MeDirect Bank (Malta) plc

Condensed Consolidated Interim Financial Statements 30 September 2018

Company Registration Number C 34125

Interim directors' report pursuant to Listing Rules 5.74 et seq

The directors present their interim financial statements of MeDirect Bank (Malta) plc ("the Bank" or "MeDirect Malta"), and its principal subsidiary, MeDirect Bank S.A. ("MeDirect Belgium" or "the subsidiary") (together referred to as the "Group" or "MeDirect Malta Group") for the six month period ended 30 September 2018.

Principal Activities

The principal activities of MeDirect Malta and MeDirect Belgium comprise lending to international corporates and the provision of banking services primarily to the mass affluent sector in Malta and Belgium, focusing primarily on term deposit savings and wealth management, as well as local corporate banking in Malta.

Financial Performance

The Group reported a profit after tax of €11.8 million for the six months ended 30 September 2018 compared with €7.1 million for the same period last year. The Group registered growth both in its net interest income and in its net fee and commission income as a result of growth in both its international lending business and its wealth management business. The current period's performance was negatively impacted by higher credit impairment charges.

During the six-months ended 30 September 2018, the Group registered net interest income of €33.7 million (30 September 2017: €31.1 million). Total operating income amounted to €37.8 million (30 September 2017: €33.7 million). Total operating expenses amounted to €25.1 million (30 September 2017: €23.9 million).

The Group continued to build its corporate lending activities both internationally and domestically. As at 30 September 2018, the Group's international and domestic loans and advances to customers ("Lending Portfolio") stood at €1.9 billion (31 March 2018: €1.7 billion), net of expected credit losses of €30.5 million (31 March 2018: collective impairment loss allowances of €5.6 million and specific impairment loss allowances of €17.0 million). In addition the Group had commitments of €433.4 million under revolving credit facilities as at 30 September 2018 (31 March 2018: €361.8 million) and other undrawn credit facilities of €52.5 million (31 March 2018: €74.7 million). As at 30 September 2018, the Group's investment portfolio, consisting of debt securities stood at €0.5 billion (31 March 2018: €0.6 billion).

Business Development

At the moment the Group is looking at broadening its asset base internationally to diversify both its risk and its income. The Group will enter new asset classes and new jurisdictions in thoughtful and well planned ways, building on our track record of both organic and inorganic growth.

On 1 February 2018, MeDirect Malta announced that the boards of directors of MeDirect Malta and Charts Investment Service Limited ("Charts") have each voted to merge Charts into MeDirect Malta, subject to receipt of all applicable regulatory approvals and completion of all legal requirements. On 1 April 2018 the shares held by MDB Group Limited in Charts were transferred to MeDirect Malta. With effect from 1 April 2018, the merger between MeDirect Malta and Charts became effective for accounting purposes. Thus all the transactions of Charts have been treated as being those of MeDirect Malta with effect from 1 April 2018.

Interim directors' report pursuant to Listing Rules 5.74 et seq - continued

Business Development - continued

During the financial period ended 30 September 2018, the Group continued to implement its business plan with the aim of sustaining the Group's long-term profitability by building its international corporate lending portfolio and its deposit customer base in the mass affluent market both in Malta and Belgium and also with select corporates in Malta.

The Group also continues to make significant investments in technology that have allowed it to enhance its online banking and investment services for its customers, together with systems to support such services. Investment services include online execution of brokerage transactions in respect of equities, bonds and funds as well as foreign exchange execution capabilities. The Group also offers online retirement and investment planning capabilities, model portfolio analytical tools to enable customers to analyse portfolio and investment alternatives and a broad range of research and market data resources.

The Group continues to fund its portfolios through deposits and through the international wholesale financial markets. The Group's significant deposit base, both in Malta and in Belgium, has strengthened and made more robust the Group's funding platform. Access to the Eurex repo platform provides efficient funding for the Group. The Group's core deposit offering is a range of fixed-term and other term deposit savings products. As at 30 September 2018, the Group's deposit base reached €2.0 billion (31 March 2018: €2 billion). The Group's deposit base also provides a potential customer base for investment and wealth management products.

The Group's Lending Portfolio primarily consists of senior secured loans and revolving credit facilities to corporate borrowers domiciled in Western Europe. Substantially all loans and revolving credit facilities in the portfolio are denominated in euro or pound sterling and substantially all of the loans are floating rate instruments (some have interest rate floors embedded within the contracts) and would not be adversely affected by material changes in interest rates.

As part of the Group's funding strategy, MeDirect Malta had set up Grand Harbour I B.V. ("GH I"), a controlled special purpose entity which has been consolidated since the Group retained all the risks and rewards of the structure. GH I was funded through two intragroup loan facilities subscribed to by MeDirect Malta and MeDirect Belgium that led to a transfer of risk from MeDirect Belgium to MeDirect Malta, without however changing MeDirect Malta Group's overall risk on a consolidated basis. MeDirect Belgium and MeDirect Malta invested in GH I on a 75% - 25% basis with the tranche bought by MeDirect Belgium (the "Senior Loan") having a senior ranking vis-à-vis the facility taken up by MeDirect Malta (the "Junior Loan").

The MDB Group (the "Regulatory Group"), which comprises MeDirect Group Limited and its subsidiaries, the MeDirect Malta Group, remains committed to operating with strong regulatory ratios and a robust liquidity position. For more information one may refer to the Pillar 3 reports issued by the MDB Group on a quarterly basis that are available on the Group's website.

The Regulatory Group, that is also considered a core domestic bank by the Central Bank of Malta, will continue to ensure that appropriate capital levels are maintained reflecting the economic environment and the challenges that the Regulatory Group is faced with. The Regulatory Group is under the Single Supervisory Mechanism ("SSM") and the direct supervision of the European Central Bank ("ECB"). The Regulatory Group is confident that it will continue to meet the high expectations of the ECB.

Interim directors' report pursuant to Listing Rules 5.74 et seq - continued

Dividends and reserves

After adjusting the Reserve for General Banking Risks in accordance with the requirements of Banking Rule ("BR") 09 - Measures addressing credit risk arising from the assessment of the quality of asset portfolios of credit institutions authorised under the Maltese Banking Act (Cap. 371), the retained earnings of the Group amounted to €46.3 million (31 March 2018: €42.5 million).

By virtue of a shareholders' resolution dated 30 May 2018, MeDirect Bank Malta plc approved the repayment of the shareholder contribution equivalent to €7.23 million.

Outlook and future business developments

The ongoing robustness of capital and liquidity ratios provide a stable foundation from which to produce attractive and sustainable returns. The strategy that has been defined by the Board of Directors over the last few years has resulted in significant growth whilst producing attractive returns and an ability to invest in the capabilities of the Group notwithstanding the low interest rate environment.

Stability in the international capital markets results in a positive effect on the Group's wealth management and investment services businesses since greater investor confidence leads to increased customer interest in the investment products offered by the Group.

The above should be construed in light of the fact that the Eurozone macroeconomic environment remains challenging, especially given the economic effects of the approaching UK Brexit, and that any reversal of the positive trends described above could have a negative effect on the Group's asset portfolios and businesses. Despite these ongoing challenges, the Group remains confident that its underlying strategy will continue to result in profitable growth. Furthermore, the Group is currently exploring new opportunities in order to diversify the Group's asset classes and the relative revenue streams.

As a result of the operations previously undertaken by Charts, MeDirect Malta will consolidate and expedite its Maltese wealth management business.

The Group has grown its corporate lending activities. The Group has recently been operating with a relatively stable leverage ratio and intends to continue to operate with a capital adequacy ratio in excess of the minimum capital requirements determined by Capital Requirements Directive ("CRD") IV and also in conformity with any other guidance issued by the Group's regulator, the ECB's joint Supervisory Team (the "JST").

The developments mentioned above enable the Board of Directors to look forward to the future with cautious optimism. Furthermore, at present the Group's shareholders are considering strategic options in relation to the Group, including a possible sale. A final decision of the outcome of this process has not been made, and it may or may not lead to a sale.

Related parties

There were no material changes in related party transactions from those detailed in the financial statements for the period ended 31 March 2018. During this period no further related party transactions materially affected the financial position or liquidity of the Group.

Interim directors' report pursuant to Listing Rules 5.74 et seq - continued

Events after the reporting date

The Group was notified on 30 November 2018 that a debtor client had entered into an agreement that is expected to lead to the successful disposal of its business during the first quarter of 2019. The reported price at which this disposal is expected to occur would lead to the recovery, in total or to a material extent, of credit losses amounting to €3.5 million that have been recognised by the Group in earlier accounting periods on the account in question; and of unaccrued interest due thereon. The Group is awaiting further information to enable it to better assess the favourable impact of this transaction, which will be reflected in its results for the full financial year ending on 31 March 2019.

Approved by the Board on 3 December 2018 and signed on its behalf by:

Michael Bussey
Chairman

Mark A. Watson
Director and Chief Executive Officer

Condensed consolidated interim statement of financial position

	As at 30 September 2018 €000	As at 31 March 2018 €000
ASSETS		
Balances with Central Banks and cash	**68,026**	103,739
Derivative financial instruments	**1,046**	470
Loans and advances to financial institutions	**111,353**	113,623
Loans and advances to customers	**1,857,428**	1,701,716
Investments - Treasury	**544,816**	560,245
Property and equipment	**1,697**	1,223
Intangible assets	**4,100**	2,495
Non-current assets classified as held for sale	**1,785**	1,785
Current tax assets	**9,759**	9,527
Deferred tax assets	**23,636**	16,104
Prepayments and accrued income	**16,030**	18,168
Other assets	**10,560**	16,510
Total assets	**2,650,236**	2,545,605

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

Condensed consolidated interim statement of financial position - continued

	As at 30 September 2018 €000	As at 31 March 2018 €000
EQUITY		
Called up issued share capital	**117,450**	117,450
Share premium	**13,464**	13,464
Shareholders' contributions	**143,196**	147,353
Reserve for general banking risks	**1,856**	1,694
Other reserves	**(217)**	(1,732)
Retained earnings	**46,345**	42,468
Total equity	**322,094**	320,697
LIABILITIES		
Derivative financial instruments	**2,297**	3,581
Amounts owed to financial institutions	**248,075**	126,428
Amounts owed to customers	**1,967,360**	1,979,159
Subordinated liabilities	**66,876**	66,949
Current tax liabilities	**194**	156
Accruals and deferred income	**36,224**	34,266
Other liabilities	**7,116**	14,369
Total liabilities	**2,328,142**	2,224,908
Total equity and liabilities	**2,650,236**	2,545,605
Memorandum items		
Commitments to purchase financial assets	**61,115**	118,250
Commitments to extend credit, guarantees and other commitments	**501,341**	449,153

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

The condensed consolidated interim financial statements on pages 5 to 33 were approved and authorised for issue by the Board of directors on 3 December 2018 and signed on its behalf by:

Michael Bussey
Chairman

Mark A. Watson
Director and Chief Executive Officer

Condensed consolidated interim statement of comprehensive income

	Period from 1 April to 30 September 2018 €000	Period from 1 April to 30 September 2017 €000
Interest income	**47,920**	45,535
Interest expense	**(14,221)**	(14,400)
Net interest income	**33,699**	31,135
Fee and commission income	**3,222**	2,565
Fee and commission expense	**(784)**	(815)
Net fee and commission income	**2,438**	1,750
Net trading income	**1,582**	1,981
Other operating income		
- Realised gains on disposal of other investments	**-**	43
- Realised gains/(losses) on disposal of loans and advances	**26**	(1,178)
- Other income	**15**	4
Total operating income	**37,760**	33,735
Personnel expenses	**(9,836)**	(9,636)
Depreciation and amortisation	**(292)**	(85)
Other administrative expenses	**(14,973)**	(14,143)
Total operating expenses	**(25,101)**	(23,864)
Net operating income before impairment charges	**12,659**	9,871
Credit impairment loss/net impairment charges	**(4,600)**	(1,021)
Profit before tax	**8,059**	8,850
Taxation	**3,778**	(1,750)
Profit for the period	**11,837**	7,100
Other comprehensive income		
Items that may be reclassified subsequently to profit or loss		
Fair valuation of FVOCI financial assets:		
- Net change in fair value, before tax	**148**	1,378
- Net amount reclassified to profit or loss, before tax	**-**	(43)
Income tax relating to other comprehensive income	**(55)**	(467)
Other comprehensive income, net of tax	**93**	868
Total comprehensive income, net of tax	**11,930**	7,968
Earnings per share (cents)	**10c**	6c

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

Condensed consolidated interim statement of changes in equity

	Share capital €000	Share premium €000	Shareholders' contributions €000	Reserve for general banking risks €000	Other reserves €000	Retained earnings €000	Total €000
Balance at 1 April 2017	117,450	13,464	60,803	1,694	(2,511)	32,923	223,823
Total comprehensive income							
Profit for the period	-	-	-	-	-	7,100	7,100
Other comprehensive income, net of tax:							
Fair valuation of FVOCI financial assets:							
- Net change in fair value arising during the period, net of tax	-	-	-	-	896	-	896
- Reclassification adjustments: net amounts reclassified to profit or loss, net of tax	-	-	-	-	(28)	-	(28)
Total other comprehensive income, net of tax	-	-	-	-	868	-	868
Total comprehensive income, net of tax	-	-	-	-	868	7,100	7,968
Transactions with owners							
Contributions by shareholder	-	-	8,200	-	-	-	8,200
Total transactions with owners	-	-	8,200	-	-	-	8,200
Balance at 30 September 2017	**117,450**	**13,464**	**69,003**	**1,694**	**(1,643)**	**40,023**	**239,991**

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

Condensed consolidated interim statement of changes in equity - continued

	Share capital €000	Share premium €000	Shareholders' contributions €000	Reserve for general banking risks €000	Other reserves €000	Retained earnings €000	Total €000
Balance at 1 April 2018 as previously stated	117,450	13,464	147,353	1,694	(1,732)	42,468	320,697
Impact on transition to IFRS 9	-	-	-	-	1,422	(7,877)	(6,455)
Impact of merger (note 1)	-	-	-	-	-	79	79
Balance at 1 April 2018 as restated	117,450	13,464	147,353	1,694	(310)	34,670	314,321
Total comprehensive income							
Profit for the period	-	-	-	-	-	11,837	11,837
Other comprehensive income, net of tax:							
Fair valuation of FVOCI financial assets:							
- Net change in fair value arising during the period, net of tax	-	-	-	-	93	-	93
Total other comprehensive income, net of tax	-	-	-	-	93	-	93
Total comprehensive income, net of tax	-	-	-	-	93	11,837	11,930
Transactions with owners							
Repayment of shareholder contribution	-	-	(7,230)	-	-	-	(7,230)
Shareholder's Contribution	-	-	3,073	-	-	-	3,073
Transfer to reserve for general banking risks	-	-	-	162	-	(162)	-
Balance at 30 September 2018	**117,450**	**13,464**	**143,196**	**1,856**	**(217)**	**46,345**	**322,094**

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

Condensed consolidated interim statement of cash flows

	Period from 1 April to 30 September 2018 €000	Period from 1 April to 30 September 2017 €000
Cash flows from operating activities		
Interest and commission receipts	**60,983**	57,090
Interest and commission payments	**(12,908)**	(13,599)
Payments to employees and suppliers	**(19,939)**	(25,369)
Operating profit before changes in operating assets/liabilities	**28,136**	18,122
(Increase)/decrease in operating assets:		
- Reserve deposit with Central Banks	**(6,562)**	86,085
- Loans and advances to financial institutions and customers	**(201,654)**	(127,297)
Increase/(decrease) in operating liabilities:		
- Amounts owed to financial institutions and customers	**93,142**	(38,592)
- Other payables	**(6,436)**	11,029
- Derivative financial instruments	**(1,460)**	(373)
Tax paid	**(768)**	(2,613)
Net cash used in operating activities	**(95,602)**	(53,639)

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

Condensed consolidated interim statement of cash flows - continued

	Period from 1 April to 30 September 2018 €000	Period from 1 April to 30 September 2017 €000
Net cash used in operating activities	**(95,602)**	(53,639)
Cash flows from investing activities		
Net acquisitions of property and equipment and intangible assets	**(2,371)**	-
Net disposals and maturities of FVOCI financial assets	**12,025**	98,469
Net cash from investing activities	**9,654**	98,469
Cash flows from financing activities		
Shareholders' contributions	**(6,186)**	8,200
Net advances from immediate parent	**371**	9,849
Net advances (to)/from group companies	**(1,078)**	955
Net cash (used in)/from financing activities	**(6,893)**	19,004
Net (decrease)/increase in cash and cash equivalents	**(92,841)**	63,834
Cash and cash equivalents at the beginning of the period	**149,414**	102,143
Cash and cash equivalents at the end of the period	**56,573**	165,977

The notes on pages 12 to 33 are an integral part of these condensed consolidated interim financial statements.

Notes to the condensed consolidated interim financial statements

1. Reporting entity

MeDirect Bank (Malta) plc ("the Bank" or "MeDirect Malta"), formerly Mediterranean Bank plc, is domiciled and incorporated in Malta. These condensed consolidated interim financial statements ("interim financial statements") as at and for the six months ended 30 September 2018 comprise MeDirect Malta and its principal subsidiary, MeDirect Bank S.A. (MeDirect Belgium) (together referred to as the "Group").

The comparative consolidated financial information also includes for consolidation purposes financial information attributable to Charts Investment Service Limited ("Charts").

On 1 February 2018, MeDirect Malta announced that the boards of directors of MeDirect Malta and Charts have each voted to merge Charts into MeDirect Malta. On 1 April 2018 the shares held by MDB Group Limited in Charts were transferred to MeDirect Malta and with effect from 1 April 2018, the merger between MeDirect Malta and Charts became effective for accounting purposes. Thus all the transactions of Charts have been treated as being those of MeDirect Malta with effect from 1 April 2018.

The financial statements of the Group as at and for the year ended 31 March 2018 are available upon request from MeDirect Malta's registered office, being The Centre, Tigné Point, Sliema TPO 0001, Malta, and are available for viewing on its website at www.medirect.com.mt.

The principal activities of the Group comprise lending to international corporates and the provision of banking services primarily to the mass affluent sector in Malta and Belgium, focusing primarily on term deposit savings and wealth management, as well as local corporate banking in Malta.

2. Basis of preparation

These condensed consolidated interim financial statements for the six months ended 30 September 2018 have been prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU applicable to interim financial reporting (IAS 34 'Interim Financial Reporting'). They do not include all information required for a complete set of financial statements prepared in accordance with International Financial Reporting Standards as adopted by the EU. However, selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in the Group's financial position and performance since the last annual financial statements as at and for the year ended 31 March 2018.

As required by IAS 34 'Interim Financial Reporting', adopted by the EU, these interim financial statements include a comparative statement of financial position presenting information as at the previous financial year end, and comparative statements of comprehensive income presenting information for the comparable interim periods of the immediately preceding financial year.

The condensed consolidated interim financial statements have been extracted from MeDirect Malta's unaudited Group management accounts for the six months ended 30 September 2018, and have been reviewed in terms of ISRE 2410 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity'. The half-yearly results are being published in terms of Chapter 5 of the Listing Rules, issued by the Listing Authority, and the Prevention of Financial Markets Abuse Act, 2005.

3. Significant accounting policies

The accounting policies applied by the Group in these interim financial statements are consistent with those applied in the financial statements for the year ended 31 March 2018.

The Group has adopted the requirements of IFRS 9 "Financial Instruments" from 1 April 2018. IFRS 9 includes an accounting policy choice to remain with IAS 39 hedge accounting which the Group has exercised. The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application. As permitted by IFRS 9, the Group has not restated comparatives.

The Group has adopted the regulatory transitional arrangements adopted by the EU on 27 December 2017. These permit banks to add back to their capital base a proportion of the impact that IFRS 9 has upon their impairment allowances during the first five years of use. The proportion that banks may add back starts at 95% in the financial year ending 31 March 2019, and reduces to 25% in the financial year ending 31 March 2023.

Apart from IFRS 9, the Group adopted IFRS 15 “Revenue from contracts with customers” and also interpretations and amendments to specific standards but these had an insignificant effect on the interim financial statements.

There are no standards that are not yet effective and that would be expected to have a material impact on the Group in the current or future reporting periods and on foreseeable future transactions

IFRS 9 'Financial Instruments'

In July 2014, the IASB issued IFRS 9 "Financial Instruments", which is the comprehensive standard to replace IAS 39 "Financial Instruments: Recognition and Measurement", and includes requirements for classification and measurement of financial assets and liabilities, impairment of financial assets and hedge accounting. The European Commission has adopted IFRS 9 Financial Instruments with Regulation (EC) No 2016/2067 of 22 November 2016. The EU effective date is the same as the IASB's effective date (annual periods beginning on or after 1 January 2018). As a result, the date of initial application of IFRS 9 for the Group was 1 April 2018. The adoption and implementation of IFRS 9 required the Group to revise its accounting processes and internal controls relating to the reporting of financial instruments so as to ensure that the requirements emanating from IFRS 9 relating to the classification of financial assets and liabilities, the impairment of financial assets and hedge accounting are met.

Classification and measurement

Under IFRS 9, the Group determines the classification and measurement basis for financial assets based on an assessment of both the business model within which the financial assets are held and a review of the contractual terms of each financial asset to determine if cash flows are solely principal and payments of interest (SPPI).

In this regard, subsequent to initial recognition, financial instruments are measured at:
(i) amortised cost if the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows (‘Hold to Collect’) and the contractual terms of the financial asset give rise to cash flows that are SPPI;
(ii) FVOCI if the financial asset is held within a business model whose objective is achieved by both holding financial assets in order to collect contractual cash flows and selling financial assets (‘Hold to Collect and Sell’) and the contractual terms of the financial asset give rise to cash flows that are SPPI; or
(iii) FVTPL if the financial asset does not pass the business model assessment and SPPI criteria.

3. Significant accounting policies - continued

Classification and measurement - continued

Once the contractual cash flows of a financial instrument fail the SPPI criterion, the instrument is automatically classified and measured at FVTPL, irrespective of the result of the business model assessment.

A business model refers to the manner in which financial assets are managed in order to achieve a particular business objective, whether by collecting contractual cash flows only, selling financial instruments, or both. The Group's business model is determined by key management personnel and the assessment is based on matters of fact, reflecting the strategic purpose and intention for the portfolio.

The business model is determined at a level that reflects how groups of financial assets are managed together to achieve a particular business objective. Therefore, if the business model is set at a portfolio level, the classification assessment for this criterion is assessed at that level. Accordingly, it is not an instrument-by-instrument analysis but is determined at a higher level of aggregation.

The Group has identified three separate portfolios which require separate business model assessments due to the fact that these are managed separately and by different business units / management teams, namely (i) the Treasury portfolio; (ii) the International Corporate Lending portfolio; and (iii) the Local Lending portfolio.

A key distinction between business models relates to whether the 'sale' of financial instruments is integral to the achievement of the desired business objectives. In order for a sale of financial instruments to steer the classification of the entire portfolio away from a 'Hold to Collect' and towards a 'Hold to Collect and Sell' business model, sales need to be integral to the objective of the business model, rather than incidental to it. In this regard, the Group performs an assessment to determine whether the sale of financial instruments from a portfolio implies that the classification of the exposures to the 'Hold to Collect' business model is inappropriate. This assessment is based on information about past sales and expectations about future sales.

For financial assets where the intention of the business model is to hold the financial assets to collect the contractual cash flows or to hold to collect and to sell, the Group assesses whether the contractual cash flow characteristics of these assets meet the SPPI requirements of IFRS 9. In this respect, the contractual cash flow characteristics are deemed to be SPPI if the terms are consistent with a basic lending arrangement.

The contractual cash flows are assessed based on conditions at the date of initial recognition of the instrument. However, if a loan modification occurs resulting in the existing loan being derecognised and a new loan recognised, the modified asset is considered as a new loan under IFRS 9 and as such is considered for the SPPI assessment. In such a case, the date of the modification is treated as the date of initial recognition of the new financial asset. If, however, the existing loan was renegotiated or modified but was not derecognised, then the contractual cash flows of the modified loan are not considered for the SPPI assessment.

The 'principal' of a financial asset refers to the fair value of the financial instrument at initial recognition rather than the amount that is due under the contractual terms of the instrument. On the other hand, 'interest' is the compensation for time value of money and credit risk, may include consideration for other basic lending risks (e.g. liquidity risk), costs associated with holding the financial assets for a particular period of time (e.g. administrative costs) and/or a profit margin.

3. Significant accounting policies - continued

Classification and measurement - continued

In performing the SPPI assessment, the Group considers the following contractual terms to determine whether these introduce variability in contractual cash flows that is inconsistent with a basic lending arrangement, amongst others:

(i) Variable interest rates, which typically consider the time value of money, credit risk and other basic lending risks and costs;
(ii) Leverage, which is a contractual cash flow characteristic that results in increased variability in contractual cash flows;
(iii) Modifications of the time value of money; and
(iv) Contractual features that could alter the timing or amount of contractual cash flows of a financial asset, such as contingent events, prepayment and extension options.

More specifically, from the assessment that the Group conducted the following classification and measurement matters have been determined:

(i) loans and advances to banks and to customers that are classified as loans and receivables under IAS 39 will continue to be measured at amortised cost under IFRS 9; and
(ii) a portfolio of debt securities classified as available-for-sale under IAS 39 will be classified at FVOCI under IFRS 9 given that the objective of the business model is achieved by both the collection of contractual cash flows and selling of the financial assets, while a portfolio of debt securities classified as available-for-sale under IAS 39 will be measured at amortised cost under IFRS 9.

Impairment

The impairment requirements apply to financial assets measured at amortised cost and FVOCI, and certain loan commitments and financial guarantee contracts. At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for expected credit losses (‘ECL’) resulting from default events that are possible within the next 12 months (12-month ECL).

In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument (lifetime ECL). Financial assets where 12-month ECL is recognised are considered to be ‘Stage 1’. Financial assets which are considered to have experienced a significant increase in credit risk would be classified as ‘Stage 2’; and financial assets for which there is objective evidence of impairment, and which considered to be in default or otherwise credit impaired, would be classified as ‘Stage 3’. Stage 2 and Stage 3 assets require the measurement of lifetime ECLs.

Significant increase in credit risk
The concept of default risk is central to IFRS 9 – therefore, a key risk parameter used by the Group in its credit risk management activities is the probability that the obligor defaults either within the next 12-month period (in case of Stage 1 exposures) or over the lifetime of the exposure (in case of Stage 2 / 3 exposures).

3. Significant accounting policies - continued

Impairment - continued

In order to identify indicators of SICR since initial recognition, the Group compares the credit risk level on each financial instrument at each IFRS 9 reporting date with the credit risk level as at the date of initial recognition. The assessment requires the consideration of all reasonable and supportable information that is available without undue cost. If a SICR is identified, the financial instruments are transferred into Stage 2 and lifetime ECLs are recognised.

To assess a SICR event, the Group considers both actual and forward-looking information relating to external market indicators, internal factors and borrower-specific information. The Group's credit risk management framework comprises the use of both quantitative and qualitative SICR triggers. However, the assessment performed by the Group to identify a SICR varies across each of the Group's portfolios of financial instruments.

- *International Corporate Lending portfolio:*

Financial instruments within the Group's International Corporate Lending portfolio are managed on an individual basis for credit purposes, whereby the Group's credit analysts have access to the obligors and their financial information, the latter comprising both historical and forecasted financial information.

The four credit quality classifications below describe the credit quality of the Group's key financial assets. An internal risk grade is assigned to each obligor.

(i) Regular - no material credit concerns.
(ii) Focus - no immediate prospect that a loss will ultimately be suffered, but worthy of close attention.
(iii) Under Surveillance - significant credit concerns and some prospect that a loss may ultimately be suffered.
(iv) Impaired - exposures have been assessed individually as impaired.

In order to identify SICR, the Group has adopted a holistic approach covering both qualitative and quantitative indicators of risk. Accordingly, the Group has defined a number of qualitative triggers for the identification of SICR through its Credit policy. These triggers are designed to capture the level of credit risk linked to each financial instrument and are reflected through the internal risk grade proposed by the Group's credit analysts and reviewed / approved by the Credit Committee.

Meanwhile, the Group's quantitative assessment to determine whether a SICR has occurred since initial recognition is based on a ratings-based approach that uses 'Point in Time' (PiT) PDs (i.e. PD in current economic conditions) for the identification of SICR.

In this regard, due to the lack of internal history of defaults, the Group uses a credit risk modelling solution developed by an external vendor to estimate unconditional PiT PDs by:

(i) Benchmarking the obligor's financial statements with those of the underlying model dataset; and
(ii) Applying a qualitative scorecard to adjust the quantitative unconditional PiT PDs to better reflect obligor-specific peculiarities.

3. **Significant accounting policies** - continued

Impairment - continued

Lifetime PDs are determined by estimating the marginal PD for each year over the life of the financial instrument. For example, for a five-year loan, PDs are calculated for each of the five years. The year-1 PD is calculated as the probability of the loan defaulting within the first year of it being issued, whereas the year-2 PD is calculated as the probability of the loan surviving the first year but defaulting in the second year. The same principle of survival applies to the PDs for the remaining years. The summation of marginal PDs results in the derivation of the cumulative lifetime PD term structure. Cumulative lifetime PDs increase at a diminishing rate as the residual life of the loan shortens.

Unconditional PDs refer to the PD term structure based on historical information and prior to the application of the forward-looking scenarios. The Group then applies multiple forward-looking macroeconomic scenarios to the unconditional PiT PD term structure in order to estimate the forward-looking probability weighted conditional PiT PD at an obligor level.

PDs are determined at an obligor-level rather than at a facility-level. Therefore, different facilities with the same obligor originated at the same time are expected to have an identical PD, whereas facilities with the same obligor originated at different time intervals will probably have different PDs, since the credit risk related to an obligor is likely to have changed in the meantime.

For the purposes of the identification of SICR, the forward-looking probability weighted conditional PiT PD estimated by the model is mapped to an implied default rating, which adopts Moody's public ratings agency scale terminology from Caa–C up to AAA.

When performing the SICR assessment, the Group compares the implied rating at origination to the implied rating at the reporting date and determines the difference in notches between them. The Group's staging criteria is therefore deemed to be based on a ratings/notch deterioration approach.

Although the Group has adopted a ratings-based approach (i.e. based on notch deterioration) for its SICR assessment, each implied rating is represented by an underlying PD.

In this regard, a simple or absolute comparison of PDs at initial recognition and at the reporting date is not appropriate to determine the stage of an exposure. All other things kept constant, the PD of a financial instrument is expected to reduce with the passage of time. Thus, in order to take this into consideration, the Group estimates the annualised PD over the remaining life of the financial asset as at the origination date and the annualised PD over the remaining life of the financial asset as at the reporting date. These are then mapped to implied ratings which are used to determine potential SICR events and consequently the credit stage of a financial instrument through a combination of relative and absolute thresholds using the implied credit ratings.

The relative threshold approach involves calculating the magnitude of the difference between the reporting date rating and the origination date rating based on the deterioration in the number of notches between the two ratings. The appropriate stage is determined based on the magnitude of this difference. On the other hand, the stage allocation decision using an absolute threshold is based on the reporting date rating of the instrument.

The quantitative assessment through the Group's implied credit rating staging criteria is considered alongside qualitative SICR triggers and form part of the overall SICR trigger assessment. In this regard, where qualitative SICR triggers are observed by credit analysts, the Group applies a management override to the model, thereby overriding the SICR quantitative assessment made by the model.

3. Significant accounting policies - continued

Impairment - continued

- *Treasury portfolio:*

The provisions of IFRS 9 include a practical expedient to measure impairment allowances using 12-month ECL for financial instruments having low credit risk as at the reporting date. Given that credit ratings are a reflection of possible significant increases in credit risk, the Group simply refers to external credit ratings in order to monitor SICR in relation to its Treasury portfolio, which comprises exposures to which a credit rating has been assigned by Moody's, Fitch and Standard & Poor's. In this regard, an exposure is deemed to have low credit risk if it is assigned an investment grade status by one of these three external credit rating agencies.

Should the credit rating of a financial instrument fall below the investment grade threshold, i.e. BBB (or equivalent) the financial instrument is deemed to have suffered a SICR. As a result, the financial instrument will be re-classified as a Stage 2 exposure, which will impact the measurement of the loss allowance, moving from a 12-month ECL assumption to a lifetime ECL assumption.

- *Local Lending portfolio:*

Similarly to the approach taken for the International Corporate Lending portfolio, the Group categorises exposures within the Local Lending portfolio, that are managed at an individual exposure level, to one of the four internal risk grades. In this regard, the Group's internal risk grades are aligned to the three stages contemplated by IFRS 9.

Financial instruments that:
(i) Have not deteriorated significantly in credit quality since initial recognition must be recognised as either "1-Regular" or "2-Focus" within the Group's internal risk grading system;
(ii) Have incurred a SICR are classified as "3-Under Surveillance", in which case the Group recognises lifetime ECLs; and
(iii) Demonstrate objective evidence of default are classified as "4-Doubtful" and assessed individually for provisioning purposes.

Definition of default

IFRS 9 does not specifically define default, but requires the Group to apply a definition that is consistent with the definition used for internal credit risk management purposes, requiring consideration of qualitative indicators, where appropriate.

IFRS 9 introduces a rebuttable presumption that default does not occur later than when a contractual repayment relating to a financial asset is 90 days past due, unless reasonable and supportable information is available to demonstrate that a more lagging criterion is more appropriate. This presumption has not been rebutted by the Group but is much more relevant for identifying defaulted exposures within the Local Lending portfolio.

The Group has decided to align the IFRS 9 definition of default to the definitions provided in the EBA and BCBS guidelines with the definition used for accounting purposes. In this regard, defaulted exposures are those that satisfy either or both of the following criteria:
(i) material exposures which are past due by more than 90 days;
(ii) the debtor is assessed as unlikely to pay its credit obligations in full without realisation of collateral, regardless of the existence of any past-due amount or of the number of days past due.

3. Significant accounting policies - continued

Impairment - continued

The Group defines a financial asset as credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Therefore, the definitions of credit-impaired and defaults are aligned as far as possible so that Stage 3 represents all loans which are considered defaulted or otherwise credit impaired.

Modified financial assets

The assessment of whether a modification (such as a change in interest rates, currency or the remaining term of the loan) is considered to be significant is critical in determining the accounting implications of modifications to an asset's contractual cash flows. In this regard, when considering a change in the contractual terms, the Group evaluates how the cash flows under the revised terms compare with the cash flows under the original terms of the loan and also takes into consideration qualitative factors. Qualitative considerations include extension of terms, insertion of credit enhancements, changes in interest rates, etc. If the modification is deemed substantial derecognition of the financial instrument is warranted.

When the modification is not substantial enough to result in the derecognition of that financial asset, the Group recalculates the gross carrying amount of the financial asset as the present value of the modified contractual cash flows discounted at the original effective interest rate (or credit-adjusted effective interest rate for Purchased or Originated Credit-Impaired ("POCI") financial assets). The difference is recognised as a modification gain or loss in profit or loss.

When there is a substantial modification to the terms of a financial asset resulting in the derecognition of the existing financial asset and the subsequent recognition of the modified financial asset, the modified asset is considered a 'new' financial asset. A loss is booked in profit or loss (normally as a write-off) since the carrying amount of the new instrument is calculated as the present value of future cash flows discounted at the original effective interest rate.

Forbearance measures

A financial asset is also derecognised if, as a result of the deterioration in the borrower's credit position, the exposure is restructured in such a manner that would result in a write-off of a portion of the debt and the inclusion of equity warrants instead.

Forbearance measures consist of concessions extended to any exposure towards a debtor facing or about to face difficulties in meeting its financial commitments with a view to recover expected principal and interest payments when a borrower is in financial difficulties. Concessions may consist of:

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

Forbearance measures typically result in terms and conditions that are more favourable than those provided initially. The key objective of granting forbearance measures is to pave the way for non-performing borrowers to exit their non-performing status, or to help prevent performing borrowers from reaching a non-performing status.

3. Significant accounting policies - continued

Impairment - continued

The modification of a financial instrument only leads to derecognition if it is significant. In this regard, when the modification of a financial instrument is deemed significant, the new instrument is typically deemed to be credit-impaired as at the modification date and therefore classified as POCI. In this case, the instrument is classified as POCI until derecognition, meaning that lifetime ECLs are required to be measured in relation to that asset until maturity (i.e. no cure is permitted).

However, in those cases where a modification is not significant enough to warrant derecognition the Group performs an assessment of whether the instrument can be classified as performing forborne (i.e. not credit impaired). This can only be the case if the exposure was not deemed to be credit-impaired at the date when the forbearance measures were extended, and the extension of the forbearance measures do not lead the exposure to be classified as credit-impaired. If the Group deems that the obligor will be able to comply with the modified terms, the exposure is deemed performing forborne and generally classified as Stage 2.

Expected credit losses

ECLs are defined as the probability-weighted estimate of credit losses over the expected life of a financial instrument. For each portfolio, the Group calculates ECLs on its financial instruments based on three key inputs, namely: probability of default ("PD"), loss given default ("LGD") and exposure at default ("EAD"). The 12-month ECL is calculated by multiplying the 12-month PD, LGD and EAD. Lifetime ECL is calculated on a similar basis for the entire residual life of the exposure.

Probability of Default

Since the PD is a probability measure used to capture the likelihood that a borrower will default over a defined period of time, this is estimated at a borrower level. The PDs for the Group's Treasury and International Corporate Lending portfolios are estimated based on statistical models developed by external vendors. On the other hand, due to the lack of internally available history of defaults within the local lending portfolio, the PDs for the Group's Local Lending portfolio are estimated based on observations of other portfolios within the market.

Loss Given Default

The LGD of an exposure measures the size of the estimated loss (as a proportion of the total EAD) that is expected to materialise in the event that a borrower defaults. In contrast with PDs, LGDs are estimated at a facility level. Whilst linked to the general credit risk of the obligor, recovery rates are also impacted by the relative ranking of a particular facility within the obligor's debt structure.

The Group's Treasury portfolio consists of covered bonds, bonds issued by supranational organisations and sovereign bonds. For its supranational exposures and sovereign exposures, the Group uses the LGD value obtained from the statistical model developed by an external vendor while for covered bonds the LGD is aligned with regulatory standards.

For all of its assets within its International Corporate Lending portfolio, the Group also uses the external vendor model to estimate recovery by benchmarking exposure-specific characteristics with the underlying dataset.

3. Significant accounting policies - continued

Impairment - continued

Finally, the LGD used for the Local Lending portfolio is driven by the loan-to-value ratio of the individual facilities, whilst also taking into consideration other factors such as costs to sell, valuation haircuts and the time value of money.

Exposure at Default

The EAD is used to estimate the Group's expected exposure at the time of default of an obligor, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, and any expected drawdowns on committed facilities.

The maximum period over which ECLs are measured is the maximum contractual period over which the Group is exposed to credit risk. For exposures within the Treasury and Local Lending portfolios, the maturity date is deemed to be equal to the contractual maturity of the exposure. However, for its International Corporate Lending portfolio, the Group makes use of behavioural rather than contractual maturity, thereby reflecting expectations on the exercise of prepayment or extension options.

To measure the EAD of off-balance sheet exposures, including loan commitments, the Group estimates the amount that a borrower will have drawn down by the time of default. Therefore, the Group estimates the part of the undrawn facility that the borrower is expected to convert into a funded amount typically referred to as a credit conversion factor (CCF).

Forward looking information

The recognition and measurement of ECL requires the incorporation of multiple forward-looking economic conditions into the ECL estimates to meet the measurement objective of IFRS 9.

In this regard, the Group uses the external vendor model solution for all of its portfolios in order to capture the level of systemic risk linked to an obligor, and to estimate forward-looking probability weighted conditional PiT PDs using multiple forecasts of macroeconomic conditions.

IFRS 9 does not require forecasts of future conditions to extend over the entire expected life of the financial instrument in question. The Group uses macroeconomic forecasts for up to 20 quarters to estimate a probability-weighted ECL. For maturities that go beyond this 5-year period, the Group extrapolates projections from available data.

3. Significant accounting policies - continued

Forward looking information - continued

- *International Corporate Lending and Treasury portfolios*

The Group applies five macroeconomic scenarios, to the unconditional PD and LGD term structures for the estimation of ECLs for its Stage 1 and Stage 2 exposures within its International Corporate Lending and Treasury portfolios. These macroeconomic scenarios are linked to a set of macroeconomic variables, including country-level variables such as country-specific GDP, that are deemed to have the highest correlation to the Group's portfolio.

In line with the requirements of IFRS 9, the Group assigns a probability weight, based on management judgement, to each of the scenarios considered in the estimation of ECLs. Due to the high level of subjectivity involved, decisions relating to the selection of scenarios, probabilities and multiples are subject to scrutiny through the Group's governance structure around credit risk.

- *Local Lending portfolio*

The Group uses the same conceptual framework as that used for the International Corporate Lending and Treasury portfolios to estimate unbiased and probability-weighted ECLs based on forward-looking macroeconomic scenarios for exposures classified in Stage 1 and 2.

The key difference lies within the number of scenarios used for Local Lending exposures, since the Group estimates unbiased and probability-weighted ECLs using three (rather than five) macroeconomic scenarios, due to the lack availability of a full set of five scenarios for the local market.

Presentation of ECL in the Statement of Financial Position

The loss allowance for financial assets that are measured at amortised cost is presented as a deduction from the gross carrying amount of the assets. On the other hand, for financial assets measured at FVOCI, the loss allowance is presented within other comprehensive income rather than against the carrying amount of the assets. Therefore, no deduction is made from the carrying amount of financial assets measured at FVOCI, which is always shown at fair value.

Hedge Accounting

The general hedge accounting requirements aim to simplify hedge accounting, creating a stronger link with risk management strategy and permitting hedge accounting to be applied to a greater variety of hedging instruments and risks, but do not explicitly address macro hedge accounting strategies.

In this regard, IFRS 9 allows entities to continue applying IAS 39 hedge accounting requirements of IAS 39. In this regard, the Group has opted to maintain the accounting policy on hedge accounting in line with the provisions of IAS 39 on all of its hedging relationships.

4. Critical accounting estimates and judgements in applying the Group's accounting policies

Estimates and judgements are continually evaluated and based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. These estimates and assumptions present a risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. The Group's management also makes judgements, apart from those involving estimations, in the process of applying the entity's accounting policies that may have a significant effect on the amounts recognised in the financial statements.

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

The significant judgements made by management in applying the Group's accounting policies and the key sources of estimation uncertainty impacting the preparation of these interim financial statements are the same as those that applied to the preparation of the financial statements as at and for the year ended 31 March 2018, as disclosed in those financial statements.

5. Operating segments

The Group has a single reportable segment represented by the investment in high credit quality collateralised instruments together with corporate lending and wealth management business. The Group's products and services and geographical areas are comparable to those as at 31 March 2018. Information about financial risks, credit concentration by sector and location, together with revenues from the single reportable segment can be obtained from the financial statements for the year ended 31 March 2018. The investment portfolio is spread across a large number of exposures diversified across the following categories: government, financial institutions and corporates.

6. Taxation

Income tax expense is recognised based on management's best estimate of the weighted average annual income tax rate expected for the financial year applied to the pre-tax income of the interim period.

The effective consolidated tax rate in the financial period ended 30 September 2018 is attributable to the increase in deferred tax assets recognised in Malta on unutilised notional interest deduction and expected credit losses using a 35% effective tax rate. The effective consolidated tax rate in the financial period ended 30 September 2017 is mainly attributable to the deferred tax recognised, on the losses registered by MeDirect Belgium throughout this financial period, at a tax rate that is higher than the effective tax rate applicable on the profits generated by MeDirect Malta. Furthermore, throughout the financial period ended 30 September 2017, expenditure reflected in the accounting records of MeDirect Belgium in relation to its international corporate lending, that is reversed on consolidation, resulted in a lower effective tax rate.

7. Financial instruments

7.1 Reconciliation of the gross amount of financial assets at 31 March 2018 and 1 April 2018

	IAS 39 Measurement category	IAS 39 Gross amount	Reclassification	Remeasurement	IFRS 9 Gross amount	IFRS 9 Measurement category
		€000	€000	€000	€000	
Financial assets						
Balances with Central Banks	Amortised cost (Loans and receivables)	103,543	-	-	103,543	Amortised cost
Investments						
- Debt and other fixed income instruments	FVOCI (Available-for-sale)	560,245	(399,347)	-	160,898	FVOCI
- Debt and other fixed income instruments		-	399,347	2,208	401,555	Amortised cost
Loans and advances to financial institutions	Amortised cost (Loans and receivables)	113,623	-	-	113,623	Amortised cost
Loans and advances to customers	Amortised cost (Loans and receivables)	1,724,354	-	-	1,724,354	Amortised cost
		2,501,765	**-**	**2,208**	**2,503,973**	

The differences in the measurement category and the gross amount of financial assets in accordance with IAS 39 and IFRS 9 at the date of initial application, 1 April 2018, are analysed through the following elements:

- Reclassifications, reflecting the movement of balances between categories of financial assets with no impact or shareholders' equity. There is no change to the carrying value of financial instruments as a result of reclassifications.
- Remeasurements, which are adjustments due to changes to the measurement bases, resulting in a change to the carrying value of the financial instrument, with a corresponding impact (net of tax) on shareholders' equity.

Upon initial application of IFRS 9, the Group decided to split the debt securities, all of which were classified as available-for-sale financial instruments and measured at FVOCI under IAS 39, into two portfolios, in order to reflect the objective of the respective business models.

One portfolio of debt securities was reclassified to financial assets measured at amortised cost given that the Group considers that these debt securities are held within a business model whose objective is achieved through the collection of contractual cash flows, which represent SPPI.

The rest of the debt securities classified as available-for-sale under IAS 39 will continue to be measured at FVOCI under IFRS 9, since these are held within a business model whose objective is achieved by both collecting contractual cash flows, which represent SPPI, and selling financial assets.

There were no changes to the classification and measurement of financial liabilities.

7. Financial instruments - continued

7.2 Reconciliation of impairment allowances under IAS 39 at 31 March 2018 to expected credit losses under IFRS 9 at 1 April 2018

The following table reconciles the impairment allowance as at 31 March 2018 measured in accordance with the IAS 39 incurred loss model to the new impairment allowance measured in accordance with the IFRS 9 expected loss model as at 1 April 2018:

	IAS 39 Impairment allowance	Remeasurement	IFRS 9 Expected credit losses
	€000	€000	€000
Measurement category			
Loans and receivables (IAS 39) / Financial assets at amortised cost (IFRS 9)			
Loans and advances to customers	22,638	10,736	33,374
Available-for-sale financial instruments (IAS 39) / Financial assets at amortised cost (IFRS 9)			
Investments	-	23	23
Available-for-sale financial instruments (IAS 39) / Financial assets at FVOCI (IFRS 9)			
Investments	-	9	9
Loan commitments and financial guarantee contracts	-	1,022	1,022
	22,638	**11,790**	**34,428**

7.3 Summary of financial instruments to which the impairment requirements in IFRS 9 are applied

	At 30 September 2018			At 1 April 2018		
	Gross amount	Allowance for ECL	Net carrying amount	Gross amount	Allowance for ECL	Net carrying amount
	€000	€000	€000	€000	€000	€000
Loans and advances to financial institutions and customers at amortised cost	**1,999,256**	**30,475**	**1,968,781**	1,838,008	33,374	1,804,634
Investments and other financial assets measured at amortised cost	**496,973**	**18**	**496,955**	539,776	23	539,753
Investments measured at FVOCI	**142,482**	**5**	**142,477**	160,898	9	160,889
Total gross amount on balance sheet	**2,638,711**	**30,498**	**2,608,213**	2,538,682	33,406	2,505,276
Commitments to extend credit, guarantees, and similar commitments (excl. leases)	**555,659**	**1,213**	**554,446**	559,904	1,022	558,882
Total nominal amount off-balance sheet[1]	**555,659**	**1,213**	**554,446**	559,904	1,022	558,882

[1] Represents the maximum amount at risk should the contracts be fully drawn upon and client default.

7. **Financial instruments** - continued

7.4 Summary of credit risk by stage distribution and ECL coverage at 30 September 2018

	Gross carrying/nominal amount			Allowance for ECL		
	Stage 1	**Stage 2**	**Stage 3**	**Stage 1**	**Stage 2**	**Stage 3**
	€000	**€000**	**€000**	**€000**	**€000**	**€000**
Loans and advances to financial institutions and customers at amortised cost	1,579,632	356,890	62,734	10,575	6,092	13,808
Investments and other financial assets measured at amortised cost	496,973	-	-	18	-	-
Investments measured at FVOCI	142,482	-	-	5	-	-
Commitments to extend credit, guarantees, and similar commitments (excl. leases)	466,616	89,043	-	744	469	-
At 30 September 2018	**2,685,703**	**445,933**	**62,734**	**11,342**	**6,561**	**13,808**

7.5 Reconciliation of movement in allowances for expected credit losses

	€000
Period ended 30 September 2018	
At 1 April 2018	34,428
ECL income statement charge for the period	4,600
Assets written off	(7,759)
Exchange and other movements	442
At 30 September 2018	31,711

The Group was notified on 30 November 2018 that a debtor client had entered into an agreement that is expected to lead to the successful disposal of its business during the first quarter of 2019. The reported price at which this disposal is expected to occur would lead to the recovery, in total or to a material extent, of credit losses amounting to €3.5 million that have been recognised by the Group in earlier accounting periods on the account in question; and of unaccrued interest due thereon. The Group is awaiting further information to enable it to better assess the favourable impact of this transaction, which will be reflected in its results for the full financial year ending on 31 March 2019.

7.6 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 Group has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Group measures the fair value of an instrument using quoted price in an active market for that instrument. A market is regarded as active if the transactions for the asset or liability takes place with sufficient frequency and volume to provide pricing information on an ongoing basis. The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads.

7. **Financial instruments** - continued

7.6 Fair value measurement - continued

If there is no quoted price in an active market, then the Group 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.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Group measures assets and long positions at a bid price and liabilities and short positions at an ask price.

7.6.1 Fair value hierarchy

The Group measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- Level 1: inputs that are quoted market prices (unadjusted) in active markets for identical instruments.

- Level 2: inputs other than quoted market prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data. Financial instruments which are generally included in this category include over-the-counter derivatives where the fair value is based on observable inputs.

- Level 3: inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

7.6.2 Use of valuation techniques

In the event that the market for a financial instrument is not active, a valuation technique is used. Valuation techniques may incorporate assumptions about factors that other market participants would use in their valuations, including:

- the likelihood and expected timing of future cash flows on the instrument;
- selecting an appropriate discount rate for the instrument; and
- judgement to determine what model to use to calculate fair value in areas where the choice of valuation model is particularly subjective.

A range of valuation techniques is employed, dependent on the instrument type and available market data. Most valuation techniques are based upon discounted cash flow analyses, in which expected future cash flows are calculated and discounted to present value using a discounting curve. Prior to considering credit risk, the expected future cash flows may be known, as would be the case for the fixed leg of an interest rate swap, or may be uncertain and require projection, as would be the case for the floating leg of an interest rate swap. Projection utilises market forward curves, if available.

Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premiums used in estimating discount rates, bond and foreign currency exchange rates and expected price volatilities and correlations.

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

7. Financial instruments - continued

7.6 Fair value measurement - continued

7.6.2 Use of valuation techniques - continued

The Group uses widely recognised valuation models for determining the fair value of common and simple financial instruments, such as interest rate and currency swaps that use only observable market data and require minimal management judgement and estimation.

Fair value of investment securities in inactive markets are based on:

- quoted prices of similar instruments, performing numerical procedures such as interpolation when input values do not directly correspond to the most active market trade parameters; or
- price quotations in respect of orderly transactions between market participants provided by reputable dealers.

7.6.3 Financial instruments measured at fair value

The following table analyses financial instruments measured at fair value at the end of the reporting period, by the respective levels within the fair value hierarchy into which the respective fair value measurement is categorised. The fair value amounts are based on the carrying amounts reflected in the condensed consolidated interim statement of financial position.

	Level 1	**Level 2**	**Level 3**	**Total**
	€000	**€000**	**€000**	**€000**
As at 30 September 2018				
Assets				
Investments				
- FVOCI financial assets	142,477	-	-	**142,477**
Derivative financial instruments	-	1,046	-	**1,046**
Total financial assets	**142,477**	**1,046**	**-**	**143,523**
Liabilities				
Derivative financial instruments	-	2,297	-	**2,297**
Total financial liabilities	**-**	**2,297**	**-**	**2,297**

	Level 1	**Level 2**	**Level 3**	**Total**
	€000	**€000**	**€000**	**€000**
As at 31 March 2018				
Assets				
Investments				
- FVOCI financial assets	560,245	-	-	**560,245**
Derivative financial instruments	-	470	-	**470**
Total financial assets	**560,245**	**470**	**-**	**560,715**
Liabilities				
Derivative financial instruments	-	3,581	-	**3,581**
Total financial liabilities	**-**	**3,581**	**-**	**3,581**

7. Financial instruments - continued

7.6 Fair value measurement - continued

7.6.3 Financial instruments measured at fair value - continued

As at 30 September 2018 and at 31 March 2018 the fair value of the FVOCI financial assets represents the closing bid price quoted in an active market.

Level 2 instruments principally comprise derivatives held for risk management that are fair valued based on valuation models with the key methodology utilised comprising the calculation of the net present value of a series of expected cash flows, taking into account the different terms of each specific contract/instrument (discounted cash flow approach). These models use as their basis independently sourced market parameters including, for example, interest rate yield curves. Market parameters are either directly observable or are implied from observable instrument prices. The model may perform numerical procedures in respect of pricing such as interpolation when input values do not directly correspond to the most active market trade parameters.

7.6.4 Transfers between levels

The Group recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the transfer has occurred.

There were no transfers between Level 1 and Level 2 of the fair value hierarchy during the period from 1 April 2018 to 30 September 2018 and during the financial year ended 31 March 2018.

7.7 Financial instruments not measured at fair value

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the respective level within the fair value hierarchy into which the respective fair value measurement is categorised. This table includes only financial instruments in respect of which fair value is estimated to be materially different than the carrying amounts.

MeDirect Malta Group	**Level 1 €000**	**Level 2 €000**	**Level 3 €000**	**Total fair values €000**	**Total carrying amount €000**
As at 30 September 2018					
Assets					
Investments	400,141	-	-	400,141	**402,339**
Loans and advances to customers	-	1,257,729	-	1,257,729	**1,257,464**
Total financial assets	**400,141**	**1,257,729**	**-**	**1,657,870**	**1,659,803**
Liabilities					
Subordinated liabilities	69,130	-	-	69,130	**66,876**
Total financial liabilities	**69,130**	**-**	**-**	**69,130**	**66,876**
As at 31 March 2018					
Assets					
Loans and advances to customers	-	1,149,073	-	1,149,073	**1,151,819**
Total financial assets	**-**	**1,149,073**	**-**	**1,149,073**	**1,151,819**
Liabilities					
Subordinated liabilities	70,309	-	-	70,309	**66,949**
Total financial liabilities	**70,309**	**-**	**-**	**70,309**	**66,949**

7. Financial instruments - continued

7.7 Financial instruments not measured at fair value - continued

The Level 1 fair values reflected in the preceding tables consist of quoted market prices of debt securities issued which are traded in active markets.

The Level 2 fair value disclosures mainly comprise price quotations in respect of internationally traded loans and advances, consisting of the Group's international loan book with foreign corporates.

The Group's financial instruments not measured at fair value comprise balances with Central Banks, loans and advances to financial institutions and customers, debt securities and amounts owed to financial institutions and customers. The fair values of these financial assets and liabilities are not disclosed given that the carrying amount is a reasonable approximation of fair value because these are either re-priced to current market rates frequently or are short-term in nature.

'Loans and advances to financial institutions' amounting to €111.4 million (31 March 2018: €113.6 million) which represent 100% of all loans and advances to financial institutions, re-price or mature in less than one year; hence their fair value is not deemed to differ materially from their carrying amount at the reporting date.

Loans and advances to customers forming part of the international lending book amounting to €537 million (31 March 2018: €468 million), net of expected credit losses, have not been reflected in the preceding tables. These mainly re-price within three months; hence their fair value is not deemed to differ materially from their carrying amount at the reporting date.

The carrying amount for local loans and advances to customers amounting to €62.6 million (31 March 2018: €81.5 million) approximates their fair value because these loans are re-pricable at the Group's discretion.

All trade receivables amounting to €0.4 million (31 March 2018: €2.7 million) are stated net of expected credit losses, within loans and advances to customers. Hence their fair value is not deemed to differ materially from their carrying amount at the reporting date.

Fair values are estimated using discounted cash flows, applying market rates. These estimates are considered Level 2 fair value estimates.

The majority of the 'Amounts owed to financial institutions' of the Group amounting to €248.1 million (31 March 2018: €126.4 million) and 'Amounts owed to customers' of the Group amounting to €1.3 billion (31 March 2018: €1.5 billion), sourced from the Maltese and Belgian markets, re-price or mature in less than one year; hence their fair value is not deemed to differ materially from their carrying amount at the reporting date. Fair values of these liabilities are estimated using discounted cash flows, applying current rates offered for deposits of similar remaining maturities. These are considered Level 2 fair value estimates. The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount payable is required to be paid.

8. Capital and reserves

Share capital

	30 September 2018 No.	31 March 2018 No.
Issued and fully paid up:		
Ordinary 'A' shares of €1 each	**117,450,106**	117,450,106
Ordinary 'B' shares of €1 each	**1**	1
	117,450,107	**117,450,107**

As at 30 September 2018 and 31 March 2018, the authorised share capital consisted of 299,999,999 Ordinary 'A' shares of €1 each and 1 Ordinary 'B' share of €1 each.

Rights and entitlements attached to ordinary shares

The holders of Ordinary 'A' shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at general meetings of the Bank. Ordinary 'B' shareholders are not entitled to vote or to receive any dividends distributed.

Share premium

Share premium as at the reporting date represents the issue of shares in prior periods as follows:

			Share premium	
Issue date	Number of shares	Premium per share €	30 September 2018 €000	31 March 2018 €000
10 August 2010	10,000,000	0.9155	**9,155**	9,155
29 September 2010	19,119,470	0.2254	**4,309**	4,309
			13,464	13,464

Shareholders' contributions

The terms and conditions of the contributions granted by MeDirect Group Limited render this instrument equity in nature in accordance with the requirements of IAS 32: Financial Instruments - Presentation:

- The Bank has no obligation to bear any servicing cost or transfer any economic benefits of any kind to the Contributor or any other person in return; and
- The Bank has no obligation to repay the contributions.

The contributions are eligible as own funds in terms of the Capital Requirements Regulation.

By virtue of a shareholders' resolution dated 30 May 2018, MeDirect Bank Malta plc approved the repayment of the shareholder contribution equivalent to €7.23 million.

By virtue of an extraordinary resolution dated 30 May 2018, the Bank accepted a shareholders' net contribution of €3.1 million.

8. Capital and reserves - continued

Reserve for general banking risks

Banking Rule ("BR") 09 issued by the MFSA requires banks in Malta to hold additional reserves for general banking risks in respect of non-performing loans. This reserve is required to be funded from retained earnings. As at 30 September 2018, the reserve for general banking risks of the Group was equivalent to €1.9 million (31 March 2018: €1.7 million). This reserve, which is distributable subject to the formal consent of the Banking Regulator, represents 100% of the regulatory allocation by virtue of paragraph 38 of the Banking Rule.

Other reserves

a) Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of FVOCI financial assets, excluding impairment losses, until the investment is derecognised, net of deferred taxation.

b) Legal reserve

According to Article 319 of the Company Code in Belgium, at least 5% of the retained earnings of MeDirect Belgium should be set aside as a statutory legal reserve until this reserve is equivalent to 10% of the capital of MeDirect Belgium. This statutory legal reserve was equivalent to €77 thousand as at 30 September 2018 and 31 March 2018.

Dividends

All reserves at the reporting date, except for the Bank's retained earnings and the shareholders' contribution, are non-distributable.

9. Contingent liabilities and commitments

Guarantee obligations

As at 30 September 2018, the Group held cash secured guarantee obligations amounting to €8.6 million (31 March 2018: €5.2 million).

Transfer of tax losses in Belgium

The tax authorities in Belgium are currently reviewing the transfer of tax losses from the former Belgian branch of MeDirect Malta to MeDirect Belgium amounting to €12.3 million and will likely challenge the transfer of these losses. As at 30 September 2018 the Group has a deferred tax asset of €3.2 million (31 March 2018: €3.1 million) in relation to the unutilised tax losses of MeDirect Belgium. On the basis of specialist advice obtained from a number of independent tax advisors in Belgium, the Group is confident that this transfer of tax losses was justified and believe that no adjustment to the deferred tax asset is deemed necessary at the end of the reporting period as it is of the opinion that the position of the Group will be ultimately upheld.

Non-cancellable operating lease commitments

As at the reporting date, the future minimum lease payments under non-cancellable operating lease agreements amount to €6.8 million (31 March 2018: €7.5 million).

9. Contingent liabilities and commitments - continued

Commitments to lend

Commitments to lend represent undrawn formal standby facilities, credit facilities and other similar commitments to lend. As at 30 September 2018, undrawn facilities on term loans amounted to €52.5 million (31 March 2018: €74.7 million). In addition the Group had commitments amounting to €433.4 million (31 March 2018: €361.8 million) under revolving credit facilities.

10. Related party transactions

There were no significant transactions with related parties during the six month period ended 30 September 2018 which would significantly alter the balances with related parties from those disclosed in the annual report for the year ended 31 March 2018.

11. Events after the reporting date

The Group was notified on 30 November 2018 that a debtor client had entered into an agreement that is expected to lead to the successful disposal of its business during the first quarter of 2019. The reported price at which this disposal is expected to occur would lead to the recovery, in total or to a material extent, of credit losses amounting to €3.5 million that have been recognised by the Group in earlier accounting periods on the account in question; and of unaccrued interest due thereon. The Group is awaiting further information to enable it to better assess the favourable impact of this transaction, which will be reflected in its results for the full financial year ending on 31 March 2019.

Independent auditor's review report

To the Board of Director MeDirect Bank (Malta) p.l.c.

Report on the review of the condensed consolidated interim financial statements

Introduction
We have reviewed the accompanying condensed consolidated interim statement of financial position of MeDirect Bank (Malta) p.l.c. as at 30 September 2018, the related condensed consolidated statement of comprehensive income, changes in equity and cash flows for the six-month period then ended and the explanatory notes ('interim financial information'). The directors are responsible for the preparation and fair presentation of this interim financial information in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU applicable to interim financial reporting (International Accounting Standard 34 'Interim Financial Reporting'). Our responsibility is to express a conclusion on this condensed consolidated interim financial information based on our review.

Scope of review
We conducted our review in accordance with International Standard on Review Engagements 2410, 'Review of Interim Financial Information Performed by the Independent Auditor of the Entity'. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion
Based on our review, nothing has come to our attention that causes us to believe that the accompanying condensed consolidated interim financial information is not prepared, in all material respects, in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU applicable to interim financial reporting (International Accounting Standard 34 'Interim Financial Reporting').

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F Axisa

Fabio Axisa
Partner

3 December 2018