Bank of Sydney

Bank of Sydney Ltd
ABN 44 093 488 629
Annual Financial Report
For the year ended
31 December 2018

Table of contents

Bank of Sydney Ltd
Directors' report
For the year ended 31 December 2018

The Directors present their report together with the financial report of the Bank of Sydney Ltd ("the Bank" and "the Consolidated Entity"), for the year ended 31 December 2018 and the audit report thereon.

Directors
The Directors of the Consolidated Entity at any time during or since the end of the financial year are:

Dr Nicholas Pappas AM
Chairman and Non-Executive Independent Director
Appointed 26 March 2001

Dr Nicholas Pappas is a Sydney lawyer in private practice. In addition to his Board role, he serves on the Bank's Board Audit Committe and Board Remuneration Committee. He is Chairman of South Sydney District Rugby League Football Club Limited ('the Rabbitohs') and South Sydney Members Rugby League Club Limited. He also serves on the Boards of the Steve Waugh Foundation - Australia, the Hellenic Club Limited and Melbourne's Hellenic Museum. Dr Pappas is Secretary of the Greek Orthodox Archdiocesan Council and Trustee of the Greek Orthodox Archdiocese of Australia Consolidated Trust. He was appointed to the General Division of the Order of Australia (AM) in 2013.

Mr Greg Gav
Non-Executive Independent Director
Appointed 31 March 2005

Mr Gav is a member of the Board Risk Management Committee. He is a Sydney Based property developer and entrepreneur. He is a Director of Mars Property Group.

Mr Nikolas T Hatzistergos
Non-Executive Independent Director
Appointed 28 August 2006

Mr Hatzistergos is the Chairman of the Board Audit Committee and a member of the Board Remuneration Committee. He is also a Managing Director of William Buck (NSW) Pty Ltd and Chairman of William Buck International Limited. He is a Director at St Basils Homes and Hellenic Club Limited and has been elected as a Member of the Governing Council and Management Board – Praxity (AISBL). He is a Director and Chairman of the Audit and Finance Committee for South Sydney District Rugby League Football Club Limited.

Hon Steve Bracks AC
Non-Executive Independent Director
Appointed 18 May 2011

The Hon Steve Bracks AC was Premier of Victoria for eight years. He now advises several leading Australian finance and service sector corporations. Mr Bracks also holds two major honorary positions: an Adviser to the Prime Minister of Timor-Leste; and Honorary Chair of The Union Education Foundation. He is Chairman of the superannuation fund Cbus; a non – executive Director of Jardine Lloyd Thomson Australia; Chairman of AFL SportsReady; Chairman of The Kardinia Park Stadium Trust; and a member of the Monash Business School Business Advisory Board (BAB); the Australian Republic Movement’s Republican Advisory Panel (RAP); and the West of Melbourne Alliance Board.

Mr Fouad Chaker
Non-Executive Director
Appointed 28 February 2011

Mr Chaker holds the position of Assistant General Manager - Commercial Banking Division, Bank of Beirut s.a.l.

Mr Hikmat El-Bikai
Non-Executive Alternate Director to Mr. Fouad Chaker
Appointed 18 May 2011 (resigned 15/3/2019)

Mr El-Bikai holds the position of Senior Executive Officer - Credit and Legal Affairs, Bank of Beirut s.a.l.

Mr. Roger Dagher
Non-Executive Director
Appointed 7 July 2016

Mr Dagher is a member of the Board Risk Management Committee, Board Remuneration Committee and Board Audit Committee. He also holds the position of Group Chief Financial Officer at Bank of Beirut s.a.l.

Mr. Ben Edney
Non-Executive Director
Appointed 15 March 2017

Mr. Ben Edney is Chairman of the Board Risk Management Committee. Mr. Edney is an accomplished finance industry expert with over 25 years domestic and international experience with National Australia Bank and KPMG in advisory, risk and restructuring. He has strong strategic and technical skills across corporate finance, restructuring and risk having led NAB's problem loan management throughout the global financial crisis. Mr. Edney is also chairman of Williams Holdings Limited in New Zealand and Nimble Money Limited.

Directors' Meetings
The number of Directors' meetings (including meetings of Committees of Directors) and number of meetings attended by each of the Directors during the financial year were:

Directors	Board Operations		Board Audit Committee		Board Risk Management Committee		Board Remuneration Committee	
	No. of meetings eligible to attend	No. of meeting attended	No. of meetings eligible to attend	No. of meeting attended	No. of meetings eligible to attend	No. of meeting attended	No. of meetings eligible to attend	No. of meeting attended
N.G. Pappas AM	6	4	6	4	-	-	1	1
N.T. Hatzistergos	6	5	6	5	-	-	1	1
G.Gav	6	5	-	-	6	5	-	-
H.S. Bracks AC	6	5	-	-	-	-	-	-
F. Chaker	6	6	-	-	-	-	-	-
H. El-Bikai	-	-	-	-	-	-	-	-
R. Dagher	6	6	6	6	6	6	1	1
B. Edney	6	6	-	-	6	6	-	-

Prior approval from the Chairman was received for all directors regarding their apologies at Board and Board Committee Meetings.

Company Secretary

Mrs. Vougamalis was appointed as Company Secretary in May 2011, she also holds the position of Chief Customer Officer and has worked in various roles throughout the Bank since 2006 including Risk Management and Credit. She holds a Bachelor's degree in Business from the University of Technology Sydney and holds a diploma in Applied Corporate Governance from the Governance Institute of Australia. She is an Associate of the Governance Institute of Australia and a registered Justice of the Peace.

Principal Activities

Principal activities of the Consolidated Entity are the provision of general banking services.

Results

The net profit of the Consolidated Entity was $11,219,000 (2017: profit of $11,005,000). The result included reversal of provisions for impairment losses for Loans and Advances of $3,799,000 (2017: $176,000). At 31 December 2018, the Consolidated Entity's net loan portfolio was $1,758m (2017: $1,474m) and its customer deposits were $1,957m (2017: $1,733m). This represents an increase of 19% in loans and an increase of 13% in deposits when compared to the balances as at 31 December 2017.

Dividends

No dividends have been paid or declared since the start of the financial year.

The Directors do not recommend payment of a dividend in respect of the financial year ended 31 December 2018 (2017: Nil).

State Of Affairs

No significant changes in the state of affairs of the Consolidated Entity occurred during the financial year.

Subsequent Events

On 1 March 2019 the Bank entered into an agreement to purchase 62 Pitt Street, located in the Central Business District of Sydney, for $50m.

Other than the matter mentioned above, there has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the Directors of the Consolidated Entity, to affect significantly the operations of the Consolidated Entity, the results of those operations, or the state of affairs of the Consolidated Entity, in subsequent financial years.

Likely Developments

The Directors believe on reasonable grounds that inclusions in this report of further information regarding likely developments in the operations of the Consolidated Entity and the expected results of those operations in future financial years is likely to result in unreasonable prejudice to the Consolidated Entity. Accordingly, this information has not been disclosed in this report.

Auditor's Independence Declaration

The auditor's independence declaration is set out on page 7 of the annual financial report.

Bank of Sydney Ltd
Directors' report (continued)
For the year ended 31 December 2018

Indemnification and Insurance of Officers
The Consolidated Entity has agreed to indemnify the Directors and certain senior executives, against all liabilities to another person (other than the Consolidated Entity or a related body corporate) that may arise from their position with the Consolidated Entity, except where the liability arises out of conduct involving a lack of good faith. The agreement stipulates that the Consolidated Entity will meet the full amount of any such liabilities, including costs and expenses.

Rounding Off
The Consolidated Entity is of a kind referred to in ASIC 2016/191 dated 24 March 2016 and in accordance with that Class Order, amounts in the financial report and Director's report have been rounded off to the nearest thousand dollars, unless otherwise stated.

Signed in accordance with the resolution of the Directors made pursuant to s.298(2) of the Corporations Act 2001.

On behalf of the Directors:

Nicholas Pappas
Chairman

Sydney, 17 April 2019

Deloitte.

Deloitte Touche Tohmatsu
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17 April 2019

The Board of Directors
Bank of Sydney Ltd
219-223 Castlereagh Street
Sydney NSW 2000

Dear Board Members

Bank of Sydney Ltd

In accordance with section 307C of the *Corporations Act 2001*, I am pleased to provide the following declaration of independence to the directors of Bank of Sydney Ltd.

As lead audit partner for the audit of the financial statements of Bank of Sydney Ltd for the financial year ended 31 December 2018, I declare that to the best of my knowledge and belief, there have been no contraventions of:

(i) the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and

(ii) any applicable code of professional conduct in relation to the audit.

Yours sincerely

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

M Stretton

Mark Stretton
Partner
Chartered Accountants

Bank of Sydney Ltd
Consolidated Statement of Profit and Loss
For the year ended 31 December 2018

	Note	2018 $'000	2017 $'000
Interest income	2	83,054	75,279
Interest expense	3	(41,517)	(36,955)
Net interest income		41,537	38,324
Non-interest income	4	7,976	8,911
Net operating income		49,513	47,235
Operating expenses	5	(37,231)	(31,633)
Reversal of/(Provision for) impairment losses on financial assets measured at amortised cost	11	3,799	176
Profit before income tax		16,081	15,778
Income tax expense	6	(4,862)	(4,773)
Profit for the year		11,219	11,005
Attributable to:			
Equity holders of the Consolidated Entity		**11,219**	**11,005**
Profit for the year		**11,219**	**11,005**

The Consolidated Statement of Profit and Loss is to be read in conjunction with the notes to and forming part of the financial report set out on pages 13 to 71.

Bank of Sydney Ltd
Consolidated Statement of Profit and Loss
and Other Comprehensive Income
For the year ended 31 December 2018

	Note	2018 $'000	2017 $'000
Profit for the year		**11,219**	**11,005**
Cash flow hedges:			
Effective portion of changes in fair value		(1,128)	99
Net amount transferred to statement of profit and loss		31	37
Other comprehensive income for the period, net of income tax	24	(1,097)	136
Total comprehensive income for the year		**10,122**	**11,141**
Attributable to:			
Equity holders of the Consolidated Entity		10,122	11,141
Total comprehensive income for the year		**10,122**	**11,141**

The Consolidated Statement of Profit and Loss and Other Comprehensive Income is to be read in conjunction with the notes to and forming part of the financial report set out on pages 13 to 71.

Bank of Sydney Ltd
Consolidated Statement of Financial Position
For the year ended 31 December 2018

	Note	2018 $'000	2017 $'000
Assets			
Cash and liquid assets	7	57,618	122,047
Due from other financial institutions	8	78,949	26,571
Investment at amortised cost	9	388,042	462,735
Loans and advances	10(a)	1,757,844	1,474,444
Derivative financial assets	19	85	3,361
Intangible assets	12	7,990	5,387
Plant and equipment	13	3,711	3,524
Deferred tax assets	14	2,850	1,773
Other assets	15	5,343	4,649
Total assets		**2,302,432**	**2,104,491**
Liabilities			
Due to other financial institutions	16	48,147	6,245
Securities sold and under repurchase agreements	17	-	85,173
Deposits	18	1,956,601	1,732,675
Derivative financial liabilities	19	5,168	120
Provisions	20	2,958	2,711
Other liabilities	21	4,910	9,325
Total liabilities		**2,017,784**	**1,836,249**
Net assets		**284,648**	**268,241**
Equity			
Contributed equity	22	210,000	200,000
Retained profits	23	70,105	60,553
Reserves	24	4,543	7,688
Total equity		**284,648**	**268,241**

The Consolidated Statement of Financial Position is to be read in conjunction with the notes to and forming part of the financial report set out on pages 13 to 71.

Bank of Sydney Ltd
Consolidated Statement of Cash Flows
For the year ended 31 December 2018

	Note	2018 $'000	2017 $'000
Cash flows from operating activities			
Interest and commission receipts		89,298	84,223
Interest payments		(39,629)	(38,038)
Cash payments to employees and suppliers		(34,470)	(30,266)
Bad debts recovered/(written off)		-	162
Income Tax Paid		(5,305)	(5,562)
		9,894	10,519
(Increase) / decrease in operating assets			
Loans and advances		(284,268)	(202,165)
Derivative Assets		3,695	(4,823)
Other assets		(2,422)	(945)
Increase / (decrease) in operating liabilities			
Due to other financial institutions		41,850	(10,895)
Deposits		221,985	240,017
Derivative liabilities		5,084	-
Securities bought under repurchase agreement		(85,068)	(5,730)
Other liabilities		(1,776)	1,055
Net cash (used in) / provided by operating activities	35(b)	**(91,026)**	**27,033**
Cash flows from investing activities			
Payments for intangible assets		(3,610)	(3,640)
Payments for plant & equipment		(1,597)	(233)
Purchase of investments at amortised cost		(135,628)	(100,800)
(Payments)/proceeds from investments at amortised cost		209,810	148,556
Net cash provided by investing activities		**68,975**	**43,883**
Cash flows from financing activities			
Proceeds from issue of shares		10,000	-
Net cash provided by financing activities		**10,000**	**-**
Net increase / (decrease) in cash held		**(12,051)**	**70,916**
Cash at the beginning of the financial year		148,618	77,702
Cash at the end of the financial year	35(a)	**136,567**	**148,618**

The Consolidated Statement of Cash Flows is to be read in conjunction with the notes to and forming part of the financial report set out on pages 13 to 71.

Bank of Sydney Ltd
Consolidated Statement of Changes in Equity
For the year ended 31 December 2018

	Contributed Equity	General reserve for credit	Cash flow hedge reserve	Retained profits	Total Equity
Balance at 31 December 2017	**200,000**	**7,773**	**(85)**	**60,553**	**268,241**
Effect of change in accounting policy - AASB 9				(3,715)	(3,715)
Balance at 1 January 2018	**200,000**	**7,773**	**(85)**	**56,838**	**264,526**
Profit and loss	-	-	-	11,219	11,219
Transfers from general reserve to retained earnings	-	(2,048)	-	2,048	-
Other comprehensive income, net of income tax					
Effective portion of changes in fair value	-	-	(1,128)	-	(1,128)
Net amount transferred to profit and loss	-	-	31	-	31
Total other comprehensive income	**-**	**-**	**(1,097)**	**-**	**(1,097)**
Total comprehensive income for the year	**-**	**(2,048)**	**(1,097)**	**13,267**	**10,122**
Issue of share capital	10,000				10,000
Balance at 31 December 2018	**210,000**	**5,725**	**(1,182)**	**70,105**	**284,648**

	Contributed Equity	General reserve for credit	Cash flow hedge reserve	Retained profits	Total Equity
Balance at 1 January 2017	**200,000**	**5,499**	**(221)**	**51,822**	**257,100**
Profit and loss	-	-	-	11,005	11,005
Transfers from retained earnings to general reserve	-	2,274	-	(2,274)	-
Other comprehensive income, net of income tax					
Net amount transferred to profit and loss	-	-	99	-	99
Effective portion of changes in fair value	-	-	37	-	37
Total other comprehensive income	**-**	**-**	**136**	**-**	**136**
Total comprehensive income for the year	**-**	**2,274**	**136**	**8,731**	**11,141**
Issue of share capital	-	-	-	-	-
Balance at 31 December 2017	**200,000**	**7,773**	**(85)**	**60,553**	**268,241**

The Consolidated Statement of Changes in Equity is to be read in conjunction with the notes to and forming part of the financial report set out on pages 13 to 71.

1 Summary of significant accounting policies

(a) General information

Bank of Sydney Ltd ("the Company") is a Company domiciled in Australia. Its registered address is Level 4, 219-223 Castlereagh Street, Sydney, New South Wales.

The Company established a Residential Mortgage Backed Securitisation Trust with its legal name as "BHB Residential Securities Trust 1" ("the Trust"). The Company acts as subscriber, manager and seller of the Trust. Perpetual Corporate Trust Limited is the Trustee. The Trust is a 100% owned subsidiary of the Company since inception. Please refer to Note 38 for further details.

The principal activities of the Company and its subsidiary ("the Consolidated Entity") are disclosed in the Director's report.

The financial report was authorised for issue by the Directors on 17th April 2019.

The significant accounting policies which have been adopted in the preparation of this financial report are:

(b) Basis of preparation

The financial report is a general purpose financial report which has been prepared in accordance with the requirements of the Banking Act 1959 and Australian Accounting Standards (including Australian Interpretations) adopted by the Australian Accounting Standards Board ("AASB") and the Corporations Act 2001. For the purposes of preparing the consolidated financial statements, the Consolidated Entity is a for-profit entity. The Consolidated Entity's financial report complies with the International Financial Reporting Standards ("IFRSs") and the interpretations adopted by the International Accounting Standards Board.

The preparation of a financial report in conformity with Australian Accounting Standards requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

These financial statements have been prepared in accordance with the historical cost convention, except for derivative financial instruments, which are stated at their fair value.

The financial report is presented in Australian dollars.

(c) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its subsidiaries). Control is achieved where the Company is exposed to, or has rights to, variable returns from its involvement with the subsidiary and has the ability to affect those returns through its power over the subsidiary. Income and expense of subsidiaries acquired or disposed of during the year are included in the consolidated statement of profit and loss and other comprehensive income from the effective date of acquisition and up to the effective date of disposal, as appropriate. Total comprehensive income of subsidiaries is attributed to the owners of the Company and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Consolidated Entity. All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

For the purpose of preparing the consolidated financial statements, the Consolidated Entity is a for-profit entity.

(d) Interest

Interest income and expense for all interest bearing financial instruments are recognised within ‘interest income’ and ‘interest expense’ in the consolidated statement of profit and loss using the effective interest rate ("EIR") method.

The EIR method is a method of calculating the amortised cost of a financial asset or a financial liability and allocating the interest income or interest expense over the relevant period.
The interest income/ interest expense is calculated by applying the EIR to the gross carrying amount of non-credit impaired financial assets (i.e. at the amortised cost of the financial asset before adjusting for any expected credit loss allowance), or to the amortised cost of financial liabilities. For credit-impaired financial assets the interest income is calculated by applying the EIR to the amortised cost of the credit-impaired financial assets (i.e. the gross carrying amount less the allowance for expected credit losses (ECLs)).

The Consolidated Entity enters into foreign exchange swaps ("FX Swaps") primarily to minimise its foreign currency risk. An FX swap consists of a spot and a forward foreign exchange impact which offset each other with a net cash outflow or inflow as forward points. The forward points expense or income in its economic substance are regarded as interest in nature, and recognised as “interest expense” or “interest income” in the consolidated statement of profit and Loss.

(e) Fees and commission income

The Consolidated Entity has adopted AASB 15 ‘Revenue from Contracts with Customers’ ("AASB 15") from 1 January 2018, replacing the previous standard, AASB 118 ‘Revenue’. AASB 15 applies to contracts with customers except for revenue arising from items such as financial instruments, insurance contracts and leases.

Under AASB 118 revenue is recognised when risks and rewards have transferred from the seller to the buyer. AASB 15 has introduced a single, principle-based five-step recognition and measurement model for revenue recognition. The five steps are:

1. Identify the contract with a customer;
2. Identify the separate performance obligations;
3. Determine the transaction price;
4. Allocate the transaction price to each performance obligation identified in Step 2; and
5. Recognise revenue when a performance obligation is satisfied.

1 Summary of significant accounting policies (continued)

(e) Fees and commission income (continued)

The Consolidated Entity has used the modified retrospective approach in adopting AASB 15 which recognises the cumulative effect of initial application through opening retained earnings as at 1 January 2018. The Consolidated Entity will not restate the comparative period financial statements. The modified retrospective approach applied to contracts not completed at 31 December 2018.

The Consolidated Entity adopted AASB 15 on certain fees and commission income where performance obligations were identified and revenue recognized in line with meeting the performance obligations.
Fees and commission income and expenses arising from financial instruments that are integral to the effective interest rate on a financial asset or liability, which AASB 15 are not applicable to, are included in the measurement of the effective interest rate.

(f) Net foreign exchange gain/loss

Net foreign exchange gain/loss includes realised gains or losses on sales or purchases of foreign currency as well as unrealised gain or losses from revaluation of the Consolidated Entity's net foreign currency exposure.

(g) Cash and cash equivalents

Cash and cash equivalents includes notes and coins on hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of less than three months, which are subject to insignificant risk of changes in their fair value, and are used by the Consolidated Entity in the management of its short term commitments.

Cash and cash equivalents are carried at amortised cost in the Statement of Financial Position.

(h) Due from other financial institutions

Due from other financial institutions comprise at call deposits and cash held with other banks and is brought to account at the gross value of the outstanding balance. Interest on receivables due from other financial institutions is recognised on an EIR basis, as described in Note 1 (d).

(i) Financial instruments

The Consolidated Entity is a financial institution that offers an extensive range of financial instruments.

The Consolidated Entity has adopted AASB 9 "Financial Instruments" issued in December 2014 ("AASB 9 (December 2014)") effective as of 1 January 2018. The standard covers four broad topics: Impairment, Classification and Measurement, Derecognition and Hedging.

Prior to adopting AASB 9 (December 2014), the Consolidated Entity early adopted AASB 9 "Financial Instruments: Classification and Measurement" issued in December 2010 ("AASB 9 Financial Instruments: Classification and Measurement (December 2010)"). Under this standard the Consolidated Entity's financial instruments were classified into two categories: amortised cost and fair value through profit and loss. Upon adoption of AASB 9 (December 2014) the financial assets continued to meet the criteria for the relevant categories and as such there have been no reclassifications of financial assets between categories upon adoption.

Financial assets

Following the adoption of AASB 9 (December 2014) the Consolidated Entity measures financial assets as:

1 Summary of significant accounting policies (continued)

(i) Financial instruments (continued)

Financial assets (continued)

(i) Amortised cost
Business model is to hold the financial assets in order to collect contractual cash flows and those cash flows represent solely payments of principal and interest.

The Consolidated Entity includes cash, loans and advances to customers, financial assets due from financial institutions in this category.

Loans and advances are initially recorded at fair value plus any transaction costs directly attributable to the acquisition or issue of the loan and are subsequently measured at amortised cost less impairment using the EIR method.

(ii) Fair value through other comprehensive income ("FVTOCI")
Business model is to both collect contractual cash flows and sell financial assets and the cash flows represent solely payments of principal and interest.

The Consolidated Entity does not hold any financial assets in this category.

(iii) Fair value through profit or loss ("FVTPL")
Where financial assets are held for trading or if the cash flows on the asset do not solely represent payments of principal and interest. The Consolidated Entity can also elect to measure a financial asset at fair value through profit or loss if it eliminates or reduces an accounting mismatch.

The Consolidated Entity includes derivatives in this category.

Financial liabilities
Under AASB 9 (December 2014) an entity shall classify all financial liabilities as subsequently measured at amortised cost unless specific criteria exist.

The Consolidated Entity classifies all its non-derivative financial liabilities as measured at amortised cost. These financial liabilities are initially recorded at fair value plus any directly attributable transaction costs using the EIR method.

Derivative financial liabilities are measured at FVTPL.

Securities sold and under repurchase agreements are classified as financial liabilities measured at amortised cost. These financial instruments are not derecognised from the balance sheet as the risks and rewards of ownership remain with the Consolidated Entity.

(j) Securitisation Cost
Costs incurred during and directly attributable to the establishment of the Trust, as described in Note 1(a), are capitalised as an asset on the balance sheet and recognised in the profit and loss on a straight line basis over the life of the Trust.

1 Summary of significant accounting policies (continued)

(k) Impairment (continued)

Non-financial assets

The carrying amounts of the Consolidated Entity's non-financial assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If the carrying amount of an asset exceeds its recoverable amount, the asset is written down to the lower amount. The write down is recognised in the consolidated statement of profit and loss in the reporting period in which it occurs.

Financial assets

Upon transition to AASB 9 (December 2014) the accounting requirements have been applied on a retrospective basis. The Consolidated Entity has adjusted the carrying amounts of financial instruments resulting from adoption of AASB 9 (December 2014), specifically the impact of the change in accounting for impairment, through opening retained profits and reserves on 1 January 2018 as if it has always applied the new requirements. As permitted by AASB 9 (December 2014) the Consolidated Entity will not restate the prior period comparative financial statements.

Collective impairment provision

AASB 9 (December 2014) introduced an Expected Credit Loss ("ECL") impairment model which is fundamentally different to the incurred loss approach under AASB 139 Financial Instruments: Recognition and Measurement. The ECL model is forward looking and does not require evidence of an actual loss event for impairment provisions to be recognised.

The adoption of AASB 9 (December 2014) has resulted in the Consolidated Entity developing and implementing a new impairment provisioning model for financial assets as outlined below.

i. The ECL is calculated as outlined below:

ECL = Exposure at Default * Probability of Default * Loss Given Default

Exposure at Default ("EAD")

EAD represents the estimated outstanding amount of credit exposure at the time of the default.

Probability of Default ("PD")

PD represents the probability that a counterparty defaults. PD is determined using a roll rate model approach to estimate the % of exposures expected to roll to a loss/default state. The roll rates are calculated using internal historical past due data. The Consolidated Entity calculates independent PD rates for the following categories of loans and advances to customers: Retail; Commercial: non-property; Commercial: property.

The Consolidated Entity determines PD rates for treasury assets and trade exposures using historical external data in the absence of meaningful internal default loss history.

1 Summary of significant accounting policies (continued)

(k) Impairment (continued)

Collective impairment provision (continued)

Loss Given Default (LGD)

LGD is an estimate of the loss arising on default. The Consolidated Entity applies different LGD rates depending on the financial asset as well as the product.

For customer loans and advances the Consolidated Entity has used the Loan-to-Value Ratio ("LVR") as an indicator for potential loss in the event of default.

ii. 3 Stage approach

In accordance with AASB 9 (December 2014) the Consolidated Entity calculates a collective provision which reflects the ECL based on a 3 stage approach. The stage which the financial asset is in determines whether the ECL is calculated using a 12 month, or Lifetime, ECL.

Lifetime ECL represents the expected credit losses that will result from all possible default events over the expected life of a financial instrument.

12 month ECL represents the portion of the Lifetime ECL that is expected to result from default events on a financial instruments that are likely within 12 months after the reporting date.

Financial assets migrate between the 3 stages based whether there has been a Significant Increase in Credit Risk ("SICR") since initial recognition. In making this assessment the Consolidated Entity considers the following reasonable and supportable quantitative and qualitative criteria: days past due, internal customer rating, hardship exposures and restructured facility.

The Consolidated Entity groups is exposures by the following product range 'customer loans and advances' and 'treasury assets and trade exposures with bank counterparties'. The table below outlines the criteria under which loans and advances migrate to stage 2.

Stage 2	Number of Days Past Due	Customer Rating [1]	Hardship Flag	Restructure Flag
Retail Products	=>30 days <90 days	=>6 <9	✓	✓
Business Loans	=>30 days <90 days	=>6 <9	✓	✓
Commercial Property	=>30 days <90 days	=>6 <9	✓	✓
Commercial Construction	=>30 days <90 days	=>6 <9	✓	✓

[1]: The Consolidated Entity uses an internal customer rating process which grades customers from 1-10.

1 Summary of significant accounting policies (continued)

(k) Impairment (continued)

Collective impairment provision (continued)

The table below outlines the criteria under which loans and advances migrate to stage 3.

Stage 3	**Number of Days Past Due**	**Customer Rating** [1]
Retail Products	=>90 days	=>9
Business Loans	=>90 days	=>9
Commercial Property	=>90 days	=>9
Commercial Construction	=>90 days	=>9

Treasury assets and trade exposures with bank counterparties migrate from Stage 1 to Stage 2 when the counterparty is downgraded by 2 or more notches in credit rating using independent rating agencies. There is no collective provisioning for any financial asset in this group in stage 3 as there will be a specific provision applied in the event that the financial asset is past due.

The following table outlines how the Consolidated Entity measures ECL based on the 3 stage approach:

<table>
<tr><th></th><th>Customer loans and advances</th><th>Treasury assets and trade exposures with Bank counterparties</th></tr>
<tr><td>Stage 1:</td><td colspan="2">12 Month ECL</td></tr>
<tr><td>Stage 2:</td><td colspan="2">Lifetime ECL</td></tr>
<tr><td>Stage 3:</td><td>Lifetime ECL</td><td>N/A</td></tr>
</table>

1 Summary of significant accounting policies (continued)

(k) Impairment (continued)

Collective impairment provision (continued)

iii. Macro-economic overlay

The Consolidated Entity applies a macro-economic overlay to adjust the ECL for the impacts of macro-economic factors. The basis of the calculations takes into consideration key macro-economic factors which are used to determine three scenarios: Base case, Good Case and Bad Case. Relative weightings are then applied to each scenario to determine the final macro-economic adjusted ECL.

iv. Measurement and recognition of ECL

The ECL is estimated as the difference between all contractual cash flows that are due to the Consolidated Entity in accordance with the contract and all the cash flows that the Consolidated Entity expects to receive, discounted at the original effective interest rate.

If the Consolidated Entity has measured the loss allowance for a financial instrument at an amount equal to lifetime ECL in the previous reporting period, but determines at the current reporting date that the conditions for lifetime ECL are no longer met, the Consolidated Entity measures the loss allowance at an amount equal to 12‑month ECL at the current reporting date.

The Consolidated Entity recognises an impairment gain or loss in the statement of profit or loss for all financial instruments with a corresponding adjustment to their carrying amount through a loss allowance account.

Specific provision

Specific provisions are considered for all customer loans and advances that are past 90 days overdue and where a loss is anticipated. For all treasury assets and trade exposures with bank counterparties specific provisions are raised when the external rating of the counterparty drops to 'junk'. A specific provision is raised for any estimated shortfall between the Consolidated Entity's exposure and the net realisable value of the financial asset.

Write offs

The Consolidated Entity writes off a financial asset where there is information indicating that there is no realistic prospect of recovery. Financial assets written off may still be subject to enforcement activities under the Consolidated Entity's recovery procedures. Any recoveries made are recognised in the statement of profit and loss.

(l) Derivative instruments

The Consolidated Entity uses derivative financial instruments to hedge its exposure to foreign exchange and interest rate risks arising from operational and financing activities. In accordance with its treasury policy, the Consolidated Entity does not hold or issue derivative financial instruments for trading purposes.

The Consolidated Entity adopted AASB 9 (December 2014) hedge accounting requirements on 1 January 2018 which reduces the constraints associated with hedge accounting, allowing more types of hedging relationships and help reduce volatility in the statement of profit and loss. AASB 9 (December 2014) simplifies hedge accounting and aligns it with the overall risk management strategies of the Consolidated Entity. All existing hedges of the Consolidated Entity are cash-flow hedges which complied with the previous and more strict criteria.

1 Summary of significant accounting policies (continued)

(l) Derivative instruments (continued)

Derivative financial instruments are recognised initially at fair value. Subsequent to initial recognition, derivative financial instruments are carried at fair value. For derivatives that are not designated in a cash-flow hedge relationship, the gain or loss on re-measurement of fair value is recognised immediately in profit or loss through the consolidated statement of profit and loss.

The fair value of interest rate swaps at the end of the reporting period are determined by calculating the present fair value of estimated future cash flows using applicable yield curves derived from quoted interest rates and the credit risk of the parties to the contract.

Cash flow hedges

A cash flow hedge is a hedge of the exposure to variability in cash flows that is attributable to a particular risk associated with all, or a component of, a recognised asset or liability (such as all or some future interest payments on variable rate debt) or a highly probable forecast transaction, and could affect profit or loss. The Consolidated Entity hedges against interest rate fluctuations associated with its floating rate deposit liabilities. This objective is achieved by entering into interest rate swaps whereby the Consolidated Entity receives floating interest and pays fixed interest. The hedging instrument in this case is the interest rate swap and the hedge item is the floating rate deposits.

Changes in the fair value of the derivative hedging instrument designated as a cash flow hedge are recognised directly in cash flow hedge reserve to the extent that the hedge is effective. If the hedge is ineffective, changes in fair value are recognised in the statement of profit and loss. If the hedging instrument no longer meets the criteria for hedge accounting, expires or is terminated, then hedge accounting is discontinued prospectively. The cumulative gain or loss previously recognised in cash flow hedge reserve remains there until the forecast transaction occurs. Refer to note 24 for cash flow hedge reserve movement.

(m) Securities lent and repurchase agreements

Repurchased transactions, where the Consolidated Entity sells securities under an agreement to repurchase, are conducted on a collateralised basis. The securities subject to the lending are not derecognised from the balance sheet, as the risks and rewards of ownership remain with the bank. Securities sold, but subject to repurchase agreements, are disclosed as part of financial liabilities.

Fees and interest relating to securities lending and repurchase agreements are recognised as interest expenses in the income statement, using the EIR method, over the expected life of the agreements.

(n) Intangible assets

Computer software

Software acquired by the Consolidated Entity is stated at cost less accumulated amortisation and accumulated impairment losses.

Expenditure on internally developed software is recognised as an asset when the Consolidated Entity is able to demonstrate its intention and ability to complete the development and use the software in a manner that will generate future economic benefits and can reliably measure the costs to complete the development.

The capitalised costs of internally developed software include all costs directly attributable to developing the software, and are amortised over the useful life. Internally developed software is stated at capitalised cost less accumulated amortisation and impairment.

1 Summary of significant accounting policies (continued)

(n) Intangible assets (continued)

Computer software (continued)

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Both purchased and internally generated software has a finite useful life and are amortised using the straight-line method, at a rate applicable to the expected useful life of the asset, not exceeding 10 years.

The amortisation rates used are as follows:

2018	2017
10% to 20%	10% to 20%

Amortisation rates and methods are reviewed annually for appropriateness. When changes are made, adjustments are reflected prospectively in current and future periods only. Amortisation expenses and any impairment charges are recognised in the income statement.

(o) Plant and equipment

Items of plant and equipment are stated at cost less accumulated depreciation and impairment losses.

Useful lives

All assets have limited useful lives and are depreciated through the statement of profit and loss using the straight-line method over their estimated useful lives.

Assets are depreciated from the date of acquisition or, in respect of internally constructed assets, from the time an asset is completed and held ready for use.

Depreciation rates and methods are reviewed annually to ensure they appropriately reflect residual values and estimated useful lives. When changes are made, adjustments are reflected prospectively in current and future periods only. The depreciation rates used for each class of asset are as follows:

	2018	2017
Plant and equipment		
Leasehold improvements	10%	10%
Plant and equipment	10% - 33%	10% - 33%
Furniture and fittings	10% - 33%	10% - 33%
Computer hardware	20% - 25%	20% - 25%
Motor vehicle	13%	13%

1 Summary of significant accounting policies (continued)

(p) Foreign currency

Foreign currency transactions are translated to Australian currency at the rates of exchange ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the rates of exchange ruling on that date.

Exchange differences relating to amounts payable and receivable in foreign currencies are brought to account as exchange gains or losses in the consolidated statement of profit and loss in the period in which the exchange rates change.

(q) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary difference when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

1 Summary of significant accounting policies (continued)

(r) Tax consolidation

The Company and its wholly-owned Australian resident entity "BHB Residential Securities Trust 1" have formed a tax-consolidated group with effect from 1 January 2015 and are therefore taxed as a single entity from that date. The head entity within the tax-consolidated group is Bank of Sydney Limited. The Trust is the only other member of the tax-consolidated group.

Tax expense/income, deferred tax liabilities and deferred tax assets arising from temporary differences of the members of the tax-consolidated group are recognised in the separate financial statements of the members of the tax-consolidated group using the 'separate taxpayer within group' approach by reference to the carrying amounts in the separate financial statements of each entity and the tax values applying under tax consolidation. Current tax liabilities and assets and deferred tax assets arising from unused tax losses and relevant tax credits of the members of the tax-consolidated group are recognised by the Company (as head entity in the tax-consolidated group).

Entities within the tax consolidated group entered into a tax sharing deed, under the terms of which, the consolidated group allocates an income tax liability by reference to the income tax liability it would have incurred if it were not a member of the consolidated group. Where a contributing member is itself a trust, the deed provides for a reduction in the member's Notional Income Tax Amount to the extent it would not be assessed to the trustee under sections 99 or 99A of the Tax Act. This should have the effect of allocating a nil amount to the Trust if the Head Company is beneficially presently entitled to all of the income of the Trust.

(s) Leases

Payments made under operating leases are recognised in the consolidated statement of profit and loss on a straight-line basis over the term of the lease.

(t) Employee entitlements

(i) Wages, salaries, annual leave and sick leave

The provision for employee entitlements to wages, salaries and annual leave represent present obligations resulting from employees' services provided up to the balance sheet date, calculated at undiscounted amounts based on expected wage and salary rates including related on-costs.

(ii) Long service leave

The provision for employee entitlements to long service leave represents the present value of the estimated future cash outflows to be made resulting from employees' services provided up to the balance sheet date.

The provision is calculated using estimated future increases in wage and salary rates including related on-costs and expected settlement dates based on turnover history and is discounted using the rates attaching to national government securities at the balance sheet date which most closely match the terms of maturity of the related liabilities.

1 Summary of significant accounting policies (continued)

(t) Employee entitlements (continued)

(iii) Superannuation plan
The Consolidated Entity contributes to a defined contribution superannuation plan. Contributions are expensed as they are incurred.

(u) Financial guarantees and letters of credit
Financial guarantees are contracts that require the Consolidated Entity to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. These contracts can take the form of guarantees or letters of credit.

After initial recognition, an issuer of such a contract shall subsequently measure it at the higher of:
(i) the amount of the loss allowance determined in accordance with Note k (impairment) and
(ii) the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of AASB 15;

(v) Derecognition of financial assets
The Consolidated Entity derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another party. If the Consolidated Entity neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Consolidated Entity recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Consolidated Entity retains substantially all the risks and rewards of ownership of a transferred financial asset, the Consolidated Entity continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Residential Mortgages subject to securitisation arrangements between the Company and the BHB Residential Securities Trust (the “Trust”) are recognised by the Company in its separate financial statements (refer to note 38) and are presented as “Loans and advances - Held by Trust subject to securitisation”. These are also included in the Consolidated Entity's balance sheet.

(w) Provisions
A provision is recognised in the balance sheet when the Consolidated Entity has a legal or constructive obligation as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

1 Summary of significant accounting policies (continued)

(x) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected.

The following are the critical judgements and estimates that the Directors have made in the process of applying the Consolidated Entity's accounting policies and that have the most significant effect on the amounts recognised in the annual financial report.

Fair value of financial Instruments

As described in note 27, the Consolidated Entity uses valuation techniques that include inputs that are based on observable market data to estimate the fair value of certain types of financial instruments. Note 27 provides detailed information about the key assumptions used in the determination of the fair value of financial instruments, as well as the detailed disclosure of carrying amounts and estimated fair value of financial assets and liabilities.

The Directors believe that the chosen valuation techniques and assumptions used are appropriate in determining the fair value of financial instruments.

Impairment

Non-Financial assets

As described in note 1(k), determining whether an individual non-financial assets is impaired requires identification of an objective indication of impairment as well as estimation of the value of the recoverable amount.

The calculation of recoverable amount requires the Consolidated Entity to estimate the expected future cash flows, future credit losses and suitable discount rate in order to calculate present value.

Financial assets

Management estimates and judgements are applied when calculating impairment provisions for financial assets, most significantly collective impairment provision.

Note 1(k) outlines the Consolidated Entity's approach to collective provisioning and the following components are the key estimates and judgements made in relation to the measurement of the collective impairment provision:

• SICR: Judgement is used in determining what criteria to assess in the assessment of what constitutes a SICR as outlined in note 1(k) as well as the underlying assessment of the individual financial asset. These criteria are assessed at each reporting date.

• Establishing groups of assets with similar risk characteristics as outlined in note 1(i) and 1(k) and 25(b). The Consolidated Entity monitors the appropriateness of the credit risk characteristics on an ongoing basis to assess whether they remain relevant.

1 Summary of significant accounting policies (continued)

(x) Use of estimates and judgements (continued)

• Establishing the number and relative weightings of forward-looking scenarios to determine the macro-economic overlay as outlined in note 1(k).
The macro-economic overlay methodology, inputs and assumptions are reviewed each period.

• PDs and LGDs, as outlined in note 1(k), are key estimates impacting the measurement of the ECL.
The provisioning methodology, including PD and LGD assumptions, data, expectations and output is reviewed each period.

(y) Application of new and revised standards

In the current year, the Consolidated Entity has applied a number of amendments to AASBs issued by the Australian Accounting Standards Board (AASB) that are mandatorily effective for an accounting period that begins on or after 1 January 2018, and therefore relevant for the current year end, including:

AASB 9 "Financial Instruments"
AASB 15 "Revenue from Contracts with Customers"
AASB 7 "Financial Instruments: Disclosures"

AASB 9 "Financial Instruments"

The application of AASB 9 (December 2014) on "classification and measurement", as well as "hedging" does not have any material impact on the disclosures or on the amount recognised in the Consolidated Entity's financial report. Please refer to note 1(i), (k), (l) and (x) for details of impact from adopting AASB 9 "Financial Instruments" December 2014 on impairment of financial assets.

The impact of the implementation of AASB 9 (December 2014) on impairment of financial assets was as outlined below for the year ended 31 December 2018. Cash and liquid assets has been assessed as having a low credit risk. The 12 month ECL has been assessed as immaterial and so no provision has been recognised.

Credit Risk Category	Items existing as at 1/1/18 that are subject to the impairment provisions of AASB 9	1/01/2018 $'000	31/12/2018 $'000
Treasury asset and trade exposure with bank counterparties	Cash and liquid assets	-	-
	Due from other financial institutions	-	54
	Investments at amortised cost	98	120
	Loans and advances-Trade	60	75
Customer loans and advances	Loans and advances-Customers	5,149	1,438
Credit Commitment and Bank Guarantee	Credit Commitment and Bank Guarantee	-	-

1 Summary of significant accounting policies (continued)

(y) Application of new and revised standards (continued)

AASB 9 "Financial Instruments" (continued)

The following table summarises the adjustments arising on adoption of AASB 9 (December 2014). The adjustments have been recognised against the Consolidated Entity's opening retained profits and reserves as at 1 January 2018

	Carrying Amount 31/12/17	Remeasurements	Carrying Amount 1/1/18	Retained Earnings effect on 1/1/18
	'000	'000	'000	'000
Financial Assets				
Cash and liquid assets	122,047	-	122,047	-
Due from other financial institutions	26,571	-	26,571	-
Investment at amortised cost	462,735	(98)	462,637	(98)
Loans and advances	1,474,444	(5,209)	1,463,928	(5,209)
Derivative financial assets	3,361	-	3,361	-
Deferred tax assets	1,773	1,592	3,365	1,592
Financial Liabilities				
Due to other financial institutions	6,245	-	6,245	-
Securities sold and under repurchase	85,173	-	85,173	-
Deposits	1,732,675	-	1,732,675	-
Derivative liabilities	120	-	120	-
Total Impact on opening retained earnings		**(3,715)**		**(3,715)**

AASB 15 "Revenue from Contracts with Customers"

AASB 15 is principles-based and primarily aims to be a single comprehensive revenue recognition framework, with a clearly explained revenue recognition approach and elaborate guidance on various revenue streams. The core principle is that an entity will recognise revenue at an amount that reflects the consideration entitled in exchange for transferring goods or services to a customer and the revenue recognition and measurement use five-step model. Interest and dividend income are excluded from the scope of AASB 15 and assessed under AASB 9 Financial Instruments.

The application of AASB 15 does not have any material impact on the disclosures or on the amount recognised in the Consolidated Entity's financial report.

1 Summary of significant accounting policies (continued)

(y) Application of new and revised standards (continued)

AASB 7 "Financial Instruments: Disclosure" (as amended)
AASB 7 "Financial Instruments: Disclosure" (as amended by AASB 9 December 2014) applies to annual periods beginning on or after 1 January 2018 but before 1 January 2019.

The Consolidated Entity has applied these amendments for the first time in the current year. The amendments require an entity to provide additional disclosures that enable users to evaluate (a) the significance of financial instruments for the entity's financial position and performance; and (b) the nature and extent of risks arising from financial instruments to which the entiry is exposed during the period and at the end of the reporting period.

The application of these amendments has had no impact on the Consolidated Entity's financial statements, apart from the additional disclosure in Note 1. Summary of significant accounting policies; Note 19. Derivative financial instruments; and Note 25. Financial risk Management (b) Credit Risk.

(z) Standards and Interpretations issued not yet adopted

AASB 16 ‘Leases’

AASB 16 amends the accounting for leases and will replace AASB 117 'Leases'. Lessees will be required to bring both operating and finance leases on Balance Sheet as a right of use asset along with the associated lease liability. Interest expense will be recognised in profit or loss using the effective interest rate method, and the right of use asset will be depreciated. Lessor accounting remains largely unchanged. AASB 16 is not mandatory until 1 January 2019.

The Consolidated Entity has completed an initial assessment of the potential impact on its financial statements but has not yet completed its detailed assessment. The actual impact of applying AASB 16 on the financial statements in the period of initial application will depend on future economic conditions, including the Consolidated Entity's borrowing rate at 1 January 2019, the composition of the Consolidated Entity's lease portfolio at that date, the Consolidated Entity's latest assessment of whether it will exercise any lease renewal options and the extent to which the Consolidated Entity chooses to use practical expedients and recognition exemptions.

So far, the most significant impact identified is that the Consolidated Entity will recognise new assets and liabilities for its operating leases of office buildings and equipment. As at 31 December 2018, the Consolidated Entity's future minimum lease payments under non-cancellable operating leases amounted to $5,059,000 on an undiscounted basis.

In addition, the nature of expenses related to those leases will now change as AASB 16 replaces the straight-line operating lease expense with a depreciation charge for right-of-use assets and interest expense on lease liabilities.

Other Standards

The following amended standards and interpretations are not expected to have a significant impact on the Group's consolidated finanical statements
-AASB 2017-4 Amendments to Australian Accounting Standards-Uncertainty over Income Tax Treatments
-AASB 2017-6 Amendments to Australian Accounting Standards-prepayment Features with Negative Compensation
-AASB 2017-7 Amendments to Australian Accounting Standards-Long-term interests in associates and Joint Ventures
-AASB 2018-1 Amendments to Australian Accounting Standards-Annual Improvements 2015-2017 cycle
-AASB 2018-2 Amendments to Australian Accounting Standards-Plan Amendment, Curtailment or Settlement
-AASB 2018-3 Amendments to Australian Accounting Standards-Reduced Disclosure Requirements

		2018	2017
		$'000	$'000
2	**Interest income**		
	Cash and liquid assets	1,355	756
	Due from other financial institutions	83	8
	Investments at amortised cost		
	- banks	12,550	15,058
	- related party	341	74
	Loans and advances	68,774	59,231
	Other interest income – parent company	(49)	152
		83,054	75,279
3	**Interest expense**		
	Due to other financial institutions		
	- banks	318	491
	- related party	224	28
	Deposits	39,674	34,744
	Other borrowings - repurchase agreement	1,301	1,691
		41,517	36,955
4	**Non-interest income**		
	Net fees and commission income	5,753	6,929
	Gain from sale of securities	304	486
	Net foreign exchange gain	1,972	1,561
	Unrealised loss on derivatives	(53)	(66)
		7,976	8,911
5	**Operating expenses**		
	Staff expenses	20,122	18,527
	Computer expenses	3,722	2,663
	Occupancy costs	3,941	3,567
	Depreciation of property and equipment	765	777
	Amortisation of intangibles	1,220	876
	Marketing expenses	1,111	726
	Other operating expenses	6,350	4,498
		37,231	31,633

	2018 $'000	2017 $'000
6 Taxation		
(a) Income tax expense		
Current tax expense		
Current period	3,876	5,067
Adjustment for prior period	(8)	-
	3,868	5,067
Deferred tax expense		
Deferred tax expense recognised in the current year	986	(294)
Adjustment for prior period	8	-
	994	(294)
Total income tax expense	**4,862**	**4,773**
(b) Reconciliation between tax expense and pre-tax net profit		
Profit before tax	16,081	15,778
Income tax using the Consolidated Entity's tax rate of 30%	4,824	4,733
Prior Year adjustment	-	-
Non-deductible expenses	38	40
Income tax expense	4,862	4,773
7 Cash and liquid assets		
Cash at bank	4,298	4,218
Cash held with central bank	53,320	117,828
	57,618	122,047

Total cash and liquid assets are all variable interest rates and are unsecured.

		2018	2017
		$'000	$'000
8	**Due from other financial institutions**		
	Within Australia	14,088	5,140
	Related parties	57,755	10,955
	Overseas	7,160	10,477
	Less: Impairment Loss Allowance	(54)	-
		78,949	26,571
	Impairment Loss Allowance		
	Prior year ending balance	-	
	Effect of change in accounting policy from AASB 9	-	
	Opening balance restated	-	
	Charge to consolidated statement of profit and loss	(54)	
	Closing balance	(54)	

Refer to Note 25 b (iii) for analysis of movement in gross balance and impairment loss allowance during the year.

		2018	2017
	Residual maturity analysis		
	At call	-	25,958
	Up to 1 month	78,891	501
	1 to 3 months	112	112
	Less: Impairment Loss Allowance	(54)	-
		78,949	26,571
9	**Investments at amortised cost**		
	Certificate of Deposits	17,980	-
	Floating rate notes	284,396	348,620
	Fixed rate bonds	85,786	114,115
	Less: Impairment Loss Allowance	(120)	-
		388,042	462,735
	Residual maturity analysis		
	Up to 1 month	12,993	10,204
	1 to 3 months	8,001	12,441
	3 to 12 months	48,715	104,627
	12 months to 5 years	312,269	335,463
	Over 5 years	6,184	-
	Less: Impairment Loss Allowance	(120)	-
		388,042	462,735
	Impairment Loss Allowance		
	Prior year ending balance	-	
	Effect of change in accounting policy from AASB 9	(98)	
	Opening balance restated	(98)	
	Charge to consolidated statement of profit and loss	(22)	
	Closing balance	(120)	

Refer to Note 25 b (iii) for analysis of movement in gross balance and impairment loss allowance during the year.

		Note	2018 $'000	2017 $'000
9	**Investments at amortised cost (continued)**			

The below carrying value of investments at amortised cost were sold with a forward repurchase date, as part of the sales and repurchase agreement with Reserve Bank of Australia. The Consolidated Entity retained risks and rewards of the investments, and therefore have not derecognised these assets.

	2018	2017
Pledged value		
Floating rate notes	-	93,200
	-	93,200

10 (a) Loans and advances

	Note	2018	2017
Loans and advances		1,719,452	1,433,705
Overdrafts		39,999	41,032
Gross loans and advances		1,759,451	1,474,738
Less -			
Collective provision	11	(1,513)	(294)
Specific provision	11	(94)	-
Net loans and advances		**1,757,844**	**1,474,444**

	2018	2017
Residual maturity analysis (excluding provisions)		
Overdrafts	40,093	41,032
Up to 1 month	244,036	198,986
1 to 3 months	26,981	56,514
3 to 12 months	71,715	103,601
12 months to 5 years	19,659	42,795
Over 5 years	1,356,967	1,031,808
	1,759,451	1,474,738

Residual maturity analysis was performed based on contractual final maturity dates of loans and advances. Refer to Note 27 for additional disclosures to meet requirements of AASB7 – *Financial Instruments: Disclosures.*

10 (b) Internal Securitisation

As further disclosed in Note 38 – Internal Securitisation, $331m (2017: $189m) of Residential Mortgages have been sold and are held by a controlled subsidiary, BHB Residential Securities Trust 1, as part of an internal securitisation.

		2018 $'000	2017 $'000
11 (a)	**Provision for Impairment**		
	Collective provisions		
	Prior year ending balance	294	263
	Effect of change in accounting policy from AASB 9	5,209	-
	Opening balance restated	5,503	
	Charge/(reversal) to consolidated statement of profit and loss	(3,990)	31
	Closing balance	1,513	294
	Specific provisions		
	Opening balance	-	46
	Write off against provision	-	(49)
	Charge to consolidated statement of profit and loss	94	3
	Closing balance	94	(0)
	Reconciliation of impairment losses		
	Collective provisions		
	- current year charge/(reversal)	(3,990)	31
	Specific provisions		
	- current year charge	94	3
	Impairment Loss Allowance		
	- current year charge	76	
	Write off of Interest	16	10
	Write off of loan Principal	5	6
	Write back of unrealized interest to profit or loss	-	(226)
	Impairment loss/(reversal of loss)	(3,799)	(176)

The Consolidated Entity did not recognise any material interest income on impaired assets as at 31 December 2018. (2017: Nil).

11 (b) Impaired assets

The balance of past due loans and impaired loans as described and explained in Note 1 (k) are as follows:

	2018 $'000	2017 $'000
Loans and advances to customers		
Past due but not impaired	41,746	60,871
Impaired	96	-
Gross impaired and past due loans	41,842	60,871
Less: Specific provision	(94)	-
Net impaired and past due loans	41,748	60,871

Refer to Note 25(b) for further details.

		2018	2017
		$'000	$'000
12	**Intangible assets**		
	Computer software		
	At cost	11,651	8,476
	Less: Accumulated amortisation	(3,661)	(3,089)
		7,990	5,387
	Opening balance	5,387	3,099
	Additions	4,086	3,167
	Disposal	(263)	-
	Amortisation expense	(1,220)	(880)
	Net book value	7,990	5,387
13	**Plant and equipment**		
	Plant and equipment		
	At cost	5,633	4,277
	Less: Accumulated amortisation	(3,510)	(3,184)
		2,123	1,094
	Leasehold		
	At cost	6,795	7,464
	Less: Accumulated amortisation	(5,245)	(5,079)
		1,550	2,385
	Motor Vehicle		
	At cost	59	59
	Less: Accumulated amortisation	(21)	(14)
		38	46
	Net book value	**3,711**	**3,524**

		2018	2017
		$'000	$'000
13	**Plant and equipment (continued)**		
	Reconciliation of the carrying values of plant and equipment and leasehold property are set out below:		
	Plant and equipment at cost		
	Opening balance	1,093	1,291
	Additions	963	131
	Transfer	477	-
	Net book value of assets disposed during the year	(34)	(26)
	Depreciation expense	(376)	(303)
		2,123	1,093
	Leasehold property at cost		
	Opening balance	2,385	2,248
	Additions	158	579
	Transfer	(477)	-
	Net book value of assets disposed during the year	(135)	-
	Depreciation expense	(381)	(441)
		1,550	2,385
	Motor vehicles at cost		
	Opening balance	46	53
	Additions	-	-
	Depreciation expense	(8)	(7)
		38	46
	Net book value	**3,711**	**3,524**
14	**Deferred tax assets**		
	Deferred income tax assets are attributable to the following items:		
	Deferred tax assets		
	Provisions	1,711	1,161
	Cash flow hedge reserve	507	36
	Fixed assets	681	628
	Total deferred tax asset	**2,899**	**1,825**
	Deferred tax liabilities		
	Securitisation start-up costs	(34)	(35)
	Prepaid balances	(15)	(17)
	Total deferred tax liabilities	**(49)**	**(52)**
	Net deferred tax asset	**2,850**	**1,773**

		Note	2018 $'000	2017 $'000
14	**Deferred tax assets (continued)**			
	Reconciliation of balances of net deferred tax assets are set out below:			
	Deferred tax assets			
	Prior year ending balance		1,773	1,538
	Effect of change in accounting policy from AASB 9		1,592	-
	Opening balance restated		3,365	1,538
	Deferred tax credit/(debit) to income statement	6(a)	(986)	294
	Deferred tax charges recognised in equity for cash flow hedge		471	(59)
	Net deferred tax asset		**2,850**	**1,773**

15 Other assets

	2018 $'000	2017 $'000
Prepayments	943	818
Other	4,400	3,831
	5,343	**4,649**

Other comprises mainly suspense accounts, sundry debtors and other miscellaneous debit balances.

16 Due to other financial institutions

	2018 $'000	2017 $'000
- parent entity	3,788	739
- Australia	-	718
- overseas	7,322	4,786
- related parties	37,037	2
	48,147	**6,245**

The parent entity refers to Bank of Beirut s.a.l and the related parties in 2018 refers to wholly owned subsidiaries and associated companies of Bank of Beirut s.a.l. Please refer to note 33(a) for details of related party relationship and transactions in 2018.

17 Securities sold and under repurchase agreements

	2018 $'000	2017 $'000
Securities sold and under repurchase agreements	-	85,173

The Consolidated Entity enters into sales and repurchase agreement with Reserve Bank of Australia, which in substance is borrowing with pledged securities. Refer to note 9 for details of investments at amortised cost sold and repurchased.

18 Deposits

	2018 $'000	2017 $'000
Current	320,067	276,122
Savings	192,316	191,979
Term	1,444,218	1,264,574
Total deposits	**1,956,601**	**1,732,675**

	2018 $'000	2017 $'000
19 Derivative financial instruments		
The Consolidated Entity enters into derivative transactions, which provide economic hedges for exposures to market risk.		
Assets		
Interest rate swaps designated as cash flow hedge - Local banks	59	547
Foreign currency forwards not designated in a hedging relationship-Parent entity	-	1,785
Foreign currency forwards not designated in a hedging relationship-Other	26	1,029
	85	**3,361**
Liabilities		
Interest rate swaps designated as cash flow hedge - Local banks	1,085	70
Foreign currency forwards not designated in a hedging relationship-Other	4,083	51
	5,168	**120**

The following tables detail various information regarding interest rate swap contracts outstanding at the end of the reporting period and their related hedged items.

Cash flow hedges

AASB 9
As at December 31, 2018

$' 000	Notional amounts Within 1 year	1 through 5 years	Over 5 years	**Total**	Carrying amount Assets	Liabilities
Interest rate risk						
Interest rate contracts	15,000	107,000	6,000	**128,000**	59	1,085
Hedge of variable rate liabilities	15,000	107,000	6,000	**128,000**	59	1,085
Weighted average fixed interest rate						
Hedge of variable rate liabilities	1.92%	2.24%	2.92%	**2.23%**		

19 Derivative financial instruments(continued)

The tables below summarise the derivatives designated as hedging instruments in qualifying cash flow hedge relationships.

AASB 9
As at December 31, 2018

$'000	Line item in the statement of financial position where the hedging instrument is located	Hedge ineffectiveness recognised in profit or loss	Changes in fair values used for calculating hedge ineffectiveness	Cash flow hedge reserve	
				Continuing hedges	Discontinued hedges
Cash flow hedges					
Interest rate risk	Derivative instruments	-	(1,503)	(1,182)	-

The Consolidated Entity's exposure to market risks and its approach to manage those risks is discussed in note 25 (c). Specifically, the Consolidated Entity is exposed to interest rate fluctuations as it pays floating interest on customer deposit liabilities and receives fixed revenues from fixed-rate financial assets. To alleviate the risk of interest rate fluctuations, the Consolidated Entity enters into interest rate swaps to receive floating rate interest and pay fixed rate interest to hedge the variability in cash flows on the floating rate deposit liabilities attributable to changes in the interest rate. In this way the Consolidated Entity exchanges floating rate interest payment, to fixed rate interest payment. The Consolidated Entity has designated cash flow hedge relationships to hedge against movements in interest rate and applies hedge accounting on these cash flow hedges.

The Consolidated Entity assesses hedge effectiveness by comparing the changes in fair value of a hypothetical derivative reflecting the terms of the portion of gross interest cash outflows that will result from the repricing or reinvestment of the Consolidated Entity's 3 month fixed short term deposit portfolio with the changes in fair value of the interest rate swaps used to hedge the exposure. The Consolidated Entity uses the hypothetical derivative method to determine the changes in fair value of the hedged item.

The Consolidated Entity has identified the following possible source of ineffectiveness in its cash flow hedge relationships:
The use of derivatives as a protection against currency and interest rate risk creates an exposure to the derivative counterparty's credit risk which is not offset by the hedged item. This risk is minimised by entering into derivatives with high credit quality counterparties.

No other source of hedge ineffectiveness are expected to affect the cash flow hedging relationship during the year.

		2018 $'000	2017 $'000
20	**Provisions**		
	Annual leave provision	1,206	1,075
	Long service leave provision	1,190	1,135
	Make good provision	562	500
		2,958	**2,711**
21	**Other liabilities**		
	Current tax liability	(387)	1,041
	Bank cheques issued awaiting clearance	1,434	2,328
	Other	3,863	5,957
		4,910	**9,325**

Other mainly includes accrued expenses, sundry creditors and other miscellaneous credit balances.

		2018 $'000	2017 $'000
22	**Contributed Equity**		
	210,000,000 ordinary shares fully paid (2017 - 200,000,000 ordinary shares fully paid)	210,000	200,000

All shares are fully paid ordinary shares, which have a par value of $1AUD, carry one vote per share and carry a right to dividends. Bank of Beirut s.a.l owns 100% of the Consolidated Entity. The Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings.

On 8 October 2018, Bank of Beirut s.a.l injected a further $10,000,000 AUD of Capital (10,000,000 ordinary shares fully paid) into the Consolidated Entity.

In the event of the winding up of the Consolidated Entity, ordinary shareholders rank after all other shareholders. Creditors are fully entitled to any proceeds on liquidation to meet outstanding amounts owing.

		2018 $'000	2017 $'000
23	**Retained profits**		
	Retained profits at beginning of year	60,553	51,822
	AASB 9 Opening adjustment	(3,715)	-
	Net profit after income tax	11,219	11,005
	Transfer from general reserve for credit losses	2,048	(2,274)
	Retained profits at year-end	**70,105**	**60,553**
24	**Reserves**		
	General reserve for credit losses		
	Opening Balance	7,773	5,499
	Transfer to retained profits during the year	(2,048)	2,274
	Closing Balance	5,725	7,773
	Cash flow hedge reserve		
	Opening Balance	(85)	(221)
	Transfer from reserves during the year	(1,097)	136
	Closing Balance	(1,182)	(85)
	Total reserves	**4,543**	**7,688**

All reserve amounts are shown net of income tax. A General Reserve for Credit Losses (GRCL) represents a reserve established to cover credit losses estimated but not certain to arise which is over and above any specific provisions raised for impaired assets. The GRCL represents lifetime expected credit losses as referred to in APS 220 Credit Quality.

25 Financial risk management

(a) Introduction and overview

The Consolidated Entity’s activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and exposures to operational risks are an inevitable consequence of being in business. The Consolidated Entity’s aim is therefore to achieve an appropriate balance between risk and return and minimise potential adverse effects on the Consolidated Entity’s financial performance.

The Consolidated Entity’s risk management policies are established to identify and analyse the risks faced by the Consolidated Entity, to set appropriate risk limits and controls and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Consolidated Entity, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

25 Financial risk management (continued)

(a) Introduction and overview (continued)

The Board has overall responsibility for the establishment and oversight of the Bank's risk management framework and sets the Consolidated Entity's risk appetite.

The Board Risk Management Committee is responsible for monitoring compliance with the Consolidated Entity's risk management policies and procedures and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Consolidated Entity. The Consolidated Entity's Executive Risk and Compliance Committee assists the Board and the BRMC in overseeing all risk management activities that are carried out, for the purpose of identifying, evaluating and managing all key business risks.

(b) Credit risk

Credit risk is the risk of financial loss to the Consolidated Entity if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from loans and advances to customers and other banks and from investment securities. For risk management reporting purposes, credit concentrations are managed on a consolidated basis to ensure that the Consolidated Entity is not unduly exposed to a single or small number of counterparties such that their default would adversely affect the financial position of the Consolidated Entity. Also, large credit exposures are monitored and reviewed on a regular basis.

For debt securities and other bills, external ratings such as Moody's and Standard & Poor's rating, or their equivalents, are used for managing credit risk exposures. Investment securities and other bills are utilised in order to maintain a portfolio of high quality liquid assets available to meet funding needs as required.

(i) Management of credit risk

The Board of Directors has delegated responsibility for the management of credit risk to the Executive Credit Committee. Risk is responsible for monitoring compliance with credit policies on a day to day basis. Responsibilities of Risk include:

- General oversight of the asset quality including the credit grading system, loan portfolio trends and concentration risks;
- Ensure that lending at all times is within the regulations, recommendations and instructions of the Australian Prudential Regulation Authority's credit policies;
- To prepare reports and returns for management, Board of Directors, and authorities;
- To monitor that all lending is complying with all external laws, regulations, guidelines, markets and internal Codes of Conduct, policies, limits and procedures; and
- Report to the Board and the Credit Committee any excesses on risk management limits.

Internal Audit undertakes regular audits of business units and Credit processes, including the effectiveness of the Credit Risk Management Framework.

25 Financial risk management (continued)

(b) Credit risk (continued)

(ii) Exposure to credit risk

The table below illustrates the Consolidated Entity's on-balance sheet loans and advances and the associated impairment provision for each, according to the Consolidated Entity's internal grading categories. The exposures set out below are based on carrying amounts.

On balance sheet items

	2018 $'000			
Customer rating	**Stage 1 12-month ECL**	**Stage 2 Lifetime ECL**	**Stage 3 Lifetime ECL**	**Total**
Customer ratings 1-5: Low risk to acceptable.	1,697,990	13,643	1,117	**1,712,750**
Customer ratings 6-8: Management attention to High risk	-	46,009	596	**46,605**
Customer ratings 9-10: Impaired	-	-	96	**96**
Total gross carrying	1,697,990	59,652	1,809	**1,759,451**
Loss allowance	(895)	(443)	(269)	**(1,607)**
Carrying Amount	1,697,095	59,209	1,540	**1,757,844**

A rating of 1 to 10 (inclusive) is applied to each borrowing entity or guarantor.

The Impairment Provision represents the total of the specific and collective provisions as set out in Note 11(a).

25 Financial risk management (continued)

(b) Credit risk (continued)

The table below represents the maximum exposure to credit risk of the Consolidated Entity as at 31 December 2018 and 2017, without taking account any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures equal gross carrying amounts as reported in the balance sheet.

	2018 $'000	2017 $'000
Credit risk exposures relating to on-balance sheet:		
Loans and advances to customers:		
Loans to individuals:		
- Retail	1,156,219	838,647
Loans to corporate entities:		
- Large corporate customers	95,904	158,691
- Small and medium size enterprises (SMEs)	507,328	477,400
Due from other financial institutions	79,003	26,571
Investments at amortised cost	388,162	462,735
Derivative financial assets	85	3,361
Total	2,226,701	1,967,405
Credit risk exposures relating to off-balance sheet items:		
Financial guarantees	6,286	10,182
Loan commitments and other credit related liabilities	168,932	161,655
Trade finance contingencies	17,528	26,510
Total	192,746	198,348

The Consolidated Entity holds collateral and other credit enhancements to cover its credit risks associated with on balance sheet and off balance sheet credit risk exposures. The estimated value of collateral and other credit enhancements amounts to $3,205 million as at 31 December 2018 ($2,705 million as at 31 December 2017). The estimated value of collateral is based on market value of the collateral and is not capped to the value of the exposure.

Refer to Note 25 b (iii) for analysis of movement in gross balance and ECL during the year.

25 Financial risk management (continued)

(b) Credit risk (continued)

Loans and advances past due, though subject to ECL calculation by the Consolidated Entity, are not considered impaired, unless other information is available to indicate the contrary. The gross value of loans and advances by class to customers that were past due, but not impaired, are presented in the table below.

31/12/2018
$'000's

	Individuals (retail customers)	Large corporate customers	SMEs	Total
Past due up to 30 days	15,274	931	9,059	25,264
Past due 30- 60 days	2,220	-	12,396	14,616
Past due 60 - 90 days	61	-	-	61
Past due more than 90 days	1,184	-	621	1,805
Total	**18,739**	**931**	**22,076**	**41,746**

31/12/2017
$'000's

	Individuals (retail customers)	Large corporate customers	SMEs	Total
Past due up to 30 days	8,575	-	18,737	27,312
Past due 30- 60 days	4,213	-	3,253	7,466
Past due 60 - 90 days	485	-	2,248	2,733
Past due more than 90 days	1,843	21,517	-	23,360
Total	**15,116**	**21,517**	**24,238**	**60,871**

The Consolidated Entity holds collateral with pledged amount totalling $83.4m for assets which are past due but not impaired as at 31 December 2018 ($78.8m as at 31 December 2017). The pledged amount of collateral is based on market value of the collateral and is capped to the value of the total approved loan limit.

25 Financial risk management (continued)

(b) Credit risk (continued)

The breakdown of the gross amount of individually impaired loans and advances by class is presented in the table below.

	2018 $'000	2017 $'000
Impaired loans		
Corporate Entities		
- SMEs	-	-
Individuals	96	-
Total	96	-

The Consolidated Entity held collateral with nil carrying value totalling the impaired assets as at 31 December 2018.

The Consolidated Entity monitors concentration of risk by sector categories. The table below breaks down the Consolidated Entity’s maximum credit exposure at their gross carrying amounts (i.e. gross of provisions) as categorised by the industry sectors of the counterparties.

31 December 2018
$'000's

		Corporate entities		
Industry type	**Individuals (Retail Customers)**	**Large Corporate Entities**	**SMEs**	**Total**
Manufacturing	13,723	-	10,803	24,526
Tourism	6,097	-	5,041	11,138
Domestic trade	39,387	15,534	229,897	284,818
Construction, Trade, Property Investment	72,112	68,388	173,905	314,405
Housing	954,526	-	14,175	968,701
Cultural, Recreational & Religious Org	909	11,314	15,773	27,996
Professional	63,977	668	52,984	117,629
Transport	2,179	-	-	2,179
Other	3,310	-	4,749	8,059
Total	1,156,220	95,904	507,327	1,759,451

25 Financial risk management (continued)

(b) Credit risk (continued)

31 December 2017
$'000's

		Corporate entities		
Industry type	**Individuals (Retail Customers)**	**Large Corporate Entities**	**SMEs**	**Total**
Manufacturing	11,357	249	15,556	27,162
Tourism	6,656	-	6,166	12,822
Domestic trade	30,328	17,778	150,378	198,483
Construction, Trade, Property Investment	73,895	128,394	238,633	440,922
Housing	665,514	-	301	665,815
Cultural, Recreational & Religious Org	913	11,942	16,611	29,466
Professional	46,484	-	47,316	93,800
Transport	2,972	328	207	3,507
Other	528	-	2,233	2,760
Total	838,647	158,691	477,400	1,474,738

(iii) *Impaired assets and calculation of ECL*

Please refer to Note 1 (i), (k) and (j) for futher details of impaired assets and calculation of ECL in relation to credit risk

25 Financial risk management (continued)

(b) Credit risk (continued)

(iii) Impaired assets and calculation of ECL (continued)

The table below analyse the movement of the gross balance (gross of provision) of customer loans and advances during the year.

	'000s			
	Stage 1	**Stage 2**	**Stage 3**	**TOTAL**
Opening Loans & Advances 1 January 2018	1,286,344	32,182	23,359	**1,341,885**
2018 Movements	-	-	-	
Closed Loans	(268,558)	(11,358)	(2,116)	**(282,032)**
New Loans	520,090	10,118	201	**530,409**
Transfer to Stage 1	2,205	(3,799)	1,594	**-**
Transfer to Stage 2	(15,710)	32,486	(16,776)	-
Transfer to Stage 3	-	(11)	11	-
Movement in Balances	(32,809)	35	(4,464)	**(37,238)**
Balance as at 31 December 2018	**1,491,562**	**59,653**	**1,809**	**1,553,024**

The table below analyse the movement of the ECL of customer loans and advances during the year.

	'000s			
	Stage 1	**Stage 2**	**Stage 3**	**TOTAL**
Opening ECL 1 January 2018	774	371	4,298	**5,443**
2018 Movements	-	-	-	
Closed Loans	(252)	(167)	(298)	**(717)**
New Loans	207	28	54	**289**
Transfer to Stage 1	1	-	(1)	-
Transfer to Stage 2	12	3,984	(3,996)	-
Transfer to Stage 3	(2)	-	2	-
Increases due to change in credit risk	177	196	149	**522**
Decreases due to change in credit risk	(131)	(3,968)	-	**(4,099)**
Provisions as at 31 December 2018	**786**	**444**	**208**	**1,438**

25 Financial risk management (continued)

(b) Credit risk (continued)

(iii) Impaired assets and calculation of ECL (continued)

The tables below analyse the movement of the gross balance, and ECL, respectively of Treasury assets and trade exposures with Bank counterparties during the year.

	Gross Balance			ECL		
	Due from other financial institutions	**Investments at amortised cost**	**Loan and advances-Trade**	**Due from other financial institutions**	**Investments at amortised cost**	**Loan and advances-Trade**
	$'000	$'000	$'000	$'000	$'000	$'000
31 December 2018						
Stage 1	79,003	388,162	206,427	54	120	75
Stage 2	-	-	-	-	-	-
Stage 3	-	-	-	-	-	-
Total	**79,003**	**388,162**	**206,427**	**54**	**120**	**75**

	Gross Balance			ECL		
	Due from other financial institutions	**Investments at amortised cost**	**Loan and advances-Trade**	**Due from other financial institutions**	**Investments at amortised cost**	**Loan and advances-Trade**
	$'000	$'000	$'000	$'000	$'000	$'000
1 January 2018						
Stage 1	26,571	462,735	132,853	-	98	60
Stage 2	-	-	-	-	-	-
Stage 3	-	-	-	-	-	-
Total	**26,571**	**462,735**	**132,853**	**-**	**98**	**60**

25 Financial risk management (continued)

(b) Credit risk (continued)

(v) Settlement risk

The Consolidated Entity’s activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed.

For certain types of transactions, the Consolidated Entity mitigates this risk by conducting settlements through a clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval/limit monitoring process described earlier. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals from Group Risk Management.

The table below presents an analysis of gross investments and financial assets due from other financial institutions by rating agency designation at 31 December 2018 and 31 December 2017, based on S&P (or their equivalent)’s ratings.

	Investments at amortised cost $'000	Due from other financial institutions $'000	Total $'000
31 December 2018			
AA- to AA+	286,572	19,405	305,977
A- to A+	90,799	1,843	92,642
BBB- to BBB+	10,791	-	10,791
Unrated	-	57,755	57,755
Total	388,162	79,003	467,165

	Investments at amortised cost $'000	Due from other financial institutions $'000	Total $'000
31 December 2017			
AA- to AA+	462,735	12,295	475,030
A- to A+	-	-	-
BBB- to BBB+	-	3,322	3,322
Unrated	-	10,954	10,954
Total	462,735	26,571	489,306

25 Financial risk management (continued)

(c) Market risk

The Consolidated Entity is exposed to market risk, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate and foreign currency instruments, which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads and foreign exchange rates.

The market risks arising from non-trading activities are concentrated in Treasury and are separately monitored by Risk. Regular reports are submitted to the Board of Directors and ALCO (Asset and Liabilities Committee).

Non-trading portfolios primarily arise from the interest rate management of the Consolidated Entity's retail and commercial banking assets and liabilities. Foreign exchange risks arise from the Consolidated Entity's non-trading portfolios of investments at amortised cost.

(i) Interest rate risk

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps, and by having pre-approved limits for re-pricing bands. Refer to note 25(c) (iii) for result of sensitivity analysis on interest rate movement.

The ALCO is the monitoring body for compliance with these limits and is assisted by Risk in its day-to-day monitoring activities.

The following tables represent the Consolidated Entity's non-trading portfolios by the earlier of contractual repricing or maturity date as at 31 December 2018 and the prior year. The total will not reconcile to the Consolidated Entity's total assets on the balance sheet as non-financial assets have been excluded from the table below.

25 Financial risk management (continued)

(c) Market risk (continued)

(i) Interest rate risk (continued)

31 December 2018	Note	Floating Interest Rate[1] $'000	1 Year or less $'000	Over 1 to 5 Years $'000	More than 5 Years $'000	Non-interest bearing $'000	Total $'000
		The earlier of maturity or repricing date					
Financial assets							
Cash and liquid assets	7	57,618	-	-	-	-	57,618
Due from other financial institutions	8	17,875	61,074	-	-	-	78,949
Investments at amortised cost	9	284,308	17,980	79,570	6,184	-	388,042
Loans and advances	10	1,698,902	24,061	34,881	-	-	1,757,844
Derivative financial assets	19	85	-	-	-	-	85
		2,058,788	103,115	114,451	6,184	-	2,282,538
Financial liabilities							
Due to other financial institutions	16	11,111	37,036	-	-	-	48,147
Deposits	18	516,015	1,435,974	4,612	-	-	1,956,601
Derivative financial liabilities	19	5,168	-	-	-	-	5,168
		532,294	1,473,010	4,612	-	-	2,009,916
Interest rate swaps[2]		-	128,000	(122,000)	(6,000)	-	-
Interest rate gap		1,526,494	(1,241,895)	(12,161)	184	-	272,622

1. Includes assets and liabilities for which the Consolidated Entity or the counter party has the contractual right to reset interest rate at any time.

2. Notional principal amounts

Comparative 2017 table is set out on the next page.

25 Financial risk management (continued)

(c) Market risk (continued)

(i) Interest rate risk (continued)

31 December 2017

		The earlier of maturity or repricing date					
	Note	Floating Interest Rate[1] $'000	1 Year or less $'000	Over 1 to 5 Years $'000	More than 5 Years $'000	Non-interest bearing $'000	Total $'000
Financial assets							
Cash and liquid assets	7	122,047	-	-	-	-	122,047
Due from other financial institutions	8	15,616	10,955	-	-	-	26,571
Investments at amortised cost	9	348,620	33,701	80,414	-	-	462,735
Loans and advances	10	1,423,386	11,973	39,085	-	-	1,474,444
Derivative financial assets	19	3,361	-	-	-	-	3,361
		1,913,030	56,629	119,499	-	-	2,089,158
Financial liabilities							
Due to other financial institutions	16	6,245	-	-	-	-	6,245
Securities sold and under repurchase agreement	17	-	85,173	-	-	-	85,173
Deposits	18	477,195	1,253,605	1,875	-	-	1,732,675
Derivative financial liabilities	19	120	-	-	-	-	120
		483,560	1,338,778	1,875	-	-	1,824,213
Interest rate swaps[2]		-	143,200	(143,200)	-	-	-
Interest rate gap		1,429,470	(1,138,949)	(25,576)	-	-	264,945

1. Includes assets and liabilities for which the Consolidated Entity or the counter party has the contractual right to reset interest rate at any time.

2. Notional principal amounts

25 Financial risk management (continued)

(c) Market risk (continued)

(ii) Foreign exchange risk

The Consolidated Entity does not hold a trading book (positions created from trading activities with a speculative purpose). The Consolidated Entity is exposed to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily. The table below summarises the Consolidated Entity's exposure to foreign currency exchange rate risk at year-end.

31 December 2018

$'000	EUR	USD	STG	AUD	Other currency	Total
Cash and liquid assets	9	330	-	56,516	763	57,618
Due from other financial institutions	8,616	43,048	-	24,036	3,249	78,949
Investments at amortised cost	-	-	-	388,042	-	388,042
Loans and advances	216	212,211	-	1,545,417	-	1,757,844
Derivative financial asset	-	-	-	85	-	85
Plant and equipment	-	-	-	3,711	-	3,711
Intangible assets	-	-	-	7,990	-	7,990
Deferred tax assets	-	-	-	2,850	-	2,850
Other assets	-	-	-	5,343	-	5,343
Total assets	**8,841**	**255,589**	**-**	**2,033,990**	**4,012**	**2,302,432**
Due to other financial institutions	-	40,355	-	7,792	-	48,147
Deposits	10,208	22,702	-	1,920,378	3,313	1,956,601
Current tax liability	-	-	-	(387)	-	(387)
Derivative liabilities	-	-	-	5,168	-	5,168
Provisions	-	-	-	2,958	-	2,958
Other liabilities	-	-	-	5,297	-	5,297
Total liabilities	**10,208**	**63,057**	**-**	**1,941,206**	**3,313**	**2,017,784**
Shareholders' equity	-	-	-	284,648	-	284,648
Total liabilities and shareholders' equity	10,208	63,057	-	2,225,854	3,313	2,302,432
Net on-balance sheet position	(1,367)	192,532	-	(191,864)	699	-
Effect of derivatives held for risk management	-	(185,900)	-	185,900	-	-
Net currency position	(1,367)	6,632	-	(5,964)	699	-

Comparative 2017 table is set out on the next page.

25 Financial risk management (continued)

(c) Market risk (continued)

(ii) Foreign exchange risk (continued)

31 December 2017

$'000	**EUR**	**USD**	**STG**	**AUD**	**Other currency**	**Total**
Cash and liquid assets	80	254	-	121,031	682	122,047
Due from other financial institutions	10,658	8,031	-	5,139	2,743	26,571
Investments at amortised cost	-	-	-	462,735	-	462,735
Loans and advances	423	137,765	-	1,336,256	-	1,474,444
Derivative financial asset	-	-	-	3,361	-	3,361
Plant and equipment	-	-	-	3,524	-	3,524
Intangible assets	-	-	-	5,387	-	5,387
Deferred tax assets	-	-	-	1,773	-	1,773
Other assets	-	-	-	4,649	-	4,649
Total assets	**11,161**	**146,050**	**-**	**1,943,855**	**3,425**	**2,104,491**
Due to other financial institutions	-	-	-	6,245	-	6,245
Securities sold and	-	-	-	-	-	
under repurchase agreements	-	-	-	85,173	-	85,173
Deposits	11,444	22,322	-	1,696,345	2,564	1,732,675
Current tax liability	-	-	-	1,041	-	1,041
Derivative liabilities	-	-	-	120	-	120
Provisions	-	-	-	2,711	-	2,711
Other liabilities	-	-	-	8,284	-	8,284
Total liabilities	**11,444**	**22,322**	**-**	**1,799,919**	**2,564**	**1,836,249**
Shareholders' equity	-	-	-	268,241	-	268,241
Total liabilities and shareholders' equity	**11,444**	**22,322**	**-**	**2,068,160**	**2,564**	**2,104,490**
Net on-balance sheet position	(283)	123,728	-	(124,305)	861	-
Effect of derivatives held for risk management	-	(71,818)	-	71,818	-	-
Net currency position	(283)	51,910	-	(52,487)	861	-

25 Financial risk management (continued)

(c) Market risk (continued)

(iii) Sensitivity analysis

The management of interest rate and foreign exchange risk against interest rate and foreign currency limits is supplemented by monitoring the sensitivity of the Consolidated Entity's financial assets and liabilities to potential standard interest rate and currency fluctuations.

The sensitivity analysis on interest rate risk is performed using the methodology of GAP IRR. The GAP IRR methodology is a method of measuring interest rate sensitivity by classifying interest rate sensitive assets, liabilities and off-balance sheet items. The instruments are split into specific pre-defined time buckets according to their maturity for fixed rate instruments, or till next re-pricing date for variable rate instruments. The size of the gap position can then be determined in each of the respective time buckets. A cumulative gap can also then be given after summing up the individual time bucket gaps. Result of the analysis is as follows:

An increase or decrease of 50 basis points in the yield curve is expected to result in a gain or loss of approximately $513,349 (2017: $580,450) on profit or loss and the same amount of increase or decrease in balance sheet assets.

The sensitivity analysis on foreign currency risk is performed by calculating the impact on the Consolidated Entity's net currency exposure in the case of a 10% increase or decrease in all foreign currency exchange rates. Result of the analysis is as follows:

An increase in currency exchange rates by 10% is expected to result in a loss of approximately $3,700 (2017: Loss $3,424) on the profit and loss and the same amount of increase in balance sheet assets. A decrease in currency exchange rates by 10% is expected to result in a gain of approximately $5,204 (2017: Gain $4,724).

(d) Liquidity risk

Liquidity risk is the risk that the Consolidated Entity will encounter difficulty in meeting obligations from its financial instruments.

The Consolidated Entity measures and manages this risk based on an analysis of the maturity profile. The management of liquidity risk for the Consolidated Entity is based on the following:

(i) Measurement and limitation of maturity profile

The maturity profile is measured on a daily basis by monitoring the mismatch of maturing assets against maturing liabilities within prescribed maturity buckets. The cumulative maturity mismatch limit is -2% out to seven days with an internal trigger of 0.5% and the cumulative negative mismatch out to one month must not exceed 15% of total liabilities.

The gross nominal outflow disclosed below is the contractual, undiscounted cash flow on the financial liability. The balances include the expected interest payable on maturity. The disclosure for derivatives shows a net amount for derivatives that are net settled, but a gross inflow and outflow amount for derivatives that have simultaneous gross settlement.

25 Financial risk management (continued)

(d) Liquidity risk (continued)

31 December 2018 $'000	Repayable on demand	3 mths or less	Over 3 mths but less then 1 yr	Over 1 but less then 5 yrs	Over 5 yrs	Total
Non-derivative liabilities						
Due to other financial institutions	48,147	-	-	-	-	48,147
Deposits	516,015	810,323	635,066	4,689	-	1,966,093
	564,162	810,323	635,066	4,689	-	2,014,240
Derivative liabilities						
Derivatives held for hedging:						
- Interest rate swaps	-	120	1,448	4,906	1,225	7,699
- Foreign currency swaps	-	4,003	-	-	-	4,003
	-	4,123	1,448	4,906	1,225	11,702
Off balance sheet commitments						
Bank guarantee	6,286	-	-	-	-	6,286
Loan commitments	168,932	-	-	-	-	168,932
Trade Finance contingencies	17,528	-	-	-	-	17,528
	192,746	-	-	-	-	192,746
Total	**756,908**	**814,446**	**636,514**	**9,595**	**1,225**	**2,218,688**

Comparative 2017 table is set out on the next page.

25 Financial risk management (continued)

(d) Liquidity risk (continued)

31 December 2017 $'000	Repayable on demand	3 mths or less	Over 3 mths but less then 1 yr	Over 1 but less then 5 yrs	Over 5 yrs	Total
Non-derivative liabilities						
Due to other financial institutions	6,245	-	-	-	-	6,245
Securities sold and under repurchase agreements	-	85,258	-	-	-	85,258
Deposits	477,195	830,998	429,504	1,875		1,739,572
	483,440	916,256	429,504	1,875	-	1,831,075
Derivative liabilities						
Derivatives held for hedging:						
- Interest rate swaps	-	346	984	3,935	-	5,265
- Foreign currency swaps	-	46	-	-	-	46
	-	392	984	3,935	-	5,311
Off balance sheet commitments						
Bank guarantee	10,182	-	-	-	-	10,182
Loan commitments	161,655	-	-	-	-	161,655
Trade Finance contingencies	26,510	-	-	-	-	26,510
	198,348	-	-	-	-	198,348
Total	**681,787**	**916,648**	**430,488**	**5,810**	**-**	**2,034,733**

26 Capital management

The Consolidated Entity’s regulator, Australian Prudential Regulation Authority (APRA), sets minimum capital requirements for the Consolidated Entity. The Board determines the internal capital requirements of the Bank. In implementing current capital requirements, APRA requires the Consolidated Entity to maintain a prescribed ratio of total capital to total risk-weighted assets.

The Consolidated Entity’s regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes ordinary share capital, retained earnings after deductions for intangible assets;
- Tier 2 capital, which includes general reserve for credit losses.

Various limits are applied to elements of the capital base.

Risk weighted assets are determined according to specific requirements that seek to reflect the varying level of risk attached to assets and off-balance sheet exposures. Regulatory capital is managed using the Basel III standard methodology.

The Consolidated Entity has complied with all externally imposed capital requirements throughout the period. There have been no material changes in the Consolidated Entity’s management of capital during the period.

The Board has a duty to ensure that the level and quality of capital are maintained commensurate with the type, amount and concentration of risks to which the Consolidated Entity is exposed from its activities. In doing so, the Board must have regards to any prospective changes in the Consolidated Entity's risk profile and capital holdings.

Capital management must be an integral part of the Consolidated Entity's risk management framework through the alignment of its risk appetite and risk profile to its capacity to absorb losses.

The processes and procedures of managing capital are set out in the Consolidated Entity's Capital Management Plan (CMP). The CMP sets out the responsibilities for the monitoring, managing and reporting of the Consolidated Entity's capital position. The strategic planning process incorporates the capital requirements to support projected loan growth. Management must take relevant action where expected capital injection is either delayed or not forthcoming.

Full disclosures required under Pillar 3, per prudential standard APS 330 “Public Disclosure”, are provided on the Consolidated Entity’s website.

26 Capital management (continued)

The Consolidated Entity's regulatory capital position at 31 December was:

	Note	2018 $'000	2017 $'000
Tier 1 Capital			
Ordinary share capital	22	210,000	200,000
Retained profits	23	70,105	60,553
Cash flow hedge reserve	24	(1,182)	(85)
Less Deductions:			
Intangible assets	12	7,990	5,387
Deferred tax assets	14	2,850	1,773
Fair value of cash flow hedges	24	(1,182)	(85)
Loan Origination Fees		2,359	1,727
ECL adjustment		(1,181)	(206)
Securitisation start-up costs		225	249
Total		267,862	251,828
Tier 2 Capital			
General reserve for credit losses		8,178	11,104
Total		8,178	11,104
Total regulatory capital		**276,040**	**262,932**
Risk weighted assets		1,201,232	1,143,958
Capital ratios			
Total regulatory capital as % of risk weighted assets		22.98%	22.98%
Total tier 1 capital as % of risk weighted assets		22.30%	22.01%

27 Fair value measurement

Fair values of financial assets and liabilities
Fair value is the price that would be received for an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value estimates were determined by the following methodologies and assumptions:

Cash and liquid assets
The carrying values of cash and liquid assets approximate their fair values, as they are short term in nature.

Due from other financial institutions
The carrying value of amounts due from other financial institutions approximates their fair value, as they are short term.

Investments at amortised cost
For fixed term deposits and bank bills, the carrying amount is a reasonable estimate of net fair value, as they are short term in nature. The net fair value of floating rate notes and fixed rate bonds are calculated by using current bid price in an active market.

Loans and advances
The carrying value of loans and advances is net of specific provisions for impairment. For variable loans and loans with rates fixed for a period less than six months, the carrying amount is a reasonable estimate of net fair value. The fair value of fixed rate loans greater than six months was calculated by discounting the future interest cash flows using a discount rate based on the current market rate, assuming constant interest rate spreads, for the average remaining term.

Due to other financial institutions, securities sold and repurchase agreement, and deposits
The carrying value of amounts due within six months to other financial institutions and other depositors, and securities sold and repurchase agreement approximate their net fair value. The net fair value of liabilities with a longer maturity has been determined by using the discount methodology described above.

Interest rate swaps
The net fair value of interest rate swap instruments have been determined by valuing them at the current market rates, being the discounted present value of the future cash flows.

FX swaps and foreign currency forward contracts
The fair value of FX swap and foreign currency forward contract instruments have been determined by valuing them at the current market value, being the discounted present value of the future cash flows.

27 Fair value measurement (continued)

The carrying amounts and estimated fair values of financial assets and liabilities are as follows:

	2018		2017	
	Carrying value	Fair value	Carrying value	Fair value
	$'000	$'000	$'000	$'000
Assets				
Cash and liquid assets	57,618	57,618	122,047	122,047
Due from other financial institutions	78,949	78,949	26,571	26,571
Investments at amortised cost	388,042	389,805	462,735	466,482
Loans and advances	1,757,844	1,758,378	1,474,444	1,474,993
Derivative financial assets	85	85	3,361	3,361
Liabilities				
Due to other financial institutions	48,147	48,147	6,245	6,245
Securities sold and under repurchase agreements	-	-	85,173	85,173
Deposits	1,956,601	1,956,586	1,732,675	1,732,644
Derivative financial liabilities	5,168	5,168	120	120

Fair value hierarchy

The table below analyses financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Level 1: quoted prices (adjusted) in active markets for identical assets and liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). For example, interest rates and yield curves observable at commonly quoted intervals, volatilities or credit risk;
- Level 3: inputs for the asset or liability that are not based on observable market data.

	Level 1	**Level 2**	**Level 3**	**Total**
31 December 2018				
Derivative financial assets	-	85	-	85
Total	**-**	**85**	**-**	**85**
Derivative financial liabilities	-	5,168	-	5,168
Total	**-**	**5,168**	**-**	**5,168**

	Level 1	**Level 2**	**Level 3**	**Total**
31 December 2017				
Derivative financial assets	-	3,361	-	3,361
Total	**-**	**3,361**	**-**	**3,361**
Derivative financial liabilities	-	120	-	120
Total	**-**	**120**	**-**	**120**

27 Fair value measurement (continued)

Fair value hierarchy (continued)

The following illustrates the fair value of financial assets and liabilities not measured at fair value:

31 December 2018	**Level 1**	**Level 2**	**Level 3**	**Total**
Cash and liquid assets	-	57,618	-	57,618
Due from other financial institutions	-	78,949	-	78,949
Investments at amortised cost	-	389,805	-	389,805
Loans and advances	-	1,758,378	-	1,758,378
Total	**-**	**2,284,750**	**-**	**2,284,750**
Due to other financial institutions	-	48,147	-	48,147
Securities sold and under repurchase agreement	-	-	-	-
Deposits	-	1,956,586	-	1,956,586
Total	**-**	**2,004,733**	**-**	**2,004,733**

31 December 2017	**Level 1**	**Level 2**	**Level 3**	**Total**
Cash and liquid assets	-	122,047	-	122,047
Due from other financial institutions	-	26,571	-	26,571
Investments at amortised cost	-	466,482	-	466,482
Loans and advances	-	1,474,993	-	1,474,993
Total	**-**	**2,090,092**	**-**	**2,090,092**
Due to other financial institutions	-	6,245	-	6,245
Securities sold and under repurchase agreement	-	85,173	-	85,173
Deposits	-	1,732,644	-	1,732,644
Total	**-**	**1,824,063**	**-**	**1,824,063**

28 Commitments for expenditure

	2018	2017
	$'000	$'000
Operating leases		
Future operating lease rentals not provided for and payable:		
Not later than one year	2,257	2,904
Later than one year but no later than two years	1,746	2,248
Later than two years but no later than five years	1,056	2,900
Later than five years	-	-
Total	5,059	8,052

29 Auditors' remuneration

Amounts paid or due and payable to the Auditors of the Consolidated Entity for:

	$	$
Auditing the financial report	329,676	284,900
Taxation services	19,800	29,293
Other non-audit services	57,310	254,162
Total	406,786	568,355

All amounts include 10% GST.

30 Commitments and contingencies

The Consolidated Entity has financial instruments with off-balance sheet risk in the normal course of business to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates.

Details of financial instruments with off-balance sheet risk are as follows (Face value in $000s):

Credit related instruments:		
Letters of Guarantee given in the normal course of business	6,286	10,182
Commitments to extend credit	168,932	161,655
Trade finance contingencies	17,528	26,510
Total	192,746	198,348

31 Directors' remuneration

Directors' income

The number of Directors of the Consolidated Entity whose income from the Consolidated Entity or related bodies corporate falls within the following bands:

$20,000 - $29,999	-	-
$50,000 - $59,999	-	1
$70,000 - $79,999	-	1
$80,000 - $89,999	2	4
$90,000 - $99,999	2	1
$100,000 - $109,999	2	-
$150,000 - $159,999	1	1
	7	8

31 Directors' remuneration (continued)

	2018 $	2017 $
Total income received, or due and receivable, by all Directors of the Consolidated Entity:		
Short term benefits	660,015	662,147
Other long term benefits	73,213	62,904
Total benefits to non-executive Directors	733,228	725,051

32 Key management personnel disclosures

Unless otherwise indicated the following were key management personnel of the Consolidated Entity during the reporting period:

Non-executive Directors
Mr Nicholas Pappas AM (Chairman)
Mr Nikolas T Hatzistergos
Mr Greg Gav
Mr Hon Steve Bracks AC
Mr Fouad Chaker
Mr Ben Edney
Mr Roger Dagher

Executives
Mr Miltiades Michaelas (Chief Executive Officer)
Mr Steven Pasas (Chief Operating Officer resigned 19/10/2018)
Mr Gary English (Chief Risk Officer)
Mr Fawaz Sankari (Executive General Manager – Chief Banking Officer)
Ms Diana Sitnikoski (Head of Credit)
Mrs Chrystalla Vougamalis (Chief Customer Officer)

	2018	2017
	$	$

32 Key management personnel disclosures (continued)

Transactions with key management personnel
The key management personnel benefits included in staff expenses are as follows:

	2018	2017
Short term benefits	2,564,849	2,793,647
Long term benefits	10,563	51,802
Other long term benefits	129,957	185,803
Total benefit	2,705,369	3,031,252

Details of non-executive Directors' remuneration are set out separately in Note 31. No other remuneration benefits were paid to key management personnel.

Loans and other transactions to key management personnel
Details of loans and other transactions with key management personnel, including their related parties, are as follows:

	2018	2017
Loans to key management personnel	13,554,984	20,638,815
Deposit accounts	17,190,631	33,289,954

For all loans and deposits to key management personnel, interest is determined at prevailing market rates and are on normal commercial terms and conditions. Further, loans provided are secured by collateral.

Other key management personnel transactions with the Consolidated Entity
Key management personnel of the Consolidated Entity hold positions in other entities that result in them having control or significant influence over the financial or operating policies of those entities.

One of those entities transacted with the Company in the reporting period. The terms and conditions of the transaction were no more favourable than those available, or which might reasonably be expected to be available, on similar transactions to non-director related entities on an arm's length basis. Details are as follows:

Director	Transaction	Note	2018	2017
			$	$
Mr Greg Gav	Rental Payments	(i)	956,499	943,200

(i) In 2016, the Consolidated Entity renewed its lease of head office with an entity related to Mr Greg Gav, to May 2019. This transaction was entered into on normal terms and conditions.

33 Related party transactions

(a) Transactions within the wholly-owned group

During the financial year the Consolidated Entity engaged in banking transactions with Bank of Beirut s.a.l., and it's wholly owned subsidiaries. All transactions were on normal terms and conditions. Please refer to notes 2, 3, 8, 9, 16, 19 and 20 for details of transactions and balances within the wholly-owned group.

(b) Transactions with other related parties

During the period the Consolidated Entity engaged in banking transactions with associated companies of Bank of Beirut s.a.l. All transactions were on normal commercial terms and conditions.

Please refer to notes 2, 3, 8, 9, 16, 19 and 20 for details of transactions and balances with other related parties.

(c) Parent entity

The parent entity of the Consolidated Entity is Bank of Beirut s.a.l., a company incorporated in Lebanon.

(d) Key Management Personnel

Key Management Personnel and their close family members are also considered related parties. Transactions and balances with them are disclosed in Note 32. The related party disclosures in consolidated statement of profit and loss do not include interest income or expense on Key Management Personnel loans and deposits.

34 Financial reporting by segments

The Consolidated Entity does not have any separately reportable segments.

35 Notes to the statement of cash flows

For the purposes of the statement of cash flows, cash includes cash on hand, cash at bank and short term deposits at call. Cash as at the end of the period as shown in the statement of cash flows is reconciled to the related items in the balance sheet as follows:

(a) Reconciliation of cash

	2018 $'000	2017 $'000
Cash	57,618	122,047
Due from other financial institutions - at call deposits	78,949	26,571
Total Cash and cash equivalents	136,567	148,618

Bank of Sydney Ltd
Notes to and forming part of the financial report (continued)
For the year ended 31 December 2018

35 Notes to the statement of cash flows (continued)

(b) Reconciliation of profit from ordinary activities after income tax to net cash used in operating activities

	2018 $'000	2017 $'000
Profit from ordinary activities after income tax	11,219	11,005
Add: non-cash items:		
Depreciation and amortisation of non-current assets	2,417	1,653
Increase/(Decrease) in specific provision	95	(46)
Increase/(Decrease) in ECL	(3,914)	31
Increase in provision for employee entitlements	247	385
Decrease in tax provision	(443)	(789)
Net Increase in prepayments/accruals	96	(670)
Loss on writing off plant and equipment	-	-
Loss from Loan write offs	-	-
Increase in derivative financial instruments	(1,602)	252
(Increases)/decreases in assets and increases/(decreases)in liabilities:		
Interest accruals	1,759	(1,302)
Loans and advances	(284,248)	(202,165)
Derivative Assets	3,695	(4,823)
Other assets	(2,422)	(945)
Due to other financial institutions	41,850	(10,895)
Deposits	221,985	240,017
Derivative liabilities	5,084	-
Sales and repurchase agreement	(85,068)	(5,730)
Other liabilities	(1,776)	1,055
Net cash used in operating activities	(91,026)	27,033

(c) Net reporting of certain cash flows

Cash flows arising from the following activities have been presented on a net basis in the statement of cash flows:

(i) Money market trading and lending activities;
(ii) Customer deposits to and withdrawals from savings, money market and other deposit accounts; and
(iii) Balances due to and from other financial institutions.

36 Events subsequent to balance date

On 1 March 2019 the Bank entered into an agreement to purchase 62 Pitt Street, located in the Central Business District of Sydney, for $50m.

Other than the matter mentioned above, there has not arisen in the interval between the end of the financial year and the date of this report any item, any other transaction or event of a material and unusual nature likely, in the opinion of the directors of the Consolidated Entity, to affect significantly the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity, in future financial years.

37 Parent entity information

The accounting policies of the parent entity, which have been applied in determining the financial information shown below, are the same as those applied to the Consolidated Entity. Refer to note 1 for a summary of the significant accounting policies relating to the Consolidated Entity.

Financial Position	2018 $'000	2017 $'000
Assets		
Cash and liquid assets	57,618	122,047
Due from other financial institutions	67,527	22,440
Investments at amortised cost	388,042	462,735
Loans and advances		
- Held by Parent Entity	1,426,426	1,285,520
- Held by Trust subject to securitisation	331,418	188,923
Derivative financial assets	85	3,361
Intangible assets	7,990	5,387
Plant and equipment	3,711	3,524
Deferred tax assets	2,850	1,773
Other assets	5,343	4,649
Receivable from securitisation Trust	11,422	4,131
Total assets	**2,302,432**	**2,104,490**
Liabilities		
Due to other financial institutions	48,147	6,245
Securities sold and under repurchase agreement	-	85,173
Deposits	1,956,601	1,732,675
Current tax liability	(387)	1,041
Derivative liabilities	5,168	120
Subordinated liabilities	-	-
Provisions	2,958	2,711
Other liabilities	5,297	8,284
Total liabilities	**2,017,784**	**1,836,249**
Net assets	**284,648**	**268,241**

37 Parent entity information (continued)

Financial Position (continued)	2018 $'000	2017 $'000
Equity		
Contributed equity	210,000	200,000
Reserves	4,543	7,688
Retained profits	70,105	60,553
Total equity	**284,648**	**268,241**

Financial Performance

Profit for the year	11,219	11,005
Other comprehensive income	(1,097)	136
Total comprehensive income	**10,122**	**11,141**

At 31 December 2018, "BHB Residential Securities Trust 1" (the Trust) owes Bank of Sydney (the Company) $342,721,457 which was eliminated on consolidated account level. During 2018, the Company received $8,099,286 as interest income and incurred $2,216,112 in operating expenses from its 100% owned internal securitisation of the Trust which was also fully eliminated on consolidated account level.

38 Securitisation

Details of the Consolidated Entity's internal securitisation at the end of the reporting period are as follows:

Name of securitisation	Principal activity	Place of incorporation and operation	Proportion of ownership interest by the Consolidated Entity
BHB Residential Securities Trust 1	Contingent Liquidity Reserve Facility	Australia	100%

38 Securitisation (continued)

During 2013, the Company packaged equitable interests in residential mortgage backed mortgage loans and transferred to “BHB Residential Securities Trust 1” (the Trust), which issued securities backed by the same loans and sold back to the Company. The Company retained risks and rewards of the subject loans as being the sole unit holder and beneficiary of the Trust in this “internal securitisation” program. The purpose of setting up the Trust was to provide a contingency liquidity reserve facility to meet any future liquidity crisis that the Company may face due to either internal or external factors.

On 13 March 2013, the Trust issued one Participation Unit ($10 each) and ten Residual Units ($10 each), all of which (100%) were purchased by the Company. Class A Notes of $197.3m and Class B Notes of $16m (total $213.3m) were issued by the Trust and all purchased by the Company. The proceeds from the above issue were used to purchase a parcel of triple A rated residential mortgage loans (rated by Moody’s) of $206.7m from the Company.

On 22 August 2018, the Company carried out a “top-up” of the Trust in order to meet Securitisation contingency funding requirements, which includes buying back of Class A Notes issued in 2017 with carrying amount of $146.2m at nil consideration and reissuing new Class A Notes of $327.9m. There was also a buy- back of Class B Notes of $19m at nil consideration with a reissue of new Class B Notes of $32m.The additional proceeds of $194.7m from Note Issue were used to purchase a further parcel of triple A rated Residential Mortgage Loans from the Company. Class A Notes qualifies for repurchase with the Reserve Bank of Australia.

As the Company owns 100% of the issued units in the Trust and has control over the Trust as defined in AASB 10 - Consolidated Financial Statements(Note b), the Trust will be accounted for as the Company’s 100% owned subsidiary.

Where relevant, credit risk, market risk and liquidity risk arising from internal securitisation transactions are captured and monitored in the Consolidated Entity’s normal risk management framework and processes. The table below presents assets securitised by the Consolidated Entity:

	2018 $'000	2017 $'000
Internal Securitisation assets		
Residential Mortgage	331,418	188,923
Cash and accrued income	11,422	4,131
	342,840	193,054

Note: cash and accrued income are held by the asset securitisation vehicles, which have not yet been distributed to the note holders.

Bank of Sydney Ltd
Directors' declaration

1 In the opinion of the Directors of the Consolidated Entity:

(a) the financial statements, set out on pages 8 to 64, are in accordance with the Corporation Act 2001, including:

(i) giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2018 and of its performance, for the financial year ended on that date;
(ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the Corporations Regulations 2001;

(b) there are reasonable grounds to believe that the Consolidated Entity will be able to pay its debts as and when they become due and payable.

2 The Directors draw attention to Note 1(b) to the financial statements, which include a statement of compliance with International Financial Reporting Standards.

Signed in accordance with a resolution of the Directors made pursuant to s.295(5) of the Corporations Act 2001.

On behalf of the Directors

Nicholas Pappas
Chairman

Sydney, 17 April 2019

Deloitte.

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Independent Auditor's Report to the Members of Bank of Sydney Ltd

Opinion

We have audited the financial report of Bank of Sydney Ltd and its subsidiary (the "Consolidated Entity") which comprises the consolidated statement of financial position as at 31 December 2018, the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, and the director's declaration.

In our opinion, the accompanying financial report of the Consolidated Entity is in accordance with the *Corporations Act 2001*, including:

(i) giving a true and fair view of the Consolidated Entity's financial position as at 31 December 2018 and of its financial performance for the year then ended; and

(ii) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

Basis for Opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Report* section of our report. We are independent of the Consolidated Entity in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

We confirm that the independence declaration required by the *Corporations Act 2001*, which has been given to the directors of the Consolidated Entity**,** would be in the same terms if given to the directors as at the time of this auditor's report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information

The directors are responsible for the other information. The other information comprises the Directors' Report included in the Consolidated Entity's annual financial report for the year ended 31 December 2018, but does not include the financial report and our auditor's report thereon.

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

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

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Responsibilities of the directors for the Financial Report

The directors of the Consolidated Entity are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Consolidated Entity 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 Consolidated Entity or to cease operations, or has no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Financial Report

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is 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 the Australian Auditing Standards 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 this financial report.

As part of an audit in accordance with the Australian Auditing Standards, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial report, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Consolidated Entity's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.

- Conclude on the appropriateness of the director's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Consolidated Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial report or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Consolidated Entity to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial report, including the disclosures, and whether the financial report represents the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Consolidated Entity to express an opinion on the consolidated financial report. We are responsible for the direction, supervision and performance of the Consolidated Entity's audit. We remain solely responsible for our audit opinion.

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

Deloitte Touche Tohmatsu

DELOITTE TOUCHE TOHMATSU

M Stretton

Mark Stretton
Partner
Chartered Accountants

Sydney, 17 April 2019