RBC Royal Bank (Aruba) N.V.

Summary Financial Statements

October 31, 2019

Contents

Independent auditor's report 3

Statements of financial position 5

Statements of income and other comprehensive income 6

Statements of changes in equity 7

Statements of cash flows 8

Notes to the financial statements 9 – 95

Independent auditor's report

To: the managing board and the supervisory board of RBC Royal Bank (Aruba) N.V.

Report on the summary financial statements 2018/2019

Our opinion

In our opinion, the accompanying summary financial statements as per 31 October 2019 and for the year then ended of RBC Royal Bank (Aruba) N.V. (the 'Company'), are consistent, in all material respects, with the audited financial statements, in accordance with the basis described in note 2.

The summary financial statements

The Company's summary financial statements, derived from the audited financial statements 2018/2019, comprise:

- the statement of financial position as at 31 October 2019;
- the statement of income and other comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the related notes to the summary financial statements.

The summary financial statements do not contain all of the disclosures required by International Financial Reporting Standards (IFRS). The financial information to be made public, based on the Directive on the Publication of the Audited Annual Financial Statements and the Supervisory Directives Section III.6 Directive on the Publication of the Audited Annual Financial Statements, issued by the Central Bank of Aruba (together the 'Regulations'), excludes certain disclosures related to the compensation of management and the supervisory board, which are set out in the audited statutory financial statements of RBC Royal Bank (Aruba) N.V.

The audited financial statements and the summary financial statements do not reflect the events that occurred subsequent to the date of our report on the audited financial statements.

The audited financial statements and our auditor's report thereon

We expressed an unmodified audit opinion on the audited financial statements in our report dated 29 January 2020.

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Responsibilities of management for the summary financial statements

Management is responsible for the preparation of the summary financial statements in accordance with the basis described in note 2.

Auditor's responsibility

Our responsibility is to express an opinion on whether the summary financial statements are consistent, in all material respects, with the audited statutory financial statements based on our procedures, which we conducted in accordance with International Standard on Auditing Standard 810 'Engagements to report on summary financial statements'.

Amsterdam, 24 April 2020
PricewaterhouseCoopers Accountants N.V.

Original has been signed by M.S. de Bruin RA

Statement of financial position
(in thousands of Aruban Florins)

		As at October 31,	
		2019	2018
Assets			
Cash and cash equivalents	3	166,740	241,971
Balances with central bank	4	73,650	79,040
Loans	5	556,097	533,374
Securities	6	8,231	17,412
Due from associated and affiliated companies	24	27,405	20,237
Assets classified as held for sale	11	485	485
Other assets	12	8,925	9,360
Intangible assets	7	9,933	12,520
Goodwill	8	-	23,654
Premises and equipment	9	15,098	15,839
Deferred tax assets	10	6,551	4,022
Total assets		873,116	957,914
Liabilities			
Due to banks		639	406
Customers' deposits	13	703,564	774,125
Due to associated and affiliated companies	24	13,285	5,034
Current income tax liabilities		10,195	8,510
Other liabilities	14	13,208	16,194
Deferred tax liabilities	10	620	6,836
Total liabilities		741,511	811,105
Equity attributable to company			
Share capital		43,865	43,865
Share premium		1,000	1,000
Regulatory loan loss reserve		16,699	16,049
Other components of equity	15	1,866	1,866
Retained earnings		68,175	84,029
Total equity attributable to company		131,605	146,809
Total liabilities and equity		873,116	957,914

The total authorized number of shares at period end was unlimited with a par value of AWG 1,000 each. All issued shares were fully paid.

The attached notes set out on pages 9 to 95 form an integral part of these financial statements.

Statement of income and other comprehensive income
(in thousands of Aruban Florins)

		Year ended October 31,	
		2019	2018
Interest income	16	43,712	41,682
Interest expense	17	(4,865)	(6,749)
Net interest income		38,847	34,933
Non-interest income	18	21,030	23,447
Total revenue		59,877	58,380
Non-interest expenses	19	(49,854)	(52,965)
Provision for credit losses on loans	5.1	(7,178)	(3,198)
Impairment losses on goodwill	8	(23,654)	-
Total non-interest expenses		(80,686)	(56,163)
Profit before taxation		(20,809)	2,217
Taxation expense	20	5,891	1,682
Net profit after taxation		(14,918)	3,899
Other comprehensive income, net of taxes:			
Net change in losses on securities		0	222
Other comprehensive income for the year, net of tax		-	222
Total comprehensive income for the year		(14,918)	4,121

The attached notes set out on pages 9 to 95 form an integral part of these financial statements.

Statement of changes in equity
(in thousands of Aruban Florins)

	Share capital	Share premium	Regulatory loan loss reserve	Other components of equity	Retained earnings	Total equity attributable to company
Year ended						
October 31, 2018						
Balance at beginning of the year	43,865	1,000	15,680	1,861	79,152	141,558
Transition adjustment				(217)	1,347	1,130
Balance as at November 1, 2017	43,865	1,000	15,680	1,644	80,499	142,688
Other comprehensive income	-	-	-	222	-	222
Income attributable to shareholders	-	-	-	-	3,899	3,899
Total comprehensive income	-	-	-	222	3,899	4,121
Appropriation to regulatory loan loss reserve	-	-	369	-	(369)	-
Balance at end of the year	43,865	1,000	16,049	1,866	84,029	146,809
Year ended						
October 31, 2019						
Balance at beginning of the year	43,865	1,000	16,049	1,866	84,029	146,809
Transition adjustment	-	-	-	-	(286)	(286)
Balance as at November 1, 2018	43,865	1,000	16,049	1,866	83,743	146,523
Other comprehensive income	-	-	-	-	-	-
Income attributable to shareholders	-	-	-	-	(14,918)	(14,918)
Total comprehensive income	-	-	-	-	(14,918)	(14,918)
Appropriation to regulatory loan loss reserve	-	-	650	-	(650)	0
Balance at end of the year	43,865	1,000	16,699	1,866	68,175	131,605

The attached notes set out on pages 9 to 95 form an integral part of these financial statements.

Statement of cash flows
(in thousands of Aruban Florins)

	Year ended October 31,	
	2019	2018
Operating activities		
Income before taxation	(20,809)	2,217
Adjustments for:		
Depreciation and amortisation	3,922	3,704
Provision for credit losses on loans	7,178	3,198
Impairment losses on goodwill	23,654	-
Losses/(gains) transferred from other components of equity	1	(1)
Gain on sale of premises and equipment	(45)	(1,028)
Operating profit before changes in operating assets and liabilities	13,901	8,090
(Increase)/decrease in operating assets:		
Balances with central bank	5,390	4,225
Loans	(29,901)	(12,233)
Due from associated and affiliated companies	(7,168)	2,042
Other assets	434	8,039
Increase/(decrease) in operating liabilities:		
Customers' deposits	(70,561)	(57,367)
Due to banks	233	(426)
Due from associated and affiliated companies	8,251	(6,435)
Other liabilities	(3,831)	(4,755)
Income taxes paid	(1,073)	-
Cash (used in) / provided by operating activities	(84,325)	(58,820)
Investing activities		
Proceed from sale of securities	9,643	9,560
Acquisition of securities	-	(17,708)
Additions to premises and equipment and intangible assets	(594)	(1,910)
Proceeds from sale of premises and equipment	45	1,355
Cash provided by investing activities	9,094	(8,704)
Net increase / (decrease) in cash and cash equivalents	(75,231)	(67,524)
Cash and cash equivalents at beginning of the year	241,971	309,495
Effects of exchange rate changes on cash and cash equivalents	-	-
Cash and cash equivalents at end of the year	166,740	241,971
Interest received	43,775	41,571
Interest paid	(11,389)	(6,486)

The attached notes set out on pages 9 to 95 form an integral part of these financial statements.

Notes to the financial statements

1 Incorporation and Business Activities

RBC Royal Bank (Aruba) N.V. (the "Bank"), was incorporated under the laws of Aruba on December 18, 1985 and started operations on February 2, 1987. The principal activities of the Bank is commercial and retail banking in Aruba. The address of RBC Royal Bank (Aruba) N.V.'s registered office is Italiëstraat 36, Aruba.

The Bank is a wholly owned subsidiary of RBC Royal Bank N.V., a company incorporated in Curaçao since November 30, 2005, when all shares were acquired from the previous parent ABC Holdings N.V., a company incorporated in Curaçao. Its ultimate parent company is Royal Bank of Canada, a company incorporated in Canada. The address of Royal Bank of Canada's registered office is 200 Bay Street, Royal Bank Plaza, Toronto, Ontario, Canada.

2 Summary of significant accounting policies, estimates and judgments

These Summary Financial Statements have been prepared as required by the Directive on the Publication of the Audited Annual Financial Statements and the Supervisory Directives Section III.6 Directive on the Publication of the Audited Annual Financial Statements, issued by the Central Bank of Aruba (together the "Regulations"). These Summary Financial Statements comprise the Statement of Financial Position, the Statement of Income and Other Comprehensive Income, the Statement of Changes in Equity, the Statement of Cash Flows, and the notes, which include a summary of the significant accounting policies and other explanatory information but which exclude certain disclosures related to the compensation of management and the Supervisory Board, which are set out in the statutory financial statements of RBC Royal Bank (Aruba) N.V.

The principal accounting policies adopted in the preparation of RBC Royal Bank (Aruba) N.V.'s financial statements are set out below. These notes are an extract of the detailed notes prepared in our statutory financial statements. The notes below are consistent in all material aspects with those from which they have been derived. Throughout this report, the word Bank refers to RBC Royal Bank (Aruba) N.V..

Basis of preparation

The financial statements, from which these Summary Financial Statements have been derived, are prepared in Aruban Florins (AWG) and in accordance with International Financial Reporting Standards. The financial statements are prepared under the historical cost convention as modified by the revaluation of securities at fair value through profit or loss (FVTPL) and fair value through other comprehensive income (FVOCI).

Use of estimates and assumptions

The preparation of these financial statements requires the use of certain critical accounting estimates that affect the reported amount of assets, liabilities, net income and related disclosures. Estimates made by management are based on historical experience and other assumptions that are believed to be reasonable. Key areas of estimation uncertainty include: determination of fair value of financial instruments, the allowance for credit losses, derecognition of financial assets, income taxes, carrying value of goodwill and other intangible assets and litigation provisions. Accordingly, actual results may differ from these and other estimates thereby impacting our future Financial Statements. Refer to the relevant accounting policies in this note for details on our use of estimates and assumptions.

2 **Summary of significant accounting policies, estimates and judgments (continued)**

Significant judgments
Management also exercises judgment that affects the carrying amounts of certain assets and liabilities and the reported amounts of revenues and expenses recorded during the period. Significant judgments have been made in the following areas and discussed as noted in the financial statements:

• Fair value of financial instruments	Note 2, Note 26
• Allowance for credit losses	Note 2, Note 5
• Goodwill and Other intangibles	Note 2, Note 7, Note 8
• Securities impairment	Note 2
• Application of the effective interest method	Note 2
• Derecognition of financial assets	Note 2
• Income taxes	Note 2, Note 20
• Provisions.	Note 2

Accordingly, actual results may differ from these and other estimates thereby impacting our future financial statements.

Non-current assets held for sale and discontinued operations
Non-current assets (and disposal groups) are classified as held for sale if their carrying amounts will be recovered principally through a sale transaction rather than through continuing use. This condition is satisfied when the asset is available for immediate sale in its present condition, management is committed to the sale, and it is highly probable to occur within one year. Assets (and disposal groups) classified as held for sale are measured at the lower of their previous carrying amount and fair value less costs to sell and are presented separately from other assets on our Statement of Financial Position.

Changes in accounting policies
During the current year, the Bank adopted IFRS 15 Revenue from Contracts with Customers (IFRS 15). As a result of the application of IFRS 15, the Bank changed the accounting policies outlined below whereby revenue is recognized when control of a service transfers to a customer, and these new policies were applied retrospectively from November 1, 2018. In completing its assessment of revenue recognition under IFRS 15, the following factors are taken into consideration sequentially, which individually will vary based on the facts and circumstances present in a contract with a customer and will require the exercise of management judgement:

1. Identified all contracts with customers;
2. Identified the separate performance obligations under a contract;
3. Determined the transaction price of the contract;
4. Allocated the transaction price to each of the separate performance obligations; and
5. Recognized the revenue as each performance obligation is satisfied.

The Bank has adopted the portfolio approach, as an operational expedient, where contracts are assessed as a portfolio as opposed to individually assessed when the characteristics of each contract is similar. Where this is done, the Bank reviews the services provided as part of the contract, the contract duration, the terms and conditions of the contract, the amount, form and timing of consideration and the timing of the transfer of the service.

2 Summary of significant accounting policies, estimates and judgments (continued)

Changes in accounting policies (continued)

Due to the high volume of the Bank's contracts that may be identical or having similar contractual terms (for example standardized banking agreements with retail customers), it is expected that this expedient will be applied to many of the Bank's current revenue streams. In addition, the Bank will not adjust for the effects of a significant financing component for contracts with a 12 months or less expected time difference between when we transfer the service to the customer and the receipt of the contract consideration.
To facilitate the operational aspects of applying IFRS 15 the Bank has elected, as an accounting policy choice, to expense rather than capitalize incremental costs to obtain a contract if the expected amortization period of the asset the Bank otherwise would have recognized is 12 months or less. Anticipated contract renewals and amendments with the same customer must be considered when determining whether the period of benefit, and therefore the period of amortization, is 12 months or less.

As permitted by the transition provisions of IFRS 15, the Bank elected not to restate comparative period results; accordingly, all comparative information is presented in accordance with the Bank's previous accounting policies as indicated below. As a result of the adoption of IFRS 15, we reduced our opening retained earnings by AWG 286 thousand, on an after tax basis as at November 1, 2018 (the date of initial application), to align the recognition of certain fees with the transfer of the performance obligations. Income which falls under the scope of IFRS 15 are not netted off against related expenses. The Bank does not incur material costs to obtain contracts with customers such as sales commissions.

Commissions and fees
Commission and fees primarily relate to transactions service fees and commissions, investment management and custodial fees, mutual fund revenue, securities brokerage commissions, , underwriting and other advisory fees, card service revenue and credit fees, and are recognized based on the applicable service contracts with customers.

Commissions related to securities brokerage services and transaction service fees/commissions related to the provision of specific transaction type services are both recognized when the service is fulfilled. Where services are provided over time, revenue is recognized as the services are provided.

Card service revenue primarily includes interchange revenue and annual card fees. Interchange revenue is calculated as a fixed percentage of the transaction amount and recognized when the card transaction is settled. Annual card fees are fixed fees and are recognized over a twelve month period.

Credit fees are primarily earned for arranging syndicated loans and making credit available on undrawn facilities. The timing of the recognition of credit fees varies based on the nature of the services provided.

When service fees and other costs are incurred in relation to commissions and fees earned, we record these costs on a gross basis in either 'other operating expenses or staff costs' based on our assessment of whether we have primary responsibility to fulfill the contract with the customer and have discretion in establishing the price for the commissions and fees earned, which may require judgment.

2 Summary of significant accounting policies, estimates and judgments (continued)

Changes in accounting policies (continued)

Impact of adoption of IFRS 15 (continued)

The table below provides the Company's Statement of Financial Position, showing the impacts of adopting the IFRS 15 requirements.

	As at October 31, 2018	Impact of IFRS 15	As at November 1, 2018
	(AWG '000)	(AWG '000)	(AWG '000)
Assets			
Cash and cash equivalents	241,971	-	241,971
Balances with central banks	79,040	-	79,040
Loans	533,374	-	533,374
Securities	17,412	-	17,412
Investment in associate companies and joint venture	-	-	-
Due from associates and affiliated companies	20,237	-	20,237
Assets classified as held for sale	485	-	485
Intangible assets	12,520	-	12,520
Goodwill	23,654	-	23,654
Premises and equipment	15,839	-	15,839
Deferred tax assets	4,022	-	4,022
Other assets	9,360	-	9,360
Total assets	957,914	-	957,914
Liabilities			
Due to banks	406	-	406
Customers' deposits	774,125	-	774,125
Due to associates and affiliated companies	5,034	-	5,034
Current income tax liabilities	8,510	-	8,510
Deferred tax liabilities	6,836	-	6,836
Other liabilities	16,194	286	16,480
Total liabilities	811,105	286	811,390
Equity attributable to parent company			
Share capital	43,865	-	43,865
Share premium	1,000	-	1,000
Regulatory loan loss reserve	16,049	-	16,049
Other components of equity	1,866	-	1,866
Retained earnings/ (accumulated deficit)	84,029	(286)	83,743
Total equity attributable to parent company	146,809	(286)	146,523
Total Equity	146,809	(286)	146,523
Total equity and liabilities	957,914	-	957,914

Other significant accounting policies

The following accounting policies are applicable to all periods presented:

Classification of financial assets
Financial assets are measured at initial recognition at fair value, and are classified and subsequently measured at fair value through profit or loss (FVTPL), fair value through other comprehensive income (FVOCI) or amortized cost based on the Bank's business model for managing the financial assets and the contractual cash flow characteristics of the instrument.

Debt instruments are measured at amortized cost if both of the following conditions are met and the asset is not designated as FVTPL: (a) the asset is held within a business model that is Held-to-Collect (HTC) as described below, and (b) the contractual terms of the instruments give rise, on specified dates, to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI).

Debt instruments are measured at FVOCI if both of the following conditions are met and the asset is not designated as FVTPL: (a) the asset is held within a business model that is Held-to-Collect-and-Sell (HTC&S) as described below, and (b) the contractual terms of the instrument give rise, on specified dates, to cash flows that are SPPI.

All other debt instruments are measured at FVTPL.

Equity instruments are measured at FVTPL, unless the asset is not held for trading purposes and the Bank makes and irrevocable election to designate the asset as FVOCI. This election is made on an instrument-by-instrument basis.

Business model assessment
The Bank determines the business models at the level that best reflects how the Bank manages portfolios of financial assets to achieve business objectives. Judgement is used in determining the business models, which is supported by relevant, objective evidence including:

- How the economic activities of the businesses generate benefits, for example through trading revenue, enhancing yields or other costs and how such economic activities are evaluated and reported to key management personnel;
- The significant risks affecting the performance of the businesses, for example, market risk, credit risk, or other risks as described in the Risk Management Note 25, and the activities taken to manage those risks;
- Historical and future expectations of sales of the loans and securities managed as part of a business model; and
- The compensation structures for managers of the businesses within the Bank, to the extent that these are directly linked to the economic performance of the business model.

<u>**Other significant accounting policies (continued)**</u>

Classification of financial assets (continued)
The Bank's business models fall into three categories, which are indicative of the key categories used to generate returns:

- HTC: the objective of this business model is to hold loans and securities to collect contractual principal and interest cash flows; sales are incidental to this objective and are expected to be insignificant or infrequent;
- HTC&S: both collecting contractual cash flows and sales are integral to achieving the objective of the business model;
- Other fair value business models: these business models are neither HTC nor HTC&S, and primarily represent business models where assets are held-for-trading or managed on a fair value basis.

SPPI assessment
Instruments held within a HTC or HTC&S business model are assessed to evaluate if their contractual cash flows are comprised of solely payments of principal and interest. SPPI payments are those which would typically be expected for basic lending arrangements. Principal amounts include the fair value of the financial asset at initial recognition from lending and financing arrangements, and interest primarily relates to basic lending return, including compensation for credit risk and the time value of money associated with the principal amount outstanding over a period of time. Interest can also include other basic lending risks and costs (for example, liquidity risk, servicing or administrative costs) associated with holding the financial asset for a period of time, and a profit margin.

Securities
Trading securities include all securities that are classified at FVTPL, by nature and securities designated at FVTPL. Obligations to deliver trading securities sold but not yet purchased are recorded as liabilities and carried at fair value. Realized and unrealized gains and losses on these securities are generally recorded as trading revenue in non-interest income. Dividends and interest income accruing on trading securities are recorded in interest income.

Investment securities include all securities classified as FVOCI and amortized cost.

Investment securities carried at amortized cost are measured using the effective interest rate method, and are presented net of any allowance for credit losses, calculated in accordance with the Bank's policy for allowance for credit losses, as described below. Interest income, including the amortization of premiums and discounts on securities measured at amortized cost are recorded in net interest income. Impairment gains or losses recognized on amortized cost securities are recorded in provision for credit losses. When a debt instrument measured at amortized cost is sold, the difference between the sale proceeds and the amortized cost of the security at the time of sale is recorded as a net gain (loss) on investment securities in non-interest income.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Securities (continued)

Debt securities carried at FVOCI are measured at fair value with unrealized gains and losses arising from changes in fair values included in other components of equity. Impairment gains and losses are included in provision for credit losses and correspondingly reduce the accumulated change in fair value included in other components in equity. When a debt instrument measured at FVOCI is sold, the cumulative gain or loss is reclassified from other components of equity to net gain (loss) on investment securities in non-interest income.

Equity securities carried at FVOCI are measured at fair value. Unrealized gains and losses arising from changes in fair value are recorded in other components of equity and not subsequently reclassified to profit or loss when realized. Dividends from FVOCI securities are recognized in interest income.

The Bank accounts for all securities using settlement date accounting and changes in fair value between trade date and settlement date are reflected in income for securities measured at FVTPL, and changes in fair value of securities measured at FVOCI between trade date and settlement dates are recorded in OCI, except for changes in foreign exchange rates on debt securities, which are recorded in non-interest income.

Fair value option

A financial instrument can be designated as FVTPL (the fair value option) on its initial recognition even if the financial instrument was not acquired or incurred principally for the purpose of selling or repurchasing. The fair value option can be used for financial assets if it eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities, or recognizing related gains and losses on a different basis (an "accounting mismatch"). The fair value option can be elected for financial liabilities if: (i) the election eliminates an accounting mismatch; (ii) the financial liability is part of a portfolio that is managed on a fair value basis, in accordance with a documented risk management or investment strategy; or (iii) there is an embedded derivative in the financial or non-financial host contract and the derivative is not closely related to the host contract. These instruments cannot be reclassified out of the FVTPL category subsequently.

Financial assets designated as FVTPL are recorded at fair value and any unrealized gains or losses arising due to changes in fair value are included in Non-interest income.

Financial liabilities designated as FVTPL are recorded at fair value and fair value changes attributable to changes in our own credit risk are recorded in OCI. Own credit risk amounts recognized in OCI are not reclassified subsequently to net income. The remaining fair value changes not attributable to changes in our own credit risk are recorded in Non-interest income. Upon initial recognition, if we determine that presenting the effects of own credit risk changes in OCI would create or enlarge an accounting mismatch in net income, the full fair value change in our debt designated as at FVTPL is recognized in net income. To make that determination, we assess whether we expect that the effects of changes in the liability's credit risk will be offset in profit or loss by a change in the fair value of another financial instrument measured at FVTPL.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Fair value option (continued)

Such an expectation is based on an economic relationship between the characteristics of the liability and the characteristics of the other financial instrument. The determination is made at initial recognition and is not reassessed. To determine the fair value adjustments on our financial liabilities designated as at FVTPL, we calculate the present value of the instruments based on the contractual cash flows over the term of the arrangement by using our effective funding rate at the beginning and end of the period.

Loans

Loans are debt instruments recognized initially at fair value and are subsequently measured in accordance with the Classification of financial assets policy provided above. The majority of our loans are carried at amortized cost using the effective interest method, which represents the gross carrying amount less allowance for credit losses.

Interest on loans is recognized in Interest income using the effective interest method. The estimated future cash flows used in this calculation include those determined by the contractual term of the asset and all fees that are considered to be integral to the effective interest rate. Also included in this amount are transaction costs and all other premiums or discounts. Fees that relate to activities such as originating, restructuring or renegotiating loans are deferred and recognized as Interest income over the expected term of such loans using the effective interest method.

Where there is a reasonable expectation that a loan will be originated, commitment and standby fees are also recognized as interest income over the expected term of the resulting loans using the effective interest method. Otherwise, such fees are recorded as other liabilities and amortized into Non-interest income over the commitment or standby period. Prepayment fees on mortgage loans are not included as part of the effective interest rate at origination. If prepayment fees are received on a renewal of a mortgage loan, the fee is included as part of the effective interest rate; and if not renewed, the prepayment fee is recognized in interest income at the prepayment date.

For loans carried at amortized cost or FVOCI, impairment losses are recognized at each balance sheet date in accordance with the three-stage impairment model outlined below.

Allowance for credit losses

An allowance for credit losses (ACL) is established for all financial assets, except for financial assets classified or designated as FVTPL and equity securities designated as FVOCI, which are not subject to impairment assessment. Assets subject to impairment assessment include loans, debt securities, interest-bearing deposits with banks, accounts and accrued interest receivable. ACL on financial assets is disclosed in the notes to the financial statements. ACL on debt securities measured at FVOCI is presented in other components of equity. Financial assets carried at amortized cost are presented net of ACL on our statement of financial position.

Off-balance sheet items subject to impairment assessment include financial guarantees and undrawn loan commitments. For these products, ACL is disclosed in the notes to the financial statements.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Allowance for credit losses (continued)

We measure the ACL on each balance sheet date according to a three-stage expected credit loss impairment model:

- Performing financial assets
  - Stage 1 – From initial recognition of a financial asset to the date on which the asset has experienced a significant increase in credit risk relative to its initial recognition, a loss allowance is recognized equal to the credit losses expected to result from defaults occurring over the 12 months following the reporting date.
  - Stage 2 – Following a significant increase in credit risk relative to the initial recognition of the financial asset, a loss allowance is recognized equal to the credit losses expected over the remaining lifetime of the asset.
- Impaired financial assets
  - Stage 3 – When a financial asset is considered to be credit-impaired, a loss allowance is recognized equal to credit losses expected over the remaining lifetime of the asset.

The ACL is a discounted probability-weighted estimate of the cash shortfalls expected to result from defaults over the relevant time horizon. For loan commitments, credit loss estimates consider the portion of the commitment that is expected to be drawn over the relevant time period.

Increases or decreases in the required ACL attributable to purchases and new originations, derecognitions or maturities, and remeasurements due to changes in loss expectations or stage migrations are recorded in provision for credit losses. Write-off and recoveries are recorded against allowance for credit losses.

The ACL represents an unbiased estimate of expected credit losses on our financial assets as at the balance sheet date. Judgment is required in making assumptions and estimations when calculating the ACL, including movements between the three stages and the application of forward looking information. The underlying assumptions and estimates may result in changes to the allowances from period to period that significantly affects the results of operations.

Measurement of expected credit losses

Expected credit losses are based on a range of possible outcomes and consider available reasonable and supportable information including internal and external ratings, historical credit loss experience, and expectations about future cash flows. The measurement of expected credit losses is based primarily on the product of the instrument's probability of default (PD), loss given default (LGD), and exposure at default (EAD) discounted to the reporting date. The main difference between Stage 1 and Stage 2 expected credit losses for performing financial assets is the respective calculation horizon. Stage 1 estimates project PD, LGD and EAD over a maximum period of 12 months while Stage 2 estimates project PD, LGD and EAD over the remaining lifetime of the instrument.

An expected credit loss estimate is produced for each portfolio segment. Relevant parameters are modeled on a collective basis using portfolio segmentation that allows for appropriate incorporation of forward looking information. To reflect other characteristics that are not already considered through modelling, expert credit judgment is exercised in determining the final expected credit losses using a range of possible outcomes.

Expected credit losses are discounted to the reporting period date using the effective interest rate.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Allowance for credit losses (continued)

Expected life

For instruments in Stage 2 or Stage 3, loss allowances reflect expected credit losses over the expected remaining lifetime of the instrument. For most instruments, the expected life is limited to the remaining contractual life.

An exemption is provided for certain instruments with the following characteristics: (a) the instrument includes both a loan and undrawn commitment component; (b) we have the contractual ability to demand repayment and cancel the undrawn commitment; and (c) our exposure to credit losses is not limited to the contractual notice period. For products in scope of this exemption, the expected life may exceed the remaining contractual life and is the period over which our exposure to credit losses is not mitigated by our normal credit risk management actions. This period varies by product and risk category and is estimated based on our historical experience with similar exposures and consideration of credit risk management actions taken as part of our regular credit review cycle. Products in scope of this exemption include credit cards, overdraft balances and certain revolving lines of credit. Determining the instruments in scope for this exemption and estimating the appropriate remaining life based on our historical experience and credit risk mitigation practices requires significant judgment.

Assessment of significant increase in credit risk

The assessment of significant increase in credit risk requires significant judgment. Movements between Stage 1 and Stage 2 are based on whether an instrument's credit risk as at the reporting date has increased significantly relative to the date it was initially recognized. The assessment is performed at the instrument level.

Our assessment of significant increases in credit risk is based on factors such as delinquency status, watch-list reports and whether or not the account is being managed by the special loans group. If any of the following conditions is met, the instrument is moved from Stage 1 to Stage 2:

1) The instrument is 30 days past due.
2) The account is included in the watch-list reporting process. The watch-list process is considered fundamental in identifying early signs of deterioration on existing accounts.
3) The account is managed by the Regional Special Loan Unit (RSLU). The RSLU portfolio today remains a mix of accounts which are in default and accounts with minimal or no delinquency. The latter remains within the purview of the specialized management team due to circumstances other than delinquency which marks the account as having a higher risk component.

Use of forward-looking information

The PD and LGD inputs used to estimate Stage 1 and Stage 2 credit loss allowances are modelled based on the macroeconomic variables (or changes in macroeconomic variables) that are most closely correlated with credit losses in the relevant portfolio. Each macroeconomic scenario used in our expected credit loss calculation includes a projection of all relevant macroeconomic variables used in our models for a five year period. Macroeconomic variables used in our expected credit loss models include, but are not limited to, unemployment rate, GDP and inflation rate.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Allowance for credit losses (continued)

Use of forward-looking information (continued)

Our estimation of expected credit losses in Stage 1 and Stage 2 is a discounted probability-weighted estimate that considers a minimum of three future macroeconomic scenarios. Scenarios and scenario weights are set at the enterprise level; considering the RBC baseline forecast and reasonable downside and upside assumptions. Scenarios are global in nature and include predictions of macroeconomic conditions in North America, Europe and the Caribbean. Having scenarios and scenario weights set at the enterprise level allows RBC to have a consistent view of macroeconomic scenarios across business lines and legal entities.

Scenarios are designed to capture a wide range of possible outcomes and weighted on the relative likelihood of the range of outcomes that each scenario represents. Scenario weights take into account historical frequency, current trends, and forward-looking conditions and are updated on a quarterly basis. All scenarios considered are applied to all portfolios subject to expected credit losses with the same probability weighting.

Definition of default

The definition of default used in the measurement of expected credit losses is consistent with the definition of default used for our internal credit risk management purposes. Our definition of default may differ across products and consider both quantitative and qualitative factors, such as the terms of financial covenants and days past due. For retail and wholesale borrowers default occurs when the borrower is 90 days or more past due on any material obligation to us, and/or we consider the borrower unlikely to make their payments in full without recourse action on our part, such as taking formal possession of any collateral held. For certain credit card balances, default occurs when payments are 180 days past due. For these balances, the use of a period in excess of 90 days past due is reasonable and supported by observable data on write-off and recovery rates. The definition of default used is applied consistently from period to period and to all financial instruments unless it can be demonstrated that circumstances have changed such that another definition of default is more appropriate.

Credit-impaired financial assets (Stage 3)

Financial assets are assessed for credit-impairment at each balance sheet date and more frequently when circumstances warrant further assessment. Evidence of credit-impairment may include indications that the borrower is experiencing significant financial difficulty, probability of bankruptcy or other financial reorganization, as well as a measurable decrease in the estimated future cash flows evidenced by the adverse changes in the payments status of the borrower or economic conditions that correlate with defaults. An asset that is in Stage 3 will move back to Stage 2 when, as at the reporting date, it is no longer considered to be credit-impaired. The asset will migrate back to Stage 1 when its credit risk at the reporting date is no longer considered to have increased significantly from initial recognition, which could occur during the same reporting period as the migration from Stage 3 to Stage 2.

When a financial asset has been identified as credit-impaired, expected credit losses are measured as the difference between the asset's gross carrying amount and the present value of estimated future cash flows discounted at the instrument's original effective interest rate. For impaired financial assets with drawn and undrawn components, expected credit losses also reflect any credit losses related to the portion of the loan commitment that is expected to be drawn down over the remaining life of the instrument.

Other significant accounting policies (continued)

Allowance for credit losses (continued)

Credit-impaired financial assets (Stage 3) (continued)
When a financial asset is credit-impaired, interest ceases to be recognized on the regular accrual basis, which accrues income based on the gross carrying amount of the asset. Rather, the accrual is calculated by applying the effective interest rate to the carrying amount, which is recorded on the Statement of Financial Position. The discount resulting from the impact of time delays in collecting principal (time value of money) is established and recorded through provision for credit losses.

ACL for credit-impaired financial assets in Stage 3 are established at the financial asset level, where losses related to impaired financial asset are identified on individually significant financial asset, or collectively assessed and determined through the use of portfolio-based rates, without reference to particular financial assets.

Individually assessed loans (Stage 3)
When individually significant loans are identified as impaired, we reduce the carrying value of the loans to their estimated realizable value by recording an individually assessed ACL to cover identified credit losses. The individually assessed ACL reflects the expected amount of principal and interest calculated under the terms of the original loan agreement that will not be recovered, and the impact of time delays in collecting principal and/or interest (time value of money). The estimated realizable value for each individually significant loan is the present value of expected future cash flows discounted using the original effective interest rate for each loan. When the amounts and timing of future cash flows cannot be estimated with reasonable reliability, the estimated realizable amount may be determined using observable market prices for comparable loans, the fair value of collateral underlying the loans, and other reasonable and supported methods based on management judgment.

Individually-assessed allowances are established in consideration of a range of possible outcomes, to the extent relevant to the circumstances of the specific borrower being assessed. Assumptions used in estimating expected future cash flows reflect current and expected future economic conditions and are generally consistent with those used in Stage 1 and Stage 2 measurement.

Significant judgment is required in assessing evidence of credit-impairment and estimation of the amount and timing of future cash flows when determining expected credit losses. Changes in the amount expected to be recovered would have a direct impact on the provision for credit losses and may result in a change in the ACL.

Collectively assessed loans (Stage 3)
Loans that are collectively assessed are grouped on the basis of similar risk characteristics, taking into account loan type, geographic location, collateral type, past due status and other relevant factors.

The collectively-assessed ACL reflects: (i) the expected amount of principal and interest calculated under the terms of the original loan agreement that will not be recovered, and (ii) the impact of time delays in collecting principal and /or interest (time value of money).

Allowance for credit losses (continued)

Collectively assessed loans (Stage 3) (continued)

The expected principal and interest collection is estimated on a portfolio basis and references historical loss experience of comparable portfolios with similar credit risk characteristics, adjusted for the current environment and expected future conditions. A portfolio specific coverage ratio is applied against the impaired loan balance in determining the collectively-assessed ACL. The time value of money component is calculated by using the discount factors applied to groups of loans sharing common characteristics. The discount factors represent the expected recovery pattern of the comparable group of loans, and reflect the historical experience of these groups adjusted for current and expected future economic conditions and/or industry factors. Significant judgment is required in assessing evidence of impairment and estimation of the amount and timing of future cash flows when determining expected credit losses. Changes in the amount expected to be recovered would have a direct impact on the Provision for credit losses and may result in a change in the ACL.

Write-off of loans

Loans are written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, they are generally written off after receipt of any proceeds from the realization of collateral. In circumstances where the net realizable value of any collateral has been determined and there is no reasonable expectation of further recovery, write off may be earlier. For credit cards, the balances are generally written off when payment is 180 days past due. Unsecured loans are generally written off at 365 days past due. Loans secured by real estate are generally written off at 2,000 days past due, with continued efforts to realize on the underlying collateral held following write off.

Modifications

The original terms of a financial asset may be renegotiated or otherwise modified, resulting in changes to the contractual terms of the financial asset that affect the contractual cash flows. The treatment of such modifications is primarily based on the process undertaken to execute the renegotiation and the nature and extent of changes expected to result. Modifications which are performed for credit reasons, primarily related to troubled debt restructurings, are generally treated as modifications of the original financial asset which can be tracked through the original asset or via establishment of a new financial asset. Modifications which are performed for other than credit reasons are generally considered to be an expiry of the original cash flows; accordingly, such renegotiations are treated as a derecognition of the original financial asset and recognition of a new financial asset.

A modified financial asset continues to be subject to the same assessments for significant increase in credit risk relative to initial recognition and credit-impairment, as described above. A modified financial asset will migrate out of Stage 3 if the conditions that led to it being identified as credit-impaired are no longer present and relate objectively to an event occurring after the original credit-impairment was recognized. A modified financial asset will migrate out of Stage 2 when it no longer satisfies the relative thresholds set to identify significant increases in credit risk, which are based on changes in days past due and other qualitative considerations.

If a modification of terms results in derecognition of the original financial asset and recognition of the new financial asset, the new financial asset will generally be recorded in Stage 1, unless it is determined to be credit-impaired at the time of the renegotiation. For the purposes of assessing for significant increases in credit risk, the date of initial recognition for the new financial asset is the date of the modification.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Determination of fair value
The fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. We determine fair value by incorporating all factors that market participants would consider in setting a price, including commonly accepted valuation approaches.

We have established policies, procedures and controls for valuation methodologies and techniques to ensure fair value is reasonably estimated. Major valuation processes and controls include, but are not limited to, profit and loss decomposition, independent price verification (IPV) and model validation standards. These control processes are managed by either Finance or Group Risk Management and are independent of the relevant businesses and their trading functions. Profit and loss decomposition is a process to explain the fair value changes of certain positions and is performed for trading portfolios. All fair value instruments are subject to IPV, a process whereby trading function valuations are verified against external market prices and other relevant market data. Market data sources include traded prices, brokers and price vendors. We give priority to those third-party pricing services and prices having the highest and most consistent accuracy. The level of accuracy is determined over time by comparing third-party price values to traders' or system values, to other pricing service values and, when available, to actual trade data. Other valuation techniques are used when a price or quote is not available. Some valuation processes use models to determine fair value. We have a systematic and consistent approach to control model use. Valuation models are approved for use within our model risk management framework. The framework addresses, among other things, model development standards, validation processes and procedures, and approval authorities. Model validation ensures that a model is suitable for its intended use and sets parameters for its use. All models are revalidated regularly.

Valuation adjustments are recorded for the credit risk of our derivative portfolios in order to arrive at their fair values. Credit valuation adjustments (CVA) take into account our counterparties' creditworthiness, the current and potential future mark-to-market of the transactions, and the effects of credit mitigants such as master netting and collateral agreements. CVA amounts are derived from estimates of exposure at default, probability of default, recovery rates on a counterparty basis, and market and credit factor correlations. Exposure at default is the amounts of expected derivative related assets and liabilities at the time of default, estimated through modeling using underlying risk factors. Probability of default and recovery rate are generally implied from the market prices for credit protection and credit ratings of the counterparty or derived from internal estimates when market data is unavailable.

Correlation is the statistical measure of how credit and market factors may move in relation to one another. Correlation is estimated using historical data and market data where available. CVA is calculated and changes are recorded in non-interest income.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Determination of fair value (continued)

In determining fair value, a hierarchy is used which prioritizes the inputs to valuation techniques. The fair value hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3). Determination of fair value based on this hierarchy requires the use of observable market data whenever available. Level 1 inputs are unadjusted quoted prices in active markets for identical assets or liabilities that we have the ability to access at the measurement date. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, and model inputs that are either observable, or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3 inputs are one or more inputs that are unobservable and significant to the fair value of the asset or liability. Unobservable inputs are used to measure fair value to the extent that observable inputs are not available at the measurement date. The availability of inputs for valuation may affect the selection of valuation techniques. The classification of a financial instrument in the hierarchy for disclosure purposes is based upon the lowest level of input that is significant to the measurement of fair value. Where observable prices or inputs are not available, management judgement is required to determine fair values by assessing other relevant sources of information such as historical data, proxy information from similar transactions, and through extrapolation and interpolation techniques. For more complex or illiquid instruments, significant judgement is required in the determination of the model used, the selection of model inputs, and in some cases, the application of valuation adjustments to the model value or quoted price for inactively traded financial instruments, as the selection of model inputs may be subjective and the inputs may be unobservable. Unobservable inputs are inherently uncertain as there is little or no market data available from which to determine the level at which the transaction would occur under normal business circumstances. Appropriate parameter uncertainty and market-risk valuation adjustments for such inputs and other model-risk valuation adjustments are assessed in all such instances. Refer to Note 26.

Interest

Interest is recognized in Interest income and Interest expense in the Statements of Income and Other Comprehensive Income for all interest bearing financial instruments using the effective interest method. The effective interest rate is the rate that discounts estimated future cash flows over the expected life of the financial asset or liability to the net carrying amount upon initial recognition. Judgement is applied in determining the effective interest rate due to uncertainty in the timing and amounts of future cash flows.

Transaction costs

Transaction costs are expensed as incurred for financial instruments classified or designated as at FVTPL. For other financial instruments, transaction costs are capitalized on initial recognition. For financial assets and financial liabilities measured at amortized cost, capitalized transaction costs are amortized through Net interest income over the estimated life of the instrument using the effective interest method.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Offsetting financial assets and financial liabilities
Financial assets and financial liabilities are offset on the balance sheet when there exists both a legally enforceable right to offset the recognized amounts and an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

Cash and cash equivalents
Cash and cash equivalents comprises cash and demand deposits with banks together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of change in value. Such investments are normally those with original maturities up to three months from the date of acquisition.

Derecognition of financial assets
Financial assets are derecognized from our Statement of Financial Position when our contractual rights to the cash flows from the assets have expired, when we retain the rights to receive the cash flows of the assets but assume an obligation to pay those cash flows to a third party subject to certain pass-through requirements or when we transfer our contractual rights to receive the cash flows and substantially all of the risk and rewards of the assets have been transferred. When we retain substantially all of the risks and rewards of the transferred assets, the transferred assets are not derecognized from our Statement of Financial Position and are accounted for as secured financing transactions. When we neither retain nor transfer substantially all risks and rewards of ownership of the assets, we derecognize the assets if control over the assets is relinquished. If we retain control over the transferred assets, we continue to recognize the transferred assets to the extent of our continuing involvement.

Management’s judgement is applied in determining whether the contractual rights to the cash flows from the transferred assets have expired or whether we retain the rights to receive cash flows on the assets but assume an obligation to pay for those cash flows. We derecognize transferred financial assets if we transfer substantially all the risk and rewards of the ownership in the assets. When assessing whether we have transferred substantially all of the risk and rewards of the transferred assets, management considers the entity exposure before and after the transfer with the variability in the amount and timing of the net cash flows of the transferred assets. In transfers that we retain the servicing rights, management has applied judgement in assessing the benefits of servicing against market expectations. When the benefits of servicing are greater than fair market value, a servicing asset is recognized in Other assets in our Statement of Financial Position. When the benefits of servicing are less than fair market value, a servicing liability is recognized in Other liabilities in our Statement of Financial Position.

Derecognition of financial liabilities
We derecognize a financial liability from our Statement of Financial Position when our obligation specified in the contract expires, or is discharged or cancelled. We recognize the difference between the carrying amount of a financial liability transferred and the consideration paid in our Statement of Income and Other Comprehensive Income.

Other significant accounting policies (continued)

Guarantees
Financial guarantee contracts are contracts that contingently require us to make specified payments (in cash, other assets or provision of services) to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument. The Bank has equal and offsetting claims against its customers in the event of a call on these commitments.

Share–based compensation
The ultimate parent company, Royal Bank of Canada, offers performance deferred share and functional unit plans (the “Plans”) to certain key employees.

Income taxes
Income tax comprises current tax and deferred tax and is recognized in our Statement of Income and Other Comprehensive Income except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current income tax payable on profits is recognized as an expense based on the applicable tax laws in each jurisdiction in the period in which profits arise, calculated using tax rates enacted or substantively enacted by the Statement of Financial Position date. Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities for accounting purposes compared with tax purposes. A deferred income tax asset or liability is determined for each temporary difference, except for earnings related to our subsidiaries, associates and interests in joint ventures where the temporary differences will not reverse in the foreseeable future and we have the ability to control the timing of reversal. Deferred tax assets and liabilities are determined based on the tax rates that are expected to be in effect in the period that the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted at the Statement of Financial Position date. Current tax assets and liabilities are offset when they are levied by the same taxation authority on either the same taxable entity or different taxable entities within the same tax reporting group (which intends to settle on a net basis), and when there is a legal right to offset. Deferred tax assets and liabilities are offset when the same conditions are satisfied. The Statement of Income and Other Comprehensive Income include items that are non-taxable or non-deductible for income tax purposes and, accordingly, this causes the income tax provision to be different from what it would be if based on statutory rates.

Deferred income taxes accumulated as a result of temporary differences and tax loss carryforwards are included on the Statement of Financial Position. On a quarterly basis, we review our deferred income tax assets to determine whether it is probable that the benefits associated with these assets will be realized; this review involves evaluating both positive and negative evidence.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Income taxes (continued)
We are subject to income tax laws in various jurisdictions where we operate, and the complex tax laws are potentially subject to different interpretations by the relevant taxation authorities and the Bank. Significant judgement is required in the interpretation of the relevant tax laws, and the determination of our tax provision, which includes our best estimate of tax positions that are under audit or appeal by relevant taxation authorities. We perform a review on a quarterly basis to incorporate our best assessment based on information available, but additional liability and income tax expense could result based on decisions made by the relevant tax authorities.

The determination of our deferred income tax asset or liability also requires significant management judgement as the recognition is dependent on our projection of future taxable profits and tax rates that are expected to be in effect in the period the asset is realized or the liability is settled. Any changes in our projection will result in changes in deferred tax assets or liabilities on our Statement of Financial Position, and also deferred tax expense in our Statements of Income and Other Comprehensive Income.

Business combinations
All business combinations are accounted for using the acquisition method. Non-controlling interests, if any, are recognized at their proportionate share of the fair value of identifiable assets and liabilities, unless otherwise indicated. Identifiable intangible assets are recognized separately from goodwill and included in Other intangibles. Goodwill represents the excess of the price paid for the business acquired over the fair value of the net identifiable assets acquired on the date of acquisition.

Goodwill
Goodwill is allocated to cash-generating units or groups of cash-generating units (CGU) for the purpose of impairment testing, which is undertaken at the lowest level at which goodwill is monitored for internal management purposes. Impairment testing is performed annually or more frequently if there are objective indicators of impairment, by comparing the recoverable amount of a CGU with its carrying amount. The recoverable amount of a CGU is the higher of its value in use and its fair value less costs of disposal. Value in use is the present value of the expected future cash flows from a CGU. Fair value less costs of disposal is the amount obtainable from the sale of a CGU in an orderly transaction between market participants, less disposal costs. The fair value of a CGU is estimated using valuation techniques such as a discounted cash flow method, adjusted to reflect the considerations of a prospective third-party buyer. External evidence such as binding sale agreements or recent transactions for similar businesses within the same industry is considered to the extent that it is available. Significant judgement is involved in estimating the model inputs used to determine the recoverable amount of our CGU, in particular future cash flows, discount rates and terminal growth rates, due to the uncertainty in the timing and amount of cash flows and the forward-looking nature of these inputs. Future cash flows are based on management's forecasts adjusted to approximate the considerations of a prospective third-party buyer. Discount rates are based on the bank-wide cost of capital, adjusted for CGU-specific risks and currency exposure as reflected by differences in expected inflation. Bank-wide cost of capital is based on the Capital Asset Pricing Model.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

CGU-specific risks include country risk, business/operational risk, geographic risk (including political risk, devaluation risk, and government regulation), currency risk, and price risk (including product pricing risk and inflation). Terminal growth rates reflect the expected long-term gross domestic product growth and inflation for the countries within which the CGU operates. Changes in these assumptions may affect the amount of impairment loss recognized in Non-interest expense.

The carrying amount of a CGU includes the carrying amount of assets, liabilities and goodwill allocated to the CGU. If the recoverable amount is less than the carrying value, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to the other non-financial assets of the CGU proportionately based on the carrying amount of each asset. Any impairment loss is charged to income in the period in which the impairment is identified. Goodwill is stated at cost less accumulated impairment losses. Subsequent reversals of goodwill impairment are prohibited.
Upon disposal of a portion of a CGU, the carrying amount of goodwill relating to the portion of the CGU sold is included in the determination of gains or losses on disposal. The carrying amount is determined based on the relative fair value of the disposed portion to the total CGU. Refer to note 8.

Other intangibles
Intangible assets represent identifiable non-monetary assets and are acquired either separately or through a business combination, or generated internally. Intangible assets acquired through a business combination are recognized separately from goodwill when they are separable or arise from contractual or other legal rights, and their fair value can be measured reliably. The cost of a separately acquired intangible asset includes its purchase price and directly attributable costs of preparing the asset for its intended use. After initial recognition, an intangible asset is carried at its cost less any accumulated amortization and accumulated impairment losses, if any. Intangible assets with a finite-life are amortized on a straight-line basis over their estimated useful lives as follows: computer software – 4 to 10 years; and customer relationships – 7 years. We do not have any intangible assets with indefinite lives.

Intangible assets are assessed for indicators of impairment at each reporting period. If there is an indication that an intangible asset may be impaired, an impairment test is performed by comparing the carrying amount of the intangible asset to its recoverable amount. Where it is not possible to estimate the recoverable amount of an individual asset, we estimate the recoverable amount of the CGU to which the asset belongs. If the recoverable amount of the asset (or CGU) is less than its carrying amount, the carrying amount of the intangible asset is written down to its recoverable amount as an impairment loss.

An impairment loss recognized previously is reversed if there is a change in the estimates used to determine the recoverable amount of the asset (or CGU) since the last impairment loss was recognized. If an impairment loss is subsequently reversed, the carrying amount of the asset (or CGU) is revised to the lower of its recoverable amount and the carrying amount that would have been determined (net of amortization) had there been no prior impairment.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Due to the subjective nature of these estimates, significant judgement is required in determining the useful lives and recoverable amounts of our intangible assets, and assessing whether certain events or circumstances constitute objective evidence of impairment. Estimates of the recoverable amounts of our intangible assets rely on certain key inputs, including future cash flows and discount rates. Future cash flows are based on sales projections and allocated costs, which are estimated, based on forecast results and business initiatives. Discount rates are based on the bank-wide cost of capital, adjusted for asset-specific risks. Changes in these assumptions may impact the amount of impairment loss recognized in Non-interest expense.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period to get ready for their intended use or sale, are added to the cost of those assets, until the assets are substantially ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalization.

All other borrowing costs are recognised in the Statement of Income and Other Comprehensive Income in the period in which they are incurred.

Translation of foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated into AWG at rates prevailing at the balance sheet date. Foreign exchange gains and losses resulting from the translation and settlement of these items are recognized in Non-interest income in the Statement of Income and Other Comprehensive Income.

Non-monetary assets and liabilities that are measured at historical cost are translated into AWG at historical rates. Non-monetary financial assets classified as securities, such as equity instruments, that are measured at fair value are translated into AWG at rates prevailing at the Statement of Financial Position date, and the resulting foreign exchange gains and losses are recorded in other comprehensive income until the asset is sold or becomes impaired. Assets and liabilities of our foreign operations with functional currencies other than AWG are translated into AWG at rates prevailing at the Statement of Financial Position date, and income and expenses of these foreign operations are translated at average rates of exchange for the reporting period.

Unrealized gains or losses arising as a result of the translation of our foreign operations are reported in other comprehensive income on an after-tax basis. Upon disposal or partial disposal of a foreign operation, a proportionate amount of the accumulated net translation gains or losses is included in Non-interest income.

2 Summary of significant accounting policies, estimates and judgments (continued)

Other significant accounting policies (continued)

Premises and equipment

Premises and equipment includes land, buildings, leasehold improvements, computer equipment, furniture, fixtures and other equipment, and are stated at cost less accumulated depreciation and accumulated impairment losses. Cost comprises the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use, and the initial estimate of any disposal costs. Depreciation is recorded principally on a straight–line basis over the estimated useful lives of the assets, which are 25 to 50 years for freehold properties, 5 to 50 years for leasehold properties 4 to 5 years for computer equipment, and 5 to 7 years for furniture, fixtures and other equipment. The amortization period for leasehold improvements is the lesser of the useful life of the leasehold improvements or the lease term plus the first renewal period, if reasonably assured of renewal, up to a maximum of 10 years. Land is not depreciated. Gains and losses on disposal are recorded in non–interest income.

Premises and equipment are assessed for indicators of impairment at each reporting period. If there is an indication that an asset may be impaired, an impairment test is performed by comparing the asset's carrying amount to its recoverable amount. Where it is not possible to estimate the recoverable amount of an individual asset, we estimate the recoverable amount of the CGU to which the asset belongs and test for impairment at the CGU level. An impairment charge is recorded to the extent the recoverable amount of an asset (or CGU), which is the higher of value in use and fair value less costs of disposal, is less than its carrying amount. Value in use is the present value of the future cash flows expected to be derived from the asset (or CGU). Fair value less costs of disposal is the amount obtainable from the sale of the asset (or CGU) in an orderly transaction between market participants, less costs of disposal.

After the recognition of impairment, the depreciation charge is adjusted in future periods to reflect the asset's revised carrying amount. If an impairment is later reversed, the carrying amount of the asset is revised to the lower of the asset's recoverable amount and the carrying amount that would have been determined (net of depreciation) had there been no prior impairment loss. The depreciation charge in future periods is adjusted to reflect the revised carrying amount.

Provisions

Provisions are liabilities of uncertain timing or amount and are recognized when we have a present legal or constructive obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are measured as the best estimate of the consideration required to settle the present obligation at the reporting date. Significant judgement is required in determining whether a present obligation exists and in estimating the probability, timing and amount of any outflows. We record provisions related to litigation, asset retirement obligations and other items. Provisions are recorded under Other liabilities on our Statement of Financial Position.

<u>**Other significant accounting policies (continued)**</u>

Provisions (continued)
We are required to estimate the results of ongoing legal proceedings, expenses to be incurred to dispose of capital assets, and credit losses on undrawn commitments and guarantees. The forward-looking nature of these estimates requires us to use a significant amount of judgement in projecting the timing and amount of future cash flows. We record our provisions based on all available information at the end of the reporting period and make adjustments on a quarterly basis to reflect current expectations. Should actual results differ from our expectations, we may incur expenses in excess of the provisions recognized.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, such as an insurer, a separate asset is recognized if it is virtually certain that reimbursement will be received.

Dividend income
Dividend income is recognized when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders have approved the dividend for unlisted equity securities.

Leasing
A lease is an agreement whereby the lessor conveys to the lessee the right to use an asset for an agreed upon period of time in return for a payment or series of payments. A finance lease is a lease that transfers substantially all the risks and rewards incidental to ownership of the leased asset to the lessee, where title may or may not eventually be transferred. An operating lease is a lease other than a finance lease.

Operating leases
When we are the lessee in an operating lease, we record rental payments on a straight-line basis over the lease term in Non-interest expense.

Finance leases
When we are the lessee in a finance lease, we initially record both the leased asset and the related lease obligation in Premises and equipment, Intangibles and Other liabilities on our Statement of Financial Position at an amount equal to the fair value of the leased asset or, if lower, the present value of the minimum lease payments, each determined at the date of inception of the lease. Initial direct costs directly attributed to the lease are recognized as an asset under the finance lease.

Share capital
We classify a financial instrument that we issue as a financial asset, financial liability or an equity instrument in accordance with the substance of the contractual arrangement.

Financial instruments issued by us are classified as equity instruments when there is no contractual obligation to transfer cash or other financial assets. Incremental costs directly attributable to the issue of equity instruments are included in equity as a deduction from the proceeds, net of tax.

2 Summary of significant accounting policies, estimates and judgments (continued)

Pre-IFRS 15 Accounting Policy

The following policy is applicable for comparative period results as at and for the year ended October 31, 2018:

Non-interest income

The Bank includes in non-interest income amounts relating to service charges. Service charges are related to the provision of specific transaction type services and are recorded when the service has been completed.

Future changes in accounting policy and disclosure

We are currently assessing the impact of adopting the following standards on our Financial Statements:

IFRS 16 Leases (IFRS 16)

In January 2016, the IASB issued IFRS 16, which sets out the principles for the recognition, measurement, presentation and disclosure of leases. The standard removes the current requirement for lessees to classify leases as finance leases or operating leases by introducing a single lessee accounting model that requires the recognition of lease assets and lease liabilities on the Statement of Financial Position for most leases. Lessees will also recognize depreciation expense on the lease asset and interest expense on the lease liability in the Statement of Income. There are no significant changes to lessor accounting.

We will adopt IFRS 16 using the modified retrospective approach by adjusting our Statement of Financial Position as at November 1, 2019, the date of initial application, with no restatement of comparative periods. The adoption of IFRS 16 as at November 1, 2019 is expected to result in an increase to total assets of approximately AWG 770 thousand, primarily representing leased premises and equipment, an increase in lease liabilities of approximately AWG 770 thousand, and a reduction to retained earnings of approximately AWG - thousand, net of taxes.

IFRS 17 Insurance Contracts (IFRS 17)

In May 2017, the IASB issued IFRS 17 to establish a comprehensive global insurance standard which provides guidance on the recognition, measurement, presentation and disclosures of insurance contracts. IFRS 17 requires entities to measure insurance contract liabilities at their current fulfilment values using one of three approaches. This new standard will be effective for us on November 1, 2021 and will be applied retrospectively with restatement of comparatives unless impracticable. We are currently assessing the impact of adopting this standard on our Financial Statements.

3 Cash and cash equivalents

	2019	2018
	(AWG '000)	(AWG '000)
Cash on hand	15,869	19,389
Treasury bills	12,992	100,983
Due from banks	137,886	121,630
Items in the course of collection with due from other banks	(7)	(32)
	166,740	241,971

Cash on hand represents cash held in tellers' tills, the vault and cash dispensing machines.

Due from banks are deposits held with other banks on demand or for fixed periods not exceeding 90 days. Treasury bills have original maturities up to three months.

There are no balances due from banks that have been pledged as security on behalf of any affiliated party this year (2018: AWG nil).

3.1 Allowance for credit losses on cash and cash equivalents

Allowance for credit losses - Treasury bills

There were no allowance for credit losses for Treasury bills less than 90 days as of October 31, 2019 (2018: nil).

4 Balances with central banks

In accordance with regulations governing banks in the region, the Bank is required to maintain monetary reserves with the Central Bank, which is based on a ratio to customers' deposits and other specified liabilities.

5 Loans

	2019	2018
	(AWG '000)	(AWG '000)
Retail	67,429	69,875
Commercial/corporate	256,437	233,943
Mortgages	255,364	245,001
Gross loans	579,230	548,819
Allowance for impairment losses (Note 5.1)	(23,133)	(15,443)
	556,097	533,376
Stage 1	502,132	456,423
Stage 2	60,193	69,903
Stage 3	16,905	22,493
Gross loans	579,230	548,819
Current	64,025	73,061
Non-current	515,205	475,758
Gross loans	579,230	548,819

5.1 Allowance for impairment losses

	For the year ended 2019				
	Balance at beginning of period (AWG '000)	Provision for credit losses (AWG '000)	Net write-offs (AWG '000)	Exchange rate and other (AWG '000)	Balance at end of period (AWG '000)
Retail	1,542	(118)	436	-	1,860
Commercial/corporate	10,398	6,819	91	-	17,309
Mortgages	3,505	464	(5)	0	3,964
Gross loans and advances	15,445	7,165	521	0	23,133
Undrawn loan commitments	267	284	-	-	551

5 **Loans (continued)**

5.1 Allowance for impairment losses (continued)

	For the year ended 2018				
	Balance at beginning of period (AWG '000)	Provision for credit losses (AWG '000)	Net write-offs (AWG '000)	Exchange rate and other (AWG '000)	Balance at end of period (AWG '000)
Retail	1,496	(450)	490	6	1,542
Commercial/corporate	8,746	2,142	(490)	0	10,398
Mortgages	4,658	1,506	(2,659)	-	3,505
Gross loans and advances	14,900	3,198	(2,659)	6	15,445
Undrawn loan commitments	264	3	-	-	267

The following tables reconcile the opening and closing allowance for credit losses, by stage, for each major product category.

Reconciling items include the following:

- Transfers between stages, which are presumed to occur before any corresponding remeasurements.
- Purchases and originations, which reflect the newly recognized assets and the related allowance during the period.
- Derecognitions and maturities, which reflect the assets and related allowance derecognized during the period without a credit loss being incurred.
- Remeasurements for allowances, which comprise of the impact of changes in model inputs or assumptions, including changes in forward-looking macroeconomic conditions; partial repayments and additional draws on existing facilities; changes in the measurement following a transfer between stages; and unwinding of the time value discount due to the passage of time. For gross carrying amounts, this represents additional draws, repayments, and the accrual of interest under the effective interest method.
- Exchange rate and other.

5 **Loans (continued)**

5.1 **Allowance for impairment losses (continued)**

	2019	2018
Gross Exposures	(AWG '000)	(AWG '000)
Performing	502,132	456,423
Underperforming	60,193	69,903
Non-performing	16,905	22,493
Loans written-off	-	-
Unearned interest	-	-
Total gross loan receivables	579,230	548,819
Less: Loan loss allowance	(23,133)	(15,443)
Less: Write offs	-	-
Loan receivables net of expected credit losses	556,097	533,376

5 Loans (continued)

5.1 Allowance for impairment losses (continued)

	For the year ended 2019			
	Allowance For Credit Losses (AWG '000)			
	Performing		Impaired	Total
	Stage 1	Stage 2	Stage 3	
Balance at beginning of period	2,724	2,957	9,764	15,446
Provision for credit losses				
Model changes	-	-	-	-
Transfers in (out) to Stage 1	1,139	(697)	(442)	-
Transfers in (out) to Stage 2	(79)	341	(263)	-
Transfers in (out) to Stage 3	(27)	(265)	292	-
Purchases and originations	1,148	124	-	1,272
Derecognitions and maturities	(258)	(478)	-	(735)
Remeasurements	152	8,931	(2,454)	6,629
Write-offs	-	-	(1,039)	(1,039)
Recoveries	-	-	1,561	1,561
Exchange rate and other	-	-	-	-
Balance at end of period	4,800	10,914	7,419	23,133

	For the year ended 2018			
	Allowance For Credit Losses (AWG '000)			
	Performing		Impaired	Total
	Stage 1	Stage 2	Stage 3	
Balance at beginning of period	2,329	1,150	11,421	14,900
Provision for credit losses				
Model changes	-	-	-	-
Transfers in (out) to Stage 1	16	(8)	(8)	-
Transfers in (out) to Stage 2	(45)	278	(233)	-
Transfers in (out) to Stage 3	(14)	(305)	319	-
Purchases and originations	787	176	-	963
Derecognitions and maturities	(305)	(266)	-	(571)
Remeasurements	(45)	1,933	918	2,806
Write-offs	-	-	(3,916)	(3,916)
Recoveries	-	-	1,257	1,257
Exchange rate and other	(0)	(0)	6	6
Balance at end of period	2,724	2,957	9,764	15,445

5 **Loans (continued)**

5.1 **Allowance for impairment losses (continued)**

Based on our collections policies substantially all of the amounts written off during the period are still subject to enforcement activities at year end.

Key inputs and assumptions:

The measurement of expected credit losses is a complex calculation that involves a large number of interrelated inputs and assumptions. The key drivers of changes in expected credit losses include our internal historical default rates, transition matrices, unemployment rate, GDP and inflation rate.

Further details on the key inputs and assumptions used as at October 31, 2019 and October 31, 2018 are provided in Note 2.

The following table compares our probability-weighted estimate of expected credit losses for performing loans to expected credit losses estimated in our base case scenario. Results reflect the Stage 1 and Stage 2 allowance for credit losses. Loan performance metrics such as delinquency and projected loss given default rates have the most significant impact on the allowance. The primary economic factors used in our calculation include unemployment, GDP growth and inflation rates.

	As at October 31, 2019	
	Carrying Value	Base Scenario
ACL on performing loans [1]	15,713,819	15,697,270
	As at October 31, 2018	
	Carrying Value	Base Scenario
ACL on performing loans [1]	5,682,223	5,644,859

(1) Represents Stage 1 and Stage 2 ACL on loans, acceptances, and commitments.

5 Loans (continued)

5.1 Allowance for impairment losses (continued)

Transfers between stages
Transfers between Stage 1 and Stage 2 is based on the assessment of significant increases in credit risk relative to initial recognition. Refer to Note 2 for further details on our policy for assessing for significant increase in credit risk. The impact of moving from 12 months expected losses to lifetime credit losses, or vice versa, varies by product and is dependent on the expected remaining life at the date of the transfer. Stage transfers may result in significant fluctuations in expected credit losses.

The following table illustrates the impact of staging on our ACL by comparing our allowance if all performing loans were in Stage 1 to the actual ACL recorded on these assets.

	As at October 31, 2019
	Performing loans (1)
ACL - all performing loans in Stage 1	5,032,565
Impact of staging	10,681,254
Stage 1 and 2 ACL	15,713,819

	As at October 31, 2018
	Performing loans (1)
ACL - all performing loans in Stage 1	2,795,075
Impact of staging	2,887,148
Stage 1 and 2 ACL	5,682,223

(1) Represents loans, acceptances and commitments in Stage 1 and Stage 2.

6 **Securities**

Carrying value of securities

The following table presents the contractual maturities of the carrying values of financial instruments held at the end of the period.

	As at October 31, 2019						
	Term to maturity[1]						
	Within 3 months (AWG '000)	3 months to 1 year (AWG '000)	1 year to 5 years (AWG '000)	5 years to 10 years (AWG '000)	Over 10 years (AWG '000)	With no specific maturity (AWG '000)	Total (AWG '000)
Fair value through profit or loss[2]							
Government debt	-	-	-	-	-	-	-
Corporate debt and other debt	-	-	-	-	-	-	-
Money market instruments	-	-	-	-	-	5,306	5,306
	-	**-**	**-**	**-**	**-**	**5,306**	**5,306**
Fair value through other comprehensive income[3]							
Treasury bills and treasury notes							
Amortized cost	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
Government and state-owned enterprises debt							
Amortized cost	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
Corporate debt							
Amortized cost	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
Equities							
Cost	-	-	-	-	-	450	450
Fair value[4]	-	-	-	-	-	2,925	2,925
	-	**-**	**-**	**-**	**-**	**2,925**	**2,925**
Amortized Cost							
Amortized cost[5]	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
	-	**-**	**-**	**-**	**-**	**-**	**-**
Total carrying value of securities	**-**	**-**	**-**	**-**	**-**	**8,231**	**8,231**

6 Securities (continued)

Carrying value of securities (continued)

	As at October 31, 2018						
	Term to maturity[1]						
	Within 3 months	3 months to 1 year	1 year to 5 years	5 years to 10 years	Over 10 years	With no specific maturity	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
Fair value through profit or loss [2]							
Government debt	-	-	-	-	-	-	-
Corporate debt and other debt	-	-	-	-	-	-	-
Money market instruments	-	-	-	-	-	4,844	4,844
	-	**-**	**-**	**-**	**-**	**4,844**	**4,844**
Fair value through other comprehensive income [3]							
Treasury bills and treasury notes							
Amortized cost	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
Government and state-owned enterprises debt							
Amortized cost	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
Corporate debt							
Amortized cost	-	-	-	-	-	-	-
Fair value	-	-	-	-	-	-	-
Equities							
Cost	-	-	-	-	-	450	450
Fair value[4]	-	-	-	-	-	2,925	2,925
	-	**-**	**-**	**-**	**-**	**2,925**	**2,925**
Amortized Cost							
Amortized cost[5]	9,643	-	-	-	-	-	9,643
Fair value	9,693	-	-	-	-	-	9,693
	9,643	**-**	**-**	**-**	**-**	**-**	**9,643**
Total carrying value of securities	**9,643**	**-**	**-**	**-**	**-**	**7,769**	**17,412**

(1) Actual maturities may differ from contractual maturities shown above since borrowers may have the right to extend or prepay obligations with or without penalties.

(2) Trading securities are recorded at fair value.

(3) Debt securities carried at fair value through other comprehensive income are presented net of allowance for credit losses.

(4) We hold equity securities designated as FVOCI as the investments are not held-for-trading purposes.

(5) Amortized cost securities, included in Investment securities are recorded at amortized cost, and are presented net of allowance for credit losses.

6 **Securities (continued)**

6.1 Unrealized gains and losses on securities at fair value through other comprehensive income

The following tables present unrealized gains and losses on securities at fair value through other comprehensive income as at the end of the period.

	As at 2019			
	Cost/Amortized cost	**Gross unrealized gains[1]**	**Gross unrealized losses[1]**	**Fair value**
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
Treasury bills and treasury notes	-	-	-	-
Government and state-owned enterprises debt	-	-	-	-
Corporate debt	-	-	-	-
Equities[2]	450	2,475	-	2,925
	450	2,475	-	2,925

	As at 2018			
	Cost/Amortized cost	**Gross unrealized gains[1]**	**Gross unrealized losses[1]**	**Fair value**
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
Treasury bills and treasury notes	-	-	-	-
Government and state-owned enterprises debt	-	-	-	-
Corporate debt	-	-	-	-
Equities[2]	450	2,475	-	2,925
	450	2,475	-	2,925

[1] Gross unrealized gains and losses include allowance for credit losses, excluding equities designated as FVOCI.
[2] Unrealized gains and losses on equities will not reclassify to profit and loss when realised.

6 **Securities (continued)**

6.2 Allowance for credit losses securities

The following tables reconcile the opening and closing allowance for debt securities at amortized cost and FVOCI by stage. Reconciling items include the following:

- Transfers between stages, which are presumed to occur before any corresponding remeasurement of the allowance.
- Purchases and originations, which reflect the allowance related to assets newly recognized during the period.
- Derecognitions and maturities, which reflect the allowance related to assets derecognized during the period without a credit loss being incurred.
- Remeasurements, which comprise the impact of changes in model inputs or assumptions, including changes in forward-looking macroeconomic conditions; partial repayments and additional draws on existing facilities; changes in the measurement following a transfer between stages; and unwinding of the time value discount due to the passage of time.
- During the twelve months ended October 31, 2019 and October 31, 2018, there were no significant changes to the models used to estimate expected credit losses.

Significant changes in the gross carrying amount of securities at amortized cost and FVOCI that contributed to changes in the allowance include the following:

Allowance for credit losses – securities at amortized cost

	For the year ended 2019			
	Allowance For Credit Losses (AWG '000)			
	Performing		Impaired	Total
	Stage 1	Stage 2	Stage 3	
Balance at beginning of period	3	-	-	3
Provision for credit losses				
Model changes	-	-	-	-
Transfers in (out) to Stage 1	-	-	-	-
Transfers in (out) to Stage 2	-	-	-	-
Transfers in (out) to Stage 3	-	-	-	-
Purchases and originations	-	-	-	-
Derecognitions and maturities	(1)	-	-	(1)
Remeasurements	(2)	-	-	(2)
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Exchange rate and other	-	-	-	-
Balance at end of period	0	-	-	0

6 Securities (continued)

6.2 Allowance for credit losses securities (continued)

Allowance for credit losses – securities at amortized cost

	For the year ended 2018			
	Allowance For Credit Losses (AWG '000)			
	Performing		Impaired	Total
	Stage 1	Stage 2	Stage 3	
Balance at beginning of period	6	-	-	6
Provision for credit losses				
Model changes	-	-	-	-
Transfers in (out) to Stage 1	-	-	-	-
Transfers in (out) to Stage 2	-	-	-	-
Transfers in (out) to Stage 3	-	-	-	-
Purchases and originations	46	-	-	46
Derecognitions and maturities	(54)	-	-	(54)
Remeasurements	5	-	-	5
Write-offs	-	-	-	-
Recoveries	-	-	-	-
Exchange rate and other	-	-	-	-
Balance at end of period	3	-	-	3

6 Securities (continued)

6.2 Allowance for credit losses securities (continued)

	2019	2018
Gross Exposures	(AWG '000)	(AWG '000)
Performing	8,231	17,415
Underperforming	-	-
Non-performing	-	-
Securities written-off	-	-
Unearned interest	-	-
Total securities	8,231	17,415
Less: Allowance for credit losses	-	(3)
Less: Write offs	-	-
Securities net of expected credit losses	8,231	17,412

6.3 Securities at amortised cost

	2019	2018
	(AWG '000)	(AWG '000)
Government and state-owned enterprises debt securities	-	9,643
	-	9,643
Current	-	9,643
Non-current	-	-
	-	9,643

6 **Securities (continued)**

6.4 Movements in securities

	FVTPL	FVOCI	Amortised Cost	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at November 1, 2018	4,844	2,925	9,643	17,412
Additions	-	-	-	-
Disposal (sale and redemption)	-	-	(9,643)	(9,643)
Gains / (losses) from changes in fair value	462	-	-	462
Foreign exchange adjustment	-	-	-	-
As at October 31, 2019	5,306	2,925	-	8,231

	FVTPL	FVOCI	Amortised Cost	Total
As at November 1, 2017	5,140	2,610	1,495	9,245
Additions	-	-	17,708	17,708
Disposal (sale and redemption)	-	-	(9,560)	(9,560)
Gains / (losses) from changes in fair value	(296)	315	-	19
Foreign exchange adjustment	-	-	-	-
As at October 31, 2018	4,844	2,925	9,643	17,412

There are no investments that have been pledged as security on behalf of any affiliated party this year (2018: nil).

7 Intangible assets

	2019	2018
	Software (AWG '000)	Software (AWG '000)
Opening net carrying value	12,520	14,991
Additions	-	-
Amortisation	(2,587)	(2,471)
Closing net carrying value	9,933	12,520
Cost	30,618	30,618
Accumulated amortisation	(20,685)	(18,098)
Net carrying value	9,933	12,520

The useful life used in the calculation of amortisation of software is 4 - 10 years.

8 Goodwill

	2019	2018
	(AWG '000)	(AWG '000)
Balance at beginning of the year	23,654	23,654
Impairment loss	(23,654)	-
Balance at end of the year	-	23,654

8 Goodwill (continued)

Goodwill represents the excess of the cost of acquisition over the fair value of the net assets of the acquired ABNAmro banking operations at the date of acquisition. These net assets have been fully integrated in the operations of the Bank. Goodwill on assets acquired was assessed to determine the need for an impairment loss as at the year-end, in accordance with IAS 36 – Impairment of assets. In 2019 throughout, this assessment used the "fair value less costs of disposal" (2018 FVLCD) method. Based on the results of the assessment, goodwill was deemed to be impaired as at October 31, 2019 and as such an impairment charge was required.

The Bank calculates fair value less costs of disposal (FVLCD) using the discounted cash flow ("DCF") method that projects future cash flows over a 5-year period. The Bank is considered to be the cash-generating unit for the purposes of this assessment. Future cash flows are based on the same factors noted below. Cash flow projections are adjusted to reflect the considerations of a prospective third-party buyer and discounted to their present value. Non-interest expenses are adjusted based on synergies that can be achieved with a prospective in-market buyer. We use significant judgement to determine inputs to the discounted cash flow model which is most sensitive to changes in future cash flows, discount rates and terminal growth rates applied to cash flows beyond the forecast period. The key assumptions used in the cash flows are as follows:

Revenue
Future cash flows are based on financial plans agreed by management, estimated based on forecast results, business initiatives, capital required to support future cash flows and returns to shareholders. Key drivers of future cash flows include net interest margins and average interest-earning assets. The values assigned to these drivers over the forecast period are based on past experience, external and internal economic forecasts, and management's expectations of the impact of economic conditions on our financial results.

Provision for credit losses
Based on assumptions for loan growth combined with assumed economic conditions and specific risk mitigation strategies being undertaken.

Non-interest expenses
Based on assumed rates of inflation and specific ongoing initiatives that will result in additional costs or result in cost savings.

Taxation
Based on prevailing tax rates in each jurisdiction in which the Group operates.

	October 31, 2019	**October 31, 2018**
Terminal revenue growth rates	1.3%	2.7%
Terminal growth rates	3.5%	4.0%
Discount rates (1)	10.4%	11.0%

(1) Pre-tax discount rates are determined implicitly based on post-tax discount rates

9 Premises and equipment

	Freehold properties	Leasehold improvement	Equipment	Capital work in	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
Year ended October 31, 2018					
Opening net book value	12,901	87	1,957	260	15,205
Additions	2	-	1,219	689	1,910
Transfers	-	-	-	-	-
Disposals	-	-	(43)	-	(43)
Depreciation	(467)	(19)	(747)	-	(1,233)
Closing net book value	12,436	68	2,386	949	15,839
At October 31, 2018					
Cost	22,831	1,510	20,772	949	46,063
Accumulated depreciation	(10,395)	(1,442)	(18,386)	-	(30,224)
Net book value	12,436	68	2,386	949	15,839
Year ended October 31, 2019					
Opening net book value	12,436	68	2,386	949	15,839
Additions	-	-	287	307	594
Transfers	-	-	-	-	-
Disposals	-	-	-	-	-
Depreciation	(512)	(23)	(800)	-	(1,335)
Closing net book value	11,924	45	1,873	1,256	15,098
At October 31, 2019					
Cost	22,829	1,510	20,847	1,256	46,442
Accumulated depreciation	(10,905)	(1,466)	(18,973)	-	(31,343)
Net book value	11,924	45	1,873	1,256	15,098

Assets pledged as security

There were no land and buildings pledged to secure borrowings of the Bank (2018: nil).

10 Deferred tax assets and liabilities

Deferred tax assets and liabilities result from tax loss carryforwards and temporary differences between the tax basis of assets and liabilities and their carrying amounts on our Financial Position. The following amounts are shown in the statement of financial position:

	As at October 31, 2019			
	Net Asset November 1, 2018 (AWG '000)	Change through equity (AWG '000)	Change through profit or loss (AWG '000)	Net Asset October 31, 2019 (AWG '000)
Net deferred tax asset/(liability)				
Allowance for credit losses	2,738	-	(572)	2,166
General loan loss provision	1,284	-	2,507	3,791
Securities	(621)	1	-	(620)
Premises and equipment	(302)	-	801	499
Goodwill	(5,913)	-	5,913	(0)
Other	-	95	-	95
	(2,814)	96	8,649	5,931
Comprising				
Deferred tax assets	4,022	95	2,434	6,551
Deferred tax liabilities	(6,836)	1	6,215	(620)
	(2,814)	96	8,649	5,931

10 Deferred tax assets and liabilities (continued)

	As at October 31, 2018			
	Net Asset November 1, 2017 (AWG '000)	Change through equity (AWG '000)	Change through profit or loss (AWG '000)	Net Asset October 31, 2018 (AWG '000)
Net deferred tax asset/(liability)				
Allowance for credit losses	1,870	(515)	1,383	2,738
General loan loss provision	1,271	-	13	1,284
Securities	(620)	(1)	-	(621)
Premises and equipment	(3,382)	-	3,080	(302)
Goodwill	(5,913)	-	-	(5,913)
	(6,774)	(516)	4,476	(2,814)
Comprising				
Deferred tax assets	3,142	(515)	1,395	4,022
Deferred tax liabilities	(9,916)	(1)	3,081	(6,836)
	(6,774)	(516)	4,476	(2,814)

As at October 31, 2019, deductible temporary differences of AWG 6.5 million (October 31, 2018: AWG 4 million) available to be offset against potential tax adjustments or future taxable income were recognized as deferred tax assets.

11 Assets classified as held for sale

	2019	2018
	(AWG '000)	(AWG '000)
Land	60	60
Buildings	425	425
	485	485
Land		
Cost	60	60
Impairment	-	-
Net book value transferred from premises and equipment	60	60
Buildings		
Cost	1,106	1,106
Impairment	-	-
Accumulated depreciation	(681)	(681)
Net book value transferred from premises and equipment	425	425

In October 2017 the management of the Bank decided to sell the 2 buildings which used to be the Noord branch and the San Nicolas branch in Aruba. The sale of the Noord branch was completed in February 2018. There are several interested potential buyers for the San Nicolas branch. The sale was expected to be completed before the end of October 31, 2019, but did not materialize. The sale is now expected to be completed before October 31, 2020 and as such the asset remains designated as held for sale.

12 Other assets

	2019	2018
	(AWG '000)	(AWG '000) Restated
Prepaid expenses	223	270
Interest receivable	1,721	1,785
Profit tax recoverable	6,981	6,981
Suspense accounts	0	324
Other	0	0
	8,926	9,360

All other assets are current assets.

13 Customers' deposits

	2019	2018
	(AWG '000)	(AWG '000)
Savings	201,325	225,402
Term deposits	116,980	107,744
Current accounts	385,258	440,979
	703,564	774,125

13.1 Sectoral analysis

	2019	2018
Consumers	286,907	326,687
Private institutions	367,146	359,728
State institutions	38,198	78,383
Other	11,313	9,327
	703,564	774,125
Current	628,460	744,148
Non-current	75,103	29,977
	703,564	774,125

14 Other liabilities

	2019 (AWG '000)	2018 (AWG '000)
Accruals and payables	3,369	2,468
Suspense accounts	136	1,244
Unclaimed balances	2,087	2,062
Deferred income	3,708	3,972
Interest payable	1,550	4,974
Contract liabilities (1)	391	381
Provisions	1,736	720
Allowance for credit losses (Note 21)	109	67
Other	121	306
	13,208	16,194
Current	7,412	10,160
Non-current	5,795	6,034
	13,208	16,194

During the year, allowance for credit losses for accounts receivable amounted to AWG 9. The accumulated credit losses on accounts receivable as at October 31, 2018 is AWG 51.

Contract liabilities[(1)]

The Group derives revenue from contracts with customers in the form of annual credit cards fees, which are paid for upfront by cardholders for the right to use certain RBC credit cards products. Under IFRS 15 – Revenue from contracts with customers, the one-time annual fee represents the transaction price received to transfer the performance obligation. However as the performance obligations will transpire over time, throughout the annual period, such revenues should be recognized over the applicable annual cycle. The above balance represents the portion of annual fee revenue which was deferred and remained outstanding as at the Statement of Financial Position date.

15 Other components of equity

Investment revaluation reserve – securities FVOCI

	2019	2018
Balance at beginning of the year	1,866	1,861
Transition adjustment	-	(217)
Net losses/(gains) arising during the year on debt securities, net of tax	-	-
Net losses/(gains)arising during the year on equity securities, net of tax	(0)	222
Net change in allowance for credit losses on debt securities carried at FVOCI, net of tax	-	-
Net realised gains on debt securities transferred to income, net of tax	-	-
Balance at end of the year	1,866	1,866

16 Interest income

	2019	2018
	(AWG '000)	(AWG '000)
Loans and advances to customers	43,044	41,037
Securities and Treasury bills	667	240
Due from banks	-	405
Due from affiliates	-	-
	43,712	41,682

16.1 Securities and Treasury bills

	(AWG '000)	(AWG '000)
FVTPL	535	(214)
FVOCI	81	346
Dividends	45	0
At amortized cost	6	108
	667	240

17 Interest expense

	2019	2018
	(AWG '000)	(AWG '000)
Customers' deposits	4,817	6,749
Due to banks	14	-
Due to affiliates	57	-
Other interest bearing liabilities	(23)	-
	4,865	6,749

18 Non-Interest income

	2019	2018
	(AWG '000)	(AWG '000)
Foreign exchange earnings	6,216	6,081
Fees and commissions	14,814	17,366
	21,030	23,447

18.1 Fees and commission income

Transaction service fee / commission	14,588	17,153
Credit related fees and commission	226	213
	14,814	17,366

19 Non-interest expenses

	2019	2018
	(AWG '000)	(AWG '000)
Staff costs	22,167	20,589
Premises and equipment expenses, excluding depreciation and operating lease rentals	1,533	1,589
Advertising	631	693
Depreciation and amortisation of (in)tangibles	3,922	3,704
Operating lease rentals	1,010	1,219
Directors' remuneration	58	48
Auditors' remuneration	225	144
Other operating expenses	20,308	24,979
	49,854	52,965

19.1 Staff costs

Wages and salaries including bonuses	20,849	19,233
Employees' retirement benefit expense	1,318	1,356
	22,167	20,589

The number of persons employed by the Bank was 140 as per October 31, 2019 (2018: 154).

19 Non-interest expenses (continued)

19.2 Other operating expenses

	2019 (AWG '000)	2018 (AWG '000)
Management fees	9,724	12,554
Credit and debit card expenses	4,653	4,902
Telephone, postage and courier expenses	909	1,181
Security costs	1,551	903
Other	3,471	5,439
	20,308	24,979

20 Taxation expense / (recovery)

	2019 (AWG '000)	2018 (AWG '000)
Current tax charge	2,758	2,794
Prior years tax charge	-	-
Deferred tax charge / (recovery)	(8,649)	(4,476)
	(5,891)	(1,682)

Reconciliation to statutory tax rate

The tax on the profit differs from the theoretical amount that would arise using the average tax rate of the country as follows:

	2019	2018
Profit before taxation	(20,809)	2,217
Prima facie tax calculated at an average rate of 2019 - 25% (2018 - 25%)	(5,202)	554
Expenses not deductible for tax purposes	8,282	(578)
Expenses deductible for tax purposes	-	-
Adjustment tax payable previous years	(322)	2,818
Net deferred tax	(8,649)	(4,476)
Income tax expense	(5,891)	(1,682)

21 Contingent Liabilities

21.1 Customers' liability under guarantees, indemnities and letters of credit

These represent the group's potential liability, for which there are equal and offsetting claims against its customers in the event of a call on these commitments. These amounts are not reflected in the statement of financial position.

	2019	2018
	(AWG '000)	(AWG '000)
Guarantees	5,654	7,128
Letters of credit	4,425	4,604
	10,079	11,732

Our credit review process, our policy for requiring collateral security, and the types of collateral security held are generally the same as required for loans. We believe that it is highly unlikely that all or substantially all of the guarantees and commitments will be drawn or settled within one year, and contracts may expire without being drawn or settled. Historically, we have not made any significant payments under such indemnifications.

As at October 31, 2019 accumulated allowance for credit losses for contingent liabilities amounted to AWG 108,654 (2018: AWG 66,953) - Note 14.

22 Credit commitments

The following table breaks down the Group's main credit exposure of credit commitments as categorized by industry sectors of counterparties:

	2019	2018
	(AWG '000)	(AWG '000)
Consumer	31,165	24,915
Manufacturing	1,673	1,656
Distribution	8,448	3,435
Financial services	8,950	3,621
Transport	3,354	3,032
Construction	992	928
Real estate	5,456	1,814
Tourism	932	437
Professional services	347	357
Utilities	103	3,019
Health services	587	1,009
Other	9,347	5,142
	71,356	49,365

23 Capital and lease commitments

There were no capital commitments as at October 31, 2019 (2018 - AWG nil).

We are obligated under a number of non-cancellable operating leases for premises and equipment. These leases have various terms, escalation and renewal rights. The minimum future lease payments under non-cancellable operating leases are as follows:

	2019	2018
	(AWG '000)	(AWG '000)
Within one year	320	307
One to five years	255	62
	575	369

Operating lease expense recorded in profit or loss for 2019 amounted to AWG 1,010,446 (2018: AWG 1,218,871).

24 Related party transactions

A number of banking transactions are entered into with related parties in the normal course of business. The loans to related parties are adequately secured or have been provided for within the adopted loan policy of the Bank. Balances and transactions between the Bank and its subsidiaries, which are related parties of the subsidiaries, have been eliminated on consolidation and are not disclosed in this note.

We have applied the low credit risk exemption on all amounts due to/from associates and affiliates as they demonstrate a low risk of default and the related RBC entity has a strong capacity to meet its contractual cash flow obligations. As a result, any ACL is deemed to be insignificant.

The following balances are outstanding related to other subsidiaries of Royal Bank of Canada.

	2019	2018
	(AWG '000)	(AWG '000)
Loans and investments		
Ultimate parent	21	31
Fellow subsidiaries	27,383	20,206
	27,405	20,237
Deposits and Other liabilities		
Ultimate parent	255	226
Fellow subsidiaries	13,029	4,808
	13,285	5,034
Interest expense		
Fellow subsidiaries	57	-
	57	-

24 Related party transactions (continued)

Key management personnel and Directors

Key management personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of RBC and its subsidiaries, directly or indirectly. They include the senior executives called the Business Management Operating Committee (BMOC). The BMOC is comprised of the President and Chief Executive Officer and those individuals that report directly to him, including the Chief Financial Officer, Chief Human Resources Officer, Chief Risk Officer, and heads of our business units. The BMOC is ultimately responsible for all material decisions. The BMOC is also responsible for establishing the overall strategic direction of the group and, in that regard, sets global parameters for the group within which the board of directors and management of each subsidiary in the group exercise their respective discretion to make decisions concerning the strategic direction and day-to-day management of the particular subsidiary. The Directors of RBC do not plan, direct, or control the activities of the group; they oversee the management of the business and provide stewardship.

Transactions, arrangements and agreements involving key management personnel, Directors and their close family members

In the normal course of business, RBC Royal Bank (Aruba) N.V. provide certain banking services to key management personnel, Directors, and their close family members. These transactions were made on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing and did not involve more than the normal risk of repayment or present other unfavourable features.

Management fees

Administrative charges by RBC Financial (Caribbean) Limited for the year ended October 31, 2019 were AWG 6,007,001 (2018: AWG 7,881,217).

Shared Service Costing charges by RBC Royal Bank (Trinidad and Tobago) Limited for the year ended October 31, 2019 were AWG 914,681 (2018: AWG 1,840,191).

RBC Royal Bank N.V., a wholly owned subsidiary of ABC Holdings N.V., charges a fee for management services provided. The total fee charged for the year ended October 31, 2019 is AWG 1,796,298 (2018: AWG 1,767,080). RBC Royal Bank (Aruba) N.V. also charged RBC Royal Bank N.V. a total fee of AWG 929,694 (2018: AWG 935,653) for management services.

Business travellers charges by RBC Canada Head Office for the year ended October 31, 2019 were AWG 1,003,431 (2018: AWG 942,356).

Trademark License Fee by Royal Bank of Canada for the year ended October 31, 2019 was AWG 2,762 (2018: 2,839).

25 Financial Risk Management

25.1 Statement of financial position - categorization

	As at 31 October 2019 (AWG '000)	2018 (AWG '000)
Assets		
Financial assets at fair value through profit or loss		
Securities	5,306	4,844
Financial assets at fair value through other comprehensive income		
Cash and cash equivalents – treasury bills	12,992	100,983
Securities – equities instruments (1)	2,925	2,925
	15,917	103,908
Financial assets at amortised costs		
Cash and cash equivalents	153,748	140,988
Balances with central bank	73,650	79,040
Loans	556,097	533,374
Securities	-	9,643
Due from associated and affiliated companies	27,405	20,237
Other assets	1,721	1,785
	812,621	785,067
Total financial assets	833,844	893,819
Non-financial assets	62,926	64,095
Total assets	896,770	957,914
Liabilities		
Financial liabilities at amortised costs		
Due to banks	639	406
Customers' deposits	703,564	774,125
Due to associated and affiliated companies	13,285	5,034
Other liabilities	3,636	7,036
	721,124	786,601
Total financial liabilities	721,124	786,601
Non-financial liabilities	26,300	24,504
Total liabilities	747,424	811,105
Total equity	149,346	146,809
Total equity and liabilities	896,770	957,914

25 **Financial Risk Management (continued)**

25.1 **Statement of financial position – categorization (continued)**

Securities – equity securities designated at FVOCI[(1)]
The Bank designated certain equity securities which are not held for trading as FVOCI. The Bank irrevocably elected to recognize the equity securities as FVOCI because the equity securities are held for the long term for strategic purposes.

The following table presents the Bank's equity instruments designated as at FVOCI at the end of the period by business category.

	Number of companies	Number of shares/units[(a)] ('000)	Carrying value 2019 (AWG '000)	Carrying value 2018 (AWG '000)	Dividends received 2019 (AWG '000)	Dividends received 2018 (AWG '000)
Business category						
Economic development	-	-	-	-	-	-
Stock exchange	-	-	-	-	-	-
Clearing house	-	-	2,925	2,925	45	45
Financial services	-	-	-	-	-	-
Other	-	-	-	-	-	-
Total			2,925	2,925	45	45

(a)During the year ended October 31, 2019 there were no disposals from the equity shares designated as FVOCI portfolio (2018: Nil).

25 Financial Risk Management (continued)

25.2 Risk Management

Risk is inherent in the bank's activities but it is managed through a process of ongoing identification, measurement and monitoring subject to risk limits and other controls. This process of risk management is critical to the bank's continuing profitability and each individual company within the group is accountable for the risk exposures relating to its responsibilities. The bank is exposed to credit risk, liquidity risk, operating risk and market risk, the latter being subdivided into trading and non-trading risks.

The independent risk control process does not include business risks such as changes in the environment, technology and industry.

Risk management structure

The Board of Supervisory Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

Board of Supervisory Directors

The Board of Supervisory Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

Risk Management Unit

A centralized Risk Management Unit provides oversight of the implementation and maintenance of risk related procedures to ensure an independent control process. The unit which is sub-divided into three departments (Group Market Risk, Group Credit Risk and Group Compliance and Operational Risk), is also responsible for monitoring compliance with risk policies and limits across the group in the three key areas of credit risk, market risk and operational risk. Each business group has decentralized units which are responsible for the independent control of risks, including monitoring the risk or exposures against limits and the assessment of risks of new products and structured transactions. These decentralized units also ensure the complete capture of the risks in risk measurement and reporting systems.

Asset/Liability Committee (ALCO)

The parent ALCO has a mandate, which includes the recommendation of policies covering investments, liquidity and market risk to the Operating Committee and the Board, and the monitoring of compliance with risk policies and limits in the areas of credit risk and market risk.

Group Investment and Capital Committee

The parent has established a Group Investment and Capital Committee, which is responsible for the review and validation of the policies and procedures applied in the valuation of financial assets and liabilities. The Committee also approves the mark to market valuation of financial assets and liabilities on a quarterly basis.

25 **Financial Risk Management (continued)**

25.2 **Risk Management**

Internal Audit

Risk management processes throughout the group are audited annually by the internal audit function that examines both the adequacy of the procedures and the group's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Board's Audit Committee and subsidiary boards' Audit Committees.

Risk measurement and reporting systems

The bank's risks are measured using methods which reflect the expected loss likely to arise in normal circumstances.

Monitoring and controlling risks is primarily performed based on limits established by the bank. These limits reflect the business strategy and market environment of the group as well as the level of risk that the group is willing to accept, with additional emphasis on selected industries and geographies.

Information compiled from all the business units is examined and processed in order to analyze, control and identify risks early. This information which consists of several reports is presented and explained to the Board of Supervisory Directors, the Board's Committees, the Asset/Liability Committees, and the head of each business unit. The reports include but are not limited to aggregate credit exposure, open currency positions, liquidity ratios and risk profile changes. On a quarterly basis senior management assesses the appropriateness of the allowance for credit losses.

For all levels throughout the bank, specifically tailored risk reports are prepared and distributed in order to ensure that all business units have access to necessary and up-to-date information.

Risk mitigation

As part of its overall risk management, the group uses derivatives and other instruments to manage exposures resulting from changes in interest rates and foreign currencies.

The risk profile is assessed before entering into hedge transactions, which are authorized by the appropriate level of seniority within the group. The effectiveness of hedges is assessed by the Group Market Risk and Group Finance units (based on economic considerations rather than the IFRS hedge accounting regulations). The effectiveness of all the hedge relationships is monitored by the Group Market Risk Unit monthly.

The bank actively uses collateral to reduce its credit risks.

25 Financial Risk Management (continued)

25.3 Liquidity Risk

Liquidity and funding risk (Liquidity risk) is the risk that the Bank may be unable to generate sufficient cash or its equivalents in a timely and cost effective manner to meet our commitments as they come due. Liquidity risk arises from mismatches in the timing and value of cash flows. The Bank's liquidity profile is structured to ensure that we have sufficient liquidity to satisfy current and prospective commitments in both normal and stressed conditions.

The Bank's liquidity management process is carried out by the Treasury department of each business unit and monitored by Caribbean Group ALCO. The Bank's liquidity management framework is designed to ensure that there are adequate reserves of cash and other liquid securities to satisfy current and prospective commitments arising from either on-balance sheet or off-balance sheet liabilities.

To manage liquidity risk within our liquidity risk appetite, limits are set on various metrics reflecting a range of time horizons and severity of stress conditions and develop contingency plans. Our liquidity risk measurement and control activities are divided into three categories as follows:

Structural (longer-term) liquidity risk
To guide our secured and unsecured wholesale term funding activities, we employ an internal metric to manage and control the structural alignment between long-term assets and longer-term funding sources from core deposits.

Tactical (shorter-term) liquid risk
To address potential immediate cash flows risks in times of stress, we use short-term net cash flow limits to control risk of material units, subsidiaries and currencies and perform stress testing assessments. Net cash flow positions are determined by applying internally-derived risk assumptions and parameters to known and anticipated cash flows for all material unencumbered assets, liabilities and off-balance sheet activities. Encumbered assets are not considered a source of available liquidity.

Contingency liquidity risk
Contingency liquidity risk planning assess the impact of sudden stress events, and our planned responses. The group's Liquidity Contingency Plan (LCP) maintained and administered by Caribbean Treasury, has been developed to guide our potential responses to liquidity crises. The contingency liquidity risk planning process identifies contingent funding needs and sources under various stress scenarios, and as result informs requirements for our earmarked unencumbered liquid asset portfolios.

USD coverage:	2019	2018
	%	%
- Tactical position	320%	1012%
- Structural position	160%	191%

25 Financial Risk Management (continued)

25.3 Liquidity Risk (continued)

The following table presents the components of the financial assets held for liquidity purposes.

	Cash on hand	Buffer	Total
	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019			
Local currency	10,333	96,936	107,270
Foreign currency	5,536	8,695	14,230
	15,869	105,630	121,500

	Cash on hand	Buffer	Total
	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2018			
Local currency	15,165	103,760	118,925
Foreign currency	4,224	12,420	16,644
	19,389	116,180	135,569

The local currency amount includes the functional reporting currencies of the jurisdictions in which the Group operates.

The buffer is held in the form of liquid cash and short term sovereign assets such as Treasury bills and Treasury notes with maturities of less than three months.

25 Financial Risk Management (continued)

25.3 Liquidity Risk (continued)

The table below presents the cash flows payable by the group under non-derivative financial liabilities by remaining contractual maturities at the statement of financial position date.

	Less than three	Three to six months	Six to twelve	One to five years	Over five years	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019						
Liabilities						
Due to banks	639	-	-	-	-	639
Customers' deposits	605,867	14,409	8,185	30,480	44,623	703,564
Due to associated and affiliated companies	13,285	-	-	-	-	13,285
Other liabilities	3,636	-	-	-	-	3,636
Total liabilities (contractual maturity dates)	623,427	14,409	8,185	30,480	44,623	721,123
As at October 31, 2018						
Liabilities						
Due to banks	406	-	-	-	-	406
Customers' deposits	667,755	60,841	17,217	28,311	-	774,125
Due to associated and affiliated companies	5,034	-	-	-	-	5,034
Other liabilities	7,036	-	-	-	-	7,036
Total liabilities (contractual maturity dates)	680,232	60,841	17,217	28,311	-	786,601

25 Financial Risk Management (continued)

25.3 Liquidity Risk (continued)

The table below summarizes the group's contingent liabilities and commitments based on contractual maturity dates.

	Up to one year	One to five years	Over five years	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019				
Guarantees, acceptances, indemnities and letters of credit	7,417	690	1,973	10,079
Credit commitments	71,356	-	-	71,356
Operating lease commitments	320	255	-	575
Capital commitments	-	-	-	-
	79,093	945	1,973	82,010
As at October 31, 2018				
Guarantees, acceptances, indemnities and letters of credit	9,240	1,038	1,454	11,732
Credit commitments	49,365	-	-	49,365
Operating lease commitments	307	62	-	369
Capital commitments	-	-	-	-
	58,911	1,100	1,454	61,465

25 Financial Risk Management (continued)

25.4 Market Risk

The bank takes on exposure to market risks, 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, currency and equity products, all of 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, foreign exchange rates and equity prices. The bankp separates exposures to market risk into either trading or non-trading portfolios.

The market risks arising from non-trading activities are measured separately by the Treasury department. Regular reports are submitted to the Group Asset/Liability Committee on a regular basis.

Non-trading portfolios primarily arise from the interest-rate management of the entity's retail and commercial banking assets and liabilities. Non-trading portfolios also consist of interest rate, foreign exchange and equity risks arising from the group's investment securities.

25.4.1 Market Risk measurement techniques

The major measurement technique used by the bank to measure and control market risk is stress testing.

Based on quarterly reports provided by the bank, Group Market Risk applies stress tests to provide an indication of the potential size of losses that could arise in extreme conditions.

25 **Financial Risk Management (continued)**

25.4 Market Risk (continued)

25.4.1 Market risk measurement techniques (continued)

Group Market Risk performs a risk sensitivity analysis by applying possible foreign currency rate stress events on the group's foreign currency trading portfolio in order to assess potential impacts to foreign exchange earnings.

25.4.2 Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Board has established limits on the level of mismatch of interest rate repricing that may be taken, which is monitored by the Treasurers and Asset/Liability Committees.

Sensitivity analyzes were conducted to determine the effect on net profit and other components of equity arising from a reasonable change in interest rates with all other variables held constant.

	Effect on net profit 2019 (AWG '000)	Effect on other components of equity 2019 (AWG '000)	Effect on net profit 2018 (AWG '000)	Effect on other components of equity 2018 (AWG '000)
Change in interest rate				
+1%	(5,610)	-	(6,491)	-
-1%	5,610	-	6,491	-

25 **Financial Risk Management (continued)**

25.4 **Market Risk (continued)**

25.4.2 **Interest rate risk (continued)**

Interest sensitivity of assets and liabilities to repricing risk

The table below summarizes the bank's exposure to interest rate repricing risk. It includes the group's financial instruments at carrying amounts, categorized by the earlier of contractual repricing or maturity dates.

	Up to one year	One to five years	Over five years	Non-interest bearing	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019					
Assets					
Cash and cash equivalents	12,992	-	-	153,748	166,740
Balances with central bank	-	-	-	73,650	73,650
Loans	40,892	107,718	407,487	-	556,097
Securities	5,306	-	-	2,925	8,231
Due from associated and			-	-	
affiliated companies	-	-	-	27,405	27,405
Other assets	1,721	-	-	-	1,721
Total financial assets	60,912	107,718	407,487	257,727	833,845
Liabilities					
Due to banks	-	-	-	639	639
Customers' deposits	305,307	30,480	44,623	323,154	703,564
Due to associated and					
affiliated companies	-	-	-	13,285	13,285
Other liabilities	3,635	-	-	-	3,635
Total financial liabilities	308,942	30,480	44,623	337,078	721,123
Interest sensitivity gap	(248,031)	77,238	362,864		

25 **Financial Risk Management (continued)**

25.4 **Market Risk (continued)**

25.4.2 **Interest rate risk (continued)**

Interest sensitivity of assets and liabilities to repricing risk (continued)

	Up to one year (AWG '000)	One to five years (AWG '000)	Over five years (AWG '000)	Non-bearing (AWG '000)	Total (AWG
As at October 31, 2018					
Assets					
Cash and cash equivalents	150,983	-	-	90,988	241,971
Balances with central bank	-	-	-	79,040	79,040
Loans	57,616	95,508	380,250	-	533,374
Securities	14,487	-	-	2,925	17,412
Due from associated and affiliated companies	-	-	-	20,237	20,237
Other assets	1,785	-	-	-	1,785
Total financial assets	224,871	95,508	380,250	193,190	893,819
Liabilities					
Due to banks	-	-	-	406	406
Customers' deposits	340,430	28,311	-	405,384	774,125
Due to associated and affiliated companies	-	-	-	5,034	5,034
Other liabilities	7,036	-	-	-	7,036
Total financial liabilities	347,466	28,311	-	410,824	786,601
Interest sensitivity gap	(122,595)	67,197	380,250		

25 **Financial Risk Management (continued)**

25.4 **Market Risk (continued)**

25.4.3 **Maturity and rate sensitivity risk**

The table below summarizes the bank's loans and advances to customers and investment securities categorized by the earlier of contractual repricing or maturity dates.

	Up to one year	One to five years	Over five years	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019				
Loans:				
Retail	17,376	43,117	6,936	67,429
Commercial/corporate	45,921	48,450	162,066	256,437
Mortgages	729	16,150	238,485	255,364
Gross loans	64,025	107,718	407,487	579,230
Securities:				
Securities at FVTPL	-	-	5,306	5,306
Securities at FVOCI	-	-	2,925	2,925
Securities at amortised cost	-	-	-	-
Gross securities	-	-	8,231	8,231
As at October 31, 2018				
Loans:				
Retail	16,694	44,462	8,719	69,875
Commercial/corporate	55,199	36,319	142,425	233,943
Mortgages	1,168	14,727	229,106	245,001
Gross loans	73,061	95,508	380,250	548,819
Securities:				
Securities at FVTPL	-	-	4,844	4,844
Securities at FVOCI	-	-	2,925	2,925
Securities at amortised cost	9,643	-	-	9,643
Gross securities	9,643	-	7,769	17,412

25 Financial Risk Management (continued)

25.4 Market Risk (continued)

25.4.3 Maturity and rate sensitivity risk (continued)

The table below summarizes the bank's lending portfolio by interest rate sensitivity.

	Fixed rate	Floating rate	Non-rate sensitive	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019				
Loans:				
Retail	67,429	-	-	67,429
Commercial/corporate	256,437	-	-	256,437
Mortgages	255,364	-	-	255,364
Gross loans	579,230	-	-	579,230
As at October 31, 2018				
Loans:				
Retail	69,875	-	-	69,875
Commercial/corporate	233,943	-	-	233,943
Mortgages	245,001	-	-	245,001
Gross loans	548,819	-	-	548,819

25.4.4 Other price risk

Other price risk arises due to the possibility that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market. The Bank is affected by changing prices of equity instruments designated as fair value through other comprehensive income with fair value movements recognised in other comprehensive income attributable to the Bank.

25 **Financial Risk Management (continued)**

25.5 Currency Risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on positions by currency. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within established limits.

25.5.1 Concentrations of currency risk – financial instruments on and off Statement of Financial Position

Assets are primarily funded by like currency liabilities thus reducing the element of cross-currency risk and in most regional markets, US dollar denominated transactions must be officially sanctioned by the relevant authorities thus reducing exposure. Currency exposure resides mainly in trading activity. The table below summarizes the group's exposure to foreign currency exchange rate risk.

	AWG	USD	EUR	Other	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019					
Assets					
Cash and cash equivalents	150,327	16,029	347	37	166,740
Balances with central bank	73,650	-	-	-	73,650
Loans	521,552	34,544	1	-	556,097
Securities	2,925	5,306	-	-	8,231
Due from associated and affiliated companies	3,878	20,069	0	3,458	27,405
Other assets	1,608	113	-	-	1,721
Total financial assets	753,940	76,061	348	3,495	833,845
Liabilities					
Due to banks	639	-	-	-	639
Customers' deposits	645,601	56,587	1,340	36	703,564
Due to associated and affiliated companies	53	11,093	-	2,139	13,285
Other liabilities	2,087	1,479	8	61	3,635
Total financial liabilities	648,379	69,159	1,348	2,236	721,123
Net statement of financial position	105,561	6,901	(1,000)	1,259	112,722
Credit commitments	46,143	25,213	-	-	71,356

25 Financial Risk Management (continued)

25.5 Currency Risk (continued)

25.5.1 Concentrations of currency risk – financial instruments on and off Statement of Financial Position (continued)

As at October 31, 2018	AWG (AWG '000)	USD (AWG '000)	EUR (AWG '000) (Restated)	Other (AWG '000)	Total (AWG '000)
Assets					
Cash and cash equivalents	204,303	33,394	4,136	138	241,971
Balances with central bank	79,040	-	-	-	79,040
Loans	506,504	26,870	-	-	533,374
Securities	12,568	4,844	-	-	17,412
Due from associated and affiliated companies	9,310	10,840	0	87	20,237
Other assets	1,743	42	-	-	1,785
Total financial assets	813,468	75,990	4,136	225	893,819
Liabilities					
Due to banks	406	-	-	-	406
Customers' deposits	691,326	78,362	4,421	16	774,125
Due to associated and affiliated companies	32	2,499	-	2,503	5,034
Other liabilities	5,492	1,473	8	63	7,036
Total financial liabilities	697,256	82,333	4,429	2,582	786,601
Net statement of financial position	116,211	(6,343)	(293)	(2,357)	107,218
Credit commitments	27,975	21,390	-	-	49,365

25.5.2 Foreign currency exchange risk

Analysis was conducted to determine the sensitivity to reasonable possible movements of select currencies against the AWG to which the Group had significant exposure at October 31 in respect of its assets and liabilities holding all other variables constant. The results revealed that as at October 31, 2019, if the AWG had weakened 10% against the Euro and all other currencies with all other variables held constant, profit before tax for the year would have been AWG 100 thousand lower (2018 – 29 thousand lower) and other components of equity would have been AWG nil million higher (2018 – AWG nil).

25 **Financial Risk Management (continued)**

25.6 Credit Risk

Credit risk is the risk that the bank will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations. The bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Counterparty limits for Corporate and Commercial counterparties are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision. For the retail portfolio the bank has stringent lending criteria which include conservative debt service coverage, loan to value ratios and stability of earnings. These exposures are continuously monitored to identify any change in the credit worthiness of the borrower. The credit quality review process allows the bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

25.6.1 Credit Risk Management

Loans and advances to customers

The bank measures the credit risk of loan and advances to Corporate and Commercial customers and to banks at the counterparty level using an internal risk rating matrix. The ratings are generated by combining weighted financial and statistical criteria with credit officer judgment which is mapped against established internal benchmarks at the time credit is granted. The bank risk rating is seven tiered as shown below and reflects the perceived counterparty risk. This means that, in principle, exposures migrate between levels as the assessment of their riskiness changes. The risk weightings and internal benchmarks are consistently reviewed and upgraded as necessary.

Group's rating	Description of the grade	Credit quality
1	Excellent	High grade
2	Very Good	High grade
3	Good	Standard grade
4	Special Mention	Substandard grade
5	Unacceptable	Past due or impaired
6	Bad and Doubtful	Past due or impaired
7	Virtual Certain Loss	Past due or impaired

25 Financial Risk Management (continued)

25.6 Credit Risk (continued)

25.6.1 Credit Risk Management (continued)

Debt securities

For debt securities external rating such as Standard & Poor's rating or their equivalents are used by Group Risk Management Unit for managing of the credit risk exposures.

25.6.2 Risk limit control and mitigation policies

The bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, industry sector and by country are approved quarterly by the Business Management Operating Committee.

Collateral

The bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advances, which is common practice. The bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- Mortgages over residential properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its periodic review of loan accounts in arrears.

Credit-related commitments

The primary purpose of those instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the bank on behalf of a customer authorizing a third party to draw drafts on the bank up to a stipulated amount under specific terms and conditions – are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

25 Financial Risk Management (continued)

25.6 Credit Risk (continued)

25.6.3 Maximum exposure to credit risk before collateral held or other credit enhancements

	Gross maximum exposure 2019 (AWG '000)	Gross maximum exposure 2018 (AWG '000)
Credit risk exposures relating to on and off balance sheet assets are as follows:		
Due from banks	137,886	121,630
Treasury bills	12,992	100,983
Balances with central bank	73,650	79,040
Loans and advances to customers	579,230	548,819
Securities at FVTPL	5,306	4,844
Securities at FVOCI	2,925	2,925
Securities at amortised cost	-	9,643
Due from associated and affiliated companies	27,405	20,237
Other assets	1,721	1,785
Total	841,115	889,906
Credit risk exposures related to off-Balance sheet financial assets are as follows:		
Contingent liabilities (letter of credit and financial guarantees)	10,079	11,732
Credit commitments	71,356	49,365
Total	81,435	61,097
Total credit risk exposure	922,550	951,003

The above table represents a worst-case scenario of credit risk exposure to the group without taking account of any collateral held or other credit enhancement attached.

25 Financial Risk Management (continued)

25.6 Credit Risk (continued)

25.6.4 Concentration of risk of financial assets with credit risk exposure by industry sectors

The following table breaks down the group's main credit exposure of their carrying amounts, as categorized by industry sectors of counterparties.

	Gross maximum exposure 2019 (AWG '000)	Gross maximum exposure 2018 (AWG '000)
Consumer	322,793	314,876
Manufacturing	1,535	1,362
Distribution	9,308	11,140
Financial services	7,765	4,458
Transport	7,086	7,688
Construction	24,957	32,187
Petroleum	-	-
Real estate	64,004	65,308
Tourism	17,896	15,308
Professional services	24,771	21,407
Utilities	2,926	7,960
Health services	33,505	28,640
Other	62,683	38,485
	579,230	548,819

25.6.5 Risk concentrations of the maximum exposure to credit risk

Concentration of risk is managed by client/counterparty and by industry sector. The maximum credit exposure to any client or counterparty as at October 31, 2019 was AWG 15,171,702 (2018: AWG 19,958,000) before taking account of collateral or other credit enhancements.

25 **Financial Risk Management (continued)**

25.6 **Credit Risk (continued)**

25.6.6 **Credit quality by class of financial assets**

	Stage 1 (AWG '000)	Stage 2 (AWG '000)	Stage 3 (AWG '000)	Total (AWG '000)
As at October 31, 2019				
Treasury bills	12,992	-	-	12,992
Due from banks	137,886	-	-	137,886
Loans:				
Retail	62,710	4,049	671	67,429
Commercial/corporate	209,258	36,224	10,955	256,437
Mortgages	230,165	19,919	5,280	255,364
Other	-	-	-	-
Loans (Gross)	502,132	60,193	16,905	579,230
Securities:				
FVTPL:				
Government	-	-	-	-
Corporate	-	-	-	-
Other	5,306	-	-	5,306
FVOCI:				
Government	-	-	-	-
Corporate	-	-	-	-
Other	2,925	-	-	2,925
Amortised cost:				
Government	-	-	-	-
Corporate	-	-	-	-
Other	-	-	-	-
Securities (Gross)	8,231	-	-	8,231
Total	661,241	60,193	16,905	738,339

25 Financial Risk Management (continued)

25.6 Credit Risk (continued)

25.6.7 Credit quality by class of financial assets (continued)

	Stage 1 (AWG '000)	Stage 2 (AWG '000)	Stage 3 (AWG '000)	Total (AWG '000)
As at October 31, 2018				
Treasury bills	100,983	-	-	100,983
Due from banks	121,630	-	-	121,630
Loans:				
Retail	64,229	4,864	782	69,875
Commercial/corporate	179,624	40,968	13,351	233,943
Mortgages	212,570	24,071	8,360	245,001
Other	-	-	-	-
Loans (Gross)	456,423	69,903	22,493	548,819
Securities:				
FVTPL:				
Government	-	-	-	-
Corporate	-	-	-	-
Other	4,844	-	-	4,844
FVOCI:				
Government	-	-	-	-
Corporate	-	-	-	-
Other	2,925	-	-	2,925
At amortised cost:				
Government	9,643	-	-	9,643
Corporate	-	-	-	-
Other	-	-	-	-
Securities (Gross)	17,412	-	-	17,412
Total	696,448	69,903	22,493	788,844

For those exposures that are neither past due nor impaired the majority are rated between standard (good) to excellent which is high grade.

25 **Financial Risk Management (continued)**

25.6 **Credit Risk (continued)**

25.6.7 Aging analysis of Stage 2 by sector

	Less than 1 mth (AWG '000)	1-3 mths (AWG '000)	Total (AWG '000)
As at October 31, 2019			
Loans:			
Retail	3,111	939	4,049
Commercial/corporate	14,045	22,179	36,224
Mortgages	14,656	5,263	19,919
	31,812	28,381	60,193

	Less than 1 mth	1-3 mths	Total
As at October 31, 2018			
Loans:			
Retail	4,324	540	4,864
Commercial/corporate	34,740	6,228	40,968
Mortgages	21,088	2,983	24,071
	60,152	9,751	69,903

25 Financial Risk Management (continued)

25.6 Credit Risk (continued)

25.6.8 Credit risk exposure on due from banks, debt securities and other bills based on the Group's internal corporate rating system

The table below presents an analysis of debt securities, treasury bills and other eligible bills by internal and equivalent rating agency designation.

	Standard & Poor's equivalent grades	2019 Total (AWG '000)	2018 Total (AWG '000)
Excellent	BB+ and higher	156,184	237,100
		156,184	237,100

25.6.9 Repossessed collateral

Repossessed collateral are sold as soon as practicable, with the proceeds used to reduce the outstanding indebtedness.

25 Financial Risk Management (continued)

25.7 Capital management

Capital management is a proactive process that ensures that the bank has and remains able to generate or raise sufficient capital on a timely and cost-effective basis to underpin its risks and ultimately protect depositors and other creditors from unexpected losses.

Capital adequacy and the use of regulatory capital are monitored by the Group's management, based on an internal risk assessment approach employing techniques based on the guidelines developed by the Basel Committee on Banking Supervision as implemented by the local banking regulators of the various territories in which the Group operates.

The Bank is governed by the risk based capital targets set by the Central Bank of Aruba, and are required to calculate capital ratios and capital-to-risk adjusted assets multiples using the framework adopted by the Central Bank of Aruba. Under the local guidelines, adjusted qualifying capital includes core capital and supplementary capital. Core capital mainly consists of fully paid and issued share capital, audited retained earnings, statutory reserve fund, capital reserves excluding asset revaluation reserves less goodwill. Supplementary capital includes subordinated debt, asset revaluation reserves and unaudited profits. Regulatory capital ratios are calculated by dividing core capital by risk-weighted assets and qualifying capital by risk adjusted assets. The required information is filed with the authorities on a monthly or quarterly basis as prescribed by the regulator.

25 Financial Risk Management (continued)

25.7 Capital management (continued)

The table below summarizes the composition of regulatory capital and the ratios of the bank for the years ended October 31.

	2019	2018
	(AWG '000)	(AWG '000)
Tier 1 capital		
Share capital (net of treasury shares)	44,865	44,865
Statutory reserve	16,699	16,049
Retained earnings	68,175	84,029
Less: goodwill	-	(23,654)
Total qualifying Tier 1 capital	129,739	121,289
Tier 2 capital		
Other components of equity	1,866	1,866
Total qualifying Tier 2 capital	1,866	1,866
Total regulatory capital	131,605	123,155
Risk-weighted assets:		
Risk weighted assets for credit risk	491,967	506,305
Total risk-weighted assets	491,967	506,305
Total regulatory capital to risk weighted assets	27%	24%

The licensed banking entity in Aruba is required to maintain a qualifying capital ratio of at least 16%. Throughout the current year and prior year, the individual licensed entity complied with all of the externally imposed capital requirements to which the entity is subject.

26 Fair value of financial assets and liabilities

Disclosures of fair value for financial instruments that are carried at amortised cost

The following fair value hierarchy table presents fair values of financial assets and liabilities that are carried at amortised cost, and therefore excludes financial instruments that are measured and disclosed at fair value on a recurring basis.

Financial assets and liabilities for which fair value are disclosed

	Fair value always approximates carrying value	Fair value may not approximate carrying value	Total Fair value
	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019			
Cash equivalents	137,886	-	137,886
Securities	-	-	-
Loans	-	556,097	556,097
Other assets	1,721	-	1,721
Due to banks	-	639	639
Customers' deposits	385,258	318,306	703,564
Other liabilities	3,636	-	3,636

	Level 1	Level 2	Level 3	Total
As at October 31, 2019				
Cash equivalents	-	137,886	-	137,886
Securities	-	-	-	-
Loans	-	-	556,097	556,097
Other assets	-	-	1,721	1,721
Due to banks	-	-	639	639
Customers' deposits	-	-	703,564	703,564
Other liabilities	-	-	3,636	3,636

26 Fair value of financial assets and liabilities (continued)

Financial assets and liabilities for which fair value are disclosed (continued)

	Fair value always approximates carrying value	Fair value may not approximate carrying value	Total Fair value
	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2018			
Cash equivalents	121,630	-	121,630
Securities	-	9,693	9,693
Loans	-	533,374	533,374
Other assets	1,785	-	1,785
Due to banks	-	406	406
Customers' deposits	440,979	333,145	774,125
Other liabilities	7,036	-	7,036

	Level 1	Level 2	Level 3	Total
As at October 31, 2018				
Cash equivalents	-	121,630	-	121,630
Securities	-	9,693	-	9,693
Loans	-	-	533,374	533,374
Other assets	-	-	1,785	1,785
Due to banks	-	-	406	406
Customers' deposits	-	-	774,125	774,125
Other liabilities	-	-	7,036	7,036

26 Fair value of financial assets and liabilities (continued)

Financial assets and liabilities for which fair value are disclosed (continued)

Carrying amounts of certain financial instruments approximate their fair values due to short-term nature and generally insignificant credit risk of the instruments: (i) loans and deposits with original maturity of less than three months or payable on demand; and (ii) certain receivables and payables in Other assets and Other liabilities.

<u>Valuation techniques and assumptions applied for the purposes of measuring fair value</u>

The fair values of financial assets and financial liabilities are determined as follows:

- The fair values of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices (includes listed redeemable notes, bills of exchange, debentures and perpetual notes).
- The fair values of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments. Loans and advances to customers are similarly valued taking into account credit portfolio experience. The valuation model is reviewed on an annual basis and updated as necessary to reflect portfolio experience.

Disclosures of fair value for financial instruments that are measured and disclosed at fair value

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.

- Level 2 fair value measurements are those derived from 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).

- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

26 Fair value of financial assets and liabilities (continued)

Valuation techniques and assumptions applied for the purposes of measuring fair value (continued)

As at October 31, 2019	Level 1	Level 2	Level 3	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
Cash equivalents at FVOCI	-	12,992	-	12,992
Securities at FVTPL				
Securities FVTPL classified				
Government and state owned enterprises debt securities	-	-	-	-
Money market instruments	5,306	-	-	5,306
	5,306	-	-	5,306
Securities FVTPL designated				
Corporate debt securities	-	-	-	-
Money market instruments	-	-	-	-
	5,306	-	-	5,306
Securities FVOCI				
Securities FVOCI classified				
Treasury bills and treasury notes	-	-	-	-
Government and state owned enterprises debt securities	-	-	-	-
Corporate debt securities	-	-	-	-
Other debt securities	-	-	-	-
Equity securities	-	-	-	-
	-	-	-	-
Securities FVOCI designated				
Treasury bills and treasury notes	-	-	-	-
Government and state owned enterprises debt securities	-	-	-	-
Corporate debt securities	-	-	-	-
Other debt securities	-	-	-	-
Equity securities	-	-	2,925	2,925
	-	-	2,925	2,925
	-	-	2,925	2,925
Total investments	5,306	12,992	2,925	21,223

26 Fair value of financial assets and liabilities (continued)

26 Fair value of financial assets and liabilities (continued)

Valuation techniques and assumptions applied for the purposes of measuring fair value (continued)

As at October 31, 2018	Level 1	Level 2	Level 3	Total
	(AWG '000)	(AWG '000)	(AWG '000)	(AWG '000)
Cash equivalents at FVOCI	100,983	-	-	100,983
Securities at FVTPL				
Securities FVTPL classified				
Government and state owned enterprises debt securities	-	-	-	-
Money market instruments	4,844	-	-	4,844
	4,844	-	-	4,844
Securities FVTPL designated				
Corporate debt securities	-	-	-	-
Money market instruments	-	-	-	-
	4,844	-	-	4,844
Securities FVOCI				
Securities FVOCI classified				
Treasury bills and treasury notes	-	-	-	-
Government and state owned enterprises debt securities	-	-	-	-
Corporate debt securities	-	-	-	-
Other debt securities	-	-	-	-
Equity securities	-	-	-	-
	-	-	-	-
Securities FVOCI designated				
Treasury bills and treasury notes	-	-	-	-
Government and state owned enterprises debt securities	-	-	-	-
Corporate debt securities	-	-	-	-
Other debt securities	-	-	-	-
Equity securities	-	-	2,925	2,925
	-	-	2,925	2,925
	-	-	2,925	2,925
Total investments	105,827	-	2,925	108,752

There were no transfers during 2019 and there were transfers from level 3 to level 1 in 2018.

26 **Fair value of financial assets and liabilities (continued)**

Positive and negative fair value movement of Level 3 financial instruments from using reasonably possible alternative assumptions

A financial instrument is classified as Level 3 in the fair value hierarchy if one or more of its unobservable inputs may significantly affect the measurement of its fair value. In preparing the financial statements, appropriate levels for these unobservable input parameters are chosen so that they are consistent with prevailing market evidence or management judgment. Due to the unobservable nature of the prices or rates, there may be uncertainty about valuation of these Level 3 financial instruments.

The following table summarizes the impact to fair values of Level 3 financial instruments using reasonably possible alternative assumptions. This sensitivity disclosure is intended to illustrate the potential impact of the relative uncertainty in the fair value of Level 3 financial instruments. In reporting the sensitivities below, we have considered offsetting balances in instances when: (i) the move in valuation factor caused an offsetting positive and negative fair value movement, (ii) both offsetting instruments are in Level 3, and (iii) when exposures are managed and reported on a net basis. With respect to overall sensitivity, it is unlikely in practice that all reasonably possible alternative assumptions would be simultaneously realized.

	Level 3 Fair value	Positive fair value movement from using reasonably possible alternatives	Negative fair value movement from using reasonably possible alternatives
	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2019			
Securities at FVTPL	-	-	-
Securities at FVOCI	2,925	371	(498)
	2,925	371	(498)

26 Fair value of financial assets and liabilities (continued)

Positive and negative fair value movement of Level 3 financial instruments from using reasonably possible alternative assumptions (continued)

	Level 3 Fair value	Positive fair value movement from using reasonably possible alternatives	Negative fair value movement from using reasonably possible alternatives
	(AWG '000)	(AWG '000)	(AWG '000)
As at October 31, 2018			
Securities at FVOCI	2,925	143	(358)
	2,925	143	(358)

Sensitivity results

As at October 31, 2019, the effects of applying other reasonably possible alternative assumptions to the Level 3 asset positions would be an increase of AWG 371 thousand and a reduction of AWG 498 thousand in fair value, of which AWG 371 thousand and AWG 498 thousand would be recorded in other components of equity, respectively. The effects of applying these assumptions to the Level 3 liability positions would result in a decrease of nil and an increase of nil in fair value as there are no liability positions.

Level 3 valuation inputs and approaches to developing reasonably possible alternative assumptions

The following is a summary of the unobservable inputs of the Level 3 instruments and our approaches to develop reasonably possible alternative assumptions used to determine sensitivity.

Financial assets or liabilities	Sensitivity methodology
Government debt and corporate debt	• Sensitivities are determined based on adjusting, plus or minus 20 bps shift in the yield curve.
Money market instruments	• Those are typically Level 1 instruments with daily NAV available. So there is no sensitivity.
Equity securities	• For private equities, sensitivities are derived from valuation range. When the fair value is kept at historical nominal value or there is no valuation range, zero sensitivity is assigned since there are no alternative assumptions.

26 **Fair value of financial assets and liabilities (continued)**

Reconciliation of Level 3 fair value measurements of financial assets

	FVTPL	FVOCI	Total
	(AWG '000)	(AWG '000)	(AWG '000)
As at November 1, 2018	-	2,925	2,925
Additions	-	-	-
Disposal (sale and redemption)	-	-	-
Gains / (losses) from changes in fair value	-	0	0
Transfer from Level 3	-	-	-
As at October 31, 2019	-	2,925	2,925

	FVTPL	FVOCI	Total
	(AWG '000)	(AWG '000)	(AWG '000)
As at November 1, 2017	5,140	4,170	9,310
Additions	-	-	-
Disposal (sale and redemption)	-	-	-
Gains / (losses) from changes in fair value	(296)	315	19
Transfer from Level 3	(4,844)	(1,560)	(6,403)
As at October 31, 2018	(0)	2,925	2,925

There were no transfers out of level 3 during 2019 and there were transfers out of level 3 during 2018.

Financial assets classified as fair value through profit or loss
For our financial assets classified as FVTPL, we measure the change in fair value attributable to changes in credit risk as the difference between the total change in the fair value of the instrument during the period and the change in fair value calculated using the appropriate risk-free yield curves.

There were no significant changes in the fair value of the financial assets classified as FVTPL attributable to changes in credit risk during the year ended October 31, 2019, and cumulatively since initial recognition of the assets.

Net gains (losses) from financial instruments classified as fair value through profit or loss
Financial instruments classified as at FVTPL, which includes mainly trading securities are measured at fair value with realized and unrealized gains and losses recognized in Non-interest income, primarily in Trading revenue.