

COMPANY REGISTRATION NUMBER 5781326

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**

**ANNUAL REPORT**

**31 MARCH 2014**

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**ANNUAL REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

<b>CONTENTS</b>	<b>PAGES</b>
<i>Officers and professional advisers</i>	2
<i>Directors' report</i>	3 - 5
<i>Strategic report</i>	6 - 13
<i>Statement of directors' responsibilities in respect of the directors' report, strategic report and the financial statements</i>	14
<i>Independent auditor's report to the shareholders of Punjab National Bank (International) Limited</i>	15 - 16
<i>Statement of financial position</i>	17
<i>Statement of profit or loss</i>	18
<i>Statement of comprehensive income</i>	19
<i>Statement of changes in equity</i>	20 - 21
<i>Statement of cash flows</i>	22
<i>Notes to the financial statements</i>	23 - 68



**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**DIRECTORS' REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

The directors have pleasure in presenting the annual report and the audited financial statements for the year ended 31 March 2014. These financial statements have been prepared in accordance with the Companies Act 2006 and applicable International Financial Reporting Standards as endorsed by the European Union.

**RESULTS AND DIVIDENDS**

The operating profit before provisions, tax and dividends for the current financial year has increased by 13.12% (\$23,871 thousand at 31 March 2014 as against \$21,103 thousand at 31 March 2013). This was led mainly by increase in net interest income by \$8,241 thousand during the year. The profit before taxation for the year ended 31 March 2014 amounted to \$8,633 thousand (2013: \$6,978 thousand) and the profit after tax is \$6,990 thousand (2013: \$5,374 thousand).

The financial statements for the reporting year ended 31 March 2014 are shown on pages 17 to 68. Performance highlights are given in the Strategic Report included as part of the financial statements.

As in the previous years, the directors have not recommended any payment of dividend on equity share capital, however, dividend at the rate of LIBOR plus 4% amounting to \$1,111 thousand (2013: \$1,168 thousand) has been paid on the amount of Perpetual Tier II capital.

Details of changes in management and governance structure of the Bank during the year are shown on page 2 of this Annual Report.

**PRINCIPAL ACTIVITY AND REVIEW OF THE BUSINESS**

Punjab National Bank (International) Limited ('PNBIL' or the 'Company' or the 'Bank'), a UK incorporated 100% subsidiary of Punjab National Bank – India (PNB), offers commercial banking services to customers and is authorised by Prudential Regulation Authority (PRA) and regulated by the Financial Conduct Authority (FCA) and the Prudential Regulation Authority (PRA). Our Parent is one of the leading public sector banks of India. PNB had an asset base of \$87.11 billion as at 31 December 2013 (prior year \$78.45 billion as at 31 December 2012). PNBIL started its operations on 10 May 2007 after obtaining regulatory approval on 13 April 2007 and its main business is to provide corporate and retail banking services to different segments of customers, particularly to those with business or personal links with India and to UK residents.

PNBIL started its operations with two branches in London, one in Southall and a second branch at Gresham Street (since now moved to 1- Moorgate London) in Central London. Five new branches were opened since then, and the Bank is presently operating through its seven branches across UK. While the Central London branch mainly caters to corporate clients, all other branches focus on retail clients. PNBIL has received a good response from the market and built a brand image in the local market.

Major activities of the Bank include accepting deposits from both retail and corporate clients, lending to retail and corporate clients, making rupee and other remittances for its clients and treasury operations to support its funds management and to meet cross currency transactions of its clients. Bank has also built a portfolio of investments on its own account, held mainly for liquidity management. The main function of the treasury operations of the Bank continues to be to resource funding for the Bank, to maintain comfortable liquidity position throughout the financial year and providing guidance on pricing of assets and liabilities.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**DIRECTORS' REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

Offering simple deposit banking products, relationship banking, retail and corporate lending and remittances continues to be the core business for the Bank. The Indian Rupee (INR) remittance scheme of the Bank has stabilised and gained popularity among the ethnic population. PNBIL launched a debit card for its current account holders and also started providing internet banking services in the year 2008-2009. During the current year, new contactless debit card under Master Card has been launched. While new customers are being issued contactless cards, existing Maestro Card holders are being provided replacement in phases. Operations in the new IBS server installed last year for the purpose of improving internet banking services were stabilised during the year, leading to increase in internet banking operations. Both the variants of Variable Rate Cash ISA and Fixed Rate Cash ISA are gaining popularity. Dedicated in-house Help Line Service Centre established last year has also stabilised and has helped the Bank in improving its relationship banking and customer service.

Key performance highlights, Business Review, Capital Structure, Risks and Uncertainties affecting the Bank and future strategy are given in the Strategic Report included as part of this Annual Report.

**DIRECTORS**

During the year under review, the two Non-Executive Directors ceased to remain on account of their unfortunate death. They have been replaced by two new Non-Executive Directors. Current directors are listed on page 2.

**INTERNAL CONTROL AND FINANCIAL REPORTING**

The directors are responsible for establishing effective internal control in the Bank and for reviewing its effectiveness. Procedures have been designed for safeguarding assets against unauthorised use or disposition; for maintaining proper accounting records; and for ensuring the reliability of financial information used within the business or for publication. Such procedures are designed to contain and manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material misstatement, errors, losses or fraud.

The directors have designed and established procedures to provide effective internal control within the Bank. Such procedures for the on-going identification, evaluation and management of the significant risks faced by the Bank have been in place throughout the year and up to 30 April 2014, the date of approval of the Annual Report for the year ended 31 March 2014.

The directors and senior management of the Bank have adopted policies which set out the Board's attitude to risk and internal control. Key risks identified by the directors are formally reviewed and assessed at least once a year by the Board vis-à-vis its risk appetite, in addition to which key business risks are identified, evaluated and managed by operating management on an on-going basis by means of procedures such as physical controls, credit and other authorisation limits and segregation of duties. The Board also receives regular reports on any risk matters that need to be brought to its attention. Significant risks identified in connection with the development of new activities are subject to consideration by the Board.

There are well established budgeting procedures in place and reports are presented regularly to the Board detailing the results of each principal business unit, variances against budget and prior year, and other performance data.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**DIRECTORS REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

The effectiveness of the internal control system is reviewed regularly by the Board and the audit committee. Board also receives reports of reviews undertaken by the internal audit function as well as reports from the external auditors which include details of internal control matters that they have identified as part of the financial statements audit. Certain aspects of the system of internal control are also subject to regulatory supervision, the results of which are monitored closely by the Board.

**STATEMENT AS TO DISCLOSURE OF INFORMATION TO THE AUDITOR**

Each of the persons who are directors at the date of approval of this annual report confirm that:

- so far as the director is aware, there is no relevant audit information of which the company's auditor is unaware, and
- the director has taken all steps that they ought to have taken to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

**ELECTIVE RESOLUTIONS**

The company, being wholly-owned by Punjab National Bank, has elected to dispense with the requirement to hold annual general meetings, present Directors' reports and financial statements before a general meeting and re-appoint its auditor annually.

**AUDITOR**

KPMG Audit Plc has notified the Company that they are not seeking re-appointment. In accordance with Section 489 of the Companies Act 2006, a resolution for the re-appointment of KPMG LLP as auditor of the Company is to be proposed at the forthcoming Annual General Meeting

**GENERAL MEETINGS**

In accordance with the Companies Act 2006 the company is not required to hold an annual general meeting



**Bhupinder Singh Passi**  
Secretary

**Company number: 5781326**

1, Moorgate, London  
EC2R 6JH (UK)

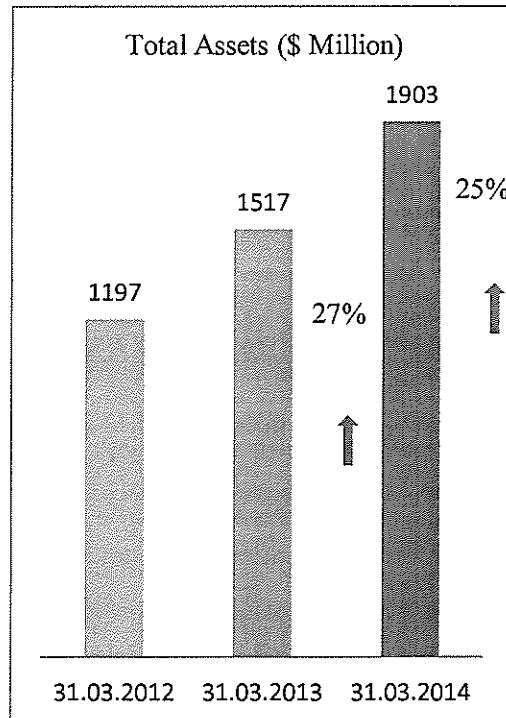
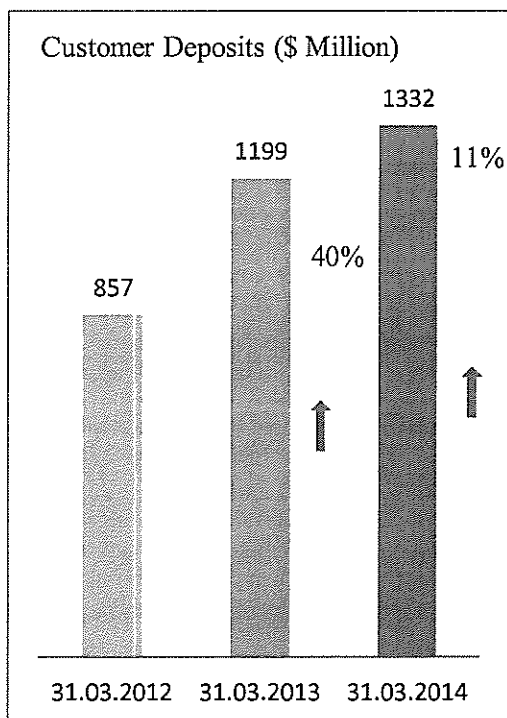
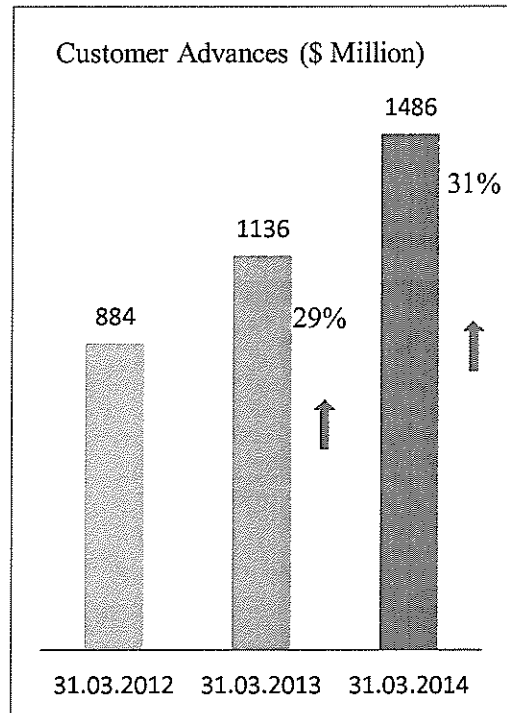
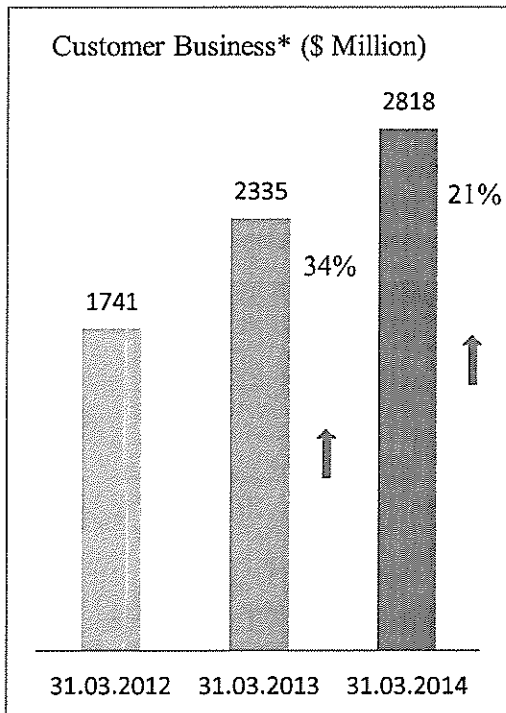
30 April 2014

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

This strategic report should be read in conjunction with the Directors' Report where some of the requirements of this report have been discussed.

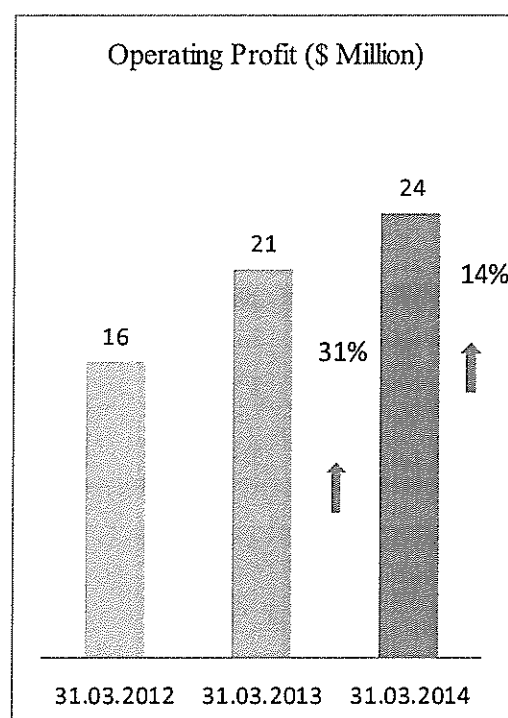
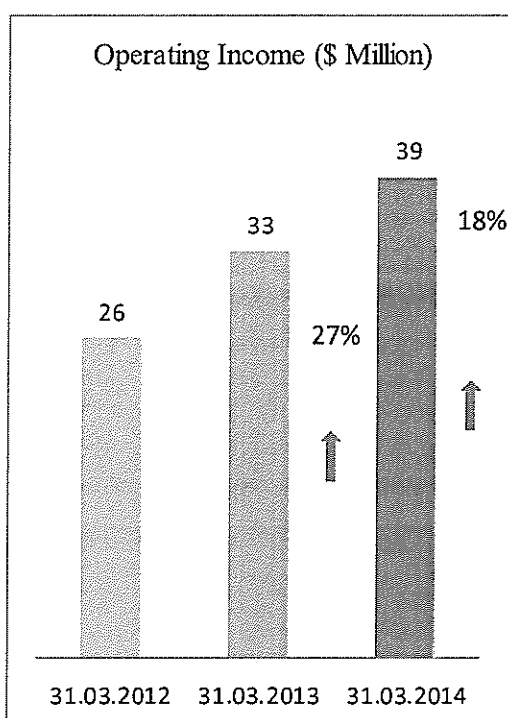
**Financial Highlights**

Key performance highlights of the Bank are as below:



\*Customer business is defined as customer advances plus customer deposits.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**



**Non-Financial Highlights**

	2012	2013	2014
No. of Branches	7	7	7
No. of Employees	85	91	96

This is the seventh year of operations for the Bank; and the Bank continued to show good progress in its business development during the financial year ended 31 March 2014. The total customer business of the Bank has increased from \$2,335,487 thousand as at 31 March 2013 to \$2,817,817 thousand as at 31 March 2014, a year-on-year increase of 20.65%. The operating profit for the year ended 31 March 2014 amounted to \$23,871 thousand (2013: \$21,103 thousand), a year on year increase of 13.12%. Operating profit was after Mark to Market loss of \$4,033 thousand (2013: \$1,308 thousand) on HFT investments, mainly UK and US treasury bills. The profit before taxation for the year ended 31 March 2014 amounted to \$8,633 thousand (2013: \$6,978 thousand) and the profit after tax is \$6,990 thousand (2013: \$5,374 thousand). As at 31 March 2014, PNBIL had total assets of \$1,902,658 thousand (2013: \$1,517,429 thousand).

During the year, total lending has increased to \$1,486,270 thousand (2013: \$1,136,138 thousand), led by increase in lending against SBLCs, against own deposits and UK commercial property. The growth in investment portfolio during the year was from \$214,588 thousand to \$235,560 thousand. Cash ISA scheme launched last year has gained popularity, the amount mobilised under this scheme is \$30,190 thousand (2013: \$1,158 thousand).

As at 31 March 2014, the main industry concentration within the Bank's loans and receivable portfolio related to loans against SBLCs and LCs of Banks (19%), UK real estate activities (16%), loans against own deposits/ deposits held with Parent (11%), mining of coal and other material (3%) and iron and steel (3%). There are no significant exposures in any other individual industry. The geographical concentration of the bank's exposure (gross assets) to various counterparties is mainly in UK (45%) and India (38%), based on risk origination basis.



**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

The Bank does not have any sovereign exposures in the Euro zone and has limited overall direct exposure in the affected geographies within Euro Zone (including Greece, Ireland, Italy, Portugal, Spain and Cyprus). Bank continues to closely monitor its exposure to such countries by keeping them under close monitoring and having regular review. Bank does not have any direct or indirect exposure in Ukraine and Russia.

Impairment under loans during the year has increased as compared to the previous year. The amount of impaired loans and advances increased to 66,793 thousand (2013: 33,747 thousand), provisions against impairment for loans increased to \$31,244 thousand (2013: \$19,079 thousand). Collective impairment provision on loans increased to \$3,508 thousand (2013: \$493 thousand). There was reduction in provision on non-performing HTM investments by \$1,069 thousand (2013: Nil).

**GOING CONCERN BASIS**

The Bank has adequate resources to continue its operations in the foreseeable future, is profitable for the year ended 31 March 2014; and has a positive net worth position. The Bank has received sufficient support from the parent in the form of capital and operational support from time to time and the same is expected to continue in the foreseeable future. UK operations remain a core part of the strategic interest of the Group. Similarly, it has maintained a stable liquidity position. Adequacy of liquidity is being ensured on a stand-alone basis, and liquidity coverage ratio and also the net stable funding ratio of the bank remain well above the regulatory minimum levels. The Bank has a strong capital position including a positive contribution to capital by way of retained earnings during the financial year, along with fresh capital injection during the year, as discussed in the 'capital structure' section. Accordingly, the directors continue to adopt the going concern basis in preparing the annual report and accounts.

**CAPITAL STRUCTURE**

The capital structure of PNBIL consists of equity attributable to equity holders comprising issued capital, subordinated debt, reserves and retained earnings. Upon migration to the Basel III norms, even though the total capital requirement has gone up and available capital reduced on account of material holdings and appropriation of fair value reserve, Bank is still able to meet the Capital Requirement.

The Capital to Risk Adequacy Ratio (CRAR) of the Bank continues to remain well above that required under the Capital Requirement Regulations (CRR) and also above that required under Individual Capital Guidance (ICG) given by the regulator to the Bank. CRAR as per CRR as on 31 March 2014 is 15.54% with Core Tier I capital ratio being 10.45%. Leverage ratio of the Bank is 8.69%. Components of regulatory capital and assessment of capital adequacy as also the leverage ratio have been given in the Pillar III disclosure, being published at the website of the Bank.

PNBIL's Risk Management Committee (RMC) as well as the Board reviews the capital structure on a quarterly basis. Throughout the year the Bank reviews the need for the injection of capital and funding to ensure on-going stability and support of its business activities. PNBIL has a regulatory capital base of \$252,637 thousand comprising share capital of \$149,631 thousand, tier II capital of \$80,000 thousand, retained earnings of \$19,700 thousand and net of regulatory adjustments. This is as against the Individual Capital Guidance by UK regulator for \$224,756 thousand.

During the year ended 31 March 2014, equity share capital of \$50,000 thousand was raised from the parent company, Punjab National Bank, in order to augment the core tier I capital ratio and to support growth in business.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

Upper Tier II Capital of \$25,000 thousand was raised in the year 2011 by issuing perpetual notes to the parent company – Punjab National Bank. This amount is included under equity in the financial statements (see note 28). Under the new Capital Requirement Regulations under CRD IV, this now qualifies as tier II capital at a level similar to the lower tier II capital.

During the year ended 31 March 2014, tier II capital of \$5,000 thousand was raised by way of subordinated redeemable bonds issued to an Indian Bank other than the Parent. Total amount of lower tier II capital is now \$55,000 thousand by way of subordinated redeemable bonds. This amount is shown in the financial statements as a financial liability (see note 26); and qualifies as Tier II capital for regulatory capital purposes. Further details of the Bank's regulatory capital ratios required under Basel III/ CRDIV are published on the Bank's website, in the form of Pillar III disclosures. Other disclosures in terms of Capital Requirement Regulations and Directives are also included in the Pillar III disclosures being placed on the website of the Bank.

### **PRINCIPAL RISKS AND UNCERTAINTIES**

Key risk for the Bank is credit risk on the loan portfolio, interest rate risk in banking book and operational risk. These risks as well as the mitigation techniques followed by the Bank are discussed at note 33 to the financial statements. The Bank has established appropriate mechanism to measure, monitor and manage these risks on on-going basis. The Board of the Bank has stipulated threshold risk limits for each of these major risks.

The Company is firmly committed to the management of risk, recognising that sound internal risk management is essential to its prudent operation, particularly with the growing complexity, diversity and volatility of markets, facilitated by rapid advances in technology and communications. Risk management is given high priority throughout the Company and is integral to the management of the business.

Responsibility for risk management policies and limits, in the level of risks assumed, lies with the Board of Directors. The Board challenges management for developing, presenting, updating and implementing these policies, controls and limits. The structure is designed to provide assurance that no single event, or combination of events, will materially affect the well-being of the Company. The Company's Board of Directors, Audit Committee and Asset and Liability Committee assist in assessing market trends, economic and political developments, and providing global strategic direction for all aspects of risk management. Additionally, the Risk Committee of the board provides a forum for in-depth review and analysis of the risks to which the Company is subject.

Active, hands-on senior management plays a key role in the identification, evaluation and management of all risks. All credit and new product decisions require direct senior management approval and the loan portfolio is continuously reviewed. Management is supported by a comprehensive structure of independent controls, analysis and reporting processes and periodic review by the Parent.

The Company has in place an extensive number of limit controls and management information systems to facilitate effective management overview. All limits are approved by the Board of Directors and reviewed at least annually. Limit compliance reports are submitted to the Audit Committee.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

The Bank's strategies and policies regarding financial risk management, including the use of financial instruments, the policy for hedging, and an indication of the exposure to financial risk is provided at note 33 to the financial statements. It also includes Bank's processes for managing its capital; its financial risk management strategy; details of its financial instruments and hedging activities; and exposure to credit, market, liquidity and other risks. Some of the issues concerning credit risk have been discussed at note 18 also.

**MARKET UNCERTAINTY**

The recent period has seen a number of developments in emerging market economies including as a consequence of idiosyncratic events. There has been a recent rise in geopolitical risks, notably involving Russia and Ukraine. Vulnerability of borrowers and financial institutions to sharp upward movements in the long term interest rates and credit spreads continues to take attention of the regulators. Risks to activity associated with very low inflation in advanced economies, especially the euro area, have come to the fore.

In emerging market economies, increased financial market and capital flow volatility remain a concern given that the Fed will continue tapering through the year 2014. The responses to the related December announcement have been relatively muted in most economies, possibly helped by the Fed's policy communication and re-calibration (including revisions to forward guidance). Nevertheless, portfolio shifts and some capital outflows are likely with Fed tapering. When combined with domestic weaknesses, the result could be sharper capital outflows and exchange rate adjustments.

**OUTLOOK**

Global activity strengthened during the second half of 2013 and is expected to improve further in 2014–15, largely on account of recovery in the advanced economies. Global growth is now projected to be slightly higher in 2014, at around 3.7 percent, rising to 3.9 percent in 2015, as per outlook forecast by IMF. Activity in the United Kingdom has been buoyed by easier credit conditions and increased confidence. Growth is expected to average 2¼ percent in 2014–15, but economic slack will remain high. Overall, growth in emerging market and developing economies is expected to increase to 5.1 percent in 2014 and to 5.4 percent in 2015. Growth in India picked up after a favourable monsoon season and higher export growth and is expected to firm further on stronger structural policies supporting investment. Outcome of general elections in India will determine the next stage of economic reforms that are vital for returning economic growth to its potential of around 8 percent. A strong mandate for a stable government, even if it is a coalition, will be key to pushing through wide ranging required reforms. Many other emerging market and developing economies have started to benefit from stronger external demand in advanced economies and China.

**REGULATORY FACTORS**

On 19 December 2013, the PRA published its rules and supervisory statements which complement the EU legislative package known as "CRD IV", covering prudential rules for banks, building societies and investment firms. The EU text was formally published in the Official Journal of the EU on Thursday 27 June 2013 with a subsequent corrigendum. The bulk of the rules contained in the legislation have taken effect from 1 January 2014.

# **PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**

## **STRATEGIC REPORT**

### **FOR THE YEAR ENDED 31 MARCH 2014**

---

CRD IV is made up of the Capital Requirements Regulation (CRR), which is directly applicable on firms across the EU, and the Capital Requirements Directive (CRD), which is being implemented through national law and final rules for the same have already been issued. The PRA, on 29 November, issued a public statement on the make-up of Common Equity Tier 1 (CET1) capital which firms will need to hold.

CRD IV is intended to implement the Basel III agreement in the EU. This includes enhanced requirements for quality and quantity of capital, a basis for new liquidity and leverage requirements, new rules for counterparty risk, and new macro- prudential standards including a countercyclical capital buffer and capital buffers for systemically important institutions. CRD IV also makes changes to rules on corporate governance, including remuneration, and introduces standardized EU regulatory reporting - referred to as COREP and FINREP. These reporting requirements will specify the information firms must report to supervisors in areas such as own funds, large exposures and financial information.

The Banking Reform Act received Royal Assent in December 2013. It will bring into law structural and cultural changes to the banking system, by:

- introducing a 'ring-fence' around the deposits of people and small businesses, to separate the high street from the trading floor and protect taxpayers when things go wrong
- making sure the new Prudential Regulation Authority can hold banks to account for the way they separate their retail and investment activities, giving it powers to enforce the full separation of individual banks
- imposing higher standards of conduct on the banking industry by introducing a criminal sanction for misconduct that leads to bank failure
- giving depositors, protected under the Financial Services Compensation Scheme, preference if a bank enters insolvency
- giving the government power to ensure that banks are more able to absorb losses
- introducing a cap on payday loans

PRA has started consultation on supervision of International Banks. While significant changes are proposed in respect of supervisory tools for branches of International Banks in UK, no major change is proposed for UK incorporated subsidiaries.

The European Central Bank (ECB) is preparing to take on new banking supervision tasks as part of a Single Supervisory Mechanism (SSM). The Single Supervisory Mechanism will create a new system of financial supervision comprising the ECB and the national competent authorities of participating EU countries. Among these EU countries are those whose currency is the euro and those whose currency is not the euro but who have decided to enter into close cooperation with the Single Supervisory Mechanism. The main aims of the SSM will be to ensure the safety and soundness of the European banking system and to increase financial integration and stability in Europe.

European Market Infrastructure Regulation (EMIR) came into effect on 15 March 2014. The main obligations under EMIR are Central Clearing for certain classes of OTC derivatives; application of risk mitigation techniques for non-centrally cleared OTC derivatives; reporting to trade repositories; and application of organizational, conduct of business and prudential requirements for CCPs. Besides, enhanced regulatory powers have been given to European Securities and Markets Authority (ESMA)

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

making it responsible for monitoring systemic risks in the European markets, including derivative markets.

**IMPACT OF MARKET FACTORS ON BANK**

Reduced economic growth in India, high volatility in exchange rates of USD and GBP to INR and global slowdown were some of the contributing factors towards default of some of the corporates, attracting higher level of impairment provisions. Besides that, our overall performance in 2013-14 was not materially impacted by the prevailing difficult economic conditions.

Our capital, funding and liquidity positions remain a source of stability for us and provide assurance to our customers and clients and support us in meeting future regulatory requirements. Capital adequacy ratio, liquidity coverage ratio and net stable funding ratio of the Bank remained above the minimum regulatory requirements and individual capital and liquidity guidance. Our funding is well diversified, majority of it being long term in nature. Besides, liquidity asset buffer, short term interbank placements and balance with Bank of England are maintained, keeping in view the immediate liquidity requirement, which may be triggered under stressed conditions. A minimum of 90 days survival period is considered for maintenance of the buffer. The Bank's capital to risk adequacy ratio is 15.54%, with core tier I capital ratio being at 10.40% - well above the requirements of CRD IV. Bank has taken steps to further augment its capital base during the coming year so as to support its planned business growth.

While FINREP returns are not presently applicable to the Bank, necessary automation software to implement the COREP reporting guidelines has been put in place. Earlier there was some delay on account of acquisition of our software vendor company by another company and impending delays in due diligence, actual take over, novation of contracts and development and installation of bridge between the software of the two companies. Mapping is being done and Bank is committed to follow all timelines in this regard. Postponement of first reporting to end June 2014 has further given time for trials and testing.

The ring-fencing proposals are not expected to have any material effect on the operations and business model of the Bank. However, we will continue to assess the impact as we model our growth plans.

Implementation of Dodd-Frank Act may have effect on proprietary trading of the Banks. Keeping in view our profile of treasury operations, its impact on the Bank may be negligible. Necessary actions will be initiated as the guidelines become clear.

The Bank maintains a pro-active stance to regulation taking a serious approach to ensuring compliance with the resulting legislation and regulation.

*Regulatory timeline*

H1 2014	Implementation of RWA calculations under Basel 3 (CRD4)
H1 2014	Implementation of CRD4 and CRR
H1 2014	Implementation of COREP reporting
H2 2014	Implementation of FINREP reporting
H2 2014	Implementation of Asset Encumbrance reporting and new disclosures

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STRATEGIC REPORT**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

2014 – 2015	Expected enactment/adoption of uniform guidelines on Non-Performing Loans and Forbearance guidelines by European Parliament/ Commission.
2014 – 2018	Phasing in of capital deductions under Basel 3 (CRD4)
2019	Implementation of Banking Reforms Act
2022	Full compliance with US Dodd-Frank Act

### **FUTURE STRATEGY**

The Bank proposes to re-launch on-line remittance product after obtaining regulatory approval for the same. Existing Maestro debit cards will be replaced with the new contactless MasterCard debit cards. Cash ISA scheme will be further popularised. Pension scheme for employees under auto enrolment scheme will be implemented. As a part of its expansion strategy in Europe, the Bank will explore the possibility of establishing an office in one of the European countries.

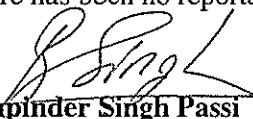
Given the economic environment, Bank plans to have cautious and controlled growth, particularly in new lending activities; and the Bank will continue to focus and enhance its credit risk framework to make it more robust. Risk rating modules will be updated based on past experience. Well capitalized, highly liquid and diverse balance sheet and disciplined growth will be the core objectives for the year.

### **CHARITABLE DONATIONS**

Charitable donations in the sum of \$7,974 were made during the year (2013: \$13,304).

### **EVENTS AFTER THE BALANCE SHEET DATE**

There has been no reportable event after the balance sheet date.



**Bhupinder Singh Passi**  
Secretary

**Company number: 5781326**

1, Moorgate, London  
EC2R 6JH (UK)

30 April 2014

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF DIRECTORS' RESPONSIBILITIES IN RESPECT OF THE DIRECTORS'**  
**REPORT, STRATEGIC REPORT AND THE FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

The directors are responsible for preparing the directors' report, strategic report and the financial statements in accordance with applicable laws and regulations.

Company law requires the directors to prepare the financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with IFRSs as adopted by the EU and applicable law.

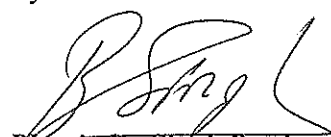
Under company law the directors must not approve the accounts unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the company and to prevent and detect fraud and irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By Order of the Board



***Bhupinder Singh Passi***  
Managing Director



***Muddoor Sadananda Nayak***  
Executive Director

30 April 2014



## **Independent auditor's report to the shareholders of Punjab National Bank (International) Limited**

---

We have audited the financial statements of Punjab National Bank (International) Limited (the 'Bank') for the year ended 31 March 2014 set out on pages 17 - 68. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

This report is made solely to the Bank's shareholders, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Bank's shareholders those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report or for the opinions we have formed.

### **Respective responsibilities of Directors and Auditor**

As explained more fully in the Statement of Directors' Responsibilities (set out on page 14), the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

### **Scope of the audit of the financial statements**

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at [www.frc.org.uk/auditscopeukprivate](http://www.frc.org.uk/auditscopeukprivate).

### **Opinion on the financial statements**

In our opinion the financial statements:

- give a true and fair view of the state of the Bank's affairs as at 31 March 2014 and of the profit for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion the information given in the Directors' Report and Strategic Report for the financial year for which the financial statements are prepared is consistent with the financial statements.





**Independent auditor's report to the shareholders of Punjab National Bank  
(International) Limited (continued)**

---

**Matters on which we are required to report by exception**

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

- adequate accounting records have not been kept by the Bank, or returns adequate for our audit have not been received from branches not visited by us; or
- the Bank's financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

A handwritten signature in black ink, appearing to read 'Suvro Dutta'.

Suvro Dutta  
(Senior Statutory Auditor)

for and on behalf of KPMG Audit Plc, Statutory Auditor  
Chartered Accountants

15 Canada Square  
London  
E14 5GL

30 April 2014

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF FINANCIAL POSITION**  
**FOR THE YEAR ENDED 31 MARCH**

	Notes	2014 \$'000	2013 \$'000
<b>Assets</b>			
Cash and cash equivalents	9	194,555	133,331
Investment securities – held for trading	10	62,113	119,857
Derivative financial instruments	11	1,973	1,169
Loans and advances to banks	12	299,720	274,216
Loans and advances to customers	13	1,170,545	895,209
Investment securities - available for sale	14	166,328	85,171
Investment securities – held to maturity	15	4,839	6,210
Property, plant and equipment	20	1,472	1,727
Intangible assets	21	168	192
Deferred tax assets	22	20	49
Prepayments and other receivables	23	925	298
<b>Total assets</b>		<b>1,902,658</b>	<b>1,517,429</b>
<b>Liabilities</b>			
Derivative financial instruments	11	202	5,836
Deposits from banks	24	280,764	115,808
Deposits from customers	25	1,361,155	1,194,617
Current tax liabilities		(254)	1,085
Subordinated liabilities and other borrowed funds	26	55,000	50,000
Other liabilities	27	11,460	6,500
<b>Total liabilities</b>		<b>1,708,327</b>	<b>1,373,846</b>
<b>Equity</b>			
Share capital	28	174,631	124,631
Retained earnings		24,706	18,827
Fair value reserve	29	(5,006)	125
<b>Total parent company shareholders' equity</b>		<b>194,331</b>	<b>143,583</b>
<b>Total equity and liabilities</b>		<b>1,902,658</b>	<b>1,517,429</b>

The financial statements were approved by the Board of Directors and authorised for issue on 30 April 2014.

M S NAYAK  
 Director

BHUPINDER SINGH PASSI  
 Managing Director

DAVID HOPTON  
 Director

M G McCAIG  
 Director

Company Registration No 5781326

The notes on pages 23 to 68 form part of these financial statements

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF PROFIT OR LOSS**  
**FOR THE YEAR ENDED 31 MARCH**

	Notes	2014 \$'000	2013 \$'000
Interest income	5	81,576	70,132
Interest expense	5	(42,537)	(39,334)
Net interest income		39,039	30,798
Net trading (loss)/income	5	(1,549)	873
Income on interest rate derivatives		467	-
Net fee and commission income	5	383	570
Other operating income	5	519	941
Operating income		38,859	33,182
Staff related costs	6	(6,920)	(5,651)
Operating lease expenses	5	(654)	(693)
Depreciation and amortisation	5	(771)	(788)
General administrative expenses	5	(6,643)	(4,947)
Provision on impaired financial assets	17	(15,238)	(14,125)
<b>Profit before tax</b>		<b>8,633</b>	<b>6,978</b>
Income tax expense	8	(1,643)	(1,604)
<b>Profit after tax</b>		<b>6,990</b>	<b>5,374</b>

The notes on pages 23 to 68 form part of these financial statements

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF COMPREHENSIVE INCOME**  
**FOR THE YEAR ENDED 31 MARCH**

	2014	2013
	\$'000	\$'000
<b>Profit for the year</b>	<b>6,990</b>	<b>5,374</b>
<b>Other comprehensive income</b>		
Items that are or may be reclassified to profit or loss		
Net change in fair value on AFS investments	(6,280)	524
Tax relating to fair value change on AFS investments	1,444	(126)
	(4,836)	398
Net amount transferred to profit and loss (AFS investments)	(295)	3,080
Other comprehensive income for the year	(5,131)	3,478
<b>Total comprehensive income attributable to equity shareholders</b>	<b>1,859</b>	<b>8,852</b>

The notes on pages 23 to 68 form part of these financial statements

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED 31 MARCH**

31 March 2014	Attributable to equity holders of the Bank			
	Issued capital	Fair value reserves	Retained earnings	Total equity
	\$'000	\$'000	\$'000	\$'000
Balance at 1 April 2013	<u>124,631</u>	<u>125</u>	<u>18,827</u>	<u>143,583</u>
<b>Total comprehensive income for the year</b>				
Profit for the year	-	-	6,990	6,990
<b>Other comprehensive income for the year</b>				
Net change in fair value of AFS investments	-	(4,836)	-	(4,836)
Net amount transferred to profit and loss	-	(295)	-	(295)
<b>Total other comprehensive income for the year</b>	-	(5,131)	-	(5,131)
<b>Total comprehensive income for the year</b>	-	(5,131)	6,990	1,859
<b>Transactions with owners recorded directly in equity</b>				
<b>Contributions by and distribution to owners of the group</b>				
Issue of Share Capital <sup>#</sup>	50,000	-	-	50,000
Dividend on Perpetual Tier II Capital	-	-	(1,111)	(1,111)
Total contributions by and distributions to owners	<u>50,000</u>	-	<u>(1,111)</u>	<u>48,889</u>
Balance at 31 March 2014	<u>174,631</u>	<u>(5,006)</u>	<u>24,706</u>	<u>194,331</u>

<sup>#</sup> Equity capital by way of issuance of shares (see note 28).

The notes on pages 23 to 68 form part of these financial statements

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF CHANGES IN EQUITY**  
**FOR THE YEAR ENDED 31 MARCH**

31 March 2013	Attributable to equity holders of the Bank			
	Issued capital	Fair value reserves	Retained earnings	Total equity
	\$'000	\$'000	\$'000	\$'000
Balance at 1 April 2012	112,131	(3,353)	14,621	123,399
<b>Total comprehensive income for the year</b>				
Profit for the year	-	-	5,374	5,374
<b>Other comprehensive income for the year</b>				
Net change in fair value of AFS investments	-	398	-	398
Net amount transferred to profit and loss	-	3,080	-	3,080
<b>Total other comprehensive income for the year</b>	-	3,478	-	3,478
<b>Total comprehensive income for the year</b>	-	3,478	5,374	8,852
<b>Transactions with owners recorded directly in equity</b>				
<b>Contributions by and distribution to owners of the group</b>				
Issue of Share Capital <sup>#</sup>	12,500	-	-	12,500
Dividend on Perpetual Tier II Capital	-	-	(1,168)	(1,168)
Total contributions by and distributions to owners	12,500	-	(1,168)	11,332
Balance at 31 March 2013	124,631	125	18,827	143,583

<sup>#</sup> Equity capital by way of issuance of shares (see note 28).

The notes on pages 23 to 68 form part of these financial statements

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**STATEMENT OF CASH FLOWS**  
**FOR THE YEAR ENDED 31 MARCH**

	2014	2013
	\$'000	\$'000
<b>Cash flows from operating activities</b>		
Total Profit for the year	6,990	5,374
<b>Adjustments for:</b>		
Amortisation of other intangible non-current assets	128	146
Depreciation of property, plant and equipment	643	642
Provision for impairment losses on financial assets	14,468	14,125
Unrealised (profit)/ losses on exchange rate difference	11	(131)
Income tax expense	1,643	1,604
	<u>16,893</u>	<u>16,386</u>
	23,883	21,760
<b>Changes in:</b>		
Held for trading financial assets	57,743	(119,857)
Loans and advances to customers	(290,516)	(241,431)
Deposits from banks	164,955	(51,828)
Other liabilities and provisions	4,925	(35)
Available for sale financial assets	(88,177)	13,031
Fair value of derivatives	(6,438)	7,483
Loans and advances to banks	(25,504)	72,594
Trade and other receivables	(626)	223
Deposits from customers	166,538	333,176
Debt securities	34	67
	<u>(17,066)</u>	<u>13,423</u>
<b>Cash flows from operating activities</b>	6,817	35,183
<b>Cash flows used in other operating activities</b>		
Income taxes paid (net)	(1,431)	(2,223)
<b>Net cash flows from operating activities</b>	5,386	32,960
<b>Cash flows from investing activities</b>		
Acquisition of property and equipment	(388)	(1,355)
Acquisition of intangible assets	(104)	(68)
Acquisition of held to maturity investments	-	-
Proceeds from maturity of held to maturity investments	2,441	14,054
<b>Net cash flows from investing activities</b>	1,949	12,631
<b>Cash flows from financing activities</b>		
Gross proceeds from issue of equity share capital	50,000	12,500
Gross proceeds from issue of subordinated liabilities	5,000	12,500
Dividend to subordinated debt holders	(1,111)	(1,168)
<b>Net cash flows from financing activities</b>	53,889	23,832
<b>Net increase in cash and cash equivalents</b>	61,224	69,423
Cash and Cash equivalents at 1 April	133,331	63,908
<b>Cash and cash equivalents at 31 March (note 9)</b>	<u>194,555</u>	<u>133,331</u>

The notes on pages 23 to 68 form part of these financial statements

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

**1] Reporting Entity**

Punjab National Bank (International) Limited is a limited company incorporated and domiciled in the United Kingdom. The Bank is a fully owned subsidiary of Punjab National Bank, one of the leading public sector banks of India. Address of the Bank's registered office is 1, Moorgate, London (UK) EC2R 6JH. The Bank is primarily involved in corporate and retail lending and other banking activities.

**2] Basis of Preparation**

**A. Statement of Compliance**

The Bank's financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs) as endorsed by the European Union and as applied in accordance with the provisions of the Companies Act 2006. The principal accounting policies adopted by the Bank are set out in note 3.

The Bank's financial statements for the year ended 31 March 2014 were authorised for issue on 30 April 2014.

**B. Basis of Measurement**

The financial statements have been prepared on the historical cost basis except for the following material items in the statement of financial position:

- derivative financial instruments are measured at fair value.
- financial instruments at fair value through profit or loss are measured at fair value; and
- available for sale financial assets are measured at fair value.

**C. Going Concern**

The financial statements are prepared on a going concern basis as the Directors are satisfied that the Bank has the resources to continue in business for the foreseeable future.

The Bank is a wholly owned subsidiary of Punjab National Bank. The Bank continues to be profitable, generating profit before tax of \$8,633 thousand in 2013-14 resulting in an increase in retained earnings and reserves of \$748 thousand after making provision for tax and dividend and other fair value reserve movement. During the current year, the Bank has raised additional equity share capital of \$50.00 million, subscribed 100% by the Parent which demonstrates ongoing parental support. Besides, the Bank has also raised additional tier II capital of \$5.00 million. This amount had been raised by the issue of fifteen years Subordinated Notes (callable after ten years) to another Bank of Indian origin. Accordingly the capital base is \$252,637 thousand as against Individual Capital Guidance by UK regulator for \$224,756 thousand.

After considering the above factors, the Directors continue to adopt the going concern basis in preparing the financial statements.



**D. Functional and Presentation Currency**

The Directors consider the US Dollar as the functional and reporting currency as the majority of the income generating financial assets and a significant component of the funding are denominated in US Dollar. Additionally 99.99% of equity capital and 100% of the Tier II capital of the Bank is denominated in US dollar. Transactions in foreign currencies are recorded in US Dollars at the rate of exchange prevailing at the rates ruling at the end of the day in which the transaction arose. Any resulting exchange differences are included in the statement of profit or loss. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange at the balance sheet date. All amounts have been rounded to the nearest thousands, except when otherwise indicated.

**D. Use of Estimates and Judgements**

The preparation of the financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of allowances required for impaired loans and receivables as well as allowances for impairment provision for available-for-sale investment securities. Estimates and judgments are continually evaluated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

Further information about key assumptions concerning the future, and other key sources of estimation and judgement, are set out in the relevant disclosure notes for the following areas:

• **Identification of impairment of financial assets**

The Bank assesses at each balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are provided for if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The Bank considers the following factors in assessing objective evidence of impairment:

- when the counterparty is in default of principal or interest payments;
- when a counterparty files for bankruptcy protection (or the local equivalent) and this would avoid or delay discharge of its obligation;
- where the Bank files to have the counterparty declared bankrupt or files a similar order in respect of a credit obligation;
- where the Bank consents to a restructuring of the obligation, resulting in a diminished financial obligation, demonstrated by a material forgiveness of debt or postponement of scheduled payments; or
- where there is observable data indicating that there is a measurable decrease in the estimated future cash flows of a group of financial assets.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

- **Allowances for impairment of loans and receivables**

The Bank periodically reviews their financial assets carried at amortised cost to identify any early signs of financial deterioration. Additionally, for those loans where there is either a default or an objective evidence of impairment, judgement is required by management in the estimation of the amount and timing of expected cash flows, realisability and valuation of collateral and in certain cases the availability and reliance on guarantees (including corporate and personal guarantees and critical assessment of willingness and ability of the guarantors) in order to determine the level of impairment allowance to be recorded. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance. Management's estimates of future cash flows on individually impaired loans are based on historical experience for assets with similar credit risk characteristics. The expected recovery is subject to execution risks associated with the recovery of collateral in different jurisdictions; and fair assessment is thus derived from management's experience of such markets.

In addition to specific allowances against individually significant loans and advances, the Bank also makes a collective impairment allowance against performing loans which represents an interim step pending the identification of impairment losses on individual assets in the group of financial assets that are collectively assessed for impairment. This takes into consideration factors such as the risk rating of the counterparty, the probability of default, the loss given default, recent loss history and the emergence period. The Bank considers an emergence period of 3 months to be appropriate based on the nature of the counterparties, frequency of the review of loan portfolio done by the management and past loan loss experience.

A change of one month in emergence period will result in an impact of \$ 830 thousand (2013: \$ 164 thousand) on the value of the impairment provision.

- **Impairment Losses on available for sale investments**

At each balance sheet date, the Bank assesses whether there is objective evidence that an available for sale asset is impaired. In case of securities in this category, where there has been significant decline in value; and due to deterioration of credit ratings which has an impact on the Bank's estimated future cash flows of the investments, management applies judgement after considering other underlying circumstances to assess if an allowance for impairment is required. These factors include the collateral structure, market insight, the length of time over which the decline has been observed and the current and expected financial performance of the counterparty.

- **Held-to-maturity investment securities**

The Bank follows the guidance of IAS 39 in classifying certain non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. In making this judgment, the Bank evaluates its intention and ability to hold such investment securities to maturity. In the event the Bank fails to keep these investments to maturity other than for specific circumstances, it will be required to reclassify the entire class as available-for-sale and the Bank will be prevented from classifying investment securities as held-to-maturity for the current and the following two financial years.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

• **Fair value measurement of financial instruments**

When available, Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis. If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

**E. Standards and Interpretations**

**a) Standards and Interpretations effective in the Current Year**

The following new and revised Standards and Interpretations have been adopted in the current year. Their adoption has not had any significant impact on the amounts reported and disclosures in these financial statements but may impact the accounting for future transactions and arrangements.

- Amendments to IAS 1 (revised June 2011) Presentation of Items of Other Comprehensive Income
- IAS 19 (revised June 2011) Employee Benefits
- Amendments to IAS 28 (May 2011) Investments in Associates and Joint Ventures
- Amendments to IAS 32 (December 2011) Financial Instruments Presentation – Amendments to Application Guidance on the Offsetting of Financial Assets and Financial Liabilities
- IFRS 7 Disclosures - Offsetting Financial Assets and Financial Liabilities (2011)
- IFRS 12 Disclosure of Interests in Other Entities
- IFRS 13 Fair Value Measurements
- Recoverable Amount Disclosure for Non-Financial Assets (Amendment to IAS 36) (2013)
- Novation of Derivatives and Continuation of Hedge Accounting (Amendments to IAS 39)
- Annual improvements to IFRS 2009 – 2011 cycle.

**b) Standards and Interpretations issued but not yet effective**

The Bank is not required to adopt the following Standards and Interpretations which are issued by IASB but not yet effective (and in some cases have not yet been endorsed by the EU):

- Investment entities (Amendments to IFRS 10, IFRS 12 and IAS 27 – not yet endorsed by EU)
- IFRS 9 Financial Instruments – Classification and Measurement of Financial assets and – Accounting for Financial Liabilities and De-recognition (not yet endorsed by EU)
- IFRS 10 Consolidated Financial Statements
- IFRIC 21 Levies
- IAS 27 - Separate Financial Statements – applies to annual periods beginning on or after 01 January 2014 (EU effective date)
- IFRS 11 Joint Arrangements
- Annual improvements to IFRSs 2010-2012 cycle.

The Bank is currently evaluating the impact of the above and other new standards, amendments to standards, revisions and interpretations.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

3] **Accounting policies**

**a) Revenue recognition**

**Interest**

Interest income and expense are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts 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. When calculating the effective interest rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses. Interest income and expense presented in the statement of profit or loss includes:

- Interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis;
- Interest on available-for-sale investment securities calculated on an effective interest basis.

**Fees and commission**

Fees and commissions including account servicing fees, remittance charges and bills collection charges are recognised on an accrual basis when the service has been provided or the significant act of delivering the services contracted by the customer has been performed.

Other fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

**Net trading income**

Net trading income comprises gains less loss related to trading assets and liabilities, and includes all realised and unrealised fair value changes and foreign exchange differences.

**b) Measurement**

**Financial assets**

The Bank classifies its financial assets in the following categories: financial assets at fair value through the statement of profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets.

**i. Financial assets at fair value through profit and loss**

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit and loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management if it meets the criteria as defined in IAS 39. Financial assets held for trading are initially recognised and measured at fair value in the statement of financial position. All changes in fair value are recognised as part of trading income in profit and loss. For a purchase transaction, from trade date until settlement date, the asset remains an off balance sheet asset and it is recognised on financial statements on the settlement date. For a sale transaction, asset continues to be on financial statements until settlement date and the transaction remains an off balance sheet commitment until then.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

**ii. Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Bank provides money or services to a debtor with no intention of trading the receivable. Loans and receivables are initially measured at fair value plus any attributable transaction costs; and subsequently measured at amortised cost using the effective interest method less any specific impairment.

**iii. Held-to-maturity**

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity.

All investments are initially recorded at cost, being the fair value of the consideration given and including acquisition charges associated with the investment.

After initial recognition, investments which are classified as held to maturity are carried at amortised cost less impairment if any.

**iv. Available for sale**

Available for sale investments are non-derivative investments that are designated as available for sale or are not classified as another category of financial assets. Available for sale investments comprise debt securities.

Interest income is recognised in profit or loss using the effective interest method. Foreign exchange gain or losses on available-for-sale debt security investments are recognised in profit or loss. Impairment losses are recognised in profit or loss.

Other fair value changes, other than impairment losses, are recognised as other comprehensive income and presented in the fair value reserve in equity. When the investment is sold, the gain or loss accumulated in equity is re-classified to profit or loss.

**Financial liabilities and equity instruments**

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into.

**i. Equity instruments**

An equity instrument is any contract that evidences a residual interest in the assets of the Bank after deducting all liabilities. Equity instruments issued by the Bank are recorded at the proceeds received, net of direct costs.

**ii. Financial liabilities**

All non-derivative financial liabilities (including deposits from customers/ Banks and subordinated liabilities) are initially measured at fair value, net of transaction costs. Financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

**iii. Deferred Income**

The arrangement fee received on long term loans is amortised during the tenure of the loan, the un-amortised amount is recognised as deferred income in the financial statements.

**c) Fair value measurement**

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or in the absence of the most advantageous market to which the Bank has access at that date.

When available, the Bank measures the fair value of an instrument using quoted price in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active, the Bank establishes fair value using another valuation technique. For derivatives, the valuation technique chosen makes maximum use of market inputs, relies as little as possible on estimates specific to the Bank, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk – return factors inherent in the financial instrument. The Bank calibrates valuation techniques and tests them for validity using prices from observable market transactions.

The best evidence of the fair value of a financial instrument at initial recognition is the transaction price – i.e. the fair value of the consideration given or received. However, in some cases, the fair value of a financial instrument on initial recognition may be different to its transaction price. If such fair value is evidenced by comparison with other observable current market transactions in the same instrument (without modification or repackaging) or based on a valuation technique whose valuables include only data from the observable markets, then the difference is recognised in profit or loss on initial recognition of the instrument.

**d) Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount reported in the balance sheet 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.

**e) De-recognition of financial assets and liabilities**

Financial assets are de-recognised when the rights to receive cash flows from the assets have expired; or where the Bank has transferred its contractual right to receive the cash flows of the financial assets and either:

- i. substantially all the risks and rewards of ownership have been transferred; or
- ii. substantially all of the risks and rewards of ownership have neither been transferred nor been retained and the Bank has not retained control of the financial assets.

Financial liabilities are de-recognised when they are extinguished, i.e. when the obligation is discharged or cancelled or expired.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

**f) Transfer of financial assets**

Bank enters into transactions involving sale and repurchase of securities resulting in the transfer of financial assets, primarily debt securities. Sale and repurchase agreements are transactions in which Bank sells a security and simultaneously agrees to repurchase it at a fixed price at a future date. Bank continues to recognise the securities in their entirety in the statement of financial position because it retains substantially all of the risks and rewards of ownership. Financial liability is recognised for the obligation to pay the repurchase price. Because the Bank sells the contractual rights to the cash flows of the securities, it does not have the ability to use the transferred assets during the term of arrangement.

**g) Impairment of financial assets**

**i) Assets carried at amortised cost**

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the asset's original effective rate. If in a subsequent period, the amount of an impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed to the extent that it is now excessive by reducing the loan impairment allowance account. The amount of any reversal is recognised in the statement of profit or loss.

**ii) Available for Sale Assets**

The Bank assesses at each Balance Sheet date whether there is objective evidence that an available for sale asset is impaired. Objective evidence that a financial asset is impaired includes observable data that come to the attention of the Bank such as a significant change in price in excess of 20 percent or prolonged decline over nine months; and due to deterioration of credit ratings which has an impact on the Bank's estimated future cash flows of the financial assets.

If an impairment loss has been incurred, the cumulative loss (measured as a difference between the original cost and the fair value) less any impairment loss on that asset previously recognised, is removed from equity and recognised in the statement of profit or loss. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised, the impairment loss is reversed through the statement of profit or loss.

**h) Derivative Financial Instruments**

The Bank enters into derivative financial instruments to manage its exposure to interest rate and foreign exchange rate risk, including exchange forward contracts, interest rate swaps and cross currency swaps. Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently re-measured to their fair value at each balance sheet date. The resulting gain or loss is recognised in profit or loss immediately. A derivative with a positive fair value is recognised as a financial asset whereas a derivative with a negative fair value is recognised as a financial liability.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

**i) Property and equipment**

**(i) Recognition and measurement**

Items of property and equipment are measured at cost less accumulated depreciation. Cost includes expenditure that is directly attributable to the acquisition of the assets. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Any gain or loss on disposal of an item of property and equipment (calculated as the difference between the net proceeds from disposal and carrying amount of the item) is recognised within other income in profit or loss.

**(ii) Subsequent costs**

Subsequent expenditure is capitalised only when it is probable that the future economic benefits of the expenditure will flow to the Bank. On-going repairs and maintenance are expensed as incurred.

**(iii) Depreciation**

Items of property and equipment are depreciated from the date they are available for use. Depreciation is calculated to write off the cost of items of property and equipment using the straight line basis over their useful estimated life. Depreciation is recognised in the statement of profit or loss. The estimated useful lives for the current and comparative periods of significant items of property and equipment are as follows:

Fixtures including computers and accessories	3-5 years
Leasehold improvements	5 years or primary period of lease term, whichever is lower.

**j) Intangible assets**

Intangible assets of the Bank include software and the same is measured at cost less accumulated amortisation and any impairment in value.

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

Software is amortised on a straight line basis in profit or loss over its estimated useful life, from the date that it is available for use. The estimated useful life of software for the current and comparative periods is over three years or the licence term whichever is the lower.

**k) Cash and cash equivalents**

Cash and cash equivalent include notes and coins on hand, balances with Banks and highly liquid financial assets with original maturities of three months or less from the acquisition date that are subject to an insignificant risk of change in their fair value and are used by the Bank in the management of its short term commitments.



**l) Recognition of deferred tax assets**

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date.

**m) Recognition and measurement of provisions and contingencies**

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessment of the time value of money and the risk specific to the liability.

A provision for restructuring is recognised when the Bank has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publically. Future operating losses are not provided for.

**n) De-recognition of financial assets**

Bank enters into sale and repurchase transactions whereby it transfers assets recognised on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not de-recognised.

**o) Share Capital and Reserves**

**(i) Upper tier II bonds**

The Bank classifies capital instruments as equity instruments in accordance with the substance of contractual terms of the instruments. The Bank's perpetual bonds are not redeemable by the holders and bear an entitlement to the distributions that is non-cumulative and at the discretion of the board of directors. Accordingly, they are presented as a component of issued capital within equity. Distributions thereon are generally recognised as dividend out of total comprehensive income attributable to the equity shareholders.

**(ii) Fair Value Reserves**

The fair value reserve comprises the cumulative net change in the fair value of available for sale financial assets until the assets are derecognised or impaired.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

**p) Income tax**

Income tax expense represents the sum of the tax currently payable and deferred income tax.

The tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the statement of profit or loss because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible. The Bank's liability for current tax is calculated using applicable tax rates.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax is calculated at the tax rates that are expected to apply in the period when the asset is realised or the liability is settled. Deferred tax is charged or credited to the statement of profit or loss, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Bank intends to settle its current tax assets and liabilities on a net basis.

**q) Operating lease commitments**

Operating leases payments are recognised as an expense in the statement of profit or loss on a straight-line basis over the lease term.

**r) Employee Benefits**

The Bank has two pay groups of employees in UK – those on secondment to the Bank from the Parent Bank and those who are locally recruited. The employees on secondment are governed by the salary structure approved by the Government of India as well as by the Board of Directors of the Parent Bank. Their salary, perquisites and allowances are fixed accordingly. Salary to the locally recruited staff is as per Board approved Human Resource Policy.

No bonus, overtime or incentive is paid by the Bank to its employees.

The Bank has subscribed to a defined contribution pension plan under which the Bank pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an employee benefit expense in profit or loss in the periods during which

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**AS AT 31 MARCH 2014**

---

**Employee Benefits (continued)**

services are rendered by employees. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in future payments is available.

**4] Operating Segments**

The Bank undertakes the business of commercial banking which is carried on within the United Kingdom. Its activities are currently managed on a centralised business model so the revenue and the costs are not attributable to any one operating or geographic segment.

The Bank has one class of business and all other services are ancillary to this. Its activities are currently managed on a centralized business model. The Chief of Decision Making of the Bank is the Board of Directors. The Board reviews all the information for the business as a whole as these ancillary activities do not have their own standalone reporting environment and protocols internally.

No revenue transaction with a single external customer or counter party amounted to 10% or more of the total revenue for the year.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**5] Operating Profit**

Operating profit is stated after charging the following:

	2014 \$'000	2013 \$'000
Interest expense	<u>42,537</u>	<u>39,334</u>
Depreciation of property and equipment	643	642
Amortisation of intangible assets	<u>128</u>	<u>146</u>
	<u>771</u>	<u>788</u>
Operating leases:		
Lease rental expenses	<u>654</u>	<u>693</u>
Fee payable to the Bank's auditor for the audit of the Bank's annual accounts	<u>240</u>	<u>213</u>
Fee payable to the Bank's auditor for other services:		
- Audit related assurance services	24	29
- Non-audit services	<u>275</u>	<u>144</u>
	<u>299</u>	<u>173</u>

	2014 \$'000	2013 \$'000
<b>Included in net trading income:</b>		
Income/(loss) related to:		
Foreign exchange	2,484	2,181
Investment securities - held for trading	<u>(4,033)</u>	<u>(1,308)</u>
	<u>(1,549)</u>	<u>873</u>

	2014 \$'000	2013 \$'000
<b>Included in operating income:</b>		
Income on services related to:		
Payment and settlement	386	718
Retail banking	120	220
Other operating income	<u>13</u>	<u>3</u>
	<u>519</u>	<u>941</u>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

5] **Operating Profit (continued)**

	2014	2013
	\$'000	\$'000
<b>Included in fee and commission expense:</b>		
ATM/ Kiosk charges	263	153
Brokerage	38	11
	<u>301</u>	<u>164</u>

	2014	2013
	\$'000	\$'000
<b>Included in general administrative expenses:</b>		
Marketing costs	213	234
Establishment expenses	1,014	701
Legal, professional and audit fees	2,519	1,581
Cost on postage, telephones and telegrams	586	377
Other administration costs	2,311	2,054
	<u>6,643</u>	<u>4,947</u>

	2014	2013
	\$'000	\$'000
<b>Included in interest income:</b>		
Interest accrued on overdraft accounts	16,988	16,425
Interest accrued on demand and term loans	48,230	34,960
Discount on bills	142	367
Interest accrued on interbank placements	1,661	3,511
Coupon/premium accrued on investment securities	9,336	10,619
Arrangement fee on loans	5,219	4,250
	<u>81,576</u>	<u>70,132</u>

	2014	2013
	\$'000	\$'000
<b>Included in interest expense:</b>		
Interest expenses on term deposits	36,007	33,688
Interest expenses on saving deposits	219	180
Interest expenses on interbank borrowings	4,023	3,435
Interest expenses on subordinated liabilities	2,288	2,031
	<u>42,537</u>	<u>39,334</u>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**6] Employee Expenses**

	2014	2013
	\$'000	\$'000
Wages and salaries	4,748	3,902
Contribution towards defined employee benefit plan	110	99
Other employee benefits	1,433	1,171
Social security costs	629	479
	<u>6,920</u>	<u>5,651</u>

Included in other employee benefits are:

	2014	2013
	\$'000	\$'000
Accommodation cost	852	668
Medical insurance and expense	127	113
Pension contributions for staff in India	7	7
Other expenses	447	383
	<u>1,433</u>	<u>1,171</u>

There are no share based payments to employees.

**7] Directors' Emoluments**

	2014	2013
	\$'000	\$'000
Emoluments	<u>569</u>	<u>445</u>

The emoluments of directors disclosed above include the following in respect of the highest paid director.

	2014	2013
	\$'000	\$'000
Emoluments of highest paid director	<u>227</u>	<u>172</u>
Contributions to external pension scheme included in the above	<u>47</u>	<u>43</u>

**8] Income Tax**

**Components of income tax expense**

	2014	2013
	\$'000	\$'000
<b>Current income tax expense</b>		
Current income tax charge	1,757	1,633
Previous year adjustment	(143)	(13)
<b>Deferred income tax (credit) / expense</b>		
Effect of rate changes	4	1
Relating to origination and reversal of temporary differences	25	(17)
Income tax expense reported in statement of profit or loss	<u>1,643</u>	<u>1,604</u>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**8] Income Tax (continued)**

**Reconciliation of income tax charge to accounting profit**

	2014	2013
	\$'000	\$'000
Profit before tax	8,633	6,978
Tax at the domestic income tax rate of 23% (2013: 24%)	1,986	1,674
Tax effect of deductible interest on Tier II Capital	(256)	-
Tax effect of non- deductible depreciation	42	50
Tax effect of other non - deductible expenses/non taxable income	10	(24)
Tax effect of rate changes	4	(83)
Previous year overprovision	(143)	(13)
Tax expense using effective rate	<u>1,643</u>	<u>1,604</u>
	2014	2013
	\$'000	\$'000
<b>Current income tax credited to equity</b>		
(Charge)/ Credit arising on AFS reserve movement	<u>1,444</u>	<u>(125)</u>
Tax effective rate	<u>19%</u>	<u>23%</u>

The corporation tax rate applicable from 1 April 2013 was 23%. The Finance Act 2012, which passed into law on 17 July 2012, included a reduction in the UK corporation tax rate from 23% to 21% with effect from 1 April 2014. In the UK budget announcement of 20 March 2013, the UK government announced its intention to further reduce the UK corporation tax rate to 20% with effect from 1 April 2015. This tax rate reduction was enacted on 17 July 2013. In the UK budget announcement of 19 March 2014, there was confirmation of the above mentioned future tax rates.

**9] Cash and Cash Equivalents**

	2014	2013
	\$'000	\$'000
Cash on hand	635	670
Cash at bank	165,246	95,966
Cash equivalent	28,674	36,695
	<u>194,555</u>	<u>133,331</u>

**10] Investment Securities – Held For Trading**

	2014	2013
	\$000	\$000
Treasury bills	<u>62,113</u>	<u>119,857</u>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**10) Investment Securities – Held For Trading (continued)**

Bank has classified its holding of UK and US treasury bills as trading assets which have been measured at fair value through profit and loss. No asset held under this category is pledged and all remain unencumbered.

The table below sets out the credit quality of trading debt securities.

	<b>Rating</b>	<b>2014</b>	<b>2013</b>
		<b>\$'000</b>	<b>\$'000</b>
Government Treasury Bills			
UK Treasury Bills	AAA	33,277	53,838
US Treasury Bills	AAA	28,836	66,019
<b>Total</b>		<b>62,113</b>	<b>119,857</b>

Investments in the trading portfolio, along with treasury bills held under AFS, are held mainly to maintain liquid asset buffer. Regular churning of such securities is made to ensure adequate marketability.

**11) Exposure to Derivatives**

The Bank deals in various currencies and it is not always possible to match the asset and liability in each currency. As a result, the Bank uses currency swaps to eliminate currency risk on long or short term currency positions. These derivatives are revalued daily and any change in their fair value is recognised in the statement of profit or loss. The total notional amount of outstanding cross currency swap contracts to which the Bank is committed is \$371,845 thousand (previous year \$392,257 thousand) and the net marked to market value of these exposures being \$1,697 thousand.

Major portion of bank's assets are on floating rate of interest where base rate is floating and linked to LIBOR or BOE rate with a fixed margin thereupon. Major portion of liabilities of the Bank are on fixed rate of interest. Bank uses interest rate swaps to eliminate interest rate risk in various reset buckets. The total notional amount of outstanding interest rate swap contracts to which the Bank is committed is \$83,512 thousand (previous year: Nil) and the net marked to market value of these exposures being \$74 thousand.

Fair value of all derivatives is as below:

	<b>31 March 2014</b>		<b>31 March 2013</b>	
	<b>Positive</b>	<b>Negative</b>	<b>Positive</b>	<b>Negative</b>
	<b>Fair</b>	<b>Fair</b>	<b>Fair</b>	<b>Fair</b>
	<b>Value</b>	<b>Value</b>	<b>Value</b>	<b>Value</b>
	<b>\$'000</b>	<b>\$'000</b>	<b>\$'000</b>	<b>\$'000</b>
Cross currency swap	1,865	168	1,169	5,836
Interest rate swap	108	34	-	-
	<b>1,973</b>	<b>202</b>	<b>1,169</b>	<b>5,836</b>



**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**11] Exposure to Derivatives (continued)**

All the deals under cross currency foreign exchange swaps and interest rate swaps are over-the-counter deals and none of them is with Central Counterparties. Table below shows analysis of counterparty credit exposure arising from derivative transactions as at 31 March 2014.

		<b>31 March 2014</b>			
	Nature of Counterparty	Nominal Amount – Buy Transaction	Nominal Amount – Sell Transaction	Positive Fair Value	Negative Fair Value
		\$'000	\$'000	\$'000	\$'000
Cross currency swaps	Bank	371,845	364,194	1,865	168
Interest rate swaps	Bank	83,512	83,437	108	34
		<u>455,357</u>	<u>447,631</u>	<u>1,973</u>	<u>202</u>

Table below shows analysis of counterparty credit exposure arising from derivative transactions as at 31 March 2013.

		<b>31 March 2013</b>			
	Nature of Counterparty	Nominal Amount – Buy Transaction	Nominal Amount – Sell Transaction	Positive Fair Value	Negative Fair Value
		\$'000	\$'000	\$'000	\$'000
Cross currency swaps	Bank	67,562	67,884	228	581
	Parent	324,695	328,765	941	5,255
Interest rate	NA	-	-	-	-
		<u>392,257</u>	<u>396,649</u>	<u>1,169</u>	<u>5,836</u>

There is no incidence of default of any counterparty with whom the Bank has entered into such contracts. No valuation adjustment is therefore required. The management has also assessed that there is no significant credit valuation adjustment or debit valuation adjustment impact on the fair value of derivatives, given the low potential future exposure of the derivatives book and the highly rated counterparties with whom derivatives are transacted.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**12] Loans and advances to banks**

	<b>31 March 2014</b>	<b>31 March 2013</b>
	<b>\$'000</b>	<b>\$'000</b>
Bills negotiated and discounted	22,044	26,439
Overdrafts	-	146
Term loans against Stand By Letters of Credit/buyers credit	267,700	196,936
Direct Loans to banks	-	5,022
Interbank placements of original maturity of more than three months	10,066	45,763
	<b>299,810</b>	<b>274,306</b>
Less impairment provisions	(90)	(90)
Net Loans and advances to Banks	<b>299,720</b>	<b>274,216</b>

At 31 March 2014 \$215,703 thousand (2013:\$132,679 thousand) of loans and advances to Banks are expected to be recovered more than 12 months after the reporting date.

**13] Loans and advances to customers**

	<b>31 March 2014</b>	<b>31 March 2013</b>
	<b>\$'000</b>	<b>\$'000</b>
Bills negotiated and discounted	278	222
Customer overdraft	343,515	297,269
Term loans	861,415	617,201
Total	<b>1,205,208</b>	<b>914,692</b>
Less impairment provisions <sup>(1)</sup>	(34,663)	(19,483)
Net Loans and advances to customers	<b>1,170,545</b>	<b>895,209</b>

<sup>1</sup>Impairment provision includes specific provision of \$31,155 thousand (2013:\$18,990 thousand), and collective provision of \$3,508 thousand (2013:\$493 thousand).

At 31 March 2014 \$601,045 thousand (2013:\$475,180 thousand) of loans and advances to customers are expected to be recovered more than 12 months after the reporting date.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

**14] Investment Securities - Available-for-Sale**

	2014	2013
	\$'000	\$'000
Marketable debt securities	<u>166,328</u>	<u>85,171</u>

At 31 March 2014 \$166,328 thousand (2013:\$85,171 thousand) of investment securities – available for sale are expected to be recovered more than 12 months after the reporting date.

Out of above, debt securities with carrying value of \$65,918 thousand (previous year: Nil) are encumbered under Sale and Repurchase agreement as a security for an interbank borrowing of \$44,439 thousand reported in note 24. The Bank continues to recognise the securities in their entirety in the statement of financial position because it retains substantially all of the risks and rewards of ownership. Transferred assets are not available for use to the Bank during the term of the arrangement. The associated liabilities have recourse only to the transferred financial assets.

**15] Investment Securities - Held to Maturity (HTM)**

	2014	2013
	\$'000	\$'000
Debt securities	7,119	9,560
Less: Impairment	(2,280)	(3,350)
Net book value of HTM securities	<u>4,839</u>	<u>6,210</u>

Refer to note 16 for details of fair value of investments which are Held to Maturity.

At 31 March 2014 \$4,619 thousand (2013:\$8,255 thousand) of investment securities – held-to-maturity are expected to be recovered more than 12 months after the reporting date.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**16] Financial Instruments**

**A. Financial Instruments carried at amortised cost**

The following table summarises the carrying amounts and incorporates the Bank's estimate of fair values of the held to maturity investment securities not presented on the Bank's balance sheet at fair value. The fair values in the table below may be different from the actual amount that will be received/ paid on the settlement or maturity of the financial instrument.

	Carrying amount		Fair value	
	2014 \$'000	2013 \$'000	2014 \$'000	2013 \$'000
Held to Maturity Securities	7,119	9,560	4,817	6,250
Less Impairment provision	(2,280)	(3,350)	-	-
Net Book Value	<u>4,839</u>	<u>6,210</u>	<u>4,817</u>	<u>6,250</u>

The total impairment provision recorded for Held to Maturity securities is against Bank's investment in one credit linked note of an investment banking company which is in liquidation. The provision for impairment is for the difference in amount between the book value and the market value of the credit linked note.

The fair value of financial instruments carried at amortised cost incorporates the Bank's estimate of the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or in the absence of the most advantageous market to which the Bank has access at that date.

The fair value of all remaining financial instruments carried at amortised cost approximates the book value, as given below:

	<i>Carrying amount and fair value</i>	
	2014 \$'000	2013 \$'000
<b>Assets</b>		
Customer and bank overdrafts	334,570	291,732
Term and bank loans	1,103,307	805,269
Interbank placements	38,740	82,459
Bills purchased	22,322	26,661
<b>Liabilities</b>		
Interbank deposits	273,205	84,645
Subordinated debts	55,000	50,000
Savings accounts	44,842	31,089
Current accounts	127,629	100,174
Fixed term deposits	1,196,243	1,094,517
Bills payable	224	190

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**A. Financial Instruments carried at amortised cost (continued)**

The basis of measurements of fair value which approximates to carrying value are as follows:

- Inter-bank deposits are generally of short dated maturity and hence the resultant impact on fair value of the same is considered insignificant.
- Subordinated debts are carried at rate of LIBOR +4/4.5% and the interest rate is reset every six months. Consequently the resultant impact on fair value of the subordinated debts is considered insignificant.
- The fair value of savings accounts and current accounts with no fixed maturity is assumed to be equal to the carrying value.
- Fair value of term deposits is expected to approximate the carrying value, since there has been insignificant change in interest rates in GBP deposits (during the year) which constitute a significant proportion of the Bank's term deposit base.
- The majority of the overdrafts and term loans are floating rate loans with interest rate reset between 3 to 6 months and consequently the resultant impact on fair value of the term loans is considered insignificant. However, no adjustment has been made to the fair value for change in credit spreads of counterparties. Impaired loans are reflected at net carrying value net of provision and that is the best estimate of fair value for such loans.
- Inter-bank placements are generally of short dated maturity and hence the resultant impact on fair value of the same is considered insignificant.

**B. Financial Instruments carried at fair value and amortised cost**

Financial instruments carried at fair value in the financial statements are Held for Trading securities (note 10), Available for sale securities (note 14) and Derivatives (note 11).

Financial instruments carried at amortised cost in the financial statements are loans and advances to banks (note 12), loans and advances to customers (note 13), investment securities held to maturity (note 15), deposits from banks (note 24) and deposits from customers (note 25).

Categories of these assets are as below:

**31 March 2014**

<b>Financial Assets:</b>	<b>Note</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
Investment securities – held for trading	10	62,113	-	-	62,113
Investment securities – available for sale	14	46,885	119,443	-	166,328
Derivative assets held for risk management	11	-	1,973	-	1,973
Loans and advances to banks	12	-	299,720	-	299,720
Loans and advances to customers	13	-	-	1,170,545	1,170,545
Investment securities held to maturity	15	-	3,522	1,317	4,839
		<u>108,998</u>	<u>424,658</u>	<u>1,171,862</u>	<u>1,705,518</u>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**B. Financial Instruments carried at fair value (continued)**

**Financial Liabilities:**

Derivative liabilities held for risk management	11	-	202	-	202
Deposits from banks	24	-	280,764	-	280,764
Deposits from customers	25	-	-	1,361,155	1,361,155
			<u>-</u>	<u>280,966</u>	<u>1,361,155</u>
					<u>1,642,121</u>

**31 March 2013**

<b>Financial Assets:</b>	<b>Note</b>	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
Investment securities – held for trading	10	119,857	-	-	119,857
Investment securities – available for sale	14	-	85,171	-	85,171
Derivative assets held for risk management	11	-	1,169	-	1,169
Loans and advances to banks	12	-	274,216	-	274,216
Loans and advances to customers	13	-	-	895,209	895,209
Investment securities held to maturity	15	-	4,826	1,384	6,210
		<u>119,857</u>	<u>365,382</u>	<u>896,593</u>	<u>1,381,832</u>
<b>Financial Liabilities:</b>					
Derivative liabilities held for risk management	11	-	5,836	-	5,836
Deposits from banks	24	-	115,808	-	115,808
Deposits from customers	25	-	-	1,194,617	1,194,617
		<u>-</u>	<u>121,644</u>	<u>1,194,617</u>	<u>1,316,261</u>

The fair value hierarchy has the following levels:

- Level 1 – Valuations based on quoted prices available in active markets for the same instrument. Securities included in Level 1 are UK and US Treasury Bills.
- Level 2 – Valuations based on quoted prices in markets that are not active, or based on pricing models for which significant inputs can be corroborated by observable market data (e.g. interest rates or exchange rates). Securities included in Level 2 are all securities presently held in AFS except UK and US treasury bills, loans and advances to Banks, Deposits from Banks, all derivatives and some investments held to maturity.
- Level 3 – Fair value measurements that include unobservable inputs that have a significant effect on the fair value measurement in its entirety. The financial instruments included in level 3 are loans and advances to customers, deposits from customers and some investments held to maturity.
- No transfers between Level 1, Level 2 and Level 3 have been made during the year.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**17] Provision on Impaired Financial Assets**

Loans and advances as in notes 12 and 13 above and HTM securities as in note 15 above include impaired assets and assets with renegotiated terms as below:

	Loans and Advances \$000	HTM Securities \$000
Gross balance of Impaired Assets	66,793	3,597
Less: specific impairment	(29,755)	(2,280)
Net Balance	<u>37,038</u>	<u>1,317</u>

**Movement in impairment provision during the year:**

<b>Specific allowances for impairment</b>	<b>2014</b>	<b>2013</b>
	\$,000	\$,000
Balance at 1 April	22,429	14,117
Impairment loss for the year		
Charge for the year	12,175	8,312
Recoveries/write offs	(1,080)	-
Balance at 31 March	<u>33,524</u>	<u>22,429</u>
Out of above		
Provision for impairment of loans and advances*	31,244	19,079
Provision for impairment of HTM securities	2,280	3,350
	<u>33,524</u>	<u>22,429</u>
<b>Collective allowances for impairment</b>		
Balance at 1 April	493	341
Impairment loss for the year:		
Charge for the year	3,015	152
Balance at 31 March	<u>3,508</u>	<u>493</u>
Total allowances for impairment	<u>37,032</u>	<u>22,922</u>
<b>The total charge to profit and loss in respect of impairment is as below:</b>		
Impairment charge on loans and advances	15,178	8,444
Impairment charge on investments held to maturity	(1,069)	-
Charge on account of other than temporary impairment of AFS securities	1,129	5,661
	<u>15,238</u>	<u>14,125</u>

\* includes reserves on renegotiated loans for discounting the expected cash flows at current market yields.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**18] Exposure to Credit Risk and Availability of Collateral Security**

The table below presents the Bank's maximum exposure to credit risk of its on-balance sheet and off-balance sheet financial instruments at 31 March 2014, before taking into account any collateral held or other credit enhancements. For on-balance sheet instruments, the maximum exposure to credit risk is the carrying amount reported on the balance sheet. For off-balance sheet instruments, the maximum exposure to credit risk represents the contractual nominal amounts. Bank's exposure to credit risk is well spread across different sectors and geographies. The Bank is affected by the general economic conditions in the territories in which it operates. Bank has set limits on the exposure to any counterparty and group of counterparties, Industry Sector Exposure and Geographical Exposure; and credit risk is also spread over Banks, Retail and Corporate customers.

The Bank's primary exposure to credit risk has increased by \$582,149 thousand when compared to March 2013 due to general business growth in the lending portfolio and increase in the AFS investment portfolio.

	31 March 2014 \$'000	31 March 2013 \$'000
<b>On Balance sheet exposure</b>		
Bilateral and syndicated loans and advances to customers	1,204,930	914,470
Loans and advances to customers under Letter of Credit/Stand by Letter of Credit/ Letter of Comfort by banks	267,700	202,104
Inter Bank placements and Cash balances with banks	204,621	179,094
Bills purchased directly from customers	278	223
Bills purchased under LC/Guarantee of banks	22,044	26,439
Securities Held to Maturity – banks	6,098	8,539
Securities Held to Maturity – Non banks	1,021	1,021
Securities available for sale – Banks	64,431	*58,638
Securities available for sale – Non Banks	101,897	*26,533
Derivative Financial Instruments	1,973	1,169
<b>Total – A</b>	<b>1,874,993</b>	<b>1,418,230</b>
<b>Off Balance Sheet Exposure</b>		
Non-Bank Commitments (LCs/LGs)	73,203	72,128
Commitments under LCs/Guarantees by Banks	2,356	2,194
<b>Total – B</b>	<b>75,559</b>	<b>74,322</b>
Undrawn Credit Facilities – Non Banks	86,564	47,886
Undrawn Credit Facilities - Banks	-	-
<b>Total – C</b>	<b>86,564</b>	<b>47,886</b>
<b>Total Exposure subject to Credit Risk (A+B+C)</b>	<b>2,037,116</b>	<b>1,540,438</b>

\* Available for sale investments were subject to market risk until March 2013.



**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**18] Exposure to Credit Risk and Availability of Collateral Security (continued)**

Bifurcation of total exposure subject to credit risk into bank and non-bank exposure is as below:

	2014	2013
	\$'000	\$'000
Exposure on Banks	569,223	478,177
Non-Bank Exposure	1,467,893	1,062,261
<b>Total</b>	<b>2,037,116</b>	<b>1,540,438</b>

**Collateral:**

Collateral is held to mitigate credit risk exposures and risk mitigation policies determine the eligibility of collateral types. Collateral types that are eligible for risk mitigation include: Deposits held under lien; residential, commercial and industrial property; fixed assets such as ship, plant and machinery; marketable securities; commodities; current assets including book debts; bank guarantees; and letters of credit. For certain types of lending – typically asset financing – the right to take charge over physical assets is significant in terms of determining appropriate pricing and recoverability in the event of default.

For loans and advances to banks and customers, the Bank held the following amounts of collateral, adjusted where appropriate.

- A. Exposure on Banks: Both for direct exposure to Banks (Placements and Bank Balances) and for exposure on Banks due to Letter of Credit/ Guarantee/ Letter of Comfort issued by the Banks, there are no separate collateral securities.
- B. Non-Bank exposure is collaterally secured as below; as at 31 March 2014:

	Retail Exposure		Non Retail Exposure		Amt. in \$ Million Total	
	Exposure	Amount Collateralised	Exposure	Amount Collateralised	Exposure	Amount Collateralised
Neither past due nor impaired:						
Internally rated AAA to A*	39.69	39.24	314.60	309.31	354.29	348.55
Internally rated BB to B*	41.72	41.06	677.17	661.11	718.89	702.17
<b>Total neither past due nor impaired</b>	<b>81.41</b>	<b>80.30</b>	<b>991.77</b>	<b>970.42</b>	<b>1,073.18</b>	<b>1,050.72</b>
Past due but not individually impaired:						
Up to 90 days	0.92	0.90	47.92	47.92	48.84	48.82
Over 90 days	5.27	4.85	76.13	75.87	81.40	80.72
<b>Total Past due but not individually impaired</b>	<b>6.19</b>	<b>5.75</b>	<b>124.05</b>	<b>123.79</b>	<b>130.24</b>	<b>129.54</b>
Loans with renegotiated terms**	2.64	2.60	91.21	85.81	93.85	88.41
Individually impaired						
Doubtful category	-	-	59.81	42.68	59.81	42.68
Loss category	0.28	0.00	7.61	0.00	7.89	0.00
<b>Total Impaired</b>	<b>0.28</b>	<b>0.00</b>	<b>67.42</b>	<b>42.68</b>	<b>67.70</b>	<b>42.68</b>
<b>Total</b>	<b>90.52</b>	<b>88.65</b>	<b>1,274.45</b>	<b>1,222.70</b>	<b>1,364.97</b>	<b>1,311.35</b>

\*Internal ratings based on PNBIL rating model.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**18] Exposure to Credit Risk and Availability of Collateral Security (continued)**

Comparative data for 31 March 2013 is as below:

	Retail Loans		Non Retail Loans		Amt. in \$ Million Total	
	Exposure	Amount Collateralised	Exposure	Amount Collateralised	Exposure	Amount Collateralised
Neither past due nor impaired:						
Internally rated AAA to A*	19.82	19.75	270.16	256.20	289.98	275.95
Internally rated BB to B*	8.62	8.21	622.74	601.40	631.36	609.61
Total neither past due nor impaired	<b>28.44</b>	<b>27.96</b>	<b>892.90</b>	<b>857.60</b>	<b>921.34</b>	<b>885.56</b>
Past due but not individually impaired:						
Up to 90 days	0.55	0.53	32.92	32.92	33.47	33.45
Over 90 days	1.84	1.74	16.65	16.38	18.49	18.12
Total Past due but not individually impaired	<b>2.39</b>	<b>2.27</b>	<b>49.57</b>	<b>49.30</b>	<b>51.96</b>	<b>51.57</b>
Loans with renegotiated terms**	-	-	27.59	20.45	27.59	20.45
Individually impaired loans:						
Doubtful category	-	-	26.75	26.75	26.75	26.75
Loss category	0.04	0.00	7.03	0.89	7.07	0.89
Total Impaired	<b>0.04</b>	<b>0.00</b>	<b>33.78</b>	<b>27.64</b>	<b>33.82</b>	<b>27.64</b>
<b>Total</b>	<b>30.87</b>	<b>30.23</b>	<b>1,003.84</b>	<b>954.99</b>	<b>1,034.71</b>	<b>985.22</b>

\*Internal ratings based on PNBIL rating model.

\*\* All loans with renegotiated terms are performing as per the terms of renegotiation; and currently there are no past due or impaired loans in this category. There are no forbore loans as on 31 March 2014 (31 March 2013: Nil).

Retail loans are loans to individual and small enterprises up to Euro 1 million.

While arriving at the value of collateral:

- Value of personal and corporate guarantees has not been considered.
- Value of securities in accounts where Bank has pari-pass charge is based on the book value in the latest available audited financial statements, where available, and is considered pro-rata in proportion to the exposure in the entity.
- The collateral values reported have been adjusted for the effects of over-collateralization.
- For Non-Bank HTM securities, current market value of the security has been considered.

The requirement for collateral is not a substitute for the ability to pay, which is the primary consideration for any lending decisions. In determining the financial effect of collateral held against loans neither past due or impaired, we have assessed the significance of the collateral held in relation to the type of lending. While doing so, where corporate or personal guarantees exist, they are not classified as secured exposures. But on case by case basis, the guarantees could be relevant as an important risk mitigation measure.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**18] Exposure to Credit Risk and Availability of Collateral Security (continued)**

Percentage of collateral held in Non Bank exposure is as below:

Percentage of value of collateral to exposure	Exposure \$ Million	
	2014	2013
100% and above*	1,318.29	906.20
76% to 99%	95.09	81.19
51% to 75%	10.44	0.31
26% to 50%	0.06	7.01
11% to 25%	-	5.32
Below 10%	9.03	5.50
Unsecured	34.98	30.20
<b>Total</b>	<b>1,467.89</b>	<b>1,035.73</b>
Average percentage of availability of Collateral*	96.35%	95.22%

\*excluding impact of over-collateralisation.

**Past due but not impaired loans**

Loans that are 'past due but not impaired' are those for which contractual interest or principal payments are past due but the Bank believes that there is no impairment on the basis of the level of security or collateral available and/or the stage of collection of amounts owed to the Bank.

**Renegotiated and forborne loans**

Loans that are renegotiated primarily to grant extended tenor to a customer who is facing some difficulties but who Bank believes is not impaired are known as 'other renegotiated loans'. Loans that are renegotiated on terms that are not consistent with those readily available in the market and/ or where Bank has granted a concession compared to the original terms of the loans, are considered to be subject to forbearance strategies and are known as 'forborne loans'. Forbearance strategies assist customers who are temporarily in financial distress and are unable to meet their original contractual repayment terms. Forbearance can be initiated by the customer, the bank or a third party and includes debt restructuring, such as a new repayment schedule, payment deferrals, tenor extensions and interest only payments.

Once a loan is subject to forbearance or is renegotiated, the loan continues to be reported as such, until the loan matures or is otherwise derecognised.

**Individually impaired loans**

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

**Doubtful and Loss category**

Loans under the doubtful category are those where there is an unlikelihood of collection of principal and/or interest sums due over time other than through sale of collateral or enforcement of security. Loans under loss category are those with probable or actual failure to collect sums even through the sale of business or collateral.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**18] Exposure to Credit Risk and Availability of Collateral Security (continued)**

The table below sets out a reconciliation of changes in the gross amount of impaired loans and advances to customers.

	2014 \$'000	2013 \$'000
Impaired loans and advances to customers at 1 April	33,747	16,178
Net Repayments in existing impaired loans and advances	(9)	-
Classified as impaired during the year	32,229	17,929
Other movements/exchange rate fluctuations	826	(360)
Impaired loans and advances to customers at 31 March	<u>66,793</u>	<u>33,747</u>

Detail of impairment allowance for loans and advances is given at Note 17.

The table below sets out a reconciliation of changes in the gross amount of impaired held-to-maturity investments:

	2014 \$'000	2013 \$'000
Impaired investments held to maturity at 1 April	4,734	5,000
Net Repayments in existing impaired investments	(1,137)	(266)
Classified as impaired during the year	-	-
Other movements/exchange rate fluctuations	-	-
Impaired investments held till maturity at 31 March	<u>3,597</u>	<u>4,734</u>

Details of impairment allowance for investment securities held-to-maturity is given at Note 17.

**Internal Ratings**

The Bank has developed internal rating models in co-ordination with the Risk Management Division of Parent Bank. All non-bank credit counterparties (except those secured by deposits with Bank/ Parent and those with loans up to £10,000) are rated on these models. Scoring is given on various financial and non-financial parameters. Rating is allocated based on overall score on the financial strength, creditworthiness and repayment capacity of the borrower.

**Derivatives, sale and repurchase agreements**

The Bank mitigates the credit risk of derivatives by entering into International Swaps and Derivative Association (ISDA) master netting agreements. Under these agreements, when a credit event such as a default occurs, all outstanding transactions under the agreement are terminated, the terminal value is assessed and only a single net amount is due or payable in settlement of all transactions. The Bank's sale and repurchase transactions are also covered by master agreements with netting terms similar to ISDA master netting agreements. The ISDA and similar master netting agreements create for the parties to the agreement a right to the set-off of recognised amounts that is enforceable only following an event of default, insolvency or bankruptcy of the Bank or the counterparties or following other predetermined events.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**19] Exposure to Eurozone Countries**

The Bank has no direct sovereign exposure (as defined by the European Banking Authority 'EBA') to any of the Eurozone countries. Gross exposure to other counterparties in the Eurozone countries as at 31 March 2014 is as below:

Name of the Country	As on 31 March 2014			As on 31 March 2013			\$'000
	Exposure to Banks	Exposure to Corporates	Total Exposure	Exposure to Banks	Exposure to Corporates	Total Exposure	
Belgium	132	30,972	31,104	3,849	22,920	26,769	
Cyprus	-	2,172	2,172	-	4,583	4,583	
Germany	611	10,336	10,947	329	-	329	
Spain	-	7,567	7,567	-	7,250	7,250	
France	279	5,315	5,594	-	5,135	5,135	
Ireland	-	7,658	7,658	-	5,249	5,249	
Netherland	-	18,863	18,863	1,071	28,707	29,778	
Luxembourg	-	**73,292	**73,292	-	-	-	
Total	1,022	156,175	157,197	5,249	73,844	79,093	
of which – to problem Eurozone countries*	-	17,397	17,397	-	17,082	17,082	

\*GIIPS (Greece, Ireland, Italy, Portugal and Spain) and Cyprus.

\*\* Out of \$73.29 Mn to Luxembourg, \$53.29 Mn is fully secured by deposits.

There is no direct/ indirect exposure on Ukraine and Russia.

An amount of USD 25,651 thousand (USD 6,261 thousand from troubled Eurozone countries) is to be received after 12 months.

At 31 March 2014 the Bank's non-sovereign exposure to GIIPS and Cyprus amounting to \$ 17.40 million was as follows:

- The Bank has an exposure in the form of a credit facility to a corporate in Ireland, having an outstanding balance of \$7.66 million. This counterparty is an Irish subsidiary of an Indian corporate and is fully guaranteed by the Indian parent. It is further fully secured by collateral security of more than 100% of the exposure.
- The Bank has an exposure in the form of a credit facility to a corporate in Spain, having an outstanding balance of \$7.57 million. This counterparty is a Spanish subsidiary of an Indian corporate and is fully guaranteed by the Indian parent. It is further fully secured by collateral security of more than 100% of the exposure.
- The Bank has an exposure in the form of a credit facility to a corporate incorporated in British Virgin Island and having its operations in Cyprus, having an outstanding balance of \$2.17 million. This counterparty is a BVI subsidiary of an Indian corporate and is fully guaranteed by the Indian promoters. It is further fully secured by collateral security of more than 100% of the exposure.

All of the above loans are in the performing category; and there is no objective evidence of impairment.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

20) **Property and Equipment**

At 31 March 2014

	Leasehold improvements \$'000	Fixtures and fittings \$'000	Total \$'000
<b>Cost</b>			
At 1 April 2013	1,934	2,586	4,520
Additions	-	388	388
Disposals	-	-	-
At 31 March 2014	<u>1,934</u>	<u>2,974</u>	<u>4,908</u>
<b>Depreciation</b>			
At 1 April 2013	(827)	(1,966)	(2,793)
Charge for year	(346)	(297)	(643)
Disposals	-	-	-
At 31 March 2014	<u>(1,173)</u>	<u>(2,263)</u>	<u>(3,436)</u>
<b>Net book value</b>			
At 1 April 2013	<u>1,107</u>	<u>620</u>	<u>1,727</u>
At 31 March 2014	<u>761</u>	<u>711</u>	<u>1,472</u>

At 31 March 2013

	Leasehold improvements \$'000	Fixtures and fittings \$'000	Total \$'000
<b>Cost</b>			
At 1 April 2012	1,066	2,208	3,274
Additions	977	378	1,355
Disposals	(109)	-	(109)
At 31 March 2013	<u>1,934</u>	<u>2,586</u>	<u>4,520</u>
<b>Depreciation</b>			
At 1 April 2012	(597)	(1,663)	(2,260)
Charge for year	(339)	(303)	(642)
Disposals	109	-	109
At 31 March 2013	<u>(827)</u>	<u>(1,966)</u>	<u>(2,793)</u>
<b>Net book value</b>			
At 1 April 2012	<u>469</u>	<u>545</u>	<u>1,014</u>
At 31 March 2013	<u>1,107</u>	<u>620</u>	<u>1,727</u>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**21] Intangible Assets**

**31 March 2014**

	<b>Software \$'000</b>
<b>Cost</b>	
At 1 April 2013	1,412
Additions	104
	<u>1,516</u>
<b>Amortisation</b>	
At 1 April 2013	(1,220)
Charge for the year	(128)
	<u>(1,348)</u>
<b>Carrying value</b>	
At 1 April 2013	<u>192</u>
At 31 March 2014	<u>168</u>

**31 March 2013**

	<b>Software \$'000</b>
<b>Cost</b>	
At 1 April 2012	1,344
Additions	68
	<u>1,412</u>
<b>Amortisation</b>	
At 1 April 2012	(1,074)
Charge for the year	(146)
	<u>(1,220)</u>
<b>Carrying value</b>	
At 1 April 2012	<u>270</u>
At 31 March 2013	<u>192</u>

**22] Deferred Tax Asset / (Liability)**

	<b>2014 \$'000</b>	<b>2013 \$'000</b>
At 1 April	49	33
Release / (charge) for year	(29)	16
At 31 March	<u>20</u>	<u>49</u>

Deferred tax is in respect of timing differences between the book value of fixed assets and their tax carrying value

Effective rate utilised to calculate deferred tax provision	<u>21%</u>	<u>23%</u>
---	------------	------------

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**23] Prepayments and other Receivables**

	2014	2013
	\$'000	\$'000
Current prepayments	762	269
Other receivables	163	29
	<u>925</u>	<u>298</u>

**24] Deposits from Banks**

	31 March 2014	31 March 2013
	\$'000	\$'000
Current accounts from banks	2,070	15,735
Overdrafts in Nostro accounts with banks	3,838	2,269
Fixed term deposits	1,651	13,159
Inter bank borrowings	273,205	84,645
Total deposits from banks	<u>280,764</u>	<u>115,808</u>

At 31 March 2014 \$25,141 thousand (2013: \$8,355 thousand) of deposits from Banks are expected to be settled more than 12 months after the reporting date.

Out of the above, inter-bank borrowing with carrying value of \$44,439 thousand (previous year: Nil) is secured by a pledge of available for sale investments with carrying value of \$65,918 thousand (previous year: Nil) under Sale and Repurchase agreement, as per details given in note 14. The financial liability is recognised for the obligation to pay the repurchase price. Such liability has recourse only to the transferred financial assets.

**25] Deposits from Customers**

	31 March 2014	31 March 2013
	\$'000	\$'000
Current accounts	121,721	82,170
Savings accounts	44,842	31,089
Fixed term deposits	1,194,592	1,081,358
Total deposits from customers	<u>1,361,155</u>	<u>1,194,617</u>

At 31 March 2014 \$495,996 thousand (2013:\$420,355 thousand) of deposits from customers are expected to be settled more than 12 months after the reporting date.



**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**26] Subordinated Liabilities and other Borrowed Funds**

	2014	2013
	\$'000	\$'000
Subordinated debt	<u>55,000</u>	<u>50,000</u>

This represents lower tier II capital received as follows:

- i. \$25,000,000 issued in March 2009, maturing in March 2019.
- ii. \$12,500,000 issued in March 2012, maturing in March 2022.
- iii. \$12,500,000 issued in October 2012, maturing in October 2022.
- iv. \$5,000,000 issued in December 2013 maturing in December 2028.

Bonds at S. No. i to iii are subscribed by the parent company while Bonds at S. No. iv are by another Bank of Indian origin.

These subordinated Bonds are listed on the Channel Islands Stock Exchange, bearing non-discretionary coupons of 4% over LIBOR for the first three and 4.5% over LIBOR for the recent issue, are redeemable by the holder; and are therefore included within subordinated liabilities.

At 31 March 2014 \$55,000 thousand (2013:\$50,000 thousand) of subordinated liabilities are expected to be settled more than 12 months after the reporting date.

**27] Other liabilities**

	2014	2013
	\$'000	\$'000
Bills payable	224	190
Other payables and accrued liabilities	5,092	2,267
Deferred income	6,144	4,043
	<u>11,460</u>	<u>6,500</u>

**28] Share Capital**

**Issued share capital**

	2014		2013	
	No.	\$	No.	\$
<b>Issued and fully paid</b>				
Ordinary shares of £1 each	2	4	2	4
Ordinary shares of \$1 each				
At start of year	124,630,625	124,630,625	112,130,625	112,130,625
New Issue of Share Capital*	50,000,000	50,000,000	12,500,000	12,500,000
At end of year	<u>174,630,627</u>	<u>174,630,629</u>	<u>124,630,627</u>	<u>124,630,629</u>

\* During the year the Bank has issued equity share capital of \$50,000,000 (previous year: \$12,500,000) to its parent company, Punjab National Bank, by way of 50,000,000 ordinary shares of \$1 each.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**28] Share Capital (continued)**

Included within the share capital is the Upper Tier II capital of \$25,000 thousand raised by the Bank in 2011 in the form of perpetual floating rate subordinated notes.

Based on the terms and conditions of the purchase agreement and in accordance with IAS 32 guidance, since the interest payments are discretionary and the bank does not have an obligation to pay cash or any other financial asset in respect of its perpetual instrument nor there is any obligation to exercise its right to call the instrument, this is classified as equity in the financial statements.

**29] Fair Value Reserves**

	Gross \$'000	Tax \$'000	Net \$'000
<b>31 March 2014</b>			
Balance at 1 April 2013	159	(34)	125
Amount transferred to statement of profit or loss	(388)	93	(295)
	(229)	59	(170)
Movement in AFS reserve in year	(6,280)	1,444	(4,836)
Balance at 31 March 2014	<u>(6,509)</u>	<u>1,503</u>	<u>(5,006)</u>

	Gross \$'000	Tax \$'000	Net \$'000
<b>31 March 2013</b>			
Balance at 1 April 2012	(4,527)	1,174	(3,353)
Amount transferred to statement of profit or loss	4,162	(1,082)	3,080
	(365)	92	(273)
Movement in AFS reserve in year	524	(126)	398
Balance at 31 March 2013	<u>159</u>	<u>(34)</u>	<u>125</u>

**30] Operating Lease Commitments**

Where Bank is the lessee, the future minimum lease payments under non-cancellable operating leases

	2014 \$'000	2013 \$'000
Less than one year	823	796
Later than one year but less than five years	1,332	1,376
	<u>2,155</u>	<u>2,172</u>

The Bank leases premises for its corporate office and branches. The leases typically run for a period of 15 to 20 years with a break clause of 5 years for the Bank and the lessor. Lease payments are liable to be modified at break period to reflect market rentals. The new premises for Corporate Office and Central London branch have a rent free period of one year out of initial five years of lease. Rent for this incentive period has been calculated on a straight line basis over the lease term and kept as provision that is included in other liabilities (note 27).

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**31] Other Commitments and Contingencies**

Commitments in respect of financial instruments were as follows:

	2014	2013
	\$'000	\$'000
Guarantees issued to third parties	5,422	5,317
Letters of credit issued	70,137	69,005
Commitment to buy treasury securities	-	4,051
Commitment to sell treasury securities	-	3,047

There were undrawn loans of \$36,490 thousand (previous year: \$24,817 thousand) and un-availed portions of sanctioned overdraft limits to the extent of \$50,074 thousand (previous year: \$23,068 thousand) as at 31 March 2014. Bills amounting to \$11,089 thousand (previous year: \$11,142 thousand) were sent/received in collection on behalf of customers. The Bank does not have any balance sheet exposure on such bills for collection.

**32] Related Party Transactions**

The ultimate controlling party of the company is Punjab National Bank, a Public sector bank incorporated in India which is both the immediate parent company and ultimate controlling party. The consolidated financial statements of Punjab National Bank are publically available at 7 Bhikaji Cama Place, New Delhi 110607, India.

The Bank regards Punjab National Bank (including all its branches in India and abroad) and its subsidiaries as related parties in view of 100% shareholding of Punjab National Bank in the company. Entire equity capital and 93.75% of tier II capital of the company is held by Punjab National Bank.

Liabilities and assets outstanding to the related parties on the balance sheet of the Bank as on 31 March 2014 are as below:

	2014	2013
	\$'000	\$'000
<b>Liabilities</b>		
Fixed Deposits	1,289	12,805
Borrowings	2,028	56,388
Current Accounts	1,979	2,323
<b>Assets</b>		
Balance in Nostro Accounts	811	568
Bills accepted/ confirmed by PNB discounted to Corporates	451	864
Placements	1,167	1,628

*Excluded from the above are loans sanctioned to corporates on Stand By Letters of Credit of Punjab National Bank amounting to \$ 24,393 thousand (previous year: \$23,044 thousand).*

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

32] **Related Party Transactions (continued)**

Contingent exposure to Punjab National Bank is as below:

Nature	2014 \$'000	2013 \$'000
Letters of Credit and Guarantees Confirmed	2,356	2,194
Cross Currency Swaps (notional) – Sell	-	328,765
Cross Currency Swaps (notional) – Buy	-	324,695

Detail of transactions of a revenue nature with Punjab National Bank is as below:

Nature	Particulars	2014 \$'000	2013 \$'000
<b>Receipts:</b>			
Interest Earned	Interest on Inter Bank Placements	2	143
<b>Payments:</b>			
A. Professional Fee	Charges for Service Level Agreement (SLA)*	185	191
B. Interest Paid on	Borrowings	471	570
	Fixed Deposits	151	421
C. Interest Paid on Capital Bonds	Upper Tier II Capital Bonds of \$25.00 Mn.	1,111	1,168
	Lower Tier II Capital Bonds of \$25.00 Mn.	1,111	1,168
	Lower Tier II Capital Bonds of \$12.50 Mn.	555	584
	Lower Tier II Capital Bonds of \$12.50 Mn.	555	279

*\*These charges were levied by Punjab National Bank, for support services provided during the year. The services provided include IT hosting, maintenance and support services to PNBIL and are backed by a Service Level Agreement (SLA).*

The Bank enters into commercial transactions with its parent company in the ordinary course of business on an arm's length basis.

Other transactions with related parties (including remuneration paid to directors which the bank considers as key management) are disclosed in Note 7. The Bank considers that the cost of secondment of executives to or from the parent company is not material.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

**33] Financial Risk Management Objectives and Policies**

**Risk Governance**

The Board of Directors have overall responsibility for risk management in the Bank. The Board has formed an Audit and Compliance Committee (ACC) and a Risk Management Committee (RMC) for overseeing the risk management function. There are various other committees formed with the role and responsibility to manage defined aspects of risk management.

The role and responsibilities of various risk management committees are set out in the following paragraphs.

*Audit and Compliance Committee (ACC)*

- Review financial statements and the Annual Report and Accounts of the company and recommend them to the Board;
- Review the effectiveness of internal controls and monitor the implementation of any remedial actions;
- Review effectiveness of risk management and report to the Board;
- Review Annual Report by Money Laundering Reporting Officer;
- Review Internal Audit reports;
- Review external audit reports, the annual audit plan and the External Auditor's annual management letter;
- Review policy exchanges and other major reports to or from the regulators;
- Review other compliance reports;
- Review regularly its own terms of reference and its own effectiveness; and
- Review regularly the status of restructured accounts.

*Risk Management Committee (RMC)*

*The RMC is formed as an executive committee and is responsible for:*

- Oversight of management of Operational Risk, Market Risk, Credit Risk and residual risks;
- Implementation of obligations under ICAAP document submitted to PRA;
- Review and modification to ICAAP;
- Maintaining adequate capital, based on the capital adequacy ratio stipulated by the regulator;
- Finalize credit rating module for the Bank and submit for the approval of the Board;
- Modify credit policy and submit for the approval of the Board;
- Finalize provisioning policy for the Bank and submit for the approval of the Board;
- Review periodic stress test on Capital requirement of the Bank; and
- Periodically apprise the Board on Risk management issues.

*Asset and Liability Management Committee (ALCO)*

The ALCO is an executive committee, which monitors and manages the Bank's balance sheet, interest rate on deposits and liquidity. The ALCO will also strive to optimize the return on Bank's funds.

*Credit Recommendation Committee*

The credit recommendation committee assesses the loan applications above \$ two hundred thousand and puts up its recommendation to the sanctioning authority.

**33] Financial Risk Management Objectives and Policies (continued)**

*Management Committee of the Board (MCB)*

The MCB, comprising of four directors, including two non-executive directors, acts as sanctioning committee for all proposals above \$7 million. The committee is also responsible for approval of all new products, review and enhancement to existing products, periodical review of stressed assets, finalizing provisioning requirements, taking stock of any breaches in any of the policies, identifying the resolution thereto, periodical review of business strategy and branch expansion plans.

**Compliance and Risk Management**

The core objective of Compliance is to support the board and senior management in fulfilling their financial services, regulatory obligations and to help maintain the Bank as a 'fit and proper' institution, in whatever form of business it undertakes, by helping to ensure compliance with the voluntary codes, principles, rules and regulations established by the various financial services regulatory organisations.

Compliance sets the overall regulatory governance arrangements and provides information, advice and guidance to business on financial services regulations. It also monitors business activities to ensure that improper conduct and failures to comply with regulatory requirements are brought to the attention of management for appropriate corrective action.

The Bank's Risk Management function is the responsibility of the Risk Management Department and the Compliance Department. The Risk Management and Compliance Departments have been delegated responsibility for the day-to-day monitoring of the individual risks by the Managing Director. The purpose of each of the areas is to ensure that market, credit and operational risk in the Bank is kept within the guidelines set by the Board.

The Managing Director is responsible for providing an oversight function that will consider all the risks on a consolidated basis and, in this respect, chairs the main risk committees. The credit and market risk, and operational risk functions report to the Risk and Compliance Director.

In order to manage its risks, the Bank adopts the following approach:

- The Bank follows the framework for policies and procedures put in place by the Board, covering all the Bank's operations. Policies are developed covering all operational areas, as well as credit risk, liquidity risk, concentration risk, trading book risk and provisioning.
- The Risk and Compliance Department is in place to establish appropriate systems for the Bank in proportion to its scale, nature and complexity. Systems are in place to address credit risk, market risk, liquidity risk, and operational risk.
- As part of the control process, the Bank's operations are reviewed by the Internal Audit function and they report their findings to the audit committee on a periodic basis.

Compliance and Risk Management provides a focal point to coordinate communications and consultations with regulatory authorities and also carries out reviews of relevant business units against applicable rules, guidance and the Bank's internal policies and procedures. The Executive

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

---

**33] Financial Risk Management Objectives and Policies (continued)**

Director has the responsibility of oversight into the compliance aspects of the Bank and he is assisted by the Money Laundering Reporting Officer and Internal auditor for effective oversight.

**Internal Audit**

The Internal Audit department monitors compliance with policies and standards and the effectiveness of internal control structures across the Bank through its programme of business audits.

The Head of Internal Audit reports regularly to the Audit Committee and the Bank's Managing Director where immediate corrective action is taken.

**Risk Categorisation**

The Bank has categorised various risks under following headings:

***Credit Risk***

Credit risk is defined as potential financial loss on account of delay or denial of repayment of principal or interest with respect to a credit facility extended by the Bank, both fund and non-fund based. Credit risk can also arise on account of downgrading of counterparties to whom credit facilities are extended or whose credit instruments the Bank may be holding, causing the value of those assets to fall.

Risks arising from adverse changes in the credit quality of borrowers or general deterioration in the economic conditions under which these counterparties operate could also affect the recoverability and value of Bank's assets and therefore its financial performance.

The following techniques are in place to mitigate the credit risks:

- The bank has an approved lending policy wherein the types of credit facilities are defined as is the sanctioning authority which grants within specific financial limits;
- Every credit facility beyond a pre-determined limit is processed through the recommending committee and sanctioned by the credit sanction committee;
- Credit risk under each loan above the threshold limit is assessed both on financial and non- financial parameters;
- Concentration risk is taken into account both with respect to individual or group exposures as well as industry wide or country wide exposures;
- Most of the facilities are secured by either tangible securities or third party guarantees;
- With respect to large value facilities including under syndicated facilities, documentation is done through external solicitors;
- Periodic review and monitoring of facilities is undertaken to identify and attend to any observed weakness in any facility;
- All facilities above prescribed threshold limits are reported to the Board from time to time;
- Lending policies and limits are periodically reviewed by the Board; and
- Risk rating of individual proposals beyond cut-off limit is done as per the internal credit risk rating model.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**33] Financial Risk Management Objectives and Policies (continued)**

Any exposure to a single party or group in excess of 10% of its capital base is considered as large exposure as per regulatory guidelines and is monitored regularly. The Bank does not have credit risk exposure to any single non-bank counterparty in excess of 25% of capital funds.

The carrying value of financial assets recorded in the financial statements represents the bank's maximum exposure to credit risk.

***Market Risk***

Market risk is defined as the potential adverse change in the Bank's income or net worth arising from movements in interest rates, exchange rates, equity prices and/or other market prices. Effective identification and management of market risk is required for maintaining stable net interest income.

The most significant forms of market risk to which the Bank is exposed are identified as interest rate risk, exchange risk and price risk. Most of Bank's liabilities are on fixed rate of interest while most of bank assets are on floating rate of interest. Bank regularly analyses the same and has fixed limits for maximum mismatch. Exchange risk arises mainly on account of the Bank's open positions. This is also monitored on a daily basis and an upper limit is fixed for the same. Assets held under the trading book are regularly marked to market and carried at fair value.

The bank is exposed to foreign exchange risk to the extent of its open position in each currency. The bank has stipulated an internal limit for maximum open position and is measuring and monitoring this open position on a daily basis.

The bank deals in various currencies and it is not always possible to match the asset and liability in each currency. As a result, the Bank uses currency swaps to eliminate currency risk on long or short currency positions. These derivatives are re-valued daily and any change in their fair value is recognized immediately in profit and loss. The total notional amount of outstanding currency exchange contracts to which the Bank is committed is \$371.85 million (2013: \$392.26 million).

The open position of the Bank as on 31 March 2014 is as follows:

Currency	Open Position '000	USD Equivalent \$'000
Indian Rupees	183,473	3,062
Pound Sterling	(2,923)	(4,873)
Euro	(1,623)	(2,337)
UAE Dirham	355	97
Canadian Dollar	216	195
Norwegian Kroner	220	37
Nepalese Rupees	815	9
Japanese Yen	938	9
Australian Dollar	(32)	(29)
Total Long Position in US Dollars		3,409
Total Short Position in US Dollars		7,239

Upward or downward movement of exchange rate by 10% may impact profitability of the Bank by \$724 thousand (2013: \$328thousand)



**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**33] Financial Risk Management Objectives and Policies (continued)**

**Interest Rate Risk (Re-pricing analysis as at 31 March 2014)**

The bank is monitoring its interest rate mismatches on a regular basis, and the potential loss on account of upward or downward movement of interest rates by 2% based on exposure as at 31 March 2014 is presented below:

Particulars	Up to 1 Month	1 - 3 Months	3 - 6 Months	6 - 12 Months	1-3 years	Over 3 Years	Non Sensitive Category	Total
ASSETS	\$ (000s)	\$ (000s)	\$ (000s)	\$ (000s)	\$ (000s)	\$ (000s)	\$ (000s)	\$ (000s)
Cash and cash equivalent	194,555	-	-	-	-	-	-	194,555
Investment securities – held for trading	-	-	-	-	-	-	62,113	62,113
Derivative financial instruments	1,686	119	-	59	-	109	-	1,973
Loans and advances to banks	10,066	109,632	58,242	10,957	110,823	-	-	299,720
Loans and advances to customers	696,887	351,842	69,615	4,211	5,632	10,250	32,108	1,170,545
Investment securities – available for sale	-	-	-	-	879	165,449	-	166,328
Investment securities – held to maturity	2,500	-	-	-	-	2,339	-	4,839
Property, plant and equipment	-	-	-	-	-	-	1,472	1,472
Intangible assets	-	-	-	-	-	-	168	168
Deferred tax assets	-	-	-	-	-	-	20	20
Prepayments and other receivables	666	-	-	259	-	-	-	925
<b>Total</b>	<b>906,360</b>	<b>461,593</b>	<b>127,857</b>	<b>15,486</b>	<b>117,334</b>	<b>178,147</b>	<b>95,881</b>	<b>1,902,658</b>
<b>LIABILITIES</b>								
Derivative financial instruments	123	32	-	13	-	34	-	202
Deposits from banks	43,519	176,359	704	60,182	-	-	-	280,764
Deposits from customers	267,773	96,530	154,520	346,335	270,363	225,634	-	1,361,155
Current tax liabilities	-	-	(254)	-	-	-	-	(254)
Subordinated liabilities	-	5,000	50,000	-	-	-	-	55,000
Other liabilities	593	333	-	-	-	-	10,534	11,460
Share Capital	-	-	25,000	-	-	-	149,631	174,631
Reserve and retained earnings	-	-	-	-	-	-	19,700	19,700
<b>Total</b>	<b>312,008</b>	<b>278,254</b>	<b>229,970</b>	<b>406,530</b>	<b>270,363</b>	<b>225,668</b>	<b>179,865</b>	<b>1,902,658</b>
Interest Rate Gap	594,352	183,339	(102,113)	(391,044)	(153,029)	(47,521)	(83,984)	-
Interest Rate Swap for Hedging	-	(41,850)	(41,662)	-	-	83,512	-	-
<b>Net Gap</b>	<b>594,352</b>	<b>141,489</b>	<b>(143,775)</b>	<b>(391,044)</b>	<b>(153,029)</b>	<b>35,991</b>	<b>(83,984)</b>	<b>-</b>
Impact of Interest Variation of 2%	495	471	(1,078)	(5,866)	(6,120)	2,879	-	(9,219)

The bank has a stipulated limit for open positions and the actual open position is measured and monitored regularly.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

33] **Financial Risk Management Objectives and Policies (continued)**

*Liquidity Risk*

Liquidity risk is the risk that the Bank may not be able to meet its payment obligations with respect to customer deposits or any borrowing or obligations under any other assets or liabilities, within stipulated time and without significant additional cost. The bank has documented liquidity policy in place, within the guidelines issued by the Prudential Regulation Authority (PRA). The Bank has a system in place to monitor total contractual inflow and outflow and to manage the gap within pre-stipulated limits prescribed by the Board and/ or the regulator. The following table analyses the Bank's assets and liabilities (based on undiscounted cash flows) into relevant maturity groupings based on the remaining period to the contractual maturity date at the balance sheet date:

As at 31 March 2014	Up to 1 m	1-3 m	3-12 m	1-2 yr	2-5 yr	Over 5 yrs	Undated	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Assets</b>								
Cash and cash equivalent	194,555	-	-	-	-	-	-	194,555
Investment securities – held for trading	62,113	-	-	-	-	-	-	62,113
Derivative financial instruments	1,686	119	59	-	109	-	-	1,973
Loans and advances to banks	10,066	21,624	52,327	128,037	67,939	19,727	-	299,720
Loans and advances to customers	407,672	50,199	111,629	139,664	321,880	139,501	-	1,170,545
Investment securities – available for sale	-	-	-	879	47,506	117,943	-	166,328
Investment securities – held to maturity	-	-	2,500	-	1,022	1,317	-	4,839
Property, plant and equipment	-	-	-	-	-	-	1,472	1,472
Intangible assets	-	-	-	-	-	-	168	168
Deferred tax assets	-	-	-	-	-	-	20	20
Prepayments and other receivables	666	-	259	-	-	-	-	925
<b>Total assets</b>	<b>676,758</b>	<b>71,942</b>	<b>166,774</b>	<b>268,580</b>	<b>438,456</b>	<b>278,488</b>	<b>1,660</b>	<b>1,902,658</b>
Derivative financial instruments	123	32	2	11	34	-	-	202
Deposits from banks	18,378	151,328	85,917	25,141	-	-	-	280,764
Deposits from customers	267,773	96,530	500,856	181,627	287,731	26,638	-	1,361,155
Current tax liabilities	-	-	(254)	-	-	-	-	(254)
Subordinated liabilities	-	-	-	-	25,000	30,000	-	55,000
Other liabilities	1,246	701	2,357	2,786	4,370	-	-	11,460
Share capital	-	-	-	-	-	-	174,631	174,631
Reserves and retained earnings	-	-	-	-	-	-	19,700	19,700
Financial guarantees and letters of credit – net of deposit	510	-	2,078	-	-	-	-	2,588
Irrevocable Loan commitments	52,866	333	-	-	-	-	-	53,199
<b>Total equity, liabilities and commitments</b>	<b>340,896</b>	<b>248,924</b>	<b>590,956</b>	<b>209,565</b>	<b>317,135</b>	<b>56,638</b>	<b>194,331</b>	<b>1,958,445</b>
<b>Net liquidity gap</b>	<b>335,862</b>	<b>(176,982)</b>	<b>(424,182)</b>	<b>59,015</b>	<b>121,321</b>	<b>221,850</b>	<b>(192,671)</b>	<b>(55,787)</b>
<b>Cumulative Liquidity Gap</b>	<b>335,862</b>	<b>158,880</b>	<b>(265,302)</b>	<b>(206,287)</b>	<b>(84,966)</b>	<b>136,884</b>	<b>(55,787)</b>	<b>-</b>

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**33] Financial Risk Management Objectives and Policies (continued)**

Comparative analysis as at 31 March 2013 was as below:

As at 31 March 2013	Up to 1 m	1-3 m	3-12 m	1-2 yr	2-5 yrs	Over 5 yrs	Undated	Total
	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000	\$'000
<b>Assets</b>								
Cash and cash equivalent	133,331	-	-	-	-	-	-	133,331
Investment securities – held for trading	119,857	-	-	-	-	-	-	119,857
Derivative financial instruments	999	112	58	-	-	-	-	1,169
Loans and advances to banks	5,168	41,331	95,038	5,578	127,101	-	-	274,216
Loans and advances to customers	313,589	17,181	89,259	122,030	228,118	125,032	-	895,209
Investment securities – available for sale	-	-	-	-	27,723	57,448	-	85,171
Investment securities – held to maturity	-	-	1,305	2,500	-	2,405	-	6,210
Property, plant and equipment	-	-	-	-	-	-	1,727	1,727
Intangible assets	-	-	-	-	-	-	192	192
Deferred tax assets	-	-	-	-	-	-	49	49
Prepayments and other receivables	236	-	-	62	-	-	-	298
<b>Total assets</b>	<b>573,180</b>	<b>58,624</b>	<b>185,660</b>	<b>130,170</b>	<b>382,942</b>	<b>184,885</b>	<b>1,968</b>	<b>1,517,429</b>
Derivative financial instruments	3,030	2,218	588	-	-	-	-	5,836
Deposits from banks	25,338	237	81,878	589	7,766	-	-	115,808
Deposits from customers	247,168	85,429	441,665	120,416	299,939	-	-	1,194,617
Current tax liabilities	1,085	-	-	-	-	-	-	1,085
Subordinated liabilities	-	-	-	-	-	50,000	-	50,000
Other liabilities	1,443	302	1,663	2,138	954	-	-	6,500
Share capital	-	-	-	-	-	-	124,631	124,631
Reserves and retained earnings	-	-	-	-	-	-	18,951	18,951
Financial guarantees and letters of credit – net of deposit	4,112	863	3,276	2,645	-	-	-	10,896
Irrevocable Loan commitments	14,456	-	-	-	-	-	-	14,456
<b>Total equity and liabilities</b>	<b>296,632</b>	<b>89,049</b>	<b>529,070</b>	<b>125,788</b>	<b>308,659</b>	<b>50,000</b>	<b>143,582</b>	<b>1,542,780</b>
<b>Net liquidity gap</b>	<b>276,548</b>	<b>(30,425)</b>	<b>(343,410)</b>	<b>4,382</b>	<b>74,283</b>	<b>134,885</b>	<b>(141,614)</b>	<b>(25,351)</b>
<b>Cumulative Liquidity Gap</b>	<b>276,548</b>	<b>246,123</b>	<b>(97,287)</b>	<b>(92,905)</b>	<b>(18,622)</b>	<b>116,263</b>	<b>(25,351)</b>	<b>-</b>

ALCO is primarily responsible for overseeing the implementation of the liquidity policy of the Bank. The Bank measures and monitors the liquidity position on a daily basis. The Bank considers the funding ability before committing additional credit facility and closely monitors the upcoming payment obligations. The Bank has an Individual Liquidity Adequacy Assessment (ILAA) document taking into account the revised guidelines issued by the regulator.

**33] Financial Risk Management Objectives and Policies (continued)**

The Bank undertakes stress tests on its liquidity position taking into account worst case scenarios, based on its own past experiences as well as industry level guidelines. The Bank has also put in place contingency plans to meet its liquidity obligations under stressed scenarios. The Bank is also holding near liquid assets (marketable assets) in its portfolio to meet its liquidity obligations. The liquidity positions are reported to the Board from time to time and the policy is reviewed periodically to meet the changing needs. The Bank is holding a Liquidity Asset Buffer in form of UK and US Treasury Bonds and balance with Bank of England to the extent of \$269,932 thousand as at 31 March 2014 (2013: \$192,588 thousand).

***Operational Risk (unaudited)***

Operational risk is defined as the potential risk of financial loss resulting from inadequate or failed internal process, systems, people or external events. Major sources of operational risks for the Bank are identified by management as IT security, internal and external fraud, process errors, money laundering risks and external events like failure of transportation, non-availability of utilities etc.

The Bank has identified each of such possible eventualities and established mitigation processes and internal controls, including IT Security Policy, maker checker for all financial transactions, a Business Continuity Plan in case of a disaster, documentation of processes and procedures, AML/CFT guidelines, staff handbook, TCF policy, anti-bribery policy, records retention policy, compliance code of conduct etc. These are tested periodically.

**34] Capital Management**

The Bank manages its capital base to maximise shareholders' value by optimising the level and mix of its capital resources. The Bank's authority to operate as a bank is dependent upon the maintenance of adequate capital resources. The Bank is required to meet minimum regulatory requirements in the UK and in other jurisdictions where regulated activities are undertaken. The Bank operates a centralised capital management model considering regulatory and economic capital. The Bank's capital management objectives are to:

- Maintain sufficient capital resources to meet the minimum regulatory capital requirements set by the Prudential Regulation Authority and the European Banking Authority.
- Maintain sufficient capital resources to support the Bank's risk appetite and economic capital requirements.
- Allocate capital to support the Bank's strategic objectives, including optimising returns on economic and regulatory capital.

**PUNJAB NATIONAL BANK (INTERNATIONAL) LIMITED**  
**NOTES TO THE FINANCIAL STATEMENTS (continued)**  
**FOR THE YEAR ENDED 31 MARCH 2014**

**34] Capital Management (continued)**

The actual capital of the Bank, including equity capital and Tier II capital eligible to be considered as capital based on the regulatory guidelines is as under:

Tier	Component	2014 \$'000	2013 \$'000
<b>Core Tier One Capital</b>	• Permanent Share Capital	149,631	99,631
	• Profit and Loss Account and Other Reserves	24,706	18,827
	• Available for Sale Reserve	(5,006)	125
		<u>169,331</u>	<u>118,583</u>
Deductions from Tier I	• Intangible Assets	(168)	(192)
	• Deferred Tax Assets	(20)	(49)
<b>Total Tier I Capital</b>	Core Tier I/ Tier I capital	<u>169,143</u>	<u>118,342</u>
Tier II Capital	• Perpetual Subordinated Debt	25,000	25,000
	• Long term dated subordinated debt	55,000	50,000
	• Collective Impairment Provision	3,508	493
		<u>83,508</u>	<u>75,493</u>
Deductions from Tier II	• Amortisation of Dated Tier II capital maturing within five years	(14)	-
<b>Total Tier II Capital</b>		<u>83,494</u>	<u>75,493</u>
Other Regulatory Deductions		-	-
<b>Total Capital</b>		<u>252,637</u>	<u>193,835</u>

The Bank is required at all times to monitor and demonstrate compliance with the relevant regulatory capital requirements of the Prudential Regulation Authority and those prescribed under Capital Requirement Regulations and Directives. The Bank has put in place processes and controls to monitor and manage the Bank's capital adequacy. No breaches were reported to the Prudential Regulation Authority during the year.

**35] Events after the Balance Sheet date**

There have been no reportable events after the balance sheet date.