MALTA DEVELOPMENT BANK
ANNUAL REPORT
& FINANCIAL STATEMENTS
2022

MDB 5 YEARS

BANK MALTI GĦALL-IŻVILUPP

MALTA DEVELOPMENT BANK

CONTENTS

ABOUT THE MALTA DEVELOPMENT BANK

The Malta Development Bank (MDB) was established by virtue of the Malta Development Bank Act which was passed by Parliament in May 2017 and came into force in November 2017. On 11 December 2017, the Minister for Finance, the Hon Prof Edward Scicluna, appointed the members of the Board of Directors and the Supervisory Board of the MDB. On the same day, the Board of Directors held their first meeting and the Bank officially commenced operations.

The MDB's strategic objective is to address market failures or financial gaps by offering financing facilities to support productive and viable operations where the market is unable or unwilling to accommodate such activities on its own in whole or part.

The MDB complements commercial banks through a non-competitive and mutually supportive relationship, thereby ensuring additionality and diversifying Malta's financial base in a cost-effective manner.

MDB's primary goal is to contribute to public policy objectives and it is therefore not driven by purely commercial and profit maximisation considerations. Nonetheless, the MDB supports only bankable investments and assesses proposals on the basis of sound banking principles, including feasibility.

In performing its promotional banking role, MDB's remit of activities covers a wide range of possible operations where there is evidence of market failure. In general terms, the MDB is engaged in the following priority areas:

- **Private Sector Development**, in particular financing the private sector through innovative financing, credit enhancement, venture capital, and advisory functions;;
- **Skills and Technology**, in particular sustaining competitiveness by investment in innovation, skills, knowledge-generation and technology;
- **Infrastructure development** of regional or national importance;
- **Green Economy**, in particular supporting clean energy and energy efficiency projects, sustainable transport, and water resources;
- **Community Services**, in particular supporting social enterprises operating community services in such sectors as education, health and housing.

OUR VISION

To make a significant contribution towards sustainable economic development by promoting inclusive and environmentally sustainable economic growth and infrastructure development.

OUR MISSION

To contribute towards sustainable economic development that benefits Maltese society in line with public policy objectives by:

- promoting inclusive and environmentally sustainable economic growth
- supporting infrastructure development
- linking entrepreneurship, investment and economic growth to improve living conditions, ensure a higher quality of life, and encourages social inclusion.

BOARD OF DIRECTORS

In exercise of the powers conferred by Article 21 of the Malta Development Bank Act, the Minister responsible for the MDB appoints the Bank's Directors. As at end 2022 the Board is composed of:

Chairperson
Prof. Josef Bonnici

Directors
Prof. Rose Mary Azzopardi
Dr Michele Cardinali
Mr Steve Ellul [1]
Mr William Spiteri Bailey[2]
Mr Anthony Valvo
Prof. Philip von Brockdorff[3]

These appointments are valid for the periods stipulated in article 21(4), (5) and (6) of the Act.
Dr Bernadette Muscat, the Bank's Chief Legal and Compliance Officer, serves as the Secretary of the Board.

1 Mr Steve Ellul was appointed on 22 June 2022 in lieu of the late Mr Paul Cardona.

2 Mr William Spiteri Bailey was appointed in replacement of Ms Jackie Camilleri on 20 December 2022.

3 Prof. Philip von Brockdorff was appointed on 25 February 2022 in lieu of Mr Robert Borg.

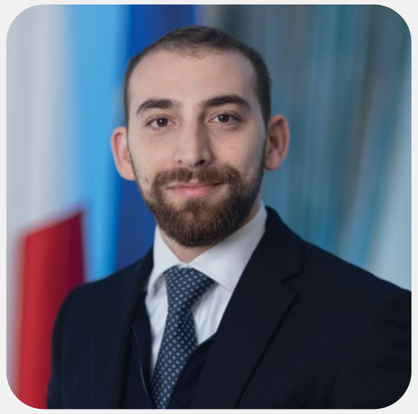
Prof. Josef Bonnici

Dr Bernadette Muscat

Prof. Rose Mary Azzopardi

Prof. Philip von Brockdorff

Mr Anthony Valvo



Dr Michele Cardinali

Mr Steve Ellul

Mr William Spiteri Bailey

LETTER OF TRANSMITTAL

Malta Development Bank

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info@mdb.org.mt
https://mdb.org.mt/

17 April 2023

The Hon. Clyde Caruana B.Com (Hons), MA (Econ.), MP
Minister for Finance and Employment
Maison Demandols
South Street
Valletta VLT 2000

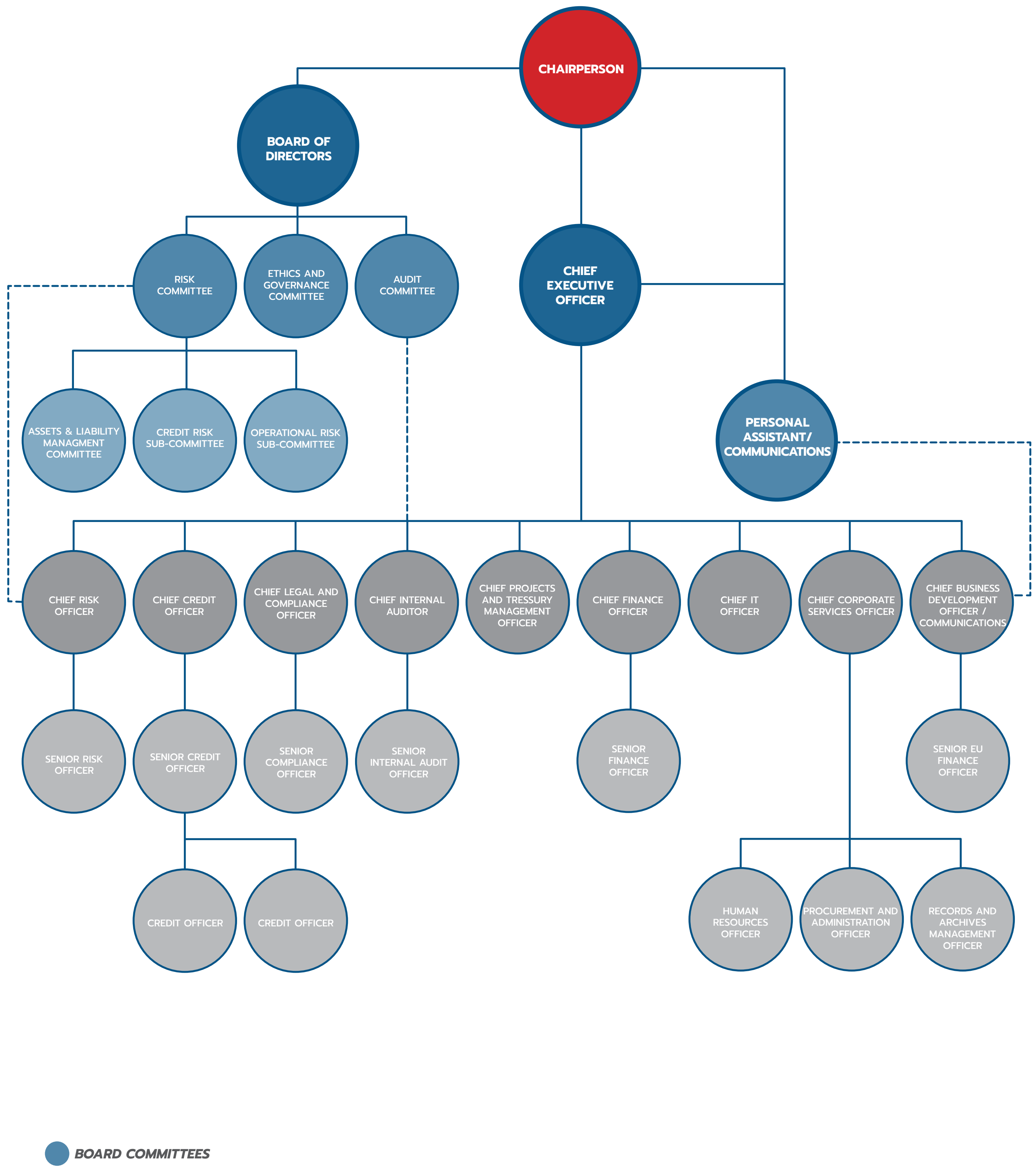
Dear Minister,

In terms of article 33 of the Malta Development Bank Act, 2017 (Cap 574), I have the honour to transmit to you a copy of the Annual Report of the Malta Development Bank for the year 2022.

In terms of article 33 of the Malta Development Bank Act, I am also transmitting a copy of the audited accounts of the Bank for the financial year ended 31 December 2022.

Yours sincerely

JOSEF BONNICI
Chairperson



CHAIRPERSON'S **STATEMENT**

Following the international economic and financial crisis and the resultant sovereign debt crisis roughly a decade ago, national promotional banks gained increasing importance at the European level as anti-cyclical agents. They helped stimulate economic recovery and acted as facilitators of the transition away from grant-dependency in the absorption of EU funding. At the time, in my role of Governor of the Central Bank of Malta, I had highlighted that there was a glaring institutional gap in the financial system in Malta and that there was a dire need for Malta to have its own national promotional bank which would bridge market gaps while supporting enterprise into the next decade of growth. I had stressed that such a new institution would play a major role as a key partner in making smarter use of public resources through its institutional and operational capacity to provide promotional financial instruments and unlock private investment.

Although the idea was at first met with a mixed reaction, perhaps given the healthy state of Malta's financial and banking sector, extensive preparatory research and consultation, involving a wide range of stakeholders eventually led to the birth of the Malta Development Bank some five years ago, a concept that was, by this time, embraced across the board. The project also achieved political consensus, as witnessed by the unanimous vote in Parliament in May 2017 approving the legislation that put Malta's first-ever national promotional bank in place.

Five years down the line, the Malta Development Bank has firmly established itself as an important economic stakeholder, positively contributing to the performance of Malta's businesses and their employees. In such a short timeframe, it has achieved international recognition among its peers and is considered as an important tool in the array of resources available to the government in its efforts to support economic growth. We have also grown sustainably in terms of our human resource base as more qualified professionals joined our ranks.

During the year in review, we have also completed our move to a newly refurbished historical building in Floriana which is more consonant to our requirements as we seek to achieve our objectives in the years ahead.

The Malta Development Bank was founded and remains attached to the strategic objective of filling market gaps by offering financing facilities where the market fails to do so. However, five years ago no one was aware how opportune the Bank's creation had been at the time, given the series of global unfavourable events that followed.

As we gradually put in place our first financing programmes, the world was propelled into one crisis after another. A once-in-a-century pandemic in 2020 uprooted normality as we knew it, pushing the world into an unprecedented economic and social crisis, putting millions of people out of their jobs and changing the economic landscape in a drastic way. As global economies started to recover from this severe disruption, high energy prices, increasing realisations of a climate catastrophe and continued supply-side disruptions fed into strong inflationary pressures which central banks around the globe sought to control through a tighter monetary policy. Furthermore, we are now well into a year of the Russian invasion into Ukraine which disrupted the supply chains of several key commodities and accentuated the inflationary spiral, with inevitable effects on global investment as soaring borrowing costs heap pressure on the economy. As a result, major economic and financial institutions are expecting growth to remain weak by historical standards, as increasing sanctions against Russia and efforts to diversify our energy sources take their toll.

Despite this turbulent context, the Maltese economy handled the past year relatively well, particularly as a result of strong net exports and recovering private consumption. Growth remained high while unemployment remained at historically low levels. Inflationary pressures have increased but remained among the lowest in the euro area, mostly due to energy subsidies provided by Government.

The MDB is proud to have been an important contributor in facilitating this recovery through its COVID-19 Guarantee Scheme (CGS). Cumulatively, the nine partnering commercial banks which participated in the CGS have sanctioned close to €500 million in working capital loans. Overall, 600 businesses, that collectively employ around 40,000 persons, were supported under the CGS. The beneficiaries range from hotels to large retail outlets, but also to many smaller firms from across the economic spectrum. Official data has clearly shown that loans to non-financial corporations in Malta would have fallen without the MDB's CGS scheme.

Throughout 2022, MDB personnel worked relentlessly on developing new financing programmes supporting the nation's policy objectives going forward. At the same time, it was cognisant that the ongoing war in Ukraine, the associated economic sanctions and political uncertainty have created significant challenges for businesses, making it more difficult for them to operate and invest.

Once more the MDB was called upon to respond countercyclically and help safeguard the Maltese economy. The Bank was again entrusted with a government guarantee and over a period of a few weeks, we launched a package of support measures in response to the economic challenges related to the war in Ukraine. The first measure was launched in May and sought to ensure the security of supply of grains, animal feeds and related products of strategic importance by assisting importers and wholesalers through the provision of urgent temporary liquidity support. Subsequently we also launched two other measures, one directed towards fuel and oil importers and the other one aimed at all business sectors. This package was designed to ensure access to bank financing to undertakings whose cashflow was adversely impacted by the disruptions in supply chains and other pressures brought about by the war.

While dedicating the necessary resources and efforts to quickly react to the economic challenges in the context of the Ukraine war, concurrently we continued to deliver on our plan to support Malta's economic recovery and regeneration. Strategic planning and smart investment in our resources and capacity over recent years have enabled us to respond swiftly to the economic ramifications of the war without derailing our efforts in supporting new investment. Indeed, we delivered on both fronts. This year we introduced seven new programmes. Besides the mentioned three Ukraine crises support schemes, we launched two new flagship schemes offering favourable financing terms and rates for new investment by Maltese SMEs as well as one scheme to support students and a sub-scheme in collaboration with the Malta Council for Science and Technology (MCST) to support innovative start-ups.

As the economy continued to demonstrate resilience throughout the year, we launched our two flagship schemes to support new SME investment, namely the SME Guarantee Scheme and the Guaranteed Co-lending Scheme. Both schemes are tailored to the specific circumstances of local business and prioritise those investment projects that contribute to a greener and more digitally oriented economy, in line with the key objectives of both the Government and the European Union. The investment gap in attaining the ambitious EU's climate targets is substantial, and the unlocking of private capital is critical in narrowing this gap. Our schemes are effective in providing the mechanism to mobilise private investment through risk mitigation and are consistent with MDB's objective to improve access to finance and to diversify the financing options to SMEs.

The Guaranteed Co-Lending Scheme is particularly innovative, even by European standards, as it introduces a new scheme of co-financing with commercial banks, blended with a partial guarantee of 60% that can address the financing needs of larger projects up to €10 million. Projects that may be considered by a commercial bank as too large or too risky - especially those investments in intangibles related to technology and digitalisation - with the involvement of the MDB such projects can be assisted with the appropriate financing solution. In this way, this scheme will help in catalysing the syndicated loan market in Malta and act as an instrument to crowd-in the participation of commercial banks in supporting bankable projects.

We are determined to magnify the outreach of MDB's promotional role by collaborating with multiple credit institutions to stimulate more active SME lending in Malta by offering the opportunity for commercial banks to act as our intermediary partners. Indeed, it is encouraging to see strong interest by banks, and we are pleased to have four of the main commercial banks in Malta expressing their interest and being accredited to act as intermediary partners of the MDB.

Together, these two new schemes can facilitate up to €180 million of new investment in the Maltese economy. Furthermore, in collaboration with MCST, through the Go-to-Market scheme, part of the portfolio is specifically allocated to start-ups willing to commercialise their technological and innovative ideas.

During 2022, the MDB also worked closely with the Managing Authority for EU Funds in connection with the Bank's role as a vehicle for leveraging EU Structural Funds. This has led to the follow-up of the hugely popular FSMA scheme by an extended FSMA Plus Scheme through which more than 430 young people and senior alumni have been able to continue their studies through €15 million financing from these MDB Schemes. I am delighted to see students from every background being able to access higher-level courses irrespective of their financial capabilities.

Despite this very active year in terms of putting in place new financing programmes, the MDB team has been very active behind the scenes in strengthening itself to meet the requirements of managing such high-level portfolios, particularly as we sought the support of the European Investment Fund (EIF) by way of risk sharing instruments under the Pan-European Guarantee Fund (EGF). We are currently taking this forward by seeking to achieve the status of becoming a direct implementing partner of the InvestEU. As Malta's promotional bank, it is our objective to act as Malta's gateway to EU financial instruments that enable greater risk sharing and a magnified transfer of benefit to Maltese businesses.

We have also been attentive in strengthening our governance structures and ensuring that the principles we seek to promote in our community are respected in our own operations as well. As a particular example, I am very fond of our staff's efforts to undertake a genuine ESG journey. To this end, the Bank is committed to develop an ESG Strategy by the end of 2023. This strategy is of a dual nature: one aspect shall focus externally on a review of guidelines covering credit and risk assessments of the Bank's promotional schemes which shall be finetuned to give more accent to ESG considerations; the other aspect concerns the way we work, focusing on internal measures aiming to embrace ESG principles, including in the way we manage our building, our waste management efforts and in ensuring equality at all levels of our operations.

It is also with great satisfaction to report that, despite the difficult operating environment that characterised the economy and financial sector in recent years, the Bank has continued to strengthen its financial performance, and for the first time generated an operating profit while the risk profile in the Bank's portfolio remained low and stable. This is the result of prudent operations based on appropriate financial practices in line with sound banking principles.

Looking ahead, the Bank will continue to strive to achieve a balance between sustainable profitability and growth against the appropriate risk levels by making sound business decisions and lend or invest funds in projects that are consistent with Malta's development objectives.

I would like to express my gratitude to the Ministry for Finance and Employment for supporting the Bank, and in particular for strengthening its capital base by an additional €20 million injection, to reach €80 million. This will enhance the Bank's risk absorption capacity to continue supporting sustainable growth by driving competition, enabling innovation, and improving access to finance.

In conclusion, I would like to thank the Board of Directors and members of staff that have contributed to the successes achieved throughout our first five years of operation, while saluting the memory of those that are no longer with us.

I look forward to continuing building on these achievements in the year ahead as we continue to help Maltese businesses charter the way for growth.

JOSEF BONNICI
Chairperson

CEO'S **STATEMENT**

It is my pleasure to introduce this report for the first time as Chief Executive Officer of the Malta Development Bank.

I became involved with the Bank back in 2015 when I was a member of the working committee tasked by the then Deputy Prime Minister, the Hon. Louis Grech, with the detailed planning of a new development bank and with preparing a draft Bill for consideration by Government.

The setting up of this working committee followed a paper prepared by the Central Bank of Malta on the benefits which such a development bank can contribute to the Maltese economy. A study was commissioned to identify more clearly the financial gaps which had to be addressed and the estimated size of the gaps. Links were formed with foreign development banks for us to understand better what was going on in other EU member states. The European Commission was eventually approached to set a remit for the Malta Development Bank which came into existence by Act of Parliament in 2017.

I joined the Bank at the beginning of 2020 as Deputy to the then Chief Executive Officer, Mr Rene Saliba. Mr Saliba was instrumental, along with Prof. Josef Bonnici, the current Chairman, in setting up the Bank and putting in practice the plans of the working committee and the requirements of the MDB Act (Act XXI of 2017). Chief Officers in various functional areas were recruited, an organisational framework drafted, the first business policies developed, formal links with international associations of promotional banks established, an IT system put in place, and an informative website published.

Fortuitously, but fortunately, the MDB was already a well-functioning institution when the world was struck by COVID-19 in 2020 and global economies practically ground to a halt. While we worked from the Central Bank Annex on the schemes requested by Government to provide urgent liquidity to local businesses via local banks, outside of our office we could see a Valletta swiftly voided of people and commerce.

Half a decade might be just a blip in history. Yet, a look back at where we came from and what has been achieved so far and under which circumstances, renders us both proud and humble at the same time. The numbers we have managed to produce in such a short period are tangible evidence of the positive impact that the Bank succeeded in exerting on Malta's economic development in recent years.

The COVID-19 pandemic, and more recently the war in Ukraine, starkly demonstrated the need to have promotional banks in place so that they can speedily act counter-cyclically to mitigate the adverse impacts of the prevailing economic cycle. Malta was no exception.

The MDB was the instrument which enabled the Government to unlock more than half a billion euro in commercial bank liquidity and achieve the benefits of financial leverage. This was an excellent demonstration of the benefits of having a national promotional bank equipped with the insititutional and operational capacity to support the economy, with Government support. Suffice to say that during these five years, the MDB reached over 700 businesses which employ some 40,000 persons, and more than 400 students, facilitating €580 million in favourable financing.

Throughout this period, we have been guided by our strategic objectives, namely filling SMEs financing gaps, supporting infrastructural development, being active in closing social gaps, promoting the adequate financing of horizontal sectors, such as digitalisation and green initiatives, acting countercyclically and supporting the country's financial stability. These initiatives form the profile of the MDB in the local economy. A young profile, though a useful and effective one.

Change being the only constant, we are conscious of the changing needs of our dynamic economy and its stakeholders, and hence we periodically scan the market to ensure that changing circumstances are being monitored and analysed so that our role remains both effective and efficient. This is why we consider communication with our stakeholders as paramount.

In this respect, we strive to maintain a constant flow of discussion with commercial banks, business representatives, as well as governmental entities and institutions, to better understand the needs of the market and society so that we can tailor our product offering to meet Malta's economic priorities.

For an organisation such as the MDB, it is of little use working in the dark. We therefore participate in several public events so that our officials engage with other stakeholders and promote and share information related to our products to the benefit of all. To do so, we have also significantly enhanced our media presence, on both traditional and social media outlets, such as LinkedIn. Our website at mdb.org.mt is kept constantly updated with news about our organisation, including new schemes and products.

As to economic impact, in aggregate the MDB currently contributes around 13% of all the banking system's outstanding loans to Maltese businesses.

The most visible impact was during the COVID-19 pandemic where the aggregate volume of business loans by the banking system in Malta increased by 9%. In the absence of MDB's support, such loans to businesses would have decreased by 2.5%.

We have made a difference in maintaining economic stability while protecting social stability by ensuring that as much as possible jobs were not lost. And we did this sustainably by using the massive guarantee provided by Government to leverage commercial bank liquidity. Due to the pace of the post-pandemic recovery and the way we designed our scheme we have so far had negligible borrower defaults. This means that Maltese businesses managed to leap over the pandemic without imposing a burden on the taxpayer. It is indeed a demonstration of the "doing-more-with-less" principle.

Much to our heart, are the two student schemes. The first scheme, Further Studies Made Affordable, was extended to a second one, Further Studies Made Affordable Plus. Supported by funding from the European Social Fund which the Managing Authority allocated to the Bank, we devised these schemes and operate them through Bank of Valletta.

These study schemes are the princes of equal opportunity. They make it possible for students to study any subject anywhere in the world irrespective whether they or their families have the required resources. And students do not have to worry about early repayment, collateral, or high interest rates. So far, €15 million in loans have been made to around 430 students.

I am also very proud of the international stature this Bank has achieved during this timeframe. We have accomplished a lot over the past two years in terms of our relationship with international institutions.

Back in 2021, we focused our efforts, given our limited resources, to access the support made available by the European Investment Fund (EIF) by way of risk-sharing instruments under the Pan-European Guarantee Fund (EGF). After months of negotiations, due diligence and consultations, towards the end of that year, the Bank signed two agreements with the EIF: a direct guarantee agreement and a counter-guarantee agreement.

With the support of the EGF guarantees, we were able to offer, for the first time, uncapped portfolio guarantees to commercial banks. This meant a higher degree of capital relief for the commercial banks and thus a higher transfer of benefit to SMEs. It was indeed an important step in our product offering that better reflects the underlying reality of our economy and financial market.

With the EGF guarantee expiring prematurely in December 2022, by the end of the year in review we applied for a mix of direct and counter-guarantees under the InvestEU guarantee products being provided by the EIF, specifically under the SME Competitiveness, Innovation and Digitalisation, and Sustainability classes. Through this approach, the MDB plans to substitute the EGF guarantee by mobilising the InvestEU guarantee via the EIF. Concurrently we are proceeding with the ambitious process of eventually becoming a direct implementing partner of InvestEU.

In order to be accredited as a direct implementing partner of InvestEU, the Bank had to make, and continues to make, a significant investment in our governance and financial management structure in order to be able to demonstrate that the Bank is able to provide a high level of protection to EU funds. Accreditation is via what is known as a Pillar Assessment. This means that the Bank would need to meet the very high standards set by the European Commission related to internal control systems, the accounting system, and other aspects including anti-money laundering, tax avoidance, data protection, credit risk management and risk governance. Basically, the Pillar Assessment is a comprehensive battery of tests covering all governance and management areas of MDB to ensure that the Bank is a top-class EU development bank.

Throughout 2022, together with an external auditor, we have worked assiduously towards this objective, which we plan to finalise by the second quarter of 2023. We remain steadfast in our bid to ensure that the process will be finalised in time for the second call for expression of interest for direct implementing partners foreseen to be issued by the European Commission in 2024. This process is of national importance as we aim to become Malta's gateway for InvestEU resources. We are working to ensure that this risk-sharing capacity is translated into enhanced benefits to Maltese businesses.

We have also worked hard to increase our capacity building through exchanges with our international partners. This gives us access to a wealth of experience that can be adapted and optimised to Malta's needs. Over the past year, the MDB has solidified its relationship with fellow EU promotional banks, enabling the exchange of best practices and the reciprocal transfer of knowledge.

In recognition of the role that the Bank enjoys within the community of European promotional banks, during the year in review, Malta was chosen to host the annual General Assembly of the European Long-Term Investors Association (ELTI), helping to put the Bank in a more prominent place on the European banking map.

Besides ELTI, the MDB is also a member of the European Association of Public Banks (EAPB), the Network of European Financial Institutions for SMEs (NEFI) and the European Association of Guarantee Institutions (AECM).

For the MDB, membership of such associations provides an excellent opportunity to exchange views with technical experts working within much larger institutions and to benefit from other promotional banks' experience as it seeks to fine-tune its product offering.

Importantly, these associations also provide us with a vehicle to participate in common positions when communicating with the institutions of the European Union and the possibility of exchanging views with other promotional banks and international financial institutions such as the European Investment Bank and Council of Europe Development Bank.

On the local front, during 2022 we moved our offices from the small Central Bank Annex on Pope Pius V Street in Valletta to a much larger building at 5, Market Street, Floriana. This move was necessitated by increasing staff numbers. A historic building in Market Street was thoroughly refurbished and brought to the highest health and safety standards providing a pleasant environment to our professional staff. Most of the work was carried out during the pandemic years, supervised in detail by our own staff who managed to transform an old building into a modern, airy, comfortable set of offices.

It was therefore a great honour and pleasure for our directors, management and staff that the Prime Minister, the Hon. Dr. Robert Abela, inaugurated the new Market Street offices on 23rd November 2023, in what is a historic occasion for the Bank.

The MDB is supervised by a Supervisory Board set up under the MDB Act. The Supervisory Board, chaired by Mr John Cassar White, has independent members as well as representatives of the Ministry of Finance, the Central Bank and the Malta Financial Services Authority. The Bank maintains an open and transparent relationship with the Supervisory Board and we very much appreciate the guidance which the Board has provided during several regular meetings.

This all bodes well for our future. But we will not rest on our laurels. The months ahead remain challenging ones.

According to the Central Bank of Malta's forecasts, Malta's GDP growth is projected to moderate significantly from 6.8% in 2022 to 3.7% in 2023. As war continues to rage in Ukraine, elevated inflationary pressures, high interest rates and human resource constraints will continue to impede business development, meaning that the path to a full recovery remains a challenging one.

Against such a scenario, the MDB shall be both proactive and adaptable to the current economic challenges. In particular, the MDB shall be at the fore to proactively promote entrepreneurship, innovation, investment, and sustainable growth.

We have invested heavily in business development so that we can continue to offer a wider range of facilities consistent with the economic and social needs of the nation.

During the year we launched seven new programmes, composed of three schemes as part of the Ukraine crisis response package, the renewed scheme for student loans and three new schemes to support new investment by SMEs and start-ups. In doing so, we have been creative in designing financing solutions adapted to the needs of Malta's businesses.

I am very encouraged by the initial feedback received by the Banks to the new financing programmes we have just started, namely the SME Guarantee Scheme and the Guaranteed Co-lending Scheme, but I do encourage investors, entrepreneurs, SME owners and other financial professionals to reach out and discover how we can help. We are there to assist.

The SME Guarantee Scheme guarantees up to 80% bank loans of up to €750,000 to SMEs. In the Guaranteed Co-Lending Scheme the commercial bank provides 50% of the loan and the MDB the other 50%. The MDB provides the commercial banks with a guarantee covering 60% of the loan. The total loan by the two banks can reach €10 million. We have already accredited four main Maltese commercial banks to participate and intermediate the two new schemes.

We developed a sub-scheme within the SME Guarantee Scheme in collaboration with the Malta Council of Science and Technology that blends a grant element with a guarantee to soften the terms of the loans to innovative start-ups.

The Guaranteed Co-Lending Scheme, on the other hand, is our first small step towards developing a syndicated loan market in Malta so that big infrastructural and other projects can be financed locally.

This year we continued consolidating our internal operations after two years of growth and transformation on the back of accelerating activity during the pandemic. The Bank's equity base has been strengthened by a €20million injection by the Government as paid-up share capital. Moreover, the Bank's operating income continued to improve noticeably, reflecting the growth in business particularly in respect of guarantee operations.

It gives us great pleasure to note that not only did the MDB provide much needed assistance and innovative products to the local economy but that for the financial year 2022 we are reporting, for the first time, a profit of €1.2 million which, after provision for possible credit losses, leaves the Bank in the black with €651,500.

After many years of managing companies, in Malta and abroad, I am now again blessed with running a superb team of dedicated professionals who regularly endeavour to go beyong the call of duty. They deal with all the complications of State Aid regulation, support commercial banks in their credit work, take care of compliance, provide IT and corporate services, analyze risk, account for our finances, run internal audits, develop our products and do research, take care of public relations, and keep our small though innovative and bold organisation running smoothly. Their enthusiasm for the good work make my life much easier.

In conclusion, my sincere gratitude goes to the Chairman and the Board of Directors for their guidance and support and to all those who collaborated with us to maintain the Bank on its growth trajectory.

A special thanks to all our EU partners and local banks with whom we worked who have proven to be reliable, proactive, and excellent partners.

And to the Ministry for Finance and Employment, the Managing Authority for EU Funds, and many other government institutions who support us in our work with resources and encouragement.

I would also like to express my heartfelt gratitude to my predecessor, Mr Rene Saliba, who steered the institution from its birth and throughout its infancy and for guiding our team through the challenging developments which characterised the initial years of our existence.

PAUL V. AZZOPARDI
Chief Executive Office

CORPORATE GOVERNANCE STATEMENT

GOVERNANCE

The Malta Development Bank Act was passed on 5 May 2017 (Act XXI of 2017 CAP 574) and came into force on 24 November 2017 through Legal Notice No 340 of 2017. On 11 December 2017, the Minister for Finance appointed the members of the Board of Directors and the Supervisory Board of the Malta Development Bank.

The Board is responsible for ensuring good governance and performs this task by setting strategic objectives and targets and taking strategic decisions on all key business issues. The regular day-to-day management, control and direction of the MDB are the responsibility of the Chief Executive Officer (CEO) and the senior management team. The CEO and the senior management team follow the strategic direction set by the Board and in turn management provides the Board with the analysis needed for Board deliberations.

BOARD STRUCTURE AND RESPONSIBILITIES

The MDB Act provides that there shall be a Board of Directors consisting of a Chairperson and four Directors chosen from the private non-bank sector appointed by the Minister as well as two independent Directors appointed by the Minister on the recommendation of the Malta Council for Economic and Social Development. The MDB Act also provides that the Board of Directors shall exercise its mandate independently and in an autonomous manner and shall not seek or receive instructions from the Government or any other public authority.

At the end of 2022, the Board of Directors was composed of Prof. Josef Bonnici as Chairman, Prof. Rose Mary Azzopardi, Dr Michele Cardinali, Mr Steve Ellul, Mr William Spiteri Bailey, Mr Anthony Valvo and Prof. Philip von Brockdorff.

Article 21 of the MDB Act provides that the Chairperson shall be appointed after consultation with the Opposition. Article 21(5) sets the term of the Chairperson at six years. In line with article 21(6), the independent Directors nominated by the Malta Council for Economic and Social Development are Prof. Philip von Brockdorff and Mr William Spiteri Bailey. Mr Steve Ellul was appointed Director on 22 June 2022 for a period of five years to replace the late Mr Paul Cardona who passed away on 4 March 2022. Prof. von Brockdorff was appointed on 25 February 2022 until 10 December 2023 to replace Mr Robert Borg for the remaining part of his term, whilst Mr Spiteri Bailey has been appointed on 20 December 2022 until 10 December 2023, to replace Ms Jackie Camilleri for the remaining part of her term. The term of the other Directors is five years in accordance with article 21(4). The differing appointment terms provides continuity. The Chairperson may be re-appointed for four years while all the other Directors may be re-appointed for three years. Mr Valvo and Prof. Azzopardi have been reappointed for a period of three years effective from 11 December 2022.

The Board of Directors are accountable to carry out their responsibilities in a professional manner and to establish the professional standards and corporate values that promote integrity in accordance with the Code of Ethics for the Board of Directors. The responsibilities of the Board are prescribed in article 22 of the MDB Act, which formally lists the matters reserved for decision by the Board. These include:

- Annual Report and Financial Statements
- Risk management policy and framework
- Strategic plan
- Budget and financing facilities
- Credit and risk-sharing policy
- Appointment and terms and conditions of the Chief Executive Officer

During the financial year under review, the Board met eleven times.

The Board delegates specific responsibilities to three committees, namely the Audit Committee, the Ethics and Governance Committees and the Risk Committee. Each Committee operates in line with respective terms of reference approved by the Board.

BOARD COMMITTEES

AUDIT COMMITTEE

The Audit Committee's role is to assist the Board in:

- Providing oversight of the financial reporting process to ensure accurate, adequate and timely financial reporting as required for statutory reporting, to meet regulatory requirements and for the proper and sound management of the Bank.
- Fostering and ensuring adequate and systematic financial management practices to be consistent and compliant with MDB's values and ethics.
- Ensuring that the Bank's overall governance, risk management and internal control frameworks are effective and aligned with the business strategy.
- Ensuring effectiveness, performance and objectivity of the internal and external auditors and other assurance providers.

The Audit Committee comprises of three Directors appointed by the Board. The members as at 31 December 2022 were Prof. Philip von Brockdorff (Chairperson), Prof. Rose Mary Azzopardi and Mr Anthony Valvo. Prof Philip von Brockdorff was appointed as the Chairperson of the Audit Committee in lieu of Mr Robert Borg with effect from 23 May 2022.

The Chief Internal Auditor attends Audit Committee meetings in a non-voting capacity. Other directors, Senior Management and Chief Officers may be invited to attend in an advisory capacity. An independent audit firm that contributes to the Internal Audit function under a co-sourcing arrangement is also invited to attend the meetings.

During 2022 the Committee received regular reports from the Chief Internal Auditor and the independent internal audit firm. The Committee reviewed the key findings from the outcome of individual internal audit reviews carried out, monitored the status of implementation of agreed audit action points emanating from audit reports, and approved the risk-based internal audit plan. The Committee also reviewed the Financial Statements of the Bank and recommended them for the approval to the Board. The review focused on the adopted accounting policies, significant assumptions and estimates adopted in the preparation of financial statements, the appropriateness of financial reporting procedures and the accuracy and completeness of disclosures in line with international financial reporting standards as adopted by the EU.

The Committee met on five occasions in 2022.

ETHICS AND GOVERNANCE COMMITTEE

The Ethics and Governance Committee is appointed by the Board to oversee that a high standard of, and best practice in, corporate governance is maintained by fostering a culture of ethics, transparency and accountability. In fulfilling its oversight responsibilities, the Committee is to:

- Ensure that the Bank's corporate governance principles, policies, standards and practices optimally support the Bank's internal control priorities.
- Foster values and establish the ethical policy framework of the Bank, ensuring compliance with professional and ethical standards.
- Provide recommendations in the best interest of MDB in relation to procurement practices and remuneration packages to achieve the strategic plan adopted by the Board.

During the year 2022, the Committee recommended a set of additional policies for the Board's approval with a view to further support the Bank's performance and control environment and legal requirements. These new policies included the Training and Development Policy, Health and Safety Policy, Evacuation and Fire Drill Procedure, Payroll Policy, and Records and Archive Management Policy. Additionally, the Committee also reviewed and approved updates to the Procurement Policy and Equality Policy.

The Committee is composed of three Directors appointed by the Board. The current members are Prof. Josef Bonnici (Chairperson), Mr Anthony Valvo and Dr Michele Cardinali. In addition, Mr Paul V. Azzopardi (CEO) and the Chief Corporate Services Officer are also members of the Committee

The Committee met on three occasions in 2022.

RISK COMMITTEE

The role of the Risk Committee is to assist the Board in:

- Fostering sound risk governance across the Bank's operations by assuring that the Bank management is taking a forward-looking perspective and anticipating changes in business conditions.
- Ensuring that processes are in place to assure the Board that management has appropriately identified, reported, assessed, managed and controlled the risks relative to the Bank's strategy and operations.
- Promoting a culture of risk awareness within the Bank through communication and education.

The Risk Committee is chaired by Prof. Josef Bonnici and includes Prof. Rose Mary Azzopardi, Director, Mr Anthony Valvo, Director, as well as MDB's CEO and the Chief Risk Officer.

Three management committees report to the Risk Committee, namely the Asset-Liability Management Committee, the Credit Management Committee, and the Operational Risk Management Committee. The roles and composition of the three management committees reporting to the Risk Committee are as follows:

1. The Asset-Liability Management Committee (ALCO) was chaired by Ms Jacqueline Camilleri, Director, and includes as members the Chief Executive Officer, the Chief Risk Officer, the Chief Credit Officer, the Chief Financial Officer, and the Chief Projects and Treasury Management Officer. All members are appointed as voting members of the Committee with meetings held at least each quarter and with additional ad hoc meetings as may be deemed necessary.

   ALCO is tasked with carrying out the functions of asset and liability management and assessing liquidity risk, interest rate risk and capital risk. The asset and liability management function involves the evaluation of structural changes to the Bank's balance sheet and the achievement of strategic objectives in relation to the financial position of the Bank.

2. The Credit Risk Management Committee oversees the credit risk assumed by the Bank and monitors the effectiveness and application of credit risk management policies and procedures.

   It is chaired by Prof. Josef Bonnici, Chairman of the MDB, and includes the Chief Executive Officer, the Chief Credit Officer, the Chief Risk Officer, the Chief Finance, the Chief Legal and Compliance Officer, and the Chief Projects and Treasury Management Officer.

3. The Operational Risk Management Committee oversees the MDB's enterprise-wide risk framework that manages the operational risks to which the MDB is exposed in its conduct of business.

   It is chaired by Prof. Rose Mary Azzopardi, Director, and includes the Chief Executive Officer, the Chief Risk Officer, the Chief Operating Officer, the Chief Information Officer and the Chief Legal and Compliance.

The composition of these three management committees reflects the entity-wide scope and inclusive nature of the Bank's risk management strategy. During 2022, the meetings of the Risk Committee and the Operational Risk Management Committee were held jointly.

During 2022, the Risk Committee received regular reports on the risks faced by the MDB and the controls in place to mitigate these risks. It has also reviewed the Operational Risk Policy and Risk Register; the Risk Appetite Framework; and the Interest Rate Risk in the Banking Book (IRRBB) and put forward policy recommendations to the Board. During this period, the Risk Committee also approved the Bank's Stress Testing Policy.

The Risk Committee, ALCO and the Credit Management Committee met four times each in 2022.

THE INTERNAL AUDIT FUNCTION

Following the setting up of the Internal Audit function in 2021 and the recruitment of the Chief Officer Internal Audit, the MDB continued to invest in strengthening its Third Line of Defence during 2022, including through the recruitment of the Senior Internal Audit Officer, to ensure adequate risk coverage commensurate with its rapid growth.

THE ROLE OF INTERNAL AUDIT

The role of the Internal Audit function is to provide the Bank's management, the Audit Committee and the Board of Directors, with independent, objective assurance, advice, and insight designed to add value and improve the Bank's operations. In its role as the Third Line within the 'Three Lines Model' which the Bank endorses, the Internal Audit function has a vital and prominent role, being responsible for an independent review of the first two lines of defence, and for promoting best practices with a view to strengthening the Bank's governance, risk and control frameworks and mechanisms. This role is performed by:

- Evaluating the effectiveness and efficiency of internal control, risk management and governance systems in the context of both current and potential future risks;
- Assessing the reliability, effectiveness and integrity of management information systems and processes (including relevance, accuracy, availability, confidentiality and comprehensiveness of data);
- Monitoring of compliance with applicable laws and regulations; and
- Safeguarding of assets, including safeguarding of wider interests such as reputation.

The most important factors that shape internal audit are the function's independence, objectivity and authority, complemented with the other fundamental pillars of integrity, confidentiality and competence. In discharging its role, the Internal Audit function is guided by the International Standards for the Professional Practice of Internal Auditing including the Institute of Internal Auditors' Code of Ethics.

INTERNAL AUDIT ACTIVITIES

In accordance with the risk-based Internal Audit Plan for 2022, which was approved by the Audit Committee, the Bank's internal auditors provided assurance through the conduct of a number of audits. These audits assessed the effectiveness of governance, risk management and control processes implemented across a number of business areas. In line with the formulation and approval of the Internal Audit Policy and Procedures, the internal auditors tendered opinions not just on risk-sensitive operational effectiveness but also on the efficiency in the use and deployment of resources.

As in previous years, the work of the Internal Audit function was complemented by specific audit services by a reputable external audit firm. The co-sourcing agreement with this firm has been extended to 2023 to carry out credit file reviews to ensure compliance by the Bank's authorised financial intermediaries with the eligibility criteria approved by the European Commission under the Temporary Framework for State aid measures for facilities granted as part of the COVID-19 Guarantee Scheme. A similar review was also undertaken by the Internal Audit function to ensure compliance by the implementing partner with the eligibility criteria set for the Bank's Guarantee Facility for Loans to SMEs.

In accordance with best practice and in order to ensure timely risk mitigation, the auditors continued to undertake ongoing follow-up activities to assess the status of the implementation of pending recommendations resulting from previous audits. Progress towards satisfactory risk mitigation was reported through follow-up reports presented to senior management and to the Audit Committee.

As part of its consulting role, the Internal Audit function provided support to other business areas within the Bank, particularly with regard to the cost-effective implementation of control and oversight activities, issues related to policy deployment, and reviews of agreements entered into with partner banks. The auditors also reviewed a number of new policies forming part of the Bank's Policy and Procedures Framework. In addition, the auditors also developed the Internal Audit Policy, supplemented by a set of Internal Audit Procedures, which were duly reviewed by the Audit Committee and approved by the Board of Directors during 2022.

The Policy and Procedures form part of the audit function's aim to continue to develop the oversight and monitoring framework systematically and to progress in line with the Bank's growth and changing business and professional needs.

As in previous years, Internal Audit conducted an independent risk analysis to update its audit universe and formulate a three-year risk-based audit plan. The plan was developed following consultations with the Chief Officers and the Bank's Senior Management. The primary focus remains on the provision of assurance relating to the Bank's credit operations which is consistent with the MDB's main line of operations and the ever-increasing participation of the local business community in the Bank's guarantee and lending schemes.

COMPLIANCE AND LEGAL ACTIVITIES

During 2022, the Legal and Compliance Department of the Bank continued to strengthen and implement the Bank's compliance framework and to provide its legal services in relation to the contractual, legislative and operational aspects falling under the remit of the Bank.

COMPLIANCE

AML Activities

On 2 March, the Board of Directors adopted the Customer Acceptance Procedures issued under MDB's AML/CFT Policy. These Procedures establish the type of customer due diligence required to be conducted when MDB onboards a new customer and provides for the ongoing review of MDB's customers. The aim of these Procedures is to manage risks that MDB may be exposed to through the provision of direct lending services to customers, to prevent MDB from being used, intentionally or unintentionally, for money laundering or funding of terrorism purposes, and to identify customers who are likely to pose a higher-than-average risk. Three levels of Know Your Customer (KYC) measures are provided in the Procedures, which are to be resorted to depending on the risks posed by the particular customer. Thus, there are the standard Customer Due Diligence (CDD) procedures to be used generally for customers who are not classified as either low- or high-risk customers, the Enhanced Due Diligence (EDD) for high-risk customers and Simplified Due Diligence (SDD) for low-risk customers. The Procedures further provide the forms which corporate customers should fill at onboarding stage and the client risk assessment form to be filled in order to establish the risk status of MDB's clients.

On 15 December, the Board of Directors approved the annual revision of the AML/CFT Policy. This Policy was originally adopted by the Board of Directors on 21 November 2019. The main amendment to the AML/CFT Policy regarded the setting up of a Special AML/CFT Committee in order to decide and resolve problematic issues regarding high AML/CFT risks facing the Bank. This Committee is composed of the CEO as Chairperson, the Money Laundering Reporting Officer (MLRO), Chief Legal and Compliance Officer, Chief Credit Officer and Chief Risk Officer. Through this Committee, a collegiate decision can be taken on high ML/FT risks facing the Bank which could, for instance, lead to the refusal of a new client or the termination of an existing business relationship with a client.

MDB's AML/CFT Business Risk Assessment (BRA) and the AML/CFT Business Risk Register were adopted by the Board of Directors on 15 December. The main aim of the BRA is for the MDB to enhance its internal risk management measures and processes through the application of appropriate risk scoring in order to prevent its systems and activities from being used for money laundering and terrorist financing purposes. The BRA presents a comprehensive analysis of the services and products which are covered by the MDB, the customers benefitting from such services and products, the types of transactions being undertaken and the delivery channels used. Following this analysis, the MDB would be in a better position to concentrate its resources on the areas which pose the highest risk. The methodology adopted in the BRA consists of the identification of risks, being the risks pertaining to the MDB, the risks pertaining to intermediation through partner banks and risks pertaining to direct borrowers. Through ongoing monitoring, the level of residual risk would be maintained to the lowest possible level by adopting or updating mitigating measures where necessary. The BRA will be reviewed and presented to the Board of Directors annually or regularly by the MLRO when necessary.

During the year under review, MDB continued to carry out due diligence procedures in respect of both its direct clients and also on its partner banks who are accredited to participate under MDB's schemes. In 2022 MDB onboarded three customers under its Ukraine Subsidised Loan Scheme and two customers under the MDB Guaranteed Co-lending Scheme. Prior to the onboarding, first-line staff conducted Customer Due Diligence (CDD) procedures including identifying the corporate structure of the customer, identification and verification of its directors and ultimate beneficial owners, and its source of wealth and source of funds. The CDD process was reviewed by the MLRO. Three main compliance reviews were carried out on three partner banks which are implementing partners under MDB's COVID-19 Guarantee Scheme (CGS) and two other reviews initiated in 2021 were also concluded. The scope of these partner bank reviews is to verify that appropriate and correct CDD procedures have been followed as required under Regulation 7 of the Prevention of Money Laundering and Funding of Terrorism Regulation. The reviews consist of requesting the banks to forward or to explain their AML/CFT policy framework, organisational set up and other relevant documentation, followed by an interview with the bank's MLRO and carrying out an on-site or off-site sampling of customer files.

During the year under review, the Legal and Compliance Department continued to provide feedback to the selected audit firm which is conducting a Pillar Assessment on MDB's governance and other policy framework. Feedback on the findings of the dry-run assessment was provided to the audit firm in October 2022. The revised AML/CFT Policy and the Business Risk Assessment presented to the Board on 15 December 2022 address a number of these findings. The revised Customer Acceptance Procedures to be presented to the Board in January 2023 will address the rest of the findings, such as the introduction of a Client Risk Assessment methodology and a Jurisdictional Risk Assessment.

In terms of law and of MDB's AML/CFT Policy, all employees are required to undertake training annually. On 15th November, the MLRO provided the annual training to staff members on both the legislative and policy framework and on important developments concerning AML/CFT issues. Staff were continuously updated with developments through regular emails sent by the MLRO, informing them of important updates.

Data Protection Update

The Data Protection Policy was adopted by the Board of Directors on 1 August 2019 and was subsequently amended annually. There are three data protection procedures annexed to this Policy, namely the Data Subject Rights Request Procedure, the Data Protection Impact Assessment Procedure and the Data Breach Procedure. The Data Retention Policy also used to be annexed to the Data Protection Policy. Annual updates to this Policy were adopted by the Board of Directors on 31 August. The most significant change made was to separate the Data Retention Policy from the Data Protection Policy. The Data Retention Policy regulates the retention, maintenance and disposal of records and documentation within MDB. In addition to the Data Retention Policy, a (live) Data Retention Schedule is kept, containing a list of all documents retained by MDB whether in electronic or paper format, and indicating the owner of the documents, the retention period for each document and the reason why a particular retention period is being recommended. Whilst both the Data Retention Policy and Schedule have been kept and updated by the Data Protection Officer, the scope of these documents goes beyond personal data since they record any type of document held by the Bank, even if it does not contain personal data. For this purpose, the Data Retention Schedule was extracted from the Data Protection Policy in order to become a stand-alone policy falling under the responsibility of the Records and Archiving Management Officer who has more visibility on all the documents held by MDB and could therefore take over the function to ensure that the maintenance and disposal of documents take place in the stipulated time and in a safe manner.

In order to implement the requirements of the GDPR, a privacy notice was published on MDB's website in 2019 indicating to the public the categories of personal data which are processed by MDB, the purpose for which they are processed, the rights of data subjects and a general indication of the applicable retention periods. The privacy notice was duly reviewed in 2022. Most of the amendments made were of a finetuning nature and mainly regarded updating the list of MDB activities involving the processing of personal data. MDB's official address on the privacy notice was also updated. The revised privacy notice was uploaded on MDB's website on 7 July 2022.

A Data Processing Register was compiled in 2019 to record all the processing activities of MDB, the scope of such processing, the legal basis for the processing, any processing agreements that have been entered into, any transfer of data to third parties, etc. The register also provides details of the retention periods of personal data held by MDB. The Data Processing Register has been updated in 2022 in order to observe statutory requirements for its yearly review. Questionnaires were distributed to staff asking for any developments in the processing of personal data (such as new processes not recorded in 2021). The register was updated on the basis of the compiled information and interviews held with staff. The updated Data Processing Register was submitted to senior management on 10 October 2022.

On 1 November, employees received their annual training on the data protection legal framework. The training was intended to ensure that MDB staff are aware of relevant data protection legislation and requirements; can recognise, handle and report breaches to the Data Protection Officer and to fulfil statutory requirements for an annual data protection training of employees.

Other Compliance activities

In 2019, the internal auditors of the Bank compiled a compliance programme for MDB based on the requirements of the MDB Act. The Legal and Compliance Unit is responsible to monitor compliance with the requirements of the MDB Act and for this purpose sends out questionnaires to the various business units to compile information on adherence to the requirements of the MDB Act. All staff are also required to provide a declaration that they abide by the requirement in article 43 of the MDB Act to retain the confidentiality of customer information. The process to compile data for this year's revision of the compliance programme commenced on 11 October. The information received was used to update the compliance programme risk dashboard, which was also presented to senior management.

On 25 November 2021, the Board adopted the Anti-Fraud Policy and the Procedures for the Investigation of Suspected Fraudulent Activities. The Anti-Fraud Policy is intended to promote a culture which deters fraudulent activity and facilitates the prevention and detection of fraud. It also sets out the procedure for the reporting and investigation of alleged cases of fraud. On 13 January 2022, training was provided to staff as a reminder of their obligations under this Policy.

As part of the Pillar Assessment process, MDB is expected to have in place Policies and Procedures which aim to ensure that EU funds are not utilised in projects linked to tax avoidance practices. This requirement is based on the 2018 Communication from the Commission on new requirements against tax avoidance in EU legislation governing in particular financing and investment operations (C(2018) 1756 final). Accordingly new Tax Avoidance Surveillance Policy and Procedures were prepared in order to address this requirement. In terms of these Policy and Procedures, MDB will be primarily responsible to conduct due diligence against tax avoidance practices in the application of EU funds in the form of loans, grants, equity or guarantees that could be allotted to MDB to manage as an implementing partner under the terms of an EU programme.

LEGAL SERVICES ACTIVITIES

During 2022 the Legal and Compliance Department worked on a number of risk sharing agreements and other agreements required to regulate relations with partner banks under MDB's new uncapped schemes, namely the Guaranteed Co-lending Scheme and the SME Guarantee Scheme as well as the new support measures not address the impact of the Ukraine crisis, namely the MDB Subsidised Loan Scheme and the MDB Liquidity Support Guarantee Scheme. The legal function was also involved in the Selection Panel for the accreditation of partner banks under MDB's various schemes. It provided general legal advice to all of MDB's Units and has provided legal input in most of MDB's policy framework as well as in discussions relating to the Pillar Assessment exercise.

STRATEGY

BUSINESS

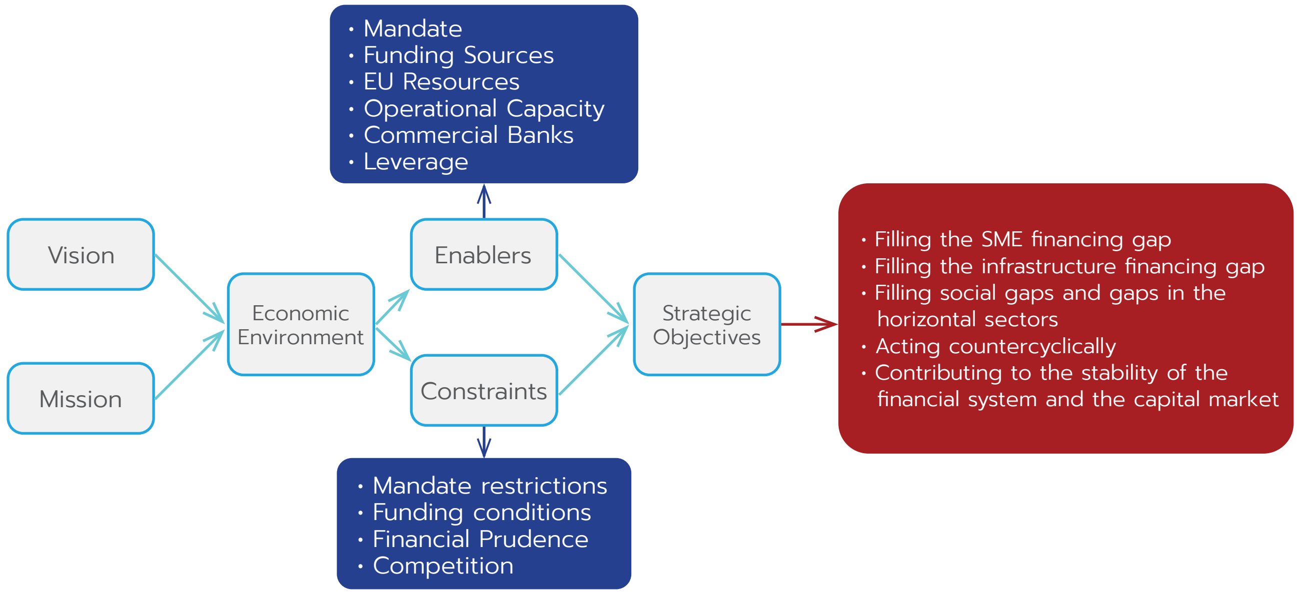
Since being set-up in late 2017, MDB's strategy and business model have evolved in line with changing economic and financial conditions, as well as public policy priorities. The MDB has shown nimbleness and adaptability in being an innovative provider of financing solutions that effectively address market gaps. The MDB is committed to continue extending its reach and to positively contribute towards inclusive and sustainable socio-economic development of Malta.

MDB's business model is in line with the recommendations emanating from a market failure study commissioned by the Government of Malta in 2015, which had identified two main market gaps in Malta: namely the financing of SME's and infrastructural projects. However, as part of its ongoing operations the MDB periodically scans the market to ensure that changing circumstances are being monitored, analysed and addressed appropriately.

To this end, as part of this ongoing process, during 2022 the MDB updated its business strategy framework. This update lays out the core elements of MDB's strategy, including its vision, mission, and strategic objectives to create a clear and effective framework to deliver on its mandate (see Figure 1). In formulating this strategy, the MDB has considered its experience and progress to date as well as the recent and projected changes in the macro-economic environment.

In brief, the strategy framework examines the Bank's role so far in supporting and developing the local economy. It provides a detailed assessment of the economic environment in which the MDB operates, including a summary of the main financial gaps. The tools and assets of the MDB - its enablers - are discussed in depth, followed by an examination of the constraints faced. This framework allows the Bank to achieve a better understanding of what lies within the Bank's ability to pursue its mission and from these considerations, the Bank can develop a number of strategic objectives to guide MDB's future development.

Figure 1: MDB's business strategy framework



The MDB's most prominent strategic objectives are; filling SMEs financing gaps; supporting infrastructural development; being active in filling social gaps; promoting the adequate financing of horizontal sectors such as digitalisation and green initiatives; acting countercyclically such as providing urgent liquidity support at times of crises; and supporting the country's financial stability where appropriate.

These strategic objectives, or initiatives, are meant to serve the MDB as flexible signposts in pursuing its vision of significantly contributing towards a higher quality of life via sustainable economic development by promoting inclusive and environmentally sustainable growth and infrastructure development. Emanating from this vision, the MDB will pursue its mission of bridging investment gaps in Malta by offering financing facilities that support productive and viable operations where the market is unable or unwilling to accommodate such activities. These objectives will entail the provision of schemes, direct financing and co-financing with the appropriate configurations and components.

The MDB shall be both proactive and adaptable to the current challenging economic scenario. Higher interest rates, coupled with elevated inflationary pressures, may hamper economic activity, and the MDB shall be at the fore to countercyclically promote entrepreneurship, innovation, investment, and sustainable growth.

SPECIAL TOPIC I
THE FIRST 5 YEARS OF THE MDB

RATIONALE FOR SETTING UP A PROMOTIONAL BANK

The principal economic rationale for a development bank or national promotional bank (NPB) is that market failures may lead to less investment and, thus, slower future growth than would be economically efficient, and that an institution with a public mandate is better placed than private operators to overcome these market failures.[4]

NPBs statutes usually stipulate clearly that the bank will focus its operations on sectors where market failures are pervasive, and which are thus underserved by commercial banks or other private finance providers.

In recent years, European NPBs have stepped up their activities, aiming to counterbalance the necessary deleveraging process in the commercial banking sector, particularly in the areas of SMEs and long-term financing. NPBs are also playing an increasingly important role in implementing EU financial instruments. Over the past few years, calls were made to exploit further the synergies between the EU budget, the European Investment Bank (EIB) Group and NPBs in policy areas such as climate change, environment, innovation, and social and human capital development. Given the urgent need to boost investment and the limited fiscal space available on average in Europe, an optimal use of public resources is needed more than ever through the intervention of NPBs.

ORIGIN AND MANDATE OF THE MDB

Origin

During the height of the European sovereign debt crisis in 2010-2012 and the ensuing global economic recession, it became clear that Malta lacked an important institution that acts counter-cyclically to mitigate the adverse impacts of the prevailing economic cycle. In the period after the sovereign debt crisis, notwithstanding the excess liquidity characterising local banks, the volume of bank lending to corporate borrowers in Malta remained subdued and lending rates remained relatively elevated when compared to the rates in other euro area countries.

The origins of the need to create a new institution to address such an institutional gap go back to the firm belief of the Central Bank of Malta (CBM) on the benefits that can be generated through the setting up of a national development bank. In 2012 a CBM delegation led by Prof. Josef Bonnici, who was CBM Governor at the time, visited a number of major development banks and institutions to obtain a better insight into the institutional and organisational aspects of promotional banks and their business models. In 2013, the CBM presented a proposal to the Government recommending the setting up of a national promotional bank in Malta. At the time, the two major political parties included the establishment of a national development bank in their electoral manifesto, indicating broad political consensus on the need to set up such an institution.

In July 2014, the Government set up a Working Group with wide representation to prepare recommendations for the setting up of a development bank and to draw the related legislative and operational framework of the bank. The Working Group consisted of officials from the Central Bank of Malta, a major credit institution, a legal firm, a financial advisory firm and the Ministry for European Affairs and Implementation of the Electoral Manifesto, and included Rene G. Saliba and Paul V. Azzopardi who were eventually appointed the first two CEOs of the Bank.

At the request of the European Commission, in 2015 the Ministry for European Affairs commissioned two studies. The first was a Market Study on Potential Existence of Market Failures in Malta which concluded that taking into account both SME finance and infrastructure financing, the total funding gap in Malta was estimated at between 29% and 39% of GDP over a period of five years, equivalent to between €2.3 billion and €3.1 billion. The second report provided a Blueprint describing the role of the Bank, its business model, products and financial projections. The Working Group collaborated very closely with the consultancy firm during the course of these market studies which also entailed extensive consultations with a wide range of domestic stakeholders.

4 See Communication from the Commission to the European Parliament and the Council; Working together for jobs and growth: The role of National Promotional Banks (NPBs) in supporting the Investment Plan for Europe

The Working Group, in conjunction with the Ministry for European Affairs, also held a series of consultations with various EU directorates, namely with Eurostat, in connection with the statistical classification of the Bank; with the Directorate-General Competition, in connection with State Aid rules; and with the Directorate-General for Financial Stability in connection with banking regulatory matters.

In April 2016, Eurostat determined that the Malta Development Bank (MDB) should be classified outside the general government sector for the purposes of classification by sector under ESA 2010. During the same year, the EU Commission published its decision that the legislation, business plan and proposed measures pertaining to the MDB are in line with State Aid rules and in conformity with the rules on the internal market.

Subsequently, the MDB was established by virtue of the Malta Development Bank Act (Act XXI of 2007, CAP 574) which was passed in May 2017 and which came into force in November 2017. The Bank commenced operations on 11 December 2017 when the Minister for Finance appointed the Board of Directors and the Board held its first meeting

Mandate

As stipulated in the MDB Act, the Bank shall contribute towards sustainable economic development that benefits the Maltese people. This mission is aligned with public policy objectives aimed at promoting inclusive and environmentally sustainable economic growth; supporting infrastructure development; and linking entrepreneurship, investment and economic growth to improved living conditions and better social inclusion.

MDB's strategic objective is to offer financing facilities that support productive and viable operations where the market is unable or unwilling to accommodate such activities on its own in whole, or part. MDB's activities focus on complementing and supplementing the operations of market players in the provision of financing facilities, particularly to SMEs, infrastructure projects that contribute to national or regional development, and projects which are socially-oriented, energy efficient and environment friendly.

Prof. Josef Bonnici, MDB Chairman: "When I was Governor of the Central Bank of Malta it became evident that the country lacked an institution to address gaps in the credit market and that a promotional bank was needed to introduce a new form of financial intermediation to support the economic and social development of Malta. I am proud that my past efforts to push forward the concept of creating a national development bank are now bearing fruit and very positive results."

CAPACITY BUILDING AND AFFILIATIONS WITH EUROPEAN NETWORKS

The MDB is proud to adhere to the highest internal governance standards and to abide with robust and best practice policies and procedures, including a clear organisational structure with well defined, transparent and consistent lines of responsibility, effective risk management processes, control mechanisms and gender-neutral remuneration policies.

Immediately after being set up in late 2017, the MDB started to invest heavily in developing its operational capacity, strengthening its organisational set-up and building a highly talented and motivated human resources team, which was crucial in enabling the MDB to gear up to fulfil its mandate and assume more responsibilities, particularly in taking a leading role during the pandemic. The MDB continued to build a team of professionals with extensive experience, knowledge, and skills and by the end of the fifth year of operations the number of employees reached 22. Concurrently, it became evident that the Bank's leased premises in Valletta could no longer accommodate the Bank's growing staff complement. Albeit working on a hybrid work model, with most staff working from home due to the pandemic, during the year 2020 the Bank acquired larger premises in Floriana that since 2022 started serving as its head office.

During the first year of the Bank's operations, the MDB was mainly engaged in a broad consultation process with potential local stakeholders to identify gaps in the financing of viable and productive initiatives, explore financing opportunities with financial intermediaries and other stakeholders, and develop financial instruments to improve access to financing, particularly for SMEs and infrastructure projects. Over the first five years, the MDB also managed to build a value-laden relationship with a number of international associations, multinational development institutions and foreign development banks. The MDB is a member of the European Association of Public Banks (EAPB), the European Long-Term Investors (ELTI), the Network of European Financial Institutions for SMEs (NEFI) and the European Association of Guarantee Institutions (AECM). Membership in these associations provides the Bank with various benefits, including exchange of information, interfacing and sharing of technical experiences and best practices; being part of a strong lobby group representing their Members at a European level; participating in consultations and discussions with EU institutions on financial instruments, regulations and legislative proposals, as well as facilitating dialogue and strategic alliances with other development banks and institutions.

During this period, the MDB also embarked on an ambitious mission to become a direct implementing partner of the InvestEU. As Malta's only promotional bank, the MDB aims to become the country's single direct entry point for the EU guarantees. The MDB collaborates closely with the European Commission, particularly through the Technical Support Instrument (TSI), which is the Commission's instrument to provide technical support to reforms in EU Member States. The TSI builds on the success of its predecessor, the Structural Reform Support Programme (SRSP). Over these first five years, the SRSP and TSI supported MDB in its capacity building efforts in preparation for the Pillar Assessment, and more recently is supporting the Bank via a study to assist in the potential development of effective equity-based and start-up financial instruments. During 2020, the MDB also benefitted from support from the European Investment Advisory Hub (EIAH), the advisory arm of the European Investment Bank, on the preparation and implementation of financial instruments under the InvestEU Programme in Malta for the current Multiannual Financial Framework. Going forward, the MDB will also be exploring potential ways of collaboration with the InvestEU Advisory Hub which is the second pillar of the InvestEU.

FINANCIAL INSTRUMENTS

MDB's role is to complement commercial banks in stimulating investment in viable projects where banks are not willing or able to provide the required financing, especially in the SME sector, and to compensate for impediments in the transmission of monetary policy. In addition, the Bank can facilitate more investment in bankable infrastructural projects. The MDB can also play a significant role as a vehicle for EU resources in the context of the EU's increased focus on financial instruments and reduced reliance on grants. The MDB can also act counter-cyclically in case of economic crises and financial instability.

NPBs around Europe are acting as facilitators of the transition away from grant-dependency in the absorption of Structural Funds to smarter use of public resources by crowding-in private actors and obtaining the benefits of financial leverage through financial instruments. These tools also allow for the combined use of various types of support, including interest rate subsidies (grants) and guarantees, which when combined can better unlock the necessary capital in addressing certain market gaps.

The MDB successfully introduced innovative blended instruments under the Further Studies Made Affordable (Plus) Scheme funded by the European Social Fund. It also provided urgent liquidity support under the COVID-19 Guarantee Scheme and more recently under the package of measures to address the impact of the war in Ukraine. Indeed, all these three schemes combine an interest rate subsidy element on top of the guarantees provided by the MDB.

Mr Rene Saliba, first CEO of the MDB "The first years of the MDB were very challenging, particularly because of resource constraints and also because few stakeholders were familiar with the role and functions of a promotional bank. I am proud that over the years the MDB earned a good reputation and was instrumental, working with the commercial banks and with other strategic entities, to address the main obstacles faced by underserved economic sectors, especially SMEs but also in other areas such as student loans and socially oriented infrastructure projects, particularly in the wake of the repercussions of the COVID-19 pandemic and the Ukraine crisis."

SME oriented schemes

The Family Business Transfer Facility was the first instrument launched by the MDB, in October 2018. The uptake of this product was lower than anticipated. In contrast, the SME Invest scheme, launched in May 2019, was highly successful and remained MDB's main guarantee scheme for new SME investments until end 2022. By this period, the allocated portfolio of €50 million was almost entirely absorbed. After conducting a series of consultations with stakeholders to explore how the effectiveness of these instruments can be enhanced, in the last quarter of 2022, the Bank launched the SME Guarantee Scheme (SGS) with the aim to replace the SME Invest as well as the Family Business Transfer Facility. The SGS seeks to enhance SME access to bank credit for new investment as well as other purposes, including for working capital related to new investment and business transfers. Facilities ranging from €10,000 up to €750,000 are supported under the scheme with a loan term of up to 10 years. Unlike the SME Invest Scheme, where the MDB guarantee of 80% of covered loans was capped at 25% of the portfolio, the MDB's guarantee under SGS is uncapped, which should encourage the partner banks to provide additional investment financing on enhanced terms since uncapped guarantees simplify commercial banks' capital adequacy calculations.

Concomitantly, for larger facilities, the Bank in 2022 launched the Guaranteed Co-Lending Scheme (GCLS), a risk-sharing facility involving co-lending between the MDB and the accredited Commercial Bank on a 50:50 basis. The GCLS caters for SMEs with larger loan requirements that exceed the €750,000 limit under the SGS. Both the SGS and GCLS were initially backed by the Pan European Guarantee Fund (EGF) and following the expiration of the EGF on 31 December 2022, the MDB is seeking the support of the EIF under the Invest-EU products.

Educational-support instruments and social infrastructural projects

In line with its commitment to facilitate new projects with a high social dimension, the MDB in October 2019 launched the Further Studies Made Affordable (FSMA) scheme to support the upskilling of Malta's youths to strengthen the country's human capital. After the FSMA portfolio of €9.25million was fully taken up by February 2022, the MDB continued to build on its success by launching the Further Studies Made Affordable Plus (FSMA+) scheme which offered a portfolio of study loans of up to €15million. Through these schemes, the Bank ensured an equality of opportunity, where students, regardless of their financial background, can develop their potential without relying on the financial backing of their parents or relatives.

During this period, the Bank also supported large-scale infrastructure projects, which experienced difficulties in accessing the appropriate bank or other financing. Through the Tailored Facility for businesses, the MDB offers favourable financing terms for bankable projects with a special focus on socially oriented initiatives, circular economy and competitiveness enhancement. Under this facility the MDB has provided a co-financed loan for the construction and completion of a University campus residence complex. The Bank is working on other projects in sectors relating to health, education, sports development and affordable housing.

Crisis response measures during the pandemic and war in Ukraine

Following the outbreak of the COVID-19 pandemic in early 2020, the strategic priority of the Bank shifted from stimulating new investment to providing urgent liquidity support so as to safeguard and preserve the continuity of national economic activity by ensuring that Maltese businesses survive the severe liquidity constraints they were facing due to the drastic restrictions resulting from the pandemic. The MDB accordingly launched the COVID-19 Guarantees Scheme (CGS) in April 2020, leveraging on a Government guarantee of €350 million through which the MDB provided a guarantee of 90% on new working capital loans granted by partner commercial banks. This enabled the creation of a portfolio with a potential of up to €777.8 million in new working capital loans to all businesses facing liquidity shortages due to the pandemic, regardless of size or sector. The CGS was complemented by a COVID-19 Interest Rate Subsidy Scheme covering up to 2.5% of the interest rate payable on CGS loans during the first two years of such loans.

More recently, in response to the outbreak of war in Ukraine in early 2022, the MDB launched a number of urgent liquidity support measures, backed by a Government guarantee, to ensure security of supply of cereals including wheat, animal feed, fuels and any other business whose liquidity was negatively impacted by the war. As in the case of the CGS, the MDB offered de-risking instruments to enable the provision of more accessible and affordable working capital loans, thus reducing the impact on the affected economic operators.

REACH AND IMPACT ON THE MALTESE ECONOMY

The MDB performs a promotional role in line with public policy. The MDB's remit of activities covers a wide range of possible operations where there is evidence of market failure. Through its schemes the MDB unlocks lending to businesses at better terms. Since the launch of the Bank's first scheme in late 2018, the MDB has been a major contributor to the Maltese economy, and as the COVID-19 pandemic brought worldwide economies to a halt, the MDB fulfilled its countercyclical role by ensuring that hundreds of businesses, predominantly SMEs, remained afloat throughout these troublesome months.

As of the end of 2022, MDB's total financing volumes, including all guarantees and loans to local business undertakings, stood at almost €600 million, predominantly spurred by around €500 million related to the CGS, and to a lesser extent, to the close to €50 million related to the SME Invest facility. The impact of MDB's schemes is also substantial on a national level, with the MDB supporting 13% of all outstanding outstanding loans to Non-Financial Corporations residing in Malta. The most visible impact was during the pandemic where business loans increased by 9% underpinned by the CGS, whereas the lack of MDB support would have resulted in a decline of 2.5% in such loans.

Moreover, the impact is also notable on the human capital front. In fact, by the end of 2022, total study loans under both the FSMA and FSMA+ schemes reached €15 million with over 400 students supported through full subsidisation of interest during the moratorium period which extends throughout the study period plus one year, no collateral requirement and no upfront contribution being required.

Mr Paul V. Azzopardi, MDB's CEO: "In a relatively short period of five years, the MDB reached over 700 businesses which employ around 40,000 persons, and more than 400 students, providing close to €600 million in loans and guarantees. Looking ahead, the MDB will continue acting as a catalyst for loan syndications by helping to pool-in diverse suppliers of credit so as to accommodate the financing needs of larger projects which are not likely to be served by one single financial intermediary. The MDB will also continue with its work of combining grants with loans to narrow or eliminate financial gaps and to act counter-cyclically when necessary."

Way forward

Market gaps arise from the inability or unwillingness of financial intermediaries to accommodate financing requirements of their customers. The MDB will continue striving to narrow these market gaps and to work on schemes offering favourable financing rates and terms, in support of the economic regeneration of the country. In addition, in recent years, Maltese financial institutions and corporations have made significant progress in addressing sustainability and climate change. In line with public policy, the Bank, through its operations, will encourage further the building of a greener, more digital, modern and resilient Maltese economy.

MOBILISING RISK-SHARING INSTRUMENTS AT EU LEVEL

The Pan European Guarantee Fund

During 2021 the destabilising effects of the COVID-19 pandemic started to tone down and accordingly the Bank re-focused its attention on the introduction of new financial instruments that are tailored to the new circumstances facing local businesses in recovery phase. To this end, in 2022, the MDB launched two financial instruments aimed at facilitating SMEs access to finance for new investment and growth. The Bank's goal was that these new financial instruments would provide enhanced features so as to facilitate additionality and give a strong boost to the recovery process. In view of the Bank's limited risk absorption capacity, MDB had sought the support of the European Investment Fund (EIF) by way of risk sharing instruments under the Pan-European Guarantee Fund (EGF).

The EGF forms part of the overall package of measures agreed by the Eurogroup on 9 April 2020 and further endorsed by the European Council on 23 April 2020. The objective of the EGF was to respond to the economic impact of the COVID-19 pandemic by ensuring that companies, particularly SMEs, in the Participating Member States have sufficient short-term liquidity available to weather the crisis, and to be able to continue their growth and development in the medium to long-term. Through EGF resources, the EIF committed €26.2 billion of financing through 295 agreements with financial intermediaries in the 22 participating countries across Europe. These agreements had the potential to mobilise up to €115 billion in financing for SMEs.

After months of negotiations, due diligence and consultations with the EIF, on 17 December 2021, the Bank signed two agreements with the EIF; a direct guarantee agreement and a counter-guarantee agreement. These agreements recognise the MDB as the intermediary party of the EGF. The EGF financial guarantees on the two new financial instruments amount to close to €80 million, and thanks to these guarantees the MDB was able to offer, for the first time, uncapped portfolio guarantees to commercial banks with a potential to generate new lending up to €180million for new investment. On 25 February 2022, the MDB conducted a soft market testing exercise with local commercial banks on the new schemes to be covered by the EGF and subsequently issued a call for expression of interest.

These two new schemes are open until December 2024. As per EGF contractual terms, the end date for the inclusion period under these agreements with the EIF was 31 December 2022. By this date, the MDB managed to sanction a total of €12.1 million in loans, all of which to customers operating in the AI and digital economic sectors. In essence, albeit in a very short period, through these agreements, the MDB was able to act as Malta's gateway for EGF financial guarantees, the benefit of which was passed on to these Maltese businesses in the form of lower interest rates, lower collateral requirements, higher tolerance to certain novel and potentially riskier sectors and thus ensuring better access to finance.

EIF's InvestEU

Over the course of 2022, the EIB Group - which is the implementing partner responsible for the management of 75% of the budgetary capacity of the InvestEU - launched a number of instruments covering all policy windows through its subsidiary, the EIF. The EIF focuses on venture capital and guarantee activities, providing risk financing to SMEs and promoting entrepreneurship.

The EIF, in its role of a guarantor, provides credit risk protection through portfolio (direct and counter-) guarantees to selected financial intermediaries. These are provided in the form of capped or uncapped guarantees and shall partly cover the credit risk of eligible debt financing transactions granted to predefined categories of final recipients and included for coverage in the respective portfolios (see Figure 2).

Figure 2: EIF Guarantee products portfolio under InvestEU

SME COMPETITIVENESS	SUSTAINABILITY	INNOVATION & DIGITALISATION
CULTURAL & CREATIVE	MICRO & SOCIAL	SKILLS & EDUCATION

As an eligible financial intermediary, the MDB was closely following these developments to possibly roll-over the EGF backed financial instruments which expired on 31 December 2022 with these EIFguarantee products under the InvestEU.

To this end, in December 2022 the MDB sent an expression of interest to the EIF for a mix of direct guarantees and counter-guarantees amounting to €52.8million under the InvestEU programme, specifically for the SME Competitiveness, Innovation and Digitalisation, and Sustainability guarantee. Through this approach, the MDB plans to start mobilising indirectly the InvestEU guarantee, while concurrently proceeding with the ambitious process of eventually mobilising directly the InvestEU guarantee when becoming a direct implementing partner thereafter (see next section).

INVESTEU AND THE PILLAR ASSESSMENT PROCESS

In 2022 the Bank continued its ambitious mission to become a direct implementing partner of the InvestEU. To be able to manage directly this InvestEU Guarantee, the MDB is required to guarantee a level of protection of the EU's financial interests by undergoing a Pillar Assessment with the objective to enable an independent auditor to report on whether the entity fulfils the requirements set out in article 154(4) of the Financial Regulation of the European Commission. More specifically, the MDB must prove that it meets the requirements with regard to 9 'pillars', namely: the internal control system: the accounting system; an independent external audit; procurement: rules and procedures for providing financing from EU funds through grants and financial instruments; exclusion from access to funding; publication of information on recipients; as well as protection of personal data. In particular, the Pillar Assessment focuses on the appropriateness of the internal controls, credit risk management, risk governance, systematic due diligence, and risk analysis, assessment and measurement of credit risk from all transactions.

Such an Assessment is required to be carried out by an external auditor on the basis of a set of terms of reference established by the European Commission.

As Malta's only promotional bank, the MDB aims to become the country's single direct entry point for such guarantees, but before doing so, it needs to undergo a thorough process to assess its eligibility for managing EU guarantees. In the beginning of 2021, following a legal and eligibility check, the European Commission informed the Bank that they have positively considered the application of the MDB to launch a Pillar Assessment. To reach this point the MDB had gone through an extensive exercise of organisational capacity building, also through the support of the Technical Support Instrument (formerly the Structural Reform Support Programme) of the European Commission, partly in preparation for this Assessment.

In February 2021, the Bank issued a Request for Quotation, inviting proposals from a number of local auditing firms for the provision of external audit services for the InvestEU Pillar Assessment. After a thorough evaluation of all submitted proposals, toward the end of 2021 the Bank's appointed adjudicating panel selected a reputable firm to provide these services.

During 2022, the selected independent auditor conducted a preliminary assessment to identify critical gaps which may negatively impact the final and full Pillar Assessment, thus pre-empting potential failing points.[5] In this preliminary assessment, or dry-run exercise, the auditors conducted interviews and walkthroughs of processes with the control owners of the respective pillars (mainly the Chief officers of the various Departments). This was done to formulate an overall high-level opinion of the potential gaps in systems, controls, rules and procedures for each pillar against the criteria set by the Commission.

In the ensuing months, several other bi-lateral meetings were held, and the identified gaps, particularly the critical ones relating to procedures focusing on AML, tax avoidance surveillance and non-cooperative jurisdictions, were thoroughly examined and improved. By November 2022 this dry-run process has been completed and the Pillar Assessment proper started immediately after. The exercise is expected to be finalised by the beginning of the second quarter of 2023. Subsequently, this Assessment will be submitted to the European Commission for its review. The MDB is hopeful that the process will be finalised in time for its application to the second call for expression for direct implementing partners foreseen to be issued in 2024.

LAUNCHING OF FINANCIAL INSTRUMENTS

During the period under review the Bank continued to consult its stakeholders to ensure that its schemes remain relevant and continue to adequately fill market gaps. Following discussions with commercial banks, business representatives, as well as other governmental entities and institutions, in 2022 the MDB launched six financial instruments and a sub-scheme.

In February 2022, to continue supporting the upskilling of Malta's youths and to strengthen the country's human capital, the Bank launched the Further Studies Made Affordable Plus (FSMA+) scheme. This scheme builds on the success of its predecessor, the FSMA scheme. These schemes have introduced to the country an assurance of equality of opportunity, where students, regardless of their financial background, can develop their potential without relying on the financial backing of their parents or relatives.

In May, the MDB launched its first support measure as part of a package in response to the war in Ukraine: the Subsidised Loan Scheme (SLS). This emergency scheme was aimed at assisting importers and wholesalers to stock reserves of wheat and animal feeds for a longer period than normal. Such abnormal stock piling at the prevailing higher prices required substantial liquidity at very short notice. The MDB was appointed by the Government to take immediate remedial action by providing urgent liquidity support in the form of direct subsidised loans to the major grain importers of up to €30million.

Following the launch of the SLS, the MDB in June 2022 rolled-out a further €150 million emergency liquidity support to businesses: the Liquidity Support Guarantee Scheme (LSGS) as part of an aid package in response to the Ukraine crisis. The LSGS consists of two measures; one open to all undertakings affected by the crisis (LSGS-A) and the other specific to the fuel and oil importers (LSGS-B). Both these Schemes were intermediated through local banks.

In the last quarter of the year under review, the Bank launched the SME Guarantee Scheme (SGS). The SGS aims at enhancing SME access to bank credit for new investment as well as other purposes; including for working capital related to new investment and business transfers. In collaboration with the Malta Council for Science and Technology (MCST), the Go-To-Market was launched as a sub-scheme of the SGS, allocating €1.5 million specifically to Research & Innovation projects.

During the same period, the Bank launched the Guaranteed Co-Lending Scheme (GCLS), a risk-sharing facility for larger facilities, involving co-lending between the MDB and the accredited commercial banks on a 50:50 basis. Both the SGS and GCLS were initially backed by the Pan European Guarantee Fund (EGF) and following the expiration of this EGF guarantee at the end of 2022, the MDB is seeking the support of the EIF under the Invest-EU products.

More detailed information on these scheme is provided in the Business Review section (see pages 57 and 58).

5 The framework for this preliminary high-level assessment is based on the European Commission's decision of 17 April 2019 on the establishing of new terms of reference for the Pillar Assessment methodology.

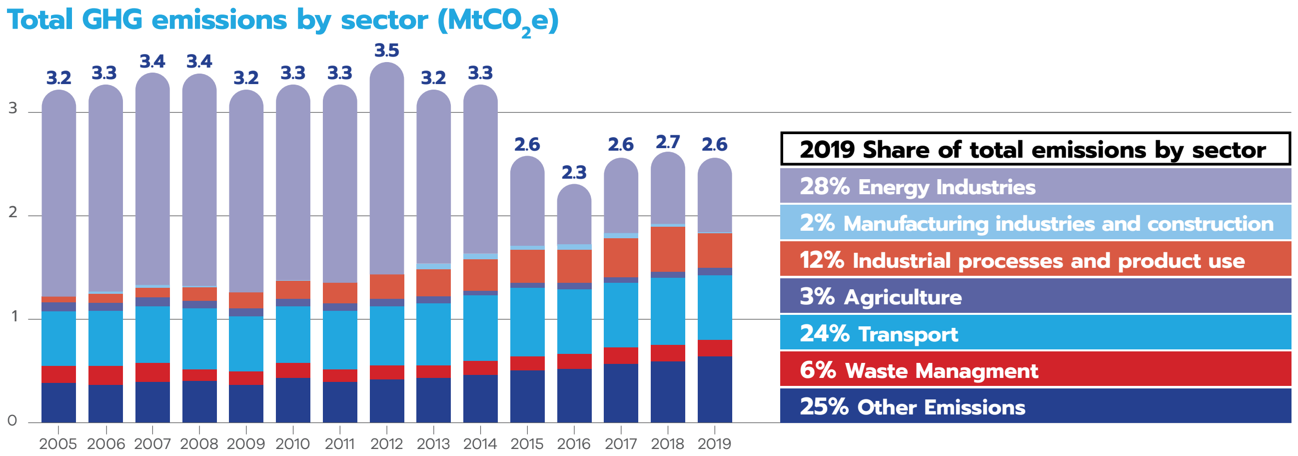
GREEN FINANCING

During the year, the Bank participated in various events and initiatives promoting greener investments. Moreover, throughout this period the MDB worked further on developing financing tools to push Malta's economic regeneration and renewal. Whilst the SGS and GCLS are available to all economic sectors, the MDB is prioritising those investment projects that aim to build a greener and more digitally oriented economy.

Data for 2019 show that Malta was responsible for greenhouse gas (GHG) emissions of 2.6 million tonnes of carbon dioxide emissions (MtCO2e). Since 2012 total emissions dropped by 26%, largely spurred by changes in the energy sector, notably the electricity interconnection with Sicily and the shift from heavy fuel oil to natural gas in local electricity generation.[6]

Offsetting in part this overall reduction, emissions from the transport sector increased by 22% between 2005 and 2019, accounting for 24% of total emissions in 2019 (see Figure 3). To this end, during 2022, the MDB continued to discuss with Transport Malta, Malta Enterprise, the Managing Authority as well as the Ministry for Environment, Energy and Enterprise, with a view of developing a financial instrument to support the faster diffusion to electric vehicles (EVs), particularly commercial EVs and related recharging infrastructures.

Figure 3: Total GHG emissions by sector in MtCo2e



Source: European Environment Agency

During 2023, the Bank is committed to continue promoting and financing environmentally friendly projects and activities. In line with the ESG strategy that the MDB is currently devising, green financing will be prioritised further to encourage the growth of the green economy, reduce the negative impact of human activities on the environment, and promote sustainability.

6 EU progress on climate action – How are the Member States doing? Climate Action in Malta, European Parliamentary Research Service, October 2021.

SPECIAL TOPIC II
TECHNICAL ASSISTANCE FROM THE EUROPEAN COMMISSION ON EQUITY AND START-UP FINANCIAL INSTRUMENTS

During 2022, the MDB continued to collaborate with the European Commission in terms of the Technical Support Instrument (TSI) which is the Commission's instrument to provide technical support for reforms in EU Member States. In line with MDB's goal to continue to broaden its range of promotional facilities, the Bank submitted a request for the provision of TSI advisory services and assistance in the designing of new financial instruments focusing on equity and start-ups. Following this request, the Commission in 2021 engaged a local firm through a competitive selection process - to assist the MDB in this project.

This TSI assistance commenced in September 2021 with the main objectives of the project being the design and launch of two new financial instruments in the Maltese market, one being an equity based financial instrument for SMEs and the other being a financial instrument to support start-ups. The assistance is also aimed at positioning the MDB as a key stakeholder in contributing to a better coordination of the various equity participation schemes and incentives in place for SMEs and start-ups, thereby improving the overall effectiveness of the current ecosystem.

In order to cater for the various financing needs along the business lifecycle, and to complement the existing credit markets in Malta, the MDB wishes to contribute to establishing a structured ecosystem to foster risk capital financing in Malta. Whilst there have been several attempts to address this gap in Malta, the initiatives in this regard have tended to be rather fragmented, resulting in a lack of coordination. Consequently, the volume of equity financing for SMEs has failed to reach the desired levels, generally leading to a lack of tangible results in this field.

Malta's business landscape is uniquely characterised by an above-average presence of micro enterprises, employing less than 10 employees. Based on statistics issued by the National Statistics Office, such enterprises account for more than 97% of all businesses registered in Malta, with a further 2% of businesses classifying as small, with a staff complement of between 10 and 49 employees. Understanding the business environment prevalent in Malta is key to the operations of MDB and is of critical importance to enable the Bank to address significant and pressing market failures as well as sub-optimal investment situations.

Malta consistently ranks among the weakest countries in the European Union for the level of investment directed at research and innovation (with only 0.66% as a percent of GDP in 2020). The financing of research and innovation (R&I) activity is essential to drive long term value added economic growth, both at a national and European level. This market gap in Malta is further exacerbated by various challenges faced by SMEs, which prevent them from reaching their full potential. This is partly owing to an underdeveloped and dispersed equity market, which steers organisations in the direction of high levels of indebtedness.

The above-mentioned conclusions and statistics confirm that the majority of Maltese businesses are microenterprises, with a substantial presence of start-ups, hence reinforcing the need to target R&I initiatives and support schemes to SMEs and start-ups (being the prevalent cohort).Furthermore, findings acknowledge the presence of several existing initiatives in the market (albeit not specifically addressing equity market gaps) but identify the limited coordination among stakeholders as one of the reasons for their limited success in bridging the persistent market gaps.

Purpose of study
The objectives of the TSI project can be categorised into two key components, namely:

(a) To help the MDB design and introduce two new financial instruments to the Maltese market, these being;
i) An equity based financial instrument for SMEs and
ii) A financial instrument to support start-ups.

(b) To set out recommendations on the role MDB may adopt to act as a catalyst to facilitate cooperation within the equity and start-up support ecosystem in Malta with the objective of integrating the various fragmented initiatives in Malta.

Figure 1 shows the workstream of this study, which was split into four stages leading to the final recommendations.

Figure 1 – Study workstream

- Current-state assessment of existing public and private initiatives in Malta associated with equity-based support to SMEs and support to start-ups, identifying the gaps in the Market.
- Detailed analysis of six best-practice instruments in selected EU countries that could serve as possible benchmarks for MDB. The key attributes were evaluated to determine which characteristics could be most suitable to address gaps in the Maltese market.
- Noted minutes from one-on-one stakeholder meetings. Organised an event for all stakeholders which allowed for the MDB to network and exchange of ideas with potential key partners.
- Took all information gathered in the gap analysis, alternative best practices, and stakeholder feedback workshop into account and outlined recommendations on feasible options for equity FIs the MDB may consider adopting.

Main deliverables of the TSI study

The following key actions and deliverables were undertaken and prepared during the separately identified components of the project:

- Performed a gap analysis on current support available for start-ups and SMEs in the Maltese market.
- Organised one-on-one session with 25 key stakeholders to obtain insight on limitations of the current ecosystem and possible future enhancements.
- Compiled benchmarking report outlining the design of six other financial instruments adopted in EU jurisdictions namely, Greece, Germany, Hungary, Czech Republic, Bulgaria and by the European Investment Bank (the European Angels Fund).
- Organised an event titled InvestMT which included presentations from the European Investment Fund and Századvég Konjunktúrakutató Zrt (a preferred advisor to the Hungarian Development Bank). It also included a panel discussion among key stakeholders. The session also served to provide market stakeholders a chance to view what work had been undertaken, possible options being contemplated and served as a platform to share their views.
- Set out recommendations for the design of two new financial instruments (FI) based on gaps identified, best practice extracted from the benchmarking exercise and based on stakeholder feedback received
- Set out recommendations for the role MDB may adopt within the start-up and SME support ecosystem.

Recommendations on two new equity financial instruments

The key recommendations of the TSI study are summarised in Figure 2 below.

Figure 2: Proposed financial instruments

	Instruments	Instrument objectives
Start-up FI	Accelerator + seed financing	• Address the financing gap at seed financing stage • Provide smart money by ensuring technical assistance is available alongside financing • Enhance the support framework for start-ups • Strengthen the start-up pipeline
SME equity FI	Commercialisation + Growth	• Improve availability and access to risk capital finance • Promote investment in innovation to support growth • Provide a follow-up funding route for start-ups in the growth stage of the business lifecycle

The TSI study recommended that the proposed financial instrument to support start-ups will take the form of an **accelerator and seed financing instrument:**

Accelerator stage will focus on providing entrepreneurs with the opportunity to research, assess and develop an initial concept. During this stage the entrepreneurs will have access to incubator services and mentoring; and

Seed stage will focus on providing (i) follow-on financing to participants in the Acceleration stage; and (ii) seed financing to other eligible start-ups which have not participated in the Acceleration stage, as long as the initial concept is developed.

In this way, this financial instrument would be able to address the financing gap at seed financing stage, provide smart money by ensuring technical assistance is available alongside financing, enhance the support framework for start-ups and strengthen the start-up pipeline.

For the second financial instrument targeted towards SMEs, it was recommended to take the form of a ***commercialisation and growth investment fund*** targeting an equity and quasi-equity investment in SMEs in the commercialisation and growth stage of their business lifecycle. In this way, this financial instrument will improve the availability and access to risk capital finance, promote investment in innovation to support growth and provide a follow-up funding route for start-ups in the growth stage of the business lifecycle.

The TSI project involved a number of detailed deliverables including the preparation of:

- a detailed report outlining the design of the proposed Accelerator and Seed financial instrument. This included a detailed design of the key attributes of the instrument, the envisaged role and responsibilities of the intermediary and state aid considerations.
- a second detailed report outlining the design of the proposed SME Equity financial instrument. This included a detailed design of the key attributes of the instrument, the envisaged role and responsibilities of the intermediary and state aid considerations.
- a report outlining a detailed action plan for the MDB and other stakeholders to pursue the implementation of the two proposed financial instruments. It also outlined in further detail the envisaged role and objectives of the MDB within the start-up and equity support ecosystem. Moreover, it outlined intermediate actions the MDB may adopt to address other market gaps identified which would complement the two proposed instruments.

Role of MDB in the implementation stage

Given the relatively short history of the MDB, it has been focusing primarily on guarantee and loan facilities while postponing its possible direct involvement in equity participation to a later stage when it will have built sufficient capacity to engage in such activities. While the MDB does not yet have the resources to implement the two equity Financial Instruments proposed in the TSI study in the short to medium term directly through its existing structure, this study supports MDB's significant role in the development of a national equity ecosystem. Given its remit to address identified funding gaps in the Maltese market and the significant work already undertaken in the analysis and design of the two new equity financial instruments, the MDB will strive to take the proposed instruments forward possibly in a role of coordinator and promotor at a national level through a process of consultations and collaboration with relevant stakeholders with a view to addressing more effectively gaps identified in the high-risk debt.

In line with its remit, the TSI study concludes that the MDB, given its experience and capacity in implementing debt-based financial instruments, is better positioned to leverage its resources to roll out blended instruments in the quasi-equity space.

Moreover, to avoid further fragmentation and increasing complexity of the support landscape, it will be imperative for the Bank to assess the complementarity between its existing instruments and any new quasi equity instruments launched. It should also coordinate with other stakeholders offering complementary support measures and avoid duplication with other schemes operated by other entities.

COMMISSION'S DECISION ON MDB'S BROADENED REMIT

In August 2016, the European Commission had approved MDB's first remit of activities backed by State aid support of up to €255million for a period of 3 years. In December 2019 the MDB was advised that although the Commission had not yet issued a formal position on the future remit of the MDB, the Commission Services consider that the Bank may continue to implement State aid measures that comply with the General Block Exemption Regulation (GBER), de minimis and operations that fall within the scope of aid measures notified to and approved by the Commission.

Following various exchanges with the Commission since early 2019, the Maltese Authorities in May 2021 formally notified the Commission on the modified proposed set-up of MDB's remit of activities and the related extended aid measures. On 12 December 2022, the Commission informed the local authorities that it approved an increase in the State aid envelope supporting MDB's projected remit of intervention for the next five years. In terms of this approval, the maximum State aid that may be provided by the Government to the MDB on non-commercial terms for its operations in the form of capital, guarantees and tax measures for the five-year period ending 31 December 2027 is of €678 million, an increase of €423 million compared to the first remit of 2016.

The Commission concluded that the measure is necessary and appropriate to improve access to finance for sectors or companies that have difficulties in obtaining sufficient finance from the market. Furthermore, the Commission found that the measure is also proportionate as MDB will limit its interventions to addressing established market failures, notably investments in areas suffering from insufficient private funding. Finally, the Commission concluded that the measure has sufficient safeguards to avoid undue negative effects on competition and trade in the EU. On this basis, the Commission approved the Maltese measure under EU State aid rules.

From a business strategy perspective, this broadened remit will allow the MDB to continue rolling out financial instruments not only under State aid measures that are compatible with GBER and de minimis Regulation, but also under the Agricultural Block Exemption Regulation (ABER), the Fishery Block Exemption Regulation (FIBER), the Guidelines on State Aid for climate, environmental protection and energy (CEEAG), or any other aid guidelines, or by way of a Notification, unless offered on terms consistent with market conditions. Thereby, this approved State aid remit will help the MDB to continue enhancing its role in supporting a broader cohort of Maltese businesses and segments that may face challenges in accessing finance.

RISK MANAGEMENT STRATEGY

The mission of the MDB is to contribute towards sustainable economic development that benefits the Maltese people by promoting inclusive and environmentally sustainable economic growth and infrastructure development. The mission reflects the statutory purpose provided for in article 4 of the Malta Development Bank Act.

The MDB fulfils its mission inter alia, by providing promotional investment and financing. Through this activity, the MDB extends credit and/or guarantees third-party loans extended by the MDB's implementing partner banks. This activity exposes the MDB to financial and non-financial risks. Accordingly, the MDB recognises that effective risk management is imperative to sustaining a sound risk culture, which is characterised, among others, by a high level of awareness concerning risk and risk management in the organisation.

The MDB manages its financial and non-financial risks effectively by employing the three lines of defence model, in line with industry best practices. This model allocates responsibility and accountability for risk management across all units and all levels of staff within the organisation, while ownership is retained by top management. The second line of defence is supported by a fully functional Risk Management Function which analyses, assesses, measures risks, develops risk-management related policies, procedures and methodologies, as well as supervises and monitors their implementation. It also recommends exposure limits and monitors the adherence to the adopted exposure limits, gives recommendations and suggestions for adequate risk management as well as reports risk to the Board and relevant committees.

ENTERPRISE RISK MANAGEMENT

The MDB's enterprise risk management framework is designed to manage the Bank's risk-taking in the context of its mission and strategy. The enterprise risk framework takes into account the Bank's risk-bearing capacity, its risk appetite, and minimum quantitative requirements for capital and liquidity.

The willingness to take risks is described in the Bank's Risk Appetite Framework with the purpose of aligning the Bank's risk-taking with the statutory requirements, strategic business objectives and capital planning. The Risk Appetite Framework provides a clear articulation of the high-level principles for the Bank's risk-taking, risk mitigation and risk avoidance.

The Risk Appetite Framework is reflected in the Bank's risk management policies which set out the principles for the management of MDB's key risks, covering credit risk, interest rate risk, operational risk and liquidity risk. During the year some of the policies were reviewed to further enhance the internal processes and controls. The review process also entailed the development of a new risk metric and a bespoke risk register to better gauge and monitor the Bank's risks.

CREDIT RISK

The MDB controls credit risk through the Credit Risk Framework, which covers all phases of the credit processes from the development of new products to request for new loans, monitoring of borrowers and final loan repayments. The Credit Risk Framework defines the internal control systems to control credit risk with an objective to act preventively. As the management of credit risk is an important factor of the MDB's business strategy, the MDB developed a comprehensive Credit Risk Framework which includes the following documents:

- A *Credit Risk Policy* that is designed to achieve satisfactory and sustainable long-term performance, combining a growing credit exposure with an acceptable level of credit quality so as to seek to result in a low incidence of bad debts. The Credit Risk Policy provides clear guidelines for the process of extending credit commensurate to the Bank's credit risk appetite and thereby provides a clear statement of the parameters within which most of the Bank's lending decisions will fall.

- A *Risk Assessment Framework* that prescribes a structured risk assessment process that is practical, sustainable and easy to understand. This ensures that the risk levels of the borrowers are within the defined tolerance thresholds without being overcontrolled or forgoing desirable opportunities.

- A *Risk Assessment Criteria* (RAC) for Guarantee-only schemes, SMEs and Large Enterprises, and Infrastructure Project Finance. The purpose of the RACs is to have an internal rating system that identifies the level of risk associated with the credit exposure in order to facilitate the management of each relationship.

- A *Credit Risk Mitigation Policy that* supports effective and intelligent risk decisions such that the Bank's credit risk management objectives are achieved. Accordingly, this policy sets the Bank's credit risk mitigation measures which are ancillary to, and complement, core credit risk considerations to ensure good and responsible lending.

Interest Rate Risk arising from non-trading activities

The principles for managing the Bank's interest rate risk are defined in the Interest Rate Risk Policy and in the decisions and conclusions made by the Board of Directors, Risk Committee, and Asset and Liability Management Committee.

The Interest Rate Risk Policy provides for the governance and measurement of interest rate risk arising from non-trading activities. It also provides for the management of interest rate risk in a way that is consistent with MDB's relevant risk appetite statement and corresponding risk indicators. For the purpose of measuring and monitoring interest rate risk, the MDB analyses the current or prospective risk to the Bank's capital and to its earnings, arising from the impact of adverse movements in interest rates. In addition to the harmonisation of interest rates applied to sources and placements, current market conditions and development projections for basic market indicators are also monitored.

OPERATIONAL RISK

The Operational Risk Management Framework establishes the principles for operational risk management. The system structure of management and responsibility has been set up, the approach to the calculation of the capital requirement for operational risk has been defined and the reporting system has been established.

The Risk Management Function maintains a bespoke Risk Register in line with the Operational Risk Management Policy. The Risk Register comprises of a list of identified risks, linked to the business objectives whose success would be threatened if the risk materialised. A systematic process was carried out to identify risks and assess their expected impact and likelihood. The events were then mapped onto a two-dimensional impact-likelihood matrix to rank these risks. The overall risk score is used to sort the risks so that the list runs from the most significant to the least significant.

LIQUIDITY RISK

The principles for the management of the MDB's liquidity are articulated in the Treasury Management Policy with decisions sanctioned by the Board of Directors or the Risk Committee as appropriate and in line with the provisions of the said policy. For the purpose of managing liquidity risk, the MDB retains callable balances with the Central Bank of Malta and reputable financial institutions as well as a maturity ladder of short-term deposits and other money market instruments such as Malta Government Treasury Bills.

The MDB monitors planned and forecast financial commitments closely and ensures that funds are available for the timely settlement of these obligations as well as capital and operational expenditure. In order to ensure effective management of liquidity, the MDB operates a liquidity ratio that is defined as the ratio of the projected net cash position as at the end of the month, to the sum of the 12-month projected net cash outflows. The Bank is prohibited by the MDB Act from taking retail deposits.

OPERATIONAL STRATEGY

CORPORATE SERVICES

The Corporate Services function ensures that operational activities and services are aligned with the corporate strategy to sustain the business needs of the Bank in a proficient and timely manner. This is achieved through strong stakeholder relationships and coordination with all business areas of the Bank.

Due to expanding staff numbers, early in 2022 the MDB decided to relocate to its new premises in Floriana rather than continue to operate from the small premises in Valletta. Refurbishment of the Floriana premises had started a year previously. The Administration and Procurement Department ensured that services and products met expectations regarding operational exigencies. The Human Resources Department sustained the recruitment of additional talent whilst supporting the well-being of all employees. The Records and Archives Management Department spearheaded initiatives to strengthen the storage, safekeeping and archiving of corporate documents.

Policies

The policy development process supports MDB's capacity expansion through the documentation of policies and procedures. During 2022 several policies were reviewed whilst new policies were approved by MDB's Board of Directors. MDB's Procurement Policy underwent considerable updates and changes to achieve even greater alignment with the EU Public Procurement rules. The policy now provides several templates and process flows that allow for the appropriate interpretation and implementation of the processes involved.

The Human Resource policy regime was further strengthened by the introduction of the Payroll Policy, Training and Development Policy, and the Health and Safety Policy. Each policy supports the MDB direction to foster its employees' development and well-being. During the policy periodic review, the Equality Policy was also reviewed and refreshed. These policies were further strengthened by developing operational procedures.

A policy was developed to cover the Records and Archives Management function of the MDB. This policy outlines the critical concepts and processes that will ensure that the Bank's records are managed with the appropriate level of security and properly stored for future reference. Furthermore, the policy also outlines the basic principles for the development of an electronic documents' repository.

Human Resources

The Human Resources Department supported the business strategy through a strong framework of policies and procedures. The Department now has a dedicated office in the new premises to organise the physical documents and implement a higher level of security in protecting personal records. The Department also continued to develop and review its policies.

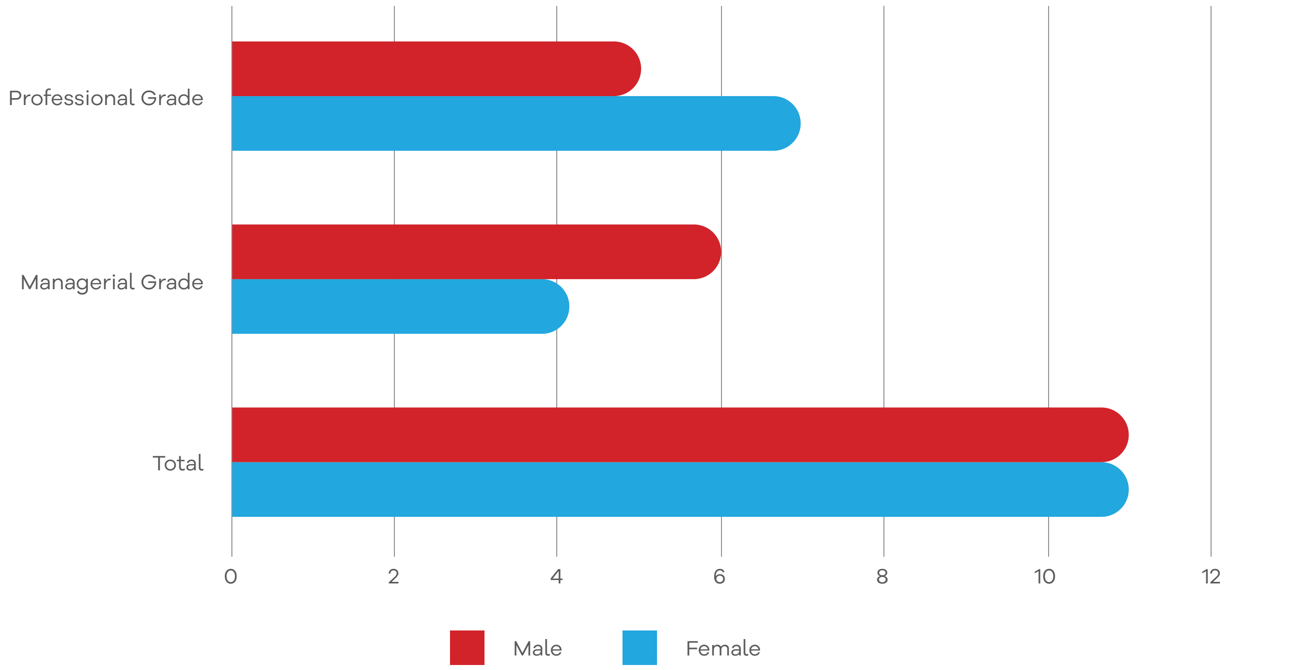
Recruitment

As MDB's business continues to expand, the need to source the top-notch talent continues to feature highly on the Bank's agenda. Several calls for recruitment were issued in 2022. These have resulted in the recruitment of a Senior Compliance Officer, Senior Internal Audit Officer, a Risk Officer, and a Credit Officer.

During 2022, the MDB recruited three females and two males. Three of the newly recruited employees filled new positions, whilst two recruits filled positions that had become vacant after previous incumbents resigned.

The headcount at the end of the year stood at 22, with an equal number of males and females. Chart 1 shows the gender composition for each grade.

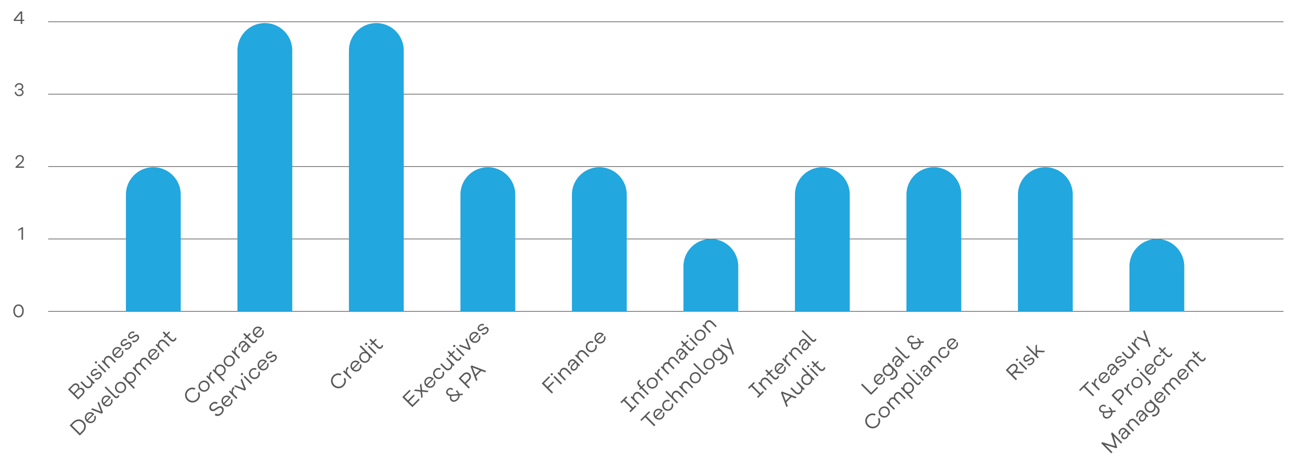
CHART 1: TOTAL NUMBER OF EMPLOYEES PER GRADE AND GENDER



On 30th June the Board of Directors appointed Mr Paul V. Azzopardi as the Bank's new Chief Executive Officer, taking over from Mr Rene Saliba following the latter's retirement. Mr Azzopardi had joined the Bank in February 2020 as Deputy Chief Executive Officer.

The staff complement in each department as at end of 2022 is highlighted in Chart 2.

CHART 2: EMPLOYEES PER DEPARTMENT



The Management team as at the end of 2022 was made up of the following:

Mr Paul V. Azzopardi, Chief Executive Officer
Mr Saviour Busuttil, Chief Corporate Services Officer
Mr Joseph Darmanin, Chief Business Development Officer
Ms Joanne Dimech, Chief Finance Officer
Ms Moira Falzon, Chief Internal Auditor
Mr Glen Lethridge, Chief Information Technology Officer
Mr Tyrone Mizzi Navarro, Chief Risk Officer
Dr Bernadette Muscat, Chief Legal and Compliance Officer
Mr Kevin Vassallo, Chief Projects and Treasury Management Officer
Ms Maria Xuereb, Chief Credit Officer

Training

The Bank's capacity to draw people and build highly technical business teams is crucial for its success. The Bank's Training and Development strategy has now also been formally reflected in a policy which was approved by the Board of Directors in 2022. Furthermore, the Bank develops and updates talent which contributes to a more mature and professional workforce. Training has become ingrained in the corporate culture of the MDB, with training sessions being held regularly, both internally and from other professional sources outside the Bank, consisting of webinars and seminars, conferences and talks. Through such training, staff members are given the opportunity and the necessary tools for self-development and professional growth on various aspects related to the Bank's activities.

MDB staff attended more than 300 hours of training averaging around 13 hours of training per employee, including compulsory continuing professional education courses. The topics covered several business areas including Finance, Anti-Money Laundering, GDPR, and Law amongst others.

Premises

March 2022 saw the first MDB staff members moving into the new premises in Floriana after all the major works were completed. The new premises are housed in an old historical building which dates back to the late eighteenth century. Renovations within the building included extensive external works as well as internal modifications and improvements. Safety at work is, and will remain, a priority for the Bank, hence great attention was given to the installation of fire doors, the strengthening of the lift structure, the opening of evacuation routes, a new fire alarm system, emergency lighting, as well as a full renovation of the basement area. The heritage features of the building were respected and retained, such as a large old kitchen with stone washing basins and stoves. This provides a relaxing setting for staff members to enjoy their short breaks in a pleasant, comfortable, canteen-like fashion. Rooms from a small adjacent building were integrated into the main premises.

The premises were officially inaugurated on 23 November 2022 by the Hon. Prime Minister, Dr Robert Abela, in the presence of the Minister for Finance and Employment, Mr Clyde Caruana, and other esteemed guests who joined the Bank's staff for this memorable occasion.[7]

7 Detailed information on the Prime Minister's visit is provided in the Significant events section on page 79.

Records and Archives Management

The Records and Archives Management Policy establishes the framework for the Bank's records management programme, outlining the responsibilities and compliance requirements expected by its staff. The Records and Archives Management Office (RAMO) has built an extensive repository of the Bank's records. It ensures that accurate and complete records are maintained, in support of the Bank's organisational and statutory requirements. A knowledge database has also been set up to act as repository for training and specialized knowledge.

Apart from the physical repository of records, RAMO introduced an electronic document management system across the Bank to enable business areas to retain accurate up-to-date records of their activities in line with the Records and Archives Management Policy. This process establishes best practices that would allow effective search results whilst ensuring that documents are only available on a need-to-know basis. The system also delivers a platform where employees can collaborate efficiently together on shared documents and projects.

RAMO has continued to develop a centralised repository for contract management. The database has become the key component of contract renewal and management at the MDB. Business areas are supported by providing periodic notifications of contract expiry and also provide a centralised repository of contract information.

The Office is the custodian of the Bank's Policies and Procedures. Through its electronic management system, employees now have a holistic understanding of the policies and procedures in place. RAMO works with the business areas to ensure the timely review of such polices.

Maintaining an appropriate record of projects' progress is critical for the MDB. To this end, RAMO manages the time measurement programme used to determine the time dedicated to specific projects and policy development. The Bank uses such time logs to enhance operational efficiencies as well as to feed into its activity-based project cost accounting system.

FINANCE FUNCTION

Finance is a key function within MDB, having as its main objectives the effective, efficient, and economical internal control and financial reporting system.

During 2022, the Finance Department has continued to focus on enhancements in the controls and process workflows with the aim to maintain accurate, timely and reliable record-keeping and reporting processes. During the year, the Finance Department documented the Manual of Financial Procedures. Various enhancements were implemented to enable the preparation of comprehensive and timely financial reports and identification of expenditure control initiatives supporting the Bank's continuous drive for operational excellence.

The Finance Department measures the Expected Credit Loss (ECL) provisions and presents recommendations to the Audit Committee regarding changes to the expected credit loss provision including material judgements, decisions and management overlays. It ensures that sufficient capital reserves are maintained to allow for potential losses resulting from credit risk.

In order to strengthen its ECL framework, during 2022, the Department developed the Expected Credit Loss Policy which sets out the accounting practices and policy choices with respect to the recognition and measurement of impairment allowances for the Bank's portfolios of financial instruments. The Bank has implemented a structured process in respect of the determination of staging of its credit exposures and monitoring of borrowers' delinquency status as prescribed by IFRS 9. The new staging procedures are intrinsically based on the credit assessment and scoring system outlined in the Credit Policy and enable the Bank to obtain visibility to and comfort on the staging of all its credit exposures. During the year, the Bank enhanced the mapping of the probability of default to internal credit grading on the basis of domestic non-financial corporate borrowers' delinquency stages in order to determine adequate loss provisions associated with the Bank's portfolios of loans and financial guarantee exposures.

The Finance Department prepares the annual budget which serves as a monitoring tool for steering operations in line with the agreed strategy of the Bank. The Budget Policy governs how the Bank implements and plans its budgetary processes. The performance monitoring system of budget vs actual variance analysis further supports the Board of Directors and management in executing MDB's strategic objectives.

In response to the MDB's sustained initiatives to provide additional lending capacity through the provision of new risk sharing schemes intermediated through partner banks as well as the provision of direct loans to finance large infrastructural projects and emergency liquidity, the Finance Department has continued to provide the necessary support to enable the timely execution, settlement and recording of payments and loan transactions.

The Finance Department is also responsible to ensure the timely submission of statutory and prudential regulatory reports in compliance with the MDB Act. Moreover, the Finance Department provides oversight of daily operational controls and procurement processes to ensure risks are properly managed.

As MDB aspires to become an implementing partner of the InvestEU, the Finance function is well-positioned to embrace further challenges in the context of enhanced reporting requirements.

SPECIAL TOPIC III
EMBRACING ESG PRINCIPLES

While traditionally companies have focused on measuring performance indicators such as turnover, costs, and other financially related measures, organisations nowadays are also increasingly adopting measures that show their impact on the environment, local communities and topics such as diversity and employee well-being.

Committing to an Environmental, Social, Governance (ESG) strategy is gaining importance for all types of businesses and institutions as investors, stakeholders, and customers are placing higher importance to ESG practices. ESG is a collective term for measuring a business's impact on social and environmental issues and its governance and performance beyond simply generating revenue or making a profit.

During 2022, ESG became a significant area of focus for MDB's Board of Directors and management team. The Bank is actively working on schemes that will support business undertakings to contribute to Malta's target of a 19% reduction in greenhouse gas (GHG) emissions by 2030 and net zero GHG no later than 2050.

The MDB is at the beginning of its ESG journey, which requires long-term planning, effort and commitment. To this end, the Bank is committed to develop an ESG Strategy by the end of 2023.

This strategy is of a dual nature: One aspect shall focus externally on a review of guidelines covering credit and risk assessments of the Bank's new promotional schemes which shall be fine-tuned to give greater emphasis to ESG considerations. The other aspect is more inward-looking, focusing on internal measures aiming to embrace ESG principles. This section deals primarily with the latter aspect.

Since its inception, the Bank's goals have focused on strong governance and providing services that are directed at developing Malta's economic growth whilst considering social domains through environmentally friendly operations.

A key part of the MDB's governance is the establishment of policies that regulate its human resource management, processes, and services. Whilst key policies covering human resources such as Code of Conduct and Equality policies were already established, in 2022, a new Health and Safety Policy was approved by the Board of Directors. The policy was launched in line with the move to the new premises. In developing an ESG programme, the MDB is also focusing on establishing an ESG team to coordinate activities that would spearhead carbon neutral or offsetting initiatives.

Gender equality is also considered a key principle of the MDB. Specific policies cover the Bank's direction on equality and maintaining a work environment totally free of harassment. Furthermore, the Remuneration Policy establishes equal pay for equal work principles.

The refurbishment of the new premises took into consideration environmentally conscious solutions. The premises houses a large cistern which was thoroughly cleaned from debris and adapted as a second-class water reservoir. Rainwater and reverse osmosis wastewater are directed to the cistern. This water is then pumped around the building to provide second-class water to the rest rooms. The volume of water collected is also being monitored so that key indicators can be monitored in the future.

Original wood apertures that were installed in the premises which could not be restored were replaced by Unplasticized Polyvinyl Chloride (UPVC) having a similar aesthetic design. These new UPVC apertures also provide superior heat and cold retention, as well as soundproofing, thus improving the environmental efficiency of the building. It is planned that some of the remaining wood apertures would also be assessed for replacement to further improve the energy efficiency of the building.

Light fixtures contribute to energy consumption. In fact, during the refurbishment of the new premises, all electrical infrastructure has been replaced by new LED fixtures that consume considerably less energy. Furthermore, all electrical appliances are rated at the highest efficiency levels. The control of electrical lights also limits unnecessary wastage of electrical power when offices are not in use. External façade lights are only switched on during specific periods to limit energy consumption. Furthermore, components of the water treatment system are only switched-on during office hours.

Waste management practices were established as soon as the employees started using the new offices. The MDB has adopted waste separation at source by providing easily accessible bins. These bins are clearly marked thus enabling employees to select the appropriate bin for the type of waste product. This process facilitates collection and disposal as it provides a standard approach. The method also allows for monitoring waste usage.

The above-mentioned examples are clear signs of the directions and decisions that have been taken internally by the MDB over the years to embrace ESG principles. The ESG Strategy will formalise the policies, the decision-making processes, and the monitoring and reporting aspects.

At its basis, the ESG Strategy will be split into five distinct stages (see Figure 1). These stages will form the backbone of an integrated strategy which will have the ability to identify and manage exposure to material ESG risks, and to provide evidence to the senior management of how different factors can affect decisions.

Figure 1: MDB's ESG Strategy Stages

Stage 1: Identify key material issues to be addressed to attain a sustainable business model.

Stage 2: Prioritisation process: defining short and long-term priorities to address gaps, risks, and leverage new opportunities.

Stage 3: Sustainability map to execute the strategy and policy.

Stage 4: Implementation process, incorporating and aligning sustainability principles with strategic goals into all management levels.

Stage 5: Application and evaluation of Key Performance Indicators initiatives and measurable targets to monitor and evaluate progress.

Looking forward, the MDB during 2023 will be establishing this baseline for its ESG Strategy and will be setting goals for improving its operations. The Bank will also be developing a programme of activities designed to meet these goals. In developing these activities, and to ensure effective implementation, the Bank will involve its staff, suppliers, and all other relevant stakeholders in the process. Transparency and openness will remain at the heart of MDB's ESG strategy, and progress will be fully communicated.

INFORMATION TECHNOLOGY

Information technology is a critical enabler for the MDB to achieve its corporate objectives. In 2022, one of the priority areas of the IT Department was to ensure that the provision of technology services at the Bank's new premises in Floriana was fully functional and capable of withstanding demands from the full staff complement who returned to work onsite on a regular basis after working remotely for around two years due to the pandemic. The Bank also invested in setting up videoconferencing systems in three dedicated areas within the new premises, thus offering staff a flexible setup for more effective collaboration, both internally and with external parties. The MDB also continued to evaluate ways to optimise its operations. In fact, in 2022 a selection of end-user devices were successfully upgraded to more recent technology and work commenced on a full redesign and implementation of a new website. These activities will continue in 2023.

From an information security perspective, various initiatives were conducted throughout the year. Two major activities consisted of the implementation of a two-factor authentication mechanism on the Bank's loan management system for stricter access control and penetration testing for all IT equipment hosted within the new premises. These penetration tests are intended to identify, and subsequently rectify, any security vulnerabilities or misconfigurations on core hardware infrastructure, and thus served to enhance the Bank's overall security posture. Further penetration testing activities are planned for 2023, targeting specific business solutions rather than hardware infrastructure, to ensure that the Bank's systems are appropriately protected from active threats.

The MDB strengthened its internal governance standards with the introduction of more IT-related policies and procedures in line with best practices. The Data Management policy was implemented to preserve data integrity, confidentiality and availability. The objective of the policy is to ensure that appropriate measures are taken by all staff to protect information and information processing systems against unauthorised use, modification, disclosure and destruction, whether accidental or intentional. The policy is supplemented with detailed procedures on how to consistently manage data across the organisation at each stage of its lifecycle, namely, creation/acquisition, storage, usage and sharing, archiving and disposal.

A second area of great importance to the Bank was the formalisation of the Business Continuity Policy. The objective of this policy is to communicate responsibilities and act as guiding principles for MDB staff to prepare for, and effectively respond to, business interruption whilst safeguarding the assets of the Bank, preserving safety of its staff, upholding its reputation and ensuring continued operations of critical activities through times of major crisis. As a key contributor in this regard, the IT Department formalised detailed procedures on how to restore service interruptions from a technology perspective, ranging from a worst-case scenario that may affect the Bank's core infrastructure to focused recovery of individual IT components and business solutions.

PROJECTS AND TREASURY MANAGEMENT FUNCTION

In the year under review, the Treasury Department sought to employ the Bank's excess liquidity in eligible financial instruments as defined in the Bank's Treasury Management Policy which aims to maximise return whilst balancing out the related risks of liquidity and credit. Excess liquidity arises from a mismatch in timing between (a) cash inflows from the Bank's funding sources and repayment of money lent out, and (b) cash outflows related to disbursements of loan assets approved by the Board and repayments of money borrowed by the Bank. The Treasury function was also involved in the liability side of the Bank's balance sheet with respect to loan agreements entered into with international development institutions, the cost thereof, and the timing, repayment, and application of funds drawn under such facilities.

PUBLIC RELATIONS FUNCTION

An Expanding Communications Strategy

Throughout the year in review, the MDB has increased its efforts to raise awareness and visibility of the role of the institution itself, the products it offers through the intermediary banks, the proposition of the Bank as a workplace of choice and its stream of activities.

Over the twelve months under review, the Bank has issued 11 press statements, in English and Maltese, detailing information relating to its schemes, besides providing comments and replies to specific enquiries by Parliament and the press. Throughout the year, the Bank increased its presence on different media sources, including audiovisual, print, online and digital media.

Aware of the increased use of professional social media by businesses and key stakeholders likely to be interested or benefit from the MDB's offering, the Bank has significantly increased its presence on LinkedIN, with a regular stream of posts attracting in excess of 38,000 impressions, with increasing levels of engagement. In less than two years since the creation of this page, it has attracted a regular following, consisting mostly of financial service practitioners, lawyers, officials from authorities and other similar stakeholders.

In parallel, with the launch of the previous year's Annual Report, the Bank also carried out a two-week online campaign targeting key news portals, focusing on the main achievements of the previous year, together with highlights of the available initiatives and schemes. These informative banners were displayed over half a million times throughout a fortnight. Users who clicked on the MDB banners were able to access an informative leaflet with more in-depth information on the Bank's activities. Evidence of the impact of such a campaign is the direct correlation with the generation of additional interest in the Bank's LinkedIN account which experienced a significant increase of traffic throughout the performance of the campaign, with impressions exceeding by 300% those of previous months.

In addition to this, MDB officials participated at a steady stream of public events including conferences and fora hosted by key stakeholders to share information during debates, panels as well as through networking.

BUSINESS REVIEW

During the year under review, the MDB launched a record number of new programmes. As challenges related to the COVID-19 pandemic and its economic consequences on local businesses had started to subside in the latter months of 2021, it was expected that the economic environment will continue to improve in 2022. Nevertheless, this cautious optimism was curtailed by the outbreak of war in Ukraine in February 2022. The ongoing conflict, the associated economic sanctions against Russia and political uncertainty have created significant challenges for businesses, making it more difficult for them to operate and invest. To this end, the MDB was once again entrusted with a Government guarantee to introduce urgent liquidity support measures as part of a package in response to the Ukraine crisis.

However, the Bank also worked on a number of other fronts to ensure that the portfolio of schemes and instruments offered are mirroring the changing needs of the economy and hence the market gap they are meant to address. During 2022, the MDB worked closely with the Managing Authority for EU Funds in connection with the Bank's role as a vehicle for leveraging EU resources. This has led to the creation of a second financial instrument focusing on higher educational attainment.

Moreover, in 2022 the MDB worked on the introduction of two new financial instruments tailored to the specific circumstances of local business and prioritising those investment projects that aim to build a greener and more digitally oriented economy. The on-going consultation process with various stakeholders continued to reveal further gaps in the provision of financing for infrastructure projects and green investments. To meet the ambitious EU's 2030 and 2050 climate targets, substantial investment is needed, and this will require private capital to be unlocked. In this regard, the Bank's focus remains on projects with a strong social dimension, as well as those that contribute to the climate and digital transition, particularly related to green mobility.

This section of the report will offer an overview of the Bank's funding sources and provide an ex-post assessment of the schemes that expired in 2022 and an outline of the new financial instruments facilitated by the MDB. Furthermore, the analysis in this section attempts to shed light on the economic importance and implications of the Bank's products in the prevailing macroeconomic scenario.

FUNDING SOURCES AND GOVERNMENT GUARANTEE

Funding

The MDB's operations have been partly funded by the paid-up capital provided by the Government in terms of article 10 of the MDB Act.[8] After being launched in 2017 with an initial paid-up equity of €30 million, the Bank's paid-up capital was increased in line with its business plan by €10 million annually in 2019, 2020 and 2021 and by €20 million in 2022 to reach €80 million.

Together with its paid-up capital, the MDB's funding model also includes bilateral borrowing as a result of agreements entered into with international development institutions. Such funds are earmarked for on-lending to local operators, both in the SME segment as well as for economic operators and public sector entities engaged in infrastructural projects, particularly those that exhibit a social or environmental dimension. To this effect, the MDB is party to a loan agreement of €45 million with the KfW Group and another loan agreement of €60 million with the European Investment Bank under the Multiple Beneficiary Intermediated Loan (MBIL) programme. These funds are utilised by the MDB to finance the facilities to support SMEs, mid-caps and infrastructure projects by private and public-sector entities.

8 The MDB has an authorised share capital of €200 million. This stems from article 10(1) of the MDB Act. In terms of the First Schedule to the Act, €60 million were subscribed by Government as initial capital. The Board of Directors is empowered by article 10(3)(b) of the MDB Act to determine the paid-up capital of the Bank. The issued and subscribed share capital of €100 million by 2025 is a projection based on the Bank's business plan and accordingly is a function of its forecast economic activity

Government Guarantee

Article 5 of the MDB Act provides that the Government shall guarantee up to 100% of all the obligations of the Bank and up to 100% of the loans, facilities or guarantees issued by the Bank. In line with the indicative targets specified in the MOU signed between the MDB and the Ministry for Finance on 16 February 2018 in terms of Article 5(2) of the MDB Act, the Government Guarantee in favour of the Bank has been increased gradually in line with the Bank's business growth. At the end of 2022, it stood at €150 million. Some 60% of these guarantees have been earmarked to cover the two main international borrowing operations with the EIB and KfW, while the balance is intended for other prospective operations which the MDB shall be carrying out on its own account.

In addition to the above guarantees, in April 2020 the Government had issued another guarantee of €350 million specifically for the COVID-19 response facilities which the MDB is managing as agent on behalf of the Government. This same guarantee also served to back the Ukraine crisis response measures launched in 2022.

MDB FACILITIES ENDING IN 2022

During the year under review, three MDB financial instruments – the COVID-19 Guarantee Schemes, the Family Business Transfer Facility, and the Further Studies Made Affordable Scheme – came to an end as their term expired or the allocated amount was fully absorbed.

Family Business Transfer Facility

The Family Business Transfer Facility was the outcome of the first risk-sharing agreement that the MDB had signed with a commercial bank, following consultations with the Family Business Office. The scheme was launched in October 2018 in the context of a renewed emphasis by Government to foster and encourage family-owned businesses, including through a number of fiscal incentives in terms of the Family Business Act 2016. The facility, intermediated by BOV as Family Business Success, was designed to enhance access to bank credit in respect of family business transfers to the next generation within the family. Through this guaranteed instrument, the MDB contributed to partial credit risk protection on the lending portfolio of BOV. More specifically, the MDB provided a guarantee fund capped at €4 million which enabled the commercial bank to generate a loan portfolio of up to €10 million for such family business transfers. The MDB was guaranteeing 80% of each eligible transaction, subject to a capping of 50% at the level of the portfolio.

The take-up under the Family Business Transfer Facility was less than anticipated. In line with the pre-set applicability terms, when the facility's term of three years came to an end during 2022, only 2 facilities amounting to €98,000 were sanctioned. One critical condition in the original scheme was that eligible beneficiaries needed to first be recognised as family businesses by the Family Business Office, in accordance with the definitions of the Family Business Act. On the basis of a field research conducted in 2021, it appeared that such a condition was considered too onerous by prospective applicants could have been one of the main reasons why the scheme has not taken off as well as projected.

Further Studies Made Affordable

In collaboration with the Managing Authority of EU funds, the MDB had launched the Further Studies Made Affordable (FSMA) financial instrument in October 2019. This was the first MDB scheme directed to individuals and not business undertakings. Moreover, it was also MDB's first blended instrument, combining an interest rate subsidy with favourable lending terms. A total portfolio of €8.25 million was made available through the intermediation of Bank of Valletta (marketed as BOV's Studies Plus) which was the bank selected by the MDB after an open call for expression of interest in 2019. The portfolio was extended by a further €1.2 million, to €9.45 million in August 2021 to cater for the strong demand. This was possible by calibrating the allocation of funds between the interest rate subsidy and the guarantee fund.

By the end of 2021 it was evident that demand for such an important facility was significantly higher than the available portfolio. To this end, the Managing Authority secured additional EU financing for the MDB to implement a new scheme, the FSMA+. By then, 275 students had been supported under the FSMA scheme, with total loans reaching €9.2 million.

COVID-19 Guarantee Schemes

Since the onset of the pandemic, the Bank has supported businesses impacted by COVID-19 with a portfolio of three complementary instruments. The COVID-19 Guarantee Scheme (CGS) was launched in April 2020 with the purpose of guaranteeing loans granted by commercial banks in Malta to meet new working capital requirements of businesses facing cashflow disruptions. The second complementary facility was the COVID-19 Interest Rate Subsidy scheme (CIRSS) which further softens the terms of working capital loans extended by banks under the CGS. The third component was the COVID-19 Small Loans Guarantee Scheme (SLGS) intended to support smaller businesses by reducing the soft collateral in the form of personal guarantees for loans up to €250,000.

MDB's intervention through these schemes was crucial in ensuring that Maltese businesses survive the severe liquidity constraints they were facing due to restrictions brought forward by COVID-19. MDB's CGS was leveraging on a Government guarantee of €350 million and by mobilising commercial banks' liquidity into the flow of credit to the real economy, the MDB was able to provide a guarantee of 90% on loans granted by commercial banks, enabling the creation of a portfolio with a potential of up to €777.8 million in new working capital loans to all businesses, regardless of size or sector.

In view of the substantially reduced credit risk exposure for the intermediating commercial banks, the benefits from the MDB guarantee were passed on to the final beneficiaries. These included a higher volume of finance, lower collateral requirement, and lower interest rates. Another important benefit for the beneficiaries relates to the wide array of eligible working capital costs covered under the CGS; these comprise salaries, rental costs, energy and water bills and fuel, unpaid invoices due to a decrease in revenues, acquisition of material and stock for continuation of business, bond coupons on listed securities, expenses directly related to contracts which were cancelled or postponed and maintenance costs.

In the light of the unfolding COVID-19 developments which suggested that the impact of the pandemic was lingering longer than anticipated, in November 2021 the Commission adopted a limited prolongation of 6 months of the State aid Temporary Framework, until 30 June 2022. This allowed Member States to extend their support schemes and ensure that businesses still affected by the crisis will not be cut off from the necessary support. To this end, the MDB wrote to the Commission to extend the Bank's COVID-19 facilities in line with the amendments of the Temporary Framework. The Commission approved the prolongation of the CGS by a further six months until end June 2022.

Nine partnering commercial banks were accredited to intermediate the CGS, and cumulatively they have sanctioned more than €500 million in working capital loans. By end 2022 this figure contracted to €482.6 million due to loan repayments as well as the fact that a number of facilities were entirely or partly withdrawn by borrowers. The latter may reflect less liquidity needs on the back of improved business sentiment and an ameliorated economic environment. Overall, CGS loans have supported around 600 businesses, that collectively employ around 40,000 persons. The supported businesses range from hotels to large retail outlets, but also to many smaller firms from all economic sectors (more detailed information on the CGS is presented on page 63).

FINANCIAL INSTRUMENTS LAUNCHED IN 2022

Further Studies Made Affordable Plus (FSMA+)

The FSMA+ facility was launched in February 2022 and builds on the success of the FSMA scheme which was introduced in 2019 and which had generated over €9 million in new study loans. Thanks to the European Social Fund (ESF) and European Social Fund Plus (ESF+), the Managing Authority allocated €5 million to support MDB's FSMA+ scheme. Like its predecessor, the FSMA+ is a blended financial instrument, combining two components: a grant element in the form of an interest rate subsidy that makes the instrument more appealing for aspiring students, and a guarantee that enhances student access to bank financing by absorbing a substantial part of the risks. Close to half of this amount is being used in the form of a grant subsidising interest payments during the moratorium period. The MDB is again providing a First Loss Guarantee covering 80% of individual loans, capped at 25% of the commercial bank's portfolio, generating a multiplier of 5, meaning that a total portfolio of €15 million is available under the scheme. Following an open call for expression of interest, Bank of Valletta has been selected to intermediate the scheme.

The FSMA+ supports students or professionals who want to pursue studies in Malta or abroad on a full time/part time basis or through distance learning. The scheme can help finance accommodation, living and travelling expenses in addition to the tuition fees on very favourable terms. The benefits of FSMA+, marketed as BOV Studies Plus+, include no collateral requirements, a longer repayment term, a moratorium during the study period plus one year during which the student does not pay interest and capital, as well as a low interest rate during the remaining term of the loan.

Ukraine crisis support measures

The outbreak of war in Ukraine in February 2022 led to a global disruption in the supply chain of several key basic commodities, an upsurge in inflationary pressures and a slowdown in international economic activity due to geopolitical tensions and a spate of sanctions against Russia. The policy response of the European Commission was the launching in March 2022 of the Temporary Crisis Framework for State Aid to facilitate the introduction of support measures to assist businesses whose liquidity was negatively impacted by the Ukraine war.

Subsidised Loans Scheme

The Subsidised Loans Scheme (SLS) was the first emergency support measure which the MDB rolled out in response to the war in Ukraine. The SLS was launched in May 2022 following the approval of the European Commission under the Temporary Crisis Framework for State Aid.

In order to ensure food security in the wake of the war, the MDB is committed to assist importers and wholesalers to stock reserves of wheat and animal feeds for a longer period than normal. Such abnormal stock piling at the prevailing higher prices requires substantial liquidity at short notice. The MDB was appointed by the Government to take immediate remedial action by providing urgent liquidity support in the form of direct subsidised loans to companies undertaking the importation and wholesale of grains including but not limited to animal feeds and related products, affected by the current crisis following the invasion of Ukraine by Russia. The SLS offers a portfolio of up to €30 million loans to these undertakings for a term of two years. Loans under this measure also benefit from an interest rate subsidy of up to 2%. The scheme is available until 31 December 2023.

Liquidity Support Guarantee Scheme - Measure A

The Liquidity Support Guarantee Scheme – Measure A (LSGS-A) was the second emergency liquidity support measure being offered by the MDB as part of a package of measures in response to the Ukraine crisis. The LSGS-A was launched in June 2022 and is a €100 million portfolio-capped guarantee scheme intermediated by partner credit institutions to provide working capital loans to undertakings affected by the war. LSGS-A is backed by a Government guarantee of 90% on each loan, capped at 50% of the total portfolio volume, for a loan term of up to six years.

The LSGS-A is open to all types of undertakings operating in all economic sectors that have been adversely impacted by the repercussions of the Ukraine crisis. All loans sanctioned under the LSGS-A are eligible for an interest rate subsidy of up to 2.5% on the outstanding amount of the working capital loan, subject to a minimum interest payment by the borrower of 0.1%. The interest rate subsidy is payable during the first two years of the loan starting from the date of first disbursement of the loan. The LSGS-A is available until 31 December 2023.

Liquidity Support Guarantee Scheme - Measure B

Launched jointly with LSGS-A, the Liquidity Support Guarantee Scheme – Measure B (LSGS-B), is the third emergency liquidity support measure being offered by the MDB as part of a package of measures to address the Ukraine crisis. LSGS-B provides short term liquidity support for importers of fuel and oil to enable them to procure strategic fuel reserves in order to ensure security of supply and more stable prices.

The LSGS-B is a €50 million portfolio uncapped guarantee scheme intermediated by partner credit institutions to provide working capital loans to importers of fuel and oil. The Government backed guarantee covers 80% of each new individual loan, without a capping on the portfolio.

All loans sanctioned under the LSGS-B are eligible for an interest rate subsidy of up to 2.5% on the outstanding amount of the working capital loan, subject to a minimum interest payment by the borrower of 0.1%. The interest rate subsidy is payable during the first two years of the loan starting from the date of first disbursement of the loan. Similar to the other Ukraine crisis measures, the LSGS-B is available till end 2023.

SME Guarantee Scheme

In addition to the above-mentioned counter-cyclical emergency support measures, the Bank during 2022 also launched two new promotional schemes to stimulate new investment and growth by SMEs. One of the innovative features of these new schemes is that unlike the Bank's previous guarantee schemes for SMEs, these facilities are not capped at portfolio level and therefore they should prove to be much more attractive to the partner intermediating banks in terms of risk absorption capacity.

The first of these new measures is the SME Guarantee Scheme (SGS) which is an €80 million uncapped portfolio guarantee scheme launched in November 2022, with the MDB providing a guarantee of 80% on all loans in the portfolio of accredited credit institutions. Consistent with MDB's objective to improve access to finance and to diversify the financing options to SMEs, the MDB seeks to magnify the outreach of its promotional role by collaborating with credit institutions to stimulate more active SME lending in Malta by offering the opportunity for banks to act as MDB's intermediary partners for the SGS. This SGS shall enable the credit institutions to be more responsive to the borrowing requirements of smaller businesses, which, in turn, allows these businesses to fulfil their growth ambitions. The SGS aims at enhancing SME access to bank credit for new investment as well as other purposes, including for working capital related to new investment and business transfers. Whilst this scheme is available to all economic sectors, the MDB will be encouraging and prioritising those investments that aim to build a greener and more digitally oriented economy.

The purpose of the SGS is to assist SMEs, including start-ups, by enhancing their access to bank financing. Eligible SMEs benefit from:

- enhanced access to credit as insufficient collateral and lack of credit history will not remain an obstacle,
- better terms and conditions and a longer repayment period,
- lower interest rates as a result of the credit risk protection from the MDB's uncapped guarantee of 80%.

Owing to these benefits, and the broad eligibility criteria, the SGS is expected to become the Bank's flagship scheme for SME financing up to €750,000, taking over the SME Invest scheme which is expected to be fully absorbed by the first quarter of 2023. The SGS will also replace the Family Business Transfer Facility, which as explained earlier, came to an end during the year under review.

Go To Market – Loan Assistance Programme

The Go-To-Market – Loan Assistance Programme, is a sub-scheme of the SGS, launched in collaboration with the Malta Council for Science and Technology (MCST). This sub-scheme is aimed at supporting projects, mainly of start-ups, which have successfully completed the Technology Development Programme of MCST and are ready to commercialise but lack the necessary financing.

The Go-To-Market – Loan Assistance Programme will assist those entities that, in spite of having viable projects, are unable to access the required bank financing mainly because of inadequate collateral, lack of credit history and the novelty of the market or technology that is perceived as higher risk under commercial banks' current credit risk evaluation practices.

This Loan Assistance Programme will further support entities through grants, which will make the project more feasible and bankable. Thus, the programme takes the structure of a blended financial instrument with the grant component directed towards three measures that help the applicants gain access to the SGS. These measures are intended to provide support in the final steps of Technological Readiness Level advancement in relation to deployment of the product or service in the operational environment. These three measures are:

(i) Measure 1 - An interest rate subsidy on the already favourable interest rates charged by commercial banks on the beneficiaries' loans under the SGS, thereby easing the repayment burden in the period where the venture is least likely to be profitable.
(ii) Measure 2 - A grant to support the provision of the up-front contribution, in part or in full, required by the commercial banks to apply for the SGS.
(iii) Measure 3 - A grant to support the collateral requirements under the SGS intended to lower the exposure of the commercial bank.

Guaranteed Co-Lending Scheme

In November 2022, the MDB also launched the Guaranteed Co-Lending Scheme (GCLS). The GCLS is a risk-sharing facility involving co-lending of up to €100 million between the MDB and accredited credit institutions on a 50:50 basis. The MDB provides an interest rate reduction on the part of the loan granted by the MDB and a guarantee of 60% on the credit institutions' part of the lending. The GCLS caters for SMEs with large loan requirements that exceed the maximum threshold of €750,000 under the SGS. The maximum loan amount under the GCLS is €10 million and the maximum term of the loans is 15 years, subject to State Aid considerations.

The GCLS offers favourable financing terms for bankable projects with a special focus on investments involving innovation, digitalisation and, more broadly, the preservation and enhancement of competitiveness; socially-oriented initiatives, particularly those involving knowledge generation, education, health and social inclusion; investment that addresses environmental issues such as water usage, water treatment, waste treatment, reduction and reuse; and investment aimed at achieving a high level of sustainability or to promote the green and circular economy.

PRODUCT OUTLINE OF MDB SCHEMES

The products outline below summarises the key features of all the schemes currently being offered by the MDB. With the exception of the Tailored Facility for Businesses and Infrastructure, and the Guarantee Facility for Loans to SMEs (better known as SME Invest), all other facilities were launched during 2022.

PRODUCT NAME	GUARANTEE FACILITY FOR LOANS TO SMES
Product Outline	This facility was launched in May 2019 with an applicability period of three years or until the portfolio is fully utilised. The scheme's inclusion period and portfolio were extended during 2022 to ensure that SMEs requiring finance are assisted until the accreditation process of credit institutions under the new SME Guarantee Scheme is completed. SME Invest is aimed at assisting SMEs in enhancing their access to finance. The facility enables commercial banks to be more responsive to the borrowing requirements of smaller businesses, which, in turn, allows these businesses to fulfil their growth ambitions. SME Invest is intermediated by Bank of Valletta.
Objective	To provide better access and more affordable finance to smaller businesses that are viable but unable to obtain the required amount of finance for their investment needs from a commercial bank. This may be due to such factors as; collateral offered by the borrower fails to meet the bank's normal requirements; the novelty or nature of the business venture falls outside the commercial bank's risk tolerance and the required repayment period proposed by the borrower exceeds what the bank may be willing or able to accept.
Structure	The MDB provides a guarantee covering 80% of the individual loans under the scheme, with a cap rate of 25% at the portfolio level, generating a multiplier of 5. Thereby, a guarantee of €10 million by the MDB enables the generation of a portfolio of up to €50 million new loans to SMEs.
Banking Facility	The size of eligible loans guaranteed under the facility ranges from a minimum of €10,000 up to a maximum of €750,000. The minimum loan size may vary from one implementing partner to another. There is a possibility of a twelve-month moratorium on capital repayments at the discretion of the commercial bank. The maximum term of loans is 10 years including the moratorium period, if any. The minimum contribution by the SME is normally 10% of the project costs, at the discretion of the commercial bank. The commercial bank may require collateral in addition to MDB's guarantee to cover the exposure.
Eligibility criteria	
Loan eligibility	The project must be supported by a viable business plan and considered bankable by the commercial bank and the MDB, which implies that the business is reasonably expected to generate sufficient cash flow to enable timely repayments. The project must not be physically completed or fully implemented on the approval date of the facility. The purpose of the financing covers a wide spectrum of possible activities including: (a) the establishment of new enterprises, (b) expansion capital, (c) capital for the strengthening and/or stabilisation of the general activities of an enterprise; (d)the realisation of new projects, penetration of new markets or new developments by existing enterprises, (e) investment-related working capital.
Eligible applicants	Applicants must be viable SMEs, established and operating in Malta. The activities of the SME should not be in the exclusion list of the MDB.
State Aid	The scheme is subject to the de minimis regulation
Benefits	Enhanced access to credit availability; better terms and conditions, including a longer repayment period.; and lower interest rates as a result of the credit risk protection from the MDB's guarantee.
Application process	The scheme is available through commercial banks. SMEs are to apply for the facility through the commercial banks by providing their borrowing proposal and any other necessary documentation. Bank of Valletta was the first implementing partner of the MDB Guarantee facility for loans to SMEs through the launch of SME Invest. The applicability period of SME Invest is scheduled to end on 31 March 2023. More information on the SME Invest scheme can be obtained from BOV Branches or Business Centre, or by sending an email to smefinance@bov.com.

PRODUCT NAME	TAILORED FACILITY FOR BUSINESSES AND INFRASTRUCTURE
Product Outline	The Tailored Facility was launched in August 2019 and is aimed at assisting businesses, including start-ups, in enhancing their access to finance. This facility offers a bespoke solution for businesses with investment plans that require credit larger than what currently is offered under other standard schemes of the MDB.
Objective	The facility is designed to address the following major barriers to lending: insufficient value or type of collateral; innovative business ventures, economic sectors or technologies which fall outside the risk appetite and tolerance of commercial banks; and other factors for which commercial banks may not be willing or able to provide the required financing in whole or part.
Structure	The required loan is co-financed by the commercial bank and the MDB in such portions as may be agreed between the parties. On a case-by-case basis, the MDB may provide a partial guarantee on the commercial bank's share of the loan.
Banking Facility	The size of the loan is determined on a case-by-case basis depending on the project being financed. The minimum term of the loan is 24 months. The maximum term depends on the lifetime of the asset being financed, to be agreed on a case-by-case basis.
Eligibility criteria	
Loan eligibility	The project must be supported by a viable business plan and considered bankable by the commercial bank and the MDB, meaning that the business is reasonably expected to generate sufficient cash flow to enable timely repayments. The purpose of the financing covers a wide spectrum of possible activities including: the establishment of new enterprises, expansion capital, capital for the strengthening and/or stabilisation of the general activities of an enterprise or the realisation of new projects, penetration of new markets or new developments by existing enterprises. New investment contributing to the promotion of national competitiveness, social inclusiveness and green and sustainable development are given priority.
Eligible applicants	Applicants must be viable undertakings, established and operating in Malta. The activities of the business should not be in the exclusion criteria of the EU.
State Aid	The provision of funding for the tailored purpose facility is made in accordance with the state aid rules and obligations of the de minimis and the General Block Exemption Regulation of the EU.
Benefits	Eligible beneficiaries benefit from enhanced access to credit as insufficient collateral and lack of credit history should not remain an obstacle when seeking finance from the banking sector. These also benefit from better terms and conditions and lower interest rates as a result of the risk sharing co-financing arrangement with the commercial bank and the protection of the MDB's guarantee, if applicable. The commercial bank shall pass on the benefit from MDB's guarantee, if applicable, to the beneficiary.
Application process	Interested business undertakings are to apply with their commercial bank by providing their borrowing proposal and any other necessary documentation. The approval of the facility is at the discretion of the commercial bank acting in conjunction with the MDB.

PRODUCT NAME	FURTHER STUDIES MADE AFFORDABLE (FSMA) SCHEME - BOV'S STUDIES PLUS+
Product Outline	This financial instrument is targeted towards students aiming at furthering their educational attainment. This scheme builds on the success of the FSMA scheme which was launched in October 2019 and which expired in February 2022. This instrument is financed under Malta's European Social Fund (ESF) and European Social Fund plus (ESF+) Operational Programmes.
Objective	The FSMA+ scheme seeks to support students in pursuing higher level of studies. FSMA+ is available to students through MDB's intermediating partner Bank of Valletta, under the BOV's Studies Plus+ scheme.
Structure	The MDB provides a guarantee covering 80% of the individual loans under the scheme which is capped at 25% of the commercial bank's portfolio, generating a multiplier of 5. EU funds are allocated into two elements: (i) Guarantee component: portfolio capped financial guarantee providing credit risk coverage; and (ii) Grant component: interest rate subsidy covering all the interest incurred during the moratorium period of each student loan.
Banking Facility	The maximum size of eligible loans guaranteed under the facility is €100,000, with a loan term of up to 15 years, including the moratorium period. The maximum term of capital moratorium covers the term of the course plus an additional twelve months, subject to a maximum moratorium period of five years.
Eligibility criteria	
Loan eligibility	Students pursuing a study programme which is an accredited course in MQF levels 5, 6, 7 and 8, as well as internationally recognised certificates. The loans are available for full time and part time studies. The loan can finance tuition fees, living expenses, accommodation fees, transport expenses, textbooks and related expenses.
Eligible applicants	The applicant has to be a Maltese citizen; or national of an EU/EEA Member State provided that such person has obtained permanent residence in Malta or is in Malta exercising his/her EU Treaty rights as an employee, self-employed person or person retaining such status. The applicant can also be a third country national that has been granted long-term residence status in Malta.
State Aid	No state aid rules apply for this scheme.
Benefits	No payment obligations to the beneficiary during the period of study plus one year. A maximum term of capital moratorium that covers the term of the course plus an additional twelve months, subject to a maximum moratorium period of five years. No interest burden on the borrower during the moratorium period. The interest due during the moratorium period is fully covered by an interest rate subsidy funded by EU Structural Funds. Attractive interest rate during the remaining term of the loan due to the MDB guarantee. No collateral or upfront contribution shall be requested from the borrower by the partnering commercial bank.
Application process	The scheme is available through MDB's intermediary partner – Bank of Valletta under the name of BOV Studies Plus+ (https://www.bov.com/news/bov-studies-plus).

PRODUCT NAME	SME GUARANTEE SCHEME (SGS)
Product Outline	The SGS, launched in 2022, is an uncapped portfolio guarantee scheme intermediated by accredited commercial banks. It is a scheme that aims at enhancing enterprises access to bank credit for new investment as well as other purposes; including for working capital related to new investment and business transfers. The facility enables commercial banks to be more responsive to the borrowing requirements of smaller businesses, which, in turn, allows these businesses to fulfil their growth ambitions. The SGS is aimed to replace the SME Invest, offering broader eligibility and a higher transfer of benefit through an uncapped guarantee
Objective	The scheme aims to assist viable SMEs accessing finance. The scheme will address the following barriers to lending: (i) inadequate collateral; (ii) lack of credit history; and (iii) novel business market, sector or technology that is perceived by finance providers as higher risk.
Structure	The MDB provides an uncapped guarantee of 80% on the loan portfolio of the financial intermediary. The scheme is open to all accredited commercial banks. A covered loan portfolio of up to €80,000,000 is being made available
Banking Facility	Facilities of €10,000 up to €750,000, with a term of loan of up to 10 years. The minimum loan size may vary from one intermediary partner to another. The MDB restricts the take up of collateral to a maximum of 20% of the facility amount. The loan term is up to 10 years and the last date for inclusion of loans is end 2024.
Eligibility criteria	
Loan eligibility	The purpose of the financing under SGS covers a wide spectrum of possible activities including: (a) the establishment of new enterprises, (b) expansion capital, (c) capital for the strengthening and/or stabilisation of the general activities of an enterprise; (d) the realisation of new projects, penetration of new markets or new developments by existing enterprises, (e) investment-related working capital, (f) business ownership transfers, in whole or in part, as long as this does not create or enhance a position of significant market dominance, conforming with applicable legislation (including but not limited to S.L 379.08).
Eligible applicants	The scheme is open to all SMEs in all economic sectors save for the excluded and prohibited activities of the MDB and the EIF. Priority will be given to projects related to green and digital investments. Applications shall be assessed by both the MDB and the intermediary partners in terms of viability.
State Aid Regime	The SGS is notified under de minimis regulations.
Benefits	Eligible enterprises benefit from: enhanced access to credit availability; better terms and conditions, including a longer repayment period, lower collateral requirements; and lower interest rates as a result of the credit risk protection from the MDB's guarantee.
Application process	The scheme is available through intermediary partners accredited by the MDB until 31 December 2024.

PRODUCT NAME	GUARANTEED CO-LENDING SCHEME FOR SMES (GCLS)
Product Outline	The GCLS is a risk-sharing facility involving co-lending between the MDB and the accredited commercial bank on a 50:50 basis. In addition, the MDB provides a guarantee of 60% on the commercial bank's part of the lending. This scheme was launched in the last quarter of 2022.
Objective	The objective of the GCLS is to enhance access to finance to SMEs that face financial and other constraints and do not fit under the SME Guarantee Scheme due to the size of the loan required.
Structure	The targeted GCLS global loan portfolio can reach up to €100 million, of which €50 million will be originated by MDB and €50 million by the participating commercial banks. MDB shall provide an additional guarantee of €30 million (60%) on the €50 million loans by the participating banks.
Banking Facility	The maximum loan amount under the GCLS is €10 million - €5 million by MDB and €5 million by the participating bank. The maximum term of the loans is 15 years, subject to State Aid considerations. The MDB loans will have the same terms and conditions as the commercial banks' loans except for the: a) Interest rate on the loan, which will be up to a minimum of 25 bps lower than that of the commercial banks: and b) Partial Guarantee – the MDB will cover 60% of the commercial banks' portion of the loan.
State Aid Regime	The GCLS is notified under both the de minimis and GBER.
Eligibility criteria	
Loan eligibility	Loans shall target: (a) the establishment of new enterprises, (b) expansion capital, (c) capital for the strengthening and/or stabilisation of the general activities of an enterprise or (d) the realisation of new projects, penetration of new markets or new developments by existing enterprises. The investment to be supported under GCLS: (a) shall be an investment in tangible and/or intangible assets relating to the setting-up of a new establishment, the extension of an existing establishment, diversification of the output of an establishment into new additional products or a fundamental change in the overall production process of an existing establishment; and (b) the investment shall be new and has not yet been started at time of approval of the loan; and (c) the minimum cash contribution to be put forward by the borrower is 20% of the total investment; and (d) shall be expected to be financially viable as assessed by the commercial bank and the MDB.
Eligible applicants	The scheme is open to all SMEs in all economic sectors. In order to be eligible, SMEs have to: run a commercial activity in the non-excluded activities sector; are a sole trader, partnership, co-operative or limited company; have a viable business proposal in the opinion of the MDB and the partner commercial bank; and prove that they are able to repay the facility. Any investments related to green and digital technologies will be prioritised.
Benefits	Lower interest rates; Longer duration; Lower collateral requirement; Enhanced access to finance
Application process	The scheme will be made available through accredited commercial banks until end-2024.

UKRAINE CRISIS RESPONSE MEASURES

PRODUCT NAME	SUBSIDISED LOANS SCHEME
Product Outline	In the wake of the war in Ukraine, the MDB launched the Subsidised Loans Scheme (SLS) in May 2022 to provide urgent liquidity support in the form of a direct subsidised loan for working capital purposes to finance the bulk importation of eligible grain commodities.
Objective	To offer temporary urgent liquidity support to ensure national security of strategic supply to undertakings engaged in the importation and wholesale of grains, including but not limited to soya, barley, alfalfa, maize, wheat and other pre-mixes utilised in the manufacturing of feeds for various types of animals as well as wheat and flour for the production of bread, pasta and other basic foodstuff.
Structure	A maximum portfolio of €30 million in direct subsidised loans by MDB for a maximum term of two years.
Banking Facility	The loans shall be covered by a maximum interest rate subsidy of 2.0% subject to a minimum interest payment by the borrower of 0.1%. Each loan under this scheme shall be covered by a guarantee of 90% issued by the Government of Malta. A maximum moratorium of 6 months with the possibility to extend to one year on a case-by-case basis. The moratorium period applies to capital repayments. During the moratorium period the interest on the loan is to be paid on a monthly or quarterly basis, as may be agreed between the MDB and the borrower.
Eligibility criteria	
Loan eligibility	Urgent liquidity needs for working capital purposes related to the importation of strategic reserves of eligible grains. The scheme shall not cover restructuring or rescheduling of existing facilities held with the commercial banks or with other related parties to the undertaking. The scheme shall not cover overdue creditors whose overdue amounts are not related to the current crisis.
Eligible applicants	All business undertakings established and operating in Malta (SMEs and large enterprises) Aid under this scheme shall not be granted to undertakings under sanctions adopted by the EU, including but not limited to: • persons, entities or bodies specifically named in the legal acts imposing those sanctions; • undertakings owned or controlled by persons, entities or bodies targeted by sanctions adopted by the EU; or • undertakings active in industries targeted by sanctions adopted by the EU, insofar as the aid would undermine the objectives of the relevant sanctions.
State Aid	The SLS is implemented in line with the provisions of the European Commission's Temporary Crisis Framework to support the economy in the context of Russia's invasion of Ukraine (OJ C 131 I/1, 24.3.2022).
Benefits	Eligible firms benefit from: enhanced access to finance for working capital needs; better terms and conditions, subsidised interest rates and a moratorium period for capital repayments.
Application process	The MDB provides the loans directly to the beneficiary for the purpose stated. Proposals are assessed by the MDB in line with the MDB's credit policy and procedures criteria.

PRODUCT NAME	LIQUIDITY SUPPORT GUARANTEE SCHEME – MEASURE A (LSGS-A)
Product Outline	In June 2022, the MDB launched the Liquidity Support Guarantee Scheme – Measure A (LSGS-A) as part of a package of measures in response to the Ukraine crisis. The LSGS-A is open to all types of undertakings operating in all economic sectors that have been adversely impacted by the repercussions of the Ukraine crisis, regardless of size.
Objective	To offer temporary liquidity support to undertakings affected by the current Ukraine-Russia crisis. Through this guarantee, the MDB aims to provide better access and more affordable working capital loans to businesses whose liquidity has been negatively impacted by the consequences of the Ukraine war.
Structure	The MDB provides liquidity support in the form of a portfolio capped guarantee which will be intermediated through accredited commercial banks. The guarantee covers 90% of each loan in the portfolio, capped at 50% of the total portfolio. Loans under the LSGS-A also benefit from an Interest Rate Subsidy.
Banking Facility	The LSGS-A guarantees working capital loans within a portfolio of up to €100 million at subsidised interest rates, for loan terms up to six years. The interest rate subsidy applicable on LSGS-A loans is up to 2.5% of the outstanding amount of the working capital loan, subject that the borrower shall pay a minimum amount of 0.1% of the interest rate charge during the interest rate subsidy period, provided that the maximum aid per undertaking granted under section 2.1 of the TCF does not exceed: (a) €250,000 for undertakings operating in the primary production sector of agricultural products, or (b) €300,000 for undertakings operating in the fishery and aquaculture sector, or (c) €2,000,000 for other undertakings.
Eligibility criteria	
Loan eligibility	LSGS-A covers urgent liquidity needs for working capital purposes, caused for instance by: • Higher prices of imported raw materials and primary goods due to disruption in supply chains; and/or • Higher costs related to electricity and gas; and/or • An increase in other working capital costs incurred by the undertaking through a direct or indirect effect of the crisis.
Eligible applicants	All business undertakings established and operating in Malta consisting of: 1. SMEs (within the meaning of Commission Regulation (EU) N°651/2014 of 17 June 2014 as amended, and 2. large enterprises.
State Aid	The LSGS-A measure is implemented in line with the Temporary Crisis Framework for State Aid measures to support the economy following the aggression against Ukraine by Russia (TCF).
Benefits	Accredited credit institutions shall provide an interest rate reduction on the average interest rate to beneficiaries as compared to similar facilities prior to the introduction of this scheme. Hence, eligible firms benefit from: enhanced access to finance for working capital needs, subsidised interest rates and better terms and conditions.
Application process	The scheme is available through MDB's partnering financial intermediary, currently Bank of Valletta.

PRODUCT NAME	LIQUIDITY SUPPORT GUARANTEE SCHEME – MEASURE B (LSGS-B)
Product Outline	In June 2022, the MDB also launched the Liquidity Support Guarantee Scheme – Measure B (LSGS-B), the third scheme as part of a package of measures in response to the Ukraine crisis. LSGS-B provides short term liquidity support for importers of fuel and oil.
Objective	To provide temporary short term liquidity support for importers of fuel and oil, which were impacted by the current crisis, in order to ensure security of supply and more stable prices.
Structure	The MDB provides liquidity support in the form of an uncapped portfolio guarantee which will be intermediated through accredited commercial banks. The guarantee covers 80% of each loan in the portfolio. Loans under the LSGS-B also benefit from an Interest Rate Subsidy.
Banking Facility	The LSGS-B guarantees working capital loans within a portfolio of up to €50 million at subsidised interest rates, for loan terms up to six years. An interest rate subsidy is applicable on LSGS-B loans up to 2.5% of the outstanding amount of the working capital loan, subject that the borrower shall pay a minimum amount of 0.1% of the interest rate charge during the interest rate subsidy period, provided that the maximum aid per undertaking granted under section 2.1 of the TCF does not exceed: (a) €250,000 for undertakings operating in the primary production sector of agricultural products, or (b) €300,000 for undertakings operating in the fishery and aquaculture sector, or (c) €2,000,000 for other undertakings.
Eligibility criteria	
Loan eligibility	LSGS-B covers the temporary increase in liquidity needs resulting from increased prices and higher amounts of fuel and oil purchases, to ensure the continuous supply of these strategically important commodities.
Eligible applicants	Importers of fuels and oil, established and operating in Malta.
State Aid	The LSGS-B measure is implemented in line with the Temporary Crisis Framework for State Aid measures to support the economy following the aggression against Ukraine by Russia (TCF).
Benefits	Credit institutions shall provide an interest rate reduction on the average interest rate to beneficiaries as compared to similar facilities prior to the introduction of the guaranteed scheme. Hence, eligible firms benefit from: enhanced access to finance for working capital needs, subsidised interest rates and better terms and conditions.
Application process	The scheme is available through MDB's partnering financial intermediaries – currently Bank of Valletta and HSBC.

OUTREACH OF MDB'S SCHEMES

This section highlights the economic importance, impact and outreach of MDB schemes, including key performance indicators, and where possible provide a qualitative assessment of the most impactful schemes offered by the MDB.

Macroeconomic backdrop

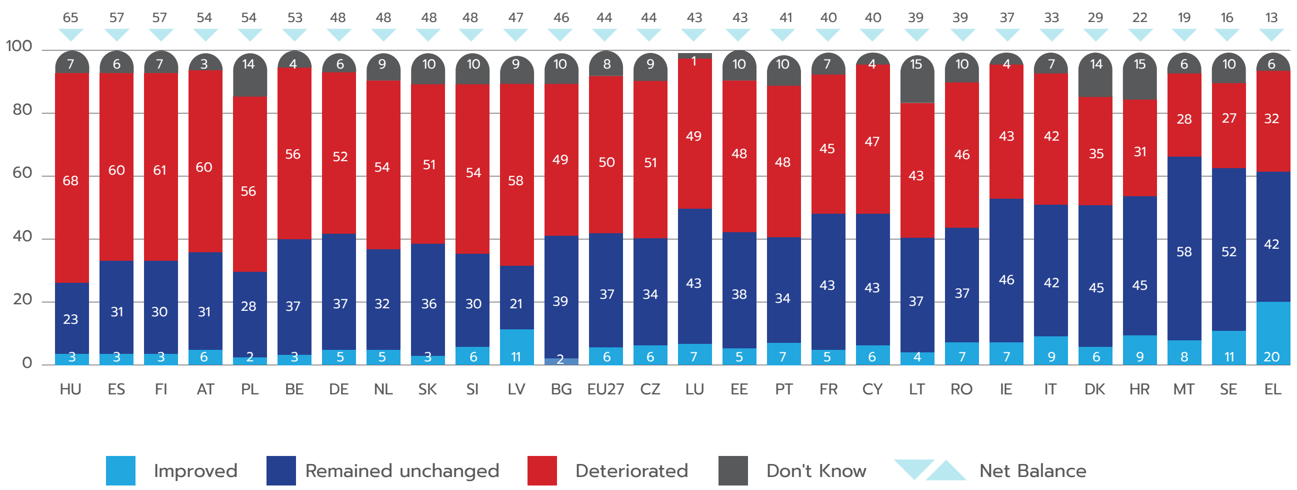
For the large part of the past decade the Maltese economy was characterised by fast growth, mainly driven by a buoyant labour market, improved public finances and higher spending power that have supported Malta's economic and social development. However, like other countries, Malta's economy was severely impacted by the COVID-19 pandemic, leading to a sharp decline in activity in 2020, particularly in tourism and other related sectors.

Malta's economy rebounded strongly from the pandemic, and in 2022 real GDP growth is estimated to have reached 6.9%, which is higher than what was projected by the European Commission and other institutions. The economy showed strong growth in both private and public consumption, which were partially countered by a drop in investment (gross fixed capital formation). In addition to the strong performance by the services sectors in general, the export of tourism services in 2022 rebounded quickly, both in terms of total number of visitors and expenditures, contributing to overall positive economic results.

Despite the overall economic buoyancy, evidence from the latest Survey on the Access to Finance of Enterprises (SAFE), carried out between April and September 2022, shows that local SMEs claimed that in net terms, the general economic situation has deteriorated when compared to a year earlier.[9] Nevertheless, in comparative terms, this deterioration was the third lowest amongst all EU Member States (see Chart 1). This relatively positive result can be attributed to various factors, particularly to the Government's intervention in buffering fuel-related inflationary pressures. Another contributing factor may have been the access to working capital loans enabled by the MDB and backed by Government guarantees which supported the flow of liquidity during these difficult times. Indeed, the same Survey shows that Maltese SMEs are the most reliant on financing related to working capital from all EU countries (see Chart 2).

CHART 1: SAFE RESULTS - GENERAL ECONOMIC OUTLOOK

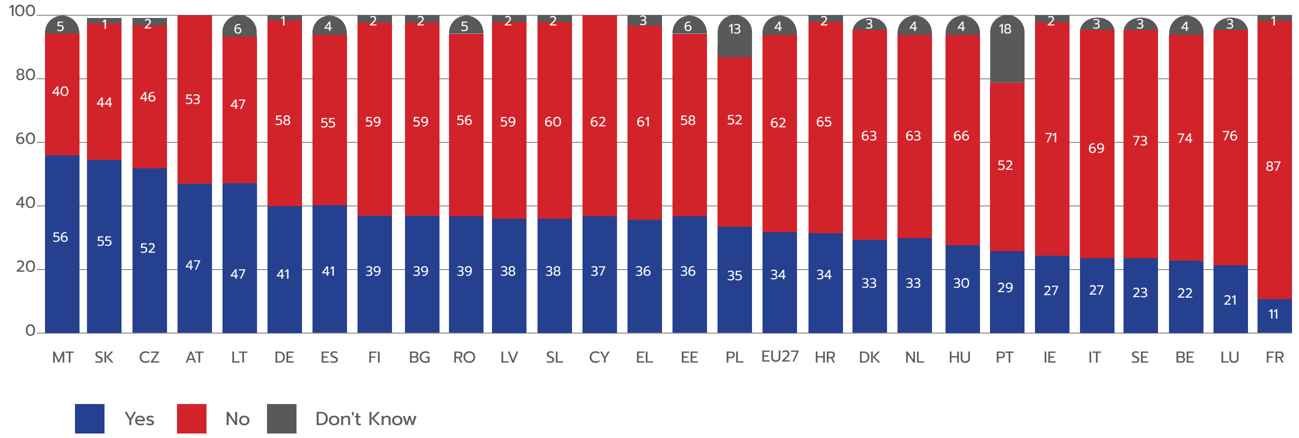
For each of the following factors, would you say that they improved, remained unchanged or deteriorated over the past 6 months? (% - General economic outlook, insofar as it affects the availability of external financing)



9 The SAFE exercise is conducted twice a year: once by the ECB covering euro area countries and once in cooperation with the European Commission covering all EU countries plus some neighbouring countries. https://single-market-economy.ec.europa.eu/system/files/2023-01/SAFE%20Analytical_Report%202022.pdf

CHART 2: SAFE RESULTS – EXTERNAL FINANCING USED FOR INVENTORY AND OTHER WORKING CAPITAL

For what purpose was external financing used by your enterprise during the past 6 months? (% - Inventory and other working capital)



Headwinds, however, remain strong. Consumers and businesses faced higher costs and core inflation (headline inflation excluding energy and unprocessed food) remained elevated, further eroding households' purchasing power. HICP inflation in 2022 reached 6.1%, despite energy prices being kept at 2020 level by government intervention. As inflationary pressures persist, monetary tightening is set to continue, weighing on business activity and exerting a drag on investment. During the year under review, the European Central Bank strengthened its efforts to fight inflation, raising rates on four occasions.

Looking forward, the European Commission is projecting that in 2023 domestic economic activity will grow at a slower pace, by 3.1%, following a wider economic slowdown in Malta's main trading partners. In 2024, real GDP growth is expected to reach 3.7%, supported by net exports and growth in domestic demand. The strong impulse to growth from the recovery in tourism is however set to moderate in 2024, as tourist flows approach pre-pandemic levels. Nonetheless, inflation in 2023 is set to remain elevated at 4.3%, due to continuing pressures in food, transport, and imported goods prices. In 2024, inflation is expected to subside to 2.4% as imported price pressures are also set to moderate.[10]

Overall risks of these projections remain tilted on the downside, reflecting high uncertainty and geopolitical tensions. Moreover, in view of the increase in inflation in 2023, together with tight labour market conditions, pressures on businesses are expected to remain high. According to the Central Bank of Malta, wage growth is projected to be relatively strong, but nominal wage growth is still forecasted to remain below consumer price inflation in 2023 due to lags in the transmission from prices to wages.[11]

Business outreach - Key Performance Indicators

COVID-19 guarantee facilities

By the end of the inclusion period in June 2022, slightly more than two years from the launch of the COVID-19 Guarantee Scheme (CGS), the total amount of working capital loans sanctioned by the nine partnering commercial banks that were accredited to roll-out the CGS stood at €482.6 million, down from the peak of €508.8 million recorded in September 2021. This drop is on the back of some withdrawals of request for facilities by borrowers. This reduction seems to indicate that due to the high level of uncertainty surrounding business activity during the pandemic, some businesses had applied for facilities, and as their business performance improved, they decided not to avail, in whole or in part, of some of the agreed loan facilities.

Reflecting this development, the number of businesses supported by CGS loans declined to 587 by December 2022 compared to 616 businesses at the end of 2021. The supported businesses collectively employ around 40,000 persons and range from hotels to large retail outlets, but also to smaller firms from all economic sectors (see Charts 3 and 4). As can be noted from the charts, firms in the tourism-related sectors (accommodation & food services activities, and wholesale & retail activities), which were the most adversely impacted by the pandemic, have collectively been granted close to €208.8 million, or 43.3%, of total loans sanctioned under the CGS.

10 https://economy-finance.ec.europa.eu/economic-surveillance-eu-economies/malta/economic-forecast-malta_en
11 https://www.centralbankmalta.org/en/news/90/2023/11091

CHART 3: COVID-19 GUARANTEE SCHEME - SANCTIONED LOANS BY ECONOMIC SECTOR (€)

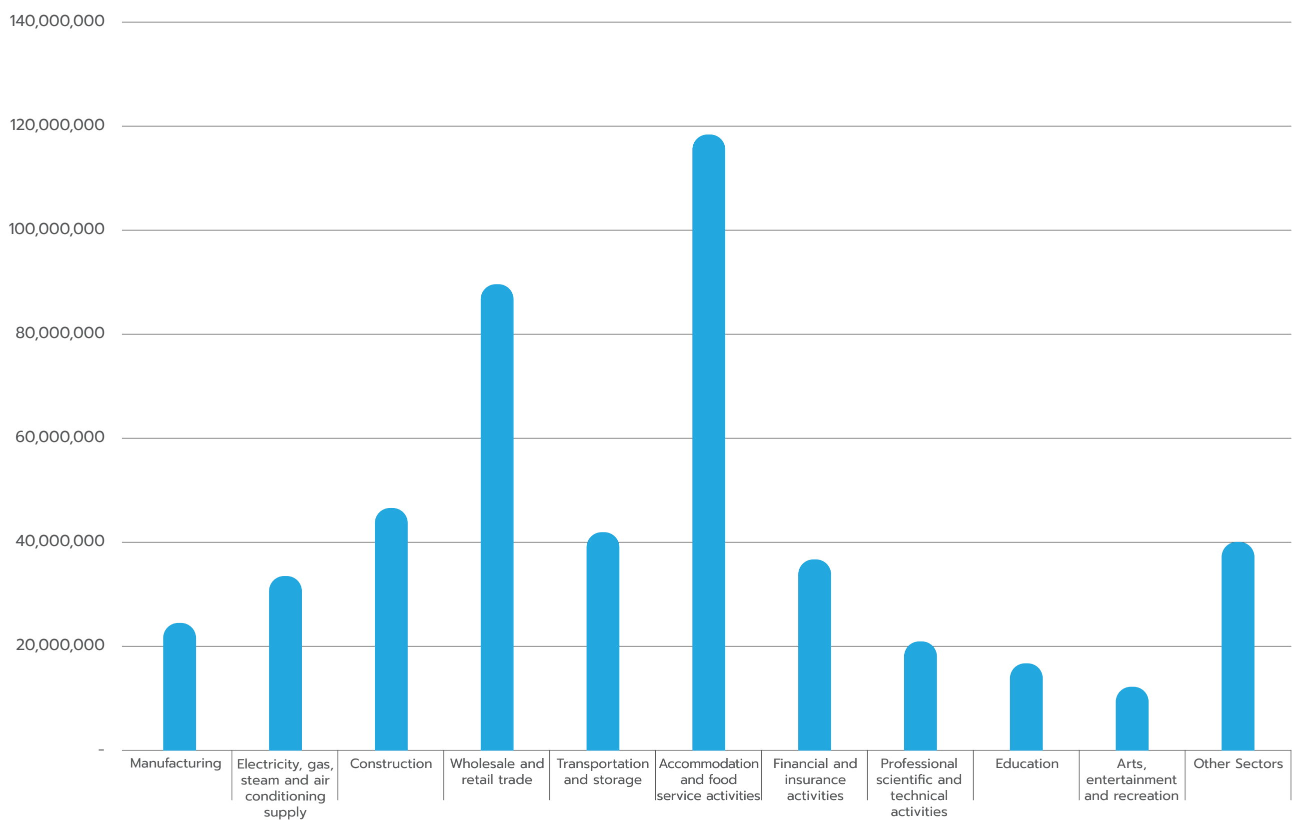
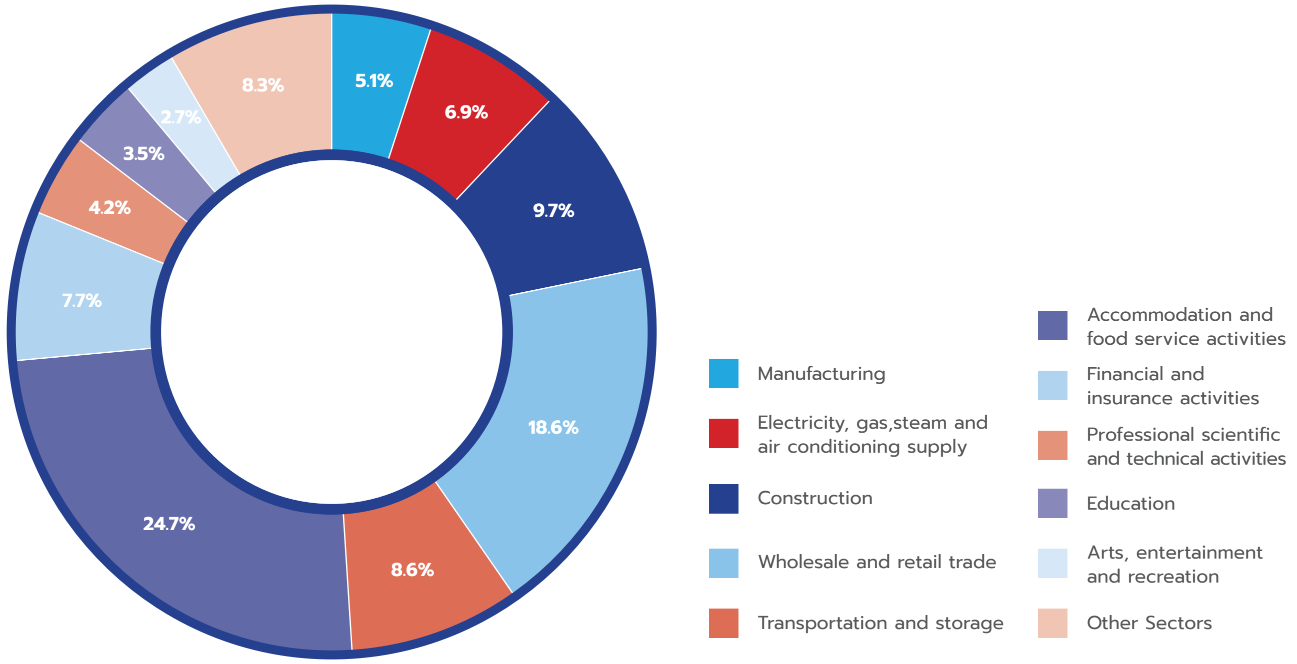
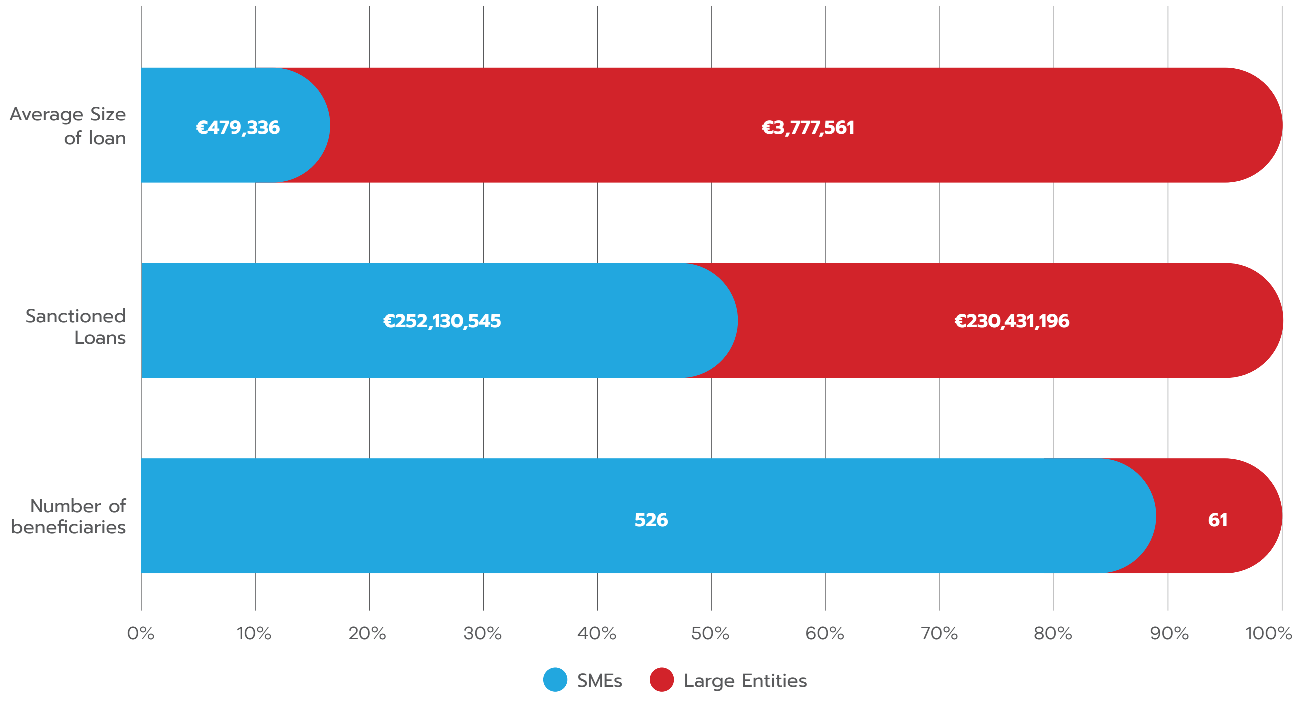


CHART 4: COVID-19 GUARANTEE SCHEME - DISTRIBUTION ACROSS ECONOMIC SECTORS (%)



Under the CGS scheme, businesses of any size were eligible to apply for a loan, with amounts that could reach up to €5 million for SMEs, and €25 million for larger entities, depending on the firm's wage bill, turnover and projected working capital requirements. Applications exceeding €2million for SMEs and €5 million for large enterprises required the prior clearance of the MDB that they meet the eligibility criteria. The average loan per facility of the 587 businesses still benefitting under the CGS at end-2022 stood at around €822,081. Out of these beneficiaries, 526 firms, 89.6% of the total, are classified as SMEs, whereas 61 are large entities (see Chart 5). As one would expect, the requested working capital loans of large enterprises were markedly higher than those requested by smaller firms. Indeed, the average loan size of SMEs amounted to €479,336, as opposed to an average of €3.8 million granted to larger entities.

CHART 5: DISTRIBUTION ACROSS BENEFICIARIES BY SIZE



Guarantee facility for loans to SMEs (SME Invest)

The MDB plays a key role in reducing borrowing costs and collateral requirements for SMEs through risk sharing instruments in conjunction with commercial banks. These products are instrumental in supporting the banks to engage more with smaller and innovative firms.

The SME Invest, which was launched in 2019, remained MDB's main guarantee scheme for new SME investments during 2022. This scheme is open to SMEs operating in all economic sectors and targets those SMEs planning new capital investment projects, providing easier access to finance through reduced collateral requirements and finance costs. Enterprises may seek bank financing up to a maximum of €750,000, at attractive interest rates and better credit terms. The applicability period of SME Invest will expire at end-March 2023 and will be replaced by the SME Guarantee Scheme during 2023.

As at end of 2022, the SME Invest scheme has injected a cumulative €47.6 million in new investments in the local economy, supporting 157 projects undertaken by local SMEs, employing close to 2,500 persons. The average term of loan duration under this scheme stood at close to 10 years (See Table 1). The projects supported by this scheme include a wide array of capital investments, comprising amongst others, projects related to refurbishing of retail outlets and warehousing, clinics, and childcare centres, but also digitalisation and solar energy rooftops.

TABLE 1: FACILITIES UNDER THE SME INVEST SCHEME

Year	*Number of facilities by type of enterprise*			
	MICRO	SMALL	MEDIUM	TOTAL
2019	15	16	3	34
2020	37	18	4	59
2021	33	19	2	52
2022	9	3	0	12
Totals	88	53	9	157

	Sanctioned loans (Euro millions)	Average loan size (Euro)	Number of employees
2019	11.5	338,088	598
2020	17.1	290,644	1043
2021	14.5	278,654	719
2022	4.4	370,750	96
Totals*	47.6	303,070	2456

** Figures refer to active facilities and exclude a small number of facilities that were sanctioned between 2019 and 2022 but were later withdrawn by applicants.*

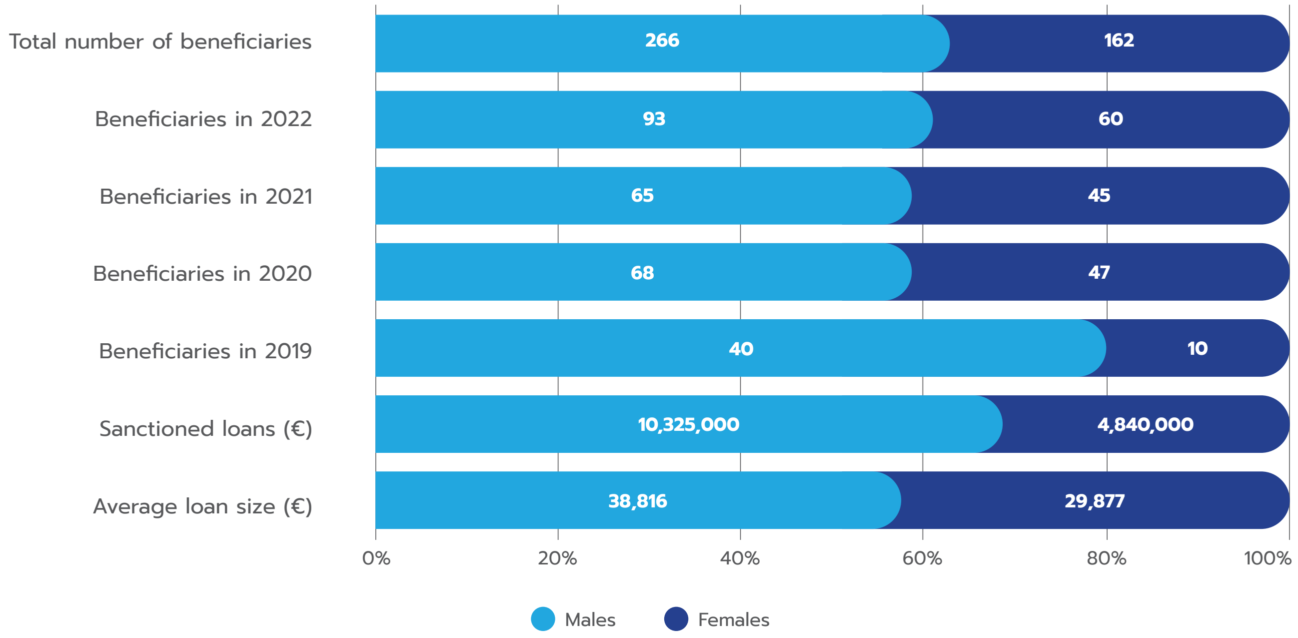
FSMA and FSMA+ schemes

Given Malta's small open economy, human capital has always been one of the country's most critical resources. The MDB is mandated to contribute to inclusive and sustainable economic growth and considers education as a major pillar in reaching this overarching objective.

Since 2019, MDB's study-loan schemes have been facilitating the financing of the cost of students' studies in Malta and overseas, including tuition, accommodation, travel, subsistence, and related expenses. The schemes cover full time, part time or distance learning study courses, at MQF levels 5 – 8, and other internationally recognised academic certificates. The maximum loan value can reach up to €100,000 for a term of up to 15 years.

Besides offering a significantly reduced interest rate, these facilities offer a moratorium on both capital repayments and interest for the period of study plus 12 months. The interest accumulated during the moratorium period is fully covered by the interest rate subsidy, which means that the student is not required to make any payments during the period of study and will also have an additional year to seek employment. No additional fees and processing fees are charged and no collateral, life insurance and up-front contribution are requested. The schemes are designed to fit the requirements of students at a stage in life where they lack financial resources and require peace of mind during their studies, without the anxiety of having to cope with loan repayments.
By the end of 2022, 429 students are being supported under the FSMA and FSMA+ schemes, an increase of 153 students when compared to end-2021. Out of these beneficiaries, 266 are males, whereas 162 are females. Total loans under both schemes reached €15.2 million by end-2022. Reflecting the higher number of male beneficiaries, as well as the skewed uptake of male students opting for the more expensive aircraft pilot courses, total sanctioned loans for males is more than twice than that of female beneficiaries. The latter is also resulting in notable differences in the average loan size by gender (see Chart 6).

CHART 6: FSMA CHARACTERSTICS BY GENDER



Under the FSMA scheme, the overall average loan size reached €35,350, which is markedly higher than what commercial banks are willing to offer in the absence of such a guaranteed scheme. The beneficiaries are aged between 19 and 50 years. However, over 80% of all beneficiaries are in the 19-30 age cohort.

As can be seen in Chart 7, the most popular courses undertaken by the beneficiaries of the FSMA scheme were for the MQF 7 level of education, which is equivalent to a Master's degree, with 215 students, or 50.1% of the total, followed by 123 beneficiaries equivalent to 28.7% of the total opting for internationally recognised certificates, predominantly courses for aircraft pilots. Reflecting the substantial costs related to the latter professional courses, the total amount sanctioned for international recognised certificates accounted for 44.7% of the total funds sanctioned under the schemes (see Chart 8). At the same time, MQF 6 level courses were taken by 72 beneficiaries, whilst loans to students pursuing MQF levels 5 (diploma) and 8 (PhD) were taken by 12 and 7 beneficiaries, respectively.

CHART 7: BENEFICIARIES SUPPORTED ACROSS QUALIFICATION LEVELS

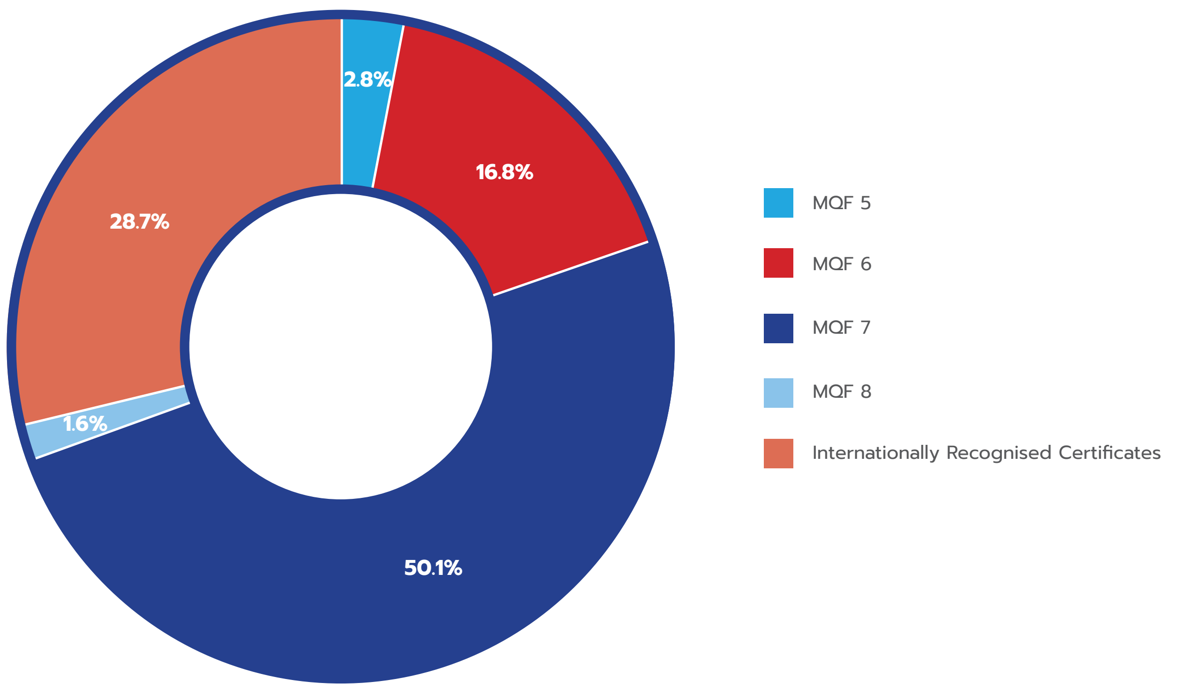
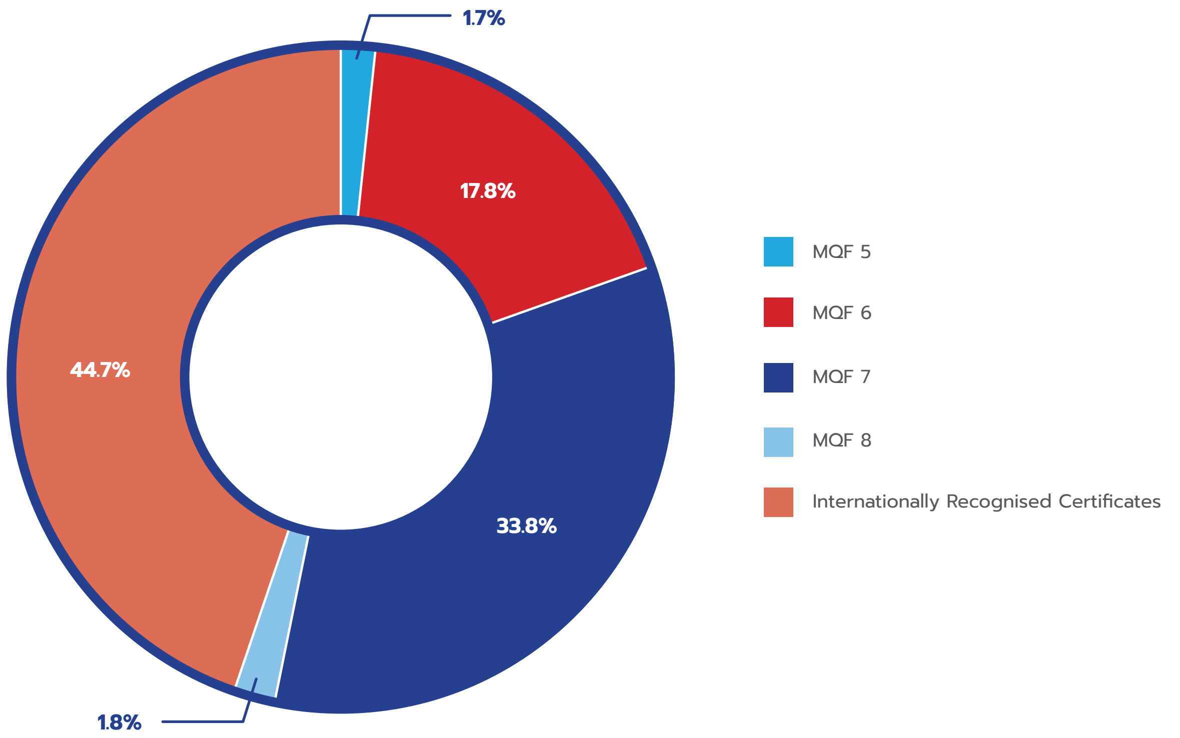


CHART 8: DISTRIBUTION OF SANCTIONED LOANS BY VALUE



MDB firmly believes that investment in human capital is crucial to expand Malta's growth potential and to ensure its long-term macroeconomic competitiveness. The take-up of these MDB schemes has been significantly higher than expected. In October 2022, the Fi-Compass, a platform for advisory services on financial instruments under EU shared management, recognised the success of the FSMA scheme and identified this instrument as one of the three best case studies of blended schemes in the EU.[12]

12 https://www.fi-compass.eu/publication/manuals/financial-instruments-education-and-learning

SPECIAL TOPIC IV
MDB'S FACILITIES IN MALTA'S ECONOMIC CONTEXT

ECONOMIC IMPACT OF MDB'S INTERVENTION

Since its establishment five years ago, the MDB has played an important role in promoting economic and social development in Malta. As a promotional financial institution that provides long-term financing and other services to support specific economic sectors, projects, or policy objectives, the MDB helps in:

(i) Addressing market gaps: the Bank helps in addressing market gaps that characterise certain sectors, particularly those related to SME and infrastructure financing.

(ii) Supporting economic growth: by providing financing and other support to businesses, entrepreneurs, and projects that otherwise would have struggled to obtain funding. This can help to stimulate economic growth, create jobs, and drive innovation.

(iii) Fostering innovation: the Bank prioritises funding for innovative projects that have the potential to create new industries or disrupt existing ones. This is important to drive technological advancement and keep Malta competitive on a European and global scale.

(iv) Supporting public policy objectives: the MDB often works closely with Government entities to support policy objectives such as environmental sustainability, social inclusion, or higher educational attainment. By providing financing for projects that support these objectives, the MDB is helping to achieve important societal goals.

Whilst it is evident that the MDB has become a critical component in Malta's financial landscape, quantifying its impact in terms of support to the overall economy is difficult. The following section aims to shed some more light on the Bank's countercyclical role, its impact in debt financing to non-financial corporations and ensuring higher educational attainment.

Countercyclical role

Development banks play a countercyclical role in the economy, meaning they can help mitigate the negative effects of economic cycles, particularly during downturns or recessions. This countercyclical role is conducted by:

(i) Counteracting credit rationing: during downturns or periods of high uncertainty, commercial banks may become more risk-averse and reluctant to lend to businesses and individuals, resulting in credit rationing.

(ii) Supporting investment: during downturns, investment is likely to decline, leading to a further contraction of economic activity. Development banks can provide long-term financing for investment projects, which can help stimulate economic growth and job creation.

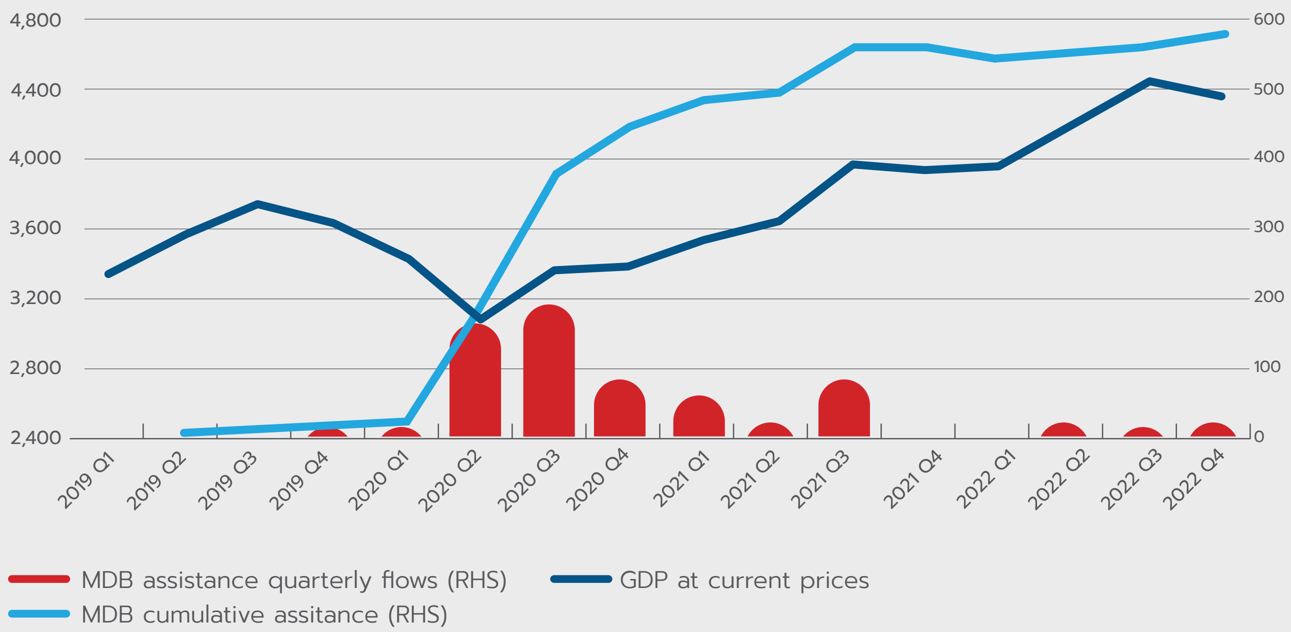
(iii) Providing stability to financial markets: Promotional banks are able to provide a degree of stability to financial markets during economic downturns by continuing to lend and invest, even when traditional banks and investors are holding back. This can help to prevent further market volatility and support confidence in the financial system.

During the global pandemic, this role came more to the fore and promotional banks took on a different dimension and started implementing countercyclical instruments. Likewise, in 2020, the MDB had rapidly shifted its focus on support measures to address the COVID-19 pandemic and its economic repercussions. Similarly, following the invasion of Ukraine by Russian forces in February 2022, the MDB was swift in its response with the launch of a package of three different measures open to all firms impacted by the war.

As can be seen in Chart 1, MDB's assistance through the COVID-19 Guarantee Schemes (CGS) and Ukraine crisis measures were in place when our local businesses were most in need. As at end 2022, a total of nearly €600 million in guarantees and loans to businesses were supported by the MDB. Over €350 million of this amount was sanctioned in the first two quarters of the CGS launch, that is, in the second and third quarter of 2020, coinciding with marked contractions in nominal GDP, estimated at 13.8% and 10.0%, respectively.

Since the launch of the first MDB scheme in mid-2019, the negative correlation coefficient between GDP and quarterly MDB assistance flows reaches 0.63, indicating a negative correlation, or movements in opposite direction, between the two variables (see Chart 1). This highlights the MDB's countercyclical role of intensifying its intervention at times of economic slowdown. This is not only evident in 2020, but also after, as economic activity started to rebound from the initial shock of the pandemic, and again towards the end of 2021 and the first quarter of 2022 when activity plateaued due to high uncertainty and intensified inflationary pressures.

CHART 1: COUNTERCYCLICAL ROLE (EURO MILLIONS)



As at end 2022, around €15.0 million in loans were sanctioned under the Ukraine support measures. Whilst the schemes are still open and it may be too early to assess the impact of these instruments, it is important to highlight that despite a relatively low take-up, these measures are important to provide reassurance and stability to markets, signalling that in case of need they can rely on MDB's assistance.

The impact of MDB's countercyclical role cannot be assessed in isolation, but as part of broader government economic regeneration measures targeted towards local businesses, which amongst others included wage supplements and subsidies on utility bills and fuels. Nevertheless, economic literature suggests that working capital problems may severely affect the supply side of the economy. In this regard, the MDB's working capital schemes during the pandemic and the ongoing war in Ukraine have been of critical importance to ensure that operating liquidity is constantly available to firms, which in turn is crucial for the efficient operation of businesses.

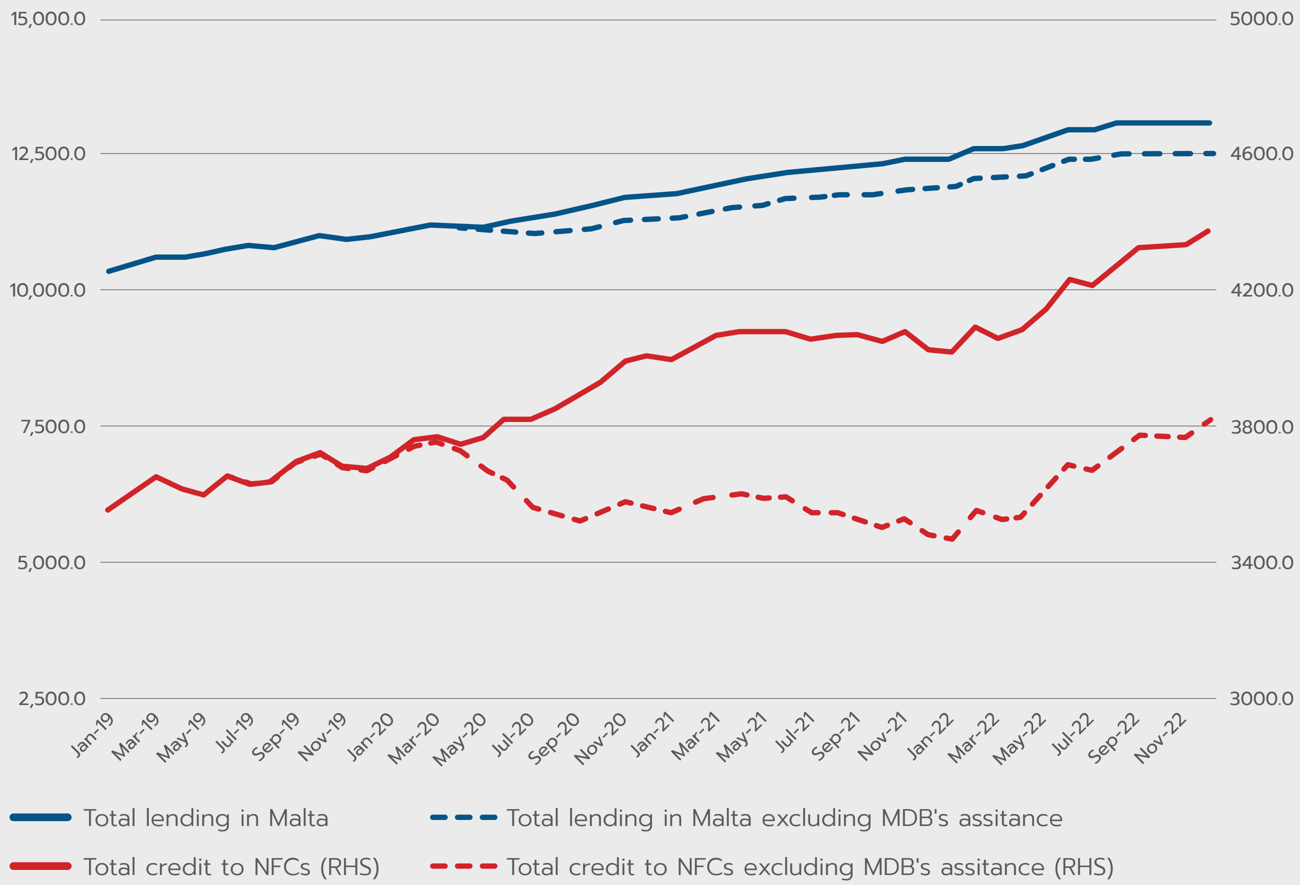
MDB's role in debt financing to Non-Financial Corporations (NFCs)

As already mentioned, by end 2022, the Bank's total financing volumes, including all guarantees and loans to local undertakings, stood at €565.8 million. This was predominantly spurred by the €482.6 million related to COVID-19 Guarantee Scheme (CGS), and to a lesser extent, by the €47.6 million related to the SME Invest facility. As can be seen in Chart 2, the impact of MDB's schemes is also substantial on a national level. Data published by the Central Bank of Malta show that outstanding loans to NFCs residing in Malta reached €4.4 billion by the end of 2022, with loans covered by MDB guarantee schemes accounting for 12.9% of this sum. Moreover, when looking at the bigger picture, over the same period, MDB's support to local businesses has reached close to 4.3% of total lending in Malta.[13]

Unsurprisingly, the impact of MDB's intervention became more pronounced with the introduction of the CGS in April 2020. Indeed, lending to NFCs (including loans supported by MDB) expanded by an annual rate of 9.0% by end 2020. Without MDB's intervention, such lending to NFCs would have contracted by 2.5%. Over time, as the economy started to recover from the pandemic, this marked gap started to narrow.

13 Total lending comprises credit to the general government, financial and non-financial corporations, insurance & pension funds, and households & non-profit institutions.

CHART 2: OUTSTANDING LOANS TO RESIDENTS OF MALTA (EURO MILLIONS)



Looking ahead, the recent quick increases in interest rates by the European Central Bank will most likely impact business investments. Monetary policy tightening can have both inflation-fighting and business investment-discouraging effects. In general, higher interest rates can help to fight inflation by making it more expensive for consumers and businesses to borrow money, which can reduce demand for goods and services and thus lower price pressures. On the other hand, higher interest rates can also discourage business investment by making it more expensive for companies to borrow money to finance new projects and expand operations. As a development bank, the MDB is monitoring these developments closely, and is adamant to continue assisting local businesses by offering schemes with the best credit terms possible. The Guaranteed Co-lending Scheme, launched in November 2022, and the SME Guarantee Scheme, which in 2023 will be replacing the SME Invest facility, should provide a very significant contribution to future MDB intervention.

Investment in Malta's human capital

During 2022, the Bank intensified its support in the upskilling of Malta's youths to strengthen the country's human capital. Thanks to the launch of Further Studies Made Affordable Plus (FSMA+) scheme, the MDB is ensuring equality of opportunity, where students, regardless of their financial background, can develop their potential without relying on the financial possibilities of their parents or relatives.

Cumulatively, the MDB has supported 429 students with more than €15 million in study loans by end 2022, the impact of such schemes is more difficult to capture as the induced multiplier effects take longer to materialise but are also more long lasting than any other economic injection. Whilst the initial round of the direct effect emanating from the monetary injection of the disbursed loans is largely leaked from the economy, as most beneficiaries are spending these funds abroad, the return in human capital is by far larger in the long run.

Investment in human capital leads to enhancement of the skills, knowledge, and abilities of individuals. From a macroeconomic perspective, investing in human capital is crucial as it guarantees a more solid basis for long-term economic growth and development.

This investment in human capital can impact the macroeconomy through:

(i) Higher productivity: As individuals gain more skills and knowledge, they can become more productive, leading to higher levels of output and economic growth.

(ii) Increased innovation: Investment in research and development and education can lead to new discoveries, technologies, and products that can improve the economy's overall competitiveness.

(iii) Higher wages: As workers become more skilled, they can command higher wages, which can lead to higher standards of living and overall economic growth.

(iv) Improved health outcomes: Investment in education is generally conducive to a healthier population, which can reduce healthcare costs, increase workforce participation, and in turn improves productivity.

(v) Reduced income inequality: a key factor in MDB's schemes is that such loans are available to all social cohorts. Thus, such investment in education and training can help reduce income inequality by providing individuals with opportunities to improve their skills and access higher-paying jobs.

SUSTAINING INFRASTRUCTURAL INVESTMENT

In line with MDB's vision, the financing of large infrastructure projects remains an important element in the Bank's overall strategy. Large-scale infrastructure projects can face difficulties in accessing the appropriate financing due to the long repayment period that is normally required to make them bankable, and the required funding may also be too large for most banks, in an institutional setting where syndication is not readily available.

During 2022, MDB has been approached by a number of entities to enquire on the possible role of the Bank in facilitating the financing of new investment related to such infrastructural projects. The MDB's clear preference is that these investments would be financed in conjunction with commercial banks, thereby highlighting the collaborative arrangement that the MDB would like to develop with the banks and also to foster the promotion of a syndicated loan market in Malta. The emphasis has mostly been on infrastructural projects related to education, sports, health, care homes, and affordable housing. Some of these projects are at an advanced discussion stage, whilst others are still at early stages and require further input from the beneficiary, which will help the bank in its analysis.

The MDB is currently exploring new funding opportunities from other multilateral development banks to support these specific projects with a social dimension.

SIGNIFICANT EVENTS

LAUNCH OF THE FSMA+

In February 2022, following MDB's open call for expression of interest, Bank of Valletta plc was selected to intermediate the Further Studies Made Affordable Plus (FSMA+) scheme, a Financial Instrument implemented by the MDB and funded by Malta's European Social Fund Operational Programme.

The official agreement was signed by BOV Chief Retail Banking Officer Kenneth Farrugia and MDB Chairman Prof Josef Bonnici in the presence of BOV Chairman Dr Gordon Cordina, Hon. Silvio Schembri, Minister for the Economy and Industry and Hon Dr Clifton Grima, Minister for Education and Sport and the Hon. Dr Stefan Zrinzo Azzopardi, Parliamentary Secretary for European Funds.

INVESTMT WORKSHOP

Following bi-lateral meetings with 25 different stakeholders, on 27 April 2022 the MDB organised the InvestMT workshop, bringing together all stakeholders involved to share with them the gaps identified in the local equity ecosystem and to discuss the potential approaches to address them. This event was supported by the European Commission's Technical Support Instrument and was facilitated by Deloitte Malta who were coordinating this project. The workshop was aimed at helping the MDB to continue bridging market gaps, particularly relating to the possibility of introducing financial instruments focusing on equity and start-ups.

The event was attended by more than the 60 participants, including representatives from the European commission's DG Reform, the European Investment Fund and other international experts. The stakeholders' views and concerns that were shared during the workshop were used as the main basis for the recommendation of two financial instruments that can be potentially applied in Malta's equity and start-up ecosystems.

COLLABORATION WITH MCST ON THE GO-TO-MARKET LOAN ASSISTANCE PROGRAMME

After a number of technical meetings with the Malta Council for Science & Technology (MCST), in October 2022, the MDB has joined MCST in developing a new product, the Go-To Market loan assistance scheme to support start-ups in commercialising technological innovations. These beneficiaries can get up to €750,000 in loans to invest in their growing business on top of MCST's grants.

PARTICIPATION IN CONFERENCES ON GREEN AND SUSTAINABLE FINANCING

During the year under review, MDB's CEO and other senior staff participated in various conferences and events promoting green and sustainable economic growth.

The MDB is proud to have supported the Malta Employers' Association in hosting a national conference, bringing stakeholders together in addressing the challenges ahead and in publishing the conclusions and recommendations made during this event. In March 2022, MDB's CEO Mr Paul V. Azzopardi, was part of a delegation that visited H.E. The President of Malta Dr George Vella during the launch of MEA's *Memorandum* to Political Parties: *Economic Sustainability, Governance and Wellbeing*- collating the Association's efforts in this regard.

During the 2022 IFS Annual Conference, MDB's CEO, shared his views during an expert panel discussion focusing on the role of sustainable finance in supporting Maltese businesses through a sustainable transition. He also explained, by way of practical examples, how the MDB is supporting the green transition.

At the Malta Chamber of SMEs national SME Conference, MDB's Chief Business Development Officer Mr Joseph Darmanin explained how the MDB acts as an enabler for the green and digital transition by facilitating favourable financing at lower rates, less collateral requirements and a longer repayment period.

Following MDB's participation in the first "National Climate Change Conference" in 2021, in September 2022, MDB's Senior EU Affairs Officer Mr Silvio Attard represented the Bank in an inter-governmental and key stakeholders' seminar on Malta's transition towards a greener economy. The MDB representative participated in panel discussions on "Financing the greening of Maltese business models: The Challenges and Opportunities" where the Bank's drive in promoting environmentally sustainable growth was highlighted.

In November, Mr Joseph Darmanin was invited to participate in Grant Thornton's annual conference: Shaping Malta's future. During an expert panel discussion on 'Financing the change', he highlighted the current challenges related to sustainability and how the MDB can help to maximise the impact of sustainable finance.

PARTICIPATION IN OTHER CONFERENCES AND EVENTS

In May 2022, Mr Silvio Attard was invited to participate in a panel discussion during the Mare Summit 2022. Mr Attard spoke about the role of the Bank in supporting the tourism industry, particularly during the pandemic. He also shared his views on the opportunities and challenges that the tourism and real estate sectors are facing in the current economic environment.

In November 2022, during the SME National Forum 2022 hosted by the Malta Employers' Association, MDB's CEO Mr Paul V Azzopardi joined a panel discussion with a number of industry stakeholders where he shared his views on addressing the need to ensure the right skills for Malta's future and competitiveness.

During the same month, MDB representatives attended a conference organised by the Malta Chamber of SMEs during the 2022 SME Week on SME's resource maximisation. MDB's Chief Business Development Officer Mr Joseph Darmanin, and the Chief Credit Officer Ms Maria Xuereb shared details of how businesses stand to benefit from MDB's schemes.

PRESENTATION DURING THE FI-COMPASS EVENT IN BRUSSELS

In October, the MDB was invited by Fi-Compass to deliver a joint presentation with the Managing Authority on the success of the FSMA scheme, in Brussels. Mr Silvio Attard, MDB's Senior EU Affairs Officer focused on the implementation side of the financial instrument, and on the outreach and benefits of the scheme. This presentation was in the context of an Fi-Compass event "Supporting education and learning with financial instruments". The event was followed by the launch of an Fi-Compass manual 'Financial instruments for education and learning' which explores the scope of support that managing authorities can provide in the fields of education and learning. This manual features the FSMA as one of three best case studies in the EU.

ELTI'S GENERAL ASSEMBLY IN MALTA

On 28 October the MDB welcomed senior officials from 30 other promotional banks as the Bank hosted the 2022 annual General Assembly of the European Long-Term Investors Association (ELTI).

ELTI members represent a European-wide network of National Promotional Banks and Institutions which offer financial solutions tailored to the specific needs of their respective country and economy.

Over the past years, ELTI has strengthened its role as a visible stakeholder which represents, at both European and national levels, the position of its 31 current members, which are notably made up of National Promotional Banks and Institutions.

During their meeting in Malta, the promotional banks discussed the key lessons learnt from the respective support measures to the multiple crises which affected the European economy in the past couple of years, namely the COVID-19 pandemic, the Russian invasion of Ukraine and the supply-related headwinds and inflationary pressures which are now leading to a rise in interest rates in most countries.

FIFTH ANNIVERSARY OF THE MDB

On 23 November 2022, on the occasion of the fifth anniversary of the establishment of the MDB, the Hon. Prime Minister Dr Robert Abela, in the presence of the Minister for Finance and Employment, Mr Clyde Caruana, and other esteemed guests, officially inaugurated the new premises of the MDB, in Floriana. During a brief ceremony, the Prime Minister announced the launch of MDB's two new financing schemes at favourable rates that will be facilitating investment of up to €180 million. He commended these schemes for the advantageous financing rates they offer and their importance in backing economic regeneration at a time of unprecedented challenges. He also praised MDB's role in strengthening market confidence during the pandemic.

In his intervention during this event, MDB's Chairman Prof. Josef Bonnici stated that the main objective of the Bank is to keep supporting the economic and social development of Malta. He added that together with commercial banks and other strategic entities, the MDB will continue addressing the key challenges faced by underserved sectors, particularly SMEs when seeking access to finance. MDB's CEO introduced the two new financing schemes and stated that in the relatively short period of five years, the MDB managed to reach over 700 businesses and almost 400 students, providing guarantees and loans of around €600 million, and safeguarding over 40,000 jobs.

INTERNATIONAL AFFILIATIONS AND COOPERATION

MDB'S MEMBERSHIP WITH EUROPEAN ASSOCIATIONS AND NETWORKS

During 2022, the MDB continued to build a value-laden relationship, and collaborated with a number of international associations, multinational development institutions and foreign development banks. The MDB is a member of the European Association of Public Banks (EAPB), the European Long-Term Investors (ELTI), the Network of European Financial Institutions for SMEs (NEFI) and the European Association of Guarantee Institutions (AECM). Membership in these associations is very beneficial for the MDB, these benefits include exchange of information, interfacing and sharing of technical experiences and best practices; being part of a strong lobby group representing their Members at a European level; participating in consultations and discussions with EU institutions on financial instruments, regulations and legislative proposals, as well as facilitating dialogue and strategic alliances with other development banks and institutions. To this end, during the year under review, membership in these associations was important to help MDB to keep abreast with the latest EU discussions in particular regarding technical dialogues on state aid developments, assistance in the wake of the war in Ukraine, the InvestEU, EU taxonomy and green financing amongst others.

In 2022 MDB representatives attended a number of meetings and seminars organised by these networks. Some of the meetings attended were the permanent working group meeting of the NEFI, NEFI's High Level Meeting, ELTI's CEOs meetings, AECM General Assembly and EAPB's Annual CEO conference. As highlighted earlier, the 2022 ELTI General Assembly was hosted by the MDB in Malta.

LAUNCH OF THE INVESTEU IN MALTA

In September 2022, a delegation from the European Investment Bank (EIB), led by EIB Vice-President Gelsomina Vigliotti came to Malta to strengthen cooperation with public and private partners, as well as launching the InvestEU programme in the country. During their stay in Malta, Ms Vigliotti and her team attended a meeting at MDB's premises where a number of topics were discussed. This fruitful meeting will serve to continue strengthening the collaborative relationship between the MDB and the EU's financing arm.

RISK AND CAPITAL MANAGEMENT

In terms of the Malta Development Bank Act (Act No XXI of 2017), the Bank takes risks consciously within the limits of prudence by applying the principles of sound banking operations to support viable projects that could be facing difficulties to access the required financing, in pursuance of the MDB's overriding objective of facilitating entrepreneurship and socio-economic development in Malta.

The MDB aims to manage risks in an informed and proactive manner, in accordance with its Risk Management Framework, such that the level of accepted risk is consistent with its underlying business activity, and that the MDB understands and is able to manage or absorb the impact of any risks that may materialise.

Towards this end, the MDB developed an organisational structure based on a framework that promotes a transparent and efficient, enterprise-wide risk management culture wherein the behaviour, attitude and decisions reflect risk awareness and mitigation. Great importance is accordingly given to the risk governance structure, which includes socioeconomic value statements, codes of conduct and ethics, policies, procedures and risk assessments. Moreover, the Risk Management function continuously strives to instil a cultural awareness that helps to establish a robust risk management framework and risk control processes across the Bank.

RISK GOVERNANCE

The risk governance structure is designed to allow for the proper understanding of existing and emerging risks through cooperation between the Board of Directors, the three lines of defence and the Supervisory Board in order to effectively execute the risk management controls. This collective effort seeks to ensure that MDB's risk culture is recognised as an essential factor to achieve its entrepreneurship and socio-economic objectives.

Supervisory Board

The MDB Act provides that the Bank is subject to the prudential oversight, regulation and supervision of a Supervisory Board appointed in terms of article 37(1) of the Act. In view of the MDB's public policy mandate, the MDB is exempt from the EU Capital Requirements Directive (CRD), the EU Capital Requirements Regulation (CRR) and other banking regulations, in terms of article 2(5) of the CRD as amended by Directive (EU) 2019/878 of the European Parliament and of the Council. The MDB is instead subject to supervision under ad hoc local regulation which should enable the MDB to fulfil its promotional role and public policy mission more effectively, while ensuring proper and sound banking conduct.

In terms of article 40 of the Act, the Supervisory Board is composed of officials from the Malta Financial Services Authority, the Central Bank of Malta, the Ministry for Finance, and two independent professionals with banking or regulatory experience. The Chairperson is appointed by the Minister from among the two independent professionals after consultation with the Opposition. At end-2022, the Supervisory Board was chaired by Mr John Cassar White and included Mr Oliver Bonello, Deputy Governor Central Bank of Malta, Dr Christopher Buttigieg, Chief Officer Supervision at Malta Financial Services Authority, Mr Paul Zahra, Permanent Secretary, Ministry for Finance and Employment, and Dr Chris Cilia, as an independent professional. Mr Zahra was appointed to the Supervisory Board in June 2022 following the retirement of Mr Alfred Camilleri as Permanent Secretary, Ministry of Finance and Employment. Following the expiry of the first term of these appointments on 11th December 2022, the Minister for Finance and Employment re-appointed the said members for a period of five years up to 10th December 2027.

In terms of article 37 of the Act, the role of the Supervisory Board is to oversee the policy pursued by the Bank and its implementation, to review the general state of affairs of the Bank, and to issue directives relating to the prudential conduct of business, capital adequacy, and risk strategy of the Bank. It shall exercise monitoring, advisory and regulatory powers to ensure sound governance and best practices by the MDB. It has the right to request any information it deems necessary. It supervises the MDB's corporate governance, as well as the MDB's compliance with regulations, the effectiveness of the Bank's management systems and internal controls, the business performance, asset-liability management, remuneration, and other aspects as specified in Part III of the Act.

The Supervisory Board also has the power to communicate analysis and recommendations to the MDB Board of Directors and to the Minister responsible for the Bank. The Supervisory Board Regulations are prescribed in the Second Schedule of the Act.

Board of Directors

The Board of the MDB is responsible for setting the risk appetite and overseeing and guiding risk management activity across the MDB. The Board has mandated that risk management be integrated and embedded into the tone and culture of the MDB, with the management team of the MDB responsible for regularly reviewing the risk register and individually confirming that the stated controls are in place. In order to effectively accomplish its tasks, the Board is assisted by three committees (namely the Audit Committee, the Ethics and Governance Committee and the Risk Committee) that are responsible for a wide range of activities as defined in the Corporate Governance Statement of this Annual Report. The members of the Board of Directors are listed on page 7.

Three lines of defence

The MDB is committed to promote a culture of integrity, high ethical standards and strong risk awareness. All individuals in the Bank are expected to contribute to and promote a sound risk culture to maintain a strong internal control environment and facilitate the operation of the Bank's enterprise risk management framework. The MDB has adopted a clear governance structure backed by a set of policies and procedures to support the presence of a sound risk culture.

MDB applies such a sound risk culture by following the three-lines-of-defence model where the first line of defence consists of the risk-taking business functions. The business functions are responsible for day-to-day risk management within their remit and are required to comply with the relevant internal policies, regulations and procedures. The second line, which incorporates the Risk and Legal & Compliance functions, and the third line, which consists of the Internal Audit function, provide oversight, monitoring and audit activities. They also conduct independent evaluations and reporting to the senior leadership team on the effectiveness of the Bank's internal control environment.

Principal Risks

The MDB is exposed to a variety of risks which have the potential to affect its financial and operational performance. The Enterprise Risk Management Framework establishes the processes to identify, assess, report and mitigate risk. The MDB has identified the following principal risks which may adversely affect the achievements of its objectives.

RISK	DESCRIPTION OF THE RISK	RISK MITIGATION MEASURE
STRATEGIC RISK	The MDB relies on demand from local businesses to meet its key strategic objective of providing credit to enterprises in Malta to address financing gaps in the Maltese credit market. Should the MDB fail to structure its products appropriately and deploy a suitable delivery strategy, there is a risk that businesses will not participate as envisaged and will not have an appetite for products offered by the MDB.	The MDB consults prospective partner banks and other relevant stakeholders at an early stage of a product offering design. The MDB also conducts soft-market testing.

CREDIT RISK	The MDB is exposed to the risk that a borrowing counterparty defaults on its obligations and fails to repay its debt in full, resulting in losses to the MDB. The MDB is exposed to credit risk (i) due to its loans to the borrowers and (ii) in respect of its risk-sharing schemes, due to loans made to final beneficiaries which have been guaranteed by the MDB.	The MDB controls credit risk through its credit risk policies and prescribed procedures that determine the internal control system with an objective to act preventively. The credit risk management framework represents the most important part of the MDB's business policy and an important factor in its business strategy. Therefore, this area is regulated by separate documents, namely: (a) the Credit Risk Policy that applies to all phases of the credit process (from the development of schemes and borrowing proposals, to risk assessments, monitoring of obligor and loan repayments) and (b) the Credit Risk Mitigation Policy, which sets the Bank's credit risk mitigation measures which are ancillary to, and complement, core credit risk considerations to ensure good and responsible lending. Other measures include the monitoring of key risk indicators and assessment of credit risk by the Risk Committee and the Board.
LIQUIDITY RISK AND INTEREST RATE RISK	Liquidity risk is the risk that the MDB cannot meet its short-term debt obligations without incurring material losses arising from the pricing of wide liquidity premia. It is the risk of loss arising from a situation where there will not be enough cash to fund day-to-day operations and that the MDB will be unable to convert assets into cash in a timely manner without incurring material losses. The MDB is also exposed to interest rate risk on its interest rate-sensitive receivables (for example securities) and interest rate-sensitive payables (for example funding positions). Adverse movements in the interest rates may result in a negative impact on the net interest income and the economic value of the equity of the MDB.	The MDB maintains the necessary level of liquidity reserves, continuously monitors current and planned liquidity, and provides sufficient funds necessary for the timely settlement of obligations and disbursements under committed loans and planned commitments. Moreover, liquidity risk is managed in a preventive manner to minimize the maturity, principal repayment and interest payment mismatch of loans provided during the course of loan programmes and other financing. The MDB seeks, to the extent possible, to reflect in its lending facilities the interest rate risk profile of the underlying funding agreements to minimize material interest rate mismatches. Liquidity and interest rate risks are managed by the ALCO, a sub-committee of the Risk Committee, and the Board of Directors.
OPERATIONAL RISK	The MDB is exposed to the risk of a loss resulting from inadequate or failed internal processes, people, and systems or from external events. When material, such risk could impact the reputation of the MDB, its financials or, at the extreme, its ability to meet its statutory purpose and strategic objectives.	The MDB controls operational risks through the Operational Risk Policy and Risk Register. The Policy establishes the basic principles for operational risk management. The Risk Register comprises of a list of identified risks, linked to the Bank's various processes. These operational risk events are ranked in terms of expected impact and likelihood. The Risk Committee and Board of Directors approve responses that mitigate the residual risks of the MDB's main processes.

CAPITAL MANAGEMENT

Capital management is a fundamental process of the Bank's risk management function. The aim is to create a common framework of action that addresses and manages all types of risks with a view to ensure that adequate mitigating actions are taken to reduce the negative impacts of adverse movements on the operations of the Bank and on the financial statements. The MDB is not subject to externally imposed capital requirements albeit the MDB Act lays down certain capital requirement parameters. The Bank is committed to ensuring it is adequately capitalised to accommodate for eventual balance sheet growth and to provide a buffer for potential credit and other losses, both in the current as well as in more severe but plausible economic scenarios.

In order to ensure that the MDB is adequately capitalised to absorb any potential losses, the Bank applies the following structured approach:

- Complement the current and future business planning with adequate capital planning to meet the minimum level of capital as internally determined by the MDB, while maintaining the risk profile set by the Board of Directors within the Bank's public policy objectives.
- Ensure that sufficient capital is maintained to cover extreme but plausible shocks due to volatilities inherent in the financial markets and cyclical macroeconomic downturns.
- Ensure efficient use of capital and in return, to the extent possible, maximise the delivery of the Bank's public policy objectives.

This structured approach ensures that the MDB adheres to its internal minimum level of capital such that it remains adequately capitalised to absorb any potential losses whilst fulfilling its public policy objectives as set by the Board of Directors.

Own funds

Although the MDB falls outside of the scope of the CRR and CRD, the MDB is committed to ensure it is adequately capitalised. The MDB is committed to holding a capital buffer that accommodates eventual balance sheet growth and provides an adequate buffer for potential losses in the current and in more severe but plausible scenarios. The paid-up share capital of the MDB as at 31 December 2022 stood at €80 million, up from €60 million as at end 2021. The share capital was provided by the MDB's sole shareholder, the Government of Malta.

As at end December 2022, the MDB's exposure in the form of guarantees stood at €7.9 million, of which €6.7 million are guaranteeing outstanding balances and €1.2 million are guaranteeing the approved credit that is still to be drawn by the borrower. Approximately, 20% of this aggregate exposure is mitigated by collateral. In terms of direct credit, the MDB's exposure stood at €19.9 million. A large share of this exposure is covered by a government guarantee and other collateral.

Within this context, the capital position of the Bank is considerably strong and significantly above the internally set minimum capital adequacy level.

FINANCIAL STATEMENTS

31 DECEMBER 2022

MDB

5 YEARS

BANK MALTI GĦALL-IŻVILUPP

MALTA DEVELOPMENT BANK

CONTENTS

DIRECTORS' REPORT

The Directors present their Annual Report and the Audited Financial Statements of the Malta Development Bank ('the Bank' or 'the MDB') for the year ended 31 December 2022.

PRINCIPAL ACTIVITIES

The Bank was set up by the Act which was passed on 5 May 2017 and came into effect on 24 November 2017 in terms of Legal Notice No. 340 of 2017. The Bank is fully owned by the Government of Malta.

The Bank's primary objective is to contribute towards sustainable economic development by promoting inclusive and environmentally sustainable economic growth and infrastructure development. It is principally engaged in addressing market failures by offering financing facilities to support productive and viable operations where the market is unable or unwilling to accommodate such activities on its own in whole or in part. The Bank's operations in support of SMEs are mainly intermediated through the local credit institutions and are focused on the provision of guaranteed or co-financing facilities. The Bank's facilities for infrastructural projects' finance can take the form of first-tier operations in the form of direct lending and co-financing. Such funding can be directed to national social and economic infrastructure by public and private sector entities.

REVIEW OF BUSINESS DEVELOPMENTS

Following the outbreak of the COVID-19 pandemic in early 2020, the strategic priority of the Bank shifted from stimulating new investment to providing urgent liquidity support to safeguard and preserve the continuity of national economic activity. In executing its mission of providing urgent liquidity support to Maltese businesses which were severely impacted by the pandemic, the Bank was entrusted to develop, administer, and implement the COVID-19 Guarantee Scheme ('CGS'), on behalf of the Government of Malta, to assist entities in financing working capital at a subsidised interest rate. The scheme was launched on 2 April 2020 through the intermediation of nine commercial banks.

More recently, in response to the outbreak of war in Ukraine in early 2022, the MDB launched a number of urgent liquidity support measures, backed by a government guarantee, to ensure security of supply of grains including wheat, animal feed, fuels and any other business whose liquidity was negatively impacted by the war. The MDB continued to create and offer de-risking instruments to enable the provision of more accessible and affordable working capital loans, thus reducing the impact on the affected economic operators. The MDB provided a portfolio of direct loans under the Subsidised Loan Scheme to the major local grain importers of €14.2 million.

The Bank continued to attract financing of new investment through its SME Loan Guarantee Scheme which is intermediated through a commercial bank. The outstanding loan portfolio covered by this scheme increased substantially during the year from €25.2 million in 2021 to €33.5 million by the end of 2022.

Following the launch of the Subsidised Loan Scheme, the MDB in June 2022 rolled-out a further €150 million in emergency liquidity support to businesses: the Liquidity Support Guarantee Scheme ('LSGS') as part of an aid package in response to the Ukraine crisis. The LSGS consists of two measures; one open to all undertakings affected by the crisis ('LSGS-A') and the other specific to the fuel and oil importers ('LSGS-B'). Both these Schemes were intermediated through local banks. There were no sanctioned loans in respect of the LSGS as at 31 December 2022.

In the last quarter of the year under review, the Bank launched the SME Guarantee Scheme ('SGS') which is aimed at enhancing SME access to bank credit for new investment as well as other purposes; including for working capital related to new investment and business transfers. In collaboration with the MCST, the Go-To-Market was launched as a sub-scheme of the SGS, allocating €1.5 million specifically to Research & Innovation projects.

During the same period, the Bank launched the Guaranteed Co-Lending Scheme ('GCLS'), a risk-sharing facility for larger facilities, involving co-lending between the MDB and the accredited commercial banks on a 50:50 basis and a guarantee of 60% on the commercial bank's loan. As of 31 December 2022, two projects were being financed under the GCLS both focusing on the innovative digitalisation sphere, having a total sanctioned amount by the MDB of €6.05 million.

More detailed information on these schemes is provided in the Business Review section of the Annual Report.

Both the SGS and GCLS were initially backed by the EGF and following the expiration of this EGF guarantee at the end of 2022, the MDB is seeking the support of the EIF under the Invest-EU products.

The Further Studies Made Affordable (FSMA) which was set up in collaboration with the Managing Authority of EU funds, has remained a popular financial instrument aimed at reducing the financing cost of students' studies locally and overseas. After the FSMA portfolio of €9.25million was fully taken up by February 2022, the MDB continued to build on its success by launching the Further Studies Made Affordable Plus ('FSMA+') scheme which offered a portfolio of study loans of up to €15million.

During this period, the Bank also supported large-scale infrastructure projects, which experienced difficulties in accessing the appropriate financing through commercial banks. The MDB has provided a co-financed loan for of €9.3 million for the construction and completion of a University campus residence complex.

FINANCIAL PERFORMANCE

The Bank has continued to strengthen its financial performance, and for the first time generated an operating profit while the risk profile in the Bank's portfolio remained low and stable. This is the result of prudent risk management operations based on sound banking practices. The Bank generated a net operating profit before provisions during the year of €1.2 million compared to a loss of €0.4 million reported for the prior year.

The net profit generated after provisions as shown in the Statement of Comprehensive Income is €0.65 million compared to a loss of €1.1 million in the previous year. This is primarily driven by an increase in net interest income from its lending operations, higher yielding financial investments, and an increase in administrative fee income from the management of guarantee schemes.

The progressive increases in interest rates by the European Central Bank, is a major departure from the very accommodating monetary policy experienced over the past decade. This development has offered MDB the opportunity to save the costs incurred due to the negative rates which were charged by local banks and the Central Bank of Malta when depositing excess liquidity with them. During the reporting period, the Bank generated a positive net interest margin of €509,541 (2021: negative net interest margin of €105,374) which was attributed partially to the increase in interest rates coupled with the acquisition by MDB of additional fixed income debt securities. As a result, the average yield on financial assets was substantially higher at 3.4% compared to the prior year of 0.4%.

The Bank's financial investment portfolio comprises a mix of fixed income debt securities which yielded a positive return of €160,575 compared to an interest income of €4,527 generated during the prior year.

Additionally, the Bank generated higher interest income from its portfolio of loans and advances to customers as new facilities and loan commitments were drawn down during the year. Total interest income for the reporting year from the Bank's direct lending facilities amounted to €321,342 (2021: €13,697).

Moreover, the Bank continued to deploy its excess liquidity through money market placements with local banks in line with the credit risk appetite of the bank. Interest income from bank placements amounted to €189,826 (2021: €152,940).

In its administrative capacity, the Bank generated administrative fee income from the CGS during 2022 of €2.6 million (2021: €1.6 million). During 2022, guarantee fee income from the SME Invest amounted to €154,418 (2021: €86,335). The increase in such income is attributed mainly to the growth and maturity of the loan portfolios underlying such schemes subject to the applicable rates established by the risk sharing arrangements with partner banks.

The Bank generated additional income of €44,795 (2021: €33,676) primarily from rental income.

Expected credit loss ('ECL') allowances increased by €528,914 (2021: €709,679) during the year to allow for credit risks mainly resulting from the higher volume of outstanding credit exposures comprising direct loan facilities and financial guarantee contracts.

A marginal year-on-year increase in operating costs of €138,709 was reported which, in the context of the continued expansion of activities driven by the management and administration of emergency loans and development of new guarantee schemes, is the outcome of the continuous drive by management to optimise the Bank's operational efficiency.

During 2022, the Bank registered a growth in its balance sheet of €18.4 million. Total assets stood at €99 million (2021: €81 million) as at the period end.

The Bank funds its operations and investments through its earnings from guarantee, lending operations and financial investments, share issuance or external funding sources. During the year, the Government subscribed to an additional €20 million of paid-up capital in terms of Article 10 of the MDB Act and in line with the Bank's business plan. At 31 December 2022, the Government of Malta held shares in MDB totalling €80 million, comprising the entire paid-up share capital of the Bank.

The MDB supplements the paid-up capital with bilateral borrowing from international development institutions. To this effect, the MDB has entered into a global loan agreement with the KfW Group. In addition, a loan agreement of €60 million was signed with the European Investment Bank under the Multiple Beneficiary Intermediated Loan (MBIL) programme. These funds will be utilised by the MDB to finance the facilities to support SMEs, mid-caps and infrastructure projects by private and public-sector entities. The support of the EIB and KfW enables a transfer of benefit in the form of a lower interest to the final beneficiaries. During the year under review, partial repayments of the fixed term loan with KfW (see Note 12) amounted to €3.9 million (2021: €5.3 million). As at 31 December 2022, the Bank had outstanding borrowings of €15.8 million from the KFW loan facility. As of the end of the year, such funding was fully deployed through projects including direct lending to SMEs and large cap infrastructure.

Other results may be referred to in the Statement of Financial Position and Statement of Comprehensive Income on pages 99 and 100 respectively.

PRINCIPAL RISKS AND UNCERTAINTIES

The principal risks and uncertainties facing the Bank are:

- **Strategic Risk** – The Bank relies on demand from the local businesses to meet its key strategic objective of providing credit to enterprises in Malta to address failures in the Maltese credit market. Should the Bank fail to structure its products appropriately and deploy a suitable delivery strategy, there is a risk that businesses will not participate as envisaged and will not have an appetite for products offered by the Bank.

- **Credit Risk** – The MDB is exposed to the risk that a borrowing counterparty defaults on its obligations and fails to repay its debt in full, resulting in losses to the MDB. The MDB is exposed to credit risk (i) due to its loans to the borrowers and (ii) in respect of its risk sharing schemes, due to loans made to final beneficiaries which have been guaranteed by the MDB.

- **Liquidity risk and Interest rate risk** - Liquidity risk is the risk that the MDB cannot meet its short-term debt obligations without incurring material losses arising from the pricing of wide liquidity premia. It is the risk of loss arising from a situation where there will not be enough cash to fund day-to-day operations and that the MDB will be unable to convert assets into cash in a timely manner without incurring material losses. The MDB is also exposed to interest rate risk on its interest rate sensitive receivables (example securities) and interest rate sensitive payables (example funding positions). Adverse movements in the interest rates may result in a negative impact on the net interest income and the economic value of the equity of the MDB.

- **Operational Risk** – The MDB is exposed to the risk of losses resulting from inadequate or failed internal processes, people, and systems or from external events. When material, such risk could impact the reputation of the MDB, its financial position or, at the extreme, its ability to meet its statutory purpose and strategic objectives. As part of operational risk, the Bank considers compliance and legal risks. The Bank's activities are subject to EU State aid and other regulations. Therefore, there is a risk that the Bank fails to comply with these regulations, resulting in reputational or financial damage to the Bank.

Note 2 to the financial statements provides further details on risks faced by the Bank.

BOARD OF DIRECTORS

During the year the following individuals served as Directors. The process for appointment and removal of Directors by the Minister for Finance is governed by Article 21 of the Act.

DIRECTOR	POSITION AT 31 DECEMBER 2022	INITIAL APPOINTMENT DATE	INITIAL APPOINTMENT EXPIRY	REAPPOINTMENT EFFECTIVE DATE	REAPPOINTMENT EXPIRY
Prof. Josef Bonnici	Chairman	11 December 2017	11 December 2023	N/a	N/a
Mr Anthony Valvo	Independent Non-executive Director	11 December 2017	11 December 2022	11 December 2022	11 December 2025
Prof. Rose Marie Azzopardi	Independent Non-executive Director	11 December 2017	11 December 2022	11 December 2022	11 December 2025
Dr Michele Cardinali	Independent Non-executive Director	14 April 2021	14 April 2026	N/a	N/a
Prof. Philip Von Brockdorff [1]	Independent Non-executive Director	25 February 2022	25 February 2028	N/a	N/a
Mr Steve Ellul[2]	Independent Non-executive Director	22 June 2022	22 June 2027	N/a	N/a
Mr William Spiteri Bailey[3]	Independent Non-executive Director	20 December 2022	10 December 2023	N/a	N/a
Ms Jacqueline Camilleri[4]		11 February 2021	4 November 2022	N/a	N/a
Mr Robert Borg[5]		11 December 2017	25 February 2022	N/a	N/a
Mr Paul Cardona[6]		11 December 2017	4 March 2022	N/a	N/a

These appointments are valid for the periods stipulated in Article 21(4), (5) and (6) of the Act.

Dr Bernadette Muscat, Chief Legal and Compliance Officer served as Secretary to the Board during the period ending 31 December 2022.

1 Prof. Philip von Brockdorff was appointed on 25 February 2022 in lieu of Mr Robert Borg.
2 Mr Steve Ellul was appointed on 22 June 2022 in lieu of the late Mr Paul Cardona.
3 Mr William Spiteri Bailey was appointed on 20 December 2022 in lieu of Ms Jackie Camilleri.
4 Ms Jacqueline Camilleri resigned on 4 November 2022.
5 Mr Robert Borg resigned with effect from 25 February 2022.
6 Mr Paul Cardona demised on 4 March 2022.

DIRECTORS' RESPONSIBILITIES

The directors are responsible to ensure that the financial statements are drawn up in accordance with the requirements of the Act. The Act requires the directors to approve financial statements which give a true and fair view of the financial position of the Bank as at the end of each reporting period and of the profit or loss for that period.

In approving these financial statements, the Directors are responsible for:

- ensuring that the financial statements have been drawn up in accordance with International Financial Reporting Standards as adopted by the EU;
- selecting and applying appropriate accounting policies;
- making accounting estimates that are reasonable in the circumstances; and
- ensuring that the financial statements are prepared on the going concern basis unless it is inappropriate to presume that the Bank will continue in business as a going concern.

The Directors are also responsible for designing, implementing and maintaining internal control as they determine necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and that comply with the Act. They are also responsible for safeguarding the assets of the Bank and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The financial statements of the Malta Development Bank for the year ended 31 December 2022 are included in the Annual Report 2022, which is published in hard-copy printed form and is available on the Bank's website. The Directors are responsible for the maintenance and integrity of the Annual Report on the website in view of their responsibility for the controls over, and the security of, the website. Access to information published on the Bank's website is available in other countries and jurisdictions, where legislation governing the preparation and dissemination of financial statements may differ from requirements or practice in Malta.

After reviewing the Bank's plans for the coming financial years, the Directors are satisfied that at the time of approving these financial statements, it is appropriate to adopt the going concern basis in preparing these financial statements.

No significant events have taken place since the financial reporting date that would have otherwise required adjustment to and/or disclosure in this Annual Report.

AUDITORS

PricewaterhouseCoopers have indicated their willingness to continue in office and a resolution for their re-appointment will be proposed at the Annual General Meeting.

Approved by the Board of Directors on 28 March 2023 and signed on its behalf by:

PROF. JOSEF BONNICI
Chairperson

PROF. PHILIP VON BROCKDORFF
Director

Registered Address

Malta Development Bank
5 Market Street,
Floriana, Malta

Independent auditor's report

To the Shareholders of Malta Development Bank

Report on the audit of the financial statements

Our opinion

In our opinion:

- The financial statements give a true and fair view of the financial position of Malta Development Bank (the Bank) as at 31 December 2022, and of the Bank's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the EU; and
- The financial statements have been prepared in accordance with the requirements of the Malta Development Bank Act (Cap. 574).

What we have audited

Malta Development Bank's financial statements, set out on pages 11 to 65, comprise:

- the statement of financial position as at 31 December 2022;
- the statement of 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 notes to the financial statements, which include significant accounting policies and other explanatory information.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report.

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

Independence

We are independent of the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) issued by the International Ethics Standards Board for Accountants (IESBA Code) together with the ethical requirements of the Accountancy Profession (Code of Ethics for Warrant Holders) Directive issued in terms of the Accountancy Profession Act (Cap. 281) that are relevant to our audit of the financial statements in Malta. We have fulfilled our other ethical responsibilities in accordance with these Codes.

Independent auditor's report - continued

To the Shareholders of Malta Development Bank

Other information

The directors are responsible for the other information. The other information comprises the Directors' report (but does not include the financial statements and our auditor's report thereon) which we obtained prior to the date of this auditor's report, and the Malta Development Bank's complete Annual Report, which is expected to be made available to us after that date.

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

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the Malta Development Bank's complete Annual Report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance in accordance with the International Standard on Auditing.

Responsibilities of the directors and those charged with governance for the financial statements

The directors are responsible for the preparation of financial statements that give a true and fair view in accordance with IFRSs as adopted by the EU and the requirements of the Malta Development Bank Act (Cap. 574), and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Independent auditor's report - continued

To the Shareholders of Malta Development Bank

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

Independent auditor's report - *continued*

To the Shareholders of Malta Development Bank

Other matter – use of this report

Our report, including the opinion, has been prepared for and only for the Bank's shareholders as a body in accordance with the Malta Development Bank Act (Cap. 574) and for no other purpose. We do not, in giving this opinion, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior written consent.

PricewaterhouseCoopers
78, Mill Street
Zone 5, Central Business District
Qormi
Malta

Fabio Axisa
Partner

28 March 2023

STATEMENT OF FINANCIAL POSITION

	NOTES	AS AT 31 DECEMBER 2022	2021
		€	€
ASSETS			
Balances with Central Bank of Malta	3	**696,456**	355,352
Loans and advances to banks	3	**24,968,231**	54,860,397
Financial investments	4	**46,803,063**	17,093,955
Loans and advances to customers	5	**20,965,084**	3,203,951
Investment property	6	**614,948**	623,519
Property and equipment	7	**3,639,852**	3,555,591
Right-of-use assets	8	**11,683**	25,703
Intangible assets	9	**19,424**	24,212
Other assets	10	**1,232,850**	856,735
Total assets		**98,951,591**	80,599,415
EQUITY AND LIABILITIES			
EQUITY			
Share capital	11	**80,000,000**	60,000,000
Accumulated losses		**(2,996,453)**	(3,647,953)
Total equity		**77,003,547**	56,352,047
LIABILITIES			
Amounts owed to banks	12	**15,769,681**	19,705,883
Amounts owed to other entities	13	**4,305,341**	2,934,768
Other liabilities	14	**1,873,022**	1,606,717
Total liabilities		**21,948,044**	24,247,368
Total liabilities and equity		**98,951,591**	80,599,415
MEMORANDUM ITEMS			
Commitments	15	**17,804,318**	14,568,671

The notes on pages 103 to 146 are an integral part of these financial statements.

The financial statements on pages 99 to 146 were approved by the Board of Directors on 28 March 2023 and signed on its behalf by:

PROF. JOSEF BONNICI
Chairperson

PROF. PHILIP VON BROCKDORFF
Director

STATEMENT OF COMPREHENSIVE INCOME

	NOTES	YEAR ENDED 31 DECEMBER	
		2022	2021
		€	€
Interest receivable and similar income	16	**687,677**	171,491
Interest payable and similar expense	17	**(178,136)**	(276,865)
Net interest (income)/expense		**509,541**	(105,374)
Income from financial guarantees	18	**154,948**	86,671
Administrative fee income	19	**2,570,400**	1,582,585
Other income	20	**44,796**	33,676
Net operating income		**3,279,685**	1,597,558
Administrative expenses	22	**(593,881)**	(552,167)
Employee compensation and benefits	23	**(1,374,844)**	(1,323,963)
Depreciation of investment property, property and equipment and right-of-use assets	6, 7, 8	**(123,528)**	(78,335)
Amortisation of intangible assets	9	**(7,018)**	(6,097)
Total operating expenses		**(2,099,271)**	(1,960,562)
Profit/(loss) for the year before changes in expected credit losses		**1,180,414**	(363,004)
Changes in expected credit losses	21	**(528,914)**	(709,679)
Profit/(loss) for the year - total comprehensive income		**651,500**	(1,072,683)

The notes on pages 103 to 146 are an integral part of these financial statements.

STATEMENT OF CHANGES IN EQUITY

	NOTES	SHARE CAPITAL	ACCUMULATED LOSSES	TOTAL EQUITY
		€	€	€
Balance as at 1 January 2021		50,000,000	(2,575,270)	47,424,730
Transactions with owners				
Capital contributed by the Government of Malta - total transactions with owners	11	10,000,000	-	10,000,000
Comprehensive income				
Loss for the year - total comprehensive income		-	(1,072,683)	(1,072,683)
Balance at 31 December 2021		**60,000,000**	**(3,647,953)**	**56,352,047**
Balance as at 1 January 2022		60,000,000	(3,647,953)	56,352,047
Transactions with owners				
Capital contributed by the Government of Malta - total transactions with owners	11	20,000,000	-	20,000,000
Comprehensive income				
Profit for the year - total comprehensive income		-	651,500	651,500
Balance at 31 December 2022		**80,000,000**	**(2,996,453)**	**77,003,547**

The notes on pages 103 to 146 are an integral part of these financial statements.

STATEMENT OF CASH FLOWS

	NOTES	YEAR ENDED 31 DECEMBER	
		2022	2021
		€	€
Cash flows from operating activities			
Net cash generated/(used in) from operating activities	24	**138,519**	(6,909,434)
Cash flows from investing activities			
Purchase of financial investments	4	**(29,931,419)**	(17,183,700)
Interest received on financial assets held as investments	16	**328,684**	94,272
Purchase of property and equipment	7,8	**(185,651)**	(362,627)
Purchase of intangible assets	9	**(2,230)**	(11,906)
Net cash used in investing activities		**(29,790,616)**	(17,463,961)
Cash flow from financing activities			
Proceeds from issue of share capital	11	**20,000,000**	10,000,000
Repayments of long term borrowing	12	**(3,936,202)**	(5,294,117)
Payments for the principal portion of lease liabilities	8	**(14,114)**	(11,796)
Net cash generated from financing activities		**16,049,684**	4,694,087
Net decrease in cash and cash equivalents		**(13,602,413)**	(19,679,308)
Cash and cash equivalents at beginning of year		**25,300,305**	44,979,613
Cash and cash equivalents at end year	25	**11,697,892**	25,300,305

The notes on pages 103 to 146 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these financial statements are set out below. Unless otherwise stated, these policies have been consistently applied to all the years presented.

1.1 BASIS OF PREPARATION

The Bank's financial statements have been prepared in accordance with the requirements of International Financial Reporting Standards ('IFRSs') as adopted by the EU and with the requirements of the Malta Development Bank Act, 2017. These financial statements are prepared under the historical cost convention, as modified by the fair valuation of certain financial assets and financial liabilities.

The preparation of financial statements in conformity with IFRSs as adopted by the EU requires the use of certain accounting estimates. It also requires the directors to exercise their professional judgment in the process of formulating and applying the Bank's accounting policies.

Standards, interpretations and amendments to published standards effective in 2022

In 2022, the Bank adopted amendments and interpretations to existing standards that are mandatory for the Bank's accounting period beginning on 1 January 2022. The adoption of these revisions to the requirements of IFRSs as adopted by the EU did not result in changes to the Bank's accounting policies impacting the Bank's financial performance or position.

Standards, interpretations and amendments to published standards that are not yet effective

Certain new standards, amendments and interpretations to existing standards which are mandatory for accounting periods beginning on or after 1 January 2023 have been published by the date of authorisation for issue of these financial statements. The Bank has not early adopted these requirements of IFRSs as adopted by the EU and the Bank's directors are of the opinion that there are no requirements that will have a possible significant impact on the Bank's financial statements in the period of initial application.

1.2 FUNCTIONAL TRANSACTIONS AND BALANCES

a) Functional and presentation currency

Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates ('the functional currency'). The financial statements are presented in euro, which is the Bank's functional and presentation currency.

b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions or valuation where items are remeasured. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in profit or loss.

1.3 FINANCIAL ASSETS

Initial recognition and measurement

The Bank recognises a financial asset in its Statement of Financial Position when it becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on the trade date, which is the date on which the Bank commits to purchase or sell the asset. Accordingly, the Bank uses trade date accounting for regular way contracts when recording financial asset transactions.

At initial recognition, the Bank measures a financial asset at its fair value plus or minus, in the case of a financial asset not recognised at fair value through profit or loss ('FVTPL'), transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset, such as fees and commissions. Transaction costs of financial assets carried at FVTPL are expensed in profit or loss.

At initial recognition, an expected credit loss ('ECL') allowance is recognised for financial assets measured at amortised cost and investments in debt instruments measured at fair value through other comprehensive income ('FVOCI'), which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

When the fair value of financial assets differs from the transaction price on initial recognition, the Bank recognises the difference as follows:

- When the fair value is evidenced by a quoted price in an active market for an identical asset (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.

- In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

Classification and subsequent measurement

The Bank classifies its financial assets in the following measurement categories:

- FVTPL;
- FVOCI; or
- Amortised cost

As of 31 December 2022 and 2021, all of the Bank's financial assets were classified under the amortised cost measurement category.

Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds and treasury bills.

Classification and subsequent measurement of debt instruments depend on:
i. the Bank's business model for managing the asset; and
ii. the cash flow characteristics of the asset.

Based on these factors the Bank classifies its debt instruments into one of the following three measurement categories:

- ***Amortised cost:*** Assets that are held for the collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI'), and that are not designated at FVTPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any ECL allowance recognised and measured as described in Note 2.4.3. Interest income from these financial assets is included in 'Interest receivable and similar income' using the effective interest rate method.

- ***FVOCI:*** Financial assets that are held for the collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and interest, and that are not designated at FVTPL, are measured at FVOCI. Movements in the carrying amount of debt instruments are taken through other comprehensive income (OCI), except for the recognition of impairment losses or impairment loss reversals, interest revenue and foreign exchange gains and losses on the instrument's amortised cost which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in 'Net investment income'. Interest income from these financial assets is included in 'Interest receivable and similar income' using the effective interest rate method.

- ***FVTPL:*** Assets that do not meet the criteria of amortised cost or FVOCI are measured at FVTPL. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognised in profit or loss and presented in the profit or loss statement within 'Net trading income' in the period in which it arises. Interest income from these financial assets is included in 'Interest receivable and similar interest' using the effective interest rate method

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

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e., its amortised cost before any impairment allowance) or to the amortised cost of a financial liability.

The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees.

When the Bank revises the estimates of future cash flows, the carrying amount of the respective financial asset or financial liability is adjusted to reflect the new estimate discounted using the original effective interest rate. Any changes are recognised in profit or loss.

The Bank reclassifies debt instruments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent, and none occurred during the period.

Business Model Assessment

Key management personnel determine the Bank's business model by considering the way financial instruments are managed in order to generate cash flows i.e. whether the Bank's objective is solely to collect the contractual cash flows from the assets or to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified and measured at FVTPL. Such assessment is performed at a 'portfolio level' as it best reflects the way the business is managed, and information is provided to management.

The information that will be considered in such assessment includes:

- the objectives for the portfolio including whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of assets;
- the method for the evaluation of the performance of the portfolio and how such performance is reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading and those that are managed and whose performance is evaluated on a fair value basis will be measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets. Securities held for trading are held principally for the purpose of selling in the near term or are part of a portfolio of financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking.

The Bank may also irrevocably designate financial assets at fair value through profit or loss if doing so significantly reduces or eliminates a mismatch created by assets and liabilities being measured on different bases.

Cash flows that represent solely payments of principal and interest

In respect of assets where the intention of the business model is to hold the financial assets to collect the contractual cash flows or to hold to collect and to sell, the Bank assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In making this assessment, the Bank considers whether the contractual cash flows are consistent with a basic lending agreement. 'Principal' is the fair value of the financial asset at initial recognition. It is not the amount that is due under the contractual terms of an instrument. 'Interest' is the compensation for time value of money and credit risk of a basic lending-type return. A basic lending-type return could also include consideration for other basic lending risks (for example, liquidity risk) and consideration for costs associated with holding the financial asset for a particular period of time (for example, servicing or administrative costs) and/or a profit margin. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

Unlike the business model assessment, the SPPI assessment is performed for each individual product or portfolio of products. The following considerations are made when assessing consistency with SPPI:

- contingent events that would change the amount and timing of cash flows such as contractual term resetting interest to a higher amount in the event of a missed payment;
- leverage features, being contractual cash flow characteristics that increase the variability of the contractual cash flows with the result that they do not have economic characteristics of interest;
- contractual terms that allow the issuer to prepay (or the holder to put a debt instrument back to the issuer) before maturity and the prepayment amount substantially represents unpaid amounts of principal and interest, which may include reasonable compensation for early termination of the contract;
- contractual terms that allow the issuer or holder to extend the contractual term and the terms of the extension option result in contractual cash flows during the extension period that are solely payments of principal and interest, which may include reasonable compensation for the extension of the contract; and
- features that modify consideration for the time value of money (for example, periodic reset of interest rates).

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective i.e. instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

The Bank subsequently measures all equity investments at fair value through profit or loss, except where the Bank's management has elected, at initial recognition, to irrevocably designate an equity investment at fair value through other comprehensive income. The Bank's policy is to designate equity investments as FVOCI when those investments are held for purposes other than to generate investment returns. This election is made on an investment by investment basis. When this election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal.

Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value. Dividends, when representing a return on such investments, continue to be recognised in profit or loss as other income when the Bank's right to receive payments is established.

Gains and losses on equity investments at FVTPL are included in the 'Net trading income' line in the income statement.

Derecognition of financial assets

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e. removed from the Bank's statement of financial position) when:

- the rights to receive cash flows from the asset have expired, or
- the Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Bank has transferred substantially all the risks and rewards of the asset, or (b) the Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Bank continues to recognise the transferred asset to the extent of its continuing involvement. In that case, the Bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

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

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

When modification happens, the Bank assesses whether the new terms are substantially different to the original terms. The Bank does this by considering, among others, the following factors:

- if the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay;
- whether any substantial new terms are introduced;
- significant extension of the loan term when the borrower is not in financial difficulty;
- significant change in the interest rate, and
- insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Bank derecognises the original financial asset and recognises a 'new' asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Bank also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in derecognition, and the Bank recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit or loss. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets).

1.4 IMPAIRMENT OF FINANCIAL ASSETS

The Bank assesses on a forward-looking basis the ECL associated with its debt instruments carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Bank recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

i. an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
ii. the time value of money; and
iii. reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Note 2.4.3 provides more detail of how the expected credit loss allowance is measured.

ECL allowances are presented in the Statement of Financial Position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- financial instruments with both a drawn and undrawn component, whereby the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Bank presents a combined loss allowance for both components, as a deduction from the gross carrying amount of the drawn component; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the Statement of Financial Position against the carrying amount of the asset because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve, i.e. presented within other comprehensive income.

1.5 OFFSETTING FINANCIAL INSTRUMENTS

Financial assets and liabilities are offset and the net amount reported in the Statement of Financial Position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

1.6 INTANGIBLE ASSETS

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use specific software. These costs are amortised over their estimated useful lives of six years. Costs associated with maintaining computer software programme are recognised as an expense as incurred.

Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Bank are recognised as intangible assets when the following criteria are met:

- it is technically feasible to complete the software product so that it will be available for use;
- management intends to complete the software product and use it;
- there is an ability to use the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use the software product are available; and
- the expenditure attributable to the software product during its development can be reliably measured.

At the end of each reporting period, intangible assets are reviewed for indications of impairment or changes in estimated future economic benefits. If such indications exist, the intangible assets are analysed to assess whether their carrying amount is fully recoverable (Note 1.9).

1.7 INVESTMENT PROPERTY

All investment property is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance costs are charged to profit or loss during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate the cost of the assets to their residual values over their estimated useful lives, as follows:

	YEARS
Buildings	75

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 1.9).

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised in profit or loss.

1.8 PROPERTY AND EQUIPMENT

All property and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of the replaced part is derecognised. All other repairs and maintenance costs are charged to profit or loss during the financial period in which they are incurred.

Depreciation is calculated using the straight-line method to allocate the cost of the assets to their residual values over their estimated useful lives, as follows:

	YEARS
Buildings	75
Improvements to property	5 - 15
Computer equipment	5
Other equipment	5 - 15
Furniture	10

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 1.9).

Property and equipment are derecognised upon disposal or when no future economic benefits are expected from their use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss in the period the asset is derecognised.

1.9 IMPAIRMENT OF NON-FINANCIAL ASSETS

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets.

An impairment loss is recognised if the carrying amount of an asset or cash-generating unit ('CGU') exceeds its estimated recoverable amount. Impairment losses are recognised in profit or loss.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

1.10 CURRENT AND DEFERRED TAX

By virtue of the Malta Development Act (Cap. 574), the Bank is exempt from all taxation under the Income Tax Act and the Duty on Documents and Transfers Act that may apply to the Bank's assets, property, income, operations and transactions.

1.11 CASH AND CASH EQUIVALENTS

Cash and cash equivalents comprise unrestricted balances and deposits with contractual maturities of less than three months from the acquisition date and which are subject to an insignificant risk of changes in their fair value. Subsequent to initial recognition, cash and cash equivalents are carried at amortised cost in the statement of financial position.

1.12 FINANCIAL LIABILITIES

Initial recognition and measurement

The Bank recognises a financial liability on its Statement of Financial Position when it becomes a party to the contractual provisions of the instrument. Financial liabilities not at FVTPL are recognised initially at fair value, being the fair value of consideration received, net of transaction costs that are directly attributable to the acquisition or the issue of the financial liability.

Classification and subsequent measurement

Financial liabilities are classified and subsequently measured at amortised cost, except for:

- financial liabilities at FVTPL: this classification is applied to derivatives, financial liabilities held for trading (e.g. short positions in the trading book and other financial liabilities designated as such at initial recognition. Gains or losses on financial liabilities designated at FVTPL are presented partially in other comprehensive income (the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability, which is determined as the amount that is not attributable to changes in market conditions that give rise to market risk) and partially profit or loss (the remaining amount of change in the fair value of the liability). This is unless such a presentation would create, or enlarge, an accounting mismatch, in which case the gains and losses attributable to changes in the credit risk of the liability are also presented in profit or loss;
- financial liabilities arising from the transfer of financial assets which did not qualify for derecognition, whereby a financial liability is recognised for the consideration received for the transfer. In subsequent periods, the Bank recognises any expense incurred on the financial liability; and
- financial guarantee contracts and loan commitments (Note 1.14).

Financial liabilities measured at amortised cost comprise principally of amounts owed to banks and entities and other liabilities.

Derecognition

The Bank derecognises a financial liability from its Statement of Financial Position when the obligation specified in the contract or arrangement is discharged, is cancelled, or expires.

The exchange between the Bank and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability.

In addition, other qualitative factors such as the currency that the instrument is denominated in, changes in the type of interest rate, new conversion features attached to the instrument and changes in covenants are also taken into consideration. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

1.13 TRADE AND OTHER PAYABLES

Trade payables comprise obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are classified as current liabilities if payment is due within one year or less (or in the normal operating cycle of the business if longer). If not, they are presented as non-current liabilities.

Trade and other payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

1.14 FINANCIAL GUARANTEE CONTRACTS AND LOAN COMMITMENTS

Financial guarantee contracts are contracts that require the guarantor to make specified payments to reimburse the holder of the guarantee for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt obligation. Loan commitments are the Bank's commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan are initially measured at fair value. Subsequently, they are measured at the higher of the credit loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15. Loan commitments provided by the Bank are measured as the amount of the credit loss allowance.

Liabilities arising on financial guarantees and loan commitments are included within provisions.

1.15 CONTINGENT LIABILITIES

Contingent liabilities are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence of one or more uncertain future events not wholly within the control of the Bank.

1.16 PROVISIONS FOR LEGAL AND OTHER CLAIMS

Provisions for legal and other claims are recognised when the Bank has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognised as interest expense.

1.17 SHARE CAPITAL

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity.

1.18 REVENUE RECOGNITION

Revenue is recognised to the extent that it is probable that future economic benefits will flow to the Bank and these can be measured reliably.

Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability.

The calculation of the effective interest rate includes all transaction costs, premiums or discounts and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or liability.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for financial assets that have subsequently become credit-impaired (or 'Stage 3'), for which interest revenue is calculated by applying the effective interest rate to their amortised cost (i.e. net of the expected credit loss provision).

Income on financial guarantees

The Bank provides financial guarantees on loan portfolios to credit institutions. These fees are charged on a periodical basis and are based on fixed contractual rates. These fees are recorded in the Income Statement within 'Income from financial guarantees'.

Administrative fee income

The Bank administers a number of schemes on behalf of the Ministry of Finance and receives fee income as a consideration for the implementation and ongoing administration of these schemes. Fees received in relation to the administration are charged on a periodical basis and are based on fixed contractual rates. These fees are recorded in the Income Statement in 'Administrative fee income'.

Revenue related to transactions is recognised at the point in time when the transaction takes place.

1.19 LEASES

A right-of-use asset ('ROU') is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The ROU asset is subsequently depreciated over the shorter of the ROU asset's useful economic life and the lease term on a straight-line basis. The ROU asset is depreciated using the straight-line method from the commencement date to the end of the lease term, unless the lease transfers ownership of the underlying asset to the Bank by the end of the lease term or the cost of the ROU asset reflects that the Bank will exercise a purchase option. In that case the ROU asset will be depreciated over the useful life of the underlying asset, which is determined on the same basis as those of property and equipment. In addition, the ROU asset is periodically reduced by impairment losses, if any, adjusted for certain remeasurements of the lease liability.

In determining the lease term, the Bank considers all facts and circumstances that create an economic incentive to exercise an extension option or not exercise a termination option over the planning horizon of five years.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. In general, it is not expected that the discount rate implicit in the lease is available, so the Bank's incremental borrowing rate is used. This is the rate that the Bank would have to pay to borrow the funds necessary to obtain an asset of a similar value in a similar economic environment with similar terms and conditions. The rates are determined for each term by adjusting swap rates with funding spreads (own credit spread).

Lease payments are allocated between the liability and finance costs. The finance costs are charged to profit or loss over the lease term to produce a constant period rate of interest on the remaining balance of the liability.

1.20 PROVISIONS FOR PENSION OBLIGATIONS

The Bank contributes towards the state defined contribution pension plan in accordance with local legislation and to which it has no commitment beyond the payment of fixed contributions. These obligations are recognised as an expense in the Income Statement as they accrue. The Bank does not contribute towards any other retirement benefit plans.

2. FINANCIAL RISK MANAGEMENT

2.1 ORGANISATION

The Board of Directors has the overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Audit and Risk Committees, which are responsible for monitoring risk in specified areas and are chaired by a non-executive director. Non-executive directors sit on these Committees, with the Chief Executive Officer also attending Board meetings. The Audit and Risk Committees report to the Board of Directors.

The Asset and Liability Committee ('ALCO') is a sub-committee of the Risk Committee and provides oversight on the asset and liability management in respect of the Bank's financial position. The ALCO recommends new products and treasury instruments to the Risk Committee, whilst also monitoring and reviewing the Bank's liquidity risk, interest rate risk and capital adequacy.

The Credit Committee is a sub-committee of the Risk Committee and provides oversight on credit risk management. The Credit Committee oversees the credit risk assumed by the Bank within the risk tolerances established by the Board and reviews and monitors the effectiveness and application of credit risk management policies and procedures and the control environment in respect of credit decisions.

The Bank's Enterprise Risk Management ('ERM') framework defines the risk appetite set by the Board and ensures proactive, adaptive and ongoing risk management. The framework addresses:

i. credit risk through the Credit Risk Management Framework;
ii. funding and liquidity risk through the Treasury Management Policy;
iii. interest rate risk arising from non-trading activities; and
iv. operational risk through the Operational Risk Framework.

The risk management policies and systems of the Bank are reviewed by the Board on a regular basis to reflect changes in market conditions, products and services offered.

2.2 RISK EXPOSURE

The Bank is exposed to the following risks:

- *Credit risk:* This is the risk of financial loss from the failure of a counterparty to fulfil its contractual obligations, or from the increased risk of default during the term of the transaction (Note 2.4).
- *Liquidity risk:* This is the risk of incurring losses due to the inability of meeting obligations as and when they become due (Note 2.6).
- *Interest rate risk:* This is the risk posed by adverse movements in interest rates that affect the Bank's banking book positions (Note 2.5.1).
- *Operational and other risks:* These are the risks of losses resulting from inadequate or failed internal processes, people and systems, or from external events.

2.3 CAPITAL MANAGEMENT

The Bank is not subject to externally imposed capital requirements. As at 31 December 2022, the Bank's paid-up share capital stood at €80 million (2021: €60 million), which has been provided by the Bank's sole shareholder, the Government of Malta.

The Bank's capital risk management process includes adherence to its internal minimum level of capital such that it remains adequately capitalised to absorb any potential losses whilst fulfilling its public policy objectives as set by the Board of Directors in accordance with the Malta Development Bank ('MDB') Act.

	2022	2021
	€	€
Capital		
Paid up share capital	**80,000,000**	60,000,000
Accumulated loss	**(2,996,453)**	(3,647,953)
Total capital	**77,003,547**	56,352,047

2.4 CREDIT RISK

2.4.1 CREDIT RISK MANAGEMENT

Credit risk is addressed in the Bank's Credit Policy Framework and is managed and controlled through established credit processes, and appropriate delegation of authorities and responsibilities assigned to the Bank's management. The credit risk policies and procedures of the Bank are reviewed periodically to reflect changes in market conditions, products and services offered.

The Bank seeks to maintain credit risk levels that are relative to the Bank's capital base and to ensure that lending decisions achieve a reasonable balance between the risks and returns of extending credit to a customer.

Any credit risk that is to be assumed by the Bank in direct lending, contingent obligations and promotional lending schemes, whether secured, unsecured or carrying a third-party indemnity of whatever kind, is presented to the Credit Risk Committee. The Credit Risk Committee analyses the financing arrangement and recommends this to the Board of Directors for their approval. This approach ascertains a clear and unequivocal process in the credit approval process.

The Bank applies a credit quality review process to provide early identification of possible changes in creditworthiness of counterparties. Facilities are generally reviewed periodically. In a facility review, the Bank analyses factors such as the customer profile, credit quality and other financial and non-financial considerations. Exposures which are performing, but exhibit early signs of deterioration (e.g. days past due and/or other early warning indicators) are rigorously analysed by the Credit team.

The Bank, in line with its principal activities and business model, originates a number of different types of financing to address market failures and financing gaps within the local market. These financial instruments are described below:

(i) Financial Guarantee contracts

The Bank issues financial guarantee contracts to credit institutions, with the aim of facilitating the provision of credit facilities to customers of the same credit institutions that are eligible under one of the Bank's credit schemes. Through these guarantees, the MDB binds itself to pay a specified sum to the intended beneficiary in case the borrowing entity fails to meet its obligations in accordance with the agreed terms.

The following financial guarantee schemes are disclosed as off-balance sheet commitments:

- Guarantee Facility for loans to SMEs (*'SME Invest'*): to provide financial guarantees for loans to Small and Medium Enterprises facilitating lending to smaller businesses that are viable but unable to obtain the required amount of finance from a commercial bank. The risk-sharing agreement entered into with counterparty commercial banks guarantees 80% of each eligible loan, subject to a portfolio capping of 25%.

- Family Business Transfer Facility (*'FBT'*): to provide financial guarantees to commercial banks to assist and facilitate family businesses to transfer their business from one generation to the next. The risk-sharing agreement entered into with counterparty commercial banks guarantees 80% of each eligible loan, subject to a portfolio capping of 50%.

- Guarantee Co-Lending Scheme (*'GCLS'*): to provide financial guarantees for loans to SMEs with a special focus on SMEs with large loan requirements aimed at achieving a high level of sustainability or to promote the circular economy. The risk-sharing agreement entered into with counterparty commercial banks guarantees 60% of each eligible loan.

As of 31 December 2022, the Bank issued financial guarantee contracts, net of repayments, amounting to €45.8 million (2021: €41.7 million). The Bank needs to honour the guarantee in the event that the borrower defaults on the obligation to the counterparty commercial bank. However, the risk sharing agreements entered into between the Bank and the counterparty commercial banks limit the credit risk exposure in the event of default by the borrower and effectively reduce the credit risk of the Bank to €11.6 million (2021: €8.4 million) (see Note 15). The Bank has earmarked a pre-determined amount of own capital to fund these credit facilities in the event of default.

During the financial years ended 31 December 2022 and 2021, the Bank was also entrusted to implement and manage the following guarantee schemes on behalf of the Ministry for European Affairs and Equality and the Government of Malta:

- Further Studies Made Affordable (*'FSMA'*) and Further Studies Made Affordable Plus (*'FSMA+'*): to provide financial guarantees and interest subsidies on loans sanctioned by third-party commercial banks in favour of individuals seeking to further their studies at a tertiary education institution or equivalent. The FSMA+ scheme was introduced during the financial year ended 31 December 2022.

- COVID-19 Guarantee Scheme (*'CGS'*): to provide financial guarantees to commercial banks to enhance access to bank financing for the working capital requirements of businesses in Malta that faced a sudden acute liquidity shortage as a result of the COVID-19 outbreak.

The FSMA, FSMA+ and CGS schemes are backed-up by a government guarantee that provides cover against all credit risks emanating from credit losses. The Government of Malta provides indemnification to the Bank in respect of all expected credit losses. The impact of these financial guarantees therefore results in a nil loss given default (LGD) and therefore a nil ECL in view of the Government support.

(ii) Loans and advances to customers

The MDB offers direct loans to private or public individuals that are eligible under one of the following credit schemes:

- Tailored Facility for Businesses: to provide favourable financing terms for bankable projects with a special focus on:

    i. SMEs particularly those involving innovation, digitalisation and, more broadly, the preservation and enhancement of competitiveness;
    ii. Socially oriented initiatives, particularly those involving knowledge generation, education, health and social inclusion;
    iii. Investment that addresses environmental issues such as water usage, water treatment, waste treatment, reduction, and reuse; and
    iv. Investment aimed to achieve a high level of sustainability or promote the circular economy.

All credit risk arising from this scheme is assumed by the Bank.

- Subsidised Loan Scheme (*'SLS'*): to provide temporary urgent liquidity support to ensure national security of strategic supply to companies undertaking the importation and wholesale of grains affected by the current macroeconomic environment following the invasion of Ukraine by Russia. The credit risk arising on these facilities is 90% guaranteed by the Government of Malta.

- Guarantee Co-Lending Scheme (*'GCLS'*): to provide loans to SMEs with a special focus on SMEs with large loan requirements aimed at achieving a high level of sustainability or to promote the circular economy. The credit risk arising on these facilities is 70% guaranteed by the European Investment Fund.

The level of economic uncertainty remained elevated during the financial year ended 31 December 2022, primarily driven by the geopolitical developments as a result of the escalation of the military conflict between Russia and Ukraine, as well as widespread supply chain disruptions experienced as the world economy recovers from the impacts of the pandemic, which triggered significant inflationary pressures across the world.

As a result, economic uncertainty continues to prevail especially in view of the increasing interest rate environment and inflationary pressures. This has impacted the performance of the Bank's expected credit loss models, requiring enhanced monitoring of model outputs.

Accordingly, the Bank performed enhanced reviews on a periodic basis to identify borrowers who were experiencing, or are likely to experience, financial difficulty as a result of the ongoing macroeconomic challenges to identify borrowers deemed to be at risk of a Significant Increase in Credit Risk ('SICR') or Unlikeliness-To-Pay ('UTP') trigger event. The Bank assessed borrowers through credit assessments, on the basis of recently obtained management information, including forecasts.

(iii) Other financial assets

Excess liquidity is employed in eligible financial assets outlined in the Treasury Management Policy with the objective of optimising adequate returns. Money market business is only conducted with financial institutions that have been included in the Bank's list of eligible counterparties.

As at 31 December 2022, the Bank's other financial assets consisted of balances held with the Central Bank of Malta, amounts placed with local banks, treasury bills issued by the Government of Malta and local sovereign and corporate debt securities. All financial assets were placed with local high-quality counterparties.

	2022	2021
	€	€
Balances with Central Bank of Malta	**696,456**	355,352
Loans and advances to banks	**24,968,231**	54,860,397
Financial investments	**46,803,063**	17,093,955
Total capital	**72,467,750**	72,309,704

As at 31 December 2022 and 2021, these financial assets were neither past due nor impaired; and the credit quality grading attributable to these assets was considered of investment grade.

2.4.2 CREDIT RISK MEASUREMENT

The measurement of credit exposure for risk management purposes considers that an exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Bank measures expected credit losses ('ECLs') using Probability of Default ('PD'), Exposure at Default ('EAD') and Loss Given Default ('LGD') parameters.

(a) Loans and advances to customers and financial guarantee contracts

The Credit Risk Policy of the Bank establishes the internal credit risk grading framework which reflects the assessment of the PD of individual counterparties or facilities for loans and advances to customers and financial guarantee contracts. The rating is initially inferred through the Risk Acceptance Criteria outlined in the Credit Risk Policy, and subsequently assessed through credit file reviews on the basis of ongoing qualitative and quantitative assessments. Internal credit risk gradings are based on payment behaviour, loan specific information and expert judgement.

Information considered by the Bank when determining the internal credit risk grades includes the payment behaviour of the borrower, other information which impacts the creditworthiness of the borrower including level of income and/or financial performance and expert judgement.

The internal credit risk gradings are defined and calibrated such that they reflect the increased risk of default at each higher risk grade.

The internal risk ratings are aligned to the different stages emanating from the requirements of IFRS 9, being; Stage 1, Stage 2 and Stage 3 (credit-impaired) which are further explained in Note 2.4.3

(b) Other financial assets

Other financial assets include balances held with the Central Bank of Malta, loans and advances to banks and financial investments. The Bank uses external risk grades to reflect its assessment of the probability of default of individual counterparties. These published grades are continuously monitored and updated. The Bank distinguishes between exposures considered 'investment grade' and 'non-investment grade' defined by recognised external rating agencies.

2.4.3 EXPECTED CREDIT LOSS MEASUREMENT

IFRS 9 outlines a 'three stage' model for impairment measurement based on changes in credit quality since initial recognition as summarised below:

- a financial instrument that is not credit-impaired on initial recognition is classified in Stage 1 and has its credit risk monitored by the Bank;
- if a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to Stage 2 but is not yet deemed to be credit-impaired;
- if the financial instrument is credit-impaired, the financial instrument is then moved to Stage 3.
- financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime ECLs that result from default events possible within the next 12 months. Instruments in Stages 2 and 3 have their ECL measured based on lifetime ECL;
- the measurement of ECL considers forward-looking information.
- purchased or originated credit-impaired financial assets are those financial assets that are credit-impaired on initial recognition. Their ECL is always measured on a lifetime basis ('Stage 3').

The ECL requirements are applicable to financial assets measured at amortised cost and FVOCI, and certain loan commitments and financial guarantee contracts. At initial recognition, an impairment allowance (or provision in the case of commitments and guarantees) is required for ECL resulting from default events that are possible within the next 12 months ('12-month ECL'). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognised are considered 'Stage 1'. Financial assets which are considered to have experienced a significant increase in credit risk would be classified as 'Stage 2' and financial assets for which there is objective evidence of impairment, thus considered to be in default or otherwise credit-impaired, would be classified as 'Stage 3'.

When determining whether the risk of default on a financial instrument has increased significantly, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analyses, credit assessment and forward-looking information.

The following diagram summarises the impairment requirements under IFRS 9:

Change in credit quality since initial recognition		
STAGE 1	**STAGE 2**	**STAGE 3**
(Initial recognition)	*(Significant increase in credit risk since initial recognition)*	*(Credit-impaired financial assets)*
12-month expected credit losses	Lifetime expected credit losses	Lifetime expected credit losses

2.4.3.1 SIGNIFICANT INCREASE IN CREDIT RISK

To determine whether the credit risk on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort, including both quantitative and qualitative information. Such analysis is based on the Bank's credit assessment and forward-looking information.

The Bank primarily identifies whether a SICR has occurred through the Bank's internal risk gradings. The Bank allocates each exposure to an internal rating grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. These factors vary depending on the nature of the exposure and the type of borrower. Exposures are subject to ongoing credit monitoring.

As referred to previously, the progressive economic recovery from the downturn caused by the COVID-19 pandemic observed during the reporting period was largely outweighed by the emerging risks induced by the geopolitical tensions between Russia and Ukraine. As a result, economic uncertainty continues to prevail, particularly with respect to the identification of customers that are deemed to be at risk of experiencing a SICR. In this respect, the Bank continued to increase the depth of its monitoring activities. As part of these credit assessments, judgement was exercised in evaluating all relevant information on indicators of impairment, particularly where factors indicate deterioration in the financial condition and outlook of borrowers affecting their ability to pay.

As a backstop indicator, the Bank presumes that SICR has occurred when an asset is more than 30 days past due. The Bank determines days past due by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received.

In the case of other financial assets, the Bank applies the low credit risk simplification to exposures considered 'investment-grade', thus they are not subject to the SICR assessment. In respect of other financial assets classified as 'non-investment grade', the Bank considers any downgrade in the external credit rating to have constituted a SICR.

2.4.3.2 DEFINITION OF DEFAULT AND CREDIT IMPAIRED

The Bank's assessment to determine the extent of increase in credit risk of a financial instrument since initial recognition is performed by considering the change in the risk of default occurring over the remaining life of the financial instrument.

The Bank considers exposures to be in default when:

- the counterparty is past due more than 90 days on any material credit obligation to the Bank or to another credit institution through which financial guarantee contracts are intermediated; or
- the counterparty is unlikely to pay its credit obligations to the Bank in full or to another credit institution through which financial guarantee contracts are intermediated, without recourse by the Bank to actions such as realising security (if any is held).

In assessing whether a borrower is in default/credit-impaired, the Bank considers indicators that are:

- qualitative – such as non-adherence to terms and conditions of sanction and/or other breaches of covenant;
- quantitative – such as overdue status; and
- based on data developed internally and obtained from external sources.

The default definition is applied consistently when modelling the PD, EAD and LGD parameters throughout the Bank's expected credit loss calculations. As referred to previously, the COVID-19 pandemic and the war between Russia and Ukraine have exacerbated the level of uncertainty, particularly with respect to the identification of customers that would have showed signs of unlikeliness to pay ('UTP'). The Bank continued to perform assessments to determine whether the short-term economic shock may transform into long-term borrower financial difficulties, thereby potentially requiring a downgrade of individual exposures or exposures sharing similar credit risk characteristics to Stage 3 to reflect the level of change in credit risk.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria, and when the Bank is satisfied that the borrower no longer shows signs of unlikeliness to pay. In line with the Bank's credit policy, all exposures which migrate to a performing status, and accordingly exit the non-performing classification are reviewed by the Risk Committee.

2.4.3.3 MEASURING ECL – EXPLANATION OF INPUTS, ASSUMPTIONS AND ESTIMATION TECHNIQUES

The ECL is measured on either a 12-month ('12M') or on a lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired.

ECLs are the discounted product of the PD, EAD, and LGD. These three components are multiplied together effectively calculating the forward-looking ECL, which is then discounted back to the reporting date. The discount rate used in the ECL calculation is the originated effective interest rate or an approximation thereof.

The 12-month ECL is calculated by multiplying the 12-month PD, LGD, and EAD. Lifetime ECL is calculated on a similar basis for the residual life of the exposure.

The PD represents the likelihood of a borrower defaulting on its financial obligation, either over the next 12 months, or over the remaining lifetime of the obligation. Accordingly, the 12-month and lifetime PDs represent the probability of default occurring over the next 12 months and the remaining maturity of the instrument, respectively.

(a) Loans and advances to customers and financial guarantee contracts

PDs are estimates at a certain date, which are calculated based on statistical rating models. The PD calculation for loans and advances to customers and financial guarantee contracts is based on transition matrices which show the probability of a borrower's transition from one internal rating class to another (or staying within the same class) within a given horizon. The main assumption is that the future PD depends on the current characteristics of the exposure or borrower.

The conditional PD is adjusted to consider forward-looking information through local macroeconomic modelling (see Note 2.4.3.4).

EAD is based on the amounts the Bank expects to be owed at the time of default, over the next 12 months or over the remaining lifetime. EAD represents the expected exposure in the event of a default (including any expected drawdowns of committed facilities). The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract. The EAD of a financial asset is the gross carrying amount at default.

The 12-month and lifetime EADs are determined based on the expected payment profile that is based on the contractual repayments owed by the borrower over a 12-month or lifetime basis.

The LGD represents the Bank's expectation of the extent of loss on a defaulted exposure. Hence, the LGD represents ECLs on the EAD given the event of default, taking into account, among other attributes, the mitigating effect of collateral values (if any) at the time it is expected to be realised and the time value of money. The 12-month and lifetime LGD are determined based on the factors which impact the recoveries made post default.

The ECL is measured from the initial recognition of the financial asset. The maximum period considered when measuring ECL (be it 12-month or lifetime ECL) is the maximum contractual period over which the Bank is exposed to credit risk. With respect to non-revolving credit facilities, the contractual life of the facility is considered.

Forward-looking economic information is also included in determining the 12-month and lifetime PD and LGD.

There were no significant changes in estimation techniques or significant assumptions made during the reporting period.

(b) Other financial assets

The PD in respect of other financial assets is determined based on publicly available realised default rates, as published by rating agencies. If a counterparty or exposure migrates between external credit ratings, this will then lead to a change in the associated PD.

2.4.3.4 FORWARD-LOOKING INFORMATION INCORPORATED IN THE ECL MODEL

The calculation of ECL incorporates forward-looking information. The Bank performs a historical analysis to identify the key economic variables affecting credit risk and expected credit losses by reference to local default rates. In this respect, during 2022, the Bank assessed the change in domestic real Gross Domestic Product ('GDP') to be a good predictor of the domestic non-financial corporate default rate. The impact of this economic variable on the PD is determined by performing statistical regression analysis to explain the historical impact that the change in this variable had on the local lending market.

The most significant period-end assumptions used for the ECL estimate are set out below:

	AS AT 31 DECEMBER 2022	
	2023	**2024**
Change in domestic real GDP	**3.7%**	3.6%

	AS AT 31 DECEMBER 2021	
	2022	**2023**
Change in domestic real GDP	**5.9%**	4.7%
Change in domestic net exports	**1.2%**	-0.3%

As with any macro-economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of uncertainty and therefore, the actual outcomes may be significantly different to those projected. The Bank considers these forecasts to represent its best estimate of the possible outcomes.

The 'base', 'upside' and 'downside' scenarios which were used are further explained below:

- the 'Base' Scenario captures business-as-usual macroeconomic expectations, whereby the current rhythm of economic activity is maintained;
- the 'Downside' Scenario is based on a subdued level of economic activity hypothesized to correspond to an economic recession; and
- the 'Upside' Scenario assumes that it would be possible to marginally improve further over the already benign economic conditions.

Each scenario is weighted by a probability of occurrence, determined by a combination of macroeconomic research and expert credit judgment, taking account of the range of possible outcomes that each chosen scenario represents. The Bank measures ECL as either a probability weighted 12-month ECL (Stage 1), or a probability weighted lifetime ECL (Stages 2 and 3).

The weightings assigned to each economic scenario were 50% (2021: 50%) for the 'Base' scenario, 30% (2021: 35%) for the 'Downside' scenario and 20% (2021: 15%) for the 'Upside' scenario. The economic scenarios were simulated over a full economic cycle.

During the reporting period, the Bank revised the probability weights assigned to the upside and downside scenarios in the context of the improved macroeconomic forecasts for Malta as published by the Central Bank of Malta. These forecasts indicated that the risks to the observed macroeconomic uncertainties appear to have materially subdued. Accordingly, the impact on the ECL as a result of the change in the assigned probability weights was not significant.

The scenarios and their attributes including the macroeconomic variables are reassessed at each reporting date. The Board considers that the probability weightings assigned to the respective scenarios reflect an unbiased evaluation of a range of possible outcomes.

Economic scenarios sensitivity analyses of ECL estimates

The outcome of the Bank's credit loss allowances estimation process is sensitive to judgements and estimations made throughout the incorporation of forward-looking economic conditions. Management has assessed the sensitivity of the Bank's ECLs by assigning a 100% weighting to the baseline, downside and upside scenario respectively. The Bank's credit loss allowances would decrease by €53,645 (2021: €33,756) if the provisions had to be calculated solely on the baseline scenario; ECLs would increase by €466,849 (2021: €148,149) if these had to be estimated using only the downside scenario and would reduce by €566,162 (2021: €233,158) if the upside scenario only was to be taken into consideration. In 2021 and 2022, the sensitivity impact was not considered to be significant, cognisant of the Bank's strong capital base.

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political changes, have also been considered but are not deemed to have a material impact and therefore no adjustment has been made to the ECL for such factors. This matter is reviewed and monitored for appropriateness on an ongoing basis.

2.4.4 MAXIMUM EXPOSURE TO CREDIT RISK

An 'exposure' is defined as the amount at risk arising from the Bank's assets and commitments. The Bank's maximum credit risk is classified into the following categories:

- Financial assets comprising principally of balances held with the Central Bank of Malta, loans and advances to banks and customers and debt securities. The maximum exposure to credit risk on these financial assets equals their gross carrying amounts.

- Financial guarantee contracts entered into on behalf of third parties. The maximum exposure to credit risk from financial guarantees is the full amount that the Bank would have to pay if the guarantees are called upon, unless the exposure is backed up by a government guarantee as detailed in Note 2.4.1.

- Lending commitments and other credit related commitments that are irrevocable over the life of the respective facilities. Most commitments to extend credit are contingent upon customers maintaining specific credit standards. These exposures are monitored similarly to loans and advances. The maximum exposure to credit risk is the full amount of the committed facilities.

The Bank's credit risk exposures reflecting the maximum exposure to credit risk before collateral held or other credit enhancements include the following:

	2022		2021	
	GROSS EXPOSURE	ECL ALLOWANCE	GROSS EXPOSURE	ECL ALLOWANCE
	€000	€000	€000	€000
Credit risk exposures relating to on-balance sheet assets:				
Financial assets measured at amortised cost				
Balances with Central Bank of Malta			-	
and other banks	**25,700**	**(35)**	55,235	(19)
Financial investments	**46,857**	**(54)**	17,094	-
Loans and advances to customers	**20,982**	**(17)**	3,204	-
Credit risk exposure	**93,539**	**(106)**	75,533	(19)
Credit risk exposures relating to off-balance sheet instruments				
Financial guarantees	**11,594**	**(1,570)**	8,356	(1,153)
Undrawn commitments to lend	**6,094**	**(25)**	6,096	-
Credit risk exposure	**17,688**	**(1,595)**	14,452	(1,153)

As of 31 December 2021, expected credit losses arising on financial investments were insignificant in view of the nature of the counterparty, being the Government of Malta. Similarly, expected credit losses in respect of loans and advances to customers and undrawn commitments to lend as of 31 December 2021 were considered to be insignificant in view of the high value of collateral securing the exposure.

2.4.5 CREDIT CONCENTRATION RISK

Within the Bank, concentration risk of losses results from inadequate diversification of the credit exposures. This risk is managed by actively monitoring, measuring, and reporting on a regular and ongoing basis the risk concentration levels against reasonable thresholds for counterparties and products.

As at 31 December 2022, no loans and advances to customers, or financial guarantee contracts were deemed to be prohibited large exposures in accordance with the requirements emanating from the MDB Act.

The Bank transacts with counterparty banks and other financial institutions. To mitigate the risk of losses in respect of such transactions, the Bank places funds solely with pre-approved reputable counterparties.

Credit concentration risk by industry sector

The Bank's financial investments (gross of credit loss allowances) were composed of local government debt securities, and other debt instruments as shown in the following table:

	2022	2021
	€000	€000
Government of Malta	**24,857**	17,094
Corporate – financial services	**22,000**	-
Net carrying amount	**46,857**	17,094

The industry sector analysis of the Bank's loans and advances to customers (gross of credit loss allowances) is set out in the following table:

	2022	2021
	€000	€000
Accommodation	**9,238**	3,204
Manufacturing	**11,744**	-
Gross loans and advances to customers	**20,982**	3,204

All financial assets were held with local counterparties in Malta.

2.4.6 INFORMATION ON THE CREDIT QUALITY OF BALANCES WITH BANKS AND DEBT SECURITIES

As at the end of the reporting period, the Bank held debt securities issued by investment grade sovereign and non-sovereign counterparties. The debt securities held by the Bank were listed on the Malta Stock Exchange, or on other recognised exchanges. Loans and advances to banks included money market placements and balances held with counterparty banks. The issuers and counterparties are approved and regularly reviewed, focusing on market developments.

At the end of the reporting period, none of these financial assets mentioned were past due or impaired.

The credit rating of Malta was classified as investment grade by external rating agencies as at 31 December 2022 and 2021.

The following tables set out information on the credit quality of financial assets measured at amortised cost. The credit quality of the financial assets is determined by external credit ratings applicable to issuers or counterparties. Explanation of the terms 12-month ECL, lifetime ECL and credit impaired are included in Notes 2.4.3.2. and 2.4.3.3.

	2022			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Balances with Central Bank of Malta and other banks at amortised cost				
Gross carrying amount	25,700	-	-	25,700
Loss allowance	(35)	-	-	(35)
Carrying amount	**25,665**	-	-	**25,665**

	2021			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Balances with Central Bank of Malta and other banks at amortised cost				
Gross carrying amount	55,235	-	-	55,235
Loss allowance	(19)	-	-	(19)
Carrying amount	**55,216**	-	-	**55,216**

	2022			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Financial investments measured at amortised cost				
Gross carrying amount	46,857	-	-	46,857
Loss allowance	(54)	-	-	(54)
Carrying amount	**46,803**	-	-	**46,803**

	2021			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Financial investments measured at amortised cost				
Gross carrying amount	17,094	-	-	17,094
Loss allowance	-	-	-	-
Carrying amount	**17,094**	-	-	**17,094**

2.4.7 INFORMATION ON CREDIT QUALITY OF LOANS AND ADVANCES TO CUSTOMERS

The credit quality of loans and advances to customers is managed by the Bank using internal credit ratings. The Bank assigns a grading of Stage 1, Stage 2 or Stage 3 (credit-impaired) on the basis of qualitative and quantitative assessments.

The following table sets out information about the credit quality of loans and advances to customers measured at amortised cost.

	2022			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Loans and advances to customers				
Gross carrying amount	20,982	-	-	20,982
Loss allowance	(17)	-	-	(17)
Carrying amount	**20,965**	-	-	**20,965**

	2021			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Loans and advances to customers				
Gross carrying amount	3,204	-	-	3,204
Loss allowance	-	-	-	-
Carrying amount	**3,204**	-	-	**3,204**

As at 31 December 2022 and 2021, the Bank's loans and advances to customers were neither past due nor impaired.

2.4.8 INFORMATION ON THE CREDIT QUALITY OF FINANCIAL GUARANTEES AND UNDRAWN COMMITMENTS TO LEND

The credit quality of financial guarantees and undrawn commitments to lend is managed by the Bank using internal credit grades. The Bank assigns a grading of Stage 1, Stage 2 or Stage 3 (credit-impaired), on the basis of qualitative and quantitative assessments.

The following table sets out information about the credit quality of financial guarantees and undrawn commitments to lend.

	2022			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Financial guarantees				
Guaranteed amounts	31,003	3,527	893	35,423
Loss allowance	(333)	(614)	(623)	(1,570)

	2021			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Financial guarantees				
Guaranteed amounts	30,361	1,793	1,200	33,354
Loss allowance	(150)	(541)	(462)	(1,153)

The guaranteed amounts are subject to a further total capping of 25% under the SME Invest portfolio and a capping of 50% under the Family Business Transfer Facility portfolio which effectively limit the credit risk exposure of the Bank to €8.0 million (2021: €8.4 million). No portfolio capping is applicable to the GCLS portfolio amounting to €3.6 million (2021: nil) (refer to Note 2.4.1 and Note 15).

	2022			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Undrawn commitments to lend	6,094	-	-	6,094
Loss allowance	(25)	-	-	(25)

	2021			
	STAGE 1 12-MONTH ECL	STAGE 2 LIFETIME ECL	STAGE 3 LIFETIME ECL	TOTAL
	€000	€000	€000	€000
Undrawn commitments to lend	6,094	-	-	6,094
Loss allowance	-	-	-	-

2.4.9 MODIFICATION OF FINANCIAL ASSETS

The contractual terms of a loan may be revised for a number of reasons, including changes in market conditions, customer retention and other factors that are not related to the credit quality of a customer. Forbearance measures comprise concessions made on the contractual terms of a loan in response to a customer's financial difficulties. The Bank categorises loans on which concessions have been granted under conditions of financial difficulties as 'forborne loans' when their contractual payment terms have been revised, because of significant concerns about the customer's ability to meet contractual payments when due.

For the purposes of determining whether changes to a customer's agreement should be treated as forbearance the following types of modification could be regarded as concessionary in cases where the customer is in financial difficulty:

- reduction of the stated interest rate for the remaining original life of the debt;
- extension of the maturity date or dates at a stated interest rate lower than the current market rate for new debt with similar risk;
- reduction of the face amount or maturity amount of the debt; and
- reduction of accrued interest.

As at 31 December 2022 and 2021, none of the Bank's loans and advances to customers were classified as forborne.

2.4.10 LOSS ALLOWANCES

Reconciliation of 12-month and lifetime ECL provision

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent 'step up' (or 'step down') between 12-month and Lifetime ECL;
- additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments derecognised in the period;
- impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- impacts on the measurement of ECL due to changes made to models and assumptions;
- discount unwinding within ECL due to the passage of time, as ECL is measured on a present value basis; and
- write-offs of allowances related to assets that were written off during the period.

The following tables explain the changes in the loss allowance between the beginning and the end of the annual period:

	2022			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Balances with Central Bank of Malta and other banks at amortised cost				
At 1 January 2022	55,235	19	55,235	19
New financial assets purchased	17,759	26	17,759	26
Repayments and disposals	(47,294)	(10)	(47,294)	(10)
At 31 December 2022	**25,700**	**35**	**25,700**	**35**
Total net income statement charge for the year				16

	2021			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Balances with Central Bank of Malta and other banks at amortised cost				
At 1 January 2021	70,583	8	70,583	8
New financial assets purchased	47,142	18	47,142	18
Repayments and disposals	(62,490)	(7)	(62,490)	(7)
At 31 December 2021	**55,235**	**19**	**55,235**	**19**
Total net income statement charge for the year				11

	2022			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Financial investments at amortised cost				
At 1 January 2022	17,094	-	17,094	-
New financial assets purchased	29,932	54	29,932	54
Other movements	(169)	-	(169)	-
At 31 December 2022	**46,857**	**54**	**46,857**	**54**
Total net income statement charge for the year				54

	2021			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Financial investments at amortised cost				
At 1 January 2021	-	-	-	-
New financial assets purchased	17,094	-	17,094	-
At 31 December 2021	**17,094**	**-**	**17,094**	**-**
Total net income statement charge for the year				-

	2022			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Loans and advances to customers at amortised cost				
At 1 January 2022	3,204	-	3,204	-
New and further lending	17,778	17	17,778	17
At 31 December 2022	**20,982**	**17**	**20,982**	**17**
Total net income statement charge for the year				17

	2021			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Loans and advances to customers at amortised cost				
At 1 January 2021	-	-	-	-
New lending	3,204	-	3,204	-
At 31 December 2021	**3,204**	**-**	**3,204**	**-**
Total net income statement charge for the year				-

Expected credit losses in respect of loans and advances to customers as at 31 December 2021 were considered to be insignificant in view of the high value of collateral securing the exposure.

	2022			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Undrawn commitments to lend				
At 1 January 2022	6,096	-	6,096	-
New lending	6,050	25	6,050	25
Loan drawdowns	(6,052)	-	(6,052)	-
At 31 December 2022	**6,094**	**25**	**6,094**	**25**
Total net income statement charge for the year				25

	2021			
	STAGE 1		TOTAL	
	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES	GROSS CARRYING AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000
Undrawn commitments to lend				
At 1 January 2021	-	-	-	-
New lending	6,096	-	6,096	-
At 31 December 2021	**6,096**	**-**	**6,096**	**-**
Total net income statement charge for the year				-

Expected credit losses in respect of undrawn commitments to lend as at 31 December 2021 were considered to be insignificant in view of the high value of collateral securing the exposure.

	2022							
	STAGE 1		STAGE 2		STAGE 3		TOTAL	
	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000	€000	€000	€000	€000
Financial guarantees								
At 1 January 2022	**30,361**	**150**	**1,793**	**541**	**1,200**	**462**	**33,354**	**1,153**
New financial guarantees originated	7,317	225	-	-	-	-	7,317	225
Repayments and disposals	(4,783)	(40)	(353)	(102)	(112)	(60)	(5,248)	(202)
Transfers:								
Stage 1 to Stage 2	(2,148)	(147)	2,148	147	-	-	-	-
Stage 2 to Stage 1	256	96	(256)	(96)	-	-	-	-
Stage 3 to Stage 2	-	-	195	45	(195)	(45)	-	-
Net remeasurement of ECL arising from stage transfers and changes in risk parameters		49		79		266		394
At 31 December 2022	**31,003**	**333**	**3,527**	**614**	**893**	**623**	**35,423**	**1,570**
Total net income statement charge for the year								417

The guaranteed amounts are subject to a further portfolio capping of 25% in respect of the SME Invest portfolio and a portfolio capping of 50% in respect of the Family Business Transfer Facility which effectively limit the credit risk exposure of the Bank to €8.0 million (2021: €8.4 million). No portfolio capping is applicable to the GCLS portfolio amounting to €3.6 million (2021: nil) (refer to Note 2.4.1 and Note 15).

	2021							
	STAGE 1		STAGE 2		STAGE 3		TOTAL	
	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES
	€000	€000	€000	€000	€000	€000	€000	€000
Financial guarantees								
At 1 January 2021	**21,541**	**292**	**1,396**	**162**	**-**	**-**	**22,937**	**454**
New financial guarantees originated	13,807	81	112	-	-	-	13,919	81
Repayments and disposals	(2,668)	(18)	(665)	-	(169)	-	(3,502)	(18)
Transfers:								
Stage 1 to Stage 2	(1,746)	(6)	1,746	6	-	-	-	-
Stage 1 to Stage 3	(573)	(18)	-	-	573	18	-	-
Stage 2 to Stage 3	-	-	(796)	(161)	796	161	-	-
Net remeasurement of ECL arising from stage transfers and changes in risk parameters		(181)		534		283		636
At 31 December 2021	**30,361**	**150**	**1,793**	**541**	**1,200**	**462**	**33,354**	**1,153**
Total net income statement charge for the year								699

2.4.11 WRITE-OFF POLICY

The Bank writes off a loan, and/or a receivable balance (and any related allowance for impairment losses) when management determines that the loan, security and/or receivable is uncollectible, and it has exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. This determination is reached after considering information such as occurrence of significant changes in the borrower/issuer's financial position such that the borrower/issuer can no longer repay the obligation, or that proceeds from collateral will not be sufficient to pay back the entire exposure. There were no write offs recorded during 2022 or 2021.

2.4.12 COLLATERAL

The Bank employs a range of policies and practices to mitigate credit risk. The amount and type of collateral required depends on an assessment of the credit risk of the underlying borrower and the nature of the lending.

Collateral obtained on loans and advances to customers refers to charges in favour of the Bank over real estate properties, cash or securities.

Collateral held as security for financial assets other than loans and advances to customers depends on the nature of the instrument. Debt securities, loans and advances to banks and balances held with the Central Bank of Malta are generally unsecured.

Collateral held in respect of financial guarantee contracts includes charges over real estate properties, cash or securities, obtained through the intermediation of counterparty commercial banks.

The Bank closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Bank will take possession of collateral to mitigate potential credit losses.

Financial guarantees that were credit impaired and in respect of which collateral in the form of immovable property was held as of 31 December 2021 are shown below:

	EXPOSURE AMOUNT	EXPECTED CREDIT LOSSES	EXTENDIBLE VALUE OF COLLATERAL
	€000	€000	€000
Financial guarantee contracts			
Credit-impaired	472	(47)	472
At 31 December 2021	**472**	**(47)**	**472**

As at 31 December 2022, all financial guarantees that were credit-impaired were unsecured.

2.5 MARKET RISK

Market risk comprises the risk of losses in value caused by unexpected changes in market prices (interest rates, equity prices, foreign exchange rates and credit spreads) before the affected positions can be closed out or hedged. Market risk for the Bank consists entirely of interest rate risk, which is the risk of losses due to adverse changes in interest rates. As at 31 December 2022 and 2021, the Bank did not have any foreign exchange exposures and neither held any equity positions.

2.5.1 INTEREST RATE RISK

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or re-price at different times or at different amounts. The risk is managed by monitoring on a continuous basis the level of mismatch of interest rate repricing, taking cognisance of the terms of the Bank's principal financial liabilities and amounts owed to banks, that are not re-priceable.

Interest Rate Benchmark Reform

The IASB published the 'Interest Rate Benchmark Reform – Phase 2: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16' in August 2020, which became effective from 1 January 2021 and was also endorsed for use by the EU during 2021. These amendments represent the second phase of the IASB's project on the effects of the interest rate benchmark reform, addressing issues affecting financial statements when changes are made to contractual cash flows as a result of the reform.

These amendments had no effect on the Bank's financial statements since the Bank was not exposed to IBOR related financial instruments during the reporting period.

Exposure to interest rate risk

The following table summarises the Bank's exposures to interest rate risks. These analyse the Bank's financial instruments, which were interest-bearing, at their carrying amounts, categorised by the earlier of contractual repricing or maturity dates.

	CARRYING AMOUNT	EFFECTIVE INTEREST RATE	LESS THAN 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 YEAR AND 5 YEARS	MORE THAN 5 YEARS
	€000	€000	€000	€000	€000	€000
As at 31 December 2022						
Financial assets						
Balances with Central Bank of Malta	696	1.80%	696	-	-	-
Loans and advances to banks	24,968	1.01%	10,987	4,994	8,987	-
Financial investments	46,803	5.10%	3,979	3,953	35,076	3,795
Loans and advances to customers	20,965	2.42%	2,197	6,590	3,534	8,644
Total financial assets	**93,432**		**17,859**	**15,537**	**47,597**	**12,439**
Financial liabilities						
Amounts owed to banks	15,770	0.60%	3,003	1,204	9,701	1,862
Total financial liabilities	**15,770**		3,003	1,204	**9,701**	1,862
Interest repricing gap			**14,856**	**14,333**	**37,896**	**10,577**
Cumulative gap			**14,856**	**29,189**	**67,085**	**77,662**

	CARRYING AMOUNT	EFFECTIVE INTEREST RATE	LESS THAN 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 YEAR AND 5 YEARS	MORE THAN 5 YEARS
	€000	€000	€000	€000	€000	€000
As at 31 December 2021						
Financial assets						
Balances with Central Bank of Malta	355	-0.50%	355	-	-	-
Loans and advances to banks	54,860	0.33%	27,926	12,934	14,000	-
Financial investments	17,094	0.05%	-	-	10,102	6,992
Loans and advances to customers	3,204	2.75%	-	-	400	2,804
Total financial assets	**75,513**		**28,281**	**12,934**	**24,502**	**9,796**
Financial liabilities						
Amounts owed to banks	19,706	0.60%	2,647	2,647	14,412	-
Total financial liabilities	**19,706**		2,647	2,647	**14,412**	-
Interest repricing gap			**25,634**	**10,287**	**10,090**	**9,796**
Cumulative gap			**25,634**	**35,921**	**46,011**	**55,807**

Interest rate profile

The table below analyses interest-earning assets and interest-bearing liabilities between those that have a fixed rate and those with a variable rate:

	2022		2021	
	FIXED	VARIABLE	FIXED	VARIABLE
	€000	€000	€000	€000
Interest-earning assets				
Balances with Central Bank of Malta	-	696	-	355
Loans and advances to banks	14,003	10,965	50,638	4,222
Financial investments	46,803	-	17,094	-
Loans and advances to customers	11,727	9,238	-	3,204
	72,533	**20,899**	**67,732**	**7,781**
Interest-bearing liabilities				
Amounts owed to banks	15,770	-	19,706	-
	15,770	**-**	**19,706**	**-**

Loans and advances to customers include variable interest rate loans of €9,256,000 (2021: €3,204,000) which are fixed for a period of 12 years since inception, and which will reprice in 2033.

Fair value sensitivity analysis for fixed-rate instruments

The Bank does not hold any fixed rate financial assets or liabilities which are measured at fair value. Loans and advances to banks and customers, amounts owed to banks and financial investments measured at amortised cost are not expected to be disposed of and are therefore not subject to fair value interest rate risk.

Cash flow sensitivity for variable rate instruments

The Bank is exposed to cash flow interest rate risk principally in respect of financial assets which are subject to floating interest rates. A sensitivity analysis in respect of interest rate changes is not required since variable rate loans and advances to customers reprice in 2033, and interest income on variable rate loans to banks is not considered significant.

2.5.2 CURRENCY RISK

At the reporting date, the Bank's financial assets and liabilities were all denominated in Euro and therefore the Bank was not exposed to currency risk.

2.5.3 FAIR VALUES OF FINANCIAL INSTRUMENTS NOT MEASURED AT FAIR VALUE

All of the Bank's financial assets are measured at amortised cost in the Statement of Financial Position and reported net of impairment allowances to reflect the estimated recoverable amounts.

The directors consider the carrying amounts of these assets, excluding financial investments, to be a reasonable estimate of their fair value principally in view of the relatively short periods to repricing or maturity from the end of the reporting period.

Financial investments

The fair value of debt securities measured at amortised cost on the Statement of Financial Position amounted to €44,983,012 (2021: €16,917,500) as at 31 December 2022, based on quoted prices.

2.6 LIQUIDITY RISK

Liquidity risk is the risk that the Bank's obligations to repay liabilities or fund new loans exceed the Bank's ability to raise funds from either the liquidation of assets or the acceptance of new funding. Liquidity risk arises when the Bank does not exactly match the maturity of assets with the maturity of liabilities as it must always be able to meet its liabilities as they fall due. Liquidity risk may also be affected by the depth of the market in which the Bank has its exposure in assets and liabilities.

The Bank's approach to managing liquidity risk is to ensure, to the extent possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation.

The Bank's liquidity risk management focuses on structuring assets and liabilities in order to diversify funding sources and maintain a spread of asset and liability maturities to the extent practicable.

The Bank's liquidity risk during 2022 and 2021 was insignificant in view of the margin of liquidity available to manage repayments of liabilities.

The following table discloses financial assets and liabilities at the end of the reporting period by the remaining period to maturity:

	CARRYING AMOUNT	WITHIN 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 YEAR AND 5 YEARS	MORE THAN 5 YEARS	NO MATURITY DATE
	€000	€000	€000	€000	€000	€000
As at 31 December 2022						
Financial assets						
Balances with Central Bank of Malta	696	696	-	-	-	-
Loans and advances to banks	24,968	10,987	4,994	8,987	-	-
Financial investments	46,803	3,978	3,954	35,076	3,795	-
Loans and advances to customers	20,965	2,197	6,590	3,534	8,644	-
Other assets	1,181	985	162	34	-	-
Total financial assets	**94,613**	**18,843**	**15,700**	**47,631**	**12,439**	**-**
Financial liabilities						
Amounts owed to banks	15,770	3,003	1,204	9,701	1,862	-
Amounts owed to other entities	4,305	-	-	-	-	4,305
Other liabilities	278	139	102	25	4	8
Total financial liabilities	**20,353**	**3,142**	**1,306**	**9,726**	**1,866**	**4,313**
Maturity gap		**15,701**	**14,394**	**37,905**	**10,573**	
Cumulative gap		**15,701**	**30,095**	**68,000**	**78,573**	

	CARRYING AMOUNT	WITHIN 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 YEAR AND 5 YEARS	MORE THAN 5 YEARS	NO MATURITY DATE
	€000	€000	€000	€000	€000	€000
As at 31 December 2021						
Financial assets						
Balances with Central Bank of Malta	355	355	-	-	-	-
Loans and advances to banks	54,860	27,926	12,934	14,000	-	-
Financial investments	17,094	-	-	10,102	6,992	-
Loans and advances to customers	3,204	-	-	400	2,804	-
Other assets	857	660	101	86	10	-
Total financial assets	**76,370**	**28,941**	**13,035**	**24,588**	**9,806**	**-**
Financial liabilities						
Amounts owed to banks	19,706	2,647	1,219	9,748	6,092	-
Amounts owed to other entities	2,935	-	-	-	-	2,935
Other liabilities	454	406	11	16	13	8
Total financial liabilities	**23,095**	**3,053**	**1,230**	**9,764**	**6,105**	**2,943**
Maturity gap		**25,888**	**11,805**	**14,824**	**3,701**	
Cumulative gap		**25,888**	**37,693**	**52,517**	**56,218**	

3. BALANCES WITH CENTRAL BANK OF MALTA AND OTHER BANKS

	2022 €	2021 €
Current		
Repayable on call and at short notice	**11,697,892**	25,300,305
Term loans and advances	**14,001,387**	29,934,479
Gross carrying amount	**25,699,279**	55,234,784
Less allowances for expected credit losses	**(34,592)**	(19,035)
Net carrying amount	**25,664,687**	55,215,749

By virtue of an agreement entered into between the Ministry for European Affairs and Equality (the 'Managing Authority') and the Bank, as the entity entrusted with the implementation of the Further Studies Made Affordable ('FSMA') and Further Studies Made Affordable Plus ('FSMA+') programmes, an amount of €4.3 million (2021: €3 million) was held in favour of, and for the ultimate benefit of the Managing Authority as part of the implementation of the FSMA programme. The said amount will be used to provide financial guarantees and interest rate subsidies on loans sanctioned by counterparty commercial banks in favour of individuals seeking to further their studies at a tertiary education institution or equivalent (see Note 13).

4. FINANCIAL INVESTMENTS

The Bank's financial investments measured at amortised cost are analysed as follows:

	2022 €	2021 €
Debt instruments		
Local government debt securities listed on the Malta Stock Exchange	**24,857,265**	17,093,955
Other local debt securities listed on the Irish Stock Exchange	**21,945,798**	-
Net carrying amount	**46,803,063**	17,093,955

The movement in the carrying amount of financial investments is summarised as follows:

	2022 €	2021 €
At 1 January	**17,093,955**	-
Acquisitions	**29,931,419**	17,183,700
Amortisation	**(168,109)**	(89,745)
Expected credit loss allowances	**(54,202)**	-
At 31 December	**46,803,063**	17,093,955

5. LOANS AND ADVANCES TO CUSTOMERS

	2022 €	2021 €
Term loans and advances	**20,982,176**	3,203,951
Less: expected credit loss allowances	**(17,092)**	-
Net carrying amount	**20,965,084**	3,203,951

6. INVESTMENT PROPERTY

	2022 €	2021 €
Year ended 31 December		
Opening net book amount	**623,519**	632,089
Depreciation charge	**(8,571)**	(8,570)
Closing net book amount	**614,948**	623,519
At 31 December		
Cost	**642,851**	642,851
Accumulated depreciation	**(27,903)**	(19,332)
Net book amount	**614,948**	623,519

Investment property is located outside of Malta and comprises of an office building which is currently being leased to a third party. As at 31 December 2022 and 2021, the Board considers the carrying amount of the investment property to be fairly close to its fair value as reflected below.

Disclosures required in terms of IFRS 13 in relation to fair value attributable to investment property are presented below.

		SIGNIFICANT UNOBSERVABLE INPUTS	
	FAIR VALUE AT 31 DECEMBER 2022 AND 2021 €	VALUATION TECHNIQUE	VALUE PER SQUARE RENTAL METRE €
Office Building	**640,000**	Equivalent value per square metre	**4,100**

This fair value is considered as Level 3 and is based on the highest and best use of the property, which is equivalent to its current use.

7. PROPERTY AND EQUIPMENT

	BUILDINGS	IMPROVEMENTS TO PROPERTY	FURNITURE	COMPUTER EQUIPMENT	OTHER EQUIPMENT	TOTAL
	€000	€000	€000	€000	€000	€000
Year ended 31 December 2022						
Opening net book amount	3,104,184	271,150	86,217	73,045	20,995	3,555,591
Additions	-	100,931	19,161	41,234	24,325	185,651
Disposals	-	-	-	(2,301)	-	(2,301)
Depreciation charge	(42,162)	(17,474)	(10,526)	(25,301)	(5,474)	(100,937)
Depreciation released on disposal	-	-	-	1,848	-	1,848
Closing net book amount	**3,062,022**	**354,607**	**94,852**	**88,525**	**39,846**	**3,639,852**
At 31 December 2022						
Cost	3,135,806	377,701	114,713	150,846	47,218	3,826,284
Accumulated depreciation	(73,784)	(23,094)	(19,861)	(62,321)	(7,372)	(186,432)
Net book amount	**3,062,022**	**354,607**	**94,852**	**88,525**	**39,846**	**3,639,852**

	BUILDINGS	IMPROVEMENTS TO PROPERTY	FURNITURE	COMPUTER EQUIPMENT	OTHER EQUIPMENT	TOTAL
	€000	€000	€000	€000	€000	€000
At 1 January 2021						
Cost	3,135,806	47,783	31,217	66,686	1,131	3,282,623
Accumulated depreciation	-	-	(6,242)	(24,382)	(262)	(30,886)
Net book amount	3,135,806	47,783	24,975	42,304	869	3,251,737
Year ended 31 December 2021						
Opening net book amount	3,135,806	47,783	24,975	42,304	869	3,251,737
Additions	-	228,987	64,335	45,227	21,763	360,312
Depreciation charge	(31,622)	(5,620)	(3,093)	(14,486)	(1,637)	(56,458)
At 31 December 2021	3,104,184	271,150	86,217	73,045	20,995	3,555,591
At 31 December 2021						
Cost	3,135,806	276,770	95,552	111,913	22,893	3,642,934
Accumulated depreciation	(31,622)	(5,620)	(9,335)	(38,868)	(1,898)	(87,343)
Net book amount	3,104,184	271,150	86,217	73,045	20,995	3,555,591

As at 31 December 2022, capital expenditure authorised and contracted for amounted to €117,000 (2021: €117,000) and is mainly related to the acquisition of immovable property. This contracted expenditure is included within Commitments in Note 15.

8. RIGHT-OF-USE ASSETS

The Bank leases motor vehicles for the use of its executives. Rental contracts are typically made for fixed periods but may have extension options. The extension options held are generally exercisable by both the Bank and the respective lessor, and hence the lease terms exclude the impact of the extension options

RIGHT-OF-USE-ASSETS

	2022	2021
	€	€
Opening net book amount	**25,703**	36,695
Additions	**-**	2,315
Depreciations	**(14,020)**	(13,307)
At 31 December	**11,683**	25,703

LEASE LIABILITIES

	2022	2021
	€	€
Current	**11,745**	13,715
Non-current	**-**	11,745
At 31 December	**11,745**	25,460

The key movements in lease liabilities principally comprise of payments and interest expense.

The total cash payments for leases in 2022 amounted to €14,114 (2021: €11,796).

The income statement reflects the following amounts relating to leases:

	2022	2021
	€	€
Depreciation charge of right-of-use asset	**14,020**	13,307
Interest expense on lease liabilities	**399**	681
	14,419	13,988

9. INTANGIBLE ASSETS

	COMPUTER SOFTWARE €
At 1 January 2021	
Cost	22,617
Accumulated amortisation	(4,214)
	18,403
Year ended 31 December 2021	
At 1 January 2021	18,403
Additions	11,906
Amortisation charge	(6,097)
At 31 December 2021	24,212
At 31 December 2021	
Cost	34,523
Accumulated amortisation	(10,311)
Net book amount	24,212
Year ended 31 December 2022	
At 1 January 2022	24,212
Additions	2,230
Amortisation charge	(7,018)
At 31 December 2022	19,424
At 31 December 2022	
Cost	36,753
Accumulated amortisation	(17,329)
Net book amount	19,424

10. OTHER ASSETS

	2022 €	2021 €
Accrued interest	**453,307**	84,693
Prepayments	**51,597**	164,053
Accrued income from financial guarantees (Note 18)	**108,693**	61,930
Accrued administrative fee income (Note 19)	**611,704**	541,963
Other receivables	**7,549**	4,096
	1,232,850	856,735

11. SHARE CAPITAL

	2022 €	2021 €
Authorised		
2,000,000 shares of €100 each	**200,000,000**	200,000,000
Issued and fully paid up		
800,000 (2021: 600,000) shares of €100 each	**80,000,000**	60,000,000

The Bank is fully owned by the Government of Malta. In accordance with article 10(1) of the Malta Development Bank Act, Chapter 574 of the Laws of Malta, the authorised share capital of the Bank is €200 million divided into 2 million shares having a par value of €100 each.

During 2022, the Bank issued 200,000 shares at par value of €100 each which were fully subscribed by the Government of Malta. In 2021, the Bank also issued 100,000 shares at par value of €100 each, which were also fully subscribed by the Government of Malta.

The Bank's objectives when managing capital are to safeguard the Bank's ability to continue as a going concern in order to perform the functions assigned to it under the Malta Development Bank Act, Chapter 574 of the Laws of Malta, and to maintain an optimal capital structure.

Government guarantee

In terms of Article 5 of the Malta Development Bank Act, the Government of Malta guarantees up to 100% of all obligations of the Bank and up to 100% of the loans, facilities and guarantees issued by the Bank. A Government guarantee was issued on 16 February 2018 in favour of the Bank. The amount of the guarantee stood at €150 million as at 31 December 2022 (2021: €150 million).

12. AMOUNTS OWED TO BANKS

	2022 €	2021 €
Current	**4,207,001**	5,294,117
Non-current	**11,562,680**	14,411,766
	15,769,681	19,705,883

On 24 June 2019, the Bank entered into a loan agreement with KfW, for the amount of €45 million. On 31 March 2020 and 30 June 2020, the Bank withdrew €10 million and €15 million respectively, however the disbursement period of this facility expired on 23 June 2022. The loan is unsecured, subject to a fixed interest rate of 0.6% and matures in 2029.

The Bank is also party to a loan agreement with the European Investment Bank for an amount of €60 million. This loan amount is made up of fixed and floating rate tranches. As at the reporting date, no amounts under this agreement had been disbursed.

13. AMOUNTS OWED TO ENTITIES

By virtue of an agreement entered into between the Managing Authority and the Bank, as the entity entrusted with the implementation of the FSMA and FSMA+ programmes, an amount of €4.3 million (2021: €3 million) was held in favour of, and for the ultimate benefit of the Managing Authority as part of the implementation of the FSMA and FSMA+ programmes. The said amount is being used to provide financial guarantees and interest rate subsidies on loans sanctioned by counterparty commercial banks in favour of individuals seeking to further their studies at a tertiary education institution or equivalent (see Note 3).

14. OTHER LIABILITIES

	2022 €	2021 €
Accounts payable	**47,257**	132,530
Lease liabilities (Note 8)	**11,745**	25,460
Accrued interest payable	**29,320**	34,600
Accruals	**189,370**	260,859
Expected credit losses on financial guarantees (Note 15)	**1,595,330**	1,153,268
	1,873,022	1,606,717

15. COMMITMENTS

As at the end of the reporting period, total outstanding commitments were as follows:

	2022 €	2021 €
Commitments		
Undrawn commitments to lend	**6,093,762**	6,096,049
Capital commitments	**117,000**	117,000
Financial guarantees		
Maximum exposure guaranteed by the MDB on SME Invest and FBT	**7,963,556**	8,355,622
Maximum exposure guaranteed by the MDB on GCLS	**3,630,000**	-
Total commitments	**17,804,318**	14,568,671

As detailed in Note 2.4.1, the Bank, in line with its principal activities and business model, originates a number of different types of financial guarantees.

The guaranteed amounts are subject to a portfolio capping of 25% in respect of the SME Invest portfolio and a portfolio capping of 50% in respect of the Family Business Transfer Facility which effectively limit the credit risk exposure of the Bank to €8.0 million (2021: €8.4 million). No portfolio capping is applicable to the GCLS portfolio amounting to €3.6 million (2021: nil) (refer to Note 2.4.1).

Financial guarantees are further explained below:

	2022			2021		
	DRAWN COMMITMENTS €	UNDRAWN COMMITMENTS €	TOTAL €	DRAWN COMMITMENTS €	UNDRAWN COMMITMENTS €	TOTAL €
Financial guarantees						
Total sanctioned loans (net of repayments)	**33,535,954**	**12,254,781**	**45,790,735**	25,291,163	16,401,514	41,692,677
Guaranteed amount by the MDB per individual exposure	**26,828,763**	**8,593,825**	**35,422,588**	20,232,930	13,121,211	33,354,141
Maximum exposure guaranteed by the MDB (portfolio capping)			**11,593,556**			8,355,622

As at 31 December 2022, the expected credit losses arising on financial guarantees amounted to €1,570,411 (2021: €1,153,268).

Expected credit losses in respect of undrawn commitments attributable to loans and advances to customers as at 31 December 2022 amounted to €24,919 (2021: nil).

16. INTEREST RECEIVABLE AND SIMILAR INCOME

	2022 €	2021 €
On loans and advances to banks and balances with Central Bank of Malta	**189,826**	153,267
On loans and advances to customers	**337,276**	13,697
	527,102	166,964
On debt instruments	**328,684**	94,272
Net amortisation of discounts and premiums	**(168,109)**	(89,745)
	160,575	4,527
Total interest receivable and similar income	**687,677**	171,491

17. INTEREST PAYABLE AND SIMILAR EXPENSE

	2022 €	2021 €
On balances with Central Bank of Malta	**1,451**	47,979
On amounts owed to banks	**176,286**	228,206
On lease liabilities (Note 8)	**399**	680
Total interest payable and similar expense	**178,136**	276,865

18. INCOME FROM FINANCIAL GUARANTEES

	2022 €	2021 €
SME Invest Scheme	**154,418**	86,335
Family Business Success Scheme	**530**	336
Total income from financial guarantees	**154,948**	86,671

As detailed in Note 2.4.1, the Bank issues financial guarantees to credit institutions (Note 15) who are eligible under one of the Bank's credit schemes. The Bank receives a portion of the interest charged by the credit institutions in the form of a guarantee fee as consideration for providing these guarantees.

19. ADMINISTRATIVE FEE INCOME

	2022	2021
	€	€
COVID-19 Guarantee Scheme	**2,505,570**	1,533,275
Further Studies Made Affordable	**34,730**	49,310
Further Studies Made Affordable Plus	**30,100**	-
Total administrative fee income	**2,570,400**	1,582,585

As detailed in Note 2.4.1, the Bank has been entrusted to implement and manage guarantee schemes on behalf of the Ministry for European Affairs and Equality and the Government of Malta. The Bank receives fee income as a consideration for the implementation and ongoing administration of these schemes.

20. OTHER INCOME

	2022	2021
	€	€
Rental income	**33,941**	32,315
Other income	**10,855**	1,361
Total other income	**44,796**	33,676

21. CHANGES IN EXPECTED CREDIT LOSSES

	2022	2021
	€	€
On balances with Central Bank of Malta and other banks	**15,557**	10,830
On financial investments	**54,202**	-
On loans and advances to customers	**17,092**	-
On undrawn loan commitments	**24,920**	-
On financial guarantee contracts	**417,143**	698,849
Total changes in expected credit losses	**528,914**	709,679

22. ADMINISTRATIVE EXPENSES

	2022	2021
	€	€
Legal and professional fees	**141,143**	156,936
Supervisory fees	**19,500**	19,500
Directors' fees	**84,572**	89,612
Travelling and accommodation	**11,908**	2,973
Memberships of local and international associations	**37,372**	41,797
Insurance costs	**51,689**	48,584
Advertising and public awareness	**27,024**	41,271
Repairs and maintenance	**72,843**	52,764
Other	**147,830**	98,730
Total administrative expenses	**593,881**	552,167

Other administrative expenses include stationery, telecommunication expenses, cleaning expenses, water and electricity, IT costs and other miscellaneous expenses.

Auditor's remuneration

Fees charged by the auditor, exclusive of VAT, for services rendered relate to the following:

	2022	2021
	€	€
Annual statutory audit	**35,000**	20,000

23. EMPLOYEE COMPENSATION AND BENEFITS

	2022	2021
	€	€
Staff costs		
- Wages, salaries and allowances	**1,304,294**	1,274,385
- Social security costs	**49,686**	42,515
- Other costs	**20,864**	7,063
Total employee compensation and benefits	**1,374,844**	1,323,963

The average number of persons employed by the Bank during the year was as follows:

	2022	2021
	€	€
Senior management	**10**	10
Middle management	**11**	9
Total average number of employees	**21**	19

24. NET CASH GENERATED FROM/(USED IN) OPERATING ACTIVITIES

	2022	2021
	€	€
Profit/(loss) for the year	**651,500**	(1,072,683)
Adjustments for:		
Depreciation of investment property, property and equipment and right-of-use assets (Notes 6, 7, 8)	**123,528**	78,335
Loss on disposal of property and equipment	**453**	-
Amortisation of intangible assts (Note 9)	**7,018**	6,097
Interest income on debt instruments	**(328,684)**	(94,272)
Net amortisation of discounts and premiums on financial investments (Note 16)	**168,109**	89,745
Change in expected credit losses (Note 21)	**528,914**	709,679
Interest expense on lease liabilities (Note 8)	**399**	681
	1,151,237	(282,418)
Changes in operating assets and liabilities:		
Decrease/(increase) in loans and advances to banks (Note 3)	**15,933,091**	(4,331,355)
Increase in loans and advances to customers (Note 5)	**(17,778,225)**	(3,203,951)
Increase/(decrease) in amounts owed to entities (Note 13)	**1,370,573**	(737,095)
(Increase)/decrease in other assets (Note 10)	**(376,115)**	1,403,958
(Decrease)/increase in accruals and accounts payable (Note 14)	**(162,042)**	241,427
Net cash generated from/(used in) operating activities	**138,519**	(6,909,434)

25. CASH AND CASH EQUIVALENTS

The table below shows an analysis of the Bank's balances of cash and cash equivalents as shown in the Statement of Cash Flows. Cash and cash equivalents comprise of demand deposits and balances with a contractual maturity of less than three months.

	2022	2021
	€	€
Balances with Central Bank of Malta and other banks		
Repayable on call and at short notice (Note 3)	**11,697,892**	25,300,305

26. RELATED PARTIES

26.1 IDENTIFICATION OF RELATED PARTIES AND THE ULTIMATE CONTROLLING PARTY

The Bank's ultimate controlling party is the Government of Malta. All functions and bodies forming part of the Government of Malta (including ministries), together with all entities that are ultimately controlled by the Government of Malta or whose share capital is entirely owned by the Government of Malta, are considered to be related parties. Key management personnel of the Bank are also considered to be related parties.

Key management personnel are defined as those persons having the authority and responsibility for planning, directing and controlling the activities of the Bank, being the Board of Directors and the Bank's chief officers.

26.2 TRANSACTIONS WITH THE SHAREHOLDER

During the year, the following transactions were undertaken by the Bank with its shareholder and other entities controlled by the shareholder:

	2022	2021
	€	€
Income received from related parties		
Interest receivable and similar income	**172,883**	80,994
Income from financial guarantees	**111,455**	93,984
Administrative fee income	**1,820,716**	1,178,656
Other income	**33,941**	32,315
Interest and expenses paid to related parties		
Interest payable and similar expense	**1,451**	47,979
Administrative expenses	**84,131**	104,508

The Bank treats all related party transactions at arm's length in a transparent, open and non-discriminatory manner. The Bank acts independently and in an autonomous manner and does not seek nor receive instructions from an authority, public or otherwise, or from any other institution.

26.3 BALANCES WITH THE SHAREHOLDER

As at the end of the reporting period, the following balances were held by the Bank with its shareholder and other entities controlled by the shareholder:

	2022	2021
	€	€
Amounts owed by related parties		
Balances with Central Bank of Malta	**696,456**	355,352
Loans and advances to banks	**6,205,936**	770,210
Financial investments	**46,803,063**	17,093,955
Other assets	**598,701**	24,000
Amounts owed to related parties		
Amounts owed to other entities	**4,305,341**	2,934,768
Other liabilities	**22,787**	13,610

26.4 TRANSACTIONS WITH KEY MANAGEMENT PERSONNEL

	2022	2021
	€	€
Compensation to key management personnel	**874,532**	815,154

27. ACCOUNTING ESTIMATES AND JUDGEMENTS

27.1 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING THE BANK'S ACCOUNTING POLICIES

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

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

27.2 MEASUREMENT OF THE EXPECTED CREDIT LOSSES

The measurement of the ECL allowance for financial guarantees is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour. Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is further detailed in Note 2.4.3 – 'Expected credit loss measurement'.

A number of significant judgements are required in measurement of ECLs, such as:

- determining the criteria for significant increase in credit risk;
- choosing appropriate models and assumptions for the measurement of ECLs; and
- establishing the number and relative weightings of forward-looking scenarios and associated ECLs.

27.3 ASSESSMENT OF ESTIMATES AND JUDGEMENTS

In the opinion of the directors, the accounting estimates and judgements made in the course of preparing these financial statements, which have been highlighted above, are not difficult, subjective or complex to a degree, which would warrant their description as critical in terms of the requirements of IAS 1.

However, the directors would like to draw attention to these accounting judgements that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the next financial year. In this respect, these primarily comprise assumptions and estimates relating to the calculation of impairment allowances in respect of financial guarantee contracts (see Note 2.4.3 – 'Expected credit loss measurement').

28. STATUTORY INFORMATION

The Malta Development Bank is a Bank established by virtue of the Malta Development Bank Act, 2017 (Act XXI of 2017 – Cap. 574) with its registered address at 5, Market Street, Floriana, Malta.

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