Bank of South Pacific Limited and Subsidiaries

Financial Statements

31 December 2019

Contents of Financial Statements

Directors' Report
for the Year Ended 31 December 2019

The Directors take pleasure in presenting the Financial Statements of the Bank of South Pacific Limited and its subsidiaries (Bank and the Group) for the year ended 31 December 2019. In order to comply with the provisions of the Companies Act 1997, the Directors report as follows:

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 PNG Exchange Markets (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 and Cambodia. The registered office is at Section 34, Allotment 6 & 7, Klinki Street, Waigani Drive, Port Moresby.

Review of operations

For the year ended 31 December 2019, the Group's profit after tax was K890.363 million (2018: K844.072 million). The Bank's profit after tax was K845.828 million (2018: K787.446 million).

The Directors are of the view that there are reasonable grounds to believe that the Bank and the Group will be able to pay their debts as and when they become due and payable; and the attached financial statements and notes thereto are in accordance with the PNG Companies Act 1997, including compliance with accounting standards and give a true and fair view of the financial position and performance of the Bank and the Group.

The results of the Bank and the Group operations during the financial year have, in the opinion of the Directors, not been materially affected by items of an abnormal nature, other than those disclosed in the financial statements.
In the opinion of the Directors, no circumstances have arisen, that make adherence to the existing method of valuation of assets or liabilities of the Bank and the Group misleading or inappropriate.

At the date of this report the Directors are not aware of any circumstances that would render the values attributed to current assets in the financial statements misleading.

No contingent liability other than that disclosed in the notes to the attached financial statements has become enforceable, or is likely to become enforceable, within a period of twelve months from the date of this report, that will materially affect the Bank and the Group in its ability to meet obligations as and when they fall due.

Dividends

Dividend totalling K653.940 million were paid in 2019 (2018: K597.364 million). A detailed breakup of this is provided in Note 24.

Directors and officers

The following were directors of the Bank of South Pacific Limited at 31 December 2019:

Sir K Constantinou, OBE	Mr. R Fleming, CSM	Mr. S Davis
Mr. E B Gangloff	Mr. A Mano	Mr. R Bradshaw
Mr. G Robb, OAM	Dr. F Lua'iufi	Mr. A Sam

Details of directors' tenure and directors and executives' remuneration during the year are provided in Note 28 of the Notes to the Financial Statements. The CEO Robin Fleming is the only executive director.

The company secretary is Mary Johns.

Independent auditor's report

The financial statements have been audited and should be read in conjunction with the independent auditor's report on page 64. Details of amounts paid to the auditors for audit and other services are shown in Note 42 of the Notes to the Financial Statements.

Donations and sponsorships

Donations and sponsorship by the Group during the year amounted to K5.581 million (2018: K8.004 million).

Change in accounting policies

Changes to accounting policies that impacted the Group's result during the year are included in Note 1(A) of the Notes to the Financial Statements.

For, and on behalf of, the Directors.

Dated and signed in accordance with a resolution of the Directors in Port Moresby this 26th day of February 2020.

Sir Kostas Constantinou, OBE
Chairman

Robin Fleming, CSM
Group Chief Executive Officer/
Managing Director

Statements of Comprehensive Income

for the Year Ended 31 December 2019

		Consolidated		Bank	
All amounts are expressed in K'000	**Note**	**2019**	**2018**	**2019**	**2018**
Interest income	2	1,585,773	1,561,691	1,477,235	1,460,484
Interest expense	2	(193,989)	(180,895)	(180,464)	(166,090)
Net interest income		1,391,784	1,380,796	1,296,771	1,294,394
Fee and commission income	3	384,761	382,508	346,951	347,892
Other income	4	364,130	363,488	373,366	353,528
Net banking operating income		**2,140,675**	**2,126,792**	**2,017,088**	**1,995,814**
Net insurance premium income		152,233	143,097	-	-
Investment revenue		168,829	156,547	-	-
Increase in policy liabilities	40(b)	(59,746)	(71,616)	-	-
Policy maintenance and investment expenses		(119,138)	(111,385)	-	-
Claims, surrender and maturities		(116,927)	(97,295)	-	-
Share of profits from associates and jointly controlled entities		5,424	19,565	-	-
Net insurance operating income	40(a)	30,675	38,913	-	-
Net operating income before impairment and operating expenses		2,171,350	2,165,705	2,017,088	1,995,814
Impairment on financial assets	5	(99,183)	(82,440)	(88,092)	(71,639)
Impairment on subsidiary	8	-	-	-	(803)
Operating expenses	5	(819,248)	(887,097)	(740,729)	(806,833)
Profit before income tax		**1,252,919**	**1,196,168**	**1,188,267**	**1,116,539**
Income tax expense	6	(362,556)	(352,096)	(342,439)	(329,093)
Net profit for the year		**890,363**	**844,072**	**845,828**	**787,446**
Other comprehensive income					
Items that may be subsequently reclassified to profit or loss					
Translation of financial information of foreign operations to presentation currency	25	10,620	1,052	5,493	1,267
Items that will not be reclassified to profit or loss:					
Recognition of deferred tax on asset revaluation reserve	25	3,642	4,948	3,664	5,435
Fair value gain on remeasurement of investment securities	25	(14)	8	(14)	8
Net movement in asset revaluation	25	(5,719)	1,624	(5,714)	-
Other comprehensive income, net of tax		**8,529**	**7,632**	**3,429**	**6,710**
Total comprehensive income for the year		**898,892**	**851,704**	**849,257**	**794,156**
Earnings per share - basic and diluted (toea)	24	**190.6**	**180.6**	**181.0**	**168.5**

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

Statements of Financial Position

As at 31 December 2019

All amounts are expressed in K'000	Note	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
ASSETS					
Cash and balances with Central Bank	10	1,816,564	1,253,449	1,510,406	966,707
Treasury and Central Bank bills	11	2,459,497	2,494,700	2,420,088	2,480,356
Amounts due from other banks	12	1,022,469	854,019	997,816	796,180
Statutory deposits with Central Banks		1,766,601	1,685,544	1,693,300	1,622,035
Other financial assets	17	2,121,071	2,555,443	1,572,755	2,073,873
Loans, advances and other receivables from customers	13	13,200,807	12,530,649	11,819,970	11,232,725
Property, plant and equipment	14	879,942	693,277	698,755	538,181
Assets subject to operating lease	14	48,133	52,433	48,133	52,433
Investment in joint ventures	9	202,040	175,579	20,787	20,038
Investment in subsidiaries	8	-	-	378,263	347,597
Intangible assets	7	196,206	174,623	177,601	152,551
Investment properties	16	168,360	153,665	-	-
Deferred tax assets	6	250,846	239,607	246,086	234,391
Tax receivable	6	27,588	12,753	30,275	17,020
Other assets	18	366,994	205,482	276,618	162,293
Total assets		**24,527,118**	**23,081,223**	**21,890,853**	**20,696,380**
LIABILITIES					
Amounts due to other banks	19	83,931	51,539	162,145	116,019
Customer deposits	20	19,339,056	18,232,766	17,981,756	16,959,170
Subordinated debt securities	21	-	75,525	-	75,525
Other liabilities	22	1,751,894	1,623,992	759,755	766,981
Deferred tax liabilities	6	31,542	31,163	-	-
Other provisions	23	203,662	194,103	186,574	177,799
Total liabilities		**21,410,085**	**20,209,088**	**19,090,230**	**18,095,494**
SHAREHOLDERS' EQUITY					
Ordinary shares	24	372,310	372,364	372,310	372,364
Retained earnings	25	2,394,382	2,156,873	2,173,836	1,976,138
Other reserves	25	346,513	339,320	254,477	252,384
Equity attributable to the members of the company		**3,113,205**	**2,868,557**	**2,800,623**	**2,600,886**
Minority interests		3,828	3,578	-	-
Total shareholders' equity		**3,117,033**	**2,872,135**	**2,800,623**	**2,600,886**
Total equity and liabilities		**24,527,118**	**23,081,223**	**21,890,853**	**20,696,380**

The attached notes form an integral part of these Financial Statements.

Statements of Changes in Shareholders' Equity

for the Year Ended 31 December 2019

All amounts are expressed in K'000	Note	Share capital	Reserves	Retained earnings	Minority Interests	Total
Bank						
Balance as at 1 January 2018		**373,001**	**260,374**	**1,777,627**	-	**2,411,002**
IFRS 9 transition provisions		-	-	(10,221)	-	(10,221)
Restated balance as at 1 January 2018		**373,001**	**260,374**	**1,767,406**	-	**2,400,781**
Net profit		-	-	787,446	-	787,446
Other comprehensive income	25	-	6,710	-	-	6,710
Total comprehensive income	25	-	6,710	787,446	-	794,156
Dividends paid during the year	25	-	-	(593,414)	-	(593,414)
Share buyback	24	(637)	-	-	-	(637)
Total transactions with owners		(637)	-	(593,414)	-	(594,051)
Transfer from Asset Revaluation Reserve	25	-	(18,116)	18,116	-	-
BSP Life policy reserve	25	-	3,416	(3,416)	-	-
Balance at 31 December 2018		**372,364**	**252,384**	**1,976,138**	-	**2,600,886**
Net profit		-	-	845,828	-	845,828
Other comprehensive income	25	-	3,429	-	-	3,429
Total comprehensive income	25	-	3,429	845,828	-	849,257
Dividends paid during the year	25	-	-	(649,466)	-	(649,466)
Share buyback	24	(54)	-	-	-	(54)
Total transactions with owners		(54)	-	(649,466)	-	(649,520)
Transfer from Asset Revaluation Reserve	25	-	(4,933)	4,933	-	-
BSP Life policy reserve	25	-	3,597	(3,597)	-	-
Balance at 31 December 2019		**372,310**	**254,477**	**2,173,836**	-	**2,800,623**
Group						
Balance as at 1 January 2018		**373,001**	**346,388**	**1,904,462**	**4,484**	**2,628,335**
IFRS 9 transition provisions		-	-	(9,903)	-	(9,903)
Restated balance as at 1 January 2018		**373,001**	**346,388**	**1,894,559**	**4,484**	**2,618,432**
Net profit		-	-	844,072	-	844,072
Other comprehensive income	25	-	7,632	-	-	7,632
Total comprehensive income	25	-	7,632	844,072	-	851,704
Dividends paid during the year	25	-	-	(597,364)	-	(597,364)
Share buyback	24	(637)	-	-	-	(637)
Loss attributable to minority interests	25	-	-	906	(906)	-
Total transactions with owners		(637)	-	(596,458)	(906)	(598,001)
Transfer from Asset Revaluation Reserve	25	-	(18,116)	18,116	-	-
BSP Life policy reserve	25	-	3,416	(3,416)	-	-
Balance at 31 December 2018		**372,364**	**339,320**	**2,156,873**	**3,578**	**2,872,135**
Net profit		-	-	890,363	-	890,363
Other comprehensive income	25	-	8,529	-	-	8,529
Total comprehensive income	25	-	8,529	890,363	-	898,892
Dividends paid during the year	25	-	-	(653,940)	-	(653,940)
Share buyback	24	(54)	-	-	-	(54)
Gain attributable to minority interests	25	-	-	(250)	250	-
Total transactions with owners		(54)	-	(654,190)	250	(653,994)
Transfer from asset revaluation reserve	25	-	(4,933)	4,933	-	-
BSP Life policy reserve	25	-	3,597	(3,597)	-	-
Balance at 31 December 2019		**372,310**	**346,513**	**2,394,382**	**3,828**	**3,117,033**

The attached notes form an integral part of these Financial Statements.

Statements of Cash Flows

for the Year Ended 31 December 2019

All amounts are expressed in K'000	Note	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
CASH FLOW FROM OPERATING ACTIVITIES					
Interest received		1,605,387	1,544,691	1,480,232	1,442,960
Fees and other income		779,565	784,910	719,567	680,110
Interest paid		(167,913)	(183,137)	(153,354)	(169,364)
Amounts paid to suppliers and employees		(776,812)	(722,282)	(646,339)	(628,865)
Operating cash flow before changes in operating assets & liabilities	29	**1,440,227**	**1,424,182**	**1,400,106**	**1,324,841**
Increase in loans, advances and other receivables to customers		(737,195)	(1,377,537)	(644,594)	(1,188,543)
Increase in statutory deposits with the Central Banks		(81,058)	(87,166)	(71,265)	(80,939)
Increase in bills receivable and other assets		(201,387)	(121,256)	(98,089)	(103,872)
Increase in customer deposits		1,106,290	446,549	1,022,586	250,889
Movement in bills payable and other liabilities		(184)	232,175	(207,231)	152,467
Net cash flow from operations before income tax		**1,526,693**	**516,947**	**1,401,513**	**354,843**
Income taxes paid	6	(383,287)	(420,430)	(363,837)	(402,213)
Net cash flow from/(used in) operating activities		**1,143,406**	**96,517**	**1,037,676**	**(47,370)**
CASH FLOW FROM INVESTING ACTIVITIES					
Decrease in government securities		429,961	695,907	561,386	785,053
Expenditure on property, plant and equipment		(82,780)	(32,766)	(79,249)	(25,804)
Expenditure on software development costs		(52,108)	(79,163)	(49,979)	(75,468)
Proceeds from disposal of property, plant and equipment		7,076	966	7,076	966
Additional funding of subsidiaries	8	-	-	(30,666)	(10,000)
Net cash flow used in investing activities		**302,149**	**584,944**	**408,568**	**674,747**
CASH FLOW FROM FINANCING ACTIVITIES					
Share buyback	24	(54)	(637)	(54)	(637)
Dividends paid	25	(653,940)	(597,364)	(649,466)	(593,414)
Principal repayments of borrowings	22	(61,153)	(102,866)	(61,153)	(102,866)
Proceeds from borrowings	22	33,670	80,273	33,670	80,273
Subordinate debt securities matured	21	(75,525)	-	(75,525)	-
Net cash flow used in financing activities		**(757,002)**	**(620,594)**	**(752,528)**	**(616,644)**
Net (decrease)/increase in cash and cash equivalents		**688,553**	**60,867**	**693,716**	**10,733**
Effect of exchange rate movements on cash and cash equivalents		10,620	1,052	5,493	1,267
Cash and cash equivalents at the beginning of the year	29	2,055,929	1,994,010	1,646,868	1,634,868
Cash and Cash Equivalents at the end of the year	29	**2,755,102**	**2,055,929**	**2,346,077**	**1,646,868**

The attached notes form an integral part of these Financial Statements.

1. Accounting Policies

The principal accounting policies adopted in the preparation of these Financial Statements are set out below. These policies have been consistently applied to all the periods presented unless otherwise stated. The assets and liabilities are presented in order of liquidity on the Statements of Financial Position.

A(i) Basis of Presentation and General Accounting Policies

The Financial Statements of the Bank of South Pacific Limited (the Bank) and the Group are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board and interpretations of these standards issued by the International Financial Reporting Interpretations Committee. They are prepared on the basis of the historical cost convention, as modified by the revaluation of certain non-current assets, financial instruments and liabilities.

Estimates and assumptions have been used to achieve conformity with generally accepted accounting principles in the preparation of these financial statements. These assumptions and estimates affect balances of assets and liabilities, contingent liabilities and commitments at the end of the reporting period, and amounts of revenues and expenses during the reporting period. Whilst the estimates are based on management's best knowledge of current events and conditions, actual results may ultimately differ from those estimates.

The financial statements are presented in Papua New Guinea Kina, expressed in thousands of Kina, as permitted by International Financial Reporting Standards.

Standards, amendments and interpretations effective in the year ended 31 December 2019

The following standards, amendments and interpretations to existing standards became applicable for the first time during the accounting period beginning 1 January 2019.

- IFRS 16, 'Leases' removes the previous IAS 17 distinction between finance leases and operating leases and now requires a lessee to recognise a lease liability representing future lease payments and a 'right-of-use asset' for virtually all lease contracts. There is an optional exemption for certain short-term leases and leases of low-value assets.
- Amendment to IFRS 9 on prepayment features with negative compensation. This amendment confirms that when a financial liability measured at amortised cost is modified without this resulting in de-recognition, a gain or loss should be recognised immediately in profit or loss. The gain or loss is calculated as the difference between the original contractual cash flows and the modified cash flows discounted at the original effective interest rate.
- IFRIC 23, 'Uncertainty over income tax treatments' clarifies how the recognition and measurement requirements of IAS 12 'Income Taxes' are applied where there is uncertainty over income tax positions. The IFRS IC had clarified previously that IAS 12, not IAS 37 'Provisions, contingent liabilities and contingent assets', applies to accounting for uncertain income tax treatments. IFRIC 23 explains how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment. A subsequent IC agenda decision also provided guidance on the presentation of uncertain tax positions.
- Annual improvements 2015 – 2017. These amendments include minor changes to:
  - IFRS 3 'Business combination' – a company remeasures its previously held interest in a joint operation when it obtains control of the business.
  - IFRS 11 'Joint arrangements' – a company does not remeasure its previously held interest in a joint operation when it obtains control of the business.
  - IAS 12 'Income taxes' – a company accounts for all income tax consequences of dividend payments in the same way.
  - IAS 23 "Borrowing costs' – a company treats as part of general borrowings any borrowings originally made to develop an asset when the asset is ready for its intended use or sale.
- Amendments to IAS 28 'Investments in associates' on long term interests in associates and joint ventures. These amendments clarify that long-term interests in an associate or joint venture to which the equity method is not applied should be accounted for using IFRS 9. This includes the impairment requirements in IFRS 9.
- Amendments to IAS 19, 'Employee benefits' on plan amendment, curtailment or settlement. These amendments require an entity to:

  - use updated assumptions to determine current service cost and net interest for the remainder of the period after a plan amendment, curtailment or settlement, and

  - recognise in profit or loss as part of past service cost, or a gain or loss on settlement, any reduction in a surplus, even if that surplus was not previously recognised because of the impact of the asset ceiling.

Standards, amendments and interpretations issued but not yet effective for the year ended 31 December 2019 or adopted early

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the entity's accounting periods beginning on or after 1 January 2020 or later periods, but the entity has not early adopted them:

- Amendments to IFRS 3 – definition of a business (effective 1 January 2020). This amendment revises the definition of a business. According to feedback received by the IASB, application of the current guidance is commonly thought to be too complex, and it results in too many transactions qualifying as business combinations.
- Amendments to IAS 1 and IAS 8 on the definition of 'material' (effective 1 January 2020). These amendments to IAS 1, 'Presentation of financial statements', and IAS 8, 'Accounting policies, changes in accounting estimates and errors', and consequential amendments to other IFRSs:
  - use a consistent definition of materiality throughout IFRSs and the Conceptual Framework for Financial Reporting
  - clarify the explanation of the definition of material; and
  - incorporate some of the guidance in IAS 1 about immaterial information.
- Amendments to IFRS 9, IAS 39 and IFRS 7 – interest rate benchmark reform (effective 1 January 2020). Following the financial crisis, the replacement of benchmark interest rates such as LIBOR and other inter-bank offered rates ('IBORs') has become a priority for global regulators. These amendments relate to hedge accounting and have the effect that IBOR reform should not generally cause hedge accounting to terminate. However, any hedge ineffectiveness should continue to be recorded in the income statement under both IAS 39 and IFRS 9. Furthermore, the amendments set out triggers for when the reliefs will end, which include the uncertainty arising from interest rate benchmark reform no longer being present.
- IFRS 17 'Insurance contracts" (effective 1 January 2022) replaces IFRS 4. IFRS 17 will fundamentally change the accounting by all entities that issue insurance contracts and investment contacts with discretionary participation features.

  It requires a current measurement model where estimates are re-measured at each reporting period. Contracts are measured using the building blocks of:
  - Discounted probability-weighted cash flows
  - An explicit risk adjustment; and
  - A contractual service margin ("CSM") representing the unearned profit of the contract which is recognised as revenue over the coverage period.

  The standard allows a choice between recognising changes in discount rates either in the statement of profit or loss or directly in other comprehensive income. The choice is likely to reflect how insurers account for their financial assets under IFRS 9.

  An optional, simplified premium allocation approach is permitted for the liability for the remaining coverage for short duration contracts, which are often written by non-life insurers.

  There is a modification of the general measurement model called the 'variable fee approach' for certain contracts written by life insurers where policyholders share in the returns from underlying items. When applying the variable fee approach the entity's share of the fair value changes of the underlying items is included in the contractual services margin. The results of insurers using this model are therefore likely to be less volatile than under the general model.

  The new rules will affect the financial statements and key performance indicators of all entities that issue insurance contracts or investments contracts with discretionary participation features. The group is in the process of assessing the impact of IFRS 17 to its insurance entities: BSP Life (Fiji) Limited and BSP Life PNG Limited.

A (ii) IFRS 16 Transitional Impact effective 1st January 2019

The Group adopted IFRS 16 Leases as issued by the IASB with a date of transition of 1 January 2019, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements. The Group did not early adopt IFRS 16 in previous periods.

As permitted by the transition provisions of IFRS 16, the Group elected not to restate comparative figures. On the initial application of IFRS 16, no adjustments had to be made to the opening retained earnings as at 1 January 2019 as the right of use assets were recognised at the amount equal to the corresponding lease liabilities. Consequently, for note disclosures, the consequential amendments have only been applied to the current period. The comparative period note disclosures repeat those disclosures made in the prior year.

Adjustments recognised on adoption of IFRS 16

On adoption of IFRS 16, the Group recognised lease liabilities in relation to leases which had previously been classified as 'operating leases' under the principles of IAS 17 Leases. These liabilities were measured at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate as of 1 January 2019. The average lessee's incremental borrowing rate applied to the lease liabilities on 1 January 2019 was 2.25%.

For leases previously classified as finance leases the entity recognised the carrying amount of the lease asset and lease liability immediately before transition as the carrying amount of the right of use asset and the lease liability at the date of initial application. The measurement principles of IFRS 16 are only applied after that date. The re-measurements to the lease liabilities were recognised as adjustments to the related right-of-use assets immediately after the date of initial application.

All amounts are expressed in K'000	**2019**
Operating lease commitments disclosed as at 31 December 2018	117,370
Discounted using the lessee's incremental borrowing rate of at the date of initial application	107,048
(Less): short-term leases recognised on a straight-line basis as expense	(2,381)
Add/(less): adjustments as a result of a different treatment of extension and termination	93,207
Lease liability recognised as at 1 January 2019	**197,874**
Of which are:	
Current lease liabilities	24,435
Non-current lease liabilities	173,439
	197,874

The associated right-of-use assets for property leases were measured on a modified retrospective basis as if the new rules had always been applied. There were no onerous lease contracts that would have required an adjustment to the right-of-use assets at the date of initial application.

The recognised right-of-use assets relate to the commercial and residential properties, and also considered dataline leases totaling K200,325 thousand.

The change in accounting policy affected the following items in the balance sheet on 1 January 2019:

- right-of-use assets – increase to K197,874.
- lease liabilities – increase to K197,874.

The net impact on retained earnings on 1 January 2019 was nil.

Practical expedients applied

In applying IFRS 16 for the first time, the Group has used the following practical expedients permitted by the standard:

- the use of a single discount rate to a portfolio of leases with reasonably similar characteristics
- the accounting for operating leases with a remaining lease term of less than 12 months as at 1 January 2019 as short-term leases
- the exclusion of initial direct costs for the measurement of the right-of-use asset at the date of initial application, and
- the use of hindsight in determining the lease term where the contract contains options to extend or terminate the lease.

B. Consolidation

The Financial Statements incorporate the assets and liabilities of all controlled entities of the Group as at 31 December 2019, and their results for the year then ended.

Controlled entities are those over which the Group has the power to govern financial and operating policies, generally accompanied by a shareholding that commands the majority of voting rights, and are commonly referred to as subsidiaries.

Subsidiaries are accounted for at acquisition under the acquisition cost method of accounting, where:

- acquisition cost is measured at fair value of assets transferred, equity issued, liabilities assumed and any directly attributable costs of the transaction;
- identifiable net assets are recorded initially at acquisition, at their fair values;
- any excess of the acquisition cost over the relevant share of identifiable net assets acquired is treated as goodwill, and any deficiency is recognised directly in the Statement of Comprehensive Income;

All intercompany transactions and balances are eliminated.

C. Investment in Associates and Joint Arrangements

Investments in Associates

Associates are entities over which the Group has significant, but not controlling influence, generally accompanied by a shareholding conferring between 20% - 50% of voting rights.

In the Financial Statements, these investments are accounted for under the equity method.

Interests In Joint Arrangements

The Group applies IFRS 11 to all joint ventures. Under IFRS 11 investments in joint arrangements are classified as either joint ventures or joint operations depending on the contractual rights and obligations of each investor. Joint ventures are accounted for using the equity method in the Financial Statements. Under the equity method of accounting, interests in joint ventures are initially recognised at cost and adjusted thereafter to recognise the Group's share of the post-acquisition profits or losses and movements in other comprehensive income. When the Group's share of losses in a joint venture equals or exceeds its interests in the entity (which includes any long-term interests that, in substance, form part of the Group's net investment in the joint ventures), the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the joint ventures.

Interests in joint ventures classified as held for sale are accounted for under IFRS 5 Non-current Assets Held for Sale and Discontinued Operations.

D. Revenue

Interest income and expense

Interest income and expense are recognised in the Statement of Comprehensive Income on an accrual basis using the effective interest rate ("EIR") method. The income arising from the various forms of instalment credit has been determined using the effective interest method.

Interest income includes coupons earned on inscribed stock, accrued discount and premium on Treasury and Central Bank bills.

Interest income and interest expense for all financial instruments measured at amortised cost is recognised using the effective interest rate method. Interest income is recognised for Stage 1 and Stage 2 financial assets measured at amortised cost by applying the EIR to gross carrying amounts of the financial instruments. For Stage 3 financial instruments, interest income is recognised by applying EIR on the net carrying value of the financial instrument.

The liability for long term insurance contracts (principally Life Insurance) has been determined in accordance with LPS 1.04 Valuation of Policy Liabilities, issued by the Australian Prudential Regulation Authority.

The policy liability is calculated in a way that allows for the systematic release of planned profit margins as services are provided to policy owners and the revenues relating to those services are received (Margin on Services methodology). Services used to determine profit recognition include the cost of expected insurance claims and the allocation of future bonuses. The liability is generally determined as the present value of all future expected payments, expenses, taxes and profit margins reduced by the present value of all future expected premiums and take into consideration projected future bonuses. The liabilities are recalculated at each balance date using best estimate assumptions. These assumptions are revisited regularly and adjusted for actual experiences on claims, expense, mortality and investment returns. The policy liability also includes policy owner retained earnings.

Insurance policy liabilities are further detailed in Note 40.

Short term insurance contracts

These contracts are the Term Life, Medical and Travel policies sold and underwritten by BSP Health Care (Fiji) Limited and BSP Life PNG Limited.

These contracts protect the Group's customers from the consequences of events such as death, medical emergency or loss on travel. Guaranteed benefits paid on occurrence of the specified insurance event are either fixed or linked to the extent of the economic loss suffered by the policyholder. There are no maturity or surrender benefits.

For all these contracts, premiums are recognised as revenue (earned premiums) proportionally over the period of coverage. The portion of premium received on in-force contracts that relates to unexpired risks at the Statement of Financial Position date is reported as the unearned premium liability. Premiums are shown before deduction of commission.

Claims and loss adjustment expenses are charged to income as incurred based on the estimated liability for compensation owed to contract holders or beneficiaries. They include direct and indirect claims settlement costs and arise from events that have occurred up to the Statement of Financial Position date even if they have not yet been reported to the Group. The Group does not discount its liabilities for unpaid claims. Liabilities for unpaid claims are estimated using the input of assessments for individual cases reported to the Group and statistical analyses for the claims incurred but not reported, and to estimate the expected ultimate cost of more complex claims that may be affected by external factors (such as court decisions).

Foreign exchange income or losses

Realised and unrealised gains or losses from foreign currency trading, or from changes in the fair value of the trading assets and liabilities are recognised as income in the Statement of Comprehensive Income in the period in which they arise.

E. Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. All other risk related fees that constitute cost recovery are taken to income when levied. Loan origination fees are deferred over the expected term of the financial instrument according to the effective interest method. The effective interest method uses the rate that exactly discounts estimated future payments and receipts through the expected life of the instrument or when appropriate, a shorter period to the net carrying amount of the financial asset.

F. Borrowing expenses

Expenses associated with the borrowing of funds are charged to the Statement of Comprehensive Income in the period in which they are incurred.

G. Provision for loan impairment

Loans are originated by providing funds directly to the borrower and are recognised when cash is advanced to borrowers.

All loans, advances and other receivables from customers are subject to continuous management review. A specific provision for loan impairment is established if there is objective evidence that the Group will not be able to collect all amounts due under the terms of loans. The amount of the provision approximates the difference between the carrying amount and the recoverable amount, which is the current best estimate of the present value of expected future cash flows arising from the asset. All bad debts are written off against the specific provision for loan impairment in the period in which they are classified as irrecoverable. Subsequent recoveries are credited to the provision for loan losses in the Statement of Comprehensive Income.

General provisions for impairment are maintained to cover incurred losses unidentified at balance date in the overall portfolio of loans, advances and other receivables from customers. The provisions are determined having regard to the level of risk weighted assets, economic conditions, the general risk profile of the credit portfolio, past loss experience and a range of other criteria. The amount necessary to bring the provisions to their assessed levels, after write-offs, is charged to the Statement of Comprehensive Income.

Impairment
The Group assesses on a forward-looking basis the expected credit losses ('ECL') associated with its debt instrument assets carried at amortised cost and with the exposure arising from loan commitments and financial guarantee contracts. The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

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

Note 34 provides more detail of how the expected credit loss allowance is measured.

H. Goodwill

Goodwill represents the excess of the cost of any acquisition over the acquirer's interest in the fair value of the identifiable assets and liabilities acquired as at the exchange transaction. Goodwill is reported in the Statement of Financial Position as an intangible asset.

In determining goodwill, management considers various factors including net selling price of the acquired business, existing market share, potential growth opportunities, and other factors inherent in the acquired business. This assessment is reviewed at each balance date, so that any indication of impairment with implications for the recoverability of goodwill can be tested, and adjustments to the carrying value of goodwill made if necessary.

I. Computer systems development costs

Costs incurred to develop and enhance the Group's computer systems are capitalised to the extent that benefits do not relate solely to revenue that has already been brought to account and will contribute to the future earning capacity of the economic entity. These costs are amortised over the estimated economic life of four to eight years using the straight-line method. Costs associated with maintaining computer software programs are recognised as an expense when incurred.

J. Property, plant and equipment

Land and buildings are carried at revalued amounts, being their fair value at the date of revaluation less subsequent accumulated depreciation and impairment losses. Fair value is determined on the basis of regular independent valuations prepared by external valuation experts, based on discounted cash flows or capitalisation of net income (as appropriate). The fair values are recognised in the financial statements and are reviewed at the end of each reporting period to ensure that the carrying value of land and buildings are not materially different from their fair values.

Any revaluation increase arising on the revaluation of land and buildings is credited to the asset revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognised as an expense in profit or loss, in which case the increase is credited to the Statement of Comprehensive Income to the extent of the decrease previously charged. A decrease in carrying amount arising on the revaluation of land and buildings is charged as an expense in the Statement of Comprehensive Income to the extent that it exceeds the balance, if any, held in the asset revaluation reserve relating to a previous revaluation of that asset. Buildings under constructions are referred to as work in progress and are accounted for at cost and subsequently reclassified to buildings (premises) upon completion.

Depreciation is provided on property, plant and equipment, including buildings but excluding land. Depreciation is calculated on a straight line basis so as to write off the net cost or other revalued amount of each asset over its expected useful life to its estimated residual value. Leasehold improvements are depreciated over the period of the lease or estimated useful life, whichever is the shorter, using the straight line method. The estimated useful life, residual value and depreciation method is reviewed at the end of each annual reporting period.

The following basis and method of depreciation is used:

Class of asset	**Method**	**Rate**
Property (excluding land)	Straight line basis	2 - 3% pa
Plant and equipment	Straight line basis	10 - 25% pa
Equipment under operating lease	Straight line basis	3 - 20% pa

Gains or losses on disposals (being the difference between the carrying value at the time of sale or disposal and the proceeds received) are taken into account in determining operating profit for the year. Where the carrying value of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Repairs and maintenance are taken into account in determining operating profit when the expenditure is incurred.

K. Leases

Bank is lessee

(i) The Group's leasing activities and how these are accounted for.
The Group leases various offices and branches for its retail operations. Rental contracts are typically made for fixed periods of 3 to 5 years but may have extension options as described in (iii) below. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. The lease agreements do not impose any covenants, but leased assets may not be used as security for borrowing purposes.

Until the 2018 financial year, leases of property, plant and equipment were classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) were charged to profit or loss on a straight-line basis over the period of the lease.

From 1 January 2019, leases are recognised as a right-of-use asset and a corresponding liability at the date at which the leased asset is available for use by the Group. Each lease payment is allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease period so as to produce a constant periodic rate of interest on the remaining balance of the liability for each period. The right-of-use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

Assets and liabilities arising from a lease are initially measured on a present value basis. Lease liabilities include the net present value of the following lease payments:

- fixed payments (including in-substance fixed payments), less any lease incentives receivable
- variable lease payment that are based on an index or a rate
- amounts expected to be payable by the lessee under residual value guarantees
- the exercise price of a purchase option if the lessee is reasonably certain to exercise that option, and payments of penalties for terminating the lease, if the lease term reflects the lessee exercising that option.

The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be determined, the lessee's incremental borrowing rate is used, being the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of similar value in a similar economic environment with similar terms and conditions.

Right-of-use assets are measured at cost comprising the following:

- the amount of the initial measurement of lease liability
- any lease payments made at or before the commencement date less any lease incentives received any initial direct costs, and
- restoration costs.

Payments associated with short-term leases and leases of low-value assets are recognised on a straight-line basis as an expense in profit or loss. Short-term leases are leases with a lease term of 12 months or less.

(ii) Variable lease payments
The Group does not have any property leases that contain variable payment terms that are linked to sales generated from a branch.

(iii) Extension and termination options
Extension and termination options are included in a number of property leases across the group. These terms are used to maximise operational flexibility in terms of managing contracts. The majority of extension and termination options held are exercisable only by the Group and not by the respective lessor.

(iv) Critical judgements in determining the lease term
In determining the lease term, management considers all facts and circumstances that create an economic incentive to exercise an extension option, or not exercise a termination option. Extension options (or periods after termination options) are only included in the lease term if the lease is reasonably certain to be extended (or not terminated).

The assessment is reviewed if a significant event or a significant change in circumstances occurs which affects this assessment and that is within the control of the lessee. During the current financial year, the financial effect of revising lease terms to reflect the effect of exercising extension and termination options did not have an impact on recognised lease liabilities and right-of-use assets.

(v) Residual value guarantees
The Group does not provide residual value guarantees in relation to its leases.

L. Cash and cash equivalents

For the purpose of the cash flow statement, Cash and cash equivalents comprise notes and coins, and balances due to and from other banks with original maturities of less than three months.

M. Financial assets & Liabilities

M(1) Financial Assets

Classification and subsequent measurement

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

- Fair value through profit or loss (FVPL); or
- Amortised cost.

The classification requirements for debt and equity instruments are described below:

a) Debt instruments

Debt instruments are those instruments that meet the definition of a financial liability from the issuer's perspective, such as loans, government and corporate bonds and trade receivables purchased from clients in factoring arrangements without recourse.

Classification and subsequent measurement of debt instruments depend on:

(i) the Group's business model for managing the asset; and
(ii) the cash flow characteristics of the asset.

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

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest ('SPPI'), and that are not designated at FVPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any expected credit loss allowance recognised and measured as described in note 34.1.2. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

- Fair value through profit or loss: Assets that do not meet the criteria for amortised cost are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognised in profit or loss and presented in the profit or loss statement within 'Net trading income' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Net investment income'. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

Business model: the business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'other' business model and measured at FVPL. Factors considered by the Group in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated. For example, the Group's business model for the mortgage loan book is to hold to collect contractual cash flows, for this portfolio there has been no history of prior period sales and no intention of future sales, hence the classification is amortised cost. Another example is debt securities held within the insurance entities of the bank which are held at FVPL to prevent an accounting mismatch with the associated insurance contract liabilities which are held at fair value through income statement.

SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Group assesses whether the financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test'). In making this assessment, the Group considers whether the contractual cash flows are consistent with a basic lending arrangement i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

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

b) Equity instruments

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

The Group subsequently measures all equity investments at fair value through profit or loss. Gains and losses on equity investments at FVPL are included in the 'Investment revenue' line in the statement of profit or loss.

Measurement methods

Amortised cost and effective interest rate

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

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees and points paid or received that are integral to the effective interest rate, such as origination fees.

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

Interest income

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets.

Initial recognition and measurement

Financial assets and financial liabilities are recognised when the entity becomes a party to the contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the Group commits to purchase or sell the asset.

At initial recognition, the Group measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions. Transaction costs of financial assets and financial liabilities carried at fair value through profit or loss are expensed in profit or loss. Immediately after initial recognition, an expected credit loss allowance (ECL) is recognised for financial assets measured at amortised cost, as described in note 34.1.2, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

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

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

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

Modification of loans

The Group sometimes renegotiates or otherwise modifies the contractual cash flows of loans to customers. When this happens, the Group assesses whether or not the new terms are substantially different to the original terms. The Group does this by considering, among others, the following factors:

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- Whether any substantial new terms are introduced, such as a profit share/equity-based return that substantially affects the risk profile of the loan.
- Significant extension of the loan term when the borrower is not in financial difficulty.
- Significant change in the interest rate.
- Change in the currency the loan is denominated in.
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

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

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

De-recognition other than on a modification

Financial assets, or a portion thereof, are derecognised when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either (i) the Group transfers substantially all the risks and rewards of ownership, or (ii) the Group neither transfers nor retains substantially all the risks and rewards of ownership and the Group has not retained control.

Th Group enters into transactions where it retains the contractual rights to receive cash flows from assets but asumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards. These transactions are accounted for as 'pass through' transfers that result in derecognition if the Group:

(i) Has no obligation to make payments unless it collects equivalent amounts from the assets;

(ii) Is prohibited from selling or pledging the assets; and

(iii) Has an obligation to remit any cash it collects from the assets without material delay.

Collateral (shares and bonds) furnished by the Group under standard repurchase agreements and securities lending and borrowing transactions are not derecognised because the Group retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met. This also applies to certain securitisation transactions in which the Group retains a subordinated residual interest.

M(2) Financial Liabilities

Classification and subsequent measurement

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

- Financial liabilities arising from the transfer of financial assets which did not qualify for de-recognition, whereby a financial liability is recognised for the consideration received for the transfer. In subsequent periods, the Group recognises any expense incurred on the financial liability; and
- Financial guarantee contracts and loan commitments.

De-recognition

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

The exchange between the Group and its original lenders of debt instruments with substantially different terms, as well as substantial modifications of the terms of existing financial liabilities, are accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. The terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective interest rate, is at least 10% different from the discounted present value of the remaining cash flows of the original financial liability. In addition, other qualitative factors, such as the currency that the instrument is denominated in, changes in the type of interest rate, new conversion features attached to the instrument and change in covenants are also taken into consideration. If an exchange of debt instruments or modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment. If the exchange or modification is not accounted for as an extinguishment, any costs or fees incurred adjust the carrying amount of the liability and are amortised over the remaining term of the modified liability.

Financial guarantee contracts and loan commitments

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to banks, financial institutions and others on behalf of customers to secure loans, overdrafts and other banking facilities.

Financial guarantee contracts are initially measured at fair value and subsequently measured at the higher of:

- The amount of the loss allowance (calculated as described in note 34.1.2);
- The premium received on initial recognition less income recognised in accordance with the principles of IFRS 15.

Expected credit loss on loan commitments provided by the Group are measured as the amount of the loss allowance (calculated as described in note 34.1.2). The Group has not provided any commitment to provide loans at a below-market interest rate, or that can be settled net in cash or by delivering or issuing another financial instrument.

For loan commitments and financial guarantee contracts, the loss allowance is recognised as a provision.

N. Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

O. Employee benefits

A liability is recognised for benefits accruing to employees in respect of wages and salaries, annual leave, and long service leave when it is probable that settlement will be recognised and they are capable of being measured reliably.

Liabilities recognised in respect of employee benefits are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Post-employment benefits - defined contribution plans

A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate fund, and there is no recourse to the Group for employees if the fund has insufficient assets to pay employee benefits relating to service up to the balance sheet date.

The Group pays contributions to publicly or privately administered superannuation plans on a mandatory, contractual or voluntary basis in respect of services rendered up to balance sheet date by all staff members other than non-citizen contract staff for whom there is no legal obligation to do so. The contributions are at the current rate of employees' gross salary. Once the contributions have been paid, the Group has no further payment obligations for post-employment benefits from the date an employee ceases employment with the Group.

P. Income tax

Current Tax

Current tax is calculated by reference to the amount of income taxes payable or recoverable in respect of the taxable profit or tax loss for the period. It is calculated using tax rates and tax laws that have been enacted or substantively enacted by the reporting date. Current tax for current and prior periods is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

Deferred tax

Deferred tax is accounted for using the balance sheet liability method. Temporary differences are differences between the tax base of an asset or liability and its carrying amount in the Statement of Financial Position. The tax base of an asset or liability is the amount attributed to that asset or liability for tax purposes.

In principle, deferred tax liabilities are recognised for all taxable temporary differences. Deferred tax assets are recognised to the extent that it is probable that sufficient taxable amounts will be available against which deductible temporary differences or unused tax losses and tax offsets can be utilised. However, deferred tax assets and liabilities are not recognised if the temporary differences giving rise to them arise from the initial recognition of assets and liabilities which affects neither taxable income nor accounting profit.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the period(s) when the asset and liability giving rise to them are realised or settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Group intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax for the period

Current and deferred tax is recognised as an expense or income in the Statement of Comprehensive Income, except when it relates to items credited or debited directly to equity, in which case the deferred tax is also recognised directly in equity.

Q. Foreign currency

The Financial Statements of the Group are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of these Financial Statements, the results and financial position of the Bank are expressed in Papua New Guinea kina, which is the Bank's functional and presentation currency.

In preparing the Financial Statements, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing on the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Foreign operations

On consolidation, the assets and liabilities of the consolidated entity's overseas operations are translated at exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the period unless exchange rates fluctuate significantly. Exchange differences arising, if any, are recognised in the foreign currency translation reserve, and recognised in profit or loss on disposal of the foreign operation.

R. Share capital

Share issue costs

External costs directly attributable to the issue of new shares are deducted from equity net of any related income taxes.

Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity in the period in which they are declared.

Dividends for the year, declared after the balance sheet date, are dealt with in the subsequent events note.

S. Asset impairment

At each reporting date, the Group reviews the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where the asset does not generate cash flows that are independent from other assets, the Group estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Goodwill, intangible assets with indefinite useful lives and intangible assets not yet available for use are tested for impairment annually and whenever there is an indication that the asset may be impaired. An impairment of goodwill is not subsequently reversed.

Recoverable amount is the higher of fair value less cost of disposal and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, but only to the extent that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in profit or loss immediately, unless the relevant asset is carried at fair value, in which case the reversal of the impairment loss is treated as a revaluation increase.

T. Non-current assets held for sale

Non-current assets (and disposal groups) classified as held for sale are measured, with certain exceptions, at the lower of carrying amount and fair value less costs to sell.

Non-current assets and disposal groups are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use. This condition is regarded as met only when the asset (or disposal group) is available for immediate sale in its present condition subject only to terms that are usual and customary for such a sale and the sale is highly probable. The sale of the asset (or disposal group) must be expected to be completed within one year from the date of classification, except in the circumstances where sale is delayed by events or circumstances outside the Group's control and the Group remains committed to a sale.

U. Investment Property

Property held for long-term rental yields is classified as investment property. Investment property comprises freehold land and buildings. It is carried at fair value. The fair values have been arrived at on the basis of the valuations carried out by Rolle and Associates and Pacific Valuations Limited, independent valuers not related to the group. The valuers have appropriate qualifications and recent experience in the valuation of properties in Fiji. The valuations were arrived at by reference to current net rental income and capital expenditure and external factors in the Fiji commercial and residential environment such as current supply and demand and expected growth.

Changes in fair values are recorded in profit or loss.

Property located on land that is held under an operating lease is classified as investment property as long as it is held for long-term rental yields and is not occupied by more than 50% by the companies in the Group. The initial cost of the property is the lower of the fair value of the property and the present value of the minimum lease payments. The property is carried at fair value after initial recognition.

V. Derivative financial instruments and acceptances

Forward foreign exchange contracts entered into for trading purposes are initially recognised at fair value and subsequently re-measured at fair value based upon the forward rate. Gains and losses on such contracts are taken to the Statement of Comprehensive Income.

Acceptances comprise undertakings by the Group to pay bills of exchange drawn on customers. The Group expects most acceptances to be settled simultaneously with the reimbursement from the customers. Customer acceptances are accounted for as off-balance sheet transactions and are disclosed as contingent liabilities and commitments.

The Group does not actively enter into or trade in complex forms of derivative financial instruments such as currency and interest rate swaps and options.

W. Segment reporting

Segments are reported in a manner consistent with the internal reporting provided to the Group's chief operating decision maker.

X. Earnings per share

Earnings per share is determined by dividing the profit or loss attributable to owners of the Bank by the weighted average number of participating shares outstanding during the reporting year.

Y. Comparatives

Comparative figures have been adjusted to conform to changes in presentation in the current year.

Z. 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 – note 1(g) and 1(s)
- Estimated goodwill impairment – note 1(h) and 7(a)
- Estimated insurance liability – note 1(d), note 22 and note 40
- Estimation of fair value of financial assets and liabilities – note 1(m) and note 39
- Estimation of fair value of non-financial assets - note 39

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). Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is further detailed in note 34.1.2.3, which also sets out key sensitivities of the ECL to changes in these elements.

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.

Detailed information about the judgements and estimates made by the Group in the above areas are set out in note 34.

2. Net interest income

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Interest income				
Loans, advances and other receivables from customers[1]	1,238,453	1,156,426	1,125,395	1,053,335
Other financial assets - inscribed stock	198,484	205,333	198,164	205,051
Treasury and Central Bank bills	141,573	194,816	140,086	193,322
Cash and balances with Central Bank	6,189	4,042	9,714	5,664
Other	1,074	1,074	3,876	3,112
	1,585,773	**1,561,691**	**1,477,235**	**1,460,484**
Less: **Interest expense**				
Customer deposits	178,053	152,008	162,912	135,167
Other banks	12,396	20,330	14,012	22,366
Subordinated debt securities	3,540	8,557	3,540	8,557
	193,989	**180,895**	**180,464**	**166,090**
	1,391,784	**1,380,796**	**1,296,771**	**1,294,394**

[1]Group interest income includes K13.079m (Bank K12.957m) recognized on impaired loans (Stage 3) to customers. The Group takes up required provisions on such interest income as detailed in the accounting policy in note 1D.

3. Fee and commission income

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Fee and commission income				
Product related	182,220	198,017	169,131	185,188
Trade and international related	21,259	18,900	20,366	18,073
Electronic banking related	143,801	129,829	132,861	118,927
Other	37,797	37,098	24,904	27,004
	385,077	**383,844**	**347,262**	**349,192**
Less: **Fee and commission expenses**				
Agencies	181	687	176	651
International Finance Corporation fees	135	649	135	649
	316	**1,336**	**311**	**1,300**
	384,761	**382,508**	**346,951**	**347,892**

4. Other income

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Foreign exchange related[1]	327,705	313,785	291,308	281,205
Operating lease rentals	7,503	8,473	7,503	8,473
Other[2]	28,922	41,230	74,555	63,850
	364,130	**363,488**	**373,366**	**353,528**

[1]Foreign exchange related income includes gains and losses from spot and forward contracts and translated foreign currency assets.

[2]2018 other income includes K19m insurance recovery for an aircraft destroyed by fire.

5. (a) Operating Expenses

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Administration	95,246	118,334	90,694	114,897
Computing	125,412	136,973	111,245	119,599
Depreciation	107,906	81,000	90,352	64,572
Amortisation of computer development	28,173	27,399	22,577	22,546
Non-executive directors costs	3,639	5,044	3,044	4,559
Non-lending losses[1]	2,318	33,226	1,654	33,094
Fixed asset impairment expenses	1,975	13,888	1,975	13,888
Premises and equipment	60,993	88,924	56,495	80,795
	425,662	**504,788**	**378,036**	**453,950**
Staff costs				
Defined contribution plans	15,531	15,262	14,133	14,021
Statutory benefit contributions	10,929	12,168	10,320	11,216
Wages and salaries	312,239	296,885	286,004	272,331
Other staff benefits	54,887	57,994	52,236	55,315
	393,586	**382,309**	**362,693**	**352,883**
	819,248	**887,097**	**740,729**	**806,833**

[1]Non-Lending losses for 2018 included K13.5m loss on aircraft destroyed by fire, offset by insurance recovery.

(b) Impairment on Financial Assets

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Loans and advances (note 13)	101,882	82,380	90,861	71,599
Treasury and Central Bank Bills (note 11)	(1,865)	40	(1,865)	40
Other Financial Assets (note 17)	(834)	20	(904)	-
	99,183	**82,440**	**88,092**	**71,639**

6. Income tax

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Income tax expense				
Current tax	368,467	365,551	348,760	347,673
Deferred tax	(8,675)	(12,443)	(9,510)	(20,623)
Current year	359,792	353,108	339,250	327,050
Adjustment to prior year estimates	2,764	(1,012)	3,189	2,043
	362,556	**352,096**	**342,439**	**329,093**
Tax calculated at 30% of profit before tax (2018:30%)	344,898	341,712	356,480	334,961
Tax calculated at respective subsidiary tax rates	22,341	14,798	-	-
Expenses not deductible for tax	6,072	4,453	995	5
Tax loss not recognised	5,548	5,379	-	-
Income not recognized for tax purposes[1]	(19,067)	(13,234)	(18,225)	(7,916)
Adjustment to prior year estimates	2,764	(1,012)	3,189	2,043
	362,556	**352,096**	**342,439**	**329,093**
Tax receivable				
At 1 January	12,753	(31,708)	17,020	(25,231)
Income tax provision	(368,467)	(365,551)	(348,760)	(347,256)
Adjustment to prior year estimates	579	(10,418)	1,004	(12,706)
Other tax related items	(564)	-	(2,826)	-
Tax payments made	383,287	420,430	363,837	402,213
At 31 December	**27,588**	**12,753**	**30,275**	**17,020**

[1]Income not recognized for tax purpose for the Bank includes dividends received from Subsidiaries which are eliminated upon consolidation whilst the Group number represents actuarial liabilities deductions allowable for BSP Life Fiji Limited

6. Income tax (continued)

All amounts are expressed in K'000	Consolidated		Bank	
	2019	**2018**	**2019**	**2018**
Deferred taxes				
Specific allowance for losses on loans, advances and other receivables from customers	56,215	48,186	53,558	45,011
General allowance for losses on loans, advances and other receivables from customers	137,768	132,757	131,960	127,518
Employee related provisions	26,721	23,983	25,944	23,103
Prepaid expenses	(1,349)	(1,361)	(1,323)	(1,337)
Other provisions	47,422	46,690	45,396	45,017
Property, plant and equipment	(70,969)	(70,128)	(30,223)	(30,338)
Unrealised foreign exchange gains	(1,876)	659	(1,876)	659
Accruals	25,372	27,658	22,650	24,758
At 31 December	**219,304**	**208,444**	**246,086**	**234,391**
Represented by:				
Deferred tax asset	250,846	239,607	246,086	234,391
Deferred tax liability	(31,542)	(31,163)	-	-
At 31 December	**219,304**	**208,444**	**246,086**	**234,391**
Deferred taxes movement:				
At 1 January	208,444	181,934	234,391	200,021
Current year movement	8,675	12,443	9,510	20,623
Adjustment to prior year estimates	2,185	9,823	2,185	9,367
Other movements	-	4,244	-	4,380
At 31 December	**219,304**	**208,444**	**246,086**	**234,391**

7. Intangible assets

All amounts are expressed in K'000	Consolidated		Bank	
	2019		**2018**	
7(a) Goodwill				
At 1 January	45,307	45,307	41,051	41,051
Net movement	-	-	-	-
Gross carrying amount	**45,307**	**45,307**	**41,051**	**41,051**

To assess whether goodwill is impaired, the carrying amount of a cash-generating unit is compared to the recoverable amount. The recoverable amount is determined based on fair value less cost to sell, primarily using an earnings multiple applicable to that cash-generating unit. The category of this fair value is Level 3 as defined in Note 39.

7. Intangible assets (continued)

Earnings multiples used in the impairment assessment for Non PNG Banks are sourced from publicly available data associated with operations displaying similar characteristics to the Non PNG Banks plus a control premium, and are applied to the current forecast earnings. The key assumption is the Price-Earnings (P/E) multiple observed, which for the Non PNG Banks were in the range of 8.3x – 13.6x (2018: 8.3x – 13.6x).
The goodwill allocated to the Non Bank Entities is not significant.

7(b) Computer development cost

All amounts are expressed in K'000	Consolidated		Bank	
	2019		2018	
At 1 January	129,316	62,511	111,500	59,699
Additions	52,108	95,326	49,978	75,469
Disposals	(2,352)	(1,122)	(2,351)	(1,122)
Amortisation expense	(28,173)	(27,399)	(22,577)	(22,546)
At 31 December	**150,899**	**129,316**	**136,550**	**111,500**
Computer development cost	291,324	245,186	256,417	212,614
Accumulated amortisation	(140,425)	(115,870)	(119,867)	(101,114)
At 31 December	**150,899**	**129,316**	**136,550**	**111,500**
Total intangible assets	**196,206**	**174,623**	**177,601**	**152,551**

8. Investment in subsidiaries

Name of Subsidiary	Principal activity	Place of incorporation and operation	Ownership %	Balance of Investment 2019	2018
BSP Capital Limited	Fund Management/ Investment Banking	PNG	100%	2,448	2,448
BSP Life (Fiji) Limited	Life Insurance	Fiji	100%	87,599	87,599
BSP Life (PNG) Limited	Life Insurance	PNG	100%	25,000	15,000
BSP Convertible Notes Limited	Capital Raising	Fiji	100%	371	371
BSP Finance Limited	Credit Institution	PNG	100%	82,503	61,837
Bank of South Pacific Tonga Ltd	Bank	Tonga	100%	71,610	71,610
Bank South Pacific (Samoa) Ltd	Bank	Samoa	98.7%	70,712	70,712
Bank South Pacific Vanuatu Ltd	Bank	Vanuatu	100%	38,020	38,020
At 31 December				**378,263**	**347,597**

	2019	2018
Represented by:		
At 1 January	347,597	338,400
Additional capital	30,666	10,000
Provision for impairment of BSP Capital Limited	-	(803)
At 31 December	**378,263**	**347,597**

9. Investment in Joint Ventures

Entity	Joint Venture/ Associate	Principal activity	Place of incorporation and operation	Proportion of ownership and voting power held 2019	2018
Suva Central Ltd	Joint Venture	Property rental	Fiji	50%*	50%*
Richmond Ltd	Joint Venture	Hotel operation	Fiji	61.3%**,50%***	61.3%**,50%***
BSP Finance Cambodia Plc	Joint Venture	Finance	Cambodia	50%*	50%*

The investments above are accounted for using the equity method in the Financial Statements.

**Both ownership and voting power held, **ownership, ***voting power held.*

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Joint ventures				
Investment in joint ventures	175,579	154,135	20,038	19,157
Investments during the year	14,458	-	-	-
Translation movement	1,812	137	219	(40)
Share of profit for the year	10,191	21,307	530	921
Net investment at 31 December	**202,040**	**175,579**	**20,787**	**20,038**
Summarised financial information of joint ventures:				
Total assets	444,720	340,266	85,039	81,740
Total liabilities	(212,455)	(159,450)	(43,464)	(43,426)
Net assets	**232,265**	**180,816**	**41,575**	**38,314**
Share of profits	10,449	14,354	530	921
Group fair value alignment	(258)	6,953	-	-
Share of profit in Group	**10,191**	**21,307**	**530**	**921**

10. Cash and balances with Central Bank

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Notes, coins and cash at bank	513,241	509,588	496,694	500,332
Balances with Central Bank other than statutory deposit	1,303,323	743,861	1,013,712	466,375
Total cash and balances with Central Bank	**1,816,564**	**1,253,449**	**1,510,406**	**966,707**

11. Treasury and Central Bank bills

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Treasury and Central Bank bills – face value	2,517,999	2,553,051	2,478,589	2,538,706
Discount for interest receivable	(50,788)	(48,772)	(50,787)	(48,771)
Less allowance for impairment	(7,714)	(9,579)	(7,714)	(9,579)
At 31 December	**2,459,497**	**2,494,700**	**2,420,088**	**2,480,356**
Allowance for impairment				
At 1 January	9,579	9,539	9,579	9,539
Provision/(release) for impairment	(1,865)	40	(1,865)	40
At 31 December	**7,714**	**9,579**	**7,714**	**9,579**

Treasury and Central Bank bills are debt securities issued by Central Banks. These bills are classified as assets held for trading and carried at fair value by the Insurance business and as assets held to collect and carried at amortised cost by the Banking businesses.

12. Amounts due from other banks

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Items in the course of collection	29,692	35,426	29,693	35,426
Placements with other banks	992,777	818,593	968,123	760,754
At 31 December	**1,022,469**	**854,019**	**997,816**	**796,180**

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

13. Loans, advances and other receivables from customers

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Overdrafts	1,008,876	912,057	933,819	848,196
Lease financing	295,381	252,293	258,659	205,744
Term loans	9,903,563	9,510,991	9,114,411	8,767,253
Mortgages	2,605,311	2,403,278	2,159,668	2,000,770
Policy loans	88,280	85,597	-	-
Gross loans, advance and other receivables due from customers net of reserved interest	**13,901,411**	**13,164,216**	**12,466,557**	**11,821,963**
Less allowance for losses on loans, advances and other receivables from customers	(700,604)	(633,567)	(646,587)	(589,238)
At 31 December	**13,200,807**	**12,530,649**	**11,819,970**	**11,232,725**

The spread of the loans are detailed in the maturity analysis table on Note 34. The loans are well-diversified across various sectors and are further analysed in Note 34. Allowance for losses includes K29.976m (Bank K28.192m) provision taken up for interest recognized on stage 3 loans.

Lease financing

The Group and the bank provide lease financing to a broad range of clients to support financing needs in acquiring movable assets such as motor vehicles and plant and equipment. Finance lease receivables are included within loans, advances and other receivables from customers and are analysed as follows:

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Gross investment in finance lease receivable				
Not later than 1 year	23,152	34,358	19,241	29,746
Later than 1 year and not later than 5 years	309,154	252,531	269,514	200,775
	332,306	**286,889**	**288,755**	**230,521**
Unearned future finance income				
Not later than 1 year	(1,319)	(1,961)	(1,116)	(1,713)
Later than 1 year and not later than 5 years	(35,606)	(32,635)	(28,980)	(23,064)
	(36,925)	(34,596)	(30,096)	(24,777)
Present value of minimum lease payments receivable	**295,381**	**252,293**	**258,659**	**205,744**
Present value of minimum lease payments receivable is analysed as follows:				
Not later than 1 year	21,833	32,397	18,125	28,033
Later than 1 year and not later than 5 years	273,548	219,896	240,534	177,711
At 31 December	**295,381**	**252,293**	**258,659**	**205,744**

13. Loans, advances and other receivables from customers (continued)

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Provision for impairment				
Movement in allowance for losses on loans, advances and other receivables from customers:				
Balance at 1 January	633,567	577,186	589,238	538,949
Net new and increased provisioning	79,064	66,073	65,049	57,277
Loans written off against provisions / (Write back of provisions no longer required)	(12,027)	(9,692)	(7,700)	(6,988)
At 31 December	**700,604**	**633,567**	**646,587**	**589,238**
Provision for impairment is represented by				
Collective provision	477,305	454,345	439,866	423,965
Individually assessed or specific provision	223,299	179,222	206,721	165,273
At 31 December	**700,604**	**633,567**	**646,587**	**589,238**
Loan impairment expense				
Net collective provision funding	17,552	15,034	13,478	11,526
Net new and increased individually assessed provisioning	61,512	51,039	51,571	45,751
Total new and increased provisioning	**79,064**	**66,073**	**65,049**	**57,277**
Recoveries during the year	(64,042)	(58,936)	(58,178)	(57,508)
Net (write back/write off)	86,860	75,243	83,990	71,830
At 31 December	**101,882**	**82,380**	**90,861**	**71,599**

14. Property, plant and equipment

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Carrying value				
Capital Work in Progress	**51,290**	**39,295**	**45,930**	**32,540**
Premises	635,068	646,574	498,827	523,923
Accumulated depreciation	(109,191)	(108,905)	(94,309)	(96,809)
	525,877	**537,669**	**404,518**	**427,114**
Equipment	397,817	366,593	296,823	266,170
Accumulated depreciation	(277,449)	(250,280)	(207,875)	(187,643)
	120,368	**116,313**	**88,948**	**78,527**
Right of Use Assets	209,354	-	184,608	-
Accumulated depreciation	(26,947)	-	(25,249)	-
	182,407	**-**	**159,359**	**-**
At 31 December	**879,942**	**693,277**	**698,755**	**538,181**

14. Property, plant and equipment (continued)

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Reconciliation is as follows:				
Capital Work in Progress				
At 1 January	39,295	70,711	32,540	51,065
Additions	129,033	118,851	120,758	108,347
Transfers	(117,038)	(150,267)	(107,368)	(126,872)
At 31 December	**51,290**	**39,295**	**45,930**	**32,540**
Premises				
At 1 January	537,669	560,019	427,114	451,281
Additions	26,067	20,492	13,479	14,355
Disposals	(4,720)	(12,049)	(4,478)	(12,049)
Revaluation gains/ (losses)	(5,416)	(488)	(6,419)	-
Depreciation expense	(27,723)	(30,305)	(25,178)	(26,473)
At 31 December	**525,877**	**537,669**	**404,518**	**427,114**
Equipment				
At 1 January	116,313	107,940	78,527	71,959
Additions	53,562	55,789	46,465	41,258
Disposals	(571)	(1,465)	(419)	(1,335)
Depreciation expense	(48,936)	(45,951)	(35,625)	(33,355)
At 31 December	**120,368**	**116,313**	**88,948**	**78,527**
Right of Use Assets				
At 1 January	-	-	-	-
Additions	209,354	-	184,608	-
Depreciation expense	(26,947)	-	(25,249)	-
At 31 December	**182,407**	-	**159,359**	-
Assets subject to operating lease				
Carrying value				
Aircraft	59,600	59,600	59,600	59,600
Accumulated depreciation	(11,467)	(7,167)	(11,467)	(7,167)
At 31 December	**48,133**	**52,433**	**48,133**	**52,433**

14. Property, plant and equipment (continued)

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Reconciliation of carrying value of aircraft is set out below:				
Aircraft				
At 1 January	52,433	70,689	52,433	70,689
Depreciation	(4,300)	(4,743)	(4,300)	(4,743)
Disposal of aircraft	-	(13,513)	-	(13,513)
At 31 December	**48,133**	**52,433**	**48,133**	**52,433**
Future minimum lease receipts				
Not later than 1 year	8,253	8,253	8,253	8,253
Later than 1 year and not later than 5 years	2,751	11,004	2,751	11,004
At 31 December	**11,004**	**19,257**	**11,004**	**19,257**

The carrying amount of land, buildings and aircraft had they been recognised under the cost model are as follows:

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Land	21,695	20,865	20,319	20,312
Buildings	148,514	155,727	140,871	146,989
Aircraft	9,274	11,165	9,274	11,165
At 31 December	**179,483**	**187,757**	**170,464**	**178,466**

Land and buildings carried at fair value

Independent valuations of the Bank's land and buildings were performed by The Professional Valuers of PNG Limited to determine the fair value of the land and buildings. The valuations, which conform to International Valuation Standards, were determined by reference to capitalization of the notional income stream approach on the Market Value basis. The recent valuation was dated 30 November 2017 for all properties except for PNG Bank residential properties which were revalued at 30 November 2019.

Assets subject to operating lease – aircraft

An independent valuation of the Bank's aircrafts was performed by Charles Taylor Aviation Asset Management to determine the current realistic fair value for each of the aircraft. The valuation, which conforms to International Valuation Standards, takes into consideration the current global market variations for the specific types of aircrafts. The effective date of the valuation was 31 May 2017.

15. Leases

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
i) Amounts recognized in the balance sheet				
Right of use assets[1]				
Properties	178,290	-	155,979	-
Equipment	4,117	-	3,380	-
	182,407	**-**	**159,359**	**-**

[1]Included in the line item 'Property, plant and equipment' in the balance sheet.

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Lease liabilities[2]				
Current	30,493	-	24,099	-
Non-Current	159,671	-	139,163	-
	190,164	**-**	**163,262**	**-**

[2]Included in the line item 'other liabilities' in the balance sheet. In the previous year, the group only recognized lease liabilities in relation to leases that were classified as 'finance leases' under IAS 17 Leases. These were presented as part of the group's borrowings. For adjustments recognized on adoption of IFRS 16 on 1 January 2019, please refer to note 1.

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Additions to the right of use assets during the 2019 financial year	**11,026**	**-**	**10,143**	**-**

ii) Amounts recognized in the statement of profit or loss

The statement of profit or loss shows the following amounts relating to leases:

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Depreciation charge of right of use assets				
Properties and equipment	28,239	-	25,359	-
Interest expense (included in finance cost)	4,572	-	3,943	-
Expense relating to short-term leases(included in administrative expenses)	22,225	-	21,717	-
Expense relating to leases of low value assets that are not short term leases (included in administrative expenses)	35	-	-	-
Total cash outflow for leases in 2019	48,432	-	45,173	-

16. Investment properties

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Opening net book value	153,665	134,020	-	-
Additions	6,619	13,930	-	-
Translation movement	1,632	(299)	-	-
Gain on revaluation	6,444	6,014	-	-
At 31 December	**168,360**	**153,665**	**-**	**-**

Investment properties have been accounted for in accordance with Note 1 (u).

17. Other financial assets

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Inscribed stock – issued by Central Bank	1,870,869	2,373,104	1,577,701	2,079,723
Less allowance for impairment	(5,170)	(6,004)	(4,946)	(5,850)
	1,865,699	**2,367,100**	**1,572,755**	**2,073,873**
Financial assets carried at fair value through profit and loss:				
Equity securities	255,372	188,343	-	-
At 31 December	**2,121,071**	**2,555,443**	**1,572,755**	**2,073,873**
Allowance for impairment				
At 1 January	6,004	5,984	5,850	5,850
Provision/(release) for impairment	(834)	20	(904)	-
At 31 December	**5,170**	**6,004**	**4,946**	**5,850**

18. Other assets

Funds in transit and other assets	194,315	48,466	146,054	41,863
Accrued interest income	101,066	99,785	93,535	92,532
Intercompany account	-	-	6,960	3,067
Outstanding premiums	17,681	14,954	-	-
Inventory	17,837	12,263	-	-
Prepayments	32,524	25,656	27,815	22,201
Accounts receivable	3,571	4,358	2,254	2,630
At 31 December	**366,994**	**205,482**	**276,618**	**162,293**

19. Amounts due to other banks

Vostro account balances	47,083	29,375	66,786	62,465
Other borrowings	36,848	22,164	95,359	53,554
At 31 December	**83,931**	**51,539**	**162,145**	**116,019**

20. Customer deposits

On demand and short term deposits	15,322,280	13,903,428	14,605,182	13,168,693
Term deposits	4,016,776	4,329,338	3,376,574	3,790,477
At 31 December	**19,339,056**	**18,232,766**	**17,981,756**	**16,959,170**

The majority of the amounts are due to be settled within twelve months of the balance sheet date as shown in the maturity analysis table on note 35. The deposits are diversified across industries and region.

21. Subordinated debt securities

Outstanding debt securities of K75.525m were settled in May 2019. The notes were issued during 2009, with a maturity date in May 2019, and interest payable semi-annually at 11% per annum. They were valued at amortised cost. There were no defaults of interest or other breaches with respect to these debt securities since issue.

22. Other liabilities

		Consolidated		Bank	
All amounts are expressed in K'000	*Note*	**2019**	**2018**	**2019**	**2018**
Policy liability	40(b)	890,147	818,198	-	-
Items in transit and all other liabilities		532,684	431,950	520,720	447,460
Borrowings		116,817	144,300	116,817	144,300
Creditors and accruals		184,941	202,789	122,218	175,221
Premiums received in advance		6,329	5,895	-	-
Outstanding claims		18,679	18,429	-	-
Claims incurred but not reported (IBNR)		2,297	2,431	-	-
At 31 December		**1,751,894**	**1,623,992**	**759,755**	**766,981**

Reconciliation of changes in liabilities arising from financing activities
A loan amounting to K253.969 million (USD80 million) was obtained in 2016 with principal repayment to commence in 2018. During 2019, the Bank paid K69.493 million and an additional loan of K33.670 million was received. Foreign currency gain of K8.340 million was recognised arising from translation, offset by depreciation of the counter party loan.

23. Other provisions

Staff related	99,629	89,674	84,934	76,543
Provision for non-lending loss	57,726	65,217	57,726	65,215
Provisions – other	46,307	39,212	43,914	36,041
	203,662	**194,103**	**186,574**	**177,799**
Staff related provisions:				
At 1 January	89,674	88,071	76,543	75,233
Provisions charge	76,227	74,525	71,812	69,787
Payouts	(66,272)	(72,922)	(63,421)	(68,477)
At 31 December	**99,629**	**89,674**	**84,934**	**76,543**

24. Ordinary shares

Number of shares in '000s, Book value in K'000	**Number of shares**	**Book value**
At 31 December 2016/1 January 2018	**467,312**	**373,001**
Share buyback	(66)	(637)
At 31 December 2018/1 January 2019	**467,246**	**372,364**
Share buyback	(6)	(54)
At 31 December 2019	**467,240**	**372,310**

In May 2014, the Directors introduced a share-buyback scheme of up to K15 million. The share-buyback commenced in July 2014 and was extended to such time when the allocated K15 million buyback was utilised, or if the Board wishes, anytime before that. As at 31 December 2019, a total of K9.192m has been bought back under this scheme.

24. Ordinary shares (continued)

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Earnings per ordinary share				
Net profit attributable to shareholders (K'000)	890,363	844,072	845,828	787,446
Weighted average number of ordinary shares in use ('000)	467,242	467,279	467,242	467,279
Basic and diluted earnings per share (expressed in toea)	**190.6**	**180.6**	**181.0**	**168.5**

Basic earnings per ordinary share is calculated by dividing the net profit attributable to shareholders by the weighted average number of ordinary shares in issue during the year. Bank of South Pacific Limited has no dilutive potential ordinary shares. Consequently, basic earnings per ordinary share equals diluted earnings per share.

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Dividends paid on ordinary shares				
Interim ordinary dividend (2019: 38 toea; 2018:36 toea)	177,551	169,341	177,551	168,210
Final ordinary dividend (2018:101 toea; 2017:91 toea)	476,389	428,023	471,915	425,204
	653,940	**597,364**	**649,466**	**593,414**

25. Retained earnings and other reserves

	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Retained earnings				
At 1 January	2,156,873	1,904,462	1,976,138	1,777,627
IFRS 9 transition provisions	-	(14,147)	-	(14,601)
Tax impact on IFRS 9 transition provisions	-	4,244	-	4,380
Restated balance as at 1 January 2019	**2,156,873**	**1,894,559**	**1,976,138**	**1,767,406**
Net profit for the year	890,363	844,072	845,828	787,446
Dividends paid	(476,389)	(428,023)	(471,915)	(425,204)
Interim Dividends paid	(177,551)	(169,341)	(177,551)	(168,210)
Disposal of assets – Asset revaluation	4,933	18,116	4,933	18,116
BSP Life policy reserve	(3,597)	(3,416)	(3,597)	(3,416)
(Gain)/loss in minority interest	(250)	906	-	-
At 31 December	**2,394,382**	**2,156,873**	**2,173,836**	**1,976,138**
Other reserves comprise				
Revaluation reserve	142,819	149,829	130,725	137,708
Capital reserve	635	635	635	635
Equity component of Fiji Class Shares	21,578	21,578	-	-
General reserve	44,503	40,920	44,503	40,920
Exchange reserve	136,978	126,358	78,614	73,121
	346,513	**339,320**	**254,477**	**252,384**
Movement in reserves for the year:				
Revaluation reserve				
At 1 January	149,829	161,373	137,708	150,389
Asset revaluation increment/(decrement)	(5,719)	1,624	(5,714)	-
Transfer asset revaluation reserve to retained earnings	(4,933)	(18,116)	(4,933)	(18,116)
Deferred tax on disposal of properties	3,642	4,948	3,664	5,435
At 31 December	**142,819**	**149,829**	**130,725**	**137,708**

25. Retained earnings and other reserves (continued)

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Capital reserve				
At 1 January	635	635	635	635
At 31 December	**635**	**635**	**635**	**635**
General reserve				
At 1 January	40,920	37,496	40,920	37,496
BSP Life policy reserve	3,597	3,416	3,597	3,416
Fiji Government green bond revaluation	(14)	8	(14)	8
At 31 December	**44,503**	**40,920**	**44,503**	**40,920**
Exchange reserve				
At 1 January	126,358	125,306	73,121	71,854
Movement during the year	10,620	1,052	5,493	1,267
At 31 December	**136,978**	**126,358**	**78,614**	**73,121**

Equity component of convertible notes

On 20 April 2010, the Group issued 3,064,967 Fiji Dollars (FJD) denominated mandatory convertible notes through its wholly owned subsidiary BSP Convertible Notes Limited (BSP CN) at an issue price of FJD5.25 (K7.30) per note.

The notes mandatorily converted to Fiji Class Shares on 20 April 2013 based on a conversion ratio of 1:1. Key rights of Fiji Class Shareholders are as follows:

(i) The right to receive dividend equal to the amount of dividend to be paid on BSP Ordinary Share.

(ii) The same voting rights as a BSP Ordinary Share and effected through a special voting share held by the Chairman of BSP.

(iii) The Fiji Class Share may be exchanged on a one for one basis into BSP Ordinary Shares at a subsequent date and at the option of BSP on the occurrence of certain prescribed events.

26. Contingent liabilities and commitments

Off balance sheet financial instruments	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Letters of credit	121,600	135,219	117,057	133,560
Guarantees and indemnities issued	366,170	473,748	341,373	433,978
Commitments to extend credit	2,088,924	1,626,879	2,003,881	1,497,722
	2,576,694	**2,235,846**	**2,462,311**	**2,065,260**

Legal Proceedings

A number of legal proceedings against the Group were outstanding as at 31 December 2019. Based on information available at 31 December 2019, the Group estimates a contingent liability of K15.8 million (2018: K21.1 million) in respect of these proceedings.

26. Contingent liabilities and commitments (continued)

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Commitments for capital expenditure				
Amounts with firm commitments not reflected in the accounts	**55,829**	**21,017**	**51,313**	**19,702**
Operating lease commitments (premises)				
Not later than 1 year	34,603	38,848	28,238	36,341
Later than 1 year and not later than 5 years	105,573	56,210	89,486	52,491
Later than 5 years	115,811	22,312	78,861	20,226
	255,987	**117,370**	**196,585**	**109,058**

27. Fiduciary activities

The Group especially through BSP Capital Limited conducts investment fund management and other fiduciary activities as responsible entity, trustee, custodian or manager for investment funds and trusts, including superannuation. These funds are not consolidated as the Group does not have direct or indirect control. Where the funds incur liabilities in respect of these activities, and the primary obligation is incurred in an agency capacity for the fund or clients rather than its own account, a right of indemnity exists against the assets of the applicable fund or trust. As these assets are sufficient to cover the liabilities and it is therefore not probable that the Group will be required to settle the liabilities, the investments in the assets and liabilities of these activities are not included in the Financial Statements.

28. Directors and executive remuneration

Directors remuneration

Directors of the company received remuneration including benefits during 2019 as detailed below:

All amounts are in Kina — **Total remuneration**

Name of Director	Meetings attended / total held	Appointed/ (Resigned)	2019 Bank	2019 Subsidiaries	2019 Total	2018 Total
Sir K. Constantinou, OBE**	8/8	-	561,304	360,000	921,304	1,311,304
R. Fleming, CSM*	8/8	-	-	-	-	-
G. Robb, OAM**	7/8	-	343,152	120,000	463,152	613,152
F. Talao	8/8	(Dec 2019)	318,152	60,000	378,152	378,152
E. B Gangloff	8/8	-	343,152	60,000	403,152	403,152
A. Mano**	6/8	-	280,652	60,000	340,652	490,652
A. Sam	8/8	-	330,652	-	330,652	330,652
Dr. F Lua'iufi	8/8	-	305,652	-	305,652	305,652
S. Davis	8/8	-	330,652	-	330,652	330,652
R. Bradshaw	8/8	-	305,652	-	305,652	305,652
			3,119,020	**660,000**	**3,779,020**	**4,469,020**
Shareholder Approved Cap					**4,500,000**	**4,500,000**

* Managing Director/Chief Executive Officer receives no fees for his services as Director during the year. Other members of BSP executive management who serve as directors of subsidiaries of BSP Group receive no fees for their services as Director.

** The 2018 remuneration included backdated allowances from 2015 to 2017 paid to directors for BSP Subsidiary boards as follows: Constantinou - K390,000, Robb - K150,000 and Mano K150,000.

28. Directors and executive remuneration (continued)

Executive remuneration

The number of employees or former employees whose income from the Bank was equal to or greater than K100,000 during the year, are classified in income bands of K10,000 as follows:

Remuneration *K'000*	2019 No.	2018 No.	Remuneration *K'000*	2019 No.	2018 No.	Remuneration *K'000*	2019 No.	2018 No.
100 – 110	53	72	500 – 510	3	2	960 - 970	1	1
110 – 120	61	53	510 – 520	2	-	970 – 980	-	1
120 – 130	47	41	520 – 530	4	-	980 - 990	1	-
130 – 140	31	22	530 – 540	2	1	1000 – 1010	1	1
140 – 150	29	30	540 – 550	-	1	1010 – 1020	-	2
150 – 160	17	21	550 – 560	1	-	1020 - 1030	1	2
160 – 170	20	21	560 – 570	-	2	1040 – 1050	-	1
170 – 180	23	14	570 – 580	2	2	1050 – 1060	-	1
180 – 190	16	20	580 – 590	1	2	1060 – 1070	2	3
190 – 200	11	10	590 – 600	2	3	1070 – 1080	1	1
200 – 210	15	10	600 – 610	1	-	1090 – 1100		1
210 – 220	14	11	610 – 620	3	2	1110 – 1120	1	1
220 – 230	9	11	620 – 630	1	2	1120 – 1130	1	1
230 – 240	8	9	630 – 640	-	1	1130 – 1140	1	1
240 – 250	16	6	640 – 650	1	-	1140 - 1150	1	-
250 – 260	4	2	650 – 660	2	-	1150 – 1160	-	1
260 – 270	4	1	660 – 670	2	1	1180 – 1190	1	1
270 – 280	5	2	670 – 680	-	1	1220 -1230	1	-
280 – 290	-	4	680 – 690	1	-	1260– 1270	1	-
290 – 300	5	2	690 – 700	-	1	1280 – 1290	1	-
300 – 310	4	2	700 – 710	1	-	1290 – 1300	-	1
310 – 320	5	1	720 – 730	1	2	1300 - 1310	2	-
320 – 330	-	3	730 – 740	1	-	1400 – 1410	1	1
330 – 340	2	3	740 - 750	1	-	1430 – 1440	1	1
340 – 350	1	2	750 - 760	1	-	1470 - 1480	-	2
350 – 360	2	7	770 -780	2	-	1480 - 1490	1	-
360 – 370	2	-	780 – 790	3	2	1490 - 1500	1	-
370 – 380	5	4	790 – 800	3	1	1550 - 1560	1	-
380 – 390	-	3	810 – 820	-	1	1680 - 1690	-	1
390 – 400	1	4	820 – 830	1	1	1740 - 1750	1	-
400 – 410	2	1	840 – 850	1	1	1750 - 1760	1	-
410 – 420	1	7	860 - 870	1	2	1760 - 1770	1	1
420 – 430	11	3	870 - 880	2	-	1770 - 1780	-	1
430 – 440	2	4	880 – 890	1	-	1850 - 1860	1	--
440 – 450	3	1	890 - 900	1	1	1880 - 1890	-	1
450 - 460	1	4	900 – 910	1	1	2150 - 2160	1	-
460 - 470	4	2	910 – 920	-	2	2500 - 2510	1	-
470 – 480	3	4	920 - 930	-	1	2560 - 2580	-	1
480 – 490	2	2	930– 940	2	-	5960 - 5970	-	1
490 – 500	4	1	950 - 960	-	1	6280 - 6290	1	-
						Total	**523**	**487**

28. Directors and executive remuneration (continued)

The specified executives during the year received these remuneration:

2019

Officer	Salary	Short Term Incentive	Non monetary	Super-annuation	Long Term Incentive	Benefits	Total
R Fleming CSM	4,148	929	43	-	1,112	49	6,281
R Loggia	1,501	267	113	-	439	188	2,508
E Ruha	1,321	323	67	-	387	54	2,152
P Beswick	1,095	268	68	-	320	103	1,854
R George	1,080	264	68	-	316	37	1,765
M Hallinan	1,095	247	66	-	320	30	1,758
P Thornton	1,095	262	30	-	320	40	1,747
D Faunt	887	168	67	75	260	40	1,497
C Michaud	901	217	66	-	264	39	1,487
N Kulu	739	208	153	62	219	28	1,409
H Rabura	747	139	111	63	219	22	1,301
A M Fenech	255	-	4	-	-	15	274
Total	**14,864**	**3,292**	**856**	**200**	**4,176**	**645**	**24,033**

2018

Officer	Salary	Short Term Incentive	Non monetary	Super-annuation	Long Term Incentive	Benefits	Total
R Fleming CSM	3,823	1,053	21	-	1,039	27	5,963
R Loggia	1,513	356	102	-	444	174	2,589
E Ruha	1,332	365	57	-	391	48	2,193
P Beswick	1,104	296	57	-	324	96	1,877
R George	1,088	282	57	-	320	23	1,770
P Thornton	1,104	283	21	-	324	36	1,768
M Hallinan	984	246	57	-	247	18	1,552
C Michaud	908	205	57	-	267	36	1,473
H Rabura	752	180	75	62	210	9	1,288
D Faunt	871	-	57	41	-	27	996
N Kulu	507	-	21	41	70	15	654
A Baliki	335	-	10	29	-	20	394
Total	**14,321**	**3,266**	**592**	**173**	**3,636**	**529**	**22,517**

29.

All amounts are expressed in K'000	Consolidated 2019	Consolidated 2018	Bank 2019	Bank 2018
Reconciliation of operating profit after tax to operating cash flow before changes in operating assets				
Operating profit after tax	890,363	844,072	845,828	787,446
Add: Tax expense	362,556	352,096	342,439	329,093
Operating profit before income tax	**1,252,919**	**1,196,168**	**1,188,267**	**1,116,539**
Major non cash amounts				
Depreciation	107,906	81,000	90,352	64,572
Amortisation of deferred acquisition and computer development costs	28,173	27,399	22,577	22,546
Net (Gain)/loss on sale of fixed assets	(2,088)	1,879	33	1,879
Movement in forex income accrual	10,620	1,052	5,493	1,267
Impairment on financial assets	99,183	82,440	88,092	71,639
Movement in payroll provisions	9,956	1,603	8,391	1,310
Impairment of subsidiary	-	-	-	803
Impairment of fixed assets	1,975	13,888	1,975	13,888
Net effect of other accruals	(68,417)	18,753	(5,074)	30,398
Operating cash flow before changes in operating assets & liabilities	**1,440,227**	**1,424,182**	**1,400,106**	**1,324,841**

Cash and cash equivalents
For the purposes of the cash flow statement, cash and cash equivalents comprise the following balances with less than 90 days maturity.

Cash and balances with Central Banks (note 10)	1,816,564	1,253,449	1,510,406	966,707
Amounts due from other banks (note 12)[1]	1,022,469	854,019	997,816	796,180
Amounts due to other banks (note 19)	(83,931)	(51,539)	(162,145)	(116,019)
	2,755,102	**2,055,929**	**2,346,077**	**1,646,868**

[1]The Group undertakes thorough compliance and due diligence reviews before entering into any correspondent banking relationships. There is also a cash and cash equivalent of K31.275 million held with counter-party Banks that are not available for use by the Group.

30. Segment information

The Bank and the Group comprise various segments, these being the provision of banking services and products, stock broking and insurance services and asset financing. For management purposes, segment information determination is based on the risks involved with the provision of core banking services and products and the Bank and Group's management reporting system. The main business lines for management purposes are core banking services in Papua New Guinea, Banking Services in other jurisdictions outside Papua New Guinea, insurance operations, stock broking, fund management and asset financing activities. The Bank and Group's business segments operate in Papua New Guinea, Fiji, Solomon Islands, Cook Islands, Tonga, Samoa, Vanuatu and Cambodia. Inter segment adjustments reflect elimination entries in respect of inter segment income and expense allocations included funds transfer pricing.

30. Segment information (continued)

Consolidated

All amounts are expressed in K'000	PNG Bank	Non PNG Bank	Non-Bank Entities	Adjust Inter Segments	Total
Analysis by segments					
Year ended 31 December 2019					
Net interest income	1,115,454	241,808	30,772	3,750	1,391,784
Other income	542,027	243,347	18,496	(54,979)	748,891
Net insurance income	-	-	34,999	(4,324)	30,675
Total operating income	**1,657,481**	**485,155**	**84,267**	**(55,553)**	**2,171,350**
Operating expenses	(582,740)	(220,439)	(20,393)	4,324	(819,248)
Impairment expenses	(58,555)	(36,244)	(4,384)	-	(99,183)
Profit before income tax	**1,016,186**	**228,472**	**59,490**	**(51,229)**	**1,252,919**
Income tax	(297,480)	(58,085)	(6,991)	-	(362,556)
Net profit after income tax	**718,706**	**170,387**	**52,499**	**(51,229)**	**890,363**
Year ended 31 December 2018					
Net interest income	1,118,342	232,513	27,707	2,234	1,380,796
Other income	532,234	228,731	11,735	(26,704)	745,996
Net insurance income	-	-	40,512	(1,599)	38,913
Total operating income	**1,650,576**	**461,244**	**79,954**	**(26,069)**	**2,165,705**
Operating expenses	(632,386)	(236,598)	(18,624)	511	(887,097)
Impairment expenses	(56,190)	(22,227)	(4,023)	-	(82,440)
Profit before income tax	**962,000**	**202,419**	**57,307**	**(25,558)**	**1,196,168**
Income tax	(287,802)	(51,409)	(12,885)	-	(352,096)
Net profit after income tax	**674,198**	**151,010**	**44,422**	**(25,558)**	**844,072**

31. Related party transactions

Related parties are considered to be enterprises or individuals with whom the Group is especially related because either they or the Bank 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 year:

- Directors and/or parties in which the 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. These transactions are carried out on commercial terms and market rates. For the year ended 31 December 2019, balances and transactions of accounts for Directors, including companies in which directorships were held by BSP directors, were as follows:

31. Related party transactions (continued)

All amounts are expressed in K'000	Consolidated 2019	2018
Customer Deposits		
Opening balances	30,925	17,731
Net movement	14,295	13,194
Closing balance	**45,220**	**30,925**
Interest paid	17	24
Loans, advances and other receivables from customers		
Opening balances	899,451	631,650
Loans issued[1]	61,750	458,213
Interest	66,032	44,390
Charges	3,869	3,376
Loan repayments	(116,634)	(238,178)
Closing balance	**914,468**	**899,451**

[1]2018 included Air Niugini Limited loan following Director Constantinou's appointment to the Board of Air Niugini Limited during 2018. Air Niugini Limited has been a customer of BSP since inception and had pre-existing facilities with BSP prior to 2018.

Subsidised transactions are provided for staff. Such transactions include marginal discounts on interest rates, and specific fee concessions. These benefits are mainly percentage-based on market rates and fees, and as such, staff accounts are always subject to underlying market trends in interest rates and fees. As at 31 December 2019, staff account balances were as follows:

All amounts are expressed in K'000	2019	2018
Housing loans	192,749	169,858
Other loans	68,197	43,826
	260,946	**213,684**
Cheque accounts	6,643	7,533
Savings accounts	20,824	13,532
	27,467	**21,065**

32. Bank operations, risks and strategies in using financial instruments

All business operations must deal with a variety of operational and financial risks. The business activities of a bank expose it to very critical and specific risks, which are principally related to the Group's primary financial intermediary role in the financial markets, including the use of financial instruments including derivatives. These risks (risk of an adverse event in the financial markets that may result in loss of earnings) include liquidity risk, foreign exchange risk, interest rate risk and credit risk.

The Group accepts deposits from customers at both fixed and floating rates and for various periods and seeks to earn above average interest margins by investing these funds in high quality assets. These margins are achieved and increased by consolidating short-term funds and lending for longer periods at higher rates whilst maintaining sufficient liquidity to meet all claims that might fall due.

The Group also seeks to optimise its interest margins by obtaining above average returns, net of provisions, through lending to commercial and retail borrowers with a range of credit standing. In addition to directly advancing funds to borrowers, the Group also enters into guarantees and other commitments such as letters of credit, performance bonds, and other bonds.

32. Bank operations, risks and strategies in using financial instruments (continued)

The Group also enters into transactions denominated in foreign currencies. This activity generally requires the Group to take foreign currency positions in order to exploit short term movements in the foreign currency market. The Board places limits on the size of these positions. The Group also has a policy of using offsetting commitments for foreign exchange contracts, effectively minimising the risk of loss due to adverse movements in foreign currencies.

Risk in the Group is managed through a system of delegated limits. These limits set the maximum level of risk that can be assumed by each operational unit and the Group as a whole. The limits are delegated from the Board of Directors to executive management and hence to the respective operational managers.

The risk management framework establishes roles, responsibilities and accountabilities of the Asset and Liability Committee, the Credit Committee, the Operational Risk Committee and the Executive Committee, the specific management committees charged with the responsibility for ensuring the Group has appropriate systems, policies and procedures to measure, monitor and report on risk management. The framework also includes policies and procedures which detail formal feedback processes to these management committees, to the Audit, Risk and Compliance Committee of the Board, and ultimately to the Board of Directors.

33. Capital adequacy

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, Cook Islands, Samoa, Tonga ,Vanuatu and Cambodia are required to adhere to prudential standards issued by the Reserve Bank of Fiji (RBF), Central Bank of Solomon Islands (CBSI), The Financial Supervisory Commission (FSC), Central Bank of Samoa (CBS), National Reserve Bank of Tonga (NRBT), Reserve Bank of Vanuatu (RBV)and the National Bank of Cambodia (NBC). One of the most critical prudential standards is the capital adequacy requirement. All banks are required to maintain at least the minimum acceptable 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 capitalised, and also applies the leverage capital ratio. The Group complies with the prevailing prudential requirements for total capital and leverage capital. As at 31 December 2019, 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 set out under the standard are: Tier 1 8%, total risk based capital ratio 12% and the leverage ratio 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 subordinated 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.

33. Capital adequacy (continued)

The Group's capital adequacy level is as follows:

All amounts are expressed in K'000	Balance sheet / notional amount 2019	Balance sheet / notional amount 2018	Risk-weighted amount 2019	Risk-weighted amount 2018
Balance sheet assets (net of provisions)				
Currency	3,583,165	2,938,993	69,942	19,502
Loans, advances and other receivables from customers	13,230,783	12,530,649	10,539,279	9,813,150
Investments and short term securities	4,580,568	5,050,143	224,510	188,343
All other assets	3,132,602	2,530,275	1,839,673	1,444,738
Off-balance sheet items	2,576,694	2,235,846	286,666	322,716
Total	**27,103,812**	**25,285,906**	**12,960,070**	**11,788,449**

Capital Ratios	Capital (K'000) 2019	Capital (K'000) 2018	Capital Adequacy Ratio (%) 2019	Capital Adequacy Ratio (%) 2018
a) Tier 1 capital	2,526,509	2,338,587	19.5%	19.8%
Total Capital	2,848,723	2,694,901	22.0%	22.9%
b) Leverage Capital Ratio			10.5%	10.3%

34. Credit risk and asset quality

34.1 Credit Risk

The Group incurs risk with regard to loans, advances and other receivables due from customers and other monies or investments held with financial institutions. Credit risk is the likelihood of future financial loss resulting from the failure of clients or counter-parties to meet contractual obligations to the Group as they fall due.

Credit risk is managed by analysing the risk spread across various sectors of the economy and by ensuring risk is diversely spread by personal and commercial customer. Individual exposures are measured using repayment performance, reviews and statistical techniques. Comprehensive credit standards and approval limits have been formulated and approved by the Credit Committee. The Credit Committee (which reports to the Board through the Executive and Chief Executive Officer) is responsible for the development and implementation of credit policy and loan portfolio review methodology. The Credit Committee is the final arbiter of risk management and loan risk concentration.

The Group has in place processes that identify, assess and control credit risk in relation to the loan portfolio, to assist in determining the appropriateness of provisions for loan impairment. These processes also enable assessments to be made of other classes of assets that may carry an element of credit risk. The Group assigns quality indicators to its credit exposures to determine the asset quality profile.

34.1.1 Credit Risk Measurement

a) Loans and advances (incl. loan commitments and guarantees)

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using Probability of Default (PD), Exposure at Default (EAD) and Loss Given Default (LGD).

34. Credit risk and asset quality (continued)

Credit risk grading

The Group uses an internal credit risk grading system that reflects its assessment of the probability of default of individual counterparties. Borrower and loan specific information collected at the time of application (such as disposable income, and level of collateral for retail exposures; and turnover and industry type for wholesale exposures) is fed into this rating model. This is supplemented with external data such as credit bureau scoring information on individual borrowers. In addition, the models enable expert judgement from the Chief Risk Officer to be fed into the final internal credit rating for each exposure. This allows for considerations which may not be captured as part of the other data inputs into the model.

The Group's rating method comprises 11 rating levels for instruments not in default (1 to 11) and three default classes (12 to 14). The master scale assigns each rating category a specified range of probabilities of default, which is stable over time. The rating methods are subject to an annual validation and recalibration so that they reflect the latest projections in the light of all actually observed defaults.

Group Internal Scale	S&P Letter Grade	Description
1	BBB+	Standard Monitoring
2	BBB	
3	BBB-	
4	BB+	
5	BB	
6	BB-	
7	B+	
8	B	
9	B-	
10	CCC+	Special Monitoring
11	CCC	
12	CCC-	Substandard
13	D-I	Doubtful
14	D-II	Loss

34.1.2 Expected Credit Loss Measurement

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

- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Group.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. Please refer to note 34.1.2.1 for a description of how the Group determines when a significant increase in credit risk has occurred.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Please refer to note 34.1.2.2 for a description of how the Group defines credit-impaired and default.

Financial instruments in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis. Please refer to note 34.1.2.3 for a description of inputs, assumptions and estimation techniques used in measuring the ECL.

34. Credit risk and asset quality (continued)

- A pervasive concept in measuring ECL in accordance with IFRS 9 is that it should consider forward-looking information. Note 34.1.2.3 includes an explanation of how the Group has incorporated this in its ECL models.

The following diagram summarises the impairment requirements under IFRS 9.

Change in credit quality since initial recognition

Stage 1	Stage 2	Stage 3
(Initial recognition)	(Significant increase in credit risk since initial recognition)	(Credit-impaired assets)
12-month expected credit losses	Lifetime expected credit losses	Lifetime expected credit losses

The key judgements and assumptions adopted by the Group in addressing the requirements of the standard are discussed below:

34.1.2.1 Significant Increase in Credit Risk (SICR)

The Group considers a financial instrument to have experienced a significant increase in credit risk when one or more of the following quantitative, qualitative or backstop criteria have been met:

- Qualitative Criteria - if the instrument meets one or more of the following criteria:
  - Significant adverse changes in business, financial and/or economic conditions in which the borrower operates
  - Actual or expected forbearance or restructuring
  - Actual or expected significant adverse change in operating results of the borrower
  - Significant change in collateral value (secured facilities only) which is expected to increase risk of default
  - Early signs of cash flow/liquidity problems such as delay in servicing of trade creditors/loans

- Quantitative criteria - applies to performing loans risk graded at 10 or 11 as per BSPs credit rating system which are 'watch list' categories. By definition, these have experienced a SICR event since inception hence needs to be classified as Stage 2, with lifetime PDs applicable. This criteria applies regardless of whether loans in these two RGs are in arrears or not.

- Backstop - A backstop is applied and the financial instrument considered to have experienced a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payments. The Group has not used the low credit risk exemption for any financial instrument in the year ending 31 December 2019.

34.1.2.2 Definition of default and credit-impaired assets

The Group defines a financial instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

Quantitative criteria

The borrower is more than 90 days past due on its contractual payments.

Qualitative criteria

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. These are instances where:

34. Credit risk and asset quality (continued)

- The borrower is in long-term forbearance
- The borrower is deceased
- The borrower is insolvent
- The borrower is in breach of financial covenant(s)
- An active market for that financial asset has disappeared because of financial difficulties
- Concessions have been made by the lender relating to the borrower's financial difficulty
- It is becoming probable that the borrower will enter bankruptcy
- Financial assets are purchased or originated at a deep discount that reflects the incurred credit losses.

The criteria above have been applied to all financial instruments held by the Group and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD) and Loss given Default (LGD) throughout the Group's expected loss calculations.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of six months. This period of six months has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different possible cure definitions.

34.1.2.3 Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or Lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition or whether an asset is considered to be credit-impaired. Expected credit losses is the product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- The PD represents the likelihood of a borrower defaulting on its financial obligation (as per "Definition of default and credit-impaired" above), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation.
- EAD is based on the amounts the Group expects to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For example, for a revolving commitment, the Group includes the current drawn balance plus any further amount that is expected to be drawn up to the current contractual limit by the time of default, should it occur.
- Loss Given Default (LGD) represents the Group's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD).

Forward-looking economic information is also included in determining the 12-month and lifetime PD, EAD and LGD. These assumptions vary by product type. Model adjustments are also included within the ECL allowance. Model adjustments are used in circumstances where it is judged that the existing inputs, assumptions and model techniques do not capture all relevant risk factors. The emergence of new macroeconomic, microeconomic factors, changes to parameters or credit risk data not incorporated current parameters are examples of such circumstance.

34. Credit risk and asset quality (continued)

The Group used statistical models to convert historical PDs into forward looking lifetime PDs. The conversion process looks at the historical relationship between long-term PDs for a particular year and the observed (annual) default rate for the same year (called the 'Z-factor') and a set of systematic factors for the year. The Group has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses which are as follows:

- GDP Growth (%)
- Change in Unemployment (%)
- Change in Equity Index (%)
- Change in Energy Index (%)
- Change in Non-Energy Index (%)
- Change in the Proportion of Downgrades (%)

These are then compared to the expected systematic factors and long-term PDs for a future year to estimate the PiT PDs for that future year. Forecasts of these economic variables (the "base economic scenario") are provided by the Group's Strategy team and provide the best estimate view of the economy over the next five years. Z-factors are estimated for five years based on forecast systematic data and all future years from year 6 are adjusted using Z- factors which diminish in magnitude from the one estimated for year 5.

Economic variable assumptions

The period-end assumptions used for the ECL estimate as at 31 December 2019 are set out below. The scenarios "base", "upside" and "downside" were used for all portfolios.

		2019	2020	2021	2022	2023
GDP Growth (%)	Base	2.60%	2.70%	2.80%	2.80%	2.80%
	Upside	3.60%	3.20%	3.50%	3.50%	3.50%
	Downside	2.10%	2.20%	2.30%	2.30%	2.30%
Change in Unemployment (% total lab force) (%)	Base	0.40%	0.00%	0.00%	0.00%	0.00%
	Upside	-1.00%	-1.00%	-1.00%	-1.00%	-1.00%
	Downside	5.00%	5.00%	5.00%	5.00%	5.00%
Change in Equity Index (%)	Base	-6.69%				
	Upside	-5.69%				
	Downside	-7.69%				
Change in Energy Index (%)	Base	-7.26%	-2.90%	-1.04%	-1.05%	-1.06%
	Upside	-6.76%	-2.40%	-0.54%	-0.55%	-0.56%
	Downside	-7.76%	-3.40%	-1.54%	-1.55%	-1.56%
Change in Non-Energy Index (%)	Base	-4.06%	-0.25%	-0.37%	-0.38%	-0.38%
	Upside	-3.56%	0.25%	0.13%	0.12%	0.12%
	Downside	-4.56%	-0.75%	-0.87%	-0.88%	-0.88%
Change in the Proportion of Downgrades (%)	Base	0.45%				
	Upside	-1.00%				
	Downside	10.00%				

34. Credit risk and asset quality (continued)

The weightings assigned to each economic scenario at 31 December 2019 were as follows:

Scenario	Base	Upside	Downside
Weight	60.00%	10.00%	30.00%

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

Sensitivity Analysis

The most significant assumptions affecting the ECL allowance are as follows:

i) GDP given the significant impact on business performance and collateral valuations; and

ii) Change in proportion of downgrades given that it is "BSP specific" and addresses potential signs of stress both within credit markets in general and in client specific portfolios.

Set out below are the changes to the ECL as at 31 December 2019 that would result from reasonably possible changes in these parameters from the actual assumptions used in the Group's economic variable assumptions:

All amounts are expressed in K'000	**2019**		**2018**	
	[-20%]	**[+10%]**	**[-20%]**	**[+10%]**
GDP Growth Rate	42,060	(19,342)	48,446	(17,586)

(GDP growth rate assumptions tested at 80% and 110% for all 3 scenarios)

All amounts are expressed in K'000	**2019**		**2018**	
	[-7%]	**[+20%]**	**[-5%]**	**[+20%]**
Change in proportion of downgrades	(1,088)	5,662	(1,451)	4,391

(Upside scenario increased from -1% to-7% (2018:-5%), downside scenario increased from 10% to 20%)

All amounts are expressed in K'000	**2019**	**2018**
Change in Scenario weighting	(32,714)	(30,002)

(Upside scenario increased from 10% to 30%, downside scenario decreased from 30% to 10%).

34.1.2.4 Grouping of instruments for losses measured on a collective basis

For expected credit loss provisions modelled on a collective basis, a grouping of exposures is performed on the basis of shared risk characteristics, such that risk exposures within a group are homogeneous.

In performing this grouping, there must be sufficient information for the group to be statistically credible. Where sufficient information is not available internally, the Group has considered benchmarking internal/external supplementary data to use for modelling purposes. The characteristics and any supplementary data used to determine groupings are outlined below:

Retail – Groupings for collective measurement

- Loan to value ratio band
- Risk Grade
- Product type (e.g. Residential/Buy to Let mortgage, Overdraft, Credit Card)

34. Credit risk and asset quality (continued)

- Repayment type (e.g. Repayment/Interest only)
- Utilisation band

Notwithstanding the grouping detailed above, all stage 3 loans are individually assessed.

The appropriateness of groupings is monitored and reviewed on a periodic basis by the Credit Risk team.

34.1.3 Credit Risk Exposure

34.1.3.1 Maximum exposure to credit risk – Financial instruments subject to impairment

The following table contains an analysis of the credit risk exposure of financial instruments for which an ECL allowance is recognised. The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets.

	2019				2018
ECL staging	**Stage 1**	**Stage 2**	**Stage 3**		
(PGK'000)	12-month ECL	Lifetime ECL	Lifetime ECL	**Total**	**Total**
Credit grade					
Standard monitoring	15,423,086	160,322	-	15,583,408	14,457,564
Special monitoring	-	503,009	-	503,009	588,756
Default	-	-	391,688	391,688	350,285
Gross carrying amount	15,423,086	663,331	391,688	16,478,105	15,396,605
Loss allowance	(277,795)	(199,510)	(223,299)	(700,604)	(633,567)
Carrying amount	**15,145,291**	**463,821**	**168,389**	**15,777,501**	**14,763,038**

Information on how the Expected Credit Loss (ECL) is measured and how the three stages above are determined is included in note 34.1.2 'Expected credit loss measurement'. The gross carrying amount includes off balance sheet items which are in scope for impairment.

34.1.3.2 Maximum exposure to credit risk – Financial instruments not subject to impairment

The following table contains an analysis of the maximum credit risk exposure from financial assets not subject to impairment (i.e. FVPL):

Maximum exposure to credit risk *(PGK000's)*	**2019**	**2018**
Trading assets		
• Equity Securities	255,372	188,343

34. Credit risk and asset quality (continued)

34.1.3.3 Collateral and other credit enhancements

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 prepares a valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically. The principal collateral types for loans and advances are:

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

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured.

Collateral held as security for financial assets other than loans and advances depends on the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured, with the exception of asset-backed securities and similar instruments, which are secured by portfolios of financial instruments.

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:

31 December 2019	**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	6,588	1,437	5,151	11,739
• Credit cards	-	-	-	-
• Term loans	18,112	3,263	14,849	23,739
• Mortgages	99,008	40,295	58,713	165,415
Loans to corporate entities:				
• Large corporate customers	197,754	142,074	55,680	127,761
• Small and medium-sized enterprises (SMEs)	67,172	33,771	33,401	79,439
• Others	3,054	2,459	595	5,745
Total credit-impaired assets	**391,688**	**223,299**	**168,389**	**413,838**
31 December 2018				
Total credit-impaired assets	**350,285**	**179,222**	**171,063**	**301,488**

34. Credit risk and asset quality (continued)

34.1.4 Loss allowance

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

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;Foreign exchange retranslations for assets denominated in foreign currencies and other movements; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period.

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

31 December 2019	Stage 1	Stage 2	Stage 3	
Expected Credit Loss	**12-month ECL**	**Lifetime ECL**	**Lifetime ECL**	**Total**
	PGK'000	**PGK'000**	**PGK'000**	**PGK'000**
Movements with P&L impact				
Transfers:				
Transfer from Stage 1 to Stage 2	(3,790)	25,930	-	22,140
Transfer from Stage 1 to Stage 3	(857)	-	18,171	17,314
Transfer from Stage 2 to Stage 1	4,316	(22,327)	-	(18,011)
Transfer from Stage 2 to Stage 3	-	(3,993)	12,451	8,458
Transfer from Stage 3 to Stage 2	-	76	(83)	(7)
Transfer from Stage 3 to Stage 1	7	-	(100)	(93)
New financial assets originated or purchased	118,207	14,232	8,168	140,607
Changes in PDs/LGDs/EADs/others	(81,067)	(33,183)	22,906	(91,344)
Total net P&L charge during the period	**36,816**	**(19,265)**	**61,513**	**79,064**
31 December 2018				
Total net P&L charge during the period	**(19,446)**	**34,480**	**51,039**	**66,073**

34. Credit risk and asset quality (continued)

The movement in gross carrying amounts between the beginning and the end of the annual period are included in the table below:

31 December 2019	**Stage 1**	**Stage 2**	**Stage 3**	
Gross Carrying Amount	**12-month Balance**	**Lifetime Balance**	**Lifetime Balance**	**Total**
	PGK'000	**PGK'000**	**PGK'000**	**PGK'000**
Movements in gross carrying amount with P&L impact				
Transfers:				
Transfer from Stage 1 to Stage 2	(146,559)	188,204	-	41,645
Transfer from Stage 1 to Stage 3	(66,009)	-	61,607	(4,402)
Transfer from Stage 2 to Stage 1	128,598	(153,149)	-	(24,551)
Transfer from Stage 2 to Stage 3	-	(35,089)	32,205	(2,884)
Transfer from Stage 3 to Stage 2	-	848	(1,238)	(390)
Transfer from Stage 3 to Stage 1	396	-	(398)	(2)
New financial assets originated or purchased	4,774,634	82,056	5,606	4,862,296
Changes in PDs/LGDs/EADs/others	(3,554,951)	(176,397)	(58,864)	(3,790,212)
Total movement in gross carrying amount with P&L impact	**1,136,109**	**(93,527)**	**38,918**	**1,081,500**
31 December 2018				
Total movement in gross carrying amount with P&L impact	**1,325,422**	**138,738**	**90,154**	**1,554,314**

34.1.5 Write-off policy

The Group writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) where the Group's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full.

The Group may write-off financial assets that are still subject to enforcement activity. The Group still seeks to recover amounts it is legally owed in full, but which have been partially written off due to no reasonable expectation of full recovery.

34. Credit risk and asset quality (continued)

34.1.6 Credit Quality – Prudential Guidelines

The Bank of Papua New Guinea has maintained a revised prudential standard for asset quality since October 2003. The revised standard specifies more detailed criteria for the classification of loans into various grades of default risk and corresponding loss provision levels as a consequence of those gradings.

An analysis by credit quality of loans outstanding at 31 December 2019 is as follows:

Consolidated	Overdrafts	Term loans	Mortgages	Lease financing	Policy loans	Total
Neither past due nor impaired	**917,146**	**9,182,602**	**2,266,451**	**281,535**	**88,280**	**12,736,014**
Past due but not impaired						
- Less than 30 days	78,078	315,403	135,827	3,334	-	532,642
- 30 to 90 days	2,703	259,078	73,368	1,311	-	336,460
	80,781	**574,481**	**209,195**	**4,645**	**-**	**869,102**
Individually impaired loans						
- Less than 30 days	3,183	4,160	3,641	328	-	11,312
- 30 to 90 days	169	9,173	10,711	2,064	-	22,117
- 91 to 360 days	1,504	31,535	28,139	1,339	-	62,517
- More than 360 days	6,093	101,612	87,174	5,470	-	200,349
	10,949	**146,480**	**129,665**	**9,201**	**-**	**296,295**
Total gross loans, advances and other receivables to customers	**1,008,876**	**9,903,563**	**2,605,311**	**295,381**	**88,280**	**13,901,411**
Less impairment provisions						(700,604)
Net Loans and Advances						**13,200,807**

34.1.7 Credit related commitments

These instruments are used to ensure that funds are available to a customer as required. The Group deals principally in the credit related commitments set out below.

Guarantees and standby letters of credit, which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties, carry the same risk as loans.

Documentary and trade letters of credit are written undertakings by the Group on behalf of a customer, authorising a third party to draw drafts on the Group for specified amounts under specified terms and conditions. They are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a conventional loan.

Commitments to extend credit represent undrawn portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. Whilst the potential exposure to loss equates to the total undrawn commitments, the likely amount of loss is less than the total commitment since the commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of these commitments because longer term commitments generally carry a greater degree of credit risk than shorter term commitments.

34. Credit risk and asset quality (continued)

34.1.8 Economic sector risk concentrations

Economic sector risk concentrations within the customer loan portfolio are as follows:

All amounts are expressed in K'000

Consolidated As at 31 December	2019	%	2018	%
Commerce, finance and other business	7,159,863	54	6,824,314	54
Private households	2,987,459	23	2,569,986	21
Government and public authorities	252,134	2	356,166	3
Agriculture	327,151	2	277,228	2
Transport and communication	1,311,306	10	1,393,929	11
Manufacturing	332,344	3	231,717	2
Construction	830,550	6	877,309	7
Net loan portfolio balance	**13,200,807**	**100**	**12,530,649**	**100**

34.1.9 Ownership risk concentrations

Ownership risk concentrations within the customer loan portfolio are as follows:

All amounts are expressed in K'000

Consolidated As at 31 December	2019	%	2018	%
Corporate / Commercial	7,703,341	58	7,206,355	58
Government	2,510,817	19	2,661,688	21
Retail	2,986,649	23	2,662,606	21
Net loan portfolio balance	**13,200,807**	**100**	**12,530,649**	**100**

35. Liquidity risk

Liquidity risk is the risk of being unable to meet financial obligations as they fall due. The Board, through the Asset and Liability Committee, sets liquidity policy to ensure that the Group has sufficient funds available to meet all its known and potential obligations.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of banking activities. An unmatched position potentially enhances profitability, but can also increase the risk of losses.

Short-term mismatch of asset and liability maturity at 31 December 2019

The maturity profile of material Assets and Liabilities as at 31 December 2019 is shown in the following schedule. The mismatching of maturity of assets and liabilities indicates an apparent negative net "current" asset position. However, as stated in the preceding paragraph, mismatched positions are established and managed to achieve profit opportunities that arise from them, particularly in a normal yield curve environment. Accordingly, this mismatched maturity position is considered manageable by the Group, and does not impair the ability of the Group to meet its financial obligations as they fall due. The Directors are also of the view that the Group is able to meet its financial obligations as they fall due for the following additional reasons:

- The Bank and the Group complies with the Cash Reserve Requirement ("CRR") set by the regulatory authorities of the jurisdictions that the Bank operates in. The CRR specifies that a bank must hold an amount equal to a percentage of its total customer deposits in the form of cash in an account maintained by the respective Central Bank. The Bank and Group complies with this daily requirement on an ongoing basis.

35. Liquidity risk (continued)

Maturity of assets and liabilities

All amounts are expressed in K'000

Consolidated As at 31 December 2019	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Assets						
Cash and balances with Central Bank	3,171,384	-	-	-	411,781	3,583,165
Treasury and Central Bank bills	380,142	688,229	1,429,812	14,760	-	2,512,943
Amounts due from other banks	745,062	229,336	48,071	-	-	1,022,469
Loans, advances and other receivables from customers	1,648,820	1,057,253	3,022,749	5,510,377	5,077,068	16,316,267
Other financial assets	2,163,885	95,236	663,474	1,160,027	772,329	4,854,951
Total assets	**8,109,293**	**2,070,054**	**5,164,106**	**6,685,164**	**6,261,178**	**28,289,795**
Liabilities						
Amounts due to other banks	-	81,468	2,463	-	-	83,931
Customer Deposits	14,019,851	1,109,765	1,794,963	719,301	1,912,151	19,556,031
Other liabilities	1,761,480	2,750	5,048	472	105,141	1,874,891
Other provisions	258,809	159	35	188	4,153	263,344
Total liabilities	16,040,140	1,194,142	1,802,509	719,961	2,021,445	21,778,197
Net liquidity gap	**(7,930,847)**	**875,912**	**3,361,597**	**5,965,203**	**4,239,733**	**6,511,598**

As at 31 December 2018	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Total
Total assets	8,381,534	1,336,540	5,201,238	6,137,115	6,076,958	27,133,385
Total liabilities	15,069,532	1,013,223	2,073,361	274,900	1,969,331	20,400,347
Net liquidity gap	(6,687,998)	323,317	3,127,877	5,862,215	4,107,627	6,733,038

36. Operational risk

Operational risk is the potential exposure to unexpected financial or non-financial losses arising from the way in which the Group conducts its business. Examples of operational risks include employee errors, systems failures, fire, floods, or similar losses to physical assets, fraud, or criminal activity. Operational risk is managed through formal policies, documented procedures, business practices and compliance monitoring.

An operational risk management function is responsible for the maintenance of these policies, procedures practices and monitoring the organization's compliance with them. The Operational Risk Committee coordinates the management process across the organization.

An independent internal audit function also conducts regular reviews to monitor compliance with approved BPNG standards and examines the general standard of control.

The Operational Risk Committee and the internal audit function mandatorily report to the Board Risk and Compliance Committee.

37. Foreign exchange risk

Foreign exchange risk is the risk to earnings caused by a change in foreign exchange rates on open currency positions. The objective of foreign exchange risk management within the Group is to minimise the impact on earnings of any such movement.

The Group accepts foreign currency denominated transactions and therefore has exposure to movements in foreign currency. The Group has a policy to offset these transactions to minimise daily exposure. As foreign exchange contracts generally consist of offsetting commitments, they involve only limited foreign exchange risk to the Group and material loss is not envisaged.

Currency concentration of assets, liabilities, and off-balance sheet items

All amounts are expressed in K'000

Consolidated As at 31 December 2019	**PGK**	**FJD**	**SBD**	**USD**	**Other**	**Total**
Assets						
Cash and balances with Central Bank	2,211,457	478,799	439,403	6,488	447,018	**3,583,165**
Treasury and Central Bank bills	2,252,907	15,702	157,886	-	33,002	**2,459,497**
Amounts due from other banks	146,354	110,404	8,788	234,437	522,486	**1,022,469**
Loans, advances and other receivables from customers	7,740,010	3,161,274	526,566	499,203	1,273,754	**13,200,807**
Other financial assets	1,578,722	507,057	258	-	35,034	**2,121,071**
Other assets	1,277,703	667,813	60,500	352	133,741	**2,140,109**
Total assets	**15,207,153**	**4,941,049**	**1,193,401**	**740,480**	**2,445,035**	**24,527,118**
Liabilities						
Amounts due to other banks	(22,119)	(59,412)	(2,400)	-	-	**(83,931)**
Customer Deposits	(12,739,985)	(3,180,962)	(907,317)	(538,226)	(1,972,566)	**(19,339,056)**
Other liabilities	(564,135)	(1,183,690)	(37,080)	(117,512)	(84,681)	**(1,987,098)**
Total liabilities	**(13,326,239)**	**(4,424,064)**	**(946,797)**	**(655,738)**	**(2,057,247)**	**(21,410,085)**
Net on-balance sheet position	**1,880,914**	**516,985**	**246,604**	**84,742**	**387,788**	**3,117,033**
Off-balance sheet net notional position	**798**	**-**	**-**	**(139,868)**	**140,009**	**939**
Credit commitments	**1,873,731**	**512,960**	**60,433**	**-**	**118,418**	**2,565,542**
31 December 2018						
Total Assets	14,553,848	4,576,805	1,213,537	614,523	2,122,510	23,081,223
Total Liabilities	(12,839,667)	(4,043,203)	(940,514)	(534,160)	(1,851,544)	(20,209,088)
Net on-balance sheet position	**1,714,181**	**533,602**	**273,023**	**80,363**	**270,966**	**2,872,135**
Off-balance sheet net notional position	**(3,263)**	**-**	**-**	**(171,679)**	**174,006**	**(936)**
Credit commitments	**1,274,345**	**522,309**	**76,059**	**-**	**176,890**	**2,049,603**

37. Foreign exchange risk (continued)

All amounts are expressed in K'000

The following table presents sensitivities of profit or loss and equity to possible changes in exchange rates applied at the end of the reporting period, relative to the functional currency of the respective Group entities, with all other variables held constant:

	At 31 December 2019		At 31 December 2018	
	Impact on profit or loss	Impact on equity	Impact on profit or loss	Impact on equity
USD strengthening by 1% (2018 – 1%)	356	356	613	613
USD dollar weakening by 1% (2018 – 1%)	(349)	(349)	(601)	(601)
AUD strengthening by 1% (2018 – 1%)	(36)	(36)	(37)	(37)
AUD dollar weakening by 1% (2018 – 1%)	35	35	36	36

38. Interest rate risk

Interest rate risk in the balance sheet arises from the potential for a change in interest rate to have an adverse effect on the revenue earnings in the current reporting period and future years. As interest rates and yield curves change over time the Group may be exposed to a loss in earnings due to the effects of interest rates on the structure of the balance sheet. Sensitivity to interest rates arises from mismatches in the re-pricing dates, cash flows and other characteristics of the assets and their corresponding liability funding. These mismatches are actively managed as part of the overall interest rate risk management process governed by the Assets and Liabilities Committee (ALCO), which meets regularly to review the effects of fluctuations in the prevailing levels of market interest rates on the financial position and cash flows of the Group. The objective of interest rate risk control is to minimise these fluctuations in value and net interest income over time, providing secure and stable sustainable net interest earnings in the long term. The table below illustrates the interest sensitivity of assets and liabilities at the balance date.

Given the profile of assets and liabilities as at 31 December 2019 and prevailing rates of interest, a 1% increase in markets rates will result in a K45 million increase in net interest income, whilst a 1% decrease in rates will result in a K52.2 million decrease in net interest income.

Interest sensitivity of assets, liabilities and off balance sheet items – re-pricing analysis

All amounts are expressed in K'000

Consolidated As at 31 December 2019	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing
Assets						
Cash and Central Bank assets	-	-	-	-	-	1,816,564
Treasury and Central Bank bills	347,001	705,379	1,401,412	5,081	624	-
Amounts due from other banks	867,654	46,543	6,016	-	-	102,256
Statutory deposits - Central Bank	-	-	-	-	-	1,766,601
Loans, advances and other receivables from customers	11,355,031	211,132	813,765	656,055	164,824	-
Other Financial Assets	437,339	151,520	559,890	800,520	211,415	162,427
Other assets	-	-	-	-	-	1,938,069
Total assets	**13,007,025**	**1,114,574**	**2,781,083**	**1,461,656**	**376,863**	**5,785,917**
Liabilities						
Amounts due to other banks	16,678	7,612	-	-	-	59,641
Customer deposits	8,678,235	1,071,740	1,628,037	299,468	10	7,661,566
Other liabilities	8,248	2,720	-	-	73,009	1,699,459
Other provisions	6,193	-	-	-	-	197,469
Total liabilities	**8,709,354**	**1,082,072**	**1,628,037**	**299,468**	**73,019**	**9,618,135**
Interest sensitivity gap	**4,297,671**	**32,502**	**1,153,046**	**1,162,188**	**303,844**	**(3,832,218)**

38. Interest rate risk (continued)

Interest sensitivity of assets, liabilities and off balance sheet items – re-pricing analysis

As at 31 December 2018	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	Non-interest bearing
Assets						
Cash and Central Bank assets	-	-	-	-	-	1,253,449
Treasury and Central Bank bills	501,889	617,953	1,344,620	30,238	-	-
Amounts due from other banks	451,160	-	8,435	1,560	-	392,864
Statutory deposits - Central Bank	-	-	-	-	-	1,685,544
Loans, advances and other receivables from customers	10,754,609	192,658	806,643	557,100	219,639	-
Other Financial Assets	435,077	51,591	536,149	1,265,005	267,621	175,579
Other assets	-	-	-	-	-	1,531,840
Total assets	**12,142,735**	**862,202**	**2,695,847**	**1,853,903**	**487,260**	**5,039,276**
Liabilities						
Amounts due to other banks	17,338	16,885	-	-	-	17,316
Customer deposits	8,058,906	925,624	1,761,696	156,585	4	7,329,951
Other liabilities	-	-	-	-	105,525	1,625,155
Other provisions	5,637	-	-	-	-	188,466
Total liabilities	**8,081,881**	**942,509**	**1,761,696**	**156,585**	**105,529**	**9,160,888**
Interest sensitivity gap	**4,060,854**	**(80,307)**	**934,151**	**1,697,318**	**381,731**	**(4,121,612)**

39. Fair values of financial assets and liabilities

There is no material difference between the fair values and carrying values of the financial assets and liabilities of the Group.

The table below analyses the Group's financial instruments carried at fair value, by levels in the fair value hierarchy.

The different levels have been defined as follows:

- Level 1 - quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 - inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 - inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Consolidated

All amounts are expressed in K'000

As at 31 December 2019	Level 1	Level 2	Level 3	Total
a) Financial assets				
Equity security	-	177,313	3,095	180,408
Non-financial assets				
Land & buildings	-	708,284	-	708,284
Assets subject to operating lease	-	-	48,133	48,133
Total assets	-	**885,597**	**51,228**	**936,825**
b) Financial liabilities				
Policy liability	-	-	890,147	890,147
Total liabilities	-	-	**890,147**	**890,147**

39. Fair values of financial assets and liabilities (continued)

As at 31 December 2018	Level 1	Level 2	Level 3	Total
a) Financial assets				
Equity security	-	118,831	2,696	121,527
Non-financial assets				
Land & buildings	-	537,669	-	537,669
Assets subject to operating lease	-	-	52,433	52,433
Total assets	-	**656,500**	**55,129**	**711,629**
b) Financial liabilities				
Policy liability	-	-	818,198	818,198
Total liabilities	-	-	**818,198**	**818,198**

	Consolidated	
Financial asset at fair value through profit & loss	**2019**	**2018**
Opening balance	54,570	72,825
Total gains and losses recognized in:		
- Profit & loss	(3,342)	(18,255)
- Other comprehensive income	-	-
Closing balance	**51,228**	**54,570**

There were no changes in valuation technique for Level 3 recurring fair value measurements during the year ended 31 December 2019. Property, plant and equipment represents commercial land and buildings owned by the Group based on valuations provided by independent valuers. The valuation is based on the capitalisation method with an assessment of the property based on its potential earning capacity. Disposal cost for properties classified as held for sale is not expected to be material.

In the normal course of trading, the Group enters into forward exchange contracts. The Group does 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.

39. Fair values of financial assets and liabilities (continued)

Forward exchange contracts outstanding at 31 December 2019 stated at the face value of the respective contracts are:

All amounts are expressed in respective FCY'000 and K'000

As at 31 December 2019		USD	AUD	EURO	GBP	JPY	Other	Total
Selling	FCY	(49,183)	(2,529)	(900)	(21)	(181,179)	(2,110)	-
	Kina	(15,371)	-	-	-	-	-	(15,371)
Buying	FCY	8,132	14,800	20	1,200	137,500	34,444	-
	Kina	16,169	-	-	-	-	-	16,169

As at 31 December 2018		USD	AUD	EURO	GBP	JPY	Other	Total
Selling	FCY	(55,913)	(958)	-	-	(149,380)	(1,000)	-
	Kina	(8,793)	-	-	-	-	-	(8,793)
Buying	FCY	4,924	55,700	-	-	5,000	15,353	-
	Kina	5,530	-	-	-	-	-	5,530

40. Insurance

(a) Net insurance operating income

	Consolidation		Bank	
All amounts are expressed in K'000	2019	2018	2019	2018
Net insurance income	**30,675**	**38,913**	-	-

(b) Policy liabilities

Key assumptions used in determining this liability are as follows:

Discount rates

For contracts in Statutory Fund 1 which have a Discretionary Patricipating Feature (DPF), the discount rate used is linked to the assets which back those contracts. For 31st December 2019 this was 6.097% per annum (31st December 2018: 6.005% per annum), based on current 10 year government bond yields and expected earnings from the investment portfolio. For contracts without DPF and Accident Business, a rate of 4.80% per annum was used at 31st December 2019 (31st December 2018: 4.80% per annum). These rates were based on the 10 year government bond rate as published by the Reserve Bank of Fiji.

40. Insurance (continued)

Investment and maintenance expenses

Future maintenance and investment expenses are based on the budgeted expenses. Future inflation has been assumed to be 3.5% per annum (31st December 2018: 3.5% per annum) for determining future expenses.

Taxation

The rates of taxation enacted or substantially enacted at the date of the valuation (20%) are assumed to continue into the future.

Mortality and morbidity

Projected future rates of mortality for insured lives are based on the Fiji Mortality Statistics table FJ90-94 Male. These are then adjusted for the Group's own experience. The mortality rates used was 65% (31st December 2018: 65%) of the FJ90-94 Male table for participating business in Statutory Fund 1.

Rates of discontinuance

Best estimate assumptions for the incidence of withdrawal and discontinuance vary by product and duration and are based on the Group's experience which is reviewed regularly. Rates used were the same as last year.

	2019	2018
Whole of Life and Endowment Insurance	14%	14%
Term Insurance	16%	16%
Accident Insurance	17%	17%

Basis of calculation of surrender values

Surrender values are based on the provisions specified in the policy contracts. There have been no changes to surrender bases during the period (or the prior periods) which have materially affected the valuation result.

Discretionary Participating Business

For most participating business, bonus rates are set such that, over long periods, the returns to contract holders are commensurate with the investment returns achieved on the pool of assets which provide security for the contract, together with other sources of profit arising from this business. Profits from these policies are split between contract holders and shareholders in accordance with the policy conditions which allow for shareholders to share in allocations at a maximum rate of 20%. For business written between 1995 and 1998 the shareholder receives 11% of profits.

In applying the contract holders' share of profits to provide bonuses, consideration is given to equity between generations of policyholders and equity between the various classes and sizes of contracts in force. Assumed future bonus rates included in the liability for the long term insurance contracts were set such that the present value of the liabilities equates to the present value of assets supporting the business together with assumed future investment returns, allowing for the shareholder's right to participate in distributions.

Reinsurance

Contracts entered into by the Group with Reinsurers under which the Group is compensated for losses on one or more contracts issued by the Group, are classified as reinsurance contracts.

As the reinsurance agreements provide for indemnification by the Reinsurers against loss or liability, reinsurance income and expenses are recognised separately in profit or loss when they become due and payable in accordance with the reinsurance agreements.

Reinsurance recoveries are recognised as claim recoveries under profit or loss. This is netted off against the claim expenses. Reinsurance premiums are recognised as Reinsurance Expenses.

40. Insurance (continued)

All amounts are expressed in K'000	2019	2018
Policy Liabilities		
Opening balance	818,198	749,876
Translation movement	11,221	(3,227)
Increase in policy liabilities	59,746	71,616
Increase in policy liabilities on revaluation of land	982	(67)
Total policy liabilities	**890,147**	**818,198**

41. Events occurring after balance sheet date

On February 7, 2020, the Bank acquired 50% shares in Devco Lao Leasing Company Limited for a consideration of USD2 million. The acquired entity will be renamed BSP Lao Leasing Company, an asset finance business which will be treated as a joint venture in the Group accounts.

42. Remuneration of auditor

	Consolidated		**Bank**	
All amounts are expressed in K'000	**2019**	**2018**	**2019**	**2018**
Financial statement audits	4,347	3,326	3,126	2,363
Other services	514	1,031	463	818
	4,861	**4,357**	**3,589**	**3,181**

The external auditor PricewaterhouseCoopers is also engaged in providing other services to the Bank and Group as required and as permitted by prudential standards. The provision of other services included taxation and general training.

Independent auditor's report

To the shareholders of Bank of South Pacific Limited

Report on the audit of the financial statements of the Bank and the Group

Our opinion

We have audited the financial statements of Bank of South Pacific Limited (the Bank), which comprise the statements of financial position as at 31 December 2019, and the statements of comprehensive income, statements of changes in shareholders' equity and statements of cash flows for the year then ended, and the notes to the financial statements which include a summary of significant accounting policies and other explanatory information for both the Bank and the Group. The Group comprises the Bank and the entities it controlled at 31 December 2019 or from time to time during the financial year.

In our opinion the accompanying financial statements:

- comply with International Financial Reporting Standards and other generally accepted accounting practice in Papua New Guinea; and
- give a true and fair view of the financial position of the Bank and the Group as at 31 December 2019, and their financial performance and cash flows for the year then ended.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our opinion.

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

Independence

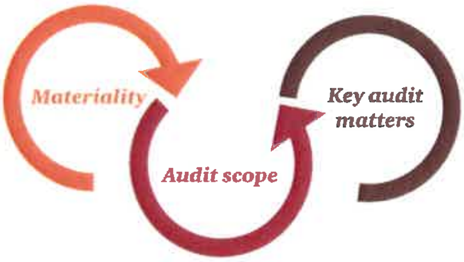
We are independent of the Bank and Group in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants (IESBA Code)*, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

Our firm carries out other services for the Group in the areas of audit-related and tax advice services. The provision of these other services has not impaired our independence as auditor of the Bank and the Group.

Our audit approach

An audit is designed to provide reasonable assurance about whether the financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the management structure of the Bank and the Group, their accounting processes and controls and the industries in which they operate.



Materiality

- For the purpose of our audit of the Group we used overall group materiality of K60.8 million which represents approximately 5% of the Group's profit before taxes.
- We applied this threshold, together with qualitative considerations, to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements on the financial statements as a whole.
- We chose Group profit before taxes as, in our view, it is the metric against which the performance of the Group is most commonly measured and is a generally accepted benchmark.
- We selected 5% based on our professional judgement noting that it is also within the range of commonly acceptable related thresholds.

Audit scope

- We (PwC Papua New Guinea) conducted the audit over all of the Group's operations in Papua New Guinea (PNG) and Solomon Islands, which are the most significant to the Group, and directed the scope of the audit of other subsidiaries included in the Group financial statements sufficient to express an opinion on the financial statements as a whole.
- For the Group's activities in Fiji, Samoa, Tonga, Cambodia, Cook Islands, and Vanuatu the audit work was performed by other PwC network firms or other firms operating under our instructions. In addition we visit significant overseas operations and this year we met with management in the Solomon Islands.
- Our audit focused on where the directors made subjective judgements; for example, significant accounting estimates involving assumptions and inherently uncertain future events.

Key audit matters

- Amongst other relevant topics, we communicated the following key audit matters to the Board Audit Committee:
  - Loan loss provisioning
  - IT systems and controls
- These matters are further described in the Key audit matters section of our report.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the financial statements for the current period. The key audit matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. We have determined the matters described below to be key matters to be communicated in our report. Further, commentary on the outcomes of the particular audit procedures is made in that context.

<table>
<tr><th>Key audit matter</th><th>How our audit addressed the key matter</th></tr>
<tr><td>
Loan loss provisioning - Refer to Note 1G & M of the financial statements for a description of the accounting policies and to Note 34 for an analysis of credit risk
Due to the magnitude of the loans and advances balances and the extent of management judgement inherent in the impairment calculations, impairment of loans and advances is an area of significance in the current year audit of the Bank and its subsidiaries.
IFRS 9 Financial Instruments (IFRS 9) is a complex accounting standard which has required considerable judgement and interpretation in its application.
The key areas of judgement included:

The determination of the impairment in applying IFRS 9, which is reflected in the allowance for losses on loans, advances and other receivables (refer to Note 13 and Note 34)
The identification of exposure for which there has been a significant increase in credit risk
Assumptions used in the expected credit loss model such as valuation of collateral and assumptions made on future values, financial condition of counterparties, expected future cash flows and forward looking macroeconomic factors
The need to apply additional model adjustments to reflect current or future external factors that are not appropriately captured by the expected credit loss model

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The procedures we performed to support our audit conclusions, included:

Consideration of the appropriateness of accounting policies and assessment of the loan impairment methodology applied, compared to the requirements of IFRS 9. This included obtaining an understanding and assessment of the reasonableness of the key outputs of the model, as well as key judgements and assumptions used by management in implementation of the model.
Reviewing the design and operating effectiveness of key controls around the credit origination processes, the credit monitoring processes and the credit inspection unit's customer loan file reviews.
Review of the impairment methodology to establish the critical fields used in the computation of Stage 1 and Stage 2 provisions. On a sample basis tested the critical fields identified to have an impact on the expected credit loss provision by agreeing this back to source documentation.
For loans and advances in Stage 1 and Stage 2, critically examining the model methodology for consistency and appropriateness. This included evaluation of the appropriateness of the estimates made on the Probability of Default, Loss Given Default and Exposure at Default. This also included assessing the appropriateness of probability-weighted and staging criteria.
For Stage 3 loans and advances, audit procedures were carried out over the completeness of the credit watch list and delinquencies, assumptions made in the valuation of collateral and recovery cash flows and mathematical accuracy of the IFRS 9 provisioning model.
For model adjustments, we considered the basis for and data used to determine the adjustments. This included making an independent assessment of both the credit environment and the macro-environment in which the Group operates.
For IFRS 9 related disclosures in the financial statements, we reviewed the accuracy and completeness in line with BSP accounting policies and IFRS 9 requirements.

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Key audit matter	How our audit addressed the key matter
IT systems and controls We focused on this area because the Group is heavily dependent on complex IT systems for the capture, processing, storage and extraction of significant volumes of transactions. There are some areas of the audit where we seek to place reliance on system functionality including certain automated controls, system calculations and reports. Our reliance on these is dependent on the Group's IT General Control (ITGC) environment, in particular, user access maintenance and changes to IT systems being authorised and made in an appropriate manner.	For significant financial statement line items, we gained an understanding of the business processes, key controls and IT systems used to generate and support those line items. Where relevant to our planned audit approach, we assessed the design and tested the operating effectiveness of the key ITGCs which support the continued integrity of the in-scope IT systems. Our procedures over ITGCs focused on user access and change management and we also carried out tests, on a sample basis, of system functionality that was key to our audit approach. Where we identified design or operating effectiveness matters relating to ITGCs and system functionality relevant to our audit, we performed alternative or additional audit procedures.

Information other than the financial statements and auditor's report

The directors are responsible for the other information. The other information comprises the Directors' Report (but does not include the financial statements and the auditors' report thereon), which we obtained prior to the date of this auditor's report, and the annual report, which is expected to be made available after that date. Our opinion on the financial statements does not cover the other information and we do not, and will not, express any form of assurance conclusion thereon.

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

When we read the annual report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

Responsibilities of the directors for the financial statements

The directors are responsible, on behalf of the Bank for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards and other generally accepted accounting practice in Papua New Guinea and the Companies Act 1997 and for such internal control as the directors determine is necessary to enable the preparation of the financial statements that give a true and fair view and are free from material misstatement, whether due to fraud or error.

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

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements, as a whole, are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

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

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

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

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

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

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

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the financial statements for the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulations preclude public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

The Companies Act 1997 requires that in carrying out our audit we consider and report on the following matters. We confirm in relation to our audit of the financial statements for the year ended 31 December 2019:

- We have obtained all the information and explanations that we have required;

- In our opinion, proper accounting records have been kept by the Bank as far as appears from an examination of those records.

Who we report to

This report is made solely to the Bank's shareholders, as a body, in accordance with the Companies Act 1997. Our audit work has been undertaken so that we might state to the Bank's shareholders those matters which we are required to state to them in an auditor's report and for no other purpose. We do not accept or assume responsibility to anyone other than the Bank and the Bank's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

PricewaterhouseCoopers

Peter Buchholz
Engagement Leader

Christopher Hansor
Partner
Registered under the Accountants Act 1996

Port Moresby
26 February 2020