

Bank of South Pacific Limited and Subsidiaries

Condensed financial statements

For the half-year ended

30 June 2020



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DIRECTORS' REPORT

The Directors of Bank of South Pacific Limited ("the Bank" or "BSP") present the financial report on the consolidated entity consisting of the Bank and its controlled entities (collectively referred to as "the Group") for the half-year ended 30 June 2020.

Directors and officers

The names of the Directors and officers of Bank of South Pacific Limited during or since the end of the half-year are:

Sir K G Constantinou, OBE	Mr R Fleming, CSM
Mr S Davis	Ms P Kevin (appointed 6 April 2020)
Mr G Robb, OAM	Mr E B Gangloff
Mr R Bradshaw	Mr A Mano (resigned 30 June 2020)
Mr A Sam	Dr F Lua'iufi

Principal activities

The principal activity of the Bank of South Pacific Limited (BSP) is the provision of commercial banking and finance services. The Group's activities also include fund management and life business services throughout Papua New Guinea and the Asia Pacific region. BSP is a company listed on the PNGX Exchange Markets Limited (PNGX), incorporated under the Companies Act of Papua New Guinea, and is an authorised Bank under the Banks and Financial Institutions Act of Papua New Guinea. The Group is also licensed to operate in the Solomon Islands, Fiji, Cook Islands, Samoa, Tonga, Vanuatu, Cambodia and Laos. The registered office is at Section 34, Allotment 6 & 7, Klinki Street, Waigani Drive, Port Moresby.

Review of operations

The net profit of the Group for the half year ended 30 June 2020, after tax was K381.940 million (half year ended 30 June 2019: K434.909 million).

In the directors' opinion, the attached condensed financial statements and notes thereto are in accordance with the PNG Companies Act 1997, including compliance with accounting standards and giving a true and fair view of the financial position and performance of the Bank and the Group.

Dated and signed at Port Moresby this 19th day of August 2020.



Sir Kostas Constantinou, OBE
Chairman



Robin Fleming, CSM
Chief Executive Officer/ Director



Report on review of interim financial information to the Directors of Bank of South Pacific Limited

Introduction

We have reviewed the accompanying condensed interim statements of financial position of Bank of South Pacific Limited (the Bank) and its subsidiaries (the Group) as at 30 June 2020 and the related condensed interim statements of comprehensive income, changes in shareholders' equity and cash flows for the six-month period then ended and notes, comprising a summary of significant accounting policies and other explanatory notes. The Directors are responsible for the preparation and presentation of this condensed interim financial information in accordance with International Accounting Standard 34, 'Interim Financial Reporting'. Our responsibility is to express a conclusion on this condensed interim financial information based on our review.

Scope of review

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

Conclusion


Based on our review, nothing has come to our attention that causes us to believe that the accompanying condensed interim financial information is not prepared, in all material respects, in accordance with International Accounting Standard 34, 'Interim Financial Reporting'.

Restriction on distribution or use

This report is made solely to the Directors of the Bank, as a body. Our review work has been undertaken so that we might state to the Directors those matters which we are required to state to them in our review report and for no other purpose. We do not accept or assume responsibility to anyone other than the Directors of the Bank, as a body, for our review work, for this report or for the conclusion we have formed.



PricewaterhouseCoopers



Peter Buchholz
Engagement Leader



Alison Judd
Partner
Registered under the Accountants Act 1996

Port Moresby
19 August 2020

PricewaterhouseCoopers,

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CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE HALF YEAR ENDED 30 JUNE 2020

	Note	Group		Bank	
		Half Year Ended 30 June	Half Year Ended 30 June	Half Year Ended 30 June	Half Year Ended 30 June
		2020	2019	2020	2019
<i>All amounts expressed are in K'000</i>					
Interest income	2(a)	786,429	792,945	733,082	739,178
Interest expense	2(a)	(76,055)	(98,849)	(70,203)	(90,659)
Net interest income		710,374	694,096	662,879	648,519
Fee and commission income	2(b)	174,211	187,287	158,085	169,335
Other income	2(c)	162,393	174,236	178,671	205,958
Net banking operating income		1,046,978	1,055,619	999,635	1,023,812
Net insurance premium income		78,687	76,529	-	-
Investment revenue		69,749	90,672	-	-
Increase in policy liabilities		(11,840)	(27,850)	-	-
Policy maintenance and investment expense		(75,217)	(70,625)	-	-
Claims, surrender and maturities		(54,611)	(55,541)	-	-
Share of profits from associates and jointly controlled entities		-	1,785	-	-
Net insurance operating income		6,768	14,970	-	-
Net operating income before impairment and operating expenses		1,053,746	1,070,589	999,635	1,023,812
Impairment on financial assets	2(d)	(111,450)	(50,431)	(103,832)	(43,639)
Operating expenses	2(e)	(405,186)	(411,732)	(369,427)	(372,218)
Profit before income tax		537,110	608,426	526,376	607,955
Income tax expense		(155,170)	(173,517)	(145,565)	(164,615)
Net profit for the period		381,940	434,909	380,811	443,340
Other comprehensive income					
<i>Items that may be subsequently reclassified to profit or loss</i>					
Translation of financial information of foreign operations to presentation currency		2,774	6,202	305	3,248
<i>Items that will not be reclassified to profit or loss</i>					
Fair value gain on remeasurement of investment securities		38	(105)	38	(105)
Net movement in asset revaluation, net of tax		(341)	(3,397)	-	(2,910)
Other comprehensive income, net of tax		2,471	2,700	343	233
Total comprehensive income for the period		384,411	437,609	381,154	443,573
Earnings per share – Basic and diluted (toea)		81.7	93.1	81.5	94.9

The attached notes form an integral part of these condensed financial statements.

CONDENSED STATEMENTS OF FINANCIAL POSITION

AS AT 30 JUNE 2020

	Note	Group		Bank	
		As at 30 June 2020	As at 31 December 2019	As at 30 June 2020	As at 31 December 2019
<i>All amounts expressed are in K'000</i>					
ASSETS					
Cash and balances with Central Bank		1,575,216	1,816,564	1,233,152	1,510,406
Treasury and Central Bank bills		2,675,896	2,459,497	2,640,096	2,420,088
Amounts due from other banks		1,125,054	1,022,469	1,087,230	997,816
Statutory deposits with Central Banks		1,390,681	1,766,601	1,315,480	1,693,300
Other financial assets		2,852,343	2,121,071	2,263,975	1,572,755
Loans, advances and other receivables from customers	4	13,164,325	13,200,807	11,785,935	11,819,970
Tax receivable		12,602	27,588	14,291	30,275
Other assets		328,261	366,994	273,556	276,618
Property, plant and equipment		862,008	879,942	682,866	698,755
Assets subject to operating lease		45,983	48,133	45,983	48,133
Investment in associates and joint ventures		210,775	202,040	20,781	20,787
Investment in subsidiaries		-	-	385,078	378,263
Intangible assets		194,250	196,206	178,364	177,601
Investment properties		224,158	168,360	-	-
Deferred tax assets		272,653	250,846	256,440	246,086
Total assets		24,934,205	24,527,118	22,183,227	21,890,853
LIABILITIES					
Amounts due to other banks		147,084	83,931	215,622	162,145
Customer deposits		19,499,643	19,339,056	18,148,631	17,981,756
Other liabilities		1,980,514	1,751,894	888,669	759,755
Deferred tax liabilities		41,202	31,542	-	-
Other provisions		215,735	203,662	197,122	186,574
Total liabilities		21,884,178	21,410,085	19,450,044	19,090,230
SHAREHOLDERS' EQUITY					
Ordinary shares		372,262	372,310	372,262	372,310
Retained earnings		2,324,559	2,394,382	2,106,101	2,173,836
Other reserves		348,984	346,513	254,820	254,477
Equity attributable to the members of the Bank		3,045,805	3,113,205	2,733,183	2,800,623
Minority interest		4,222	3,828	-	-
Total shareholders' equity		3,050,027	3,117,033	2,733,183	2,800,623
Total equity and liabilities		24,934,205	24,527,118	22,183,227	21,890,853

The attached notes form an integral part of these condensed financial statements.

CONDENSED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

FOR THE HALF-YEAR ENDED 30 JUNE 2020

<i>All amounts expressed are in K'000</i>	Share Capital	Reserves	Retained earnings	Minority interest	Total
GROUP					
Balance at 1 January 2020	372,310	346,513	2,394,382	3,828	3,117,033
Net profit	-	-	381,940	-	381,940
Other comprehensive income	-	2,471	-	-	2,471
Total comprehensive income	-	2,471	381,940	-	384,411
2019 final dividend paid	-	-	(451,369)	-	(451,369)
Share buyback	(48)	-	-	-	(48)
Profit attributed to minority interest	-	-	(394)	394	-
Total transaction with owners	(48)	-	(451,763)	394	(451,417)
Balance at 30 June 2020	372,262	348,984	2,324,559	4,222	3,050,027
Balance at 1 January 2019					
Balance at 1 January 2019	372,364	339,320	2,156,873	3,578	2,872,135
Net profit	-	-	434,909	-	434,909
Other comprehensive income	-	2,700	-	-	2,700
Total comprehensive income	-	2,700	434,909	-	437,609
2018 final dividend paid	-	-	(475,173)	-	(475,173)
Share buyback	(37)	-	-	-	(37)
Profit attributed to minority interest	-	-	3	(3)	-
Total transaction with owners	(37)	-	(475,170)	(3)	(475,210)
Transfer from asset revaluation reserve	-	(3,205)	3,205	-	-
Balance at 30 June 2019	372,327	338,815	2,119,817	3,575	2,834,534
BANK					
Balance at 1 January 2020	372,310	254,477	2,173,836	-	2,800,623
Net profit	-	-	380,811	-	380,811
Other comprehensive income	-	343	-	-	343
Total comprehensive income	-	343	380,811	-	381,154
2019 final dividend paid	-	-	(448,546)	-	(448,546)
Share buyback	(48)	-	-	-	(48)
Total transaction with owners	(48)	-	(448,546)	-	(448,594)
Balance at 30 June 2020	372,262	254,820	2,106,101	-	2,733,183
Balance at 1 January 2019					
Balance at 1 January 2019	372,364	252,384	1,976,138	-	2,600,886
Net profit	-	-	443,340	-	443,340
Other comprehensive income	-	233	-	-	233
Total comprehensive income	-	233	443,340	-	443,573
2018 final dividend paid	-	-	(471,915)	-	(471,915)
Share buyback	(37)	-	-	-	(37)
Total transaction with owners	(37)	-	(471,915)	-	(471,952)
Movement in asset revaluation reserve	-	(3,205)	3,205	-	-
Balance at 30 June 2019	372,327	249,412	1,950,768	-	2,572,507

The attached notes form an integral part of these condensed financial statements.

CONDENSED STATEMENTS OF CASH FLOWS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

	Note	Group		Bank	
		Half Year Ended 30 June		Half Year Ended 30 June	
		2020	2019	2020	2019
<i>All amounts expressed are in K'000</i>					
CASH FLOW FROM OPERATING ACTIVITIES					
Interest received		763,696	791,518	774,898	721,198
Fees and other income		343,373	376,493	336,005	325,842
Interest paid		(86,210)	(91,290)	(81,342)	(83,256)
Amounts paid to suppliers and employees		(364,853)	(348,612)	(352,131)	(308,988)
Operating cash flow before changes in operating assets and liabilities		656,006	728,109	677,430	654,796
Increase in loans, advances and other receivables from customers		(51,482)	(547,354)	(47,417)	(488,995)
(Decrease)/increase in customer deposits		160,587	(145,214)	166,875	(157,765)
(Increase)/Decrease in statutory deposits with the Central Banks		375,920	16,647	377,820	21,660
Increase in other assets		(3,069)	(175,799)	(12,288)	(117,846)
Increase/(decrease) in other liabilities		65,674	(58,513)	(48,679)	(118,648)
Net cash flow from / (used in) operating activities		1,203,636	(182,124)	1,113,741	(206,798)
Income taxes paid		(152,293)	(151,276)	(139,563)	(138,153)
Net cash flow from / (used in) operating activities		1,051,343	(333,400)	974,178	(344,951)
CASH FLOW FROM INVESTING ACTIVITIES					
(Increase) / decrease in government securities		(947,633)	357,936	(911,190)	424,192
Expenditure on property, plant and equipment		(60,561)	(65,644)	(53,488)	(60,785)
Proceeds for disposal of property, plant and equipment		326	7,061	285	7,061
Additional funding of subsidiaries		-	-	(6,066)	(6,208)
Net cash flow from/(used in) investing activities		(1,007,868)	299,353	(970,459)	364,260
CASH FLOW FROM FINANCING ACTIVITIES					
Share buyback		(48)	(37)	(48)	(37)
Dividends paid		(451,369)	(475,173)	(448,546)	(471,915)
Principle and interest repayments of borrowings		(26,135)	(13,328)	(26,134)	(13,328)
Proceeds from borrowing		229,387	-	229,387	-
Net cash flow used in financing activities		(248,165)	(488,538)	(245,341)	(485,280)
Net increase/(decrease) in cash and cash equivalents		(204,690)	(522,585)	(241,622)	(465,971)
Effect of exchange rate movements on cash and cash equivalents		2,774	6,202	305	3,248
Cash and cash equivalent at the beginning of the year		2,755,102	2,055,929	2,346,077	1,646,868
Cash and cash equivalents at the end of the period	10	2,553,186	1,539,546	2,104,760	1,184,145

The attached notes form an integral part of these condensed financial statements.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

1. Statement of significant accounting policies

1.1 Statement of compliance

The half-year report is prepared in accordance with International Financial Reporting Standard IAS 34 'Interim Financial Reporting' as well as the requirements of the Companies Act 1997. The half-year financial report does not include notes of the type normally included in an annual financial report and should be read in conjunction with the most recent annual financial report.

1.2 Basis of preparation

The condensed financial statements are denominated in Papua New Guinea Kina, which is the reporting currency of the Group. All financial information presented in Papua New Guinea Kina has been rounded to the nearest thousand Kina, unless otherwise stated.

The condensed financial statements have been prepared on the basis of historical cost, except for the revaluation of certain non-current assets and financial instruments. Cost is based on the fair values of the consideration given in exchange for assets.

The accounting policies and methods of computations adopted in preparation of the half-year financial report are consistent with those adopted and disclosed in the Group's 2019 financial report for the financial year ended 31 December 2019.

1.3 Critical Accounting estimates and judgments

The application of the Group's accounting policies requires the use of estimates and assumptions. If different assumptions or estimates were applied, the resulting values would change, impacting the net assets and income of the Group.

This note provides an overview of the areas that involve a higher degree of judgement or complexity, and major sources of estimation uncertainty that have a significant risk of resulting in a material adjustment within the next financial year. Detailed information about each of these estimates and judgements is included in the related notes together with information about the basis of calculation for each affected line item in the financial statements.

The areas involving significant estimates of judgments are:

- Estimated impairment of financial or non-financial assets
- Estimated goodwill impairment
- Estimated insurance liability
- Estimation of fair value of financial assets and liabilities
- Estimation of fair value of non-financial assets

Measurement of credit loss allowance for financial assets measured at amortised cost in line with IFRS 9 is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses).

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

1.3 Critical Accounting estimates and judgements (continued)

A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for significant increase in credit risk;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL.

The loan loss provisioning remains a significant risk and involves a high level of judgement. The quantum of ECL provisioning has increased reflecting the tighter economic conditions being experienced in across all regions which the Bank operates due to COVID-19 related measures.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 30 JUNE 2020

2. Operating profit before income tax

Operating profit before income tax is determined after including:

(a) Net interest income

	Half Year Ended		Half Year Ended	
	30 June		30 June	
<i>All amounts expressed are in K'000</i>	2020	2019	2020	2019
Interest Income				
Loans, advances and other receivables from customers	613,266	608,199	556,520	552,121
Treasury bills	76,567	76,511	75,965	75,749
Other financial assets - Inscribed stock	94,854	105,149	94,671	105,010
Other	1,742	3,086	5,926	6,298
	786,429	792,945	733,082	739,178
<i>Less:</i>				
Interest Expense				
Customer deposits	69,898	85,363	63,515	76,664
Other banks	4,006	10,095	4,746	10,604
Subordinated debt securities	2,151	3,391	1,942	3,391
	76,055	98,849	70,203	90,659
	710,374	694,096	662,879	648,519

(b) Fee and commission income

Product related	87,940	90,811	81,136	84,333
Trade and international related	9,270	10,580	8,895	10,137
Electronic banking related	59,492	67,990	56,761	63,030
Other	17,509	17,906	11,293	11,835
	174,211	187,287	158,085	169,335

(c) Other income

Foreign exchange related	145,207	160,775	130,425	143,748
Operating lease rentals	3,751	3,751	3,751	3,751
Other*	13,435	9,710	44,495	58,459
	162,393	174,236	178,671	205,958

*Other income for Bank includes K32.6 million (2019:K49.4 million) dividends received from subsidiaries, which is eliminated upon consolidation.

(d) Impairment on financial assets

New write offs	41,826	47,559	40,984	46,752
Net increase in provisions	98,121	35,449	90,989	28,631
Recoveries during the period	(31,303)	(29,921)	(30,975)	(29,091)
Provisions on Government Securities	2,806	(2,656)	2,834	(2,653)
	111,450	50,431	103,832	43,639

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

2. Operating profit before income tax (continued)

(e) Operating expenses

	Group		Bank	
	Half year ended 30 June		Half year ended 30 June	
	2020	2019	2020	2019
<i>All amounts expressed are in K'000</i>				
Staff costs	188,970	195,763	173,504	180,106
Depreciation	62,304	58,061	57,797	53,663
Computing	66,782	62,597	55,474	55,578
Premises and equipment	30,896	32,312	28,976	28,863
Administration and other costs	56,234	62,999	53,676	54,008
	405,186	411,732	369,427	372,218

3. Dividends

On 22 May 2020, the directors declared a final dividend of 96 toea per share for the year ended 31 December 2019 which was paid on 19 June 2020. The declared final gross dividend amount was K451.369 million (June 2019: K475.173 million). Net dividend paid after dividend withholding tax was K444.636 million (June 2019: K464.163 million).

4. Loans, advances and other receivables from customers

	Group		Bank	
	As at 30 June	As at 31 December	As at 30 June	As at 31 December
	2020	2019	2020	2019
<i>All amounts expressed are in K'000</i>				
Gross loans, advances and other receivables from customers net of reserved interest	13,952,894	13,901,411	12,513,973	12,466,557
Less allowances for losses on loans, advances and other receivables from customers	(788,569)	(700,604)	(728,038)	(646,587)
Net loans, advances and other receivables from customers	13,164,325	13,200,807	11,785,935	11,819,970
<i>Economic sector risk concentrations</i>				
Commerce, finance and other business	7,243,561	7,159,863	6,473,712	6,327,586
Private households	3,149,565	2,987,459	2,740,594	2,636,736
Government and public authorities*	178,285	252,134	169,699	237,209
Agriculture	343,715	327,151	327,083	310,334
Transport and communication	1,027,184	1,311,306	949,614	1,223,612
Manufacturing	336,967	332,344	296,634	303,435
Construction	885,048	830,550	828,599	781,058
	13,164,325	13,200,807	11,785,935	11,819,970

*Total by Government ownership at 30 June 2020 was K2,399 million (31 December 2019: K2,511 million).

NOTES TO THE CONDENSED FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 30 JUNE 2020

5. Maximum exposure to credit risk, collateral and other credit enhancements

The following table contains an analysis of the credit risk exposure of financial instruments for which an Expected Credit Loss allowance is recognised. The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets, including off balance sheet items.

ECL staging	As at June 2020				As At December 2019
	Stage 1	Stage 2	Stage 3	Total	Total
(PGK'000)	12-month ECL	Lifetime ECL	Lifetime ECL		
Credit grade					
Standard monitoring	14,342,020	1,658,433	-	16,000,453	15,583,408
Special monitoring	-	485,844	-	485,844	503,009
Default	-	-	487,046	487,046	391,688
Gross carrying amount	14,342,020	2,144,277	487,046	16,973,343	16,478,105
Loss allowance	(270,697)	(263,612)	(254,260)	(788,569)	(700,604)
Carrying amount	14,071,323	1,880,665	232,786	16,184,774	15,777,501

The Group employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation. The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period.

The Group closely monitors collateral held for financial assets considered to be credit-impaired, as it becomes more likely that the Group will take possession of collateral to mitigate potential credit losses. Financial assets that are credit-impaired and related collateral held in order to mitigate potential losses are shown below:

	Gross exposure	Impairment allowance	Carrying amount	Fair value of collateral held
Credit-impaired assets	PGK'000	PGK'000	PGK'000	PGK'000
Loans to individuals:				
• Overdrafts	666	423	243	1,022
• Credit cards	1,175	503	672	1,968
• Term loans	32,831	14,601	18,230	31,179
• Mortgages	113,981	41,870	72,111	174,225
Loans to corporate entities:				
• Large corporate customers	281,919	164,664	117,255	227,445
• Small and medium-sized enterprises (SMEs)	56,197	32,066	24,131	67,701
• Other	277	133	144	118
Total credit-impaired assets	487,046	254,260	232,786	503,658

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

6. Capital adequacy and liquid assets ratio

The Group is required to comply with various prudential standards issued by the Bank of Papua New Guinea (BPNG), the official authority for the prudential supervision of banks and similar financial institutions in Papua New Guinea. Additionally, subsidiaries and branches in Fiji, Solomon Islands, Cooks Islands, Samoa, Tonga, Vanuatu, Cambodia and Laos are required to adhere to prudential standards issued by the Reserve Bank of Fiji, Central Bank Solomon Islands, The Financial Supervisory Commission, Central Bank of Samoa, National Reserve Bank of Tonga, Reserve Bank of Vanuatu, National Bank of Cambodia and Bank of Laos P.D.R. respectively. One of the most critical prudential standards is the capital adequacy requirement. All banks are required to maintain at least the minimum measure of capital to risk-weighted assets to absorb potential losses. The BPNG follows the prudential guidelines set by the Bank of International Settlements under the terms of the Basel Accord. The BPNG revised prudential standard 1/2003, Capital Adequacy, prescribes ranges of overall capital ratios to measure whether a Bank is under, adequately, or well-capitalized, and also specifies the leverage capital ratio. The Group complies with the prevailing prudential requirements for total capital and leverage capital. As at 30 June 2020, the Group's total capital adequacy ratio and leverage capital ratio satisfied the capital adequacy criteria for a 'well-capitalised' bank. The minimum capital adequacy requirements as set out under the standard is as follows: capital adequacy ratio for Tier 1 is 8%, total capital adequacy is 12% and the leverage capital ratio is 6%.

The measure of capital used for the purposes of prudential supervision is referred to as base capital. Total base capital varies from the balance of capital shown on the Statement of Financial Position and is made up of tier 1 capital (core) and tier 2 capital (supplementary). Tier 1 capital is obtained by deducting from equity capital and audited retained earnings (or losses), intangible assets including deferred tax assets. Tier 2 capital cannot exceed the amount of tier 1 capital, and can include subordinate loan capital, specified asset revaluation reserves, un-audited profits (or losses) and a small percentage of general loan loss provisions. The leverage capital ratio is calculated as Tier 1 capital divided by total assets on the balance sheet.

Risk weighted assets are derived from on-balance sheet and off-balance sheet assets. On-balance sheet assets are weighted for credit risk by applying weightings (0, 20, 50 and 100 per cent) according to risk classification criteria set by the BPNG. Off-balance sheet exposures are risk weighted in the same way after converting them to on-balance sheet credit equivalents using BPNG specified credit conversion factors.

<i>Risk weighted capital ratios</i>	As at 30 June 2020		As at 31 Dec 2019	
	K'000	%	K'000	%
Tier 1 capital	2,058,044	16.0%	2,526,509	19.5%
Total capital	2,747,227	21.3%	2,848,723	22.0%
Leverage capital ratio		8.4%		10.5%

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

7. Contingent liabilities and commitments

The primary purpose of credit related commitments are to ensure that funds are available to a customer as required. Guarantees and standby letters of credit, which represent irrevocable assurances that the bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans. Cash requirements under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Group do not generally expect the third party to draw funds under the agreement.

Commitments to extend credit represent the unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss, though not difficult to quantify, is considerably less than the total unused commitments since most commitments to extend credit are subject to customers maintaining approved specific credit standards. While there is credit risk associated with the remainder of commitments, the risk is considered to be modest, since it results from the possibility of unused portions of loan authorisations being drawn by the customer and, second, from these drawings subsequently not being repaid as due. The total outstanding contractual amount of commitments to extend does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

The Bank operates in a number of regulated markets and is subject to regulatory reviews and inquiries. From time to time these may result in fines or other regulatory enforcement actions. As at reporting date there are no matters of this nature for which the Bank expects to result in a material economic outflow of resources.

Off-balance sheet financial instruments

The following table indicates the contractual amounts of the Bank and Group's off-balance sheet financial instruments that commit it to extend credit to customers.

	Group		Bank	
	As at 30 June 2020	As at 31 December 2019	As at 30 June 2020	As at 31 December 2019
<i>All amounts expressed are in K'000</i>				
Letters of credit	113,081	121,600	111,677	117,057
Guarantees and indemnities issued	294,850	366,170	277,551	341,373
Commitments to extend credit	2,615,847	2,088,924	2,533,858	2,003,881
	3,023,778	2,576,694	2,923,086	2,462,311

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

7. Contingent liabilities and commitments (continued)

Commitments for capital expenditure

Amounts with firm commitments, and not included in the accounts as at 30 June 2020 amounted to K48 million (31 December 2019: K55.8 million).

Contingent liability

A number of legal proceedings against the Group were outstanding as at 30 June 2020. Based on information available at 30 June 2020, the Group estimates a contingent liability of K15.8 million in respect of these proceedings (31 December 2019: K15.8 million). The Bank operates in a number of regulated markets and is subject to regulatory reviews and inquiries. From time to time these may result in fines or other regulatory enforcement actions. As at reporting date there are no matters of this nature for which the Bank expects to result in a material economic outflow of resources.

Operating lease commitments – predominantly residential premises

	Group		Bank	
	As at 30 June 2020	As at 31 December 2019	As at 30 June 2020	As at 31 December 2019
<i>All amounts expressed are in K'000</i>				
Not later than 1 year	8,961	13,768	8,013	12,754
Later than 1 year and not later than 5 years	2,263	2,617	13	73
Later than 5 years	688	824	-	18
	11,912	17,209	8,026	12,845

Includes leases not in the scope of IFRS 16.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS FOR THE HALF-YEAR ENDED 30 JUNE 2020

8. Derivative financial instruments

In the normal course of trading, the Bank and Group enter into forward exchange contracts. The Group do not actively enter into or trade in complex forms of derivative financial instruments such as currency and interest rate swaps and options.

Exposures in foreign currencies arise where the Group transacts in foreign currencies. This price risk is minimised by entering into counterbalancing positions for material exposures as they arise. Forward and spot foreign exchange contracts are used.

Forward exchange contracts outstanding, stated at the face value of the respective contracts are:

All amounts expressed are in '000

As at 30 June 2020		USD	AUD	EURO	GBP	JPY	Others	Total
Selling	FCY	(72,108)	(38,427)	(1,630)	(166)	(150,003)	(3,279)	
	Kina	(249,510)	(91,221)	(6,330)	(705)	(4,816)	(3,773)	(356,355)
Buying	FCY	24,016	43,500	-	666	35,000	51,645	
	Kina	83,101	103,264	-	2,830	1,124	113,667	303,986

As at 31 December 2019		USD	AUD	EURO	GBP	JPY	Others	Total
Selling	FCY	(49,183)	(2,529)	(900)	(21)	(181,179)	(2,110)	
	Kina	(182,945)	(6,039)	(3,437)	(90)	(5,525)	(7,189)	(205,225)
Buying	FCY	8,132	14,800	20	1,200	137,500	34,444	
	Kina	44,307	35,133	78	5,099	4,415	119,183	208,215

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

9. Related parties

Related parties are considered to be enterprises or individuals with whom the Group is especially related because either they or the Group are in a position to significantly influence the outcome of transactions entered into with the Group, by virtue of being able to control, dominate or participate in a fiduciary capacity, in decision-making functions or processes. The Group conducted transactions with the following classes of related parties during the period:

- Directors and/or parties in which a director has significant influence.
- Key management personnel and other staff and/or parties in which the individual officer has significant influence.

A number of banking transactions are entered into with these related parties in the normal course of business, and include loans, deposits, property rentals, share transfers and foreign currency transactions.

Significant related party balances relating to loans and advances to customers are as follows:

	Group	
	As at 30 June 2020	As at 31 December 2019
<i>All amounts expressed are in K'000</i>		
Loans to :		
Parties where the related party is a director	519,224	867,741
Parties where the related party is an executive	45,238	37,022
General staff	9,425	9,705
	573,887	914,468

10. Notes to condensed statements of cash flows

For the purpose of the cash flow statements, cash and cash equivalents comprise the following balances with less than 90 days maturity.

	Group		Bank	
	As at 30 June		As at 30 June	
	2020	2019	2020	2019
<i>All amounts expressed are in K'000</i>				
Cash and balances with Central Banks	1,575,216	1,180,815	1,233,152	934,970
Amounts due from other banks	1,125,054	763,091	1,087,230	694,054
Amounts due to other banks	(147,084)	(404,360)	(215,622)	(444,879)
	2,553,186	1,539,546	2,104,760	1,184,145

The Group undertakes thorough compliance and due diligence reviews before entering into any correspondent banking relationships. Amounts due from other banks includes deposit of K31.406 million (December 2019: K31.275 million) held with counter-party Banks that are not available for use by the Group.

NOTES TO THE CONDENSED FINANCIAL STATEMENTS

FOR THE HALF-YEAR ENDED 30 JUNE 2020

11. Segment information

The following is an analysis of the Group's revenue and results by reportable operating segment for the periods under review:

All amounts expressed are in K'000

Half Year Ended 30 June 2020	PNG Bank	Non PNG Banks	Non Bank Entities	Adjust Inter Segments	Total
Interest income	598,975	179,707	17,969	(10,222)	786,429
Interest expense	(35,161)	(50,647)	(2,144)	11,897	(76,055)
Net Interest income	563,814	129,060	15,825	1,675	710,374
Other income	232,543	97,467	10,406	(3,812)	336,604
Net insurance income	-	-	8,921	(2,153)	6,768
Total operating income	796,357	226,527	35,152	(4,290)	1,053,746
Operating expenses	(294,681)	(104,265)	(9,350)	3,110	(405,186)
Impairment expenses	(76,156)	(31,680)	(3,614)	-	(111,450)
Profit before income tax	425,520	90,582	22,188	(1,180)	537,110
Income tax	(128,237)	(22,617)	(4,316)	-	(155,170)
Net profit after income tax	297,283	67,965	17,872	(1,180)	381,940
Total Assets	17,084,459	7,443,656	1,814,041	(1,407,951)	24,934,205
Total Liabilities	(14,855,460)	(6,462,085)	(1,362,661)	796,028	(21,884,178)
Half year Ended 30 June 2019					
Interest income	612,094	173,578	17,737	(10,464)	792,945
Interest expense	(52,072)	(54,992)	(2,493)	10,708	(98,849)
Net interest income	560,022	118,586	15,244	244	694,096
Other income	237,765	118,390	8,925	(3,557)	361,523
Net insurance income	-	-	14,616	354	14,970
Total operating income	797,787	236,976	38,785	(2,959)	1,070,589
Operating expenses	(290,918)	(113,049)	(10,488)	2,723	(411,732)
Impairment expenses	(31,527)	(16,820)	(2,084)	-	(50,431)
Profit before income tax	475,342	107,107	26,213	(236)	608,426
Income tax	(142,492)	(27,421)	(3,604)	-	(173,517)
Net profit after income tax	332,850	79,686	22,609	(236)	434,909
Total Assets	16,980,168	7,393,898	1,628,588	(1,475,536)	24,527,118
Total Liabilities	(14,598,007)	(6,489,778)	(1,229,019)	906,719	(21,410,085)

12. Subsequent events

There are no adjusting or disclosing events after the end of the reporting period.