings along with recurring items is approved in advance with the permission of the Chairman and circulated to all members.

Division of responsibilities

The responsibilities of the Board members are set out in the Board TORs, which are aligned with a respective statement of responsibilities prepared under the senior management regime for each Board member. The Chairman is responsible for leading the development of and monitoring the effective implementation of policies and procedures for the induction, training and professional development of all members of the Board.

The Chairman sets the Board's agenda primarily focusing on strategy, performance, value creation and accountability and ensures that adequate time is available for discussion on all agenda items, in particular strategic issues. Along with other Board members, the Chairman is also responsible for leading the development of the Bank's culture.

The two appointed independent non-executive directors ("INEDs") support the Board in the oversight functions on the basis of requisite skill sets and experience needed for effectively performing their respective SMF roles. Collectively and individually, the INEDs provides adequate challenge to other members of the Board and the senior management team in the course of discharging their oversight responsibilities as board members.

The non-executive directors ("NEDs") along with INEDs are responsible for setting the Bank's strategic objectives and goals and reviewing the performance of the executive team. They approve and keep an oversight of the Bank's strategy and business plan prepared by the executive team. They also review and challenge the business performance of the Bank, approve the budget and financial forecasts, and ensure that the business of the bank is managed to balance risk and reward. They also scrutinise the delivery of the strategy within the risk and control framework set by the Board and satisfy themselves on the integrity of financial reporting.

The Chief Executive Officer ("Executive Director") is responsible for managing the Bank's business on a day-to-day basis on behalf of the Board. The business is managed within the strategy, risk appetite and control frameworks set and overseen by the Board. The Executive Director has specific management responsibilities for which he is accountable to the Board, such as executing the business plan, delivering planned results, managing risk, systems and the control framework, and delivering timely and accurate information to the Board.

EFFECTIVENESS

The composition of the Board

The size of the Board is aligned with the overall governance structure required for the effective oversight of the business, risk and control framework, operational, regulatory and compliance and financial performance of the Bank. The composition of the Board has been established to ensure the availability of a pool of resource with relevant knowledge and experience to manage the strategic objectives of the Bank.

The Board comprises of seven directors – the Chairman, two INEDs, two NEDs and two Executive Directors. The relevant knowledge of Board members and diversity of their experience allows all directors to actively and effectively participate in the meetings.

The Board considers Carey Leonard and Gerald Gregory to be independent within the meaning of the UK Corporate Governance Code. They do not perform any executive or other role or have any relationship with the Bank that, in the Board's view, would affect their objectivity and judgement in performing their respective function.

Appointment to the board

Appointments to the Board are made by carrying out a formal and rigorous process of evaluating candidates by the Board members, selected on the skills and experience required for their particular appointment. The Bank usually uses an external executive search firm for shortlisting candidates.

Commitment

The Bank has a balanced combination of non-executive, independent non-executive and executive directors keeping in view the complexity and nature of the Bank's operations. All directors in accordance with their terms of appointment are required to allocate sufficient time to the Bank to discharge their responsibilities effectively and efficiently.

Development

The Bank provides a detailed overview of the business to all directors on their joining of the Board. The process includes a formal presentation conducted by senior executive management covering their respective areas including but not limited to strategy and risk management, business development, credit, AML and compliance, operations, treasury and finance, information technology and cyber security. There is also continuous interaction between executive management and the Board members, which allows the new directors to gain further knowledge and insight about Bank's business.

All directors are required to complete in-house online courses, which comprehensively cover areas such as AML, information security, fraud prevention, anti-bribery and corruption, whistle-blowing, complaints handling, data protection etc. In addition, directors are also receiving periodic updates related to emerging risks to keep them abreast of new challenges within financial services.

Information and support

The Chair ensures that the Board members receive accurate, timely and clear information for effective decision-making processes and applies sufficient challenge to major proposals. The Directors keep close liaison with the executive management of the Bank for a better understanding of the business operations of the Bank. Furthermore, the Board has independent access to senior management and the Board Secretary at all times.

The Board Secretary ensures timely and accurate information flows within the Board and its committees and between senior management and the NEDs. Senior management of the Bank present information related to all key areas, such as risk management, credit, compliance, operations, finance and audit to the Board through its committees.

Evaluation

Each Board member undergoes a periodic evaluation process by completing a self-assessment questionnaire, which is discussed with the Chairman of the Board. The assessment aims to assess the performance evaluation of each member by recognising strengths and addressing weaknesses.

To assess the overall performance of the Board, each member also completes a questionnaire on board effectiveness, which includes areas of strategic goals and objectives, governance, risk management, quality of information and leadership.

Re-election

In accordance with the provisions in the Articles of Association, all directors who have been appointed by the Board must stand for re-election every three years.

ACCOUNTABILITY

Board committees

To help carry out its responsibilities, the Board has also established the following committees with terms of reference setting out matters relevant to the committees' composition, responsibilities and administration.

Board Risk Committee

Membership	Carey Leonard	Chairman
	Gerald Arthur Gregory	Member
	Anjum Iqbal	Member
	Rajat Garg	Member

Board Audit and Compliance Committee

Membership	Gerald Arthur Gregory	Chairman
	Carey Leonard	Member
	Anjum Iqbal	Member
	Rajat Garg	Member

Board Risk Committee

Primary responsibilities are to:

- Review the overall approach of the Bank to risk, its management and reporting line framework to ensure the effective application of the risk management framework.
- Assess and regularly review the three lines of defence model implemented by the Bank for its effectiveness.
- Provide assurance on the Bank-wide risk management framework and monitor the overall risk profile of the Bank through effective control processes.
- Annually review the Risk Appetite Statement and consider the adequacy of risk limits and returns.
- Set guidelines for maintaining risk control parameters for all types of risk across the business, including policies, control standards, underwriting standards, risk exposure limits or other control levers.
- Receive information on any material breaches of risk limits, policies or procedures and agree proposed action as soon as practically possible.
- Consider and make recommendations to the Board regarding the appointment, removal and resignation of employees with SMF responsibilities under the Senior Management Regime (SMR) with the exception of Directors.

Board Audit and Compliance Committee

An independent Audit and Compliance Committee is responsible for challenging executive management and the Bank's internal and external auditors as part of a good governance process. Primary responsibilities are:

- Review key internal control policies, processes and procedures and assess the effectiveness of those keeping in view the size, nature and complexities of Bank's operations.
- Review the effectiveness of the Bank's internal audit in the context of the Bank's overall risk management system.
- Review and assess independence of internal audit function.
- Make recommendations on the internal and external auditors' appointment, reappointment and removal.
- Review and monitor the independence of the external auditors.
- Discuss the financial statements and the quality of the underlying accounting processes with the member of management responsible for accounting and finance.
- Review and approve the non-audit services policy in respect of the external auditors.
- Review and approve accounting policies and changes therein.
- Review policies to ensure the Bank's ongoing compliance with relevant legal and regulatory requirements.
- Ensure that its recommendations to combat money laundering, terrorist financing and financial crime risks are incorporated into the Bank's ongoing procedures and monitoring infrastructure.
- Oversight of adequacy of processes put in place by the management to manage Conduct Risk.
- Oversight of the adequacy of the training and competency framework required fulfilling the Bank's obligations under the SMR and the Certification Regime.
- Review and ensure the implementation and compliance of EU audit legislation in liaison with external auditors.

Board meetings

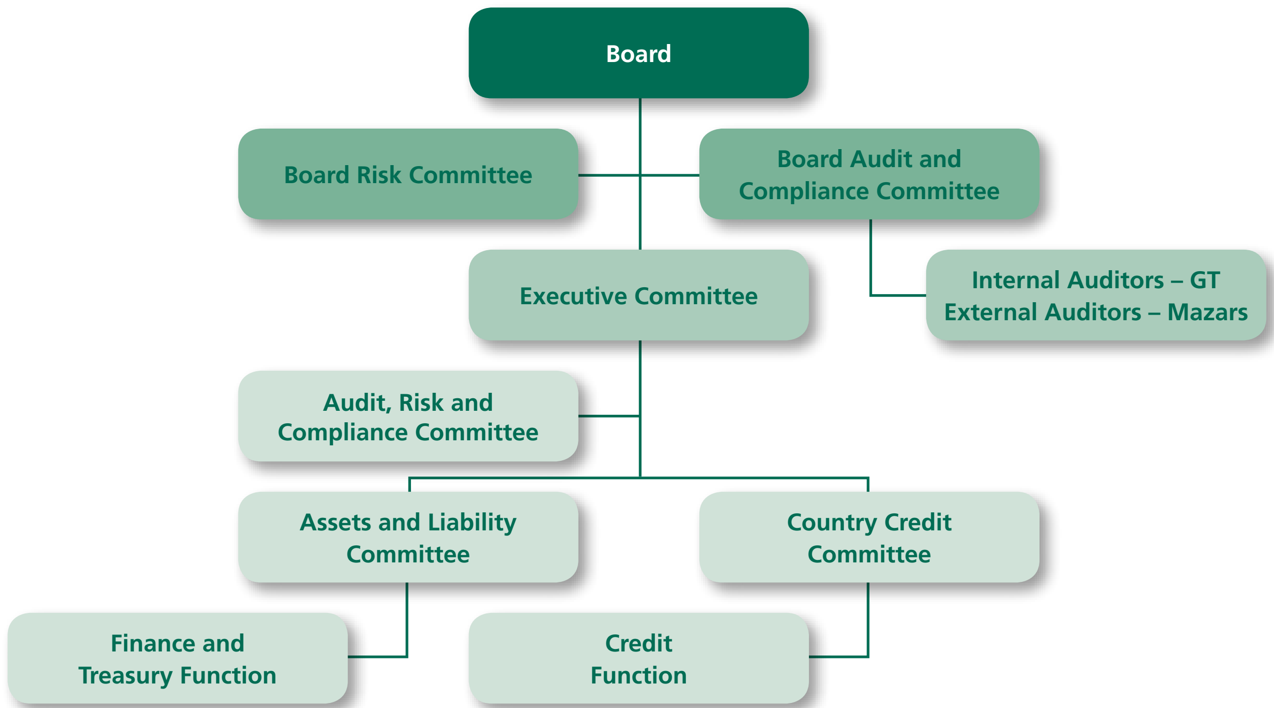
The Board meets regularly at least four times a year at quarterly intervals and holds additional meetings as and when the Board thinks appropriate. Four Board meetings were held during 2020. The agenda, together with Board papers, are sent in full to the directors not less than three business days before the intended date of the Board meeting. The Board Secretary prepared minutes of Board meetings, with details of decisions reached.

At each regular Board meeting, the executive management of the Bank made presentations to the Board on various aspects, including business performance, financial performance, corporate governance and outlook. Throughout 2020, Directors of the Bank also participated in the consideration and approval of matters of the Bank by way of written resolutions circulated to them. Supported written materials were provided in the circulation and the Board Secretary gave verbal briefings as and when required.

All Directors attended the Board and its committee meetings held during the year.

Interaction with management committees

There is a formal division of responsibilities matrix, which identifies the responsibilities of the Board and those of the management through its respective committees. Management committees are responsible for oversight of various operational processes through which the strategy and objectives set by the Board are achieved. These are clearly defined and approved in terms of reference of each management committee.



The CEO and EXCO represent the principal forum for conducting the day-to-day business of the Bank. The terms of reference of EXCO are approved by the Board. Executive Committee is represented at the Board through the CEO. While retaining the ultimate responsibility for the actions taken, the CEO and EXCO at its discretion has delegated certain responsibilities to the following standing sub-committees:

- Asset and Liability Committee
- Audit Risk and Compliance Committee
- Country Credit Committee
- Operations and Technology Committee
- Human Resource Committee
- Business Development Committee

The Chairman of the respective committee presents key matters arising from each of the above committees to EXCO, which are also reported to the Board or its committees through various management information presented in Board or its committee meetings as appropriate.

Financial and business reporting

The Board has put in place appropriate checks and controls to ensure that financial and business information presented in the financial statements provides a balanced and fair assessment of the Bank's performance, business model and strategy.

Risk management and internal control

The Board reviews and approves the overall risk appetite of the Bank. The Board has established and maintained a framework for the overall sound and proper internal control and risk management processes. The Board regularly receives reports on, and reviews the effectiveness of, the risk and control processes to support the strategy and objectives.

REMUNERATION

The Board is responsible for the review and approval of the Bank's HR Policy including remuneration practices. The Board, on the recommendation of the Chief Executive Officer, approves the annual staff remuneration plan along with the total remuneration for senior executive staff.

The Bank's remuneration policy is in line with market practice and is weighted towards performance-based development. The Bank is fully cognisant of having a remuneration policy that is aligned with its long-term objectives and can provide support in the successful implementation of its business strategy. The remuneration policy has been developed while keeping in view the core values of the Bank, which has trust at its core supported by integrity, teamwork, respect, responsibility and commitment. Values are upheld continuously and embedded at all levels of the organisation.

The Bank recognises that robust performance assessment is essential for the sustained success and development of the Bank and its employees. The Bank's performance assessment creates a shared vision of the purpose and aims of the Bank and ensures that each employee understands how he or she makes their contribution.

Performance is reviewed annually against predefined measures and efforts are recognised through a combination of monetary and non-monetary benefits. The performance management framework is managed through the Bank's senior executive management.

The Bank's remuneration structure is not linked to any pre-defined business targets for front-end staff. Annual performance rewards are based on overall performance of the Bank and then of the employee based on overall achievement during the year. A key consideration given in evaluating the performance of employees is their overall conduct and compliance with relevant rules and competencies demonstrated during the year.

RELATIONS WITH SHAREHOLDERS

The Bank is a wholly owned subsidiary of Habib Bank AG Zurich ("the Parent Bank"). The Chair discusses matters relating to governance and business strategy of the Bank with the other shareholders. The Chair ensures that views of shareholders are shared with the Board.

Constructive use of annual general meeting

All members of the Board are encouraged to attend the annual general meeting of the Bank to be used as an opportunity to interact and communicate with the shareholder.

Independent auditor's report

to the members of Habib Bank Zurich plc

Opinion

We have audited the financial statements of Habib Bank Zurich plc (the 'Bank') for the year ended 31 December 2020 which comprise the Income Statement, Statement of Other Comprehensive Income, Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows and notes to the financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and international accounting standards in conformity with the requirements of the Companies Act 2006.

In our opinion, the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and:

- give a true and fair view of the state of the Bank's affairs as at 31 December 2020 and of the Bank's profit for the year then ended; and
- have been properly prepared in accordance with international accounting standards in conformity with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the parent company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, as applied to public interest entities and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate.

Our audit procedures to evaluate the directors' assessment of the Bank's ability to continue to adopt the going concern basis of accounting included but were not limited to:

- Undertaking an initial assessment at the planning stage of the audit to identify events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern;
- Making enquiries of the directors to understand the period of assessment considered by them, the assumptions they considered and the implication of those when assessing the Bank's future financial performance;
- Evaluating management's Going Concern assessment of the company;
- Evaluating stress tests applied to the company's liquidity and regulatory capital;
- Assessing and challenging key assumptions and mitigating actions put in place in response to COVID-19;
- Considering the consistency of the directors' forecasts with other areas of the financial statements and our audit; and
- Evaluating the appropriateness of the directors' disclosures in the financial statements on going concern.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Bank's ability to continue as a going concern for a period of at least twelve months from when the financial statements are authorised for issue.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) we identified, including those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. 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.

We summarise below the key audit matters in forming our audit opinion above, together with an overview of the principal audit procedures performed to address each matter and, where relevant, key observations arising from those procedures.

These matters, together with our findings, were communicated to those charged with governance through our Audit Completion Report.

Key Audit Matter	How our scope addressed this matter
Loan loss provisions Credit risk is an inherently judgemental area due to the use of subjective assumptions and a high degree of estimation. IFRS 9 requires the Bank to recognise expected credit losses ("ECL") on financial instruments which involve significant judgement and estimates. The most significant areas where we identified greater levels of management judgement are: • Staging of loans and the identification of Significant Increase in Credit Risk; • Key assumptions in the model including probability of default ("PD") and loss given default ("LGD") including the present value of future cash flows from collateral; • Use of macro-economic variables reflecting a range of future scenarios; • Completeness & valuation of post-model adjustments; & • Other factors such as payment holidays and other indicators of impairment triggers as a result of COVID-19 are also considered in the assessment. The effect of these matters is that, as part of our risk assessment, we determined that the provision for impairment on loans and advances has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole.	We have tested the design and operating effectiveness of the processes relevant to the ECL estimate. We have also performed the following procedures: • We have challenged the appropriateness of the Bank's IFRS 9 impairment methodology including challenging the reasonableness of the assumptions, assessing the appropriateness of the model's design and recalculating the PD and LGD for a selection of loans. We have engaged our in-house credit risk specialists in this process. • We have challenged the appropriateness of the Bank's macroeconomic variables, economic scenarios used and the probability weightings applied. We used our in-house economist in this process. • We have tested a selection of loans based on characteristics and identified the appropriateness of the staging. • We have developed with our in-house credit specialists an auditor's estimate of the ECL using assumptions relevant to the Bank's portfolio and assessed the reasonableness of the applied post model adjustment. **Our observations** We found the judgements applied and the resulting estimates to be reasonable.

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

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and on the financial statements as a whole. Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall materiality	£355,000
How we determined it	0.5% of net assets was used in determining our materiality
Rationale for benchmark applied	We believe that the benchmark of net assets as a key focus of users of the financial statements, who, in the current environment, may be more focused on balance sheet strength as determined by regulatory capital in which net assets is a good proxy. We have therefore used equity given its importance to the company's solvency and regulatory capital resources.
Performance materiality	Performance materiality is set to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements in the financial statements exceeds materiality for the financial statements as a whole Similarly, performance materiality relating to a materiality level determined for a particular class of transactions, account balances or disclosures set to reduce to an appropriately low level of probability that the aggregate of uncorrected misstatements in that particular class of transactions, account balance or disclosure exceeds the materiality level for that particular class of transactions, account balance or disclosure. Performance materiality of £213,000 was applied in the audit.
Reporting threshold	We agreed with the directors that we would report to them misstatements identified during our audit above £11,000 as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

As part of designing our audit, we assessed the risk of material misstatement in the financial statements, whether due to fraud or error, and then designed and performed audit procedures responsive to those risks. In particular, we looked at where the directors made subjective judgements such as making assumptions on significant accounting estimates.

We tailored the scope of our audit to ensure that we performed sufficient work to be able to give an opinion on the financial statements as a whole. We used the outputs of a risk assessment, our understanding of the company,

its environment, controls and critical business processes, to consider qualitative factors in order to ensure that we obtained sufficient coverage across all financial statement line items.

Other information

The other information comprises the information included in the other than the financial statements and our auditor's report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, 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 and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. 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.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- 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; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements

Matters on which we are required to report by exception

In light of the knowledge and understanding of the group and the parent company and its environment obtained in the course of the audit, we have not identified material misstatements in the Strategic Report or the Directors' Report.

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

- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent company 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.

Responsibilities of Directors

As explained more fully in the Directors' Responsibilities statement set out on page 31, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company'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 directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

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 (UK) 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.

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect material misstatements in respect of irregularities, including fraud. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

Based on our understanding of the Bank and its industry, we identified that the principal risks of non-compliance with laws and regulations related to regulations and supervisory requirements of the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) and laws and regulations, such as the Companies Act 2006, and we considered the extent to which non-compliance might have a material effect on the financial statements.

In identifying and assessing risks of material misstatement in respect to irregularities including non-compliance with laws and regulations, our procedures included but were not limited to:

- At the planning stage of our audit, gaining an understanding of the legal and regulatory framework applicable to the company, the industry in which it operates and considered the risk of acts by the company which were contrary to the applicable laws and regulations;
- Discussing with the directors and management the policies and procedures in place regarding compliance with laws and regulations;
- Discussing amongst the engagement team the identified laws and regulations, and remaining alert to any indications of non-compliance; and
- During the audit, focusing on areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our general commercial and sector experience and through discussions with the directors (as required by auditing standards), from inspection of the Bank's regulatory and legal correspondence and review of minutes of directors' meetings in the year. We identified that the principal risks of non-compliance with laws and regulations related to breaches of regulatory requirements of the PRA and the FCA. We also considered those other laws and regulations that have a direct impact on the preparation of financial statements, such as the Companies Act 2006.

Our procedures in relation to fraud included but were not limited to:

- Making enquiries of the directors and management on whether they had knowledge of any actual, suspected or alleged fraud;
- Gaining an understanding of the internal controls established to mitigate risks related to fraud;

- Discussing amongst the engagement team the risks of fraud; and
- Addressing the risks of fraud through management override of controls by performing journal entry testing.

The primary responsibility for the prevention and detection of irregularities including fraud rests with both those charged with governance and management. As with any audit, there remained a risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal controls.

As a result of our procedures, we did not identify any key audit matters relating to irregularities. The risks of material misstatement that had the greatest effect on our audit, including fraud, are discussed under "Key audit matters" within this report.

A further description of our responsibilities is available on the Financial Reporting Council's website at www.frc.org.uk/auditorsresponsibilities.

Other matters which we are required to address

Following the recommendation of the audit committee, we were appointed by the Board of Directors on 29 January 2021 to audit the financial statements for the year ending 31 December 2020 and subsequent financial periods. The period of total uninterrupted engagement is one year.

The non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company and we remain independent of the group and the parent company in conducting our audit.

Our audit opinion is consistent with the additional report to the audit committee.

Use of the audit report

This report is made solely to the parent 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 parent 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 parent company and the parent company's members as a body for our audit work, for this report, or for the opinions we have formed.

David Allen (Senior Statutory Auditor)
For and on behalf of Mazars LLP
Chartered Accountants and Statutory Auditor
Tower Bridge House
St Katharine's Way
London E1W 1DD

14 May 2021

Income statement

For the year ended 31 December 2020

	Notes	2020 (£ 000')	2019 (£ 000')
Interest income		21,773	23,079
Interest expense		(5,784)	(5,684)
Net interest income	6	**15,989**	**17,395**
Fee and commission income		1,732	1,438
Fee and commission expense		(242)	(128)
Net fee and commission income	7	**1,490**	**1,310**
Net foreign exchange income		8	201
Fair value gain on derivative financial instruments		258	45
Gain on sale of financial investments		-	308
Other income	8	220	354
Net other income		**486**	**908**
Staff costs	9	(10,807)	(10,115)
Depreciation	19	(971)	(932)
Administrative and general expenses	10	(4,910)	(5,129)
Operating expenses		**(16,688)**	**(16,176)**
Operating profit before credit impairment losses		**1,277**	**3,437**
Credit impairment (charges) / reversals	11 & 31.15	(588)	303
Profit before tax		**689**	**3,740**
Tax charge	12	(89)	(256)
Profit after tax		**600**	**3,484**

Profit for the year arises from continuing operations.

The accompanying notes on pages 58 to 121 form an integral part of the financial statements.

These financial statements were approved by the Board of Directors and authorised for issue on 14 May 2021.

Birmingham University

Statement of Other Comprehensive Income

For the year ended 31 December 2020

	Notes	2020 (£ 000')	2019 (£ 000')
Profit after tax		**600**	**3,484**
Items that may be reclassified subsequently to the income statement:			
Fair value through other comprehensive income reserve			
- Net gains from changes in fair value	27	117	308
- Deferred tax charge	27	(22)	(58)
		95	250
Net losses transferred to income statement due to impairment		13	30
Other comprehensive income for the year net of tax		**108**	**280**
Total comprehensive income for the year		**708**	**3,764**
Total comprehensive income for the year attributable to equity holders		**708**	**3,764**

Profit for the year arises from continuing operations.

The accompanying notes on pages 58 to 121 form an integral part of the financial statements.

These financial statements were approved by the Board of Directors and authorised for issue on 14 May 2021.

Statement of Financial Position

As at 31 December 2020

	Notes	2020 (£ 000')	2019 (Represented) (£ 000')
Assets			
Cash in hand and with central bank	14	79,410	58,964
Due from banks	15	111,857	98,298
Loans and advances to customers at amortised cost	16	455,954	430,233
Financial investments	17	104,357	84,586
Derivative assets held for risk management	18	616	357
Property and equipment	19	7,779	8,483
Other assets	20	888	1,070
Deferred tax assets	13	1,272	1,285
Total assets		**762,133**	**683,276**
Liabilities and Equity			
Liabilities			
Due to banks at amortised cost	21	40,091	6,722
Due to customers at amortised cost	22	623,644	577,013
Derivative liabilities held for risk management	18	358	312
Accruals, deferred income and other liabilities	23	5,622	7,039
Current tax liabilities	24	103	570
Deferred tax liabilities	27	70	48
Subordinated liabilities	25	20,063	20,098
Total liabilities		**689,951**	**611,802**
Equity			
Called up share capital	26	60,000	60,000
Retained earnings		11,826	11,226
Fair value through other comprehensive income reserve	27	356	248
Total equity		**72,182**	**71,474**
Total liabilities and equity		**762,133**	**683,276**

Signed on behalf of the Board of Directors

Chairman
(Muhammad H. Habib)

Director
(Satyajeet Roy)

The accompanying notes on pages 58 to 121 form an integral part of the financial statements.
These financial statements were approved by the Board of Directors and authorised for issue on 14 May 2021.
The 2019 financial statements are re-presented due to reclassification of related assets and liabilities.

Statement of Changes in Equity

For the year ended 31 December 2020

	Called up Share Capital (£ 000')	Fair value through other comprehensive income reserve (£ 000')	Retained earnings (£ 000')	Total (£ 000')
Balance as at 1 January 2020	**60,000**	**248**	**11,226**	**71,474**
Profit after tax	-	-	600	**600**
Fair value through other comprehensive income (net gains during the year)	-	117	-	**117**
Deferred tax	-	(22)	-	**(22)**
		95	-	**95**
Net losses transferred to OCI due to impairment		13	-	**13**
Balance as at 31 December 2020	**60,000**	**356**	**11,826**	**72,182**

	Called up Share Capital (£ 000')	Fair value through other comprehensive income reserve (£ 000')	Retained earnings (£ 000')	Total (£ 000')
Balance as at 1 January 2019	**60,000**	**(32)**	**9,683**	**69,651**
Adjustment on initial application of IFRS 16				
- Change in accounting policy	-	-	(182)	(182)
- Deferred tax impact on change in accounting policy	-	-	35	35
	-	-	(147)	(147)
Balance as at 1 January 2019	**60,000**	**(32)**	**9,536**	**69,504**
Dividend paid	-	-	(1,794)	**(1,794)**
Profit after tax	-	-	3,484	**3,484**
Fair value through other comprehensive income (net gains during the year)	-	308	-	**308**
Deferred tax	-	(58)	-	**(58)**
		250	-	**250**
Net losses transferred to OCI due to impairment		30	-	**30**
Balance as at 31 December 2019	**60,000**	**248**	**11,226**	**71,474**

The accompanying notes on pages 58 to 121 form an integral part of the financial statements.
These financial statements were approved by the Board of Directors and authorised for issue on 14 May 2021.

Cash Flow Statement

For the year ended 31 December 2020

	Notes	2020 (£ 000')	2019 (Represented) (£ 000')
Cash flows from operating activities			
Profit before tax		689	3,740
Adjusted for:			
- Impairment losses / (Reversals) on loans and advances at amortised cost	11	588	(303)
- Gain sale of financial assets at fair value through other comprehensive income		-	(308)
- Depreciation	19	971	932
		2,248	**4,061**
Net (increase)/decrease in operating assets			
Loans and advances to banks at amortised cost		(13,756)	(39,565)
Loans and advances to customers at amortised cost		(26,097)	(30,721)
Derivative financial instruments for risk management		(259)	(190)
Other assets		286	206
Net increase/(decrease) in operating liabilities			
Due to banks at amortised cost		33,369	(10,677)
Due to customers at amortised cost		46,631	53,520
Derivative financial instruments for risk management		46	175
Accruals, deferred income and other liabilities		(991)	(438)
Current tax liabilities		(570)	(561)
Tax paid		(77)	(372)
Net cash inflow / (outflow) from operating activities		**40,830**	**(24,562)**
Cash flows from investing activities			
Purchase of property and equipment		(267)	(457)
Purchase of financial investments		(39,436)	(13,163)
Maturity / sale of financial investments		19,780	32,572
Net cash (outflow) / inflow from investing activities		**(19,923)**	**18,952**
Cash flows from financing activities			
Payment of dividend		-	(1,794)
Leases paid		(426)	(436)
Payment of interest on subordinated liabilities		(35)	(6)
Net cash outflow from financing activities		**(461)**	**(2,236)**
Net increase / (decrease) in cash and cash equivalents		**20,446**	**(7,846)**
Cash and cash equivalents at the beginning of the year		58,964	66,810
Cash and cash equivalents at the end of the year		**79,410**	**58,964**

The accompanying notes on pages 58 to 121 form an integral part of the financial statements.

The 2019 financial statements are re-presented due to reclassification of related assets and liabilities.

Notes to the Financial Statements

For the year ended 31 December 2020

1. The company and its operation

Habib Bank Zurich plc ("the Bank or HBZ UK") was incorporated in the United Kingdom on 28 January 2014 as a public limited company. The Bank is a wholly owned subsidiary of Habib Bank AG Zurich, Weinbergstrasse 59, PO Box 225, 8042 Zurich, Switzerland ("The Group"). The Group's financial statements are available at www.habibbank.com.

2. Basis of preparation

These financial statements have been prepared in accordance with International Accounting Standards in conformity with the requirements of the Companies Act 2006

The functional currency of the Bank is Pound Sterling, which is also the presentational currency of these financial statements.

3. Basis of measurement

The financial statements have been prepared on a historical cost basis, except for the following material items:

Items	Measurement basis
Financial assets at FVOCI (applicable from 1 January 2019)	Fair value
Derivative financial instruments	Fair value

4. Going concern

As detailed in the Directors' Report, the Directors believe that it remains appropriate to prepare the financial statements on a going concern basis for the foreseeable future from the reporting date. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the Bank's financial position, future projections of profitability, cash flows and capital and liquidity resources and the longer-term strategy of the business.

The Bank's capital and liquidity plans have been stress tested against a severe but plausible downside scenario used in the assessment of the ICAAP and ILAAP reviewed and approved by the Board of Directors. The Board concluded that both capital and liquidity remained within present regulatory requirements over the going concern period. The Directors also considered the subordinated debt of £20m, which was rolled over for another 5 years as agreed with the parent bank on the date of its maturity on 1 April 2021.

The year 2020 was an unexpected period both in terms of uncertainty and instability primarily caused by the Covid-19 outbreak. The Bank continues to demonstrate that its financial resources and operational capabilities are adequate and dependable to manage risks associated with ongoing impact of Covid 19.

The Directors' assessment to continue to adopt the going concern basis include risk assessment identifying factors impacting the business operations and financial implications associated with Covid 19.

There are no material uncertainties identified that may post any doubt on the Bank's ability to continue as a going concern on the foreseeable future.

5. Accounting Policies

5.1 Compliance with international Financial Standards

The financial statements of the Bank have been prepared in accordance with the Companies Act 2006 and with International Accounting Standards in conformity with the requirements of the Companies Act 2006.

Changes to significant accounting policies are described on Note 5.4.

5.2 New standards and amendments to existing standards

This below provide a summary of (a) new standards and amendments that are effective for the first time for periods commencing on or after 1 January 2020 (i.e., years ending 31 December 2020), and (b) forthcoming requirements, being standards and amendments that will become effective on or after 1 January 2021.

The following standards and interpretations apply for the first time to financial reporting periods commencing on or after 1 January 2020:

- Amendments to IAS 1 and IAS 8 – Definition of material. The IASB has made amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors which use a consistent definition of materiality throughout International Financial Reporting Standards and the Conceptual Framework for Financial Reporting, clarify when information is material and incorporate some of the guidance in IAS 1 about immaterial information.
- Amendments to IFRS 3 – Definition of a business. The amended definition of a business requires an acquisition to include an input and a substantive process that together significantly contribute to the ability to create outputs. The definition of the term 'outputs' is amended to focus on goods and services provided to customers, generating investment income and other income, and it excludes returns in the form of lower costs and other economic benefits.
- Amendments to IFRS 7, IFRS 9 and IAS 39 – Interest rate benchmark reform. The amendments made to IFRS 7 Financial Instruments: Disclosures, IFRS 9 Financial Instruments and IAS 39 Financial Instruments: Recognition and Measurement provide certain reliefs in relation to interest rate benchmark reforms.
- Revised Conceptual Framework for Financial Reporting. The IASB has issued a revised Conceptual Framework which will be used in standard-setting decisions with immediate effect. Key changes include:
  - increasing the prominence of stewardship in the objective of financial reporting
  - reinstating prudence as a component of neutrality
  - defining a reporting entity, which may be a legal entity, or a portion of an entity
  - revising the definitions of an asset and a liability
  - removing the probability threshold for recognition and adding guidance on derecognition
  - adding guidance on different measurement basis, and
  - stating that profit or loss is the primary performance indicator and that, in principle, income and expenses in other comprehensive income should be recycled where this enhances the relevance or faithful representation of the financial statements.

The adoption of the standards above did not result in material changes to the financial statements.

The following standards and interpretations had been issued but were not mandatory for annual reporting periods ending on 31 December 2020.

- IFRS 17 – Insurance Contracts (1 January 2023). IFRS 17 was issued in May 2017 as replacement for IFRS 4 Insurance Contracts. It requires a current measurement model where estimates are re-measured in each reporting period.
- Amendments to IFRS 16 – Covid-19-related Rent Concessions (1 June 2020). As a result of the COVID-19 pandemic, rent concessions have been granted to lessees. Such concessions might take a variety of forms, including payment holidays and deferral of lease payments.
- Amendments to IAS 1 – Classification of Liabilities as Current or Non-current (1 January 2022). The narrow-scope amendments to IAS 1 Presentation of Financial Statements clarify that liabilities are classified as either current or non-current, depending on the rights that exist at the end of the reporting period. Classification is unaffected by the expectations of the entity or events after the reporting date (e.g. the receipt of a waiver or a breach of covenant).
- Amendments to IAS 16 – Property, Plant and Equipment: Proceeds before intended use (1 January 2022). Prohibits an entity from deducting from the cost of an item of PP&E any proceeds received from selling items produced while the entity is preparing the asset for its intended use. It also clarifies that an entity is 'testing whether the asset is functioning properly' when it assesses the technical and physical performance of the asset.
- Amendments to IFRS 3 – Reference to conceptual framework (1 January 2022). Minor amendments were made to IFRS 3 Business Combinations to update the references to the Conceptual Framework for Financial Reporting and add an exception for the recognition of liabilities and contingent liabilities within the scope of IAS 37 Provisions, Contingent Liabilities and Contingent Assets and Interpretation 21 Levies. The amendments also confirm that contingent assets should not be recognised at the acquisition date.
- Amendments to IAS 37 – Onerous contracts (1 January 2022). The amendment to IAS 37 clarifies that the direct costs of fulfilling a contract include both the incremental costs of fulfilling the contract and an allocation of other costs directly related to fulfilling contracts.
- Annual Improvements to IFRS Standards 2018-2020 (1 January 2022).
  - IFRS 9 Financial Instruments – clarifies which fees should be included in the 10% test for derecognition of financial liabilities.
  - IFRS 16 Leases – amendment of illustrative example 13 to remove the illustration of payments from the lessor relating to leasehold improvements, to remove any confusion about the treatment of lease incentives.
  - IFRS 1 First-time Adoption of International Financial Reporting Standards – allows entities that have measured their assets and liabilities at carrying amounts recorded in their parent's books to also measure any cumulative translation differences using the amounts reported by the parent.
  - IAS 41 Agriculture – removal of the requirement for entities to exclude cash flows for taxation when measuring fair value under IAS 41.
- Sale or contribution of assets between an investor and its associate or joint venture – Amendments to IFRS 10 and IAS 28 (not yet set). The IASB has made limited scope amendments to IFRS 10 Consolidated financial statements and IAS 28 Investments in associates and joint ventures. The amendments clarify the accounting treatment for sales or contribution of assets between an investor and its associates or joint ventures.

The above standards and interpretations are not result in material changes to the financial statements.

5.3 Critical accounting estimates and judgements

The preparation of the Bank's financial statements in accordance with IFRS requires management to make judgements, estimates and assumptions that affect the application of the Bank's and the reported amounts of revenues, expenses, assets and liabilities and the accompanying disclosures. Actual results may differ from estimates.

Estimates and assumptions predominantly relate to ECL modelling, impairment of loans and advances and the determination of useful lives and residual values for property and equipment.

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

5.3.1 Judgement

Information about judgements made in applying accounting policies that have the most significant effects on the amounts recognised in the financial statements is included in the following notes:

- Note 5.5.3: classification of financial assets: assessment of business model within which the assets are held and assessment of whether the contractual terms of the financial assets are SPPI on the principal amount outstanding.

- Note 31.8: establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining methodology for incorporating forward-looking information into measurement of ECL and selection and approval of models used to measure ECL.

In determining the amount of the impairment loss, the Bank is required to exercise a degree of judgement.

The accuracy of the provision would therefore be affected by unexpected changes to these assumptions.
The table below shows the estimated ECL impact on key principle portfolios for both a positive growth (Upward scenario) and a downturn (Downward scenario) of macroeconomic variables used by the Bank in estimating the Estimated Credit Loss (Loss).

The inputs have been modelled by replacing the Baseline macroeconomic variables with the Downside and Upside movement re-calibrating the PDs and LGDs.

Impact on ECL	2020	2019
Improvement in Debt to GDP Ratio and unemployment rate 5%	5% decrease	7% decrease
Improvement in Debt to GDP Ratio and unemployment rate 10%	10% decrease	14% decrease
Improvement in Debt to GDP Ratio and unemployment rate 20%	21% decrease	27% decrease
Deterioration in Debt to GDP Ratio and unemployment rate 5%	5% decrease	7% increase
Deterioration in Debt to GDP Ratio and unemployment rate 10%	11% decrease	15% increase
Deterioration in Debt to GDP Ratio and unemployment rate 20%	21% decrease	31% increase

- *Effective interest rate:* Bank makes assumptions around the expected lives of mortgages and the collateral support to calculate the effective interest rate for specific customer. Management regularly reviews these assumptions and compares with actual results.

- *Tax position:* Recognition and measurement of deferred tax assets is based on business profit forecasts. Details on the recognition of deferred tax assets is provided in Note 13.

- *Fair value of derivatives and financial assets:* The Bank measures Fair Value through Other Comprehensive Income (FVOCI) at fair value using market prices and Derivative financial instruments based on observable market data. Note 30 provide the determination criteria of the fair value of financial instruments with significant unobservable inputs.

- Note 5.5.8 provides the recognition and measurement of provision and contingencies.

5.3.2 Assumptions and estimation uncertainties:

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ended 31 December 2020 is included in the following notes.

Impairment of financial instruments at Note 5.5.3 on Page 63 explains determining inputs into the ECL measurement model, including incorporation of forward-looking information

These estimates and assumptions are explained in the notes below.

5.4 Changes in accounting policies

The Bank has consistently applied the accounting policies as set out on Note 5.5 to all periods presented in these financial statements.

5.5 Significant accounting policies

Revenue recognition

5.5.1 Interest income and expense

Interest income and expense are recognised in profit or loss using the effective interest method, the 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- The gross carrying amount of the financial asset under stage 1 and stage 2; or
- The net amount (gross carrying amount less provisions held) under stage 3; or
- The amortised cost of the financial liability

When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Bank estimates the future cash flows considering all contractual terms of the financial instruments but does not consider the future credit losses.

The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss.

The 'gross carrying value of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

5.5.2 Fee and commission income

The Bank provided banking services to personal and business customers, including account management, foreign currency transactions and servicing fees.

Fee and commission income is accounted for depending on the services to which the income relates:

- Revenue from account services and servicing fees is recognised over time as the services are provided.
- Commitment fees form an integral part of the effective interest rate of a financial instrument. These are recognised as an adjustment to the effective interest rate and recorded in interest income; and
- Loan termination represents fee paid by customers on early repayment of loans is recognised at the time loan is settled by the customer.
- Fees for ongoing account management are charged to the customer's account as per schedule of fee and charges. The Bank sets the rates separately for personal and business banking customers in each jurisdiction on monthly basis.
- Revenue earned on the execution of a significant act is recognised in fee income when the act is completed including trade finance income;
- Transaction-based fees for interchange and foreign currency transactions are charged to the customer's account when the transaction takes place.
- Bank provides locker services to the customers, the fee of which is charged upfront on annual basis and amortised monthly.
- Other fees charged to the customer's account when the transaction takes place

5.5.3 Financial assets and liabilities

Recognition and initial measurement

The Bank initially recognises loan and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated. All other financial instruments (including regular-way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Group becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue. The fair value of a financial instrument at initial recognition is generally its transaction price.

Classification

IFRS 9 contains three principle classification categories for financial assets: measured at amortised cost (AC), fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows.

Under IFRS 9 the fair value changes in financial liabilities are presented as follows:

- The amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- The remaining amount of change in the fair value is presented in profit or loss.

Business model assessment

The Bank has considered the business model objective for each category of financial assets. For all loans and advances to banks and customers, the objective is to collect the contractual cash flows. The Bank maintains financial investments in (i) held to collect and (ii) held to collect and sell. For financial investments held to collect,

the objective is to collect the contractual cash flows while for the financial investments held to collect and sell, the objective is to collect the contractual cash flows and sell the assets.

The Bank makes an assessment of the objectives of a business model in which as asset is held at a portfolio level as it best reflects the way the business is managed, and information is provided to management.

Assessment whether contractual cash flows are solely payment of principal and interest (SPPI Test)

For the purposes of this assessment, ‘principal’ is defined as the fair value of the financial asset on initial recognition. ‘Interest’ is defined as consideration of the time value of money and for the credit risk associated with the principal amount during a particular period of time and for basic lending risk and costs, as well as profit margin.

The Bank has made an assessment of the cash flow characteristics (SPPI test) of financial assets and concluded that loans and advances to banks and customers will continue to be recognized at amortized cost and financial investments at fair value through other comprehensive income and at amortised cost.

In assessing whether the contractual cash flows are SPPI, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows that it would not meet its condition.

As a result of the assessments made, the Bank does not consider there is any material impact to the classification and measurement of its financial assets and liabilities.

Based on Bank’s assessment it does not hold any financial assets, which fail to meet the SPPI test.

Financial Assets

As required by IFRS 9 classification and measurement of financial assets is based on the Bank’s business model for managing the asset and the asset’s contractual cash flow characteristics.

Amortised Cost

A financial asset is measured at amortised cost if it meets both the following conditions and is not designated as FVTPL

- The asset is held with the business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified basis to cash flows that are SPPI.

Fair value through other comprehensive income (FVOCI)

A debt instrument is measured at FVOCI only if it meets both the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial assets give rise on specific dates to cash flows that are SPPI.

There is no equity instrument maintained by the Bank measured at FVOCI

Fair value through profit and loss (FVTPL)

- All other financial assets are classified as measured at FVTPL.

Financial liabilities

All financial liabilities are measured at amortised cost, except for financial liabilities at fair value through profit or loss. Such liabilities include derivatives (other than derivatives that are financial guarantee contracts or are designated and effective hedging instruments).

Islamic financing and Investments

The Bank introduced Islamic financing and deposits products in 2020 under the brand name 'Sirat'. The Bank offers financing products to its customers namely Commodity Murabaha and Diminishing Musharika.

Murabaha is a contract for the sale of goods at cost plus an agreed profit mark-up. Under the arrangement entered into between the Bank and customer, the Bank purchases a commodity and then sells it to a customer on a deferred settlement basis with an agreed mark-up. The delivery of the goods is immediate but payment may be deferred. Commodity Murabaha is a specific example of such a contract where the item being sold is a metal commodity

Musharika financing is made through a contract under which the Bank will enter into an agreement to jointly purchase a property with another party on ongoing basis or for a limited time. In the particular arrangements with the Bank will sell its share in this partnership to the customer until they become the sole owner of the specific asset, therefore, making the product Diminishing Musharika financing. Rental income will be received relating to that proportion of the property owned by the Bank at any point in time. The transaction is recognised as a financial asset upon legal completion of the property purchase and the amount receivable is recognised at an amount equal to the net investment in the transaction.

Where initial direct costs are incurred by the Bank such as legal and valuation fees and commission that are incremental and directly attributable to negotiating and arranging the transaction, these costs are included in the initial measurement of the receivable and the amount of income over the term will be reduced. Rental income is recognised at a constant periodic rate of return on the Bank's net investment.

Investment securities are non-derivative financial assets which are purchased for profit and intended to be held for an indefinite period of time, but may be sold in response to liquidity requirements or changes in profit rates or exchange rates. They are classified as FVOCI and are initially recognised at fair value including direct and incremental transaction costs, and subsequently measured at FVOCI. The cash flows received by the Bank are solely payments of principal and profit on the outstanding balance or sale proceeds in the event of a sale.

Gains and losses arising from changes in the fair value of investment security assets, other than foreign exchange gains and losses from monetary items, are recognised directly within a separate component of equity, until the financial assets are derecognised or impaired at which time the cumulative gain or loss previously recognised within equity is transferred to the statement of comprehensive income.

Islamic deposits

Customer Wakala deposits consist of an Islamic financing transaction, which represents an agreement whereby the customer appoints the Bank as agent to invest a certain sum of money, per specific conditions in order to achieve an expected specified return. The Bank, as agent, is obliged to return the invested amount in case of default, negligence or violation of any of the terms and conditions of the Wakala. Balances are valued based on their amortised cost.

Revenue recognition

Profit on Commodity Murabaha and Diminishing Musharika is recognised as income on a time-apportionment basis over the period of the contract, based on applying the effective profit rates to the principal amounts outstanding.

The accounting policies for Islamic financial assets and liabilities are consistent with those applied for similar financial assets and liabilities.

Derecognition

Financial Assets

The Bank derecognise a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including new asset obtained less any liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

Financial Liabilities

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

Modification of financial assets and financial liabilities

Financial Assets

If the terms of a financial asset were modified, then the Bank evaluated whether the cash flows of the modified assets were substantially different.

If the cash flows were substantially different, then the contractual rights to cash flows from the original financial asset were deemed to have expired. In this case, the original financial asset was derecognised, and a new financial asset was recognised at fair value plus any eligible transaction cost. Any fees received as part of the modification are accounted for as follows:

- Fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and
- Other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different term. If the Bank plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place.

The Bank derecognises a loan to a customer, when the terms and conditions have been renegotiated to the extent that, substantially, it becomes a new loan, with the difference recognised as a derecognition gain or loss, to the extent that an impairment loss has not already been recorded. The newly recognised loans are classified as Stage 1 for ECL measurement purposes.

When assessing whether or not to derecognise a loan to a customer, amongst others, the Bank considers the following factors:

- change in currency of the loans
- introduction of equity feature
- change in counterparty
- if the modification is such that the instrument would no longer meet the SPPI criterion

If the modification does not result in cash flows that are substantially different, as set out below, the modification does not result in derecognition. Based on the change in cash flows discounted at the original EIR, the Bank records a modification gain or loss, to the extent that an impairment loss has not already been recorded.

Financial Liabilities

The Bank derecognises a financial liability when its terms were modified, and the cash flows of the modified liability were substantially different. The Bank considers a modification substantial based on qualitative factors and if it results in a difference between the adjusted discounted present value and the original carrying amount of the financial liability of, or greater than, ten percent. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss.

Fair value measurement

'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 in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When one is available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as 'active' if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

Impairment of financial assets

ECL are probability-weighted estimates of credit losses. They are measured as follows:

Financial assets that are not credit impaired at the reporting date: at the present value of all cash shortfalls i.e., the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive.

Financial assets that are credit-impaired at the reporting date: at the difference between the gross carrying amount and the present value of the future cash flows.

IFRS 9 Impairment applies to financial instruments that are not measured at fair value through profit and loss (FVTPL). Financial assets falling within the scope of impairment are provided for by calculating their Expected Credit Loss (ECL). This requires considerable judgement regarding how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis.

Estimated Credit Loss (ECL)

ECL is an estimate of present value of cash shortfalls over the life of the financial instrument and is computed as a product of probability of default (PD), loss given default (LGD) and exposure at default (EAD). The present value of cash shortfalls is calculated by taking into account the time value of money and forward-looking information.

Probability of default (PD)

The PD represents the expected point-in-time probability of a default over the next 12 months and remaining lifetime of the financial instrument, respectively, based on conditions existing at the balance sheet date and future economic conditions that affect credit risk.

Loss given default (LGD)

The LGD represents the expected loss conditional on default, taking into account the mitigating effect of collateral, its expected value when realized, and the time value of money.

Exposure at default (EAD)

The EAD represents the expected exposure at default, taking into account the repayment of principal and interest from the balance sheet date to the default event together with any expected drawdown of a facility.

Measurement of ECL

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluation of a range of possible outcomes that incorporates forecasts of future economic conditions. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions.

In determining ECLs, the Bank has considered two macroeconomic variables, (i) government debt to GDP and (ii) unemployment rate and weighted these according to their likely occurrence. The scenarios include a baseline scenario, based on the current economic environment, an upturn scenario and a downturn scenario. Scenario forecasts were weighted by the scenario's probability of occurrence in order to arrive at the probability-weighted macroeconomic impact over the 5-year forecast horizon.

The estimation and application of this forward-looking information will require significant judgement and be subject to appropriate internal governance and scrutiny.

Loss allowance for ECL are presented in the statement of financial position as follows:

Financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
Loan commitments, off balance sheet items and financial guarantees: generally, as a provision;

Where a financial instrument includes both a drawn and an undrawn component / off balance sheet items, and the Bank cannot identify the ECL on the loan commitment component separately for those on the drawn components: The Bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and

Debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and recognised in the fair value reserves.

Significant increase in credit risk (SICR)

A critical element to the implementation of IFRS 9 Impairment is determining whether there has been a significant increase in risk of a credit exposure since origination to classify the assets into one of three stages as set out below.

The Bank considers 30 days past due (DPD), marking the status of a loan as non-performing, a rating downgrade, restructure tag, or cross product defaults as being strong indicators of a significant increase in credit risk of an account. Hence, staging rules have been determined based on these criteria, as explained below:

Impairment is measured as either 12 months ECL, or Lifetime ECL depending on the change in credit risk associated with the financial instrument. The approach allocates financial instruments into three stages:

Staging Criteria

Stage 1 – 12-month ECL

The Bank assesses ECLs on exposures where there has not been a significant increase in credit risk since initial recognition and that were not credit impaired upon origination.

Stage 2 – Lifetime ECL

The Bank assesses ECLs on exposures where there has been a significant increase in credit risk since initial recognition but are not credit impaired. Bank recognises a lifetime ECL (i.e., reflecting the remaining lifetime of the financial asset).

Stage 3 – Lifetime ECL

The Bank identifies ECLs on those exposures that are assessed as credit impaired based on whether one or more events that have a negative impact on the estimated future cash flows of that asset have occurred. For exposures that have become credit impaired, a lifetime ECL is recognized as a specific provision, and interest revenue is calculated by applying the effective interest rate to the amortised cost (net of provision) rather than the gross carrying amount.

Write off

Loan and debt securities are written off (either partially or in full) where there is no reasonable expectation of recovering a financial asset in entirely or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or source of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

Recoveries of amount previously written off are included in 'impairment loss on financial instruments' in the statement of profit or loss or OCI.

Financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

Hedge accounting

IFRS 9 also incorporates hedge accounting rules that intend to align hedge accounting with risk management practices. There is also an accounting policy choice to defer the adoption of IFRS 9 hedge accounting and to continue with IAS 39 hedge accounting. As the Bank does not currently adopt hedge accounting, this part of the standard does not currently impact the Bank.

5.5.4 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 that, in the case of a non-financial variable, it is not specific to a party to the contract (i.e., 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 expected to have a similar response to changes in market factors.
- It is settled at a future date.

All derivative instruments are held at fair value through profit or loss. Derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative. Derivative assets and liabilities arising from different transactions are only offset, if they meet the offsetting criteria under IAS 32.

5.5.5 Employee benefits

Short-term employee benefits, such as salaries, paid absences and other benefits, are accounted for on an accrual basis over the period which employees have provided services in the year. Bonuses are recognised to the extent that the Bank has a present obligation to its employees that can be measured reliably. All expenses related to employee benefits are recognised in the income statement in staff costs, which is included within operating expenses.

The Bank provides a defined contribution pension scheme for its staff. For this scheme, the Bank recognizes contributions due in respect of the accounting period in the income statement. Any contributions unpaid at the balance sheet date are included as a liability.

5.5.6 Cash and cash equivalents

Cash and cash equivalents represent Cash in hand and readily available balances held with the central bank.

5.5.7 Property and equipment

Property and equipment are initially recognised at acquisition cost, including any costs directly attributable to bringing the assets to the location and condition necessary for it to be capable of operating in the manner intended by the Bank's management.

Property and equipment are subsequently measured using the cost model at cost less accumulated depreciation and impairment losses, if any. The Bank adheres to IAS 36, Impairment of Assets which, seeks to ensure that property and equipment assets are not carried at more than their recoverable amount (i.e., the higher of fair value less costs of disposal and value in use).

At the end of each reporting period, the Bank assesses whether there is any indication that a property and equipment may be impaired (i.e., its carrying amount may be higher than its recoverable amount). If there is an indication that a property and equipment may be impaired, then the asset's recoverable amount is calculated. An impairment is recognised in profit or loss as the difference between carrying value and recoverable amount.

Depreciation is provided on a straight-line basis over estimated useful lives as follows:

Freehold improvements	25 Years
Leasehold improvements	Over the remaining period of the lease
Leased assets (ROU)	Over the remaining period of the lease
Motor vehicles	5 years
Furniture, fixtures and fittings	3 - 5 years
Computer hardware	4 years
Buildings	40 years

The assets' useful lives are reviewed, and adjusted if appropriate, at the reporting date. Gains or losses arising on the disposal of property and equipment are determined as the difference between the disposal proceeds and the carrying amount of the assets and are recognised in profit or loss within other operating income.

5.5.8 Provisions and contingent liabilities

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

Provisions are measured at the estimated expenditure required to settle the present obligation, based on the most reliable evidence available at the reporting date, including the risks and uncertainties associated with the present obligation.

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are disclosed in the financial statements unless the probability of an outflow of resources is remote.

Contingent assets are not recognised. Contingent assets are disclosed in the financial statements when an inflow of economic benefits is probable.

5.5.9 Taxes

Income tax on the profit or loss for the year comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

Current tax is the tax expected to be payable on the taxable profit for the year, calculated using tax rates enacted or substantively enacted by the balance sheet date, and any adjustment to tax payable in respect of previous year.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the balance sheet and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax asset is recognised based on availability of future taxable profit against which carry-forward tax losses can be used. Future profits are based on financial projections prepared based on some key assumptions, which may vary in future due to internal and external factors such as projected growth, economic outlook, interest rates.

Deferred tax is determined using tax rates and legislation enacted, or substantively enacted, by the balance sheet date and is expected to apply when the deferred tax asset is realised, or the deferred tax liability is settled.

Deferred and Current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered.

5.5.10 Foreign currency translation

Transactions in foreign currencies are initially recorded at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into the functional currency at the rate of exchange ruling at the reporting date. Exchange rate differences are recognised in profit and loss.

5.5.11 Segment Reporting

The Bank undertakes commercial banking, which is carried on mainly within the United Kingdom and all other services are ancillary to commercial banking activities. The management information system and reporting to Board is also aligned to this business model.

The Bank currently manages its business activities on a centralised basis; as a result, the revenue and costs are not attributable to any one operating and geographic segment. No revenue transaction with a single external customer or counterparty amounted to 10% of total revenue for the year.

5.5.12 Accounting for leases

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Group uses the definition of a lease in IFRS 16.

At commencement or on modification of a contract that contains a lease component, the Bank allocates consideration in the contract to each lease component on the basis of its relative standalone price. However, for leases of branches and office premises the Bank has elected not to separate non-lease components and accounts for the lease and non-lease components as a single lease component.

The Bank recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to branches or office premises less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, the Bank uses its incremental borrowing rate as the discount rate.

Lease payments are allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease term so as to produce a constant period rate of interest on the remaining balance of the liability. The incremental borrowing rate is used that the Bank would have to pay to borrow the funds necessary to obtain an asset of a similar value in a similar economic environment with similar terms and conditions. The rates are determined for each economic environment in which Bank operates.

The incremental borrowing rate is the discount rate that Bank determines by analysing its borrowings from various external sources and makes certain adjustments to reflect the terms of the lease and type of asset leased.

The Bank discounted lease payments using its incremental borrowing rate. The weighted average rate applied is 1.25%.

The lease liability is measured at amortised cost using the effective interest method.

Leases are recognised as a ROU asset and a corresponding liability at the date at which the leased asset is made available for use.

Short-term leases and leases of low-value assets

The Bank has elected not to recognise right-of-use assets and lease liabilities for short-term and low value leases, including lease of a rental premises. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

6. Net interest income

	Notes	2020 (£ 000')	2019 (£ 000')
Interest income			
Funds held with central bank		146	402
Due from banks	6.1	982	1,458
Loans and advances to customers	6.2	19,453	19,421
Negative interest on due to customers	6.3	49	105
Financial investments – FVOCI	6.4	966	1,387
Financial investments – Amortised cost		177	306
		1,143	1,693
Total interest Income		**21,773**	**23,079**
Interest expense			
Due to banks	6.5, 6.6	(360)	(100)
Due to customers		(5,021)	(5,113)
Subordinated liabilities		(368)	(431)
Finance cost on lease liability	6.7	(35)	(40)
Total interest Expense		**(5,784)**	**(5,684)**
Net Interest Income		**15,989**	**17,395**

Interest income against loans and advances to customers included total of £480k (2019: £469k) relating to impaired financial assets and has been considered as part of the cash flows when assessing for individual impairment provisions.

6.1 This includes profit of £104k (2019: £66k) on the Islamic money market placements.

6.2 This includes the profit of £557k (2019: Nil) customer Islamic lending products.

6.3 This includes the interest charged on deposits maintained in the currencies of Euro and Swiss Franc.

6.4 This includes income on Sukuk investments £103k (2019: 65k) earned by the Bank.

6.5 This includes the £304k (2019: Nil) being the interest charged by Habib Bank AG Zurich (parent) against the fiduciary deposits maintained by the bank.

6.6 This includes the profit of 6k (2019: Nil) paid by the Bank on Islamic deposit products.

6.7 This represents the interest expense charged during the year on lease liabilities following the adoption of IFRS 16.

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7. Net fee and commission income

	2020 (£ 000')	2019 (£ 000')
Fee and commission income		
Loan termination fee	40	82
Customer transaction fees	273	329
Trade Finance	813	413
Other fees and commission on banking and credit products	606	614
Total fee and commission income	**1,732**	**1,438**
Fee and commission expense		
Bank charges	(175)	(90)
Commission on internet deposits	(22)	(1)
Other fees and commission	(45)	(37)
Total fee and commission expense	**(242)**	**(128)**
Net fee and commission income	**1,490**	**1,310**

7.1 Disaggregation of fee and commission income

In the above table, fee and commission income with customers in the scope of IFRS 15 is disaggregated by major type of services.

The following table provides information about receivables and contract liabilities from contacts with customers:

8. Other income – net

	2020 (£ 000')	2019 (£ 000')
Receivables included in other assets	25	27
Deferred income included in other liabilities	121	130

The fee and commission income with customers is measured based on the consideration specified in a contract with a customer. The Bank recognised revenue when it transfers control over a service to a customer.

Other income – net	Notes	2020 (£ 000')	2019 (£ 000')
Right to light	8.1	-	105
Other		220	249
Total other income		**220**	**354**

8.1 This represents the amount received by Bank being “right to light” compensation. A “right to light” is an easement that gives a landowner the right to receive light through defined apertures in buildings on his or her land. The Bank received the above compensation as a result of a third-party development near to its head office reducing light to the Bank’s building.

9. Staff costs, including Directors' emoluments

	2020 (£ 000')	2019 (£ 000')
Salaries and allowances	(8,768)	(8,116)
Social security costs	(1,415)	(1,413)
Pension costs – defined contribution plan	(624)	(586)
Total staff costs	**(10,807)**	**(10,115)**
Average number of employees (Nos)	149	145
Actual number of employees (Nos)	138	150
Directors emoluments		
– Total emoluments of Directors – £ 000	907	928
– Total number of directors to whom retirement benefits are accruing – Nos	3	3
– Salary and benefits paid to the highest paid Director – £ 000	534	573

The emoluments of Directors disclosed above include salary and social security cost. Pension contribution included in Directors emoluments is £31k (2019: £26k).

The Parent bank paid emoluments of other Non-Executive directors' and has not recharged the Bank specifically for their services.

Key management personnel:

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Bank.

The key management personnel are the members of the Bank's Executive Committee together with its Directors. The table below details, on an aggregated basis, key management personnel compensation:

	2020 (£ 000')	2019 (£ 000')
Salaries and other short-term benefits	1,410	1,490
Post-employment benefits	82	81
Total staff costs	**1,492**	**1,571**
Loans outstanding – £ 000	142	154
No of persons	1	1

The loans are on secured basis and expected to be settled in cash. The loans attracted interest rate of 3%.

No provisions have been recognised in respect of loans given to key management personnel.

Deposits placed – £ 000	37	13
No of persons – Nos	3	3

10. Other operating expenses

	Notes	2020 (£ 000')	2019 (£ 000')
Premises running costs		(1,575)	(1,646)
Legal and Professional charges		(522)	(702)
Auditor's remuneration	10.1	(210)	(188)
IT and communication costs		(395)	(453)
Branches operation charges		(354)	(414)
Group direct expenses		(1,636)	(1,496)
Travelling and conveyance		(143)	(103)
Marketing and advertisement		(21)	(40)
Miscellaneous		(54)	(87)
Total other operating expenses		**(4,910)**	**(5,129)**

10.1 Auditors remuneration

	2020	2019
Statutory audit fee	(200)	(170)
Client Asset and Money audit fee	(10)	(11)
K-Helix Licence fee	-	(7)
Total Auditors remuneration	**(210)**	**(188)**

11. Credit impairment (charges) / reversals

	2020 (£ 000')	2019 (£ 000')
Loans and advances to customers		
– Charged during the year	(1,116)	(998)
– Recovered / settled during the year	740	1,532
– Net (losses) / gains	**(376)**	**534**
Financial investments		
– Net losses	(15)	(33)
Due from banks		
– Net losses	(197)	(198)
Impairment (losses) / gains on financial assets	**(588)**	**303**

12. Taxation

	2020 (£ 000')	2019 (£ 000')
Corporate tax:		
Current year	(103)	(570)
Prior year	27	22
	(76)	(548)
Deferred tax:		
Current year	(13)	292
	(89)	**(256)**

		2020 (£ 000')		2019 (£ 000')
Tax reconciliation				
Profit before tax		**689**		**3,740**
Expected tax charge	(19)%	(131)	(19)%	(711)
Permanent disallowable expenses	(17)%	(117)	(3)%	(126)
Deferred tax not recognized	16%	111	2%	75
Deferred tax on losses not previously recognized	3%	21	13%	484
Prior year adjustment	4%	27	1%	22
Total tax charge	**(13)%**	**(89)**	**(7%)**	**(256)**

The corporation tax rate from 01 April 2017 to 31 March 2023 is set at 19%. The Chancellor has announced increase in the corporation tax rate to 25% for the financial year beginning 1 April 2023 but it has not been substantively enacted.

13. Deferred tax assets

Deferred taxes are calculated on temporary differences under the liability method using the tax rates expected to apply when the liability is settled, or the asset is realised.

Deferred tax assets mainly relate to carry forward losses. The amount of carry forward losses available as at 31 December 2020 was £19.95 million (2019: £19.35 million) on which estimated amount of deferred tax not recognised amounted to £3.8 million (2019: £3.3 million). The Bank only account for deferred tax on the basis of future profits for a foreseeable period not exceeding four years. The Bank is of the view that assumptions used for preparing cash flow projections beyond such period are subject to significant change.

The table below shows the deferred tax assets including the movement in the deferred tax account during the year:

2020 £ 000'	Tax losses carried forward	IFRS 9 adoption	IFRS 16 adoption	Total
Opening balance as at 01 January 2020	1,122	130	33	1,285
Charged to statement of income	(7)	(3)	(3)	(13)
Balance as at 31 December 2020	**1,115**	**127**	**30**	**1,272**

2019 £ 000'	Notes	Tax losses carried forward	IFRS 9 adoption	FV Loss on FVOCI investments	IFRS 16 adoption	Total
Opening balance as at 01 January 2019		810	148	10	-	968
Charged to Equity	27	-	-	(10)	35	25
Charged to statement of income		312	(18)	-	(2)	292
Balance as at 31 December 2019		**1,122**	**130**	**-**	**33**	**1,285**

14. Cash in hand and with central bank

	Notes	2020 (£ 000')	2019 (£ 000')
Balance with central bank	14.1	78,819	58,190
Cash in hand		591	774
Total cash in hand and with central bank		**79,410**	**58,964**

14.1 This includes an amount of £3m (2019: £3m) held as a settlement cap for Image Clearing System.

14.2 No ECL was calculated on above as there is immaterial credit risk involved.

15. Due from banks

	Notes	2020 (£ 000')	2019 (£ 000')
Money market placements	15.1	77,753	74,904
Cash in current accounts		20,866	17,027
Bankers' acceptances		13,510	6,383
Cash in margin accounts	Note 15.2	260	320
		112,389	98,634
Estimated credit loss (ECL – Stage 1)		**(532)**	**(336)**
Total due from banks		**111,857**	**98,298**

15.1 This includes Islamic placements of £25.2 million (2019: 8.0 million).

15.2 This represents cash held with counterparties in accordance with collateral requirement under Credit Support Annex (CSA) agreements.

16. Loans and advances to customers at amortised cost

	Notes	2020 (£ 000')	2019 (Represented) (£ 000')
Commercial loans	16.1	422,293	394,177
Overdraft		23,943	30,160
Discounted bills & trade finance loans		14,871	10,580
Other loans including staff loans		262	354
Gross loans and advances to customers		**461,369**	**435,271**
Less: Provision for impairment		(5,415)	(5,038)
Net loans and advances to customers	16.2	**455,954**	**430,233**

16.1 This includes Islamic financing of £25.1 million (2019: Nil).

16.2 The 2019 financial statements are re-presented due to reclassification of related assets and liabilities.

16.3 Provision for impairment

	2020 (£ 000')	2019 (£ 000')
Balance at the beginning of the year	5,038	5,583
Impairment charged to profit and loss	1,116	998
Reversals during the period	(740)	(1,532)
Net impairment charged to P&L	376	(534)
Write off / Other	1	(11)
Total provision for impairment	**5,415**	**5,038**

17. Financial investments

	Notes	2020 (£ 000')	2019 (£ 000')
Debt Securities			
Investment securities measured at amortised cost	17.1	16,799	16,917
Investment securities measured at FVOCI	17.2	87,558	67,669
Total financial investments		**104,357**	**84,586**
Investment securities measured at amortised cost			
Multilateral development banks		16,799	16,917
Investment securities measured at FVOCI			
General government		1,670	519
Multilateral development banks		19,539	16,392
Financial institutions		42,464	46,910
Corporates		23,885	3,848
		87,558	67,669
Total financial investments		**104,357**	**84,586**

17.1 As at 31 December 2020 financial investments of £6 million (2019: Nil) was encumbered against borrowing of £5 million from the Bank of England under TFSME scheme (2019: Nil).

17.2 This includes investments in Sukuk of £3.3 million (2019: 3.5 million) held by the Bank.

18. Derivative financial instruments

The Bank transacts derivatives to manage and hedge its own risk and that of its customers.

The Bank uses derivatives for hedging purposes for an economic perspective in the management of its own asset and liability portfolios. This enables the Bank to mitigate the market risk, which would otherwise arise from structural imbalances.

Forward foreign exchange currency contracts are Over the Counter agreements to deliver, or take delivery of, a specified amount of an asset or financial instrument based on a specific rate applied against the underlying asset or financial instrument, at a specific date.

Derivatives are measured at their fair value, which is calculated as the present value of the future expected net contracted cash flows at market related rates as of the balance sheet date.

The fair values and notional amounts of derivative instruments are as follows:

	2020 (£ 000')	2019 (£ 000')
Notional amount	35,704	22,830
Fair value asset	616	357
Fair value liability	358	312

19. Property and equipment

2020 £ 000'	Land	Leasehold Premises (ROU)	Freehold and leasehold improvements	Property and other equipment	Furniture, fixture and fittings	Motor vehicles	Total
Cost							
As at 1 January 2020	1,050	4,806	11,036	2,014	1,952	106	20,964
Additions	-	-	19	228	20	-	267
As at 31 December 2020	**1,050**	**4,806**	**11,055**	**2,242**	**1,972**	**106**	**21,231**
Accumulated Depreciation							
As at 1 January 2020	-	2,010	7,018	1,593	1,754	106	12,481
Depreciation	-	376	402	137	56	-	971
As at 31 December 2020	**-**	**2,386**	**7,420**	**1,730**	**1,810**	**106**	**13,452**
Net book value as at 31 December 2020	**1,050**	**2,420**	**3,635**	**512**	**162**	**-**	**7,779**
Net book value as at 31 December 2019	**1,050**	**2,796**	**4,018**	**421**	**198**	**-**	**8,483**

2019 £ 000'	Land	Leasehold Premises (ROU)	Freehold and leasehold improvements	Property and other equipment	Furniture, fixture and fittings	Motor vehicles	Total
Cost							
As at 1 January 2019	1,050	-	10,785	1,838	1,922	106	15,701
Application of IFRS 16	-	4,806	-	-	-	-	4,806
Additions	-	-	251	176	30	-	457
As at 31 December 2019	**1,050**	**4,806**	**11,036**	**2,014**	**1,952**	**106**	**20,964**
Accumulated Depreciation							
As at 1 January 2019	-	-	6,631	1,491	1,687	106	9,915
Application of IFRS 16	-	1,634	-	-	-	-	1,634
Depreciation	-	376	387	102	67	-	932
As at 31 December 2019	**-**	**2,010**	**7,018**	**1,593**	**1,754**	**106**	**12,481**
Net book value as at 31 December 2019	**1,050**	**2,796**	**4,018**	**421**	**198**	**-**	**8,483**
Net book value as at 31 December 2018	**1,050**	**-**	**4,154**	**347**	**235**	**-**	**5,786**

20. Other assets

	2020 (£ 000')	2019 (£ 000')
Corporation tax	77	372
Prepayments	365	254
Receivable from Parent bank	6	7
Value added tax refundable	277	336
Customer transaction fee receivable	25	27
Other	138	74
Total other assets	**888**	**1,070**

21. Due to banks at amortised cost

	Notes		
Due to Parent bank (Habib Bank AG Zurich, Switzerland)	21.1	32,473	4,047
Due to associates (fellow subsidiaries)		2,417	2,274
Due to central bank (TFSME)	21.2	5,001	-
Other deposits		200	401
Total due to banks		**40,091**	**6,722**

21.1 This includes fiduciary deposits £26.4 million (2019: Nil) accepted by the Bank from Habib Bank AG Zurich (parent) and having maturities ranging from 3 months to 18 months.

21.2 The Bank become the member of the Bank of England's Term Funding Scheme with additional incentives for SME (TFSME). The funding under the scheme is made available for a period up to 4 years. Interest rate on TFSME is linked to BoE Base Rate, which is currently 0.1% per annum.

22. Due to customers at amortised cost

	2020 (£ 000')	2019 (£ 000')
Time deposits	407,312	358,477
Current and demand accounts	215,729	218,028
Margin accounts	93	-
Call deposits	510	508
Total due to customers	**623,644**	**577,013**

23. Accrual, deferred income and other liabilities

	Notes	2020 (£ 000')	2019 (Represented) (£ 000')
Bills payable		990	1,198
Lease Liability	23.2	2,582	2,973
Staff costs payable		709	611
Accrued expenses		575	915
Deferred income		121	130
VAT reverse charge payable to HMRC		-	636
Other		645	576
Total accrual, deferred income and other liabilities		**5,622**	**7,039**

23.1 The 2019 financial statements are re-presented due to reclassification of related assets and liabilities.

23.2 The Bank leases a number of branch and office premises. The leases typically run for a period of 8 years approximately, with an option to renew the lease after that date. Following the adoption of IFRS 16, the Bank has presented lease liabilities with the other liabilities.

The Bank also has short term lease of premises with contract terms of 12 months. The Bank has elected not to recognise right-of-use assets and lease liabilities for that lease.

Previously these leases were classified as operating leases under IAS 17.

Information about leases for which the Bank is lessee is presented below:

Right-of-use assets

Right-of-use assets relate to leased branch and office premises that are presented within property and equipment.

	2020 (£ 000')	2019 (£ 000')
Balance at 1 January	2,796	3,172
Depreciation charge for the year	(376)	(376)
Balance at 31 December	**2,420**	**2,796**

Amount recognised in profit & loss	2020 (£ 000')	2019 (£ 000')
Interest on lease liabilities	35	40
Expense related to short term lease	53	53
	88	**93**

Amount recognised in statement of cash flows	2020 (£ 000')	2019 (£ 000')
Total cash flows for leases	426	436
	426	**436**

24. Current tax liabilities

	2020 (£ 000')	2019 (£ 000')
Provision for corporation tax	103	570
Total current tax liabilities	**103**	**570**

25. Subordinated liabilities

The Parent bank, Habib Bank AG Zurich, issued a subordinated loan of £20m in 2016, providing T-2 capital to the Bank. The loan carries interest at a rate of 6-month Libor plus 125 bps per annum to be paid semi-annually.

The initial term of the loan is five years. The term of loan can be extended for one additional year on each anniversary with the mutual consent of both lender and borrower after the expiry of the initial term.

Subordinated liabilities are measured at amortised cost using the effective interest method under IFRS 9.

26. Share capital

	2020 (£ 000')	2019 (£ 000')
Called up and fully paid		
60 million authorised and fully paid ordinary shares of £1 each (2019: 60 million ordinary shares of £1 each)	60,000	60,000
Share Capital	**60,000**	**60,000**

27. Fair value loss on financial assets at fair value through other comprehensive income

	2020 (£ 000')	2019 (£ 000')
Fair value movement		
FV gain at the beginning of the year	252	(56)
FV movement during the year	117	308
FV (loss) / gain at the end of the year	369	252
Deferred tax movement		
Deferred tax liability at the beginning of the year	(48)	10
Net movement during the year	(22)	(58)
	(70)	(48)
	299	204
Net losses of FVOCI transferred due to impairment		
– Transferred on initial application of IFRS 9	44	14
– FV loss during the year	13	30
	57	44
	356	**248**

28. Contingent liabilities and commitments

The Bank enters into transactions, which exposes it to tax, legal and business risks in the ordinary course of business. Provisions are made for known liabilities, which are expected to materialise. Contingent obligations and banking commitments, which the Bank has entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities.

	2020 (£ 000')	2019 (£ 000')
Direct credit substitutes		
– Guarantees	10,032	5,868
Trade related contingent liabilities		
– Letters of credit	629	656
– Acceptances	21	36
– Confirmation on export letters of credit	24,688	6,387
Unused credit facilities	14,361	15,216

Unused credit facilities refer to commitments to make loans and revolving credits.

Commitments generally have fixed expiry dates, or other termination clauses. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash requirements. The potential credit loss is less than the total commitments since most commitments to extend credit are contingent upon customers maintaining specific standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

29. Related party disclosure

Details of transactions between the Bank and related parties are summarized below.

	2020 (£ 000')	2019 (£ 000')
Banking transactions:		
– Interest earned from Parent bank	244	364
– Interest and expenses paid to Parent bank*	2,335	1,955
– Transactions with parent bank and fellow subsidiaries**	28,675	9,878
Outstanding balance:		
– Due to Parent bank including subordinated loan**	52,536	24,145
– Due to fellow subsidiaries	2,417	2,274
– Due from related parties	6,486	5,760

* Interest and expenses represent interest of £699k (2019: £460k) charged on borrowings / fiduciary deposits and allocation of group expenses of £1,636k (2019: £1,495k).

** This includes fiduciary deposits £26.4 million (2019: Nil) accepted by the Bank from Habib Bank AG Zurich (parent) and having maturities ranging from 3 months to 18 months.

The Bank's related parties include Parent bank and fellow subsidiaries.

The transactions arose from the ordinary course of business and on the same terms and conditions as for comparable transactions with third party counterparties.

Key management personnel information is disclosed in note 9.

30. Fair value of financial instruments

30.1 Fair value measurement:

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. It is a measure as at a specific date and may be significantly different from the amount, which will actually be paid or received on maturity or settlement date. Fair values of financial assets and liabilities measured at fair value are determined on the basis of their gross exposures. The carrying amount of the financial instruments is a reasonable approximation of fair values as illustrated in the table below.

30.2 Valuation of financial assets and liabilities

Assets and liabilities carried at fair value or for which fair values are disclosed has been classified into three levels based on significance and observability of inputs to determine the fair values.

Level 1 fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets or liabilities. Products classified as level 1 predominantly comprise debt securities where observable prices are available in the market.

Level 2 This category comprises forward currency contracts, valued using external exchange rates.

Level 3 portfolios are those where the valuation technique includes input not based on observable data and the unobservable inputs have a significant effect on the instruments' valuation. Where the fair value cannot be reliably determined for an investment, the instrument is measured at cost.

The Bank had no level 3 financial instruments.

30.3 Financial instruments carried at fair value and basis of valuation

£ 000'	2020 Level 1	2020 Level 2	2020 Level 3	2020 Total
Financial investments				
– Fair value through other comprehensive income	87,558	-	-	87,558
Derivative financial instruments-assets	-	616	-	616
Total financial assets carried at fair value	**87,558**	**616**	**-**	**88,174**
Derivative financial instruments-liabilities	**-**	**358**	**-**	**358**
Total financial liabilities carried at fair value	**-**	**358**	**-**	**358**

£ 000'	2019 Level 1	2019 Level 2	2019 Level 3	2019 Total
Financial investments				
– Fair value through other comprehensive income	67,669	-	-	67,669
Derivative financial instruments-assets	-	357	-	357
Total financial assets carried at fair value	**67,669**	**357**	**-**	**68,026**
Derivative financial instruments-liabilities	**-**	**312**	**-**	**312**
Total financial liabilities carried at fair value	**-**	**312**	**-**	**312**

30.4 Financial instruments not measured at fair value

The following table sets out the fair value of financial instruments not measured at fair value and analyse them by the level in the fair value hierarchy into which each fair value measurement is categorised.

£ 000'	Level 1 2020	Level 2 2020	Level 3 2020	Total fair value 2020	Total carrying amount 2020
Assets					
Cash in hand and with central bank	79,410	-	-	79,410	79,410
Due from banks	-	-	111,857	111,857	111,857
Loans and advances to customers	-	-	424,465	424,465	455,954
Financial investments	16,235	-	-	16,235	16,799
Liabilities					
Due to banks	-	-	40,091	40,091	40,091
Due to customers	-	-	622,129	622,129	623,644
Subordinated liabilities	-	-	19,958	19,958	20,063

£ 000'	Level 1 2019	Level 2 2019	Level 3 2019	Total fair value 2019	Total carrying amount 2019
Assets					
Cash in hand and with central bank	58,964	-	-	58,964	58,964
Due from banks	-	-	98,298	98,298	98,298
Loans and advances to customers	-	-	390,606	390,606	430,233
Financial investments	16,065	-	-	16,065	16,917
Liabilities					
Due to banks	-	-	6,722	6,722	6,722
Due to customers	-	-	575,188	575,188	577,013
Subordinated liabilities	-	-	19,571	19,571	20,098

The fair value of cash in hand and with central bank, due from banks and due to banks approximate to their carrying amount due to their short-dated nature of less than 1-year maturity.

The fair value of loans and advances to customers, due to customers and subordinated liabilities is estimated using valuation models, such as discounted cash flow techniques. Inputs into the valuation techniques include interest rates and outstanding maturities.

The fair value of other financial instruments is estimated using valuation models, such as discounted cash flow techniques. Input into the valuation techniques includes expected lifetime credit losses, interest rates and outstanding maturities.

31. Risk management

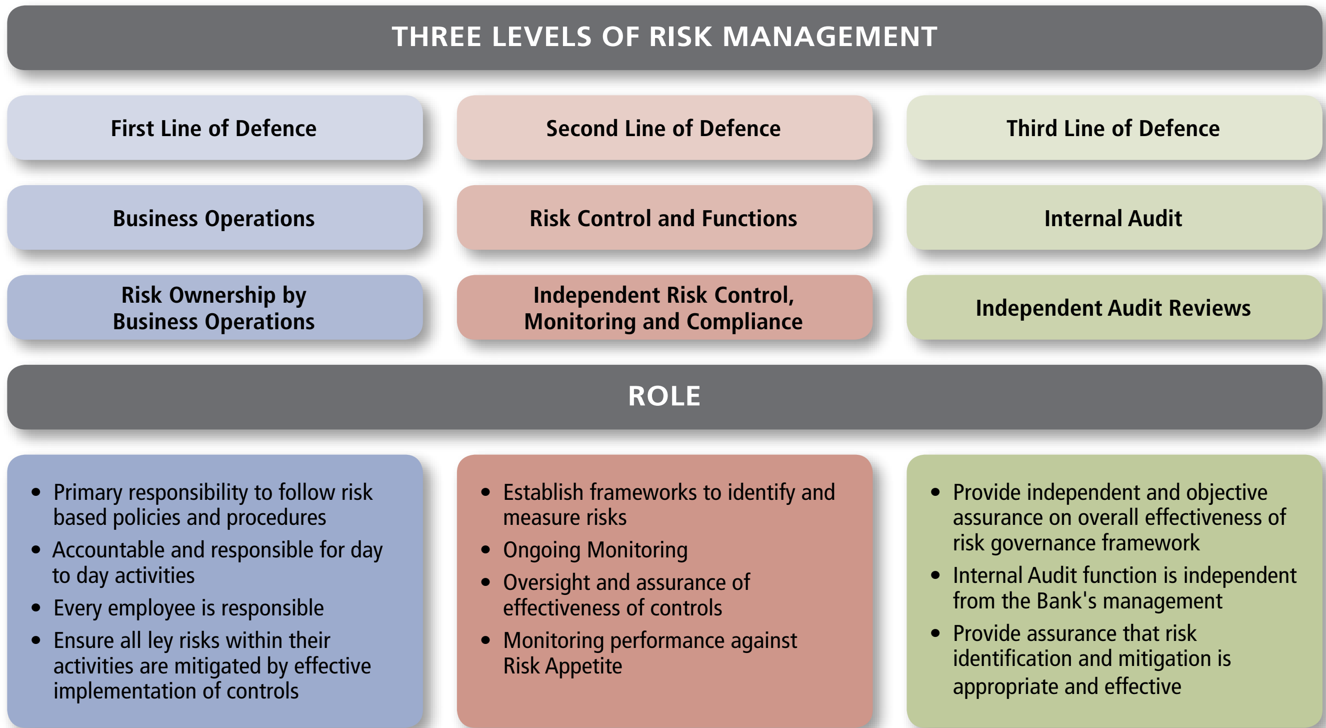
The Bank has an overall risk management framework set out in line with its risk appetite, documented within a set of risk management policies approved by the Board. Risk appetite defines the types and amounts of risk that the Bank is willing to take in pursuit of its business strategy. This is reviewed regularly and provides qualitative statements and quantitative measures to assist with the monitoring of various risk types. This process is underpinned by disclosure of risk exposures to Board, its committees and the senior management.

The Bank's approach to Risk Management is built on the principle of low to medium risk appetite and Investment return horizon, which is medium to long term. In order to achieve this, the Bank offers conventional products where the focus is on personalised customer service.

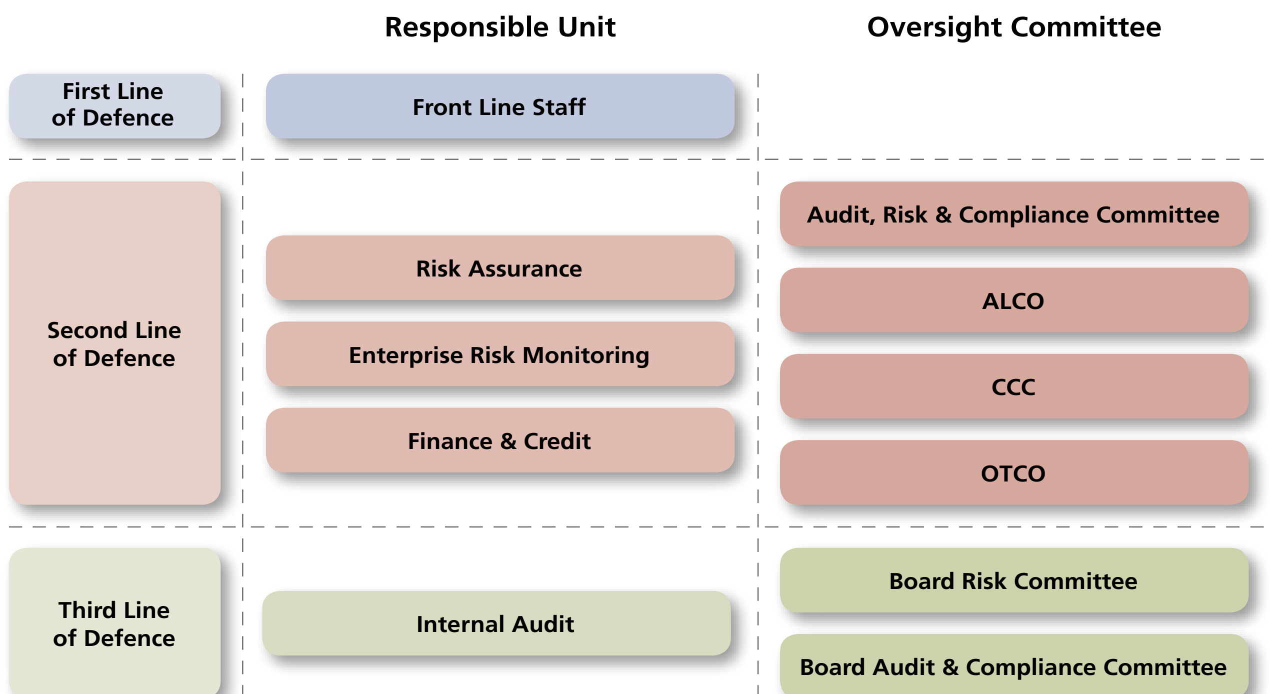
The Bank maintains an internal controls system, with clear responsibilities for risk management, applying governance model, which enables oversight and management of risks. These specific responsibilities include:

- Review and determine the risk appetite of the Bank;
- Identify and evaluate the principal risks to the Bank's Business model and the achievement of its strategic objectives, including risks that could threaten its capital or liquidity;
- Review of the risk management and internal control systems and satisfy itself that they are functioning effectively, and corrective action is being taken where necessary;
- Capital, liquidity and earnings are protected by the effective controlling of the risk exposures across all material risk types and businesses;
- Ensure that an appropriate risk culture is instilled in the Bank; and
- A strong ethical and risk culture is maintained so that risk awareness is embedded into all activities.

For smooth running and effective risk / threat identification and mitigation, the Bank operates on the 3 lines of Defence model.



The BRC provides oversight to the overall effectiveness of enterprise risk management framework.
Three Lines of Defence Oversight Process:



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31.1 Board Committees

The Board of Directors has established Committees of the Board for effective oversight of business strategy and key risks. To implement an effective governance, process the Board established "Board Risk Committee" (BRC) and "Board Audit and Compliance Committee" (BACC).

The Board Risk Committee (BRC) oversees and challenges the risk management function to ensure that governance arrangements, risk framework and systems and controls are evaluated and managed properly. BRC periodically review the risk framework to evaluate its adequacy and appropriateness under the prevailing business environment and in light of major changes in internal or external factors. It provides assurance on the Bank-wide risk framework and monitors the overall risk profile of bank through effective control processes. BRC annually review the Risk Appetite Statement and consider the adequacy of risk limits and returns.

The independent internal audit function reports into BACC and conduct reviews of all key risk areas including the risk management framework. Reports are presented to BACC and the Board.

31.2 Management responsibilities

At an operational level the Risk Management Framework is managed through a management committee structure with delegated authorities from the Board. The Executive Committee presides over the committees and is responsible for implementing the Bank's strategic objectives and managing the business with adequate controls within the risk appetite of the Bank.

The management of the Bank through committee structure allows for Enterprise-Wide Risk Management through the consideration of different aspects and challenge at decision-making levels. Significant and relevant decisions and issues at other committees are escalated to EXCO for information and consideration as appropriate. This structure ensures that management of the Bank's operations, strategic decision-making and risk management are undertaken on a consultative basis at committee level by experienced functional and business personnel.

The ALCO is the committee responsible to review and recommend to the EXCO the capital and liquidity related matters. The EXCO reviews and further recommend the same to the BRC and Board for its consideration, review and approval.

31.3 Credit risk

Credit Risk is defined as loss of principal or a loss of a financial reward stemming from a borrower's failure to repay a loan or otherwise meet a contractual obligation resulting in financial loss to the Bank. It is also measured in terms of credit losses or provisions charged to the profit and loss account. Qualitative information also used to assess issues related to the effectiveness of the risk appetite.

The Bank manages its credit risk through documented Credit Risk Management Framework ("CRMF"), which is part of the overall Risk management framework. CRMF serves as a collection of tools, processes and methodologies that support the Bank in identifying, assessing, monitoring and controlling the credit risk.

The CRMF also provides a sound basis for more informed risk-based decision-making across the business areas. The CRMF includes the credit risk appetite, which defines the Bank's target customer segment, industries and

products and risk acceptance criteria. CRMF also reflects regulatory requirements and guidelines in the UK while also referencing the overall credit risk framework and guidelines of the Group.

Through CRMF the Board ensure that the Bank has a clear and measurable statement of its credit risk appetite against which the strategy to achieve the credit related aspects of its business plan can be actively assessed. In order to measure its achievements against this goal, the Board is provided with robust, well calibrated and sufficiently granular management information so that they can provide an effective challenge to management's actions.

31.4 IFRS 9 Implementation and Model Validation

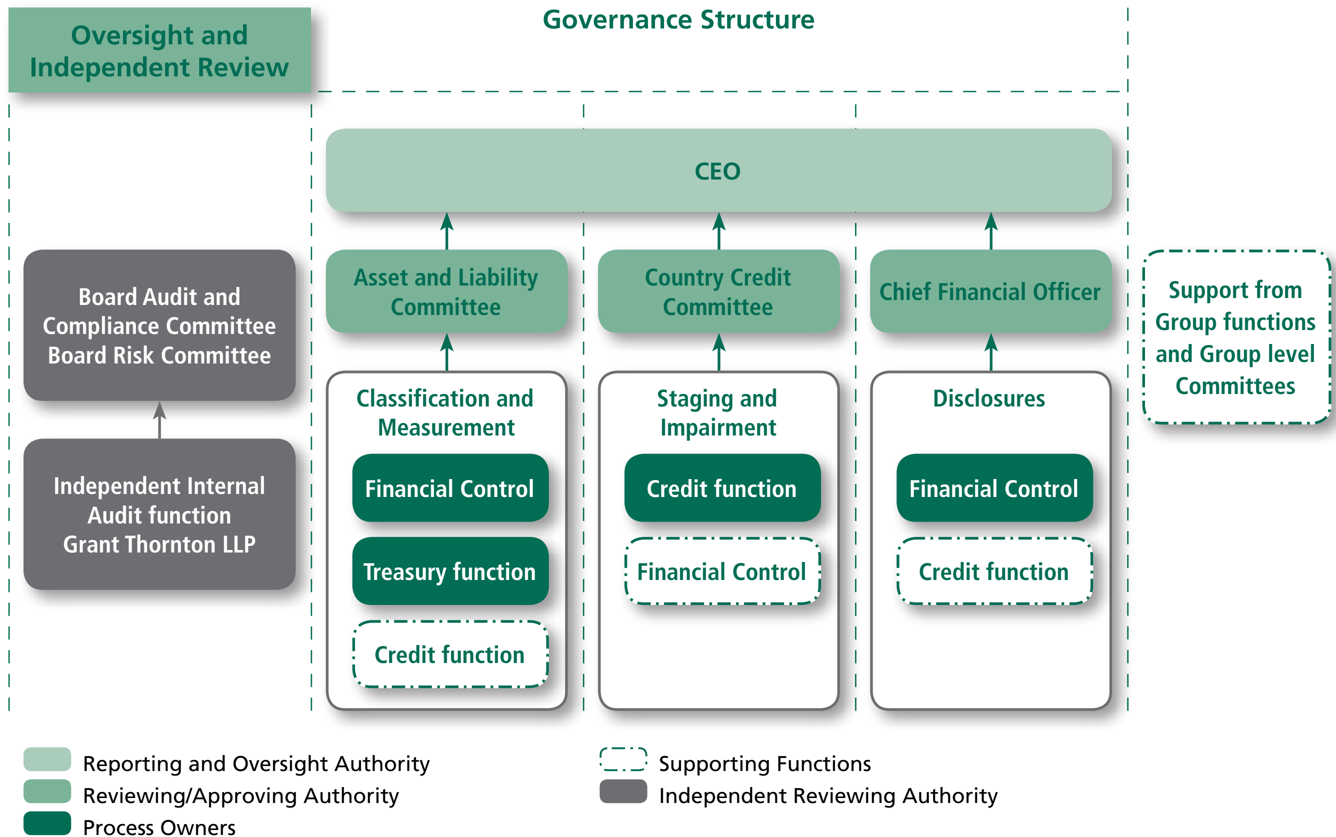
The Bank adopted IFRS 9 'Financial Instruments' by implementing suitably developed models with the assistance of external consultants. The Bank relevant credit processes and impairment requirements which relates to model and data governance, credit impairment and value adjustments were tailored to align with the requirements of IFRS9. Details are explained in Notes 5.5.3 above. In this section the Bank has provided details related to governance and risk management process related to credit risk management and ECL.

The Bank has followed the approach in designing ECL methodologies, which are commensurate with its size, complexity, structure, economic significance and profile of exposure. The approach taken is considered proportionate in the context of the size of the Bank within the UK financial market, its relative lack of complexity as well as minimal volatility in its credit losses since the change in its lending model from 2013, which is mainly geared towards, real estate lending secured by residential and commercial income generating properties.

The Bank established principles for ongoing IFRS 9 governance to ensure effective oversight of IFRS 9 processes. IFRS 9 governance structure incorporates Credit, Risk and Finance departments as central support functions for each component of IFRS 9, defines clear process owners and reviewing functions and utilises the three lines of defence to ensure an effective framework. The Group IFRS Central Team is responsible for maintaining and updating ECL models in consultation with the Bank's Country Credit Committee and ALCO with final approval from the BRC. The Central Team also produces a monthly Quality Report, which analyses reasons for variances from the previous month for the ECL.

Governance Structure outlined below are the three lines of defence for the four key IFRS 9 processes, classification and measurement, staging, impairment and disclosures.

- The process owners i.e., Credit, Financial Control and Treasury form the first line of defence
- The reviewing/approving functions i.e., Chief Executive Officer, Chief Financial Officer, Head of Credit, Country Credit Committee and Country Asset and Liability Committee forms the second line of defence with support from Group Central IFRS 9 Team
- The independent review functions i.e., Internal Audit the Board Risk Committee and the Board Audit and Compliance Committee forms the third line of defence



The Bank has also put in place appropriate control to cover credit risk model governance risk. The objective was to set out the governance for the development, validation / review, deployment and maintenance of the credit risk related models. The implemented controls put in place framework for governance along the different stages of the model life cycle.

The purpose of these controls is to set out in particular the principles and requirements for effective governance of the Bank's Expected Credit Loss (ECL) models and methodologies used for estimating the respective risk components. The main statistical models in scope of these controls include the following:

- credit risk rating model for rating of obligors belonging to the Corporate / SME portfolios
- probability of default ("PD") models (and /or methodologies)
- loss given default ("LGD") models (and /or methodologies)
- exposure at default ("EAD") models (and /or methodologies)
- credit conversion factor ("CCF") models (and /or methodologies), and
- macroeconomic models.

For the purpose calculating ECL Bank has developed models for types of financial assets

- Customer Lending – separate models for property lending and other lending
- Investments and Financial Institutions

31.5 Probability of Default – model methodology

The Bank collects performance and default information about its credit risk exposures analysed by type of product and borrower or region as well as by credit risk grading. For some portfolios, information from external credit reference agencies is also used.

The Bank employs statistical models to analyse the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

Probability of Default is one of the three risk components needed to estimate ECL under IFRS 9. PD is defined as probability that a borrower will be unable to meet his/her debt obligations over a stipulated time period. IFRS 9 requires PD to be a Point in Time ("PiT") as opposed to a Through the Cycle (TTC) estimate, implying that the PD associated with each internal rating grade should reflect current economic conditions rather than the long-term average.

For ECL calculation, Bank segregates 'Loans and advances to customers' in two categories i.e., lending secured against property and other lending.

The PD was computed for the Property Lending portfolio using flow rate analysis, where migration matrices were built to track the historical performance of customers into default status over a twelve-month performance period in order to arrive at the default rate.

While developing the model, an 'ever default' definition was employed in order to capture all accounts obtaining default status over a twelve-month period, regardless of whether the customer ceased to be in default at the end of the period. The default rate obtained from this calculation is considered to be a point-in-time estimate of the PD.

31.6 Loss Given Default – model methodology

The LGD for the Other Lending portfolio is computed at an account level and leverages the Basel F-IRB LGD. The main drivers of Basel F-IRB LGD framework are seniority of the facility, facility type (secured / unsecured), security (collateral type) and security coverage of the facility (level of collateralization). The LGD computed using the Basel LGD framework is adjusted using a beta-regression. The methodology utilises macroeconomic data and facility level collateral coverage to predict LGD estimates based on Basel LGD estimates. The adjustment is performed to reflect potential dependency on macroeconomic factors and to remove the element of conservatism (floors) included in the Basel LGD estimates.

As the Bank's Property Lending exposures essentially follow the 'Held to Collect' business model, a workout LGD approach to measurement was adopted to estimate potential losses. This approach involves use of contracts which have defaulted over a period of time to calculate internal recovery and loss cash flows to compute the 'Net Present Value' (NPV) of the loss as percentage of the EAD.

The final loss on the exposure was arrived at by adding the loss estimates for the cure, restructure and recovery nodes, weighted by the probability of the account flowing into either of the three nodes. This was divided by the Exposure at Default to derive the LGD %. The final LGD takes into account the cost of recovery and also includes a discount rate to discount the recovered amounts to the point of default.

31.7 Exposure at Default

For amortizing facilities, cash flows are used to determine the principal outstanding as of a given reporting date, while for non-amortizing facilities, such as bonds where only coupon payments are made periodically (with the principal falling due on the bond's maturity date), the principal outstanding will remain unchanged on each reporting date. Since the Bank has a low amortising portfolio 100% EAD as on the reporting date is representative of the expected exposure at default.

31.8 Determining whether credit risk has increased significantly (significate increase in credit risk – SICR)

The Bank assesses whether credit risk has increased significantly since initial recognition at each reporting date. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower, and the geographical region. What is considered significant differs for different types of lending, in particular between wholesale and retail. As a general indicator, credit risk of a particular exposure is deemed to have increased significantly since initial recognition when triggered on the Bank's quantitative modelling.

The credit risk may also be deemed to have increased significantly since initial recognition based on qualitative factors linked to the Bank's credit risk management processes that may not otherwise be fully reflected in its quantitative analysis on a timely basis. This will be the case for exposures that meet certain heightened risk criteria, such as placement on an early warning indicator or watch list. Such qualitative factors are based on its expert judgement and relevant historical experiences.

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- the criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- the criteria do not align with the point in time when an asset becomes 30 days past due;
- the average time between the identification of a significant increase in credit risk and default appears reasonable;
- exposures are not generally transferred directly from 12-month ECL measurement to credit- impaired; and
- there is no unwarranted volatility in loss allowance from transfers between 12-month PD (Stage 1) and lifetime PD (Stage 2).

As a backstop, the Bank considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

31.9 Curing policy

If there is evidence that there is no longer a significant increase in credit risk relative to initial recognition, then the loss allowance on an instrument returns to being measured as 12-month ECL. Some qualitative indicators of an increase in credit risk, such as delinquency or forbearance, may be indicative of an increased risk of default that persists after the indicator itself has ceased to exist. In these cases, the Bank determines a probation period during which the financial asset is required to demonstrate good behaviour to provide evidence that its credit risk has declined sufficiently.

Under IFRS 9, exposures transferred into Stage 2 and Stage 3 are deemed to be significantly riskier than those falling within Stage 1. Hence the Bank seeks objective evidence of an improvement in customer credit worthiness prior to relegating a Stage 2 or Stage 3 account back to Stage 1.

The Bank follows a three-month time period or payment of three consecutive instalments for movements from Stage 3 to Stage 2 and three-month time period or payment of three consecutive instalments for movement from Stage 2 to Stage 1, implying that once the triggers for movement to Stage 2 or Stage 3 cease to exist, the exposure would still remain in Stage 2/Stage 3 for the duration of the cool-off period. Once the cool-off period is over, the exposure may be transferred out of Stage 2/Stage 3. The Bank may choose to adopt a stricter cool off period in line with updates to its credit policy.

Movement	Time Period	Instalments
Stage 2 to Stage 1	3 months	3
Stage 3 to Stage 2	3 months	3

31.10 Definition of default

The classification is consistent with the 90 DPD definition of default adopted by the Bank for the portfolio and the 30 & 90 DPD rebuttable presumptions provided under IFRS 9 for classification of financial instruments into Stage 2 and Stage 3.

In order to maintain a default definition consistent with both regulatory guidelines and the Bank's business practices for management of credit risk, an exposure has been considered non-performing if:

- The account is 90 or more days overdue on contractual payments; or
- Based on observed payment delays or early warning indicators detected as a result of the Country Credit function's portfolio monitoring activities, the account has been tagged as Default. The management taken such decision when the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held). Further, it is becoming probable that the Bank will restructure the account as a result of bankruptcy due to borrower's inability to pay its credit obligations.

While developing the model, an 'ever default' definition has been employed by the Bank in order to capture all accounts obtaining default status over a twelve-month period, regardless of whether the account ceases to be in default at the end of the period.

31.11 Impairment

IFRS 9 Impairment applies to financial instruments that are not measured at fair value through profit and loss (FVTPL). Financial assets falling within the scope of impairment are provided for by calculating their Expected Credit Loss (ECL). This requires considerable judgement regarding how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. ECL is an estimate of present value of cash shortfalls over the life of the financial instrument and is computed as a product of probability of default (PD), loss given default (LGD) and exposure at default (EAD). The present value of cash shortfalls is calculated by taking into account the time value of money and forward-looking information.

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluation of a range of possible outcomes that incorporates forecasts of future economic conditions. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions.

31.12 Incorporation of forward-looking information

The estimation and application of forward-looking information requires significant judgement and are subject to appropriate internal governance and scrutiny. The Bank incorporates forward-looking information into both the assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and the measurement of ECL.

The macroeconomic model built for Lending products contains the following exogenous variables capable of explaining the Property Lending default rates:

- Unemployment Rate
- Government debt to GDP Ratio

In order to comply with the requirements of IFRS 9, the ECL estimates should adjusted through updating selected macroeconomic variables to bring the Point in Time PD estimates for each segment to forward looking.

As a result of pandemic outbreak in March 2020 the UK Government provided unprecedented support to the economy through various schemes such as furlough scheme, government back loans to businesses and individuals, reduction in VAT, stamp duty and business rates, prohibiting landlords from evicting tenants due to non-payment of rents, introduction of moratorium and tailored support under regulatory guidance. As a consequence, the Government had to borrow significant amount, which resulted in increase in Government Debt-to-GDP ratio.

Although, the government support was able to support millions of jobs the impact of the pandemic was more far reaching in particular on hospitality and retail sector due to continuous lockdown of the economy. Unemployment rate, which was at it's all time low in 2019 started increasing as businesses were forced to lay-off employees due to near zero activity.

31.13 Post Model Adjustment (PMA)

The Bank analysed the impact of change in PD by updating the macroeconomic variable against the behaviour of the portfolio during 2020. It was observed that the outcome was not consistent as quality of the portfolio remained steady since the start of the pandemic demonstrating no signs of significant increase in credit risk. Overall performance of the portfolio also depicted improvement from start of the pandemic as number of customers who requested for the first moratorium in April 2020 significantly reduced at year end, which also demonstrated no evidence of SICR at a portfolio level.

The Country Credit Committee (CCC) noted that although there was a significant deterioration in macroeconomic variables, which may become more adverse in 2021, the performance of the portfolio is not likely to be impacted as demonstrated by the behaviour seen during the year when the impact of the pandemic was worst. The CCC also considered the stress impact on the portfolio as a consequence of decrease in property prices and deterioration of borrowers cashflows, which was assessed through number of rapid portfolio reviews carried out during the year.

The CCC took comfort from low LTV and already stressed Debt Service ratio, which represents conservative credit risk management policy of the Bank.

The CCC noted that IFRS 9 ECL models were prepared by the Bank in 2017. A substantial degree of uncertainty exists regarding the cyclical behaviour of the ECL model in IFRS 9 and its impact on banks' behaviour. Therefore, information on the cyclical behaviour of the ECL model and how banks may adjust their behaviour in response to pandemics for credit losses is still scarce. The Bank's current ECL model were prepared on data set, which has not seen the impact of economic downturn as a result of which the outcome has not been able to absorb such large variation in macroeconomic variables. Accordingly, the CCC applied the post model adjustments on the ECL value driven from the model by adjusting the PD and LGD values, to arrive at ECL values, which is management estimate provided appropriate expected loss coverage.

The estimation made by the Bank was discussed by the Board and considered appropriate keeping in view the performance of the portfolio observed during pandemic and prospect of improvement in overall economic conditions in 2021.

31.14 Modified financial assets and forbearance

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer.

When the terms of a financial asset are modified and the modification does not result in de-recognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

When modification results in de-recognition, a new loan is recognised and allocated to Stage 1 (assuming it is not credit-impaired at that time).

The Bank renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities) to maximise collection opportunities and minimise the risk of default. Under the Bank's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. All such situations are discussed and approved as per the credit sanction process by the Country Credit Committee. The Bank accommodates the forbearance situations by deferring the principal repayments, providing an Interest moratorium, converting the overdraft into an amortising loan, or by using a letter of credit to finance trade finance rather than an Overdraft.

All customers assessed under a forbearance process with revised repayment terms are kept under a close monitoring process. Once the circumstances leading to a forbearance process related to a loan no longer exists, and customers demonstrate continuous repayment history, the loan is no longer considered as forborne.

The Bank was proactive in taking the required measures to manage the extraordinary situation as a result of outbreak of the Covid 19. Some of the key steps taken by the Bank are set out below:

- Increase in frequency of credit committee meetings to review the portfolio
- Enhanced evaluation of new proposals and renewal cases
- Rapid Portfolio Reviews (RPR) to identify impact of COVID-19 on industry segments and analyse the Bank's position to identify customers for enhanced monitoring
- Review and approval of loan moratorium application on a case by case through customer engagement
- Assessment of expected increase in NPL and ECL through RPR
- Enhanced reporting to BRC in monthly meetings

A comprehensive risk assessment process was followed by the Bank in evaluating the moratorium need of the customers, which included discussion with the customers, understanding their cash flow and liquidity needs and making available the support they needed to continue their businesses. In accordance with the regulatory guidance received throughout 2020 the Bank provided the required financial support to its customers through moratorium and tailored support.

Loans and advances to customers at amortised cost £ 000'	2020 Stage 1	2020 Stage 2	2020 Stage 3	2020 Total
Moratorium process	2,724	-	3,179	5,903
Tailored support	21,216	4,121	794	26,131
Total	**23,940**	**4,121**	**3,973**	**32,034**

During the year, loans amounting to £2.99 million including those under tailored support (2019: £3.1 million) were considered as forborne of which £0.3 million (2019: £0.3 million) were classified as impaired. A provision of £3k (2019: £16k) was made against forborne loans.

31.15 Loss allowance

The following tables show reconciliations from the opening to the closing balances of the loss allowance by class of financial instrument.

Amount in £ 000'

Due from banks at amortised cost	2020 Stage 1	2020 Stage 2	2020 Stage 3	2020 Total	2019 Total
Balances at the beginning of the year	336	-	-	**336**	137
New provisions	257	-	-	**257**	74
Increased provisions	7	-	-	**7**	163
Recovered / settled / reduced	(67)	-	-	**(67)**	(39)
Net measurement of loss allowance	197	-	-	**197**	198
Other movement	(1)	-	-	**(1)**	1
Balances at the closing of the year	**532**	**-**	**-**	**532**	**336**

Loans and advances to customers at amortised cost	2020 Stage 1	2020 Stage 2	2020 Stage 3	Amount in £ 000' 2020 Total	2019 Total
Balances at the beginning of the year	1,233	193	3,612	5,038	5,583
New provisions	145	-	-	145	215
Increased provisions	10	50	911	971	783
Recovered / settled / reduced	(59)	(90)	(591)	(740)	(1,532)
Net measurement of loss allowance	96	(40)	320	376	(534)
Transferred to 12 month's ECL Stage 1	13	(13)	-	-	-
Transferred to lifetime ECL stage 2 Credit not impaired	(3)	3	-	-	-
Transferred to lifetime ECL stage 3 Credit impaired	(10)	(65)	75	-	-
Uncollectable written off / other	-	-	1	1	(11)
Balances at the closing of the year	**1,329**	**78**	**4,008**	**5,415**	**5,038**

The contractual amounts outstanding on financial assets that were written off during the year ended 31 December 2020 are subject to enforcement activity.

Financial investments	2020 Stage 1	2020 Stage 2	2020 Stage 3	Amount in £ 000' 2020 TOTAL	2019 TOTAL
Balances at the beginning of the year	1	-	-	**1**	2
New provisions	-	-	-	**-**	2
Increased provisions	15	-	-	**15**	31
Net measurement of loss allowance	15	-	-	**15**	33
Other movement	(2)	-	-	**(2)**	(4)
Impairment of FVOCI investment shown under OCI	(13)	-	-	**(13)**	(30)
Balances at the closing of the year	**1**	**-**	**-**	**1**	**1**

The following table provides reconciliation between:

- Amounts shown in above tables reconciling of opening and closing balances of loss allowance per class of financial instrument; and
- The impairment losses on financial instruments' line item in the statement of profit and loss.

Amount in £ 000'

	Due from banks at amortised cost	Loans and advances to customers at amortised cost	Financial investments	Total
New provisions	257	145	-	402
Increased provisions	7	971	15	993
Uncollectable recovered / settled	(67)	(740)	-	(807)
Total – 2020	**197**	**376**	**15**	**588**
Total – 2019	**198**	**(534)**	**33**	**(303)**

31.16 Credit quality analysis

The following table set out information about the credit quality of financial assets measured at amortised cost and FVOCI debt. Unless specifically identified, for financial assets, the amounts in the table represent the gross carrying amounts.

Amount in £ 000'

	2020 Stage 1	2020 Stage 2	2020 Stage 3	2020 Total	2019 Total
Cash in hand and with central bank	79,410	-	-	79,410	58,964
Due from banks	112,389	-	-	112,389	98,634
Loans and advances to customers	441,858	4,791	14,720	461,369	435,271
Financial investments – amortised cost	16,800	-	-	16,800	16,919
Financial investments – FVOCI debt instruments	87,558	-	-	87,558	67,668
	104,358	-	-	104,358	84,587
	738,015	4,791	14,720	757,526	677,456
Loss allowance	(1,857)	(83)	(4,008)	(5,948)	(5,375)
	736,158	**4,708**	**10,712**	**751,578**	**672,081**

The following table provide information about the credit quality of financial assets outstanding as at the balance sheet date in terms of regular, past due and impaired.

Amount in £ 000'

2020	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Total
Current & past due up to 1 month	79,410	112,389	450,769	104,358	616	747,542
Past due 1 to 3 months	-	-	1,570	-	-	1,570
Past due over 3 months	-	-	9,030	-	-	9,030
Gross exposure	79,410	112,389	461,369	104,358	616	758,142
Less: impairment	-	(532)	(5,415)	(1)	-	(5,948)
Net exposure	**79,410**	**111,857**	**455,954**	**104,357**	**616**	**752,194**

Amount in £ 000'

2019	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Total
Current & past due up to 1 month	58,964	98,634	429,744	84,587	357	672,286
Past due 1 to 3 months	-	-	3,173	-	-	3,173
Past due over 3 months	-	-	2,354	-	-	2,354
Gross exposure	58,964	98,634	435,271	84,587	357	677,813
Less: impairment	-	(336)	(5,038)	(1)	-	(5,375)
Net exposure	**58,964**	**98,298**	**430,233**	**84,586**	**357**	**672,438**

The table below sets out information about the overdue status of loans and advances to customers in Stage 1, 2 & 3:

Amount in £ 000'

Age bracket	2020 Stage 1	2020 Stage 2	2020 Stage 3	2020 Total	2019 Total
< 30 days	29,835	1	6	29,842	24,372
> 30 days to 60 days	-	321	30	351	2,562
> 60 days to 90 days	-	-	1,219	1,219	611
> 90 days to 180 days	-	-	2,198	2,198	654
> 180 days	50	-	6,782	6,832	1,700
Total overdue	29,885	322	10,235	40,442	29,899
Not overdue	411,973	4,469	4,485	420,927	405,372
Gross loans and advances to customers	441,858	4,791	14,720	461,369	435,271
Less: Impairment allowance	(1,324)	(83)	(4,008)	(5,415)	(5,038)
Net loans and advances to customers	**440,534**	**4,708**	**10,712**	**455,954**	**430,233**

31.17 Credit Risk Ratings

For the purpose of credit risk ratings, the Bank segregates its loans and advances portfolio into two categories namely, Property Sector lending and Other Lending (primarily comprising of commercial lending). Property sector lending covers major portion of the total lending portfolio. The Bank follows a program-based lending approach for property sector lending with clearly defined Risk Acceptance Criteria (RAC) for this segment rather than a credit risk rating methodology.

The Bank recognises loans and advances as past due when the customer does not meet its contractual payment obligations.

The Bank regards a loan and advance or a debt security as impaired if there is objective evidence that a loss event has an impact on future estimated cash flows from the asset.

The following table sets out the credit quality of non-trading Financial assets split by external rating, where applicable:

Amount in £ 000'

2020	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
AAA to AA-	78,863	21,589	-	53,165	-	-	153,617
A+ to A-	-	11,144	-	51,171	132	12,682	75,129
BBB+ to B-	-	61,306	-	-	98	17,295	78,699
Unrated	547	17,818	455,954	21	386	55,458	530,184
	79,410	**111,857**	**455,954**	**104,357**	**616**	**85,435**	**837,629**

Amount in £ 000'

2019	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
AAA to AA-	58,203	84	-	52,302	-	-	110,589
A+ to A-	-	11,576	-	32,284	4	2,711	46,575
BBB+ to B-	-	77,765	-	-	5	9,215	86,985
Unrated	761	8,873	430,233	-	348	39,067	479,282
	58,964	**98,298**	**430,233**	**84,586**	**357**	**50,993**	**723,431**

The above numbers represent the carrying values of the financial assets and firm commitments.

The following table shows as analysis of counterparty credit exposures arising from derivative transactions. Derivative transactions of the Bank are fully collateralised by cash.

Amount in £ 000'

£ 000'	Total Notional amount	Total Fair value	Over-the-counter Other bilateral collateralized Notional amount	Fair value
2020				
Derivative assets	35,717	616	35,717	616
Derivative liabilities	35,076	(358)	35,076	(358)
2019				
Derivative assets	22,570	357	22,570	357
Derivative liabilities	22,492	(312)	22,492	(312)

31.18 Concentration of Risk

Concentration arises when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar features that would cause their ability to meet contractual obligations to be affected by changes in economic, political or other conditions. The Country Credit Committee primarily manages concentration risk. The Bank Assets and Liabilities Committee also monitor credit concentration. All material exposures are reported to the Board Risk Committee, which escalates material concerns to Board of Directors.

Concentration of financial assets and credit related contingent liabilities:

Amount in £ 000'

2020	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
Supernationals	78,863	-	-	35,991	-	-	114,854
Financial Institutions	-	111,857	-	44,480	230	50,303	206,870
Industrial & commercial	-	-	394,940	23,886	386	32,156	451,368
Individual	-	-	61,014	-	-	2,976	63,990
Other	547	-	-	-	-	-	547
	79,410	**111,857**	**455,954**	**104,357**	**616**	**85,435**	**837,629**

2019	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
							Amount in £ 000'
Supernationals	58,203	-	-	33,828	-	-	92,031
Financial Institutions	-	98,298	-	46,910	9	18,334	163,551
Industrial & commercial	-	-	370,704	3,848	348	32,292	407,192
Individual	-	-	59,529	-	-	367	59,896
Other	761	-	-	-	-	-	761
	58,964	**98,298**	**430,233**	**84,586**	**357**	**50,993**	**723,431**

Supernational include investment made by the Bank in high rated bonds issued by sovereigns and multilateral development banks.

Geographical concentration of financial assets and credit related contingent liabilities:

2020	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
							Amount in £ 000'
UK	79,410	57,093	400,887	28,017	387	36,133	**601,927**
Europe excl UK	-	1,221	17,344	36,440	229	17,722	**72,956**
Asia	-	34,661	4,442	17,064	-	24,014	**80,181**
North America	-	36	29,439	3,109	-	-	**32,584**
Africa	-	10,106	3,842	-	-	7,566	**21,514**
USA	-	6,881	-	14,468	-	-	**21,349**
Australia	-	1,859	-	5,259	-	-	**7,118**
	79,410	**111,857**	**455,954**	**104,357**	**616**	**85,435**	**837,629**

2019	Cash and balances with central bank	Due from banks	Loans and advances to customers	Financial investments	Derivatives	Contingent liabilities and commitments	Total
							Amount in £ 000'
UK	58,964	63,058	385,136	12,447	353	44,817	**564,775**
Europe excl UK	-	442	10,428	42,852	4	3,037	**56,763**
Asia	-	16,376	4,713	14,099	-	21	**35,209**
North America	-	122	25,481	3,002	-	-	**28,605**
Africa	-	17,084	4,475	-	-	3,118	**24,677**
USA	-	1,145	-	6,936	-	-	**8,081**
Australia	-	71	-	5,250	-	-	**5,321**
	58,964	**98,298**	**430,233**	**84,586**	**357**	**50,993**	**723,431**

The Bank held cash and cash equivalents of £78.8 million as at 31 December 2020 (2019: £58.2 million) with central bank that is rated at least AA- to AA+ as per approved external credit rating agencies.

31.19 Collateral Management

Collateral Risk is mitigated through the use of readily marketable collateral, avoidance of collateral with high volatility and use of haircuts as per approved Bank's policy.

Collateral values are assessed by professional valuers. The Bank uses a panel of valuers selected through a robust due diligence process. Residential or commercial collateral values used by the Bank are based on vacant possession values, which provides fair degree of conservativeness to the values used for calculating LTV. The Bank generally performs valuation of properties every five years.

Key threat arising along with controls & mitigations in place are tabulated below:

Collateral Risk	Controls & Mitigation in Place
Risk arising from reduction in collateral values	• Generally acceptable collateral – Cash, Residential & Commercial Property, Bank Guarantees, Shares & Bonds & life insurance with surrender value. • Lien is marked against cash taken as collateral • Charge is recorded in Bank's name in land registry relating to residential and commercial properties taken as collateral. • Other collateral like Bank Debenture, Stocks, Receivables, Personal Guarantees also available but discounted for lending and provision decisions. • Well defined haircuts for all collateral with Property haircuts arrived at on the basis of type of property, location and market conditions • Property Stress tests conducted every six months
Risk arising from inadequate perfection of Security for Customer Borrowing	• Credit Administration unit centralised • Standardisation of documents and processes for Risk mitigation • Duly reviewed & approved panel of solicitors & valuation firms

The Bank accepts collateral subject to legal review and appropriate documentation in accordance with the Credit Risk Management Policy. The Credit Department keeps a comprehensive record of collateral received and is responsible for regular updates to the valuation of the underlying collateral. The documentation entered into with the obligor specifies the Bank's rights and ability to liquidate the collateral, if required. The Country Credit Committee is responsible for decisions regarding liquidation or appropriation of collateral based on recommendations from the Head of Credit and advice from the Legal Department.

The carrying amount of financial assets recorded in the balance sheet, net of any allowances for losses, represents the Bank's maximum exposure to credit risk without taking account of any collateral obtained. The fair value of collateral and security enhancements held against loans or advances to customers is shown below:

Collateral Type	2020 Collateral Value	2020 Advances	2019 Collateral Value	2019 Advances
				Amount in £ 000'
Commercial real estate	703,311	338,898	618,715	301,217
Residential real estate	210,906	99,481	227,686	109,949
Cash collateral	34,718	18,545	29,021	20,991
Other collateral	-	-	-	-
Guarantees	-	-	-	-
Unsecured	-	4,445	-	3,114
Total	**948,935**	**461,369**	**875,422**	**435,271**

The Bank doesn't hold collateral against any of the financial asset other than loans and advances to the customers.

The following table stratifies credit exposures from mortgage loans and advances to customers by ranges of loan-to-value (LTV) ratio. LTV is calculated as the ratio of gross amount of the loan – to the value of the collateral. The value of the collateral for mortgage loans is based on the collateral value at origination updated based on changes in valuation. For credit-impaired loans the value of collateral is based on the most recent appraisals and taking into account any reduction in values as a result of forced sales.

Loans and Advances

Amount in £ 000'

LTV Bracket	2020 Stage 1	2020 Stage 2	2020 Stage 3	2020 Total	2019 Stage 1	2019 Stage 2	2019 Stage 3	2019 Total
Less than 50%	134,120	4,625	3,741	142,486	90,210	7,863	2,251	100,324
51-70%	295,139	0	5,834	300,973	274,295	-	-	274,295
71-90%	5,054	166	461	5,681	39,381	-	464	39,845
91-100%	2,129	0	0	2,129	1,957	182	-	2,139
More than 100%	5,416	0	4,684	10,100	10,853	-	7,815	18,668
Grand Total	**441,858**	**4,791**	**14,720**	**461,369**	**416,696**	**8,045**	**10,530**	**435,271**
Collateral	**919,376**	**7,700**	**21,859**	**948,935**	**842,086**	**21,568**	**11,768**	**875,422**

31.20 Market risk

Market risk refers to the risk to an institution resulting from movements in market prices, in particular, changes in interest rates, foreign exchange rates, and equity and commodity prices.

Market risk is the potential for loss of earnings or economic value due to adverse changes in financial markets. Banks involved in proprietary trading are exposed to market risk due to change in interest or foreign exchange rates.

University College London (UCL)

31.21 Interest Rate Risk Management

Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair value of financial instruments. Interest rate risk at the Bank is well managed and contained and the Bank has no significant long term or complex interest rate positions. The Bank seeks to minimize the negative impact on net interest income of adverse movement in interest rates.

The Bank uses its own base rate for pricing of products, which can be changed with 30 days' notice to the customers. Therefore, any significant fluctuation in interest rate is unlikely to have a material impact on the Bank as it can re-price its lending and customer deposit books. The Bank is exposed to interest rate risk on its fixed rate investment portfolio maintained to meet the Liquidity Coverage Ratio (LCR) requirement. However, this is only limited to a portion, which is monitored in ALCO.

Customers' deposits are mostly short tenors (<1year) and priced in accordance with market conditions and the Bank's cost of funds. Hence the interest rate risk on the same is limited.

The following table provides a summary of the interest rate re-pricing profile of the Bank's financial assets and liabilities. Items have been allocated to time bands by reference to the earlier of the next interest rate reset date and the contractual maturity date.

Amount in £ 000'

2020	Within 3 months	<3 to 6 months	<6 months to 1 year	<1 to 2 years	<2 to 3 years	< 3 to 4 years	No specific re-pricing	Total
Assets								
Cash in hand & with central bank	78,819	-	-	-	-	-	591	79,410
Due from banks	48,237	21,975	7,220	-	-	-	34,425	111,857
Loans & advances to customers	2,203	459,166	-	-	-	-	-	461,369
Financial investments								
– fair value through other comprehensive income	47,824	2,995	3,814	11,210	14,049	7,667	-	87,559
- Amortised cost	-	-	-	16,799	-	-	-	16,799
Derivative financial instruments	375	96	145	-	-	-	-	616
Total assets	**177,458**	**484,232**	**11,179**	**28,009**	**14,049**	**7,667**	**35,016**	**757,610**
Liabilities								
Due to banks	2,000	9,246	17,471	-	-	5,020	6,354	40,091
Due to customers	168,677	140,590	98,648	-	-	-	215,729	623,644
Derivative financial instruments	262	87	9	-	-	-	-	358
Subordinated liabilities	-	20,063	-		-	-	-	20,063
Total Liabilities	**170,939**	**169,986**	**116,128**	**-**	**-**	**5,020**	**222,083**	**684,156**
Net Gap (Assets – Liabilities)	**6,519**	**314,246**	**(104,949)**	**28,009**	**14,049**	**2,647**	**(187,067)**	**73,454**

2019	Within 3 months	<3 to 6 months	<6 months to 1 year	<1 to 2 years	<2 to 3 years	< 3 to 4 years	No specific re-pricing	Amount in £ 000' Total
Assets								
Cash in hand & with central bank	58,190	-	-	-	-	-	774	58,964
Due from banks	45,162	29,850	-	-	-	-	23,286	98,298
Loans & advances to customers	61	434,426	670	114	-	-	-	435,271
Financial investments								
– fair value through other comprehensive income	55,416	1,002	6,481	3,091	1,679	-	-	67,669
- Amortised cost	-	-	-	-	16,917	-	-	16,917
Derivative financial instruments	287	65	5	-	-	-	-	357
Total assets	**159,116**	**465,343**	**7,156**	**3,205**	**18,596**	**0**	**24,060**	**677,476**
Liabilities								
Due to banks	6,722	-	-	-	-	-	-	6,722
Due to customers	193,190	62,789	95,870	7,138	-	-	218,026	577,013
Derivative financial instruments	263	49	-	-				312
Subordinated liabilities	-	-	-	20,098	-	-		20,098
Total Liabilities	**200,175**	**62,838**	**95,870**	**27,236**	**-**	**-**	**218,026**	**604,145**
Net Gap (Assets – Liabilities)	**(41,059)**	**402,505**	**(88,714)**	**(24,031)**	**18,596**	**-**	**(193,966)**	**73,331**

Interest Rate Sensitivity Analysis

The sensitivity to the income statement to various interest risk variables is considered on daily basis. An analysis of sensitivity to an increase or decrease in market interest rates, assuming no asymmetrical movement in yield curves and a constant financial position, is as follows at the financial year end.

	2020 Impact on P&L (£ 000')	2019 Impact on P&L (£ 000')
25bps increase in interest rate	91	17
25bps decrease in interest rate	28	17
50bps increase in interest rate	182	16
50bps decrease in interest rate	52	16

31.22 Foreign Currency (FX) Risk Management

Foreign Exchange risk – is the risk that the Bank will suffer a loss as a result of an adverse movement in exchange rates.

The Bank has identified FX risk component of its market risk that could lead to losses considering the nature of Bank's business. As the Bank is not running a trading book it is not exposed to FX risk to a large extent.

The Bank has developed various management reports to measure and manage foreign exchange risk. The Bank's open foreign exchange positions are monitored intraday. The foreign exchange exposures are managed by the treasury front office with a maximum allowable net open position ("NOP") of £1m with a maximum amount of £250,000 in a single currency. The Bank considers this an acceptable risk exposure. Client transactions are generally executed on a matched basis reducing the risk of losses. The Bank does not engage in proprietary trading.
This eliminates the likelihood of FX losses.

Key Risk Indicators exceeding tolerance are reviewed in the CCC & ALCO & reported to the Audit Risk and Compliance Committee (ARCC) together with remedial action plans.

The Bank's net open position (NOP) as at 31 December 2020 was £0.06m (2019: £0.06m)

Currency	2020 (£ 000')	2019 (£ 000')
USD	4	17
EUR	(2)	16
PKR	5	3
ZAR	24	(3)
CAD	(4)	2
INR	3	11
Others	31	18

31.23 Liquidity Risk Management

The Bank's liquidity risk is clearly articulated in its "Liquidity Risk Management Policy" (LRMP) approved by the Board of Directors. The Bank maintains adequate liquidity levels all the time to cover its short- and medium-term liquidity risks over an appropriate set of time horizons for both BAU and stressed conditions. The Bank keeps a liquid asset buffer of High-Quality Liquid Assets as required by European Union (EU) regulations. The Bank also maintains substantial liquidity in the Bank of England Reserve account and in short term deposits to meets its liquidity requirements.

Liquidity risk is the risk that the Bank is unable to meet its obligations as they fall due and in the currency in which they are due. Typically, this arises from a mismatch in the cash flows arising from assets, liabilities and contingencies. To limit this risk, the Bank manages the maturities of its assets and liabilities and its cash flows on a daily basis.

The Bank has put in place strategies, policies, processes and systems that enable it to identify measure, manage and monitor liquidity risk over an appropriate set of time horizons, including intraday, so as to ensure that it maintains adequate levels of liquidity buffers. The Bank's liquidity policy is based on maintaining sufficient liquid resources to ensure there is no significant risk that its liabilities cannot be met as they fall due.

The Board oversees liquidity risks. The risks identified in the Bank's risk profiles are all at a level, which are in line with the current business operations and the Business Plan. The Bank has a clearly defined liquidity risk appetite approved by the Board. This forms the basis of its liquidity risk policy as well as systems and controls around the management of liquidity adequacy. The Bank will continue to review and update its liquidity risk management framework based on feedback from PRA experience and from developments in market and industry best practices.

In order to achieve the above, the Bank has identified several risk factors, which form components of the Bank's overall liquidity risk profile. These include but are not limited to:

- Wholesale secured and unsecured funding risk
- Retail funding risk
- Intra-day liquidity risk
- Intra-group liquidity risk
- Cross-currency liquidity risk
- Off-balance sheet liquidity risk
- Franchise viability risk
- Marketable assets risk
- Non-marketable assets risk
- Funding concentration risk

The Treasury Department is responsible for the day-to-day management of funding and liquidity with particular attention to the level of mismatch between assets and liabilities as well as currency exposure. The Finance Department provides daily monitoring reports against the regulatory and MI requirements, with a clear escalation process for reporting adverse outcomes. The ALCO coordinates and provides direct oversight on the whole process of liquidity risk management in accordance with their terms of reference approved by the Board.

The Bank has the following liquidity profile that analyses assets and liabilities into relevant maturity buckets based on the remaining period to contractual maturity. The maturity profile is the representative of its contractual undiscounted cash flows.

Amount in £ 000'

2020	Carrying amount	Gross nominal inflow/ (outflow)	Within 1 month	1-3 months	3 months -1 year	1-5 years	>5 years
Financial asset by type							
Non-derivative assets							
Cash in hand & with central bank	79,410	79,417	79,417	-	-	-	-
Due from banks	111,857	112,188	53,304	29,614	29,270	-	-
Loans & advances to customers	455,954	499,703	90,526	23,439	59,196	325,902	640
Financial investments							
– fair value through other comprehensive income	87,558	88,562	-	3,732	19,211	65,619	-
– Amortised cost	16,799	17,100	-	-	-	17,100	-
	751,578	**796,970**	**223,247**	**56,785**	**107,677**	**408,621**	**640**
Derivative assets							
Risk management	616						
Outflow		25,751	2,592	8,957	14,202	-	-
Inflow	-	(25,156)	(2,478)	(8,699)	(13,979)	-	-
	616	**595**	**114**	**258**	**223**	**-**	**-**
Financial liability by type							
Non-derivative liabilities							
Due to banks	40,091	(40,405)	(8,668)	-	(26,717)	(5,020)	-
Due to customers	623,644	(625,314)	(279,874)	(103,811)	(241,629)	-	-
Subordinated liabilities	20,063	(20,196)	-	-	-	(20,196)	
Lease liability	2,582	(2,560)	(77)	(278)	(1,458)	(747)	
	686,380	**(688,475)**	**(288,619)**	**(104,089)**	**(269,804)**	**(25,963)**	**-**
Derivative liabilities							
Risk management	358	-	-	-	-	-	-
Outflow	-	9,613	2,173	3,345	4,095	-	-
Inflow	-	(9,920)	(2,234)	(3,497)	(4,189)	-	-
	358	**(307)**	**(61)**	**(152)**	**(94)**	**-**	**-**

Amount in £ 000'

2019	Carrying amount	Gross nominal inflow/ (outflow)	Within 1 month	1-3 months	3 months -1 year	1-5 years	>5 years
Financial asset by type							
Non-derivative assets							
Cash in hand & with central bank	58,964	59,001	59,001	-	-	-	-
Due from banks	98,298	98,469	40,152	28,283	30,034	-	-
Loans & advances to customers	430,233	502,313	30,685	9,579	20,586	70,901	370,562
Financial investments							
– fair value through other comprehensive income	67,669	67,951	2,505	6,124	13,628	45,694	-
– Amortised cost	16,917	17,120	-	-	-	17,120	-
	672,081	**744,854**	**132,343**	**43,986**	**64,248**	**133,715**	**370,562**
Derivative assets							
Risk management	357					-	-
Outflow		13,643	2,878	3,513	7,252	-	-
Inflow	-	(13,305)	(2,765)	(3,358)	(7,182)	-	-
	357	**338**	**113**	**155**	**70**	**-**	**-**
Financial liability by type							
Non-derivative liabilities							
Due to banks	6,722	(6,723)	(6,723)	-	-	-	-
Due to customers	577,013	(578,977)	(285,889)	(124,878)	(160,789)	(7,421)	-
Subordinated liabilities	20,098	(20,299)	-	-	-	(20,299)	-
Lease liability	2,796	(2,952)	(76)	(294)	(1,478)	(1,104)	
	606,629	**(608,951)**	**(292,688)**	**(125,172)**	**(162,267)**	**(28,824)**	**-**
Derivative liabilities							
Risk management	312	0	-	-	-	-	-
Outflow	-	8,080	1,893	3,283	2,904	-	-
Inflow	-	(8,373)	(1,986)	(3,424)	(2,963)	-	-
	312	**(293)**	**(93)**	**(141)**	**(59)**	**-**	**-**

The Bank has disclosed a contractual maturity analysis for its financial instruments. This includes a maturity analysis for financial assets that it holds as part of its managing liquidity risk – e.g., financial assets that are expected to generate cash inflows to meet cash outflows on financial liabilities – because the Bank considers that such information is necessary to enable financial statement users to evaluate the nature and extent of its liquidity risk.

The Bank liquidity risk management measures includes access to Bank of England facilities under the Sterling Money Framework which are Reserve Account, Indexed Long Term Repo facility and Discount Window Facility. Such arrangement can be utilised by providing eligible securities to the Bank of England as collateral.

Exposure to Liquidity risk

The key measure used by the Bank for managing liquidity risk is the ratio of high-quality liquid assets (HQLA) to deposits from customers and short-term funding. For this purpose, HQLA divided by deposits from customers and banks. Bank also considers the liquidity coverage ratio (LCR) being another strong tool for liquidity Risk.

Details of the reported ratios at the reporting date and during the reporting period were as follows:

	2020 (Unaudited) Liquidity coverage %	2020 (Unaudited) HQLA to deposits %	2019 (Unaudited) Liquidity coverage %	2019 (Unaudited) HQLA to deposits %
As at 31 December	227%	19%	160%	16%
Average for the period	219%	17%	178%	17%
Maximum for the period	332%	22%	220%	23%
Minimum for the period	158%	13%	131%	12%

Liquidity Reserves	2020 Carrying amount	2020 HQLA	2019 Carrying amount	2019 HQLA
Balance with central bank	78,819	75,815	58,190	55,173
Cash in hand	591	591	774	774
Unencumbered debt securities issued by sovereigns and supranational	33,426	33,011	33,788	33,788
Other assets	15,502	8,074	3,800	1,900
	128,338	**117,491**	**96,552**	**91,635**

31.24 Financial assets and financial liabilities

Classification of financial assets and financial liabilities

The following table provides a reconciliation between line items in the statement of financial position of categories of financial instruments.

31 December 2020 Amount in £ 000'	Mandatorily at FVPTL	FVOCI – debt instruments	Amortised cost	Estimated credit loss	Total carrying amount
Cash in hand and with central bank	-	-	79,410	-	79,410
Due from banks	-	-	112,389	(532)	111,857
Loans and advances to customers	-	-	461,369	(5,415)	455,954
Financial investments	-	87,558	16,800	(1)	104,357
Derivative assets held for risk management	616	-	-	-	616
Total financial assets	**616**	**87,558**	**669,968**	**(5,948)**	**752,194**
Due to banks	-	-	40,091	-	40,091
Due to customers	-	-	623,644	-	623,644
Derivative assets held for risk management	358	-	-	-	358
Current tax liabilities	-	-	103	-	103
Subordinated liabilities	-	-	20,063	-	20,063
Other liabilities	-	-	990	-	990
Total financial liabilities	**358**	**-**	**684,891**	**-**	**685,249**

31 December 2019 Amount in £ 000'	Mandatorily at FVPTL	FVOCI – debt instruments	Amortised cost	Estimated credit loss	Total carrying amount
Cash in hand and with central bank	-	-	58,964	-	58,964
Due from banks	-	-	98,634	(336)	98,298
Loans and advances to customers	-	-	435,271	(5,038)	430,233
Financial investments	-	67,669	16,918	(1)	84,586
Derivative assets held for risk management	357	-	-	-	357
Total financial assets	**357**	**67,669**	**609,787**	**(5,375)**	**672,438**
Due to banks	-	-	6,722	-	6,722
Due to customers	-	-	577,013	-	577,013
Derivative assets held for risk management	312	-	-	-	312
Current tax liabilities	-	-	570	-	570
Subordinated liabilities	-	-	20,098	-	20,098
Other liabilities	-	-	1,198	-	1,198
Total financial liabilities	**312**	**-**	**605,601**	**-**	**605,913**

31.25 Encumbered assets

Certain assets are pledged as collateral to secure liabilities under Credit Support Annex ("CSA") for derivative liabilities and as security deposits relating to FX forward transactions. The holders of these securities do not have the right to sell or re-pledge the asset except where specifically disclosed. The aggregate amount of collateral pledged under CSAs is £0.26m as on 31 December 2020 (2019: £ 0.32m) as mentioned at note 15.2.

As at 31 December 2020 financial investments of £6 million (2019: Nil) was encumbered against borrowing of £5 million from the Bank of England against TFSME scheme (2019: Nil) as mentioned at note 17.1.

31.26 Operational Risk Management

Operational Risk is the risk that the Bank triggers one or more of the below situations due to failed internal processes, people and systems – these can be internal or external to the Bank:

- Adversely impacts customers (customers are defined as customer of the Bank as well as internal "customers" such as colleagues with a dependency on particular output or service)
- Incurs losses e.g., operational losses (this includes temporary losses i.e., where recovery is made or is in progress of being made)
- Breaches in regulatory requirements or other policies and practices of the Bank

The Bank's operational processes exist to support the servicing of customers and to maintain compliance with relevant regulation. These imperatives will be robustly protected. The Bank will ensure that it remains compliant with the latter but its approaches to the former will vary according to priority and need. In terms of customer service, the Bank will actively employ flexible approaches to maintaining and protecting delivery and to this end will incur reasonable costs as required.

The Bank adopts the Basic Indicator approach for calculating Operational Risk capital as set out in the CRR and consequently embarks on rigorous risk identification exercises to establish any Pillar 2 requirements for Operational Risk.

31.27 Capital Management and Risk

The primary objective of capital management is to maintain strong capital to support medium to long-term business growth. An effective capital management process provides resilience arising from both internal and external factors resulting in additional capital requirements. The Bank maintains strong capital ratios not only to support its business and maximise shareholders' value but also to maintain depositors' and market confidence. The Prudential Regulation Authority sets and monitors the capital requirement for the Bank.

The Bank's capital has been invested by the Parent bank to support long-term business growth of the Bank, which includes capital resources to meet Total Capital Requirement (Pillar 1 and Pillar 2), CRD Buffers and PRA Buffer. The Bank also maintains an internal capital buffer over and above the minimum regulatory capital requirement. The Bank also takes into account changes in economic conditions; risk characteristics of its activities and regulatory requirement in managing its capital structure and make adjustments to it in the light of such changes. The Bank has put in place processes and controls to monitor and manage its own funds and no breaches were reported to the PRA during the period.

The Bank's regulatory capital consists of the sum of the following elements:

- Common equity Tier 1 (CET 1) capital, which includes ordinary share capital and retained earnings, and Tier 2 capital which includes qualifying subordinated liabilities.

	2020 (£ 000')	2019 (£ 000')
Share capital	60,000	60,000
Retained earnings	11,826	11,226
Tier 1 capital	**71,826**	**71,226**
Subordinated liability	20,000	20,000
IFRS 9 (ECL) impact of regulatory capital	540	426
	20,540	20,426
Own funds	**92,366**	**91,652**

32. Ultimate Parent Company

The Bank is a wholly owned subsidiary undertaking of Habib Bank AG Zurich, which is the ultimate controlling parent, incorporated in Switzerland. The largest group in which the results of the company are consolidated is Habib Bank AG Zurich, Switzerland.

33. Significant Events after the Balance Sheet Date

The subordinated liability of £20 million as referred in notes 25 and 31.27 was rolled over for another period of 5 years by the parent bank in April 2021.

The Directors confirms that a part from the above there were no significant events since the reporting date that require to be disclosed.

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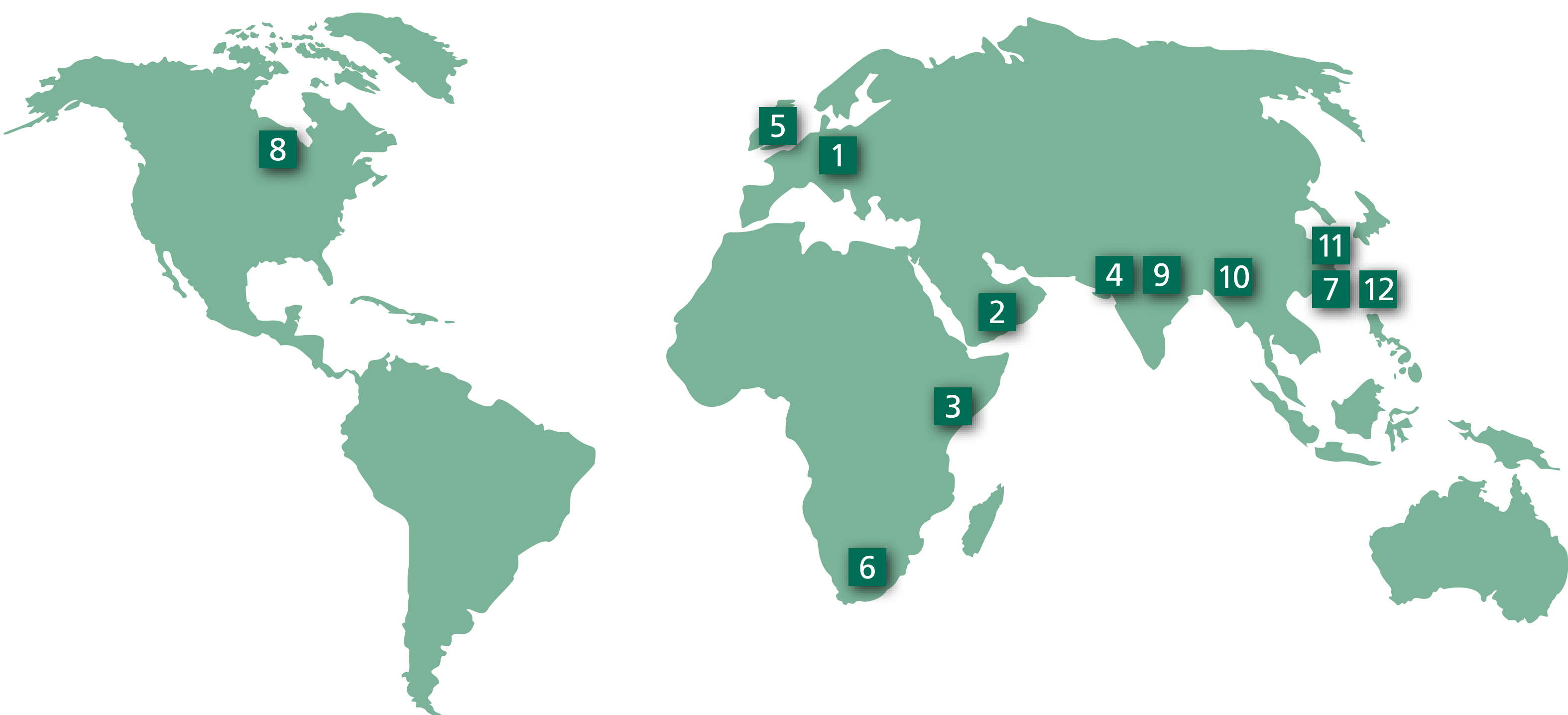
International Network



Head Office	1	Switzerland	Habib Bank AG Zurich	
Branches	1	Switzerland	Habib Bank AG Zurich	1 Branch
	2	UAE	Habib Bank AG Zurich	8 Branches
	3	Kenya	Habib Bank AG Zurich	4 Branches
Subsidiaries	4	Pakistan	Habib Metropolitan Bank Ltd	406 Branches
	5	United Kingdom	Habib Bank Zurich plc	8 Branches
	6	South Africa	HBZ Bank Ltd	9 Branches
	7	Hong Kong	Habib Bank Zurich (Hong Kong) Ltd	2 Branches
	8	Canada	Habib Canadian Bank	3 Branches
Representative offices	9	Pakistan	Habib Bank AG Zurich	
	10	Bangladesh	Habib Bank AG Zurich	
	11	China	Habib Bank AG Zurich	
	12	Hong Kong	Habib Bank AG Zurich	

Habib Bank AG Zurich is the trading name of Habib Bank Zurich plc.
Registered office: Habib House, 42 Moorgate, London EC2R 6JJ.
Registered in England and Wales: Company registered number: 08864609.

Authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority
and the Prudential Regulation Authority under registration number 627671.
Habib Bank Zurich plc is covered by the Financial Services Compensation Scheme.