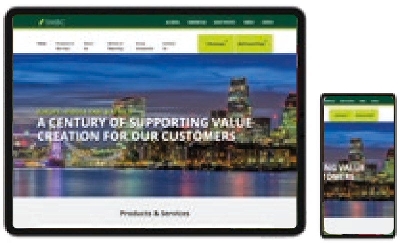
SMBC Group

SMBC Bank International plc

A trusted partner for the long term

Annual report and financial statements
Year ended 31 March 2023

Contents



Find out more online

smbcgroup.com/emea

Company registration

Registered as a public limited company in England and Wales under company number 04684034

Regulatory registration

Authorised by the Prudential Regulation Authority and regulated by the Prudential Regulation Authority and the Financial Conduct Authority
Financial Services Register number: 223304

Registered office

100 Liverpool Street, London, EC2M 2AT, United Kingdom

Pillar 3 document

www.smbcgroup.com/emea/pillar3

Auditor

KPMG LLP
15 Canada Square
London
E14 5GL

Presentation of information

In this document the terms 'SMBC BI', 'Bank', 'we', 'us' or 'our' refer to SMBC Bank International plc. The Bank's parent company is Sumitomo Mitsui Banking Corporation, which is shown as 'SMBC'. 'SMBC Group' refers to the corporate group of companies of Sumitomo Mitsui Financial Group, shown as 'SMFG', and of which the Bank is a part. The term 'EMEA' refers to Europe, Middle East and Africa. The Bank's affiliate company SMBC Nikko Capital Markets Limited is shown as 'SMBC Nikko CM'.

This Annual Report contains forward-looking statements that involve inherent risks and uncertainties. Please see Forward-looking statements on **page 153.**

Chair's Statement

> I would like to thank colleagues across the business whose commitment and professionalism was integral to the Bank's strong performance during the year, despite the ongoing disruption caused by the pandemic.
>
> **Alan Keir**
> Chair

17%
Increase in operating income

USD 340.3m
Profit before tax

Although 2022 witnessed a gradual emergence from the COVID-19 pandemic, it was still a year of disruption and volatility, given the conflict in Ukraine, rising interest rates and inflationary pressures across the globe. Despite these factors, the Bank had a strong year in terms of financial performance, and we remain cautiously optimistic regarding the opportunities in front of us.

Of note, operating income increased 17%, helped by the rising interest rate environment, combined with a 50% reduction in impairment charges, to deliver profit before tax of circa USD 340m. Performance was robust across the majority of the Bank's business lines and we benefitted from increased transaction volumes in support of evolving customer requirements. Expenses registered an increase, primarily from investment in business growth. The Bank remained well capitalised with a CET1 ratio of 17.8%.

On behalf of my fellow Directors, I would like to thank colleagues across the business whose commitment and professionalism was integral to the Bank's strong performance during the year, despite the ongoing disruption caused by the pandemic. I would also like to acknowledge the contribution of our outgoing CEO, Kei Nakamura, who has returned to Tokyo as Co-Head of SMBC Group's Global Business Unit, where he will retain responsibility for the EMEA Division. Kei's contribution to the Bank's success is highly valued, and he has helped us navigate unprecedented times during his tenure. He is succeeded by Hideo Kawafune, who has previously served as Deputy CEO and as Deputy Head of the EMEA Division for SMBC Group. Hideo's appointment will ensure a smooth transition and a high degree of continuity in our strategy and focus. We also welcomed Keith Macdonald to the Board as a non-executive Director. Keith brings considerable technology and operations expertise, and his appointment will help us further evolve the Bank's technology governance and operational resilience. I am pleased to say that after the year-end, Sophie O'Connor joined the Board as a non-executive Director. Sophie further strengthens the Board's expertise in risk management and finance, having significant experience in these areas as both an executive and non-executive. I believe that Keith's and Sophie's appointments leave the Board well-positioned for the future.

The Bank continues to make good progress towards the implementation of a universal banking model through the integration into the Bank of the securities business of SMBC Nikko CM Limited. Combining our banking and securities businesses will allow us to improve the customer experience, strengthen our risk and control frameworks, and generate operational efficiencies. Integration remains subject to regulatory approval, but comprehensive business plans have been submitted and preparedness continues in earnest, with integration currently targeted for financial year 2024. Evolving our risk management framework will be key to the successful transfer of the securities business into the Bank, to ensure the combined enterprise can be appropriately managed. Key components of the framework are already embedded in our activities and are subject to robust scrutiny and governance at both functional and Board Risk Committees.

I am pleased to see the further progress we have made with our Environmental, Social and Governance (ESG) credentials, in line with our net zero commitments. Sustainability risk, including climate change, is increasingly embedded in all aspects of the Bank's business and strategy, and we continue to develop appropriate products and advisory services to support the Bank's clients with their transition strategies. The Bank also continues to invest in its procedures, training and governance processes, with many employees actively participating in key industry forums to support the development of market standards and best practice.

The Bank recognises the increasing attention being paid to diversity and inclusion by our stakeholders and I am pleased that we continue to make progress. Driving gender equality remains a critical activity for the Bank and while our gender pay gap has improved, it still highlights a need to do more. While we anticipate meeting our Women in Finance Charter targets in the forthcoming year, further positive action is needed to realise our longer-term aspirations for balance in our business. Beyond gender, the Bank's work to evolve cultural diversity, race, ethnicity, sexual orientation and disability is driving our aspiration to create a truly inclusive culture. As ever, I am grateful for the support we receive from our employee networks, who generously contribute their time and perspectives to advise and inform the Bank's strategies and the evolution of equitable policies.

> **Combining our banking and securities businesses will allow us to improve the customer experience, strengthen our risk and control frameworks, and generate operational efficiencies.**

The Bank also recognises its role in contributing to positive social change and, this year, we have introduced new early careers strategies for talent from all socio-economic backgrounds. We continue to introduce new ways for our talent to volunteer in support of charitable and community organisations. and together we have donated funds to a number of charities, including those supporting the humanitarian relief efforts in both Ukraine and Turkey-Syria.

All of this work aligns to the Bank's corporate values and long-term ESG commitments, and we remain committed to the effort and investment needed to deliver lasting and positive change.

Alan Keir
Chair
7 July 2023

Business overview

The Directors present the Strategic Report of SMBC Bank International plc for the year ended 31 March 2023.

The Bank is a wholly owned subsidiary of SMBC, which is one of the world's largest banks by total assets, providing an extensive range of corporate and consumer banking services in Japan and globally.

SMBC is a core member of SMFG, a Tokyo-based holding company which is one of Japan's largest financial institutions. Through its subsidiaries and affiliates, SMFG offers a diverse range of financial services, including commercial banking, leasing, securities, credit card, consumer finance and other services.

There are four main aspects to the Bank's business:

1 Relationships

The Bank's business is with selected corporate and sovereign institutional customers where it provides a range of corporate banking services, supported by the wider SMBC Group. The Bank works in EMEA with Japanese and Asian corporates and non-Japanese investment and sub-investment corporates, including financial institutions, and selected top-tier corporates and sovereigns in the emerging markets and other areas of EMEA.

2 Products and services

The Bank provides a wide range of products and services, including syndicated and bilateral loans and specialist financial advisory services, as well as deposits and foreign exchange. The Bank particularly seeks to leverage its presence and expertise in project finance in the energy and infrastructure sectors; trade finance including supply chain finance; aircraft and maritime finance; LBO finance; and ECA, advisory and other structured credit.

3 New business development

The primary approach to developing new business opportunities is to seek organic growth, leveraging the Bank's expertise and diversification of the credit portfolio. The expansion into new business areas is considered in conjunction with risk appetite.

4 Organisational growth

The development of the organisation, including strengthening governance and risk control, is recognised as the foundation for sustainable growth. The Bank provides management, marketing and operational services to other SMBC Group companies under Service Level Agreements, receiving fees as income for those services.

The Bank works closely with other SMBC Group companies to provide a full range of financial services solutions. Many of the Bank's transactions are undertaken in cooperation with SMBC Nikko Capital Markets Limited (SMBC Nikko CM), through which it provides customers with debt and equity capital markets and derivative products under integrated bank-securities operations, and SMBC Bank EU AG, which is a credit institution established in Germany that provides business and financial services in the European Economic Area.

Key client sectors

- Automotive and manufacturing
- Aircraft and aviation
- Chemicals and petrochemicals
- Commodities
- Financial institutions
- Infrastructure
- Maritime and shipping
- Metals and mining
- Energy and utilities
- Sovereign institutions

Services

- Corporate lending
- Sustainable finance
- Syndicated and bilateral loans
- Diversified payment rights
- Deposits
- Merger and acquisition (M&A) financing
- Foreign exchange
- Corporate and M&A advisory ●
- Cross-border M&As ●
- Debt and equity capital markets ●
- Derivatives ●

● Offered by SMBC Nikko CM

Customer-facing departments

This overview of the Bank's customer-facing businesses reflects the comprehensive nature of the Bank's business offering.

Corporate Banking Department 1
Japanese and Asian corporates in EMEA

Corporate Banking Department 2
Non-Japanese corporates in Western Europe

Global Trade Finance Department
Trade finance products and services

Transportation Department
Aviation and maritime

Global FIG Department
Financial institutions

Loan Capital Markets Department
Syndication and asset distribution

Global Transaction Banking Department
Electronic and transaction banking services

Financial Markets Department
Treasury and foreign exchange

International & Structured Finance Department
Structured finance, advisory, ECA, project finance, Central and Eastern Europe and emerging markets

Specialised Products Department
Leveraged buy out, securitised products, real estate and fund finance

Strategy and objectives

"To be a trusted partner for the long term"

The Bank's purpose

This is underpinned by the business model, which is to provide corporate finance in a way that supports the Bank's aspiration for long-term sustainable growth, ensuring that it is well funded, well controlled and that there is a sensible balance between risk and reward.

Strategy and objectives

The Bank has four corporate objectives:

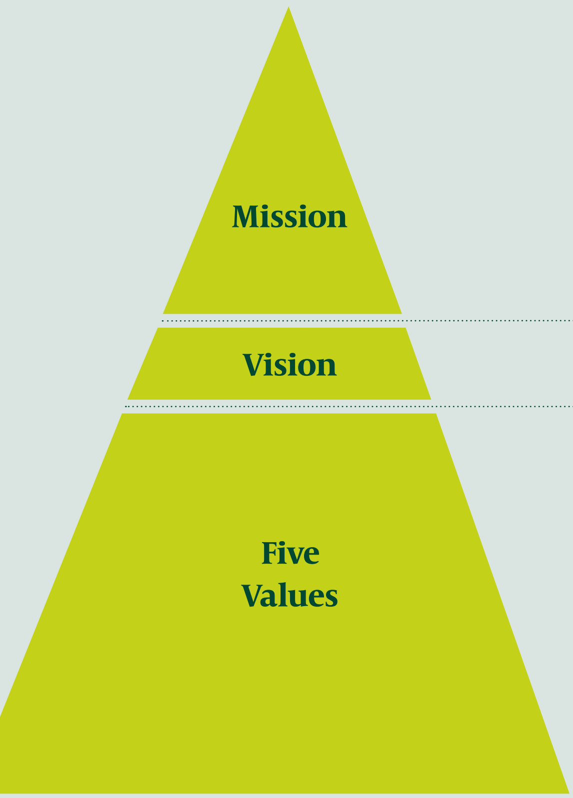
Serving customers
To be the bank of choice for its EMEA customers through the provision of high quality value-added services in cooperation with SMBC Group companies.

Sustainable growth
To run the business in a way that is appropriately balanced and sustainable; to develop an efficient and effective infrastructure to support sound business growth; and to provide services to relevant SMBC Group entities through Service Level Agreements.

Competitive edges
To establish and develop those areas where the Bank feels it has a particularly strong position in customer relationships, product capabilities and global reach.

Team SMBC Group
To share and help realise SMBC Group's Mission, Vision and social value creation. The Bank also shares the Group's Five Values, which are an integral part of the Bank's culture.

SMBC Group's Mission, Vision and Five Values



Mission

We grow and prosper together with our customers, by providing services of greater value to them.

We aim to maximise our shareholders' value through the continuous growth of our business.

We create a work environment that encourages and rewards diligent and highly-motivated employees.

We contribute to a sustainable society by addressing environmental and social issues.

Vision

A trusted global solution provider committed to the growth of our customers and advancement of society.

Five Values

Integrity As a professional, always act with sincerity and a high ethical standard.

Customer First Always look at it from the customer's point of view, and provide value based on their individual needs.

Proactive & Innovative Embrace new ideas and perspectives, don't be deterred by failure.

Speed & Quality Differentiate ourselves through the speed and quality of our decision-making and service delivery.

Team 'SMBC Group' Respect and leverage the knowledge and diverse talent of our global organisation as a team.

The Bank's purpose and strategy is consistent with and supports the wider SMBC Group's Mission, Vision and Five Values.

To inform our behaviours and to deliver the best outcomes for our stakeholders

Review of the year

Business environment

Over the year, central banks have sought to control inflation, with the US Federal Reserve, European Central Bank and Bank of England seeking to prioritise this over economic growth. The current rate of fiscal and monetary tightening is raising concern with policymakers that inflation is more entrenched than expected, requiring higher interest rates for longer. The ongoing conflict in Ukraine has the potential to prolong food and energy inflation pressures, in tandem with creating further bottlenecks to supply chains.

Europe has demonstrated its resilience, which reflects several factors including efforts by governments to diversify energy supplies, while shielding vulnerable corporates and households from rising prices. Labour markets have also remained resilient. Oil and gas producers in the Middle East continued to benefit in the year from high energy prices and increasing demand for their exports from Western buyers seeking alternatives to sanctioned Russian energy. Africa also benefitted from the surge in commodity prices in the year, but at the year-end, this has begun to taper off and most economies appear to be poised for a pronounced slowdown.

Strategy development

Against the uncertain economic backdrop, the Bank's focus has remained on lending to top-tier borrowers but it has also expanded its risk appetite to allow for the development of high margin transactions and products on a selective basis while maintaining a well-diversified credit portfolio. The Bank believes this strategy has served it well in the year and will prudently continue this approach into the following year and beyond.

During the year, the Bank set out its intention to start operations as a universal bank. The first step in this process will be the transfer of the securities business from SMBC Nikko CM to the Bank. This transfer remains subject to the completion of legal and regulatory processes and is not currently expected to take effect until financial year 2024. The Board believes that the benefits of the transfer will include an enhanced experience for customers transacting with the Bank, offer opportunities for enhanced efficiency and profitability, and the development of career opportunities for colleagues.

+ Further information on the Bank's activities in the year can be found in the Chair's Statement on **pages 3 and 4** and throughout the **Strategic Report.**

Review of the year continued

Performance commentary

Operating income at USD 1,014.4m increased vs. last year by 17%, primarily driven by an increase in fees and commissions and trading income.

Net interest income at USD 224.1m reduced year-on-year by 31%, partly as a result of lower balance sheet usage and loans and advances to customers. This includes increased interest expense on the Bank's deposit base due to increasing interest rates and is broadly offset by increased Trading income from management of currency balances, and higher income on interest-earning assets.

Net fees and commissions income increased by 13% to USD 528.5m, primarily driven by an increase in fees received from SMBC Group companies through Service Level Agreement arrangements. Since Brexit, the SMBC Group has changed its structure, leading to increased fees from SMBC Group companies for the Bank's contribution on deals booked in and services provided to SMBC Group's other locations.

Trading income has increased year-on-year, driven by revenue from foreign exchange derivatives which are used to manage the currency composition and liquid asset requirements of the Bank. This has benefitted from the rising interest rate environment on USD balances vs. other currencies and is broadly offset by increased interest expense incurred on USD-denominated deposits.

Operating expenses (excluding impairments) increased by 5% to USD 626.4m driven by movements in Other Expenses of USD 201.3m, which have increased 21% compared to the previous year due mainly to increased information technology (IT) costs, being costs shared across the SMBC group and ongoing investment.

Impairment costs at USD 47.7m decreased by USD 48.1m year-on-year driven by an improvement in the model-driven provisions with improved economic indicators, partially offset by an increase in the post model adjustments. Since the start of the Russia–Ukraine conflict on 24 February 2022, there has been continued economic uncertainty, including a higher inflation and interest rate environment. The Bank considered the direct as well as indirect impact of these events in assessing the provisions on its loan portfolio in the context of entities having operations in Russia and counterparties affected by ongoing economic challenges. The Bank has increased its post-model adjustments in relation to economic uncertainty as explained in note 4 to the financial statements; however, the overall ECL has reduced as a result of an improvement in economic variables.

Profit before tax at USD 340.3m increased year-on-year due to higher operating income and lower impairment costs, partially offset by an increase in operating expenses.

The balance sheet at USD 52.7bn nominally decreased by 3% vs. the previous year, driven by a reduction in loans and advances to customers.

In other comprehensive income, there was a net loss of USD 12.7m on the Bank's defined benefit pension scheme. The loss was primarily driven by a reduction in the valuation of the pension plan assets, reflecting the higher interest rate environment. The full year results are set out in the Statement of Comprehensive Income on page 87. The Directors do not recommend the payment of a dividend in respect of the year ended 31 March 2023.

Key performance indicators

The Board and management use a range of financial and non-financial key performance indicators (KPIs) to help them understand how the Bank is performing and to monitor its compliance with regulatory requirements.

Set out below are the key KPIs used.

Financial KPIs

Return on equity

Profit after tax of USD 252.1m (2022: USD 131.9m) divided by the average monthly equity in the year of USD 5,022.3m (2021: USD 4,910.4m)

5.0%

2023	5.0%
2022	2.7%
2021	5.1%

Tier 1 capital ratio

Tier 1 capital of USD 5,083.0m divided by total risk weighted assets of USD 28,579.2m

17.8%

2023	17.8%
2022	16.3%
2021	16.7%

Cost income ratio

Net operating expenses (excluding impairment losses) of USD 626.4m divided by operating income of USD 1,014.4m

61.8%

2023	61.8%
2022	68.0%
2021	61.0%

Non-performing loan ratio

Gross exposure non-performing loans of USD 478.6m divided by on-balance sheet gross exposure total loans of USD 21,189.0m

2.3%

2023	2.3%
2022	2.0%
2021	2.0%

Leverage ratio

Regulatory Tier 1 capital of USD 5,083.0m divided by Capital Requirements Regulation leverage exposure of USD 36,713.4m

13.8%

2023	13.8%
2022	12.4%
2021	7.7%

Net profit

Profit for the year attributed to equity holders of the parent

USD 252.1m

2023	252.1m
2022	131.9m
2021	240.9m

Gross income

Operating income

USD 1,014.4m

2023	1,014.4m
2022	870.8m
2021	841.0m

Total assets

USD 52,661.1m

2023	52,661.1m
2022	54,017.1m
2021	53,568.5m

Non-financial KPIs

Progress against the Women In Finance Charter targets

+ Read more **page 20**

Carbon emissions

+ Read more **pages 34 to 38**

Supplier payment periods

+ Read more **page 57**

Looking ahead

At the year-end, the global economy appeared to be on a slightly more assured footing than many had anticipated in the latter half of 2022, but significant risks remain. As explained further in the Principal and Emerging Risks section on **pages 13 to 15,** Western economies face significant and increasing headwinds on growth, and uncertainty over how the conflict in Ukraine will unfold could weigh on household consumption and business investment decisions. In addition, tightening financial and monetary policies could lead to lower demand, a rise in unemployment and consumers cutting back on discretionary spending or 'trading down' to cheaper alternatives to save money.

The Bank believes that, over the coming year, business opportunities will be driven by factors including green capital expenditure, renewed European industrial policy (for instance, in relation to biofuels and hydrogen) and the potential intensification of M&A activity after the consensus of peak interest rates is reached.

The Bank will continue to work towards the enhancement of its Corporate and Investment Bank platform and allocate resources to more profitable areas to help deliver long-term sustainable growth. A key area of activity for the Board and its Committees will be the oversight of the activities, both in terms of control structures and business strategy, required to ensure the successful completion of the SMBC Nikko CM securities business transfer.

Other areas of focus are expected to include the further pursuit and embedding of the Sustainability Framework and Strategy, maintaining financial and operational resilience, developing governance and risk management arrangements, and seeking to simplify operations through efficiency measures, whilst responding to the developing regulatory environment. In terms of the business environment, particular attention will be required to assess and manage the risks arising from geopolitical events, energy costs spikes and persistent inflation.

Risks and uncertainties

The Bank is exposed to certain risks and uncertainties in conducting its business.

The risk categories employed by the Bank are set out below, together with information on the principal and emerging risks at the year-end.

+ Information on the way in which the Bank manages risk can be found in the Risk Management section on **pages 73 to 80** and this is incorporated by cross-reference. Additionally, information on financial risk management can be found in note 4 to the financial statements on **pages 99 to 122**.

Principal risks

Type	Description	How risks are managed
Credit	The risk of any losses the Bank may incur due to reduction or loss of the value of assets (including off-balance sheet assets) arising from any credit events, such as the deterioration of a borrower's financial standing.	Credit risk is identified, managed and monitored individually and in aggregate. A number of approaches are used such as limits, indicators and stress testing. Example key indicators include earnings volatility, obligor, sector and country concentration limits and credit quality metrics.
Liquidity	The risk that the Bank cannot meet its liabilities, unwind or settle its positions as they become due.	Liquidity risk is identified, managed and monitored using a number of approaches such as limits, indicators and stress testing. Example key indicators include liquidity coverage ratio, net stable funding ratio and survivability period metrics under stress scenarios.
Market	The risk that movements in interest rates, foreign exchange rates or stock prices will change the market value of financial products, leading to a loss.	The Bank uses Value at Risk to a 99% confidence interval to measure and control market risk alongside other relevant metrics.
Conduct	The risk of the Bank's actions, inactions or behaviours resulting in poor outcomes for its customers and stakeholders, damaging the integrity of the financial markets or undermining effective competition.	The Conduct Rules form the basis of the Bank's approach to conduct risk management. The Bank assesses conduct using a suite of targeted metrics.
Operational and other non-financial	The risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events, including legal risks. There is also an increasing regulatory and Bank focus on operational resilience. As a result of the Bank's activities, it assumes other potential risk impacts such as reputational, conduct and others which it manages within the overall policy framework.	Operational risk is managed with a view to maximising resilience and continuity whilst maintaining acceptable levels of residual risk. Example key indicators used to monitor, measure and report operational risk include operational risk losses and an operational risk profile score underpinned by diverse operational risk indicators. Several appropriate approaches are used to manage other non-financial risks. Further details are contained in the Risk Management section on **pages 73 to 80**.
Model	The potential loss resulting from errors in the development, implementation or use of internal models.	Model risk is managed through the Model Risk Management framework, which comprises four key components: model governance and control, model management, model development and independent model validation.
Sustainability, including climate change	Sustainability risk results from ESG issues, events or conditions that have the potential to substantially impact (financially, reputationally or physically) the Bank, SMBC Group, its clients, the environment and/or society. This risk can manifest itself across all risk types.	This is managed under the Sustainability Risk Framework which is embedded in the broader risk framework and business.

Risks and uncertainties continued

Risk profile

At the year-end, the Bank's risk profile was within the overall risk appetite established by the Board. The risk profile relative to risk appetite is reported monthly at the Executive Committee and quarterly at the Risk Committee.

Principal and emerging risks

The principal and emerging risks at the year-end are described below.

1 Russia–Ukraine conflict

In response to the conflict between Russia and Ukraine, Western countries have stepped up economic sanctions on Russian banks, corporates and individuals in order to apply pressure on the Russian Government and have also sought to reduce their reliance on Russian energy imports. Russia's sovereign rating has seen multiple downgrades by credit rating agencies since the start of the conflict.

Apart from the direct credit risk impact arising from the downgrade in ratings of the Bank's Russian obligors, the Bank is also monitoring the medium- to long-term impacts to both Russian and non-Russian obligors through, for instance, the slowdown of economies, increase of commodities prices and disruption of supply chains. Further information on Expected Credit Losses at the year-end can be found in note 4 to the financial statements (Financial Risk Management).

In terms of non-financial risks, the Bank has responded to the increased legal, regulatory and operational risks due to the unprecedented escalation of multiple sanctions regulations across various jurisdictions and has strengthened monitoring of IT and cyber risks. The Bank is also aware that draft Russian laws have been prepared which, if enacted, may impact colleagues of Russian nationality working in SMBC Group's UK and EMEA operations.

2 Recession risk in the UK, Eurozone and US

Western economies face significant and rising headwinds on growth. The Russia–Ukraine conflict has already acted as a drag on economic activity through multiple channels, including tighter financial conditions, disruptions to trade and higher imported inflation. Uncertainty over how the conflict will unfold could itself weigh on household consumption and business investment decisions. At the same time, lingering challenges from the pandemic could also restrain output, including by exacerbating shortages of labour and key manufacturing inputs.

Central banks are now focused on containing inflationary risks, with a tighter monetary policy cycle either well underway or on the horizon across most jurisdictions. Meanwhile, public sector balance sheets appear stretched after the pandemic-induced shock to financial revenues and expenditures. Tightening financial and monetary policies could lead to lower demand, a rise in unemployment and consumers cutting back on discretionary spending or 'trading down' to cheaper alternatives to save money.

The Bank is considering and managing this risk in a number of ways including:

- Appropriate consideration of risk appetite for new/increased business;
- Simulating potential stress impacts and managing capital and liquidity prudently; and
- Close monitoring of more vulnerable sectors, asset classes and countries.

Conversely, the Bank is also prepared and stands ready to support key clients should conditions worsen.

Principal and emerging risks continued

3 Central Bank policy changes (impact to global and emerging economies)

Monetary policy is at an inflection point. Following the synchronised easing cycle that followed the pandemic, many central banks are now engaged in the process of winding down quantitative easing and other policy support, and raising interest rates from their historical lows.

With the UK and many major economies experiencing the highest inflation rates in decades, the Bank of England and Federal Reserve have brought forward interest rate rises to control demand. Tightening interest rates to control inflation risks economic turbulence, lower growth and rising unemployment. If inflation persists along with higher interest rates, there is a risk of 'stagflation' and a persistent low growth economy with higher unemployment, which will impact businesses in cyclical sectors.

Borrowers will need to pay higher interest expenses to service debt, which will reduce their free cash flow to invest and grow the business. Companies may cut back on plans to borrow and look to de-leverage due to the higher cost of debt, which would reduce business opportunities for the Bank.

Emerging market borrowers also have more exposure to interest rates as they often have large foreign currency debt to service, but local currency cash flow. This may limit the Bank's business opportunities and risk appetite with existing and new emerging markets borrowers.

Interest rate rises could positively impact the Bank's profitability as income increases due to a potential rise in interest margin. This could be driven by higher net interest income from lending over the funding cost and higher income from deploying its own capital. However, this may be offset by increases in personnel and other expenses due to inflationary pressures.

The Bank undertakes interest costs sensitivity analysis in portfolio monitoring and new credit assessments to ensure borrowers can service debt in a rising interest rate environment. With reduced demand growth, corporate downgrades and defaults may rise. The companies and sectors most exposed to economic cyclicality and lower discretionary consumer spending, for instance, non-food retail, leisure and automotive, would likely experience stress, downgrades and credit costs.

The Bank takes a long-standing cautious approach to industry sectors exposed to discretionary consumer spending and conducts close portfolio monitoring and stress testing to inform its view. The Bank also prudently manages its own funding costs and interest rate risks.

4 Cyber and phishing attack

Cyber threats continue to present a significant risk to any organisation with an IT presence. The nature of the threat is constantly evolving, with new threat actors, delivery mechanisms and emerging technologies increasing the likelihood of an attack being successful. Impacts can range from information theft to unavailability of systems and services.

The Bank's customers expect it to provide a reliable, available service that protects their sensitive information. Any cyber attack may result in loss of customer confidence, damage to the Bank's reputation, financial loss (including recovery costs and increased costs of working) and possible regulatory penalties or intervention.

The Bank has a robust 'defence in depth' strategy. Technical and procedural controls are implemented at multiple levels to detect, prevent and respond to potential threats and anomalous behaviour. All technologies are updated regularly to minimise the probability of attacks exploiting known and well-publicised vulnerabilities. The Bank has a well-established security perimeter that is monitored 24/7 by the Security Operations Centre. Any incidents are escalated through the Bank's incident management process, which is tested regularly. All staff receive comprehensive security awareness training and participate in regular phishing campaigns.

Risks and uncertainties continued

Principal and emerging risks continued

5 Financial Crime, Sanctions and Conduct

In response to the Russia–Ukraine conflict, the sanctions environment has been both highly volatile and rapidly changing. Additional efforts have been applied to ensure the Bank keeps pace with regulation and law, including meeting extra-territorial requirements.

As an example, where UK sanctions regulations might typically be amended once every five years, the UK's Russia regulation was amended nine times in less than three months. Additionally, the UK has introduced emergency designation powers to introduce sanctions listings that are published by other countries. The EU and US have taken similar, though not identical, measures and Japan has also been active in introducing new sanctions. Since 5 December 2022, the G7 countries and Australia have implemented the first price cap on Russian crude oil which prohibits G7 domiciled service providers from facilitating trade in these commodities unless the goods are sold at or below the capped price. From 5 February 2023, the same countries implemented further cap restrictions on refined Russian products.

This has resulted in a complex legislative landscape and the Bank is coordinating in real time with counterparts in Tokyo and New York to ensure SMBC Group entities are able to comply with their local obligations.

To strengthen the control framework with regards to regulatory developments more generally, an automated UK regulatory horizon scanning system was onboarded, automatically assigning emerging regulatory change to relevant subject matter experts within the Bank to action. The Bank has provided prevention of financial crime training to a number of the Bank's customers in addition to ongoing mandatory training of all staff.

A mock Suspicious Transaction and Order Reporting visit was arranged with external consultants to assess the Bank's market abuse governance and control framework. In addition, new conduct policies have been introduced to set out a consistent and transparent approach to the identification, understanding and management of conduct risk at all levels of the organisation.

6 US and China confrontation

Relations between the US and China are now at their most acrimonious in decades. The conflict intensified under the previous US President and shows no sign of abating since the current President took over. The Chinese President is also expected to remain in power, and policy against the US is unlikely to change in the near future.

The US and China confrontation is considered to have a wide range of risks, including the impact on geopolitical risks in Hong Kong and Taiwan, as well as economic risks such as tighter restrictions on semiconductor exports to China and the exclusion of Chinese products.

In addition to closely monitoring the direct impact to China-related exposure, the Bank is also mindful of the indirect impact of supply chain instability, through individual and portfolio monitoring, and potential impacts on Japan. The Bank considers these risks in stress testing scenarios.

Non-Financial and Sustainability Information Statement

Below is the Non-Financial and Sustainability Information Statement as required by sections 414CA and 414CB of the Companies Act 2006. The information set out in the table below is incorporated by cross-reference. The Bank has voluntarily reported the climate-related financial disclosures elements of section 414CB.

One requirement of section 414CB is to include information on the policies pursued on the five areas shown below. The Bank has policies and processes in place which govern the way in which it carries out its business in these and other areas. Information on the relevant principal policies is shown below, together with page references where further information can be found.

Any breaches of policy may be self-reported or identified through ongoing review activity, including reviews performed by the Compliance Monitoring Function or Audit Department. Breaches are taken seriously and, depending on the nature of the breach, may result in an assessment for disciplinary action.

Reporting requirement	Section of the annual report	Page references	Relevant policies
Environmental matters	– Sustainability – TCFD	**Pages 21 to 38**	Credit Policies
Employees	– People and culture – Stakeholders – Colleagues	**Pages 17 to 20** **Pages 56 and 57**	– Whistleblowing 'Speak Up' Policy – Employee Handbook
Social matters	– Sustainability – Stakeholders – Environment and Community	**Pages 21 to 29** **Page 56**	– Credit Policy – Customer Focused Compliance Policies – Customer Voice Policy – Anti-Money Laundering and Combating Terrorist Finance Policy – Market Abuse Regulation Policy and related policies
Human rights	– Sustainability	**Pages 21 to 29**	– Anti-Slavery Policy – Slavery and Human Trafficking Statement
Anti-bribery and corruption	– Sustainability	**Pages 21 to 29**	Anti-Bribery and Corruption Policy
Climate-related financial disclosures		**Pages 30 to 38**	
Principal risks		**Pages 12 to 15**	
Description of the business model		**Pages 5 to 7**	
Explanation of amounts in financial statements		**Page 9**	
Non-financial key performance indicators		**Pages 20, 34 to 38 and 57**	

People and culture

The Bank recognises its people as its key asset and is committed to developing the skills and diversity of the workforce. The Bank promotes high ethical standards and a culture where everyone feels able to be their authentic selves at work.

Culture

The Bank's culture is based on five pillars:

1. Provide an excellent service to customers and colleagues through collaboration, teamwork and a sense of shared purpose.
2. Build the Bank's brand by being a reliable and trusted partner to its customers and contribute positively to the societies in which it operates.
3. Protect the Bank's customers and markets by conducting its business in a transparent, prudent and compliant manner.
4. Treat each other with respect and integrity and embrace diversity in all its forms.
5. Be focused, creative and proactive in evolving the business to meet new challenges.

Culture

Monitoring culture

The Board oversees the development of the Bank's culture and, through the year, has done so by considering:

- the results of an employee engagement survey issued every six months which helps the Bank to identify areas for action to improve culture and engagement. During the year, the overall engagement score has remained consistent, while the number of employees responding to the survey has increased. Examples of how the Bank has responded can be found in the Stakeholder Engagement section on **pages 56 and 57**.
- a quarterly KPI report that tracks adherence to the five culture pillars and the remedial plans put in place where performance had deteriorated.

In addition, adherence to the Bank's values and culture within departments has been considered as part of Internal Audit's ongoing work plan, the results of which are considered by the Audit Committee.

Developing culture

At an executive level, the Bank's culture initiatives are coordinated by a Culture Forum, which comprises members from all business functions, including the Culture Champions, who are responsible for delivering action plans at a departmental level. The Forum also includes members of the senior management team, whose role has a direct impact on the evolution of the Bank's conduct and culture. The Forum's discussions in the year have included the post-COVID return to office, the adoption of hybrid working, the impact of culture on diversity and inclusion, and corporate social responsibility. The Forum recognises the importance of employee engagement and feedback in developing the Bank's culture, and examples of this in the year included:

- Introduction of a Deal of the Month celebratory lunch. Hosted by senior management, the purpose of the lunch is to celebrate success and to discuss ways in which the Bank's culture can evolve and how to develop the Bank's strategic and business capabilities.
- Development of an Employee Value Proposition framework setting out what it means to work for the Bank. The initial findings were tested with the Board, employee focus groups and external partners, and will be launched formally, both internally and externally, in the year beginning 1 April 2023.

People

Progressive Working Framework

During the year, the Bank continued to modernise its working practices and policies through the introduction of a Progressive Working Framework designed to enhance collaboration and innovation by combining employee policies, new ways of working in its new London office and building upon the adoption of collaborative technologies. The Bank believes that by supporting alternative working hours and locations, hybrid working will help it retain, attract and develop a diverse talent pool of employees, and enhance engagement and commitment.

A hybrid working survey of all UK employees was issued in the year, with 87% of respondents (comprising the Bank and certain other SMBC Group (EMEA) companies) saying that hybrid working has been positive for them personally, with advantages including less time spent commuting and better balance with personal commitments. In response to some of the challenges identified around collaboration and meeting participation, the Bank issued training on hybrid working techniques and how to lead hybrid teams.

People and culture continued

Performance, learning and talent development

The Bank seeks to support enhanced performance and continuous development through a regular set of 'Performance Snapshot' conversations between employees and their managers. Employees are encouraged to have a professional development plan to identify their development needs and opportunities. Whilst employees are encouraged to take ownership for their development, support provided by the Bank includes funding for professional qualifications, in-house training programmes, secondments and mentoring.

A series of talent programmes develop leadership capability and enable the Bank to focus on critical organisational needs. In the year, the Bank relaunched 'Elevate', a programme that aims to increase confidence, awareness and tolerance in participants, promote diverse talent and foster inclusive leadership.

Diversity and inclusion

The Bank is an inclusive and equal opportunities employer, and its policy is that all individuals are appointed, trained, developed and promoted on the basis of merit and ability. Selection criteria and procedures are designed to eliminate bias, and opportunities for challenge are embedded within these to ensure processes are fair and equitable. The Bank is a proud signatory to the UK's Race at Work Charter and Women in Finance Charter, and SMBC Group is a signatory to the Valuable 500 initiative, an international initiative promoting disability inclusion in business.

The Board recognises the importance of the Bank attracting, developing and retaining diverse talent, and receives regular reports on the Bank's talent strategy and progress on diversity and inclusion initiatives. In the year, the Bank has focused on embedding the four pillars of its Diversity and Inclusion Strategy, summarised opposite:

Diversity and Inclusion Strategy

Building equitable systems
- Ensuring that policies and processes are as fair, equitable and inclusive as possible.

Promoting balance
- Attracting, developing and retaining diverse talent at all levels of the organisation.

Leading with respect
- Consciously creating an inclusive culture in which different perspectives are valued.

Driving advocacy
- Being active allies and promoting the Bank's ambitions externally to candidates and customers.

Building equitable systems

Building equitable systems includes implementing workplace adjustments and support to facilitate the employment and maximise the potential of colleagues who identify as having a disability and/or long-term health condition or injury. In the year, the Bank enhanced its process to identify and implement adjustments. To support greater disability confidence, a new accessibility toolkit was introduced which focuses on promoting disability allyship across the Bank.

The Bank recognises that access to role models can have a positive impact on beliefs about career progression in underrepresented groups and, in the year, extended its networking and mentoring programme, 'InspirHer!', to all female colleagues. The programme provides the opportunity for participants to meet senior female colleagues and to gain guidance on how to navigate their careers, take ownership for their own development and progress into senior roles.

Promoting balance

A 'Sharing Diversity Information' campaign was launched in the UK to encourage all colleagues to disclose their diversity data, which will enable the Bank to track and measure success and identify where further intervention may be required.

The Bank also recognises the importance of improving access to careers in financial services for underrepresented groups and this has been a key focus of the Bank's early talent programmes:

- Kaika, the Bank's front office programme, achieved 53% female representation, 60% ethnic minority representation and 40% lower socio-economic background representation.
- The Industrial Placement Programme provides work experience for students in their penultimate year at university. This year, 39% of students graduating from the Programme accepted a permanent role with the Bank, 57% of whom were female and 36% of whom were minority ethnic.
- An IT Apprenticeship scheme was launched in March 2023, with 10 apprentices joining the programme, 50% of whom were female and 100% of whom were minority ethnic.

Leading with respect

The Bank recognises that senior management accountability is critical for driving progress and that leaders play a pivotal role in creating a culture of inclusion. This year, the Bank has strengthened the connection between performance in relation to diversity and inclusion and overall reward to drive greater accountability.

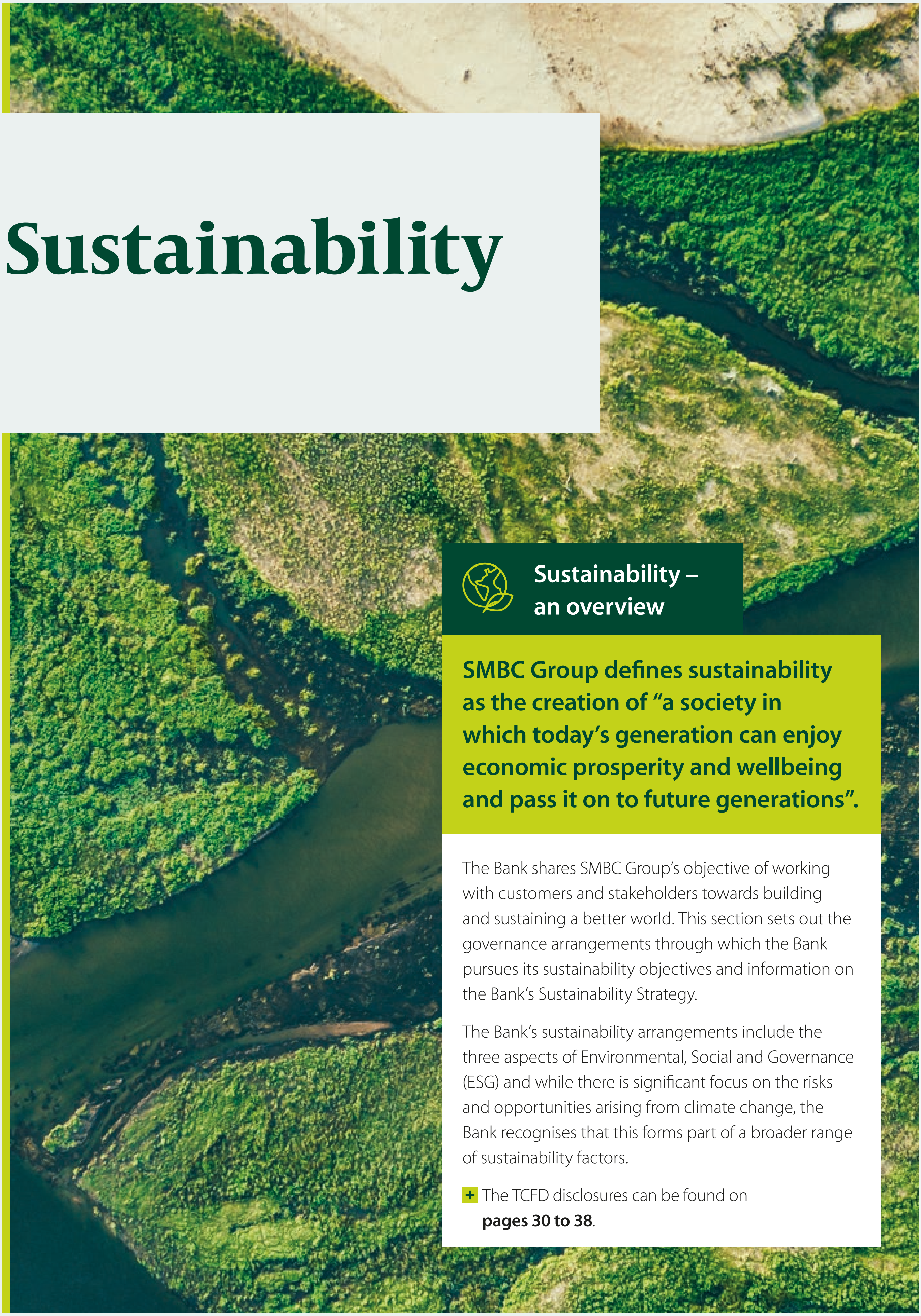
Driving advocacy

The DRIVE (diversity, respect, inclusion, value and equality) employee groups play a key role in helping everyone in the Bank understand the different experiences people may have as a result of their identity. There are four diversity and inclusion groups under DRIVE: Balance (gender), Black Employees & Allies (race and ethnicity), Niji (LGBTQ+) and UNIQUE (disability, mental health and neurodiversity) and a networking initiative (Collaborate). Over the course of the year, all groups have run events and other activities to build awareness and promote allyship.

SMBC Group is a proud signatory of the Women in Finance Charter, which is a commitment to see gender balance at all levels across financial services firms. The Bank's ambition is to have 30% of all senior roles filled by females by 2023. Female talent is in high demand as all organisations seek to make progress on their diversity representation and, as a result, the Bank's senior female representation decreased over the year from 33.5% to 32.6%. On an SMBC Group (EMEA) basis, the decrease was from 29.5% to 29%. The Bank recognises that sustained commitment is critical to driving change, and increasing representation of women at all levels remains a priority.

+ The Bank's gender pay report can be found here **https://www.smbcgroup.com/emea/about-us/diversity-inclusion.** The Bank believes that pay reporting helps it learn more about the key drivers for gaps and enables it to think of interventions that can be put in place to ensure the Bank can reach its goal of creating a workforce that enables everyone to thrive.

Sustainability



Sustainability – an overview

SMBC Group defines sustainability as the creation of "a society in which today's generation can enjoy economic prosperity and wellbeing and pass it on to future generations".

The Bank shares SMBC Group's objective of working with customers and stakeholders towards building and sustaining a better world. This section sets out the governance arrangements through which the Bank pursues its sustainability objectives and information on the Bank's Sustainability Strategy.

The Bank's sustainability arrangements include the three aspects of Environmental, Social and Governance (ESG) and while there is significant focus on the risks and opportunities arising from climate change, the Bank recognises that this forms part of a broader range of sustainability factors.

+ The TCFD disclosures can be found on **pages 30 to 38**.

Sustainability governance – oversight

The Board, supported by its Committees, is responsible for setting and monitoring the development of the Sustainability Strategy. The activities undertaken in the year are set out below.

Sustainability remains an important element of the Directors' ongoing education plan. During the year, the Directors received briefings from internal and external specialists on climate litigation, greenhouse gas (GHG) emissions regulations and economic security, facilitated emissions and understanding transition plans. In addition, certain members of the Board have engaged with Chapter Zero, the UK Chapter of the Climate Governance Initiative, and received briefings from professional advisers on climate matters.

Key activities undertaken by the Board and its Committees in the year

Meeting	Activities
Board	– Approving on a recommendation from the Risk Committee a new ESG Risk Statement (more information **on page 59**). – Considering quarterly updates on progress made against the Sustainability Strategy, including performance against targets. – Considering the results of a third party engagement to develop the Bank's approach in key areas, including assessing customers' transition arrangements and the development of a sustainable finance framework. – Assessing the Bank's Net Zero Plan. – Considering the Bank's lending approach to specific sectors. – Considering developments at the SMBC Group level and assessing implications for the Bank.
Audit Committee	– Reviewing the climate and Streamlined Energy and Carbon Reporting disclosures and the development of the Bank's capability to disclose Scope 3 emissions.
Disclosures Committee	– Considering the current and emerging disclosure landscape across EMEA on climate change matters. – Development of the climate disclosures.
Risk Committee	– Considering a quarterly sustainability risk report, including how management has responded to Internal Audit findings on the framework of sustainability risk management. – Considering the results of a gap analysis of the Bank's climate risk practices against a PRA Dear CEO letter on climate-related financial risk and climate stress scenario assessment.
Remuneration Committee	– Approving the Bonus Fund Cap Calculation Operating Procedures, which include ESG measures of departmental performance.
Executive Committee	– Considering the quarterly ESG dashboard and receiving reports on the EMEA Sustainability Programme Steering Committee's discussions. – Considering customer account planning proposals in respect of financed emissions. – Reviewing trends in climate litigation.

Sustainability continued

Sustainability governance – implementation and execution

Nobuyuki Takiguchi is the executive Director responsible for overseeing the Bank's climate and sustainability initiatives. His responsibilities include developing the Sustainability Strategy and ensuring this is embedded within the overall Corporate Strategy, developing the ESG Risk Statement and framework, escalation of significant business and strategic developments to the Board, and overall climate governance. Nobuyuki is supported in this work by the EMEA Sustainability Programme (ESP) and functional specialists.

Committees and Reporting

Board of Directors

Other SMBC Group entities in EMEA

Executive Committee

Risk & Control Committees

EMEA Sustainability Programme Steering Committee

Governance

Sustainability Management Meeting/Programme Management

Working Groups

Business & Product Development

Risk Management

Carbon Footprint

Reporting & Disclosure

Sustainability Training & Communications

Sustainability Data & Platform

Sustainability Public Affairs & Policy

The ESP is responsible for overseeing the Bank's sustainability activities and works alongside the Risk and Control Committees, which consider sustainability issues at an operational level as part of the Bank's day-to-day activities.

+ Further information on the Risk and Control Committees can be found on **page 75.**

Given the Bank's role as SMBC's headquarters in EMEA, the scope of the ESP also includes SMBC Nikko CM and other SMBC Group entities in EMEA, and this helps ensure there is good coordination and alignment in sustainability activities.

Meeting	Members	Purpose and responsibilities	Frequency/reporting
ESP Steering Committee	– Head of Sustainability Strategy (Chair) – Nobuyuki Takiguchi, Hideo Kawafune – Chief Risk Officer, General Counsel, Chief Compliance Officer, General Manager of Loan Capital Markets Department – Senior executives from SMBC EMEA affiliates	– Setting the Sustainability Strategy and overall ownership of the ESP's business plan. – Considering the Bank's competitive position and driving strategic progress. – The Committee has delegated day-to-day responsibility for delivering the ESP to the Sustainability Management Meeting. – Challenging the Sustainability Management Meeting and Workstreams to ensure timely progress is being made and approving resource needs.	– Monthly meetings and additionally as required. – Significant discussions reported to the Board by Nobuyuki Takiguchi and Head of Sustainability Strategy.
Sustainability Management Meeting	– Head of Sustainability Strategy (Chair) – Workstream leads	– Delivery of the ESP's objectives. – Day-to-day management of the ESP. – Ensuring that business and regulatory requirements are met. – Project planning. – Early identification and management of issues and risks. – Addressing working group interdependencies. – Assessing operating model impacts.	– Monthly and additionally as required. – Reports to the Steering Committee on progress toward agreed goals and notification of issues.
Working Groups	– Each led by a functional specialist	– Progressing the ESP in their areas of expertise. – Developing and delivering on a work plan to support the strategy. – Strategic and governance matters relating to each Workstream reviewed by Head of Sustainability Strategy.	– Each Workgroup reports to the Sustainability Management Meeting.
Programme Management	– Overseen by Project Management Office – Planning representatives	– ESP governance and planning. – Ensuring robust project management, including issues and actions tracking. – Supporting the Steering Committee and Sustainability Management Meeting.	– As required

Sustainability continued

Sustainability Strategy

The Sustainability Strategy has four elements:

1 Customers

Support clients in their journey to sustainability

Given the Bank's key client sectors and supported markets, it is exposed to businesses that are natural resources intensive and markets that are at varying stages of regulating environmental and social standards. The Bank believes that the most direct means of influencing customer ESG performance is by using its long-standing customer relationships to help identify the most material ESG issues and opportunities, share insights on sector strategies and leading practice, and offer financing and advisory services for firms to invest in their performance.

The Bank has invested in its own capabilities by hiring technical experts from industry, working with external expert advisors to develop sector specific research and ensuring functional specialists are involved in key external forums, such as the Science Based Targets Initiative, the Loan Markets Association Sustainable Finance Steering Committee and Net Zero Banking Alliance (NZBA) sector sub-tracks, so that employees can contribute to the development of the market and stay informed on leading practice. In addition to meeting individually with customers on their sustainability strategies, the Bank has held customer events through which it has shared insights and connected clients with functional specialists. Examples of topics covered include ESG in emerging markets, changes in the renewables energy sector and developments in new energies.

2 Solutions

Recognised as a leading provider of green and sustainable finance solutions

The Bank recognises that maintaining the integrity of the sustainable finance market is critical in allowing capital to flow toward more sustainable business activities. Therefore, the Bank has set an ambition to not only make a significant contribution to SMBC Group's 10-year JPY 50 trillion sustainable finance commitment (increased by SMBC Group in May 2023 from JPY 30 trillion), but to do so in a way that respects market standards and aims to support ambitious performance. The Bank has put in place procedures, training and a governance process to facilitate ESG-labelled transactions that are aligned to market standards.

The Bank's sustainable finance performance is measured by the value of ESG-labelled transactions, the number of transactions for which the Bank is in the ESG Coordinator role, league table performance among peer banks in EMEA, and the number of transactions that are escalated for review.

In 2022, SMBC was honoured to receive awards related to sustainable finance, including the Financial Institutions Deal of the Year Award at the Bonds, Loans & Sukuk Turkey Awards 2022. This award was received for a transaction with a Turkish financial institution where SMBC acted as Sustainability Coordinator, Bookrunner and Mandated Lead Arranger for a syndicated Sustainability-Linked Term Loan. The pricing of this loan was tied in part to that bank's ability to improve diversity among farmers in the agricultural sector. Although the lending for this transaction was ultimately undertaken by SMBC's London branch, the Bank's specialist teams provided the expertise and engaged with the customer and other counterparties.

3 Business

Embed sustainability risk management and culture in all aspects of the business

Risk management

The Bank approaches sustainability risk, including climate change, in the same manner as it approaches all risk, through the lens of the Identify, Measure and Monitor, Manage and Report (IMMR) framework. The Bank uses data, tools and expertise (internal and external) to identify and assess sustainability related risks. Depending on the potential materiality, policies and processes are implemented to measure, monitor and report these risks, both internally and externally. This framework reinforces the consideration of sustainability risk in the Bank's business and strategy decisions, and is achieved through embedding the risk in strategic tools and processes, such as the Internal Capital Adequacy Assessment Process (ICAAP), Risk Appetite Framework and Risk Appetite Statement, as well as the risk inventory. This allows the Board and management to understand and oversee the most material sustainability risks and the related control environment.

Training

The Bank has established a structured framework to train its people on sustainability and ESG topics with the objective of building the skills, knowledge and expertise required to deliver the Sustainability Strategy. In the year, over 30 training events were held, exceeding the target to deliver 3,000 training hours on sustainability. Mandatory training modules were also issued to provide a foundation level of knowledge to all employees and specialist knowledge for employees in specific roles. Training topics in the year included the Bank's Sustainability Strategy, sustainable finance products, governance and procedures, and avoiding greenwashing.

4 Footprint

Proactively pursue GHG emission reductions with an aim to be net zero by 2030 or sooner (Scope 1 and 2) and by 2050 (Scope 3)

A significant area of focus in the year has been on reducing the carbon footprint of the Bank's business activities and operations, in line with SMBC Group's public commitments to achieve net zero emissions in its own operations by 2030 and in its overall loan and investment portfolio by 2050. In line with this commitment, SMBC Group is a member of the NZBA and Net Zero Asset Mangers Initiative (NZAMI). SMBC Group has also set medium-term greenhouse gas emissions reduction targets for the power, oil and gas, and coal sectors, and has also established a Net Zero Transition Plan. SMBC Group is also a signatory to the Poseidon Principles. As a signatory to these Principles, the Group has committed to measuring the carbon emissions of its lending portfolio of financed ships and, starting from December 2022 , disclosing the alignment of its portfolio with the trajectory to achieve a 50% reduction in emissions by 2050 vs. 2008 (the United Nations–International Maritime Organization target).

The Bank's Net Zero strategy is focused on using the key levers available to it to steer its portfolio toward clients and business activities that are best positioned to thrive in a low carbon economy. This year, the Bank made significant progress in its capabilities related to the Group's net zero commitment by working with an external advisor to analyse the Bank's power and energy sector portfolios, create a forward-looking plan to achieve interim targets and improve the framework for evaluating client transition strategies. Using this analysis, the Bank has set client-level account engagement plans with varying levels of engagement intensity. This client-level engagement is a key lever available to the Bank to steer its portfolio, alongside Bank policies and the development of new, net zero aligned business activities.

+ Further information on the way the Bank is managing its footprint, including the Streamlined Energy and Carbon Report, can be found on **page 36**.

Sustainability continued

Conduct of activities for sustainable growth

The Bank recognises that to achieve sustainable growth it is necessary that its activities are conducted in line with all legal and regulatory requirements. Conduct key risk indicators (KRIs), which seek to provide effective risk identification, are regularly reviewed, including by the Executive and Risk Committees. Set out below is information on how the Bank manages the risk arising from the conduct of its activities and its key policies.

The Bank's policy framework aims to help its people understand good conduct, positive behaviours, and how to raise and address concerns. The policies set out the Bank's approach to the identification, understanding and management of conduct risk at individual, departmental and organisational levels. They also explain that conduct applies to both financial and non-financial behaviours and that conduct is recognised as being closely linked to the Bank's values, culture and an environment of psychological safety.

Speak Up is a key component of the Bank's governance and risk management framework. The Bank's aim is that all colleagues feel able to raise concerns about incidents of wrongdoing or suspected malpractice (financial and/or non-financial), without fear of criticism, discrimination or unfair punishment. The Speak Up framework seeks to create a culture of openness for all employees including those working remotely and to demonstrate that malpractice and wrongdoing are taken seriously and will be dealt with at the highest level to prevent poor outcomes for employees, customers and other stakeholders. There are various internal and external channels available to raise concerns, and these include an independent firm working in partnership with the Bank through which reports can be raised anonymously.

Key policies

Description	Outcome
Customer Voice Policy How the Bank identifies, records, investigates, responds to and escalates expressions of dissatisfaction. Where errors are a consequence of the Bank's actions, it always seeks to ensure that customers do not suffer any detriment. **Customer-focused Compliance Policies** These set out the processes through which the Bank ensures adherence to regulatory requirements when dealing with customers, ensuring they are treated fairly.	– Information on customer dissatisfaction considered by Risk Committee and Executive Committee. – During the year, the level of complaints was very low and all were managed in line with the Bank's Policy to customers' satisfaction. – Policies reviewed regularly to reflect regulatory change and the development of the business.
New products and services All new products and services are subject to a risk assessment and monitoring process, and are reviewed on a cycle to ensure they remain appropriate for the purpose originally intended.	– Review process intended to ensure that products and services are offered in a way that meets customer expectations, conform with legal and regulatory requirements, and are consistent with the Sustainability Strategy.
Whistleblowing 'Speak Up' Policy Sets out the routes through which concerns can be raised	– The Audit Committee receives a quarterly report on the nature of whistleblowing reports received and considers reports on the whistleblowing systems and controls. – The Board receives an annual report from the Whistleblowers' Champion on the autonomy and effectiveness of the whistleblowing procedures.
ESG Risk Statement How the Bank identifies, measures, manages, monitors and reports sustainability related areas of heightened risk to the Bank, the environment and society.	– The Statement remains under constant review to reflect evolving requirements. – Developments have been overseen by the Risk Committee.

Prevention of financial crime and anti-bribery and corruption

The Bank has zero tolerance towards all forms of financial crime, including money laundering, bribery and corruption, fraud and non-compliance with financial sanctions. The Bank has developed, and will continue to develop, financial crime-related systems and controls for mitigating financial crime risks, including policies, standards, procedures, guidance, training and risk assessment models. All employees are required to adhere to the Bank's prevention of financial crime policies, on which they receive training on joining the Bank and annually.

Description	Outcome
Anti-Money Laundering and Combating Terrorist Finance Policy Sets out the due diligence processes to prevent money laundering and fraud, and to combat the financing of terrorism. **Anti-bribery and Corruption Policy** Sets out the processes through which the Bank seeks to prevent bribery and corruption.	– The MLRO reports to the Risk Committee annually on the operation and effectiveness of the arrangements to counter the risk of the Bank being used to further financial crime. – In addition, the Risk Committee receives quarterly reports on topics of significance and conducts deep-dives as required. – Policies reviewed regularly to reflect regulatory change and the development of the business.

Prevention of slavery and human trafficking

The Bank's approach to slavery and human trafficking is guided by the principle that it should not be involved, directly or indirectly, in the commission or facilitation of the offences set out in the Modern Slavery Act 2015. This approach is documented in an Anti-Slavery Policy and supported by Operational Standards, which set out the requirements and obligations applicable to all employees to prevent modern slavery and/or human trafficking and on which training is given. The Policy and Standards are prepared in consideration of best practice guidance issued by the UK Home Office and international bodies, including the United Nations and International Labour Organisation. SMBC Group is a signatory to the United Nations Global Compact and the 10 principles related to human rights, labour standards, environment and anti-corruption measures.

The Bank's Standards require anti-slavery due diligence to be undertaken on all counterparties. This includes seeking an Anti-Slavery Statement or equivalent document and undertaking adverse news screening incorporating specific terms relevant to slavery and human trafficking. The Bank has an ongoing commitment to maintaining and improving its systems and processes to mitigate the risk that it might be involved in the commission or facilitation of slavery and human trafficking in any part of its operations, supply chain (including customers, contractors and suppliers), products, services and employee activities. The Bank also expects its suppliers and business partners to undertake ethical business practices, particularly in, but not limited to, economic sectors where there are higher risks of Slavery and Human Trafficking.

+ Further information can be found in the Bank's Slavery and Human Trafficking Statement at: **www.smbcgroup.com/emea/antislavery**. This Statement is reviewed and approved annually by the Board.

Sustainability continued

Prevention of market abuse

The Bank has a suite of policies in place setting out its arrangements for adhering to the regulatory and legal requirements that protect the integrity of the markets in which the Bank operates, and the rules and standards of conduct to which all the Bank's people must adhere.

All employees are required on joining the Bank and annually thereafter to undertake training on the prevention of market abuse. All employees, regardless of role, are required to notify the Compliance Department immediately should they have a reasonable suspicion that a transaction might constitute insider dealing or market manipulation.

Communities

During the year, the Bank established a Corporate Social Responsibility (CSR) team with the objective of developing and delivering a cohesive approach to community engagement, including consistency with SMBC Group's global approach and alignment to the relevant UN Sustainable Development Goals. The CSR function led the development of a new CSR strategy informed by the results of an employee survey to understand employees' views on CSR matters, to identify what activities they were already involved with and what would enable the Bank to create more consistent engagement in the future.

The Bank recognises the importance of contributing to society and, in support, offers employees a variety of ways to engage with community activities, including a paid volunteering allowance; matched funding of employee donations (up to a certain limit); a Give-As-You Earn salary sacrifice scheme; and access to a select number of corporate memberships in arts and culture, with associated employee benefits. The Bank's CSR activities in the year included:

- Fundraising appeal in support of the humanitarian aid work of the International Committee of the Red Cross in and around Ukraine, and after the devastating earthquakes in Turkey and Syria.
- Donation to a charity of decommissioned furniture and non-sensitive hardware. Unclaimed coins and clothes were also donated to local charities.
- The hosting of team volunteering days, including International Volunteer Week in December with almost 200 colleagues participating.
- The formation of a Global CSR Forum, involving SMBC Group internationally.

The CSR strategy has four pillars:

1. **Elevating the levels of corporate philanthropy and charitable giving**
2. **Increasing participation in volunteering to leverage the intellectual capital available across the Bank to help create positive social impact**
3. **Supporting employees with their fundraising aspirations**
4. **Leveraging the Bank's corporate assets by increasing engagement with corporate memberships and to make real estate assets and networks available to support the Bank's local communities**

Task Force on Climate-related Financial Disclosures

This section provides information on the Bank's approach to managing the risks and opportunities arising from climate change.

+ Further information relevant to this TCFD Report can be found in the Sustainability section. Where this is the case, the relevant page numbers are indicated.

SMBC Group recognises that addressing climate change issues is one of the most important global concerns of the 21st century. The Bank fully supports SMBC Group's climate objectives and works closely with colleagues across the Group to ensure alignment in activities and the application of global policies. As a result, certain aspects of this section describe activities the Bank has undertaken as part of SMBC Group. Although there is close cooperation with SMBC Group, the Board and its Committees retain responsibility for overseeing and making key decisions in respect of the Bank's own activities.

With effect from the financial year beginning 1 April 2023, it will be necessary for the Bank to report its climate disclosures in line with the requirements of The Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022. However, the Directors recognise the importance of climate change to the Bank's stakeholders and considers it appropriate for the Bank to report its current arrangements. It has done so using the Task Force on Climate-related Financial Disclosures (TCFD) framework and the statutory requirements.

+ SMBC Group's TCFD Report 2022 can be accessed here: **https://www.smfg.co.jp/english/sustainability/materiality/environment/climate/pdf/tcfd_report_e_2022.pdf**

Governance

The Bank adopts a holistic approach to sustainability, which aims to consider all elements, including climate change. This approach is reflected in the governance framework the Bank has implemented to oversee and manage its sustainability work. Information on the following governance aspects relevant to the TCFD Report can be found in the Sustainability section as follows:

Further information

Disclosures

+ Overview of sustainability matters considered by the Board and Board Committees in the year **page 22**.
+ Board briefings received in the year **page 22**.
+ Overall governance framework, including the roles and responsibilities of the Board, Board Committees, individual Directors and the EMEA Sustainability Programme **page 23**.

Task Force on Climate-related Financial Disclosures continued

Strategy

The Bank recognises that climate change will present both risks and commercial opportunities for its business, which will vary by time horizon considered. These risks and opportunities are considered in the Bank's strategic planning process.

Climate Risks

	Risk Type	Event Examples	Possible Impacts
Physical	Acute	Increased frequency, severity of climate-related weather events, for example, droughts, floods and storms	– Business disruption – Damage to property
	Chronic	Progressive changes in climate patterns resulting in, for example, sea level rise, sustained higher temperatures, biodiversity loss	– Damage to property – Reduced productivity – Supply chain impacts
Transition	Policy & Regulation	Abrupt adoption of climate-related policies such as taxation of emissions	– Decreased asset values or stranded assets – Disruption of business models – Increased public scrutiny – Increased costs
	Technological	Faster than expected adoption of new net zero technologies or demise of legacy ones	
	Market Demand	Faster than expected changes in demand for goods and services based on climate impacts	

Considering the Bank's climate and wider sustainability-related opportunities, the Bank believes that SMBC Group's status as one of the world's leading project financiers and renewable energy lenders positions it well to finance the significant investment needed into new energies, renewable energy and power infrastructure in the short to medium term. The Bank also has close and long-standing relationships across the energy, power, transportation and building sectors where transition advisory services are in high demand.

Bearing in mind these risks and opportunities, the Board has approved, and oversees, the Sustainability Strategy.

The Bank's ESG Advisory & Solutions Hub, a dedicated resource of ESG experts that advise customers on topics, such as how to finance their low carbon transition needs, technological and sectoral developments and investor perspectives on ESG, has been key in allowing the Bank to capitalise on sustainability-related opportunities. The Bank's sustainable finance business has continued to grow because of this strong collaboration.

At present, the Bank offers the following sustainable finance solutions:
- Green Loans
- Sustainability-Linked Loans
- Social Loans
- Sustainable Supply Chain Finance
- Green Deposits
- Renewable energy, new energy and energy transition lead arranging and advisory
- ESG ratings and framework advisory
- In partnership with SMBC Nikko Capital Markets, SMBC Group is able to offer a range of ESG-related capital markets products, including ESG derivatives, which were introduced during 2022.

Further information

Disclosures

+ Overview of Sustainability Strategy **pages 25 and 26**.

The Bank considers products to be labelled Green, Social, Transition or Sustainability-Linked if they align with the Bank's internal sustainable finance procedures and checklist, which are based on guidance from the Loan Market Association (LMA) and supported by regular training. Members of the ESG Advisory & Solutions Hub represent SMBC Group on the LMA Sustainable Finance Steering Committee, which provides guidance to the industry on loan structuring, as well as the Science Based Targets initiative (SBTi) Oil and Gas Expert Advisory Group to ensure the Bank's energy sector clients have access to robust and science-based advice.

Whilst developing the sustainable finance business is important, the Bank recognises that its Sustainability Strategy needs to be integrated into all aspects of business strategy. The Bank is taking a two-pronged approach of engaging with existing customers to understand their transition plans and focusing on growing its business by serving customers who it believes are either embarking on a credible transition or are already engaged in business activities needed to support the future net zero economy. This year, it developed and is in the process of introducing a new framework for evaluating customers' transition plans, considering factors such as quantitative targets, alignment with a 1.5°C pathway, board-level governance, evidence of implementation and a commitment to transparency and disclosure.

The Bank performs scenario analysis using three of the Network for Greening the Financial System scenarios, reviewing both physical and transition risk. The Bank believes its top risk is transition risk for high emitting sectors, such as Power and Energy, which will likely be impacted by government policy updates or changes in consumer preferences in the medium term. This is reflected in the Bank's strategy through its current or planned efforts to engage with clients in these sectors to evaluate and support their transition maturity, offer sustainable finance solutions to meet their needs and adjust the Bank's appetite for future business opportunities based on customers' transition maturity. Based on this scenario analysis, the Bank believes its strategy remains resilient, as it has mechanisms for limiting its exposure to customers without an adequate transition strategy.

Risk management

Sustainability risk results from ESG issues, events or conditions that have the potential to substantially impact (financially, reputationally or physically) the Bank, SMBC Group, its customers, the environment and/or society. This risk can manifest itself across all risk types. Sustainability risk includes climate change-related risk.

Information relevant to the TCFD Report can also be found in the Sustainability section:

Further information

Disclosures

+ Sustainability risk governance and how this is implemented in the risk management framework **pages 23 and 24**.

Risk-based approach to client assessment

The Bank is currently focused on the higher risk sectors as defined by its policies, and is evolving the tools, processes and factors considered in assessing client risk. Over the year, the Bank has developed, and continues to develop, the function that has been established to manage sustainability risk, including climate change-related risk. The key tools in place that inform business and strategy decisions include:

- Climate Change Risk Assessment (CCRA)
- Equator Principles
- Stress testing and ICAAP
- Risk Register
- Risk Appetite Framework
- Regulatory Horizon Scanning Tool

The Bank intends to evolve these tools to improve its assessment and risk management capabilities.

Climate Change Ratings Assessment (CCRA) tool

The Bank has developed a CCRA tool through which it assigns a climate risk (transition and physical) assessment score for each customer. Transition risk represents financial risks/losses that could arise from the process of adjusting towards a low carbon economy. This includes changes in technology, social preferences and legislation. Physical risk represents the financial risks or losses that could arise as a result of climate- and weather-

Task Force on Climate-related Financial Disclosures continued

related events, such as heatwaves, floods, droughts and sea level rises. The combination of the CCRA tool and broader consideration of sustainability risks in transactions enables the Bank to understand customers' sustainability risk and energy transition plans. This information is included in internal transaction documentation prepared by front office teams and assessed as part of the credit and transaction approval process. All the Bank's clients are in scope of the CCRA except sovereign and sub-sovereign public sector clients, as the tool is designed for assessing commercial customers.

The Bank continues to enhance the tool to reflect the evolution of data, tools, capabilities and internal, industry and regulatory developments and maturity. Future enhancements will include a further expansion of the tool's capabilities to assess a broader range of sustainability issues and factors.

Equator Principles

SMBC Group has adopted the Equator Principles, a set of principles for determining, assessing and managing social and environmental risks in finance to large-scale development projects. It has established a team within its Tokyo Corporate Sustainability Department to assess social and environmental risks in accordance with the Principles.

Stress testing and ICAAP

The Bank has undertaken climate risk scenario analysis and stress testing since 2019, with a modelling horizon of 30 years. The scope of the stress testing is consistent with the scope of the CCRA scorecard, with the majority of the Bank's portfolio covered except public sector obligors.

The Bank's scenario analysis is broadly aligned with the Bank of England's Climate Biennial Exploratory Scenario (CBES) (announced in November 2020 with results published in May 2022) and, through it, the Bank analyses the stress impact on its portfolio of three scenarios: No additional policy (>4°C temperature change), Early Policy Action (<2°C) and Late Policy Action (<2°C). The stress scenarios inform the potential credit impact of climate change in the existing portfolio over the long term, and the results are included within the Bank's capital assessment and ICAAP document. Climate risk modelling is still in its infancy. Due to a lack of historical data to forecast how climate risk could impact default risk, expert judgement is utilised in the calibration of climate risk-related Probabilities of Default.

The Bank has conducted a gap analysis by comparing the Bank of England results and its observations on firms' practices with the Bank's climate stress tests results and methodology. The result of the gap analysis showed that the Bank had made good progress in integrating climate risk into its existing risk and reporting frameworks whilst highlighting areas for further enhancement. The Bank's climate risk stress test results are broadly in line with CBES participants with respect to impact on annual profits. As part of the overall plan based on this gap assessment, the Bank's climate stress test methodology will be further enhanced to better align with the CBES participants and to address the data and modelling gaps identified.

Risk Register

An internal taxonomy of key risks and controls is used to inform the ongoing identification of risks. The Bank recognises that sustainability risks, including climate change, are inherent across the spectrum of risk categories. This has allowed the Bank to consider how climate change risk impacts each of the risk drivers and the control environment in place to manage them.

Risk Appetite Framework

The purpose of risk appetite is to define the broad-based level of risk that the Bank is able and willing to undertake in pursuit of its objectives. The Risk Appetite Framework ensures formal identification and consensus about the strategic-level risks which the Bank is facing and is a key tool for the business. With effect from 1 April 2023, SMBC Group introduced climate-related targets to manage portfolio GHG emissions in each sector/business unit to align with the 1.5°C scenario. The Bank is aligned to the Group's climate-related targets. The Bank has KRIs and control measures in respect of climate and sustainability within its Risk Appetite Framework and intends to further develop its capabilities so that further strategic climate and sustainability risk appetite steering measures are in the framework in the future.

Regulatory Horizon Scanning Tool

Regulatory horizon scanning is an important process for the Bank as it facilitates the identification of upcoming prudential regulatory changes and/or guidance which are materially relevant to any/all SMBC legal entities and branches across EMEA, encompassing diverse topics, including sustainability risk and disclosures. This process provides a standardised view of the impact of the relevant regulations on the Bank and their current status (i.e. proximity to implementation).

Metrics and targets

Management Information (MI)

Management information, metrics and targets are key components of the Sustainability Strategy and Risk Framework and allow the Bank to make more effective and efficient data-driven strategic business and risk decisions.

During the year, the Bank has developed its approach to the measurement of climate metrics and, in particular, its ability to measure the emissions associated with its lending (financed emissions), which is a key metric to measure alignment with net zero ambitions.

The Bank will continue to evolve its approach with the aim of increasing usability and transparency while considering proportionality, data quality and other factors.

In line with the Bank's Booking Policy, many transactions originated by or worked on by Bank employees are ultimately booked in other EMEA entities of SMBC Group. Given this, some of the Bank's sustainability metrics and targets are prepared on an SMBC Group (EMEA) basis, rather than an SMBC BI specific basis. The Bank believes this approach encourages its people to work more closely with SMBC Group to the benefit of customers.

Presented below are a selection of the most relevant performance and risk indicators, with further information shown later in this section. The Bank has selected these indicators for inclusion in this Report as they support the Sustainability Strategy, are aligned with indicators disclosed by the wider SMBC Group, and documented evidence of the underlying data means the indicators are reliable and verifiable.

The indicators shown below state whether these have been prepared on a Bank only basis or on an SMBC Group (EMEA) basis.

Measure	Metric	Basis	Target	FY2022	FY2021
Sustainable finance	Sustainable finance – USD bn	SMBC (EMEA)	USD 12bn	**USD 16.131bn**	USD 11.049bn
Operational emissions	tCO_2 per FTE	SMBC BI	Net zero by 2030*	**0.83 tCO_2e/FTE**	1.02 tCO_2e/FTE**
Financed emissions	GHG emissions from loan/ investment portfolio	–	Net zero by 2050*	**–**	–
	Oil & Gas – $MtCO_2e$	SMBC BI	Reduce by 12 – 29% by 2030*	**0.15 $MtCO_2e$**	0.84 $MtCO_2e$
	Power – gCO_2e/kWh	SMBC BI	138 - 195 gCO_2e/ kWh by 2030*	**191 gCO_2e/kWh**	111 gCO_2e/KWh
Climate Change Risk Assessment	Clients Assessed for Climate Change Risk – % of clients	SMBC BI	80%	**98%**	84%
Exposure to carbon-related sectors	Exposure to carbon-related sectors – % of portfolio	SMBC BI	–	**58%**	56%

* SMBC Group-level target – SMBC's net zero targets, for both operational emissions and financed emissions, are SMBC Group-level global targets. The Bank measures its performance on these metrics to ensure it is contributing to SMBC Group's overall net zero goal.

** The FY2021 data for tCO_2e per FTE has been re-aligned to mandatory SECR reporting only, thus the figure has been restated from 1.47 to 1.02 tCO_2e per FTE.

Task Force on Climate-related Financial Disclosures continued

Sustainable finance

The Bank's sustainable finance target is a key part of how it measures whether it is achieving its ambitions to support its customers in their journey to sustainability and to be recognised as a leading provider of green and sustainable finance solutions.

The target to provide USD 12bn of sustainable finance in the financial year is an EMEA-wide target, so this metric is prepared on an SMBC Group (EMEA) basis. The Bank's performance contributes to SMBC Group's global commitment to provide JPY 50 trillion (increased by SMBC Group in May 2023 from JPY 30 trillion) between financial year 2020 and financial year 2029, as part of its GREEN x GLOBE 2030 strategy.

The Bank again grew its sustainable finance business in FY2022, reflecting both the expansion of labelled transactions industry-wide, as well as the EMEA-wide investment made in building capacity at SMBC. At the end of the financial year, SMBC Group (EMEA) was ranked 5th in the Dealogic Mandated Lead Arranger League Tables for Green and Sustainability-Linked Loans on a 12-month rolling basis.

Total of sustainable finance facilities (presented on an SMBC Group (EMEA) basis).

Product	FY2022 (of which SMBC lending/underwriting/arranging amount) (USDm)	FY2022 (of which SMBC lending/underwrite amount) (USDm)	FY2021 (USDm)
Total*	**16,131**	**12,383**	11,209

* A portion is provided in partnership with SMBC Nikko CM.

The Bank has an internal definition for what transaction types qualify as sustainable finance, controls for ensuring this definition is met and adhered to, and processes for identifying and tracking relevant transactions. The Bank's internal methodology refers to best practice industry standards such as the LMA Sustainability Linked Loan Principles and the ICMA Green Bond Principles. If a transaction qualifies as sustainable finance, either the amount lent or arranged by the Bank, as applicable, is accounted as sustainable finance. The amount lent or underwritten by the Bank is also presented in the table to allow comparability with previous years.

Operational emissions (Streamlined Energy and Carbon Reporting)

The UK Government's Streamlined Energy and Carbon Reporting (SECR) policy was implemented on 1 April 2019. The Bank meets the SECR qualification criteria in the UK and, as in previous years, is reporting the emissions from its operations.

In the year, the Bank moved into a new headquarters building. British Land's 100 Liverpool Street development is a BREEAM Outstanding rated building, with efficient thermal envelope design and highly efficient building services equipment, such as a rooftop solar PV array and a 'grey' and rain-water system, with extra filtration on the air conditioning system. It achieved an 'Excellent' BREEAM fit-out rating in September 2022.

Energy consumption (kWh), both direct and indirect, has increased in the year by 0.5%, mainly due to an increase in the energy consumption associated with data centres (25% increase), arising from extra data service capacity used during the reporting period.

Scope 1 and 2 emissions have reduced in the year by 11% and the intensity metric for emissions, $kgCO_2e$/FTE employee, has reduced by 19%.

The Bank is committed to better reporting and understanding its environmental impacts. In the year, the Bank engaged a new booking partner for business travel, which has enabled it to improve the quality of its data on emissions from travel and hotel stays, which were not previously included. There has been an increase in travel-related Scope 3 emissions compared to the previous reporting period, arising from increased travel after the COVID-19 pandemic, as well as the more detailed reporting.

Due to the customer relationship-driven nature of the Bank's business, business travel will continue to be a factor in the Bank's emissions. The Bank seeks to minimise the impact of through its travel policy and the carbon footprint information in its travel booking tool.

Metric	FY2022	FY2021	Difference (%)
Total energy use (MWh)	**9,646**	**9,602**	**+ 0.5%**
Total GHG emissions Scope 1 and 2 (location-based tCO_2e)	**1,494**	1,669	-11%
Total GHG emissions Scope 1 and 2 (market-based tCO_2e)	**682**	643	+ 6%
Total SECR mandatory GHG emissions (location-based tCO_2e)	**1,497**	1,683	-11%
Total SECR mandatory GHG emissions (market-based tCO_2e)	**685**	657	+4%
– Of which Scope 1 (location-based tCO_2e)	**416**	406	+2%
– Of which Scope 1 (market-based tCO_2e)	**237**	311	-24%
– Of which Scope 2 (location-based tCO_2e)	**1,078**	1,263	-15%
– Of which Scope 2 (market-based tCO_2e)	**444**	331	+34%
– Of which Scope 3 (grey fleet tCO_2e)	**3.61**	14.01	-74%
Scope 3 emissions (tCO_2e)**	**2,286**	859	+166%
Emissions per employee (tCO_2e/FTE)	**0.83**	**1.02*** **	**-19%**

* Total energy use includes gas, electricity consumption associated with leased offices and data centres, plus fuel from grey fleet, i.e. emissions from business travel in rental cars or employee-owned vehicles.

** Total Scope 3 emissions includes the mandatory SECR requirements (fuel from grey fleet) and voluntary categories of business travel, electricity including transmission and distribution losses, waste and water emissions.

***The FY2021 data for tCO_2e per FTE has been re-aligned to mandatory SECR reporting only, thus the figure has been restated from 1.47 to 1.02 tCO_2e per FTE.

Task Force on Climate-related Financial Disclosures continued

Financed emissions

SMBC Group is committed to aligning its lending portfolio with net zero emissions by 2050 and joined the Net Zero Banking Alliance in October 2021. Measuring the emissions associated with its lending, known as financed emissions, is how the Bank assesses its progress towards its net zero commitment.

Currently, the Bank measures the financed emissions associated with its lending in the oil and gas and the power sectors. The methodology used is aligned with the Partnership for Carbon Accounting Financials (PCAF) Standard and is detailed below.

SMBC has set Group-level interim targets for the financed emissions associated with its lending to oil and gas and power portfolios. The targets are:

- Reduce the absolute amount of financed emissions from its oil and gas portfolio by between 12% and 29%, compared to a 2020 baseline, by 2030.
- Reduce the emissions intensity of its power portfolio to a range between 138 - 195 gCO_2e/kWH, compared to a 2020 baseline, by 2030.

Presented below is the Bank's financed emissions performance, including the amount of exposure in scope of financed emissions monitoring and control, the emissions performance, and the PCAF data quality score – a measure of the data quality on which the Bank's financed emissions calculations are based.

The measurement of financed emissions performance is a relatively new process for the the Bank and, as such, it is continually working to expand the scope and quality of measurement, for example, through the provision of more and better-quality emissions data. Additionally, due to the PCAF calculation methodology, changes in financed emissions year-on-year can be impacted by a variety of factors aside from real-world emissions reductions, such as changes in client exposure or enterprise value. Given this, the Bank anticipates some fluctuation in financed emissions performance as market practice and data availability mature.

Asset classes in scope of financed emissions calculations represent on-balance sheet lending. Off-balance sheet activity, including guarantees, letters of credit and capital markets, are not in scope. The rationale for including asset classes in scope is whether an agreed industry standard for financed emissions accounting is well established by PCAF and widely used for the asset class.

As mentioned in the Strategy section above, the Bank intends to achieve its emissions reductions targets by increasing its exposure to customers with clear transition strategies and projects aligned to a net zero economy for the future. The Bank also intends to increase engagement with clients with insufficient transition plans with the goal of providing financing needed to implement lower emissions business models, and ultimately, to limit exposure to customers or projects not on a similar trajectory to SMBC Group through lending policy.

The Bank is taking steps to control its financed emissions and new guidelines will be implemented for originating business with clients in scope of financed emissions calculations, with the aim of originating business with clients that have adequate transition plans. By steering the portfolio towards clients with good transition plans that will make real-world emissions reductions, the Bank intends to reduce its financed emissions based on real-world emissions reductions rather than simply on the transfer of polluting assets from one owner to another.

The Bank will expand the scope of sectors for which it calculates financed emissions and will set interim targets to align with net zero.

Sector	Target	FY2022			FY2021		
		Total outstanding (USDm)	**Financed emissions**	**PCAF data quality score**	Total outstanding (USDm)	Financed emissions	PCAF data quality score
Oil & Gas	Reduce by 12 – 29% by 2030*	**149**	**0.15 $MtCO_2e$**	**4.62 Scope 1-2 4.52 Scope 3**	262	0.84 $MtCO_2e$	4.29 Scope 1-2 4.29 Scope 3
Power	138 - 195 gCO_2e/kWH by 2030*	**1,000****	**191 gCO_2e/kWH**	**2.84 Scope 1**	900***	111 gCO_2e/kWH	2.98 Scope 1

* SMBC Group-level target
** This total outstanding excludes USD 181m due to insufficient data (FY2022)
*** This total outstanding excludes USD 421m due to insufficient data (FY2021)

Climate change risk assessment

As described in the Risk Management section, the Bank identifies, monitors, measures, manages and reports climate-related risks by conducting its Climate Change Ratings Assessment (CCRA) on a client-by-client basis. To measure whether the Bank is achieving its ambition to embed sustainability risk management in all aspects of its business, the metric % of clients assessed for climate change risk is used. This is the % of clients for which CCRA has been completed out of the total number of clients in scope of CCRA.

Exposure to carbon-related sectors

The Bank measures exposure to sectors defined as carbon-related, as it can be used as a proxy for climate transition risk.

Companies operating in carbon-intensive sectors have a greater reliance on carbon-based energy; therefore, they would be expected to be faced with greater transition risks and uncertainties as the economy is transitioning from carbon-based energy to lower carbon energy. However, this is a blunt metric used as a proxy for transition risk. For example, included in the exposure to carbon-related sectors is green and sustainable finance extended to clients in hard-to-abate sectors. The Bank will continue to evolve its understanding and differentiation of exposure to these sectors.

Exposure to carbon-related sectors is measured separately to general sector limits that the Bank maintains to control credit risk more generally.

Presented below is the Bank's exposure to carbon-related sectors, broken down by sector in accordance with the Task Force on Climate-related Financial Disclosures definition.

Carbon-related assets with sector breakdown	FY2022			FY2021		
	Loans and advances to customers (USDm)	Commitments and guarantees (USDm)	Total (USDm)	Loans and advances to customers (USDm)	Commitments and guarantees (USDm)	Total (USDm)
Energy	**2,227**	**4,445**	**6,672**	2,833	5,478	8,311
Transport	**2,300**	**1,074**	**3,374**	2,789	1,115	3,904
Materials and Buildings	**4,641**	**4,002**	**8,643**	3,929	3,990	7,919
Agriculture, Food and Forest Products	**296**	**682**	**978**	888	752	1,640
Carbon-related Assets Grand Total	**9,464**	**10,203**	**19,668**	10,440	11,335	21,775
Total Loans and Advances, and Commitments and guarantees	**17,713**	**16,192**	**33,905**	19,943	18,608	38,551
Carbon-related assets / Total Loans and Advances, and Commitments and guarantees	**53%**	**63%**	**58%**	52%	61%	56%

The total exposure levels shown are for the Bank only and include on-balance and off-balance exposure. The sectors subject to evaluation were extracted as per the definition of carbon-related assets in the supplementary guidance of the TCFD recommendations. This is presented differently from the SMBC Group calculation. SMBC Group reports carbon-related assets exposure as a percentage of leverage ratio total exposure while the Bank uses Total Loans and Advances to customers and Commitments and guarantees in order to align to the financial section of this annual report.

Governance at a glance

Governance

The Board of Directors

The Directors who were in office and the composition of the Board Committees at 31 March 2023 are shown below. Since the year-end, Keiichiro Nakamura has left the Board and Sophie O' Connor has been appointed to the Board.

Name	Board of Directors	Committees: Audit	Nomination	Remuneration	Risk	Executive
Non-executive Directors						
Alan Keir	C	–	C	C	M	–
Kazuya Ikeda	M	–	–	M	M	–
Patricia Jackson	M	M	M	M	C	–
Keith Macdonald	M	M	M	M	M	–
Charlotte Morgan	M	C	M	M	M	–
Executive Directors						
Hideo Kawafune	M	–	–	–	–	C
James Fenner	M	–	–	–	–	M
Nobuyuki Takiguchi	M	–	–	–	–	M
Former Director						
Keiichiro Nakamura (resigned 4 April 2023)	M	–	–	–	–	C
Appointed after the year-end						
Sophie O'Connor (appointed 31 May 2023)	M	M	M	M	M	–

C Chair of Board or Committee

M Member of Board or Committee

+ On the invitation of the respective Chairs, members of the Board and management team also attend meetings, further details on which are shown on **pages 62 to 68**.

Board Committees

The Board Committees provide oversight of, and make recommendations on, the matters delegated to them by the Board.

Board of Directors
+ See pages 41 to 43 for more information

Audit Committee
+ See pages 62 and 63

Nomination Committee
+ See page 65

Remuneration Committee
+ See page 66

Risk Committee
+ See page 67

Executive Committee
+ See page 68

Disclosures Committee
+ See page 64

Further information

- Information on how the Board and its Committees and management have engaged with stakeholders can be found on **pages 54 to 59**.
- Information on the activities of the Board and Committees in the year can be found as shown above and in the Sustainability section on **page 22**.

The Board of Directors

Alan Keir

Chair

Appointed to the Board:
12 October 2016
Appointed as Chair: 1 January 2022

Skills and experience

In his executive career Alan held a number of leadership positions at HSBC, including Group Managing Director of HSBC Holdings plc from 2011 until his retirement in 2016. Alan has considerable experience in many aspects of corporate, investment and retail banking, including strategy, risk management and governance. He is also experienced in retail services and commercial property.

Other appointments

Non-executive Director and Chair of the Audit and Risk Committee of Majid Al Futtaim Holding LLC, a non-executive Director of Majid Al Futtaim Trust LLC and a non-executive Director and Chair of the Risk Committee of Nationwide Building Society.

Hideo Kawafune

Chief Executive Officer

Appointed to the Board:
3 April 2018
Appointed as CEO: 4 April 2023

Skills and experience

Alongside his role as CEO, Hideo is also Managing Executive Officer and Head of EMEA Division of SMFG and SMBC. Prior to his appointment as CEO, he was Deputy CEO with responsibility for overseeing internal controls and governance. He was the Bank's Chief Operating Officer between 2018 and 2021 with responsibility for corporate planning, human resources and financial reporting matters. Hideo's previous experience includes international assignments in strategic and business planning, risk management and business promotion.

Other appointments

A non-executive Director of SMBC Nikko CM. He is also Chair of the Supervisory Board of Shimano Europe B.V.

James Fenner

Deputy Chief Executive Officer

Appointed to the Board:
2 February 2022

Skills and experience

James has responsibility for coordinating leveraged buyout, structured products and investor businesses. He is also an Executive Officer of SMBC and Deputy Head of the EMEA Division of SMBC. Before taking his current role, James was the General Manager responsible for Specialised Products, which includes leveraged buyout, securitisation, subscription finance and real estate financing. James has significant senior-level experience in leveraged and loan capital markets in investment banking and was previously Chief Executive Officer at a corporate bank, giving him experience in areas including financial and risk management and strategic planning.

Other appointments

None.

Kazuya Ikeda

Non-executive Director

Appointed to the Board:
1 June 2022

Skills and experience

Kazuya is a Managing Executive Officer of SMFG and SMBC and General Manager of SMFG's Strategic Planning Department, Global Business Unit and SMBC's Strategic Planning Department, Global Banking Unit. He has extensive business and strategic planning experience gained from various assignments in Tokyo and Singapore.

Other appointments

None.

Patricia Jackson

Independent non-executive Director

Appointed to the Board:
1 January 2022

Skills and experience

Patricia has considerable experience as a non-executive director. She is the non-executive chair of SMBC Nikko CM and has chaired the risk committees of a variety of financial institutions, including Lloyd's of London. She built up the banking risk practice at EY and was head of the risk governance practice for Europe, the Middle East, India and Africa. At the Bank of England, she was the head of the Financial Industry and Regulation Division and represented the UK on the Basel Committee for Banking Supervision. Patricia has extensive knowledge of banking, capital markets, risk management and regulation.

Other appointments

Chair of the Board of SMBC Nikko CM and a non-executive director of Handelsbanken PLC.

Keith Macdonald

Independent non-executive Director

Appointed to the Board:
12 October 2022

Skills and experience

Keith left Standard Chartered in 2021 having most recently been the chief operating officer for corporate, commercial and institutional banking. He has significant technology experience gained through leadership roles at Standard Chartered and Bear Stearns and through the establishment of his own technology businesses. He also has significant experience in business operations and finance.

Other appointments

A director of Circularity.IO Limited, a digital advertising company of which he is co-founder.

The Board of Directors continued

Charlotte Morgan

Independent non-executive Director

Appointed to the Board:
1 September 2017

Skills and experience

Charlotte is a Chartered Accountant and Corporate Treasurer. Her executive career included Standard Chartered Group, where she was Head of Corporate Treasury and Tax, and finance roles in a range of banking and financial services businesses. Charlotte has been a non-executive director of FCE Bank PLC and Vice-President of the Association of Corporate Treasurers, where she is currently a member of the Policy and Technical Panel.

Other appointments

Charlotte is a non-executive director and Chair of the Audit Committees of UK Export Finance and Union Bank of India (UK) Limited, a Governor of the University of Westminster and a trustee of the classical music charities London Sinfonietta and Second Movement.

Sophie O’Connor

Independent non-executive Director

Appointed to the Board:
31 May 2023

Skills and experience

After qualifying as a Chartered Accountant, Sophie held a variety of roles at Bank of America Merrill Lynch where she gained experience of finance, risk management and operations, through chief finance officer and chief operating officer roles of businesses in the UK and US. She is now an experienced financial services non-executive Director who has chaired the audit committee of a number of significant financial services firms.

Other appointments

Non-executive Chair of Embark Group Limited, non-executive director and Chair of the Audit Committee of Scottish Widows Limited and Senior Independent Director and Chair of the Risk Committee of BUPA Insurance Limited. She is also a trustee of the charity Chance to Shine.

Nobuyuki Takiguchi

Chief Operating Officer

Appointed to the Board:
11 April 2022

Skills and experience

Nobuyuki has responsibility for corporate planning, human resources, financial reporting, project management and information technology matters. The majority of Nobuyuki’s career has been spent in the UK where he has held roles in operations, strategic planning and information technology. He is an Executive Officer of SMBC.

Other appointments

A non-executive director of the SMBC Group companies, JRI Europe Limited, SMBC Advisory Services Saudi Arabia and Sumitomo Mitsui Finance Dublin Limited.

Statement of Corporate Governance arrangements

The Board is committed to maintaining high standards of corporate governance within the Bank.

For the year ended 31 March 2023, the Board has applied the Wates Corporate Governance Principles for Large Private Companies (Wates Principles) and information on how it has done so is set out in the following pages.

Principle 1
Purpose and leadership

"An effective board develops and promotes the purpose of a company, and ensures that its values, strategy and culture align with that purpose."

The Bank's purpose is to be "a trusted partner for the long term". This reflects the long-term relationship-based approach the Bank adopts in carrying out its business for the benefit of its stakeholders:

- **"Trust"** is a cornerstone of the Bank's offering and identity.
- **"Partner"** and **"partnership"** are words frequently used in the Bank and wider SMBC Group as they emphasise the two-way, win-win nature of what the Bank regards as a successful relationship.
- **"Long term"** is associated with trust, partnership and stability. Having a long-term view and thinking of relationships as long-term associations is central to the Bank's business activities.

The Bank's purpose, values and culture form a framework that helps guide corporate and individual behaviours. On joining the Bank, employees are made aware of this framework through the Employee Handbook, with further resources available on the intranet.

During the year, the Board enhanced the way it considers the linkage between strategy, the business and purpose by requiring executives to explain how items submitted to the Board for approval relate to and are consistent with the Bank's purpose.

+ Mission, Vision and Values **page 7**.

+ Culture and developments in the year **page 18**.

Statement of Corporate Governance arrangements continued

Principle 2
Board composition

"Effective board composition requires an effective chair and a balance of skills, backgrounds, experience and knowledge, with individual directors having sufficient capacity to make a valuable contribution. The size of a board should be guided by the scale and complexity of the company."

Board composition and diversity

At the date of signing the financial statements, the Board comprised nine Directors. The non-executive Directors Alan Keir, Charlotte Morgan, Keith Macdonald, Patricia Jackson and Sophie O'Connor are deemed independent as they have no material business or other relationships with the Bank that could influence their exercise of independent judgement. Kazuya Ikeda is nominated by the Bank's shareholder and is not deemed independent.

The Board includes a separate Chair and CEO to ensure a clear division of responsibilities between the leadership of the Board and the executive leadership of the business. The CEO is assisted in his role by the other executive Directors and the senior management team, and through the work of the Executive Committee.

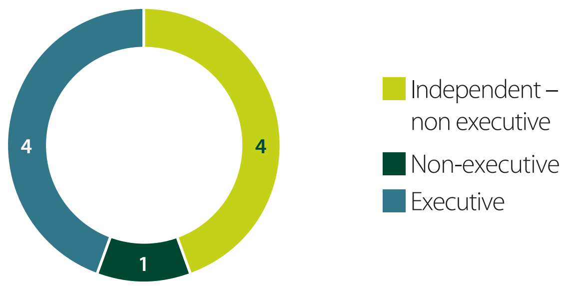
The overall size and composition of the Board is assessed by the Nomination Committee, and this is informed through ongoing skills and effectiveness assessments.

The Board has in place a Diversity Policy which states a target that at least 25% of the Board will be made up of women, while also ensuring an appropriate mix of skills, experience and competencies on the Board. The Board also commits to taking positive action to source applications from Asian, Black and other Minority Ethnic candidates. At the year-end, the Board did not meet its gender target as female Directors represented 22% (two out of nine Directors) of the Board. Due to changes in the composition of the Board after the year-end, at the date of signing the financial statements, female Directors represented 33% of the Directors (three out of nine Directors).

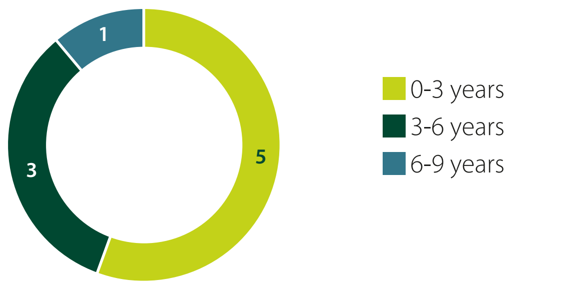
Board composition at the year-end

Gender diversity

Types of Director



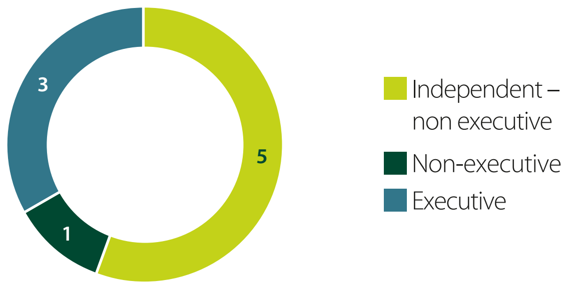
Length of service



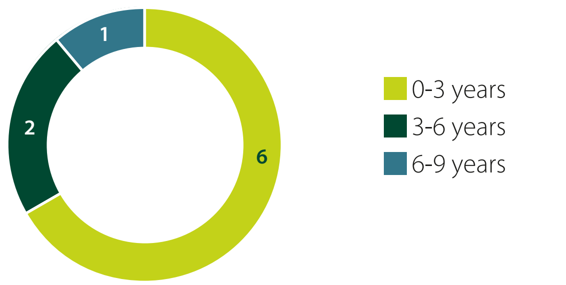
Board composition at the date of signing the financial statements

Gender diversity

Types of Director



Length of service



The level of Board diversity has been an area of focus for the Nomination Committee in the year, and this has been a key consideration in the discussions on Director succession planning. The Nomination Committee has also been briefed on regulatory and other developments in respect of Board and senior management diversity, and is keeping its diversity target under review.

Board appointments

The Nomination Committee is responsible for assessing and recommending Director candidates to the Board for approval. As part of this process, the Committee considers a candidate's skills, experience and values, and has regard to the level of diversity and experience and main areas of competency of the Board.

Recent Board skills and effectiveness assessments had highlighted that the Board would benefit from greater expertise in information technology and operations management. During the year, the Bank engaged a search firm to identify a non-executive Director who could bring these attributes to the Board. Following review of a diverse list of candidates and subsequent interviews, on the recommendation of the Nomination Committee, the Board approved the appointment of Keith Macdonald as a Director.

Also during the year, the Nomination Committee and Board approved the appointment of Hideo Kawafune as CEO, following the reassignment of Keiichiro Nakamura to another role within SMBC Group. Hideo was appointed CEO on 4 April 2023, having held the position of Deputy CEO during the year.

Subsequent to the year-end, the Board appointed Sophie O'Connor as a Director. Sophie's appointment reflected the Nomination Committee's objective to develop succession options amongst the non-executive Directors. The process for Sophie's appointment was the same as that followed for Keith as described above.

Statement of Corporate Governance arrangements continued

Principle 2 continued
Board composition

Responsibilities of the Board and Committee Chairs

The Board and Committee Chairs are responsible for ensuring that meeting activities are undertaken in accordance with the applicable terms of reference. They are expected to take a strategic view in agenda-setting. The Chairs also have specific responsibilities as shown below:

Responsibility	How achieved
Ensuring that meeting members operate effectively as a team and that debate is encouraged and facilitated, whilst achieving closure of items.	– Assessed through effectiveness reviews and steps taken to address points identified. – Board members meet each other outside formal meetings and there is frequent additional contact between them. – Chairs and Company Secretary discuss who should attend meetings to ensure appropriate consideration of items. – All matters arising from meetings are recorded and tracked to completion.
Ensuring appropriate time is allocated for the consideration of items.	– Meeting agendas are set by the respective Chair in consultation with the Company Secretary. – Agendas and meeting arrangements are structured to allow sufficient time for discussion of all matters, with a focus on those items requiring approval or strategic consideration. – Agenda setting is aided by a forward planner which is updated regularly to reflect the requirements and areas of focus of the Board and Committees.
Ensuring that members have sufficient time to consider critical issues, obtain answers to questions or concerns and are not faced with unrealistic deadlines for decision-making.	– Meeting papers are circulated to Directors as far in advance of meetings as possible and, typically, at least one week before a meeting.
Ensuring that the meeting receives clear, accurate and timely information.	– Meetings are arranged to allow inclusion of the most recent month-end data in papers. – Guidance documentation issued by the Company Secretariat to assist management in the preparation of papers.

Effectiveness

A review of the effectiveness of the Board and the Audit, Risk and Remuneration Committees was performed in the year by Independent Audit Limited, an independent third party. The scope of this review included assessment of meeting composition, how stakeholder interests, people and culture matters are considered, and the provision of information and support to the Board and Committees. The review identified many areas of strength where the Board and its Committees were functioning well, for instance, in the working relationship with SMBC Group and the quality of Board and Committee papers, and it was believed these attributes give the Board a strong foundation now and for the future.

Suggestions for future improvement were also identified, with the key themes being as follows:

On behalf of the Board, the Nomination Committee reviewed the action plans put in place to address the points identified and had ongoing oversight of the progress in implementing the plans. The progress made to embed the improvements will be assessed through the internal effectiveness review to be undertaken in 2023. This opportunity will also be taken to seek the Directors' views on any other areas where effectiveness can be enhanced.

Themes	Action taken
Meeting papers and presentations	– The Company Secretary sought the views of the independent non-executive Directors on the style of presentations given to the Board and its Committees. Updated guidance was subsequently provided to executives on the preparation of meeting materials. Further consideration will be given to the style of verbal presentations made at meetings.
Methods of stakeholder engagement	– Provision of further opportunities for the Board to engage directly with employees, including advising the independent non-executives of all relevant employee-led events.
Board education	– Inclusion on the Board education plan of legal and regulatory developments relating to Directors' duties and obligations.

Statement of Corporate Governance arrangements continued

Principle 3
Director responsibilities

"The board and individual directors should have a clear understanding of their accountability and responsibilities. The board's policies and procedures should support effective decision-making and independent challenge."

Board and Committees

The Chair of each Committee provides a report on the Committee's activities to the Board. The responsibilities of the Board and Committees are detailed in terms of reference, which are reviewed regularly and updated as required. The Board is responsible for appointing the Board Chair and the Chairs of all Board Committees. The membership of the Audit, Remuneration, Risk and Nomination Committees is also reserved for the Board in consultation with the relevant Committee Chair. The members of the Executive Committee are determined by the CEO. An overview of the matters considered by the Board Committees in the year can be found on **pages 62 to 68**.

Accountability

The Directors each have in place an annually reviewed role description document and, as required by the Senior Managers Regime, a Statement of Responsibilities. These documents are supported by a Board approved corporate governance document giving further information on the roles and responsibilities of the Directors, summarised in the table below:

Role	Responsibility	How achieved
Non-executive Directors	– Provision of independent judgement on all matters related to the Bank's strategic direction, leadership, performance, resources, risk management and overall governance. – Independent directors are required to constructively challenge and test strategic proposals.	– Annual checks undertaken to assess independence (see below). – The strategic planning and development process takes place throughout the year and is subject to quarterly Board discussion.
Executive Directors	– Under the leadership of the CEO, responsibility for running the business. – Implementing the strategies approved by the Board. – Ensuring the Board's decisions are implemented appropriately.	– Board approved strategy and policies provide a framework for managing the business. – CEO report submitted quarterly to the Board. – Framework of management reporting to the CEO. – Departmental reports considered monthly by Executive Committee. – Escalations Document in place identifying certain events which, should they occur, require immediate notification to one or more Board or Committee Chairs then the Board as a whole. This Document was updated regularly in the year to reflect business developments and specific requests from the Board and Committees.

Role	Responsibility	How achieved
	– To be knowledgeable about all aspects of the business even if they have responsibility for a particular area of the business.	– All new Directors are given a personalised learning and development plan. – Ongoing learning needs are identified through annual effectiveness reviews. This is supplemented by briefings given as part of the Board education plan. – All executive Directors are a member of the Executive Committee at which Bank-wide matters are considered.

Independence

All Directors are required annually to complete a questionnaire through which any potential conflicts of interest are identified. The non-executive Directors are required to seek the approval of the Bank and SMBC in advance of them being appointed a director of any other company so that any potential conflicts of interest with the Bank can be identified and, as necessary, managed.

Integrity of information

Multiple systems capture, record, process and store the financial and non-financial information used for Board, Committee and corporate reporting. The Bank continually enhances its controls over these systems to ensure accuracy is maintained and to improve simplicity and transparency. The data used for reporting is subject to internal and external audit review and, as deemed necessary, external assurance review. During the year, the Audit Committee received quarterly reports on the effectiveness of the Bank's internal financial controls.

External audit arrangements

The Audit Committee is responsible for managing the Bank's relationship with its external auditor, ensuring that at least every 10 years the external audit will be considered for re-tender. Each year, the Audit Committee reviews a letter from the external auditor setting out how, in its view, its objectivity and independence is maintained. The Audit Committee has approved a policy setting out the criteria and process of approval to be followed for the provision by the auditor of non-audit services. This policy was updated in the year to reflect new international requirements on the provision of such services.
The Audit Committee members regularly meet the KPMG Audit partner in the absence of executive management.

Audit and Assurance Policy

During the year, the Audit Committee reviewed a draft Audit and Assurance Policy, which documents how the Board obtains assurance on any company reporting beyond that provided by the annual audit of the financial statements. This Policy was approved by the Audit Committee after the year-end. The Policy has been prepared in response to the Government White Paper 'Restoring Trust in Audit and Corporate Governance' and its subsequent publications.

Statement of Corporate Governance arrangements continued

Principle 4
Opportunity and risk

"A board should promote the long-term sustainable success of the company by identifying opportunities to create and preserve value, and establishing oversight for the identification and mitigation of risks."

Further information

+ Classification of risks – **page 12**.
+ Principal and emerging risks – **pages 13 to 15**.
+ Oversight of sustainability targets and risk management – **pages 30 to 38**.
+ Identification and management of risk – Risk Management section starting on **page 73**.

Opportunity

Medium- and long-term strategic opportunities are identified through the annual Corporate Strategy development process, which in the year has involved:

- consideration by the Board of high level strategic principles, including those of SMBC Group;
- a strategy discussion meeting involving the Boards and senior executives of the Bank and SMBC Nikko CM; and
- review and challenge of the draft and final strategy document

The Chief Executive Officer and Chief Operating Officer report quarterly to the Board on strategic and business developments and are accountable to the Board for the delivery of the strategy. They are supported in this through a half-yearly senior executive management conference where strategy is discussed at a departmental level and on specific areas of business focus. Any expansion of the business into new areas or the identification of short-term strategic opportunities are considered in conjunction with risk appetite and discussed by the Board.

Risk

The Board is responsible for establishing a framework of controls that enables risk to be managed and assessed, and sets the Risk Appetite Statement each year. It delegates certain of these responsibilities to the Risk and Audit Committees as set out below:

On the basis of the activities performed by the Risk Committee and Audit Committee in the year, the Board considers the Bank's risk management and internal control systems to be appropriate. These systems are designed to identify, evaluate and manage, rather than eliminate, all of the Bank's risks and can only provide reasonable and not absolute assurance against material misstatement or loss.

Committee	Ongoing responsibilities and activities undertaken	Specific reviews at the year-end
Risk Committee	– Assessing effectiveness of risk management and internal controls. – Reviewing the status of risk against Appetite. – Reviewing the results and management's response to the Compliance Monitoring Programme review activity which provides assurance on compliance with relevant laws, regulations, policies and procedures. – Deep-dive reviews into areas of focus. In the year, these have included cyber risk, cross-border marketing Risk Appetite Framework and KYC monitoring findings.	– Effectiveness of the risk management framework and internal controls at the year-end through which the Committee considered the results of a management assessment and attestation process of the key risks facing the Bank, along with the related key controls. The Committee concluded that the framework was adequate and that management had taken or was taking the necessary actions to remedy any weaknesses identified in the framework of controls.
Audit Committee	– Assessing effectiveness of internal financial controls. – Considering the results of Internal Audits, which address the design and implementation of key controls used to manage risks across the organisation. Monitoring is also performed of actions taken to address audit issues to confirm appropriate improvements are implemented. – Considering the results of external audit findings. – Reviewing whistleblowing trends, which offer insights into possible risk areas.	– Effectiveness of the internal controls over financial reporting at the year-end. All controls were assessed as either satisfactory or partially satisfactory, with action plans in place to improve the latter.

Statement of Corporate Governance arrangements continued

Principle 5
Remuneration

"A board should promote executive remuneration structures aligned to the sustainable long-term success of a company, taking into account pay and conditions elsewhere in the company."

The Remuneration Committee's responsibilities include overseeing the development and implementation of the Bank's remuneration policies and practices. Information on the activities undertaken by the Committee in the year can be found on **page 66**.

The Bank's approach to fixed and variable rewards is set out in a Remuneration Policy, an updated version of which was approved by the Remuneration Committee and Board in the year. With limited exceptions, this Policy does not apply to employees of SMBC seconded to the Bank, the remuneration of whom is governed by rules established by SMBC in Japan.

The Policy aims to support the Bank's long-term aims and seeks to encourage long-term stability and sustainability, particularly of the capital base, and promote steady growth and keen risk awareness. All employees are eligible to participate in the annual performance-related bonus scheme, with variable pay outcomes determined by the performance of the Bank and relevant department, and both the contribution and conduct of the employee.

In the year, the performance of the most senior individuals was assessed using a balanced scorecard to drive sustainable business performance. The scorecards included financial goals, non-financial goals linked to the Bank's five cultural pillars (including ESG targets), as well as an assessment of the individual's conduct. The Risk Committee also assessed the risk adjustments inherent within the overall bonus pool calculation to ensure these took suitable account of the Bank's performance in the year and the current and future risk environment. In addition, the Remuneration Committee reviewed and approved the variable and salary awards made to all material risk takers.

The Remuneration Committee also supported in the year the provision of an exceptional salary adjustment of £2,000 (or equivalent local currency) to the Bank's Associate and Assistant Vice President employee population. This was to recognise the particular cost-of-living challenges the current inflationary environment has posed for the Bank's more junior employees and to ensure that the Bank continues to provide a competitive level of reward to its people that fairly recognises the contribution they make to the Bank's success.

Principle 6
Stakeholder relationships and engagement

"Directors should foster effective stakeholder relationships aligned to the company's purpose. The board is responsible for overseeing meaningful engagement with stakeholders, including the workforce, and having regard to their views when taking decisions."

The Board and management recognise the need to engage with the Bank's stakeholders and to consider their interests, and information on the ways in which they have done so is set out on **pages 54 to 59**.

Section 172(1) Statement

Section 172(1) of the Companies Act 2006 requires company directors to act in the way they consider, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard to the:

(a) likely consequences of any decision in the long term
(b) interests of employees
(c) need to foster business relationships with suppliers, customers and others
(d) impact of the company's operations on the community and the environment
(e) desirability of the company maintaining a reputation for high standards of business conduct
(f) need to act fairly as between members of the company

This section describes how in the year the Directors have had regard to the above matters (the section 172(1) matters) when performing their duty under section 172(1) and forms the statement required under section 414CZA of the Companies Act 2006. Given the Bank is a wholly-owned subsidiary, the need to act fairly as between members of the company is less relevant to the Directors' discussions than the other section 172(1) matters.

Stakeholders – overview

The Bank's key stakeholders are those groups that most materially impact the Bank's strategy or are impacted by it and are:

- **Customers**
- **Environment and community**
- **Colleagues**
- **Suppliers**
- **Regulators**
- **SMBC Group**

During the year, the Board confirmed that the Bank's identified stakeholder groups remained current and appropriate, subject to minor changes to the descriptions used.

The Board recognises that the Bank's success is dependent on its stakeholders and that its activities impact its stakeholders in different ways. When presenting to the Board and its Committees, members of management are required to identify in supporting documentation the stakeholder groups and section 172(1) matters relevant to the item, which are then considered by the Directors in their discussions and decision-making.

High standards of business conduct

The Board recognises the need for the Bank to exercise high standards of business conduct. Oversight of conduct is primarily through the Risk and Executive Committees and information on how they do so is set out in the Sustainability section on **pages 21 to 29**.

Section 172(1) Statement continued

A long term view

In the year, the Board approved the Corporate Strategy, ICAAP document and Internal Liquidity Adequacy Assessment Process (ILAAP) document, all of which are prepared on a three-year time horizon. The Chief Risk Officer also reported to the Board on the extent to which the risks inherent within the Strategy were consistent with the Board approved risk appetite.

Stakeholder engagement

The Board delegates to management the authority to run the business on a day-to-day basis and to execute the strategy approved by the Board. The Bank therefore engages with stakeholders in many ways and at all levels of the business to understand their needs, priorities and concerns. These interactions take place in the context of the strategies and policies set by the Board and its Committees, and significant interactions are reported as necessary to those meetings. The Board also actively seeks opportunities to engage directly with stakeholders. Set out below are examples of what engagement has occurred in the year and the impact of that engagement.

Customers

'Customer first' is one of the Bank's core values and it seeks to build its brand by being a reliable and trusted partner to its customers.

Interaction with customers is primarily through relationship managers and product specialists, but the CEO and other members of the Executive Committee also regularly meet customers to develop strategic partnerships. Significant interactions and notable transactions are reported to the Board as required.

The Bank frequently hosts customer seminars and seeks to provide value-added services, such as the provision of training to customers on anti-financial crime measures and development opportunities through the Future Treasury Leaders series.

During the year, the Bank continued to implement enhanced processes and organisational structures with the aim of improving the customer experience. An area of focus has been the way in which the Bank requests and collates KYC onboarding information.

A further area of focus in the year has been to work with customers on the transitioning of remaining legacy transactions referencing synthetic GBP LIBOR ahead of the discontinuation of 1-month and 6-month synthetic GBP LIBOR settings on 31 March 2023, and preparations for the discontinuation of the relevant USD LIBOR settings on 30 June 2023 (and which will be subject to a further synthetic USD publication period until 30 September 2024). The Bank has worked closely with its customers with the objective of taking a proactive and leading role across lender syndicates and project finance industry associations to drive the transition from LIBOR to risk-free rates. A communications plan was put in place to notify impacted clients of the implications of non-transition, with additional focused communications for any deals identified to be at high risk of non-transition.

To supplement this exercise, comprehensive training has been provided to each front office and relevant supporting departments to facilitate their discussions with customers and other stakeholders. For those deals where the Bank is driving LIBOR transition (bilateral loans and syndicated deals where the Bank is Agent), the Bank has sought to proactively collaborate with relevant customers and stakeholders, and continues to target the transition of all legacy deals ahead of the USD LIBOR discontinuation deadline. The Bank has also engaged with customers, syndicate finance parties and other stakeholders to transition the small amount of remaining synthetic GBP LIBOR transactions.

Environment and community

The Bank recognises the importance of working towards building and sustaining a better world.

+ The Board and Committees, supported by the EMEA Sustainability Programme, have been actively engaged in overseeing and developing the Bank's sustainability capabilities in the year. Further information on this can be found on **pages 21 to 29**.

The Bank's intranet contains briefing materials for front office colleagues on how they can best support the Bank's customers to reduce their environmental impact and information on the steps being taken by the Bank to operate more sustainably. Townhalls and other briefings have also been held in the year, such as the Annual Sustainability Week in November 2022 which included events to increase employees' awareness on topics including sustainable finance products, ESG threats and opportunities, the energy efficiency of the Bank's headquarters building and personal actions to increase sustainability.

In the year, the Board considered the results of a CSR survey through which it was able to understand what colleagues around the Bank regarded as important to develop the Bank's approach to CSR. These views were incorporated into the new Board-supported CSR strategy.

+ Further information on the CSR Strategy can be found on **page 29**.

Colleagues

The Bank regards its people as its key asset and recognises they are central to the Bank achieving its sustainable growth objective.

The Board seeks feedback from colleagues in a combination of ways, including through direct engagement and the results of employee surveys.

Areas of focus for the Board and the Nomination Committee in the year have included diversity and inclusion, talent management and career progression. Each quarter, the Board met representatives of the DRIVE employee diversity networks to discuss areas of activity and focus for that network. The Board has followed up these discussions with additional agenda items to consider the development and results of the networks' activities. Insights into talent management and career progression were provided to the Board from a meeting with female managing directors. Additional insights have been provided through individual briefing meetings with non-executive Directors and presentations from the participants on the senior leadership development programme.

Direct interactions have been complemented by the Nomination's Committee review of the feedback of employee surveys and focus groups. Also in the year, the Board participated in a facilitated discussion on regulatory developments in respect of diversity and inclusion, and the role of boards and senior leaders in progressing cultural change. Reflecting this focus, during the year, the Executive Committee mandated the holding of new senior-level forums to discuss methods to increase senior female representation in the Bank.

The results of these interactions are being used by the Bank to inform its approach to talent management and employee mobility, and this is being overseen by the Nomination Committee.

In addition to attending Board events, Directors have participated in events at individual department level, such as conferences, and for the Bank as a whole, such as those arranged by the DRIVE groups.

Section 172(1) Statement continued

Colleagues continued

Other notable engagement with employees in the year included:

- Weekly emails from the CEO and townhall meetings with senior executives providing updates on business matters.
- Mental Health Awareness Week in May 2022 through which daily briefings were issued and webinars held on different aspects of mental health.
- Annual Inclusion Week in September 2022 with the objective of enabling employees to identify and embed actions to promote diversity and inclusion in the Bank.
- A series of events was held in November and December 2022 to mark the UN International Day of Persons with Disabilities to help raise awareness of and celebrate those employees with mental health challenges, neurodiversity, and visible and invisible disabilities.
- The Intranet was used to explain strategic and business initiatives, and provide updates on business projects and employee voice stories on matters important to individuals.

Suppliers

The Bank relies upon external suppliers to provide certain products or services that assist it in the running of its business. Suppliers are engaged for a variety of reasons, including the provision of expertise or resource that the Bank may or may not possess itself.

Engagement with suppliers is coordinated through a dedicated team and with executives who require supplier services. A procurement process is in place for all supplier engagements, which includes a rigorous due diligence process. These checks include steps relating to compliance with laws and regulations, such as anti-bribery and corruption and modern slavery, and cost efficiency. Ongoing monitoring of suppliers is also undertaken. Particular focus is given to relationships with outsourcing providers and such engagements are subject to the Bank's third party risk management framework. Any critical outsourcing requires the approval of the Operational & General Risk Committee.

During the year, the Bank paid 59% (FY2021: 76%) of its invoices within 30 days, with the average being payment within 39 days (FY2021: 29 days).

Given some deterioration in the payment periods was experienced during the year, the Executive Committee and Board reviewed the process to understand the root cause and the remedial steps being taken to address this. The Bank's response has included short-term actions, such as process changes to improve payment performance and long-term actions to maintain improvements. The Bank sought to engage closely with its vendors as it made these enhancements in the year.

Reflecting developing regulatory expectations, the Bank is enhancing its third party risk management framework in order to increase efficiencies and implement a new target operating model (TOM) for third party management. The Risk Committee continues to regularly monitor the progress in implementing the TOM and the linkage this has in other matters under its consideration, such as operational and cyber resilience.

Regulators

The Bank is required to comply with its regulators' rules and to ensure the integrity of the financial markets in which it operates. The Board recognises that failure to comply with these requirements will impact the Bank's ability to carry out its business and serve its customers.

During the year, individual Directors and members of the Executive Committee met the PRA and FCA at annual strategy, continuous assessment and other meetings. The Board and Committees have also received regular reports on significant regulatory matters, such as new regulation and Dear CEO and CFO letters, and overseen the Bank's response on matters including the annual evaluation letters, the evolving sanctions environment and USD LIBOR transition. At an executive level, the Bank has established a public affairs function to ensure it is aware of and engages on regulatory and industry change that may impact the Bank's business and that of its stakeholders.

SMBC Group

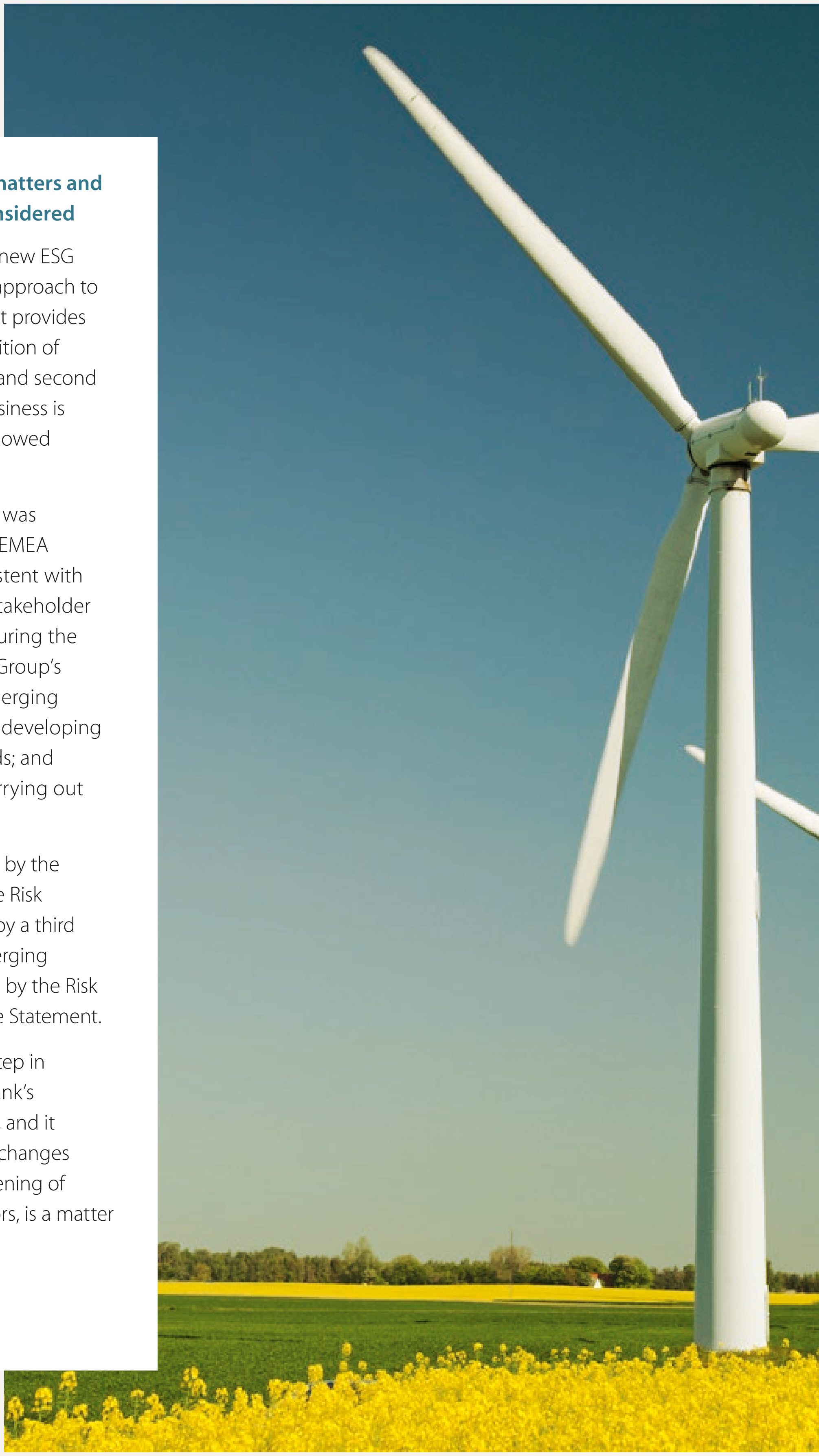
The Bank recognises the importance of the role it plays to further the Mission and Vision of SMBC Group, particularly through the expansion of the Group's franchise in EMEA and provision of services to a number of SMBC Group companies in EMEA. The Bank has therefore identified SMBC Group as a key stakeholder.

The Bank engages closely with SMBC and Group affiliated companies at all levels. A representative of the shareholder, Kazuya Ikeda, is appointed to the Board and, during the year, provided quarterly updates on SMBC Group strategy and significant business developments. He has also acted as a link between the Board and SMBC Group on matters requiring Group input.

The independent non-executive Directors regularly met senior executives of SMBC Group, including the Group President, Co-Head of Global Business Unit and members of the Audit and Supervisory Committee.

During the year, a senior-level forum, attended by the Board Chairs and CEOs of the Bank and SMBC Nikko CM, and the CEO of SMBC Bank EU, was established to further enhance the coordination of business activities and other strategic matters between those companies.

Section 172(1) Statement continued



Example of how the section 172(1) matters and stakeholder interests have been considered

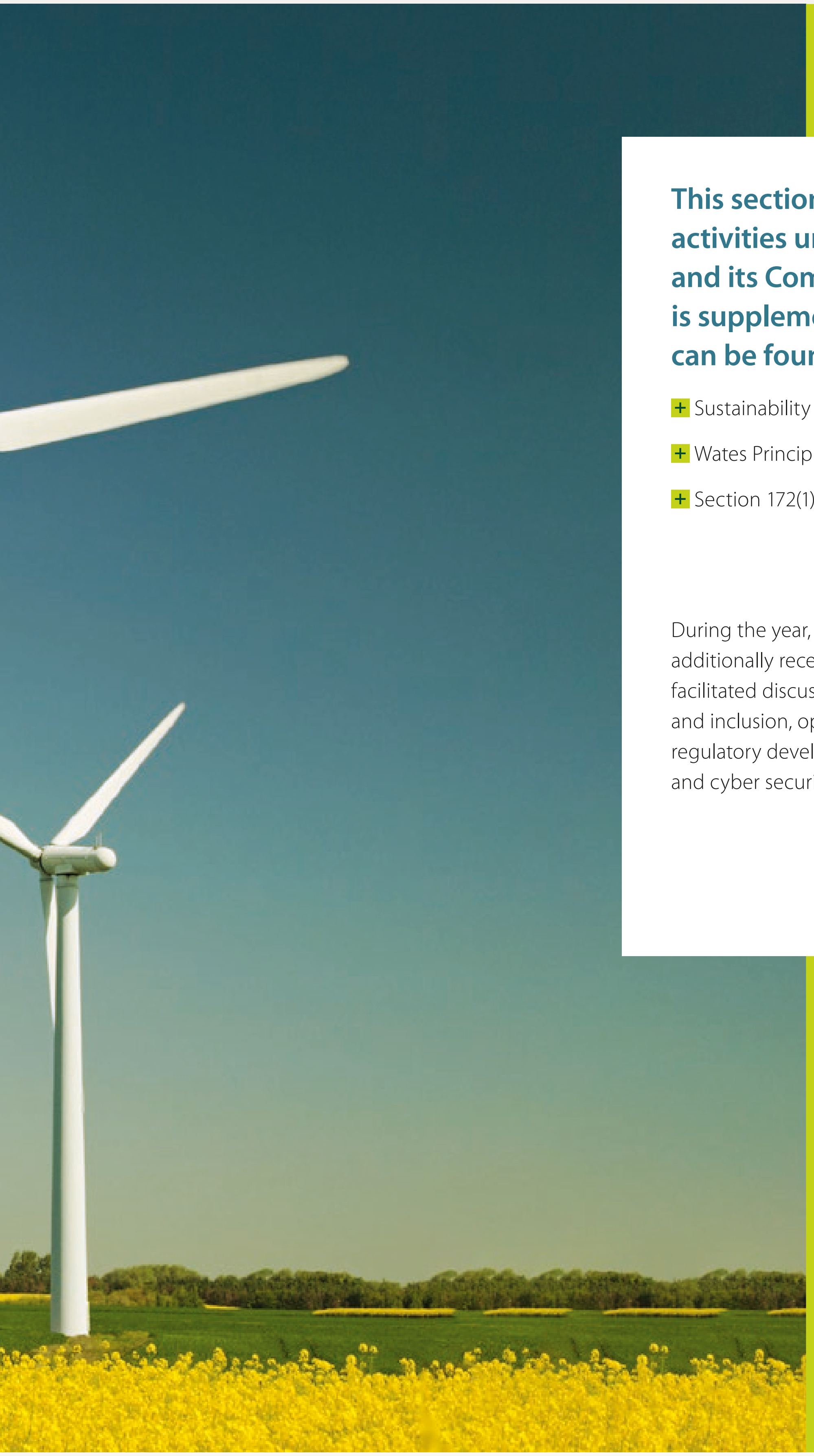
During the year, the Board approved a new ESG Risk Statement to formalise the Bank's approach to managing sustainability and ESG risks. It provides guidance on topics including the definition of Sustainability Risk, the roles of the first and second lines of defence, definitions of what business is prohibited (disallowed) or restricted (allowed conditionally) and escalation paths.

The preparation of the Risk Statement was overseen at an executive-level by the EMEA Sustainability Programme (ESP). Consistent with the Board's approach of considering stakeholder interests, the ESP's work included: ensuring the Statement was consistent with SMBC Group's overall risk policies; understanding emerging practice in EMEA and the objective of developing the Bank's approach to those standards; and understanding the implications for carrying out business with certain customer types.

The views of SMBC Group were sought by the management team and reflected in the Risk Statement. The Bank was also advised by a third party to ensure it fully understood emerging practice. These points were considered by the Risk Committee and Board in approving the Statement.

The Statement is recognised as a first step in a longer-term process to mature the Bank's Sustainability Risk control environment, and it remains under regular review. Material changes to the Statement, such as the strengthening of origination guidelines in high risk sectors, is a matter reserved for the Board.

Report of Board activities



This section includes the principal activities undertaken by the Board and its Committees in the year and is supplemented by information that can be found in:

- Sustainability **pages 21 to 29**.
- Wates Principles **pages 44 to 53**.
- Section 172(1) Statement **pages 54 to 59**.

During the year, the Board met eight times and additionally received briefings and participated in facilitated discussions on topics including: diversity and inclusion, operational risk, regulatory reporting, regulatory developments, digitalisation, automation and cyber security.

Report of Board activities continued

The principal matters considered by the Board in the year included:

Responsibility in terms of reference	Principal matters considered
Strategy and business	– Development of strategy in response to business performance and changes in the macroeconomic and business environment. The full year strategy was approved based on discussions held at the Strategy Day. – Development of the business strategy and other matters related to the transfer to the Bank of the securities business of SMBC Nikko CM (subject to completion of legal and regulatory processes), including the Bank's risk management arrangements post the transfer. – A number of sustainability matters were considered, details of which can be found on **page 22**. – Approving the operational resilience self-assessment. – Status of strategic project activity. – The Slavery and Human Trafficking Statement was approved, reflecting internal control enhancements and updated statutory guidance.
Financial	– Approval of the annual report and accounts, Pillar 3 disclosures and UK Tax Strategy. – Methodology for calculating RoE and progress in implementing measures to enhance returns.
Risk management and internal controls	– Oversight of the Bank's response to the ongoing impact of the Russia–Ukraine conflict, including on the cyber risk environment and credit portfolio, and the actions being taken to respond to changes in UK and EU sanctions legislation. – Approving the ICAAP, ILAAP and Recovery and Resolution documentation. – Testing the solvent wind-down plan in a crisis scenario in conjunction with SMBC Nikko CM. The lessons learned from this exercise were subsequently considered by the Risk Committee.
People	– Approving the appointments to the Board in the year. – Reviewing the talent management strategy which is to attract, enable and secure diverse talent and leadership committed to driving the evolution of the business, and the steps being taken to deliver the strategy given an increasingly competitive recruitment market.
Governance	– Annual report of the Whistleblowers' Champion on the Speak Up arrangements. – Establishment of a Disclosures Committee as a Sub-Committee of the Audit Committee (further details **page 64**).

Report of Board Committees

Audit Committee

The Audit Committee's responsibilities include:

– Considering matters related to the preparation and audit of the annual report and accounts engagement with the external auditor, internal financial controls and taxation.
– Safeguarding the independence and overseeing the performance of the Audit Department, considering the results of Internal Audit and Credit Review activity and the appointment and dismissal of the Co-General Managers of the Audit Department.
– Assessing the effectiveness of the Bank's whistleblowing arrangements.

Charlotte Morgan, a chartered accountant, is Chair of the Committee. At the year-end, the Committee comprised two other independent non-executive Directors, Patricia Jackson and Keith Macdonald. During the year, the composition of the Committee was changed with the Chair of the Board, Alan Keir, and the shareholder representative non-executive Director, Kazuya Ikeda, stepping down as members. These changes were made to reflect the UK Corporate Governance Code provisions for an audit committee to be comprised of independent non-executives and for the Chair of the Board to not be an audit committee member. Although the Board has not adopted the UK Corporate Code, it recognises the Code as governance best practice and agreed it appropriate to make these changes.

On the invitation of the Committee Chair, meetings are also attended by Hideo Kawafune, Nobuyuki Takiguchi, Co-Heads of the Audit Department and Head of Finance and Control. The engagement partner of the external auditor, KPMG, also attends meetings.

During the year, the Audit Committee met four times. The principal matters considered in the year are set out below. The matters related to the financial statements include discussions held after the year-end in respect of this annual report:

Responsibility in terms of reference	Principal matters considered
Matters related to the financial statements	– Development of the IFRS 9 models and approval of key management judgements. – Outcome of the Expected Credit Losses models and challenging the post-model adjustments. – Reviewing and approving litigation provisions and the judgements and assumptions relating to the pension scheme calculation. – TCFD and climate emissions reporting.
Regulatory reporting	– The Pillar 3 disclosures, with the Committee approving for recommendation to the Board the full year disclosures. – Results of a review undertaken to assess the controls and processes required to produce a Single Customer View report as required under the Financial Services Compensation Scheme.

Report of Board Committees continued

Responsibility in terms of reference	Principal matters considered
Internal controls	– The status of internal financial controls and the results of the work undertaken to strengthen those controls.
Taxation	– The UK Tax Strategy, approved by the Committee for recommendation to the Board. – Intra-Group transfer pricing arrangements and tax risk, reflecting the services provided by the Bank to other SMBC Group companies.
External audit	– Fees for the external audit, including the audit of the Paris branch. – Independence and objectivity of the external auditor and the terms of its engagement for undertaking the audit of the financial statements and providing assurance in respect of the LIBOR submission process.
Internal audit	– Approving the Internal Audit and Credit Review plans, including the risk assessment on which the plans are based, of the Internal Audit and Credit Review Groups. The Committee also monitored the Groups' resourcing arrangements and professional development. – The reports issued by Internal Audit on the activities undertaken by the Bank, the responses from management and the implementation of agreed action plans. The Committee seeks to foster a constructive attitude to Internal Audit in the business and an open and transparent relationship between them. – Credit Review monitoring results on the effectiveness of credit files were reviewed each quarter. – Review of assurance arrangements over the Pillar 3, recovery and resolution, and the capital and liquidity adequacy documents.
Whistleblowing	– The integrity, independence and effectiveness of the whistleblowing systems and controls. – An overview from the Chief Compliance Officer on themes identified through whistleblowing.

Disclosures Committee (Sub-Committee of the Audit Committee)

The Committee was established in the year to enhance the process for the development and review of the annual report and accounts, which it is then responsible for recommending to the Audit Committee for approval. The Chair of the Disclosures Committee is Charlotte Morgan, with the other attendees being Nobuyuki Takiguchi, Head of Finance, the Head of Communications and the Company Secretary. The Chief Operating Officer, under delegated authority from the Board, determines the executive membership of the Committee.

During the year, the Disclosures Committee met twice and additionally after the year-end. The principal matters considered in the year are set out below. The matters related to the financial statements include discussions held after the year-end in respect of this annual report:

Responsibility in terms of reference	Principal matters considered
External reporting trends	– Developments in narrative and financial reporting, including review of relevant FRC publications.
Annual report and accounts	– Design of the annual report. – Review of the non-financial and financial disclosures, including deep-dives into topics such as the emissions and sustainability disclosures and accounting for ESG loans.

Report of Board Committees continued

Nomination Committee

The Nomination Committee's responsibilities include:

- Assessing and recommending candidates to the Board to fill Board, Senior Manager Function and other senior executive management vacancies.
- Assessing Board composition, performance and skills.
- Reviewing Board and senior management succession plans.

Alan Keir is the Chair of the Committee. The Committee includes the other independent non-executive Directors. On the invitation of the Chair, meetings are also attended by Hideo Kawafune, Nobuyuki Takiguchi and the Head of Human Resources.

During the year, the Nomination Committee met four times and the principal matters considered included:

Responsibility in terms of reference	Principal matters considered
Board composition	– The results of a review undertaken by the Company Secretary of the terms of appointment of the independent non-executive Directors in respect of length of service, expected time commitment, Committee membership, indemnities and insurance. This review led to a change in the membership of the Audit Committee and new processes for assessing the non-executive Directors' time commitment. – The appointments of Keith Macdonald and Hideo Kawafune. After the year-end, the Committee approved the appointment of Sophie O'Connor
Diversity and inclusion	– Progress against the Bank's Women in Finance Charter commitments and the strategies and initiatives in place to increase senior female representation. There was a particular focus on understanding the causes of employee attrition and the results of employee feedback.
Succession planning	– Succession plans for the independent non-executive Directors and senior executives.
Effectiveness	– The action plans to address the findings arising from the Board and Committees effectiveness review undertaken in the year.

Remuneration Committee

The Remuneration Committee's responsibilities include:

- Overseeing the development and implementation of remuneration policies and practices, which includes specific responsibility for recommending the Remuneration Policy to the Board for approval.
- Other significant remuneration matters, including approving the remuneration of Material Risk Takers (MRTs) and the bonus fund cap calculation.

Alan Keir is the Chair of the Committee. The Committee includes the other non-executive Directors. On the invitation of the Chair, meetings are also attended by Hideo Kawafune, Nobuyuki Takiguchi, the Head of Human Resources and, as necessary, the Chief Risk Officer.

During the year, the Remuneration Committee met four times and the principal matters considered included:

Responsibility in terms of reference	Principal matters considered
Remuneration review	– The strategy for the remuneration reviews for the year ended 31 March 2023 was approved, including both the approach for fixed and variable compensation and the remuneration of individual MRTs. The release of deferred awards to MRTs was also approved following assessment of individual conduct.
Remuneration policies and documents	– Revisions to the Remuneration Policy, Bonus Fund Cap Calculation Operating Procedures and Cash and Phantom Share Scheme Rules to ensure that the documents remained current. – Implementation of an enhanced employee performance adjustment framework and approval for the supporting policy documentation. – Gender Pay Report, which was approved for recommendation to the Board.
Regulatory	– Approval for submission of the required annual remuneration returns. – Consideration of regulatory developments relating to remuneration.

Report of Board Committees continued

Risk Committee

The Risk Committee's responsibilities include:

- Considering risk management structures and systems.
- Considering the status of risk relative to risk appetite and the main areas of risk faced by the Bank.
- Reviewing the ICAAP and ILAAP documents, the recovery and resolution documentation, and regulatory engagement and compliance.

Patricia Jackson is the Chair of the Committee. The Committee includes the other non-executive Directors. On the invitation of the Chair, meetings are also attended by members of management, including Hideo Kawafune, Nobuyuki Takiguchi, Chief Risk Officer, Chief Compliance Officer, General Counsel and Co-Heads of the Audit Department.

During the year, the Risk Committee met four times and the principal matters considered included:

Responsibility in terms of reference	Principal matters considered
Risk management and internal controls	– Principal and emerging risks and the status of risk relative to risk appetite. – Proposals to update risk appetite thresholds were approved, reflecting developments in the business and the approval of the new fiscal year's Corporate Strategy. – Proposals to enhance the Bank's three lines of defence framework. – The Enterprise Risk Management Policy, setting out the core governing principles and framework of risk management, was updated and approved for recommendation to the Board. – Results of Compliance Monitoring Programme review activities. – Information on the sustainability risk matters considered can be found on **page 22**.
Stress and scenario testing	– The scenario tests used for the ICAAP calculation.
Model Risk Management	– The implementation of new regulatory requirements for model risk management and how the Bank was updating its systems and controls to meet the new requirements.
Financial crime prevention	– The MLRO's annual report was reviewed, supplemented at the Committee's request by a six-month interim report updating developments in controls and project activity over the first half year. – Development of a new approach to monitor high financial crime risk countries, products and services. – Development of sanctions legislation and how the Bank was responding.
Conduct and legal risk	– Development of a new cross-border marketing Risk Appetite Framework. – Key conduct metrics evolution. – Results of an impact assessment of the new Consumer Duty regulation.
Projects	– The status of risk-related projects was considered including: development of the data management strategy and programme, and operational resilience framework. – Development of the trade and transactions reporting control framework.
Systems and security	– Status of implementing new IT systems. – The cyber risk threat environment and status of internal controls.
Capital, liquidity and resolution	– The ICAAP, ILAAP and recovery and resolution documentation were approved for recommendation to the Board.

Executive Committee

The Executive Committee is responsible for overseeing the management of the business.

The Committee is Chaired by the CEO and attended by members of the senior management team. The Committee meets monthly and reports to the Board of Directors. The non-executive Directors receive a copy of the papers and minutes of all Committee meetings.

During the year, the Executive Committee met 12 times and the principal matters considered included:

Responsibility in terms of reference	Principal matters considered
Projects	– The overall strategic project portfolio and the status of significant projects.
Risk management	– The overall risk profile, significant risk developments, the top 10 risks and emerging risks. – The impact of developments in the credit markets and the status of the credit portfolio. Monthly reviews were undertaken of the level of impairment costs.
Compliance, financial crime and legal	– Conduct risk KRIs, regulatory developments and the results arising from Compliance Monitoring Programme reviews. – Developments in sanctions legislation, particularly in respect of Russia. – The status of periodic customer account reviews and progress in closing dormant accounts. – Areas of significant legal activity, including arrangements with preferred legal suppliers and the status of litigation.
Financial performance	– Business performance and drivers of overall financial performance.
Systems and security	– The status of key IT projects, including the implementation of ISO 20022. – Cyber security risk trends and emerging risks.
Operations	– Initiatives undertaken to improve operational efficiency. – The status of key operational projects, including development of a Data Management Office, data governance, operational resilience and third party risk management.
People	– Women In Finance Charter targets by Department, resulting in the establishment of senior-level meetings at which methods to increase senior female representation were discussed. The results of these discussions were subsequently considered by the Committee and are being used to inform the approach to develop female talent and employee mobility more generally. – Review of hybrid working survey results and consideration of how to develop departmental communication strategies on hybrid working.
Audit	– Results of Internal Audit and Credit Review activities and progress made by management to implement recommendations made.

Approved by the Board of Directors and signed on behalf of the Board

Hideo Kawafune
Chief Executive Officer
7 July 2023

Directors' Report

The Directors submit their Report and the audited financial statements for the year ended 31 March 2023.

An indication of likely future developments is included in the Strategic Report. No other important events requiring disclosure have occurred since the year-end.

Other information that is relevant to the Directors' Report, and which is incorporated by reference into this Report, can be found as follows:

Other information	Section	Page
Principal and emerging risks	Risks and uncertainties	**Pages 12 to 15**
Policy on the employment of disabled persons	People and culture – Diversity and Inclusion	**Pages 19 and 20**
Streamlined Energy and Carbon Report	Task Force on Climate-related Financial Disclosures	**Page 36**
Statement of Corporate Governance arrangements	Corporate Governance	**Pages 44 to 53**
Engagement with employees	Section 172(1) Statement	**Pages 56 and 57**
Engagement with suppliers, customers and other stakeholders	Section 172(1) Statement	**Pages 54 to 59**
Managing risk	Risk Management	**Pages 73 to 80**
Financial instruments	Notes 3(e), 4 and 5 to the financial statements	**Pages 95 to 125**
Hedge accounting	Note 13 to the financial statements	**Pages 135 to 142**

Results and dividends

The Bank recorded net profit of USD 252.1m for the year ended 31 March 2023 (2022: net profit of USD 131.9m). No dividends have been declared or paid in the year and the Directors do not recommend the payment of a final dividend.

Directors

The list of current Directors can be found in the Strategic Report on page 39. Changes to the Directors during the year and up to the signing of this Report are set out below.

Name	Position	Effective date of appointment/ resignation
Nobuyuki Takiguchi	Executive Director	Appointed 11 April 2022
Hirofumi Otsuka	Non-executive Director	Resigned 1 June 2022
Kazuya Ikeda	Non-executive Director	Appointed 1 June 2022
Keith Macdonald	Independent non-executive Director	Appointed 12 October 2022
Keiichiro Nakamura	Executive Director	Resigned 4 April 2023
Sophie O'Connor	Independent non-executive Director	Appointed 31 May 2023

During the financial year, the independent non-executive Directors benefitted from qualifying third party indemnity provisions and these provisions remain in place at the date of this Report. The Bank has directors' and officers' liability insurance in place in respect of certain losses or liabilities to which the Bank's officers may be exposed in the discharge of their duties.

Political donations

The Bank made no political donations or contributions during the year (2022: nil).

Overseas office

At the date of signing this Report, the Bank had one operational branch which is established in Paris.

Research and development

The Bank develops new products and services in the ordinary course of its business. The Bank's policy is that any new or potentially new product or service is subject to a risk assessment and monitoring process.

Going concern

The Directors believe that the Bank has adequate financial resources and is well placed to manage its business risks successfully despite the current uncertain outlook for the global economy and the banking sector. In addition, the Directors believe the Bank will be able to continue in operation and meet its liabilities, taking into account its current position and the principal risks faced, over a period of at least 12 months from the date of approval of these financial statements.

In making this assessment, the Directors have considered a wide range of detailed information relating to present and future conditions, including projections of profitability, and liquidity and capital requirements and resources.

+ Further information on this can be found in note 2 to the financial statements on **pages 91 and 92**.

Directors' Report continued

Based on their assessment, the Directors conclude that the Bank has adequate resources to continue operations for a period of at least 12 months from the date of these financial statements and, therefore, it is appropriate to adopt the going concern basis.

Disclosure of information to auditor

Each person who is a Director of the Bank as at the date of approval of this Report confirms that:

- so far as the Director is aware, there is no relevant audit information of which the Bank's auditor is unaware; and
- the Director has taken all the steps that he or she ought to have taken as a Director in order to make him or herself aware of any relevant audit information and to establish that the Bank's auditor is aware of that information.

Auditor

Pursuant to section 485 of the Companies Act 2006, the Bank appointed its existing auditor, KPMG LLP, as its auditor for the financial year beginning 1 April 2019. This appointment was made following completion of an audit tender process, which was undertaken in line with the requirements of Statutory Auditors and Third Country Auditors Regulations 2016.

KMPG LLP has expressed its willingness to continue in office and the Board recommends that KPMG LLP be reappointed as the Bank's auditor. A resolution proposing the reappointment of KPMG LLP and giving authority to the Audit Committee to determine its remuneration will be submitted to the forthcoming Annual General Meeting.

Approved by the Board of Directors and signed by order of the Board

Mark Bradley
Company Secretary
7 July 2023

Statement of Directors' responsibilities in respect of the Strategic Report, the Directors' Report and the financial statements

The Directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with International Financial Reporting Standards as adopted by the United Kingdom (IFRSs as adopted by the UK) and applicable law.

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

- select suitable accounting policies and then apply them consistently.
- make judgements and estimates that are reasonable, relevant and reliable.
- state whether they have been prepared in accordance with IFRSs as adopted by the UK.
- assess the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Strategic Report and a Directors' Report that complies with that law and those regulations.

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

Board of Directors at the date of signing

Chair of the Board
Alan Keir

Executive Directors
Hideo Kawafune
James Fenner
Nobuyuki Takiguchi

Non-executive Directors
Kazuya Ikeda
Patricia Jackson
Keith Macdonald
Charlotte Morgan
Sophie O'Connor

Approved by the Board of Directors and signed by order of the Board

Mark Bradley
Company Secretary

7 July 2023

Risk Management Report

This section sets out the Bank's approach to managing risk.

Further information

The Bank's principal and emerging risks can be found on **pages 13 to 15**.

Risk strategy

The Bank's risk strategy is designed to support the Corporate Strategy and the achievement of sustainable growth over the long term. The risk strategy comprises four pillars, being the foundations upon which the Bank seeks to achieve its strategic objectives.

Business model

- Achieve sustainable business growth and manage earnings volatility by prudent risk taking and appropriate pricing of risk.

Solvency and liquidity

- Maintain capital and liquidity resources in surplus over business needs and regulatory requirements.

Conducting business

- Adhere to the letter and spirit of all applicable legal and regulatory requirements and ensure that actions (or failure to act) do not cause an adverse outcome for the Bank, its customers, suppliers and other key stakeholders.

Operational Resilience

- Maintain an operational risk framework comprising people, processes and systems to a high standard in order to ensure resilience against both internal and external operational disruptions.

Risk management objectives

The Bank's risk management objectives are to:

- ensure the Bank's strategic risk pillars, risk strategy statements and risk appetite measures are observed and maintained in the pursuit of the Bank's strategic objectives;
- maintain a risk appetite that maximises risk/return whilst ensuring that the Bank always maintains adequate capital;
- ensure that prudent levels of liquidity are in place to fund the Bank even under stressed conditions;
- maintain fair and ethical relationships with all the Bank's customers;
- manage and mitigate risk that the Bank assumes because of its business strategy;
- maintain an adequate and effective control environment; and
- ensure that the Bank adheres to the letter and spirit of laws and regulations governing its business.

Segregation of duties: Roles and responsibilities in the management of risk

Three lines of defence

The Bank has adopted the three lines of defence model. This approach separates the ownership and management of risk from the functions that oversee risk and the function that provides independent assurance.

First line of defence –
Functions that own and manage risk

Second line of defence –
Functions that oversee risk

Third line of defence –
Functions that provide independent assurance

First line

Senior management in the first line of defence are ultimately responsible for the risks and controls that fall within their area of responsibility. Each department operates within the risk appetite threshold in the context of its own strategy, taking into account the Bank's overall risk management framework and Corporate Strategy. This approach is designed to ensure that risk appetite is cascaded down to those areas where risk is taken.

Second line

The Risk Management Department, Compliance Department and Credit Department are collectively the Bank's second line of defence. These departments are independent from the business areas that generate risk and operate within a governance framework that allows them to exercise professional judgement and make recommendations in an effective and impartial manner.

Third line

Audit Department is the third line of defence and comprises an Internal Audit Group and a Credit Review Group. The objective of Internal Audit is to provide reasonable assurance to the Board, management and other stakeholders that an effective internal control environment has been established to protect the Bank's assets, reputation and sustainability. To achieve this objective, the Internal Audit Group conducts audits and provides related services using a risk-based approach and through meeting the Chartered Institute of Internal Auditors (CIIA) Standards and following the Guidance on Effective Internal Audit in the Financial Services Sector issued by the CIIA.

Additional assurance is provided by the Credit Review Group, which is responsible for reviewing the credit grading process and is similar to a credit quality assurance function. Audit Department acts independently of the Bank's business units. The two Co-General Managers of the Audit Department report to the Audit Committee at its quarterly meetings.

Risk Management continued

Executive-level Risk and Control Committees

The Risk and Control Committees are executive-level committees that have been established to consider certain areas of risk. These include:

Asset and Liability Management Committee

This Committee is primarily responsible for considering market and liquidity risk management issues, and asset and liability management issues, discussing operations and funding policy (including the long-term funding strategy) and reporting on risk appetite, monitoring limits, guidelines and compliance with regulatory requirements.

Credit Risk Committee

This Committee is primarily responsible for discussing a range of credit issues including consideration of credit risk key risk indicators, portfolio analysis, sector analysis and asset allocation, as well as credit risk appetite. It also reviews matters such as business origination guidelines and issues arising from the ongoing credit review activity performed by the Audit Department's Credit Review Group.

Cyber Resilience Committee

This Committee drives change and improvement activity to ensure the Bank meets the expectations set out by the Financial Conduct Authority and other regulators in the area of cyber and technical resilience. This includes governing the Cyber Resilience Strategy and Change Programme.

Finance Committee

This Committee is responsible for providing control, governance, transparency and challenge around finance matters. Key matters overseen and considered by the Committee include financial reporting, external audit, regulatory reporting and taxation.

Financial Crime and Reputational Risk Committee

This Committee is responsible for overseeing the embedding of the Bank's Financial Crime Risk Provisions and Policies, as detailed in the Financial Crime Risk Appetite Statement, and for overseeing the embedding of the approach to reputation risk. The Committee is independent of other Committees but reports significant matters to the Executive Committee and Risk Committee.

Operational and General Risk Committee

This Committee is primarily responsible for examining and discussing matters related to general risk management issues. The subjects discussed include risk issues arising in relation to the overall risk management framework, the risks arising from the implementation of new products and services, and the Operational Risk Management Framework and elements thereof, such as information systems issues, information security matters, compliance and regulatory matters, and Internal Audit findings.

Prudential Regulatory Committee

This Committee is primarily responsible for considering a number of prudential risk issues, including examining the governance processes, assumptions and results related to the ICAAP, recovery and resolution planning, wind-down analysis, ILAAP, credit risk management models, non-credit risk-related models and prudential regulatory horizon scanning.

Key elements of risk management framework

The key elements of the Bank's approach to risk management are as follows:

Risk identification and assessment

The key principles used for risk identification and assessment are:

- to identify the major risks that could impact the Bank's long-term sustainability;
- to assess the likelihood and impact of the risks materialising; and
- to assess the robustness of the controls that mitigate the risks.

The Bank has several key processes to ensure its risks are identified and assessed, including for enterprise risks the top 10 risks and emerging risks, and Risk Register processes. Information on risk category level identification and assessment processes can be found in the sections on credit risk, market risk, liquidity risk, operational and other risks, and conduct risk.

Risk measurement and monitoring

The key principles for risk measurement and monitoring are to:

- measure risk exposure by loss modelling, enterprise-level KRIs and scenarios;
- provide capital methodology and implementation;
- facilitate senior management understanding of the severity of the risk;
- ensure appropriate reporting to Board, Risk Committee and Executive Committee of inherent and post-mitigation risk via KRIs to facilitate any mitigation and/or changes to the risk appetite; and
- maintain a record of accepted risks.

Risk management (control and mitigation)

The Bank seeks to control and mitigate inherent risk as far as possible to ensure that it remains within the risk appetite. Risks are monitored on an inherent (pre-control/mitigation) and residual (post-control/mitigation) basis to assess the Bank's risk profile.

The risk control and mitigation the Bank undertakes is in the form of:

- tangible security;
- financial collateral, both funded and unfunded;
- risk governance, policy and procedures, including risk appetite and business level limits;
- individual and collective controls; and
- other mitigation and control actions.

The control and mitigation are articulated in the policy framework for the main risk types. Controls that implement the policies are contained in the relevant procedure manuals for the Bank's operational processes.

Risk reporting and escalation

The key principles for risk reporting and escalation are as follows:

- Ensuring that senior management is provided with the necessary information regarding the Bank's principal risks so that an informed view of the Bank's risk profile can be made;
- Ensuring that all material risks are reported and deliver a complete view of the whole range of risks the Bank faces;
- The principal risks facing the Bank are reported at the appropriate monthly Risk and Control Committee meetings. These Committees have responsibility for the principal risk categories and related risk management matters; and
- Delivering a Risk Report that incorporates the key themes/messages from the Risk and Control Committees to the Executive Committee monthly.

Risk Management continued

Risk appetite setting

The purpose of risk appetite is to define the broad-based level of risk the Bank is willing to accept in pursuit of its strategic objectives. The risk appetite and risk strategy are complementary, aligning with and supportive of the Corporate Strategy.

The Bank's key principles for its Risk Appetite Framework are:

- The risk appetite of the Bank is set by the Board. This is undertaken on an annual basis as part of the strategic planning process;
- The risk appetite is driven by both top-down Board leadership and bottom-up involvement of business units and second line teams;
- To facilitate embedding of risk appetite into the Bank and its culture;
- To evaluate opportunities for appropriate risk taking and act as a defence against excessive risk taking;
- To promote robust discussions about the risk profile of the Bank as a result of its activities;
- To be adaptive, where appropriate, to changes in business and market conditions;
- To cover all the Bank's activities;
- That Board-level appetite changes should drive real changes in risk taking at the business level;
- That risk taking is calibrated to the Bank's long-term sustainability; and
- That risk appetite setting is an integral part of the Bank's strategy.

Stress testing and scenario analysis

Stress testing and scenario analysis are used across the principal risks to ensure that the Bank can adequately understand and quantify risks not only as they currently exist, but as they might develop in times of stress.

Reverse stress testing

Reverse stress testing (RST) is used to identify and monitor the factors and the stress levels that have the potential to cause the Bank's business model to become unviable. Reverse stress testing is an important part of the overall risk management framework and assists management in understanding key vulnerabilities and to identify potential control enhancements.

The Bank's RST is developed in conjunction and alignment with the Risk Assessment processes (Risk Register and top 10 risks and emerging risks) and is included in the ICAAP.

Model Risk Management Framework

All internal models used to conduct stress testing are subject to the Model Risk Management Policy. This Policy is the governing document for all stress testing-related models, covering credit, market, liquidity and operational risks. All stress testing models are subject to a self-assessment against the model risk management principles published by the PRA and the findings of this are reported in the ICAAP document.

Risk management training

The key principles for risk management training are:

- To facilitate senior management understanding and engagement with key risk management topics and processes;
- To ensure an appropriate and up-to-date framework is in place so that the required skill sets are updated and refreshed regularly, thereby reinforcing the three lines of defence; and
- To communicate the Bank's risk culture and framework throughout the organisation on a quarterly basis

The Bank conducts training across all user groups and levels of seniority through an ongoing process, tailored as appropriate to each group.

Credit risk

Credit risk is the risk of any losses the Bank may incur due to a reduction or loss of the value of assets (including off-balance sheet assets) arising from any credit events, such as the deterioration of a borrower's financial standing.

The framework

The Bank ensures that the level of credit risk it takes is in line with its risk appetite and business model through the following key measures:

- Having a credit risk management framework that consists of appropriate controls and senior management governance and oversight.
- The establishment of well-defined policies and procedures for the identification, measurement and control of credit risk.
- A centralised credit risk control function, under the responsibility of the Chief Risk Officer, who has a right of veto on credit and underwriting transactions.
- Having thorough risk analysis and reporting functions, conducted by a credit management team with the capabilities and resources to evaluate and monitor the exposures and limits.
- The implementation of the Bank's Risk Appetite Framework.
- Ensuring understanding of vulnerabilities through stress testing and reverse stress testing.
- Ensuring the Bank's model governance framework is robust.
- Having strong rating systems to measure the risk of individual transactions.
- Regular reviews conducted by Audit Department's Credit Review Group to ensure compliance with policies, procedures and market best practice.
- A fully comprehensive credit assessment is undertaken at a transaction and client level including: analysis of a variety of financial measures (e.g. cash flow) and quantitative analysis of industrial trends such as the competitiveness of a borrower's products, services and management calibre.

Market risk

Market risk is the risk that movements in interest rates, foreign exchange rates or stock prices will change the market value of financial products, leading to a loss.

The Bank ensures the level of market risk is in line with the Bank's risk appetite and business model through the following controls:

- Value at Risk (VaR) is a measure of the maximum expected loss in a portfolio to a given degree of confidence over a specified period. The Bank has in place an ongoing programme of back-testing and analysis for the VaR model.
- Interest rate risk in the banking book refers to the current or prospective risk to the Bank's capital and earnings arising from adverse movements in interest rates that affect the Bank's banking book position.

This is assessed using:

  - The scenarios as prescribed by the Basel Committee on Banking Supervision (parallel/non-parallel) which are assessed monthly and then daily in the event pre-amber limits are breached;
  - Historical scenarios, for example, Lehman, Black Monday and the more recent COVID-19 period assessed monthly, which considers the Bank's current positions against past crises;
  - Daily market risk reporting of net basis point value (BPV) limits for the overall portfolio and by major currency (GBP, USD, EUR and JPY) respective maturity ladder;
- Monitoring and assessing the daily profit and loss to ensure it is in line with the Bank's expectation; and
- Managing, monitoring and reporting the Bank's Early Warning Indicators (EWIs).

Risk Management continued

Liquidity risk

Liquidity risk is the risk that the Bank cannot meet its liabilities or unwind or settle its positions as they become due. The Bank ensures that the level of liquidity risk is in line with its risk appetite and business model through the following main measures:

- The establishment of a clear, consistent Risk Appetite Framework, and its underpinning quantitative risk metrics, EWIs and KRIs, that is understood across the Bank.
- Defining clear roles and responsibilities for the management of liquidity under normal and stressed circumstances.
- The implementation of a robust committee framework to manage liquidity risk issues, with clear terms of reference and standard agendas.
- Regular management information to demonstrate that the Bank is operating within risk appetite, along with other select metrics.
- Regular senior management training.
- Within the governance framework outlined above, the Bank has established a liquidity risk management approach as a core component of the risk management process. The purpose of the framework is to ensure that the Bank is successfully following its strategy while operating within the bounds outlined by the Liquidity Risk Appetite Statement.
- A variety of internal and regulatory metrics to measure and control liquidity risk.

Operational and other risks

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events including legal risks.

Operational risk arises as a result of the Bank's day-to-day operations and is relevant to every aspect of the business. Operational risk management is embedded through regular engagement with the business, challenge where required, operational risk reporting and training. This is further supported by the execution of the following processes to ensure the operational risk profile is understood and managed:

- Operational risk appetite definition and calibration.
- Operational risk identification, assessment and measurement.
- Control and mitigation.
- Reporting and escalation.

The ongoing management of operational risk is supported by diverse processes and tools, which include: operational risk event/material incident reporting, scenario analysis, risk register, risk issue/acceptance identification, product approval framework, operational risk capital approach, risk indicator governance framework, third party risk management/outsourcing, IT and cyber risk oversight, and project monitoring.

Operational resilience

Operational resilience concerns the Bank's ability to prevent, adapt, respond to, recover and learn from operational disruptions.

The Bank supports a number of Important Business Services and must ensure that, over time, these are as resilient as possible, so that in the event of an operational disruption, it avoids causing intolerable harm to customers and, where relevant, to the wider market.

The Bank has established and embedded a number of key operational resilience components in its business, including:

- Important Business Services
- Impact Tolerances
- Mapping
- Scenario Testing
- Self-assessment
- Lessons learned
- Governance and oversight

By March 2025, the Bank is required to have developed key components and operational capabilities which improve its operational resilience and address its lessons learned so it can consistently remain within its impact tolerances in the event of an operational disruption. The Bank has an active Operational Resilience programme which is scoping, designing and then implementing the changes required in order to iteratively improve its resilience to the required standard during the transition period. This includes enhancements to business continuity, incident management, technology and cyber resilience, and the establishment of a formal business service management capability.

Conduct risk

The risk of the Bank's actions, inactions or behaviours resulting in poor outcomes for customers and/or stakeholders, damaging the integrity of the financial markets or undermining effective competition.

The Conduct Rules form the basis of the Bank's approach to conduct risk management. The Bank has a policy framework to help all colleagues in understanding good conduct, positive behaviours, and raising and addressing concerns.

+ Further information is set out on **Pages 27 to 29**.

To support the policy framework, the Bank provides training, advice and guidance to help colleagues in meeting the regulatory and legal requirements, and the rules and standards of conduct to which all employees must adhere.

Conduct key risk indicators, which seek to provide effective risk identification, are regularly reviewed, including by the Executive and Risk Committees, to ensure proportionality and relevance and to encourage organisational learning, constructive challenge and inclusion, as well as improved engagement and accountability.

There is a strong overlap between operational risk and conduct risk. To that end, when executing the key processes of the Operational Risk Management Framework, conduct risk is considered. Specifically, the following processes include a conduct risk flag to support the assessment of the conduct risk profile:

- Key risk indicators
- Operational Risk Events
- Risk Register
- New Product and Services process

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Independent auditor's report

to the members of SMBC Bank International plc

1. Our opinion is unmodified

We have audited the financial statements of SMBC Bank International plc ("the Bank") for the year ended 31 March 2023 which comprise the Statement of comprehensive income, Statement of financial position, Statement of changes in equity, Statement of cash flows, and the related notes, including the accounting policies in note 3.

In our opinion the financial statements:

- give a true and fair view of the state of the Bank's affairs as at 31 March 2023 and of its profit for the year then ended;
- have been properly prepared in accordance with UK-adopted international accounting standards; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were first appointed as auditor by the shareholders on 10 July 2009 (and then reappointed on 31 January 2019). The period of total uninterrupted engagement is for the fourteen financial years ended 31 March 2023. We have fulfilled our ethical responsibilities under, and we remain independent of the Bank in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

Overview		
Materiality: financial statements as a whole		$10.0m (31 March 2022: $15.0m) 4.2% (31 March 2022: 5.3%) of average profit before tax of the last three years
Key audit matter		**vs 31 March 2022**
Recurring risks	Impairment of loans and advances	◄►

2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgement, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matter, in arriving at our audit opinion above, together with our key audit procedures to address this matter and, as required for public interest entities, our results from those procedures

This matter was addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on this matter.

	The risk	Our response
Impairment of loans and advances at amortised cost, including off-balance sheet elements Charge: $ 47.7m (31 March 2022: $95.8m) Provision: $265.1m (31 March 2022: $284.3m) *Refer to Note 4 (a) (accounting policy and credit risk disclosures).*	**Subjective estimate:** The estimation of expected credit losses ("ECL") on loans and advances involves significant judgement and estimates. The key areas where we identified greater levels of management judgement and therefore increased levels of audit focus in the Bank's determination of ECL are: **-Model estimations** –Inherently judgemental modelling is used to estimate ECLs which involves determining Probabilities of Default ("PD"), Loss Given Default ("LGD"), and Exposures at Default ("EAD"). The ECL global corporates portfolio models (which cover 93% of the total loans and advances to customers), in particular the PD model, and the criteria selected to identify a significant increase in credit risk are the key drivers of the expected credit loss calculation (including staging of assets) and are therefore the most significant judgemental aspects of the Bank's ECL modelling approach. -**Economic scenarios** –IFRS 9 requires the Bank to measure ECLs on an unbiased forward-looking basis reflecting a range of future economic conditions. Significant judgement is applied to determining the economic scenarios used and the probability weightings applied.	Our procedures included: — **Control testing:** We tested the design and implementation and operating effectiveness of the key control over the approval of credit grade assessments which is used as a key input into the PD models. — **Our financial risk modelling expertise:** We involved our own credit risk modellers who assisted in evaluating the Bank's impairment methodologies for compliance with IFRS 9, evaluating the model output for the global corporates portfolio model by inspecting the corresponding model functionality and independently implementing the model by rebuilding the model code and comparing our independent output with management's output; and assessing and reperforming, for this model, the reasonableness of the model predictions by comparing them against actual results and evaluating the resulting differences. — **Our economic scenario expertise:** We involved our own economic specialists to assess and challenge the appropriateness of the economic scenarios (including macro-economic variables selection) and the probability weights assigned to them. We also assessed the overall reasonableness of the economic forecasts by comparing the Bank's forecasts to our own modelled forecasts, with a particular focus on the UK and EU real GDP, UK and EU equity prices. We also assessed the reasonableness of the Bank's considerations of the ECL impact resulting from the continuing economic uncertainty including recent inflationary pressures.

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The risk	Our response
-**Lifetime expected credit losses on customer exposures in Stage 3** –The identification and measurement of Stage 3 assets is an inherently judgmental area within the financial statements. These are individually determined based on certain assumptions about the recovery of the asset using various key inputs including the expected future cash flows, discount rates, and expected recovery strategies. -**Qualitative adjustments** – Adjustments to the model-driven ECL results were raised by the Bank primarily to address issues relating to model limitations, model responsiveness or emerging trends including the impact of the persistent economic uncertainty and the effects of the Russia/Ukraine conflict. Such adjustments are inherently uncertain and significant management judgement is involved in estimating these amounts. The effect of these matters is that, as part of our risk assessment, we determined that the expected credit loss provisions on loans and advances to customers has a high degree of estimation uncertainty, with a potential range of reasonable outcomes greater than our materiality for the financial statements as a whole. The financial statements (note 4) disclose the sensitivity estimated by the Bank. -**Disclosure quality** –The disclosures regarding the Bank's application of IFRS 9 are key to understanding the key judgements and material inputs to the IFRS 9 ECL results.	— **Assessing individual exposures:** For the full population of Stage 3 exposures, we understood the latest developments with each borrower and the basis for classifying and measuring the exposure as Stage 3 and considered whether key judgements were appropriate given the borrower's circumstances. We also re-performed the lifetime expected credit loss calculation, testing key inputs or assumptions including the expected future cash flows, discount rates and challenging the expected recovery strategy. — **Testing qualitative adjustments**: With the assistance of our financial risk modelling specialists, we challenged the Bank's approach to recognising post model adjustments (PMAs) and whether it was appropriate to do so. For the adjustments recognised, and in particular the uncertainty PMA, we assessed whether the key assumptions used were reasonable and the method used for calculation of the PMA is appropriate. We also independently recalculated the PMAs to check them for accuracy. — **Assessing transparency**: We evaluated whether the disclosures appropriately reflect and address the uncertainty which exists when determining the Bank's overall ECL. As a part of this, we assessed the sensitivity analysis that is disclosed. In addition, we challenged whether the disclosure of the key judgments and assumptions made was sufficiently clear. **Our results** Based on the testing performed, we found the resulting estimate to be acceptable.(31 March 2022: acceptable)

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3. Our application of materiality and an overview of the scope of our audit

Materiality for the financial statements as a whole was set at $10.0m (31 March 2022: $15.0m), determined with reference to a benchmark of average profit before tax (PBT) over the past three years, of which it represents 4.2% (31 March 2022: 5.3%).

In line with our audit methodology, our procedures on individual account balances and disclosures were performed to a lower threshold, performance materiality, so as to reduce to an acceptable level the risk that individually immaterial misstatements in individual account balances add up to a material amount across the financial statements as a whole. Performance materiality was set at 75% (31 March 2022: 75%) of materiality for the financial statements as a whole, which equates to $7.5m (31 March 2022: $11.2m). We applied this percentage in our determination of performance materiality because we did not identify any factors indicating an elevated level of risk.

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding $0.5m (31 March 2022: $0.75m), in addition to other identified misstatements that warranted reporting on qualitative grounds.

Our audit of the Bank was undertaken to the materiality and performance materiality levels specified above and was performed by a single audit team.

We were able to rely upon the Bank's internal control over financial reporting in several areas of our audit, where our controls testing supported this approach, which enabled us to reduce the scope of our substantive audit work; in other areas the scope of the audit work performed was fully substantive.

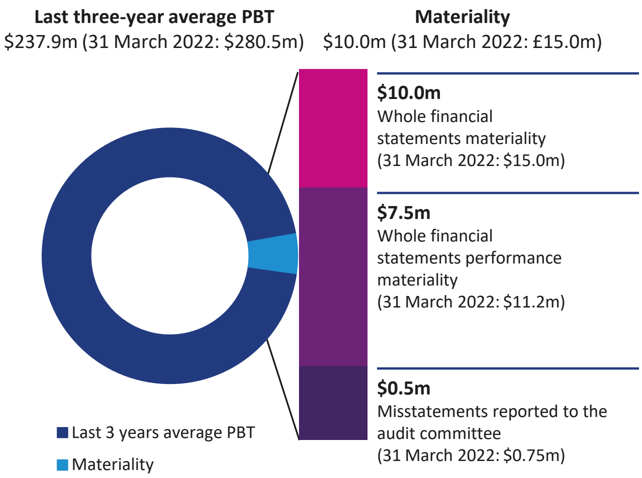
Certain processes and controls operate at the Bank's Parent locations in Tokyo and New York. We instructed the participating audit teams in Tokyo and New York to perform specific risk-focused audit procedures as follows:

- Controls and tests of details over credit impairment model inputs; and
- Certain IT general and application controls on systems hosted by the Parent.

We evaluated the work which the participating audit teams performed in these areas. We conducted on-site visits of both the locations to perform a review of the procedures performed at these locations.

4. Going concern

The directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Bank or to cease its operations, and as they have concluded that the Bank's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").



We used our knowledge of the Bank, the financial services industry, and the general economic environment to identify the inherent risks to the business model and analysed how those risks might affect the Bank's financial resources or ability to continue operations over the going concern period. The risks that management considered most likely to adversely affect the Bank's available financial resources over this period and which we challenged were those arising from recession arising as a consequence of the Russia/Ukraine conflict and high commodity prices and inflation.

We considered whether these risks could plausibly affect the availability of financial resources in the going concern period by comparing severe, but plausible downside scenarios that could arise from these risks individually and collectively against the level of available financial resources indicated by the Bank's financial forecasts.

Our procedures also included an assessment of whether the going concern disclosure in note 1 to the financial statements gives a complete and accurate description of the Directors' assessment of going concern.

Our conclusions based on this work:

- we consider that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate;
- we have not identified, and concur with the directors' assessment that there is not, a material uncertainty related to events or conditions that, individually or collectively, may cast significant doubt on the Bank's ability to continue as a going concern for the going concern period; and
- we found the going concern disclosure in note 1 to be acceptable.

However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the above conclusions are not a guarantee that the Bank will continue in operation.

5. Fraud and breaches of laws and regulations – ability to detect

Identifying and responding to risks of material misstatement due to fraud

To identify risks of material misstatement due to fraud ("fraud risks") we assessed events or conditions that could indicate an incentive or pressure to commit fraud or provide an opportunity to commit fraud. In this risk assessment we considered the following:

- Our meetings throughout the year with the Bank's Chief Risk Officer, General Counsel and Chief Compliance Officer and review of the Bank's compliance reporting summaries;
- Enquiries of operational managers, internal audit and the Board Audit Committee, including obtaining and reviewing supporting documentation concerning the Bank's policies and procedures relating to:
  - detecting and responding to the risk of fraud and whether they have knowledge of any actual, suspected or alleged fraud; and
  - the internal controls established to mitigate risks related to fraud.
- The Bank's remuneration policies, key drivers for remuneration and bonus levels;
- Discussions among the engagement team regarding how and where fraud might occur in the financial statements and any potential indicators of fraud. The engagement team includes senior individuals and staff who have extensive experience of working with banks, and this experience was relevant to the discussion about where fraud risks may arise.

We communicated identified fraud risks throughout the audit team and remained alert to any indications of fraud throughout the audit.

As required by auditing standards, and taking into account possible pressures to meet profit targets and our overall knowledge of the control environment, we perform procedures to address the risk of management override of controls, in particular the risk that Bank's management may be in a position to make inappropriate accounting entries and the risk of bias in accounting estimates and judgements such as ECL on loans and advances to customers. On this audit we do not believe there is a fraud risk related to revenue recognition because there is limited complexity in the calculation and recognition of revenue.

We identified a fraud risk related to the estimation of ECL, specifically relating to qualitative adjustments in response to significant estimation that involves subjective judgments or uncertainties that are difficult to corroborate. Further detail in respect of ECL is set out in the key audit matter in section 2 of this report.

We did not identify any additional fraud risks. Our audit procedures included evaluating the design and implementation and operating effectiveness of relevant internal controls, assessing significant accounting estimates for bias as well as substantive procedures to address the fraud risks. These procedures also included identifying journal entries to test based on risk criteria and comparing the identified entries to supporting documentation.

Identifying and responding to risks of material misstatement due to non-compliance with laws and regulations

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements. For this risk assessment, matters considered included the following:

- our general commercial and sector experience;
- discussion with the Directors and other management (as required by auditing standards);
- inspection of the Bank's regulatory and legal correspondence;
- inspection of the policies and procedures regarding compliance with laws and regulations; and
- relevant discussions with the Bank's key regulatory supervisors including the Prudential Regulation Authority and Financial Conduct Authority.

As the Bank operates in a highly regulated environment, our assessment of risks of material misstatement also considered the control environment, including the Bank's higher level procedures for complying with regulatory requirements. Our assessment included inspection of key policies in place, understanding the role of the compliance function in establishing these and monitoring compliance and inspection of whistleblowing and complaints reports.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

The potential effect of these laws and regulations on the financial statements varies considerably.

Firstly, the Bank is subject to laws and regulations that directly impact the financial statements including:

- financial reporting legislation (including related companies' legislation);
- distributable profits legislation; and
- taxation legislation (direct and indirect).

We assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Secondly, the Bank is subject to many other laws and regulations where the consequences of non-compliance could have a material effect on amounts or disclosures in the financial statements, for instance through the imposition of fines or litigation or the loss of the Bank's licence to operate. We identified the following areas as those most likely to have such an effect:

- Specific aspects of regulatory capital and liquidity;
- Customer conduct rules;
- Money laundering;
- Sanctions list and financial crime; and
- Certain aspects of company legislation recognising the financial and regulated nature of the Bank's activities.

Auditing standards limit the required audit procedures to identify non-compliance with these laws and regulations to enquiry of the directors and other management and inspection of regulatory and legal correspondence, if any. If a breach of operational regulations is not disclosed to us or evident from relevant correspondence, an audit will not detect that breach.

In relation to the legal matters disclosed in note 19 we performed audit procedures which included making enquiries of the Bank's General Counsel. We obtained legal confirmations from the Bank's external counsel.

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Context of the ability of the audit to detect fraud or breaches of law or regulation

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it.

In addition, as with any audit, there remained a higher risk of non-detection of fraud, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. Our audit procedures are designed to detect material misstatement. We are not responsible for preventing non-compliance or fraud and cannot be expected to detect non-compliance with all laws and regulations.

6. We have nothing to report on the strategic report and the directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

— we have not identified material misstatements in those reports;

— in our opinion the information given in the strategic report and the directors' report for the financial year is consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

7. We have nothing to report on the other matters on which we are required to report by exception

Under the Companies Act 2006, we are required to report to you if, in our opinion:

— adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or

— the financial statements are not in agreement with the accounting records and returns; or

— certain disclosures of directors' remuneration specified by law are not made; or

— we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

8. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 72, the directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Bank or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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 our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and 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.

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

9. The purpose of our audit work and to whom we owe our responsibilities

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

Satish Iyer

Satish Iyer (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL
7 July 2023

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Statement of comprehensive income
For the year ended 31 March 2023

	Notes	2023 USDm	2022 USDm
Interest income[1,2]		**1,240.6**	468.2
Interest expense		**(1,016.5)**	(142.5)
Net interest income		**224.1**	325.7
Fees and commissions income		**570.1**	518.6
Fees and commissions expense		**(41.6)**	(49.4)
Net fees and commissions income		**528.5**	469.2
Net trading income		**261.8**	75.9
Operating Income		**1,014.4**	870.8
Net impairment loss on financial assets	4	**(47.7)**	(95.8)
Personnel expenses	6	**(373.2)**	(385.2)
Depreciation and amortisation	15,16	**(51.9)**	(42.7)
Other expenses	6	**(201.3)**	(166.3)
Net operating expenses		**(674.1)**	(690.0)
Profit before income tax		**340.3**	180.8
Income tax charge	10	**(88.2)**	(48.9)
Profit for the year attributed to equity holders of the parent		**252.1**	131.9
Other comprehensive income net of tax:			
Items that will never be reclassified to profit and loss			
Actuarial (losses)/gains on defined benefit scheme		**(12.7)**	20.0
Items that will be reclassified to profit and loss			
Movement in cash flow hedge reserve		**3.5**	5.6
Movement in fair value hedge reserve		**0.3**	0.2
Effect of changes in tax rate		**–**	(0.1)
Other comprehensive income net of income tax		**(8.9)**	25.7
Total comprehensive income for the year		**243.2**	157.6

1 All interest income was calculated using the effective interest rate method.

2 Interest income mainly relates to interest recognised on financial assets measured at amortised cost.

The notes on pages 91 to 152 are an integral part of these financial statements.

Statement of financial position
As at 31 March 2023

	Notes	2023[1] USDm	2022[1] USDm
Assets			
Cash and balances at central banks		**25,880.0**	25,255.4
Settlement balances		**115.5**	96.9
Loans and advances to banks	11	**3,223.6**	3,988.6
Loans and advances to customers	11	**17,712.7**	19,942.6
Reverse repurchase agreements		**1,266.9**	1,197.9
Investment securities	12	**1,045.1**	1,009.2
Derivative assets	13	**2,085.6**	1,430.4
Other assets	14	**928.9**	696.3
Intangible assets and goodwill	15	**56.4**	46.7
Property and equipment	16	**254.4**	254.6
Current tax asset	10	**24.2**	6.0
Deferred tax asset	10	**26.0**	32.1
Pensions surplus	9	**41.8**	60.4
Total assets		**52,661.1**	**54,017.1**
Liabilities			
Deposits by banks		**24,989.5**	26,376.9
Customer accounts		**18,669.0**	19,754.1
Debt securities in issue	17	**1,048.7**	976.0
Derivative liabilities	13	**1,877.3**	1,322.6
Other liabilities	18	**847.3**	583.7
Other provisions		**12.0**	34.5
Current tax liability		**–**	–
Deferred tax liability	10	**27.9**	23.1
Total liabilities		**47,471.7**	**49,070.9**
Shareholders' equity			
Called up share capital	20	**3,200.1**	3,200.1
Other reserves		**110.5**	106.7
Retained earnings		**1,878.8**	1,639.4
Total equity		**5,189.4**	**4,946.2**
Total liabilities and equity		**52,661.1**	**54,017.1**

1 The risk management policy disclosures on credit, market and liquidity risk described on pages 78 and 79 are incorporated into these financial statements by reference.

These financial statements were approved by the Board of Directors and signed on its behalf by:

Nobuyuki Takiguchi
7 July 2023

The notes on pages 91 to 152 are an integral part of these financial statements.

Company registration number 4684034

Statement of changes in equity
For the year ended 31 March 2023

	Share capital USDm	Retained earnings USDm	Capital redemption USDm	Hedge reserve USDm	Fair value reserve USDm	Total USDm
At 1 April 2022	**3,200.1**	**1,639.4**	**100.0**	**6.7**	**–**	**4,946.2**
Total comprehensive income for the year						
Net profit for the period	**–**	**252.1**	**–**	**–**	**–**	**252.1**
Other comprehensive income, net of tax						
Net gains/(losses) transferred to net profit	**–**	**–**	**–**	**(6.7)**	**–**	**(6.7)**
Actuarial gain/(loss) on defined benefit scheme	**–**	**(12.7)**	**–**	**–**	**–**	**(12.7)**
Change in fair value of assets classified as fair value through other comprehensive income (FVOCI)	**–**	**–**	**–**	**–**	**0.3**	**0.3**
Effective portion of changes in fair value	**–**	**–**	**–**	**10.2**	**–**	**10.2**
Effect of changes in tax rate	**–**	**–**	**–**	**–**	**–**	**–**
At 31 March 2023	**3,200.1**	**1,878.8**	**100.0**	**10.2**	**0.3**	**5,189.4**
At 1 April 2021	3,200.1	1,487.6	100.0	1.1	(0.2)	4,788.6
Total comprehensive income for the year						
Net profit for the period	–	131.9	–	–	–	131.9
Other comprehensive income, net of tax						
Net gains/(losses) transferred to net profit	–	–	–	(1.1)	–	(1.1)
Actuarial gain/(loss) on defined benefits scheme	–	20.0	–	–	–	20.0
Change in fair value of assets classified as FVOCI	–	–	–	–	0.2	0.2
Effective portion of changes in fair value	–	–	–	6.7	–	6.7
Effect of changes in tax rate	–	(0.1)	–	–	–	(0.1)
At 31 March 2022	**3,200.1**	**1,639.4**	**100.0**	**6.7**	**–**	**4,946.2**

The notes on pages 91 to 152 are an integral part of these financial statements.

Statement of cash flows
For the year ended 31 March 2023

	2023 USDm	2022 USDm
Reconciliation of profit before tax to net cash flows from operating activities:		
Profit for the year before tax	**340.3**	180.8
Adjustments for non-cash items:		
Net impairment loss on financial assets	**47.7**	95.8
Unrealised exchange movements on non operating assets and liabilities	**(1,076.0)**	(1,121.7)
Depreciation and amortisation	**51.9**	42.7
Changes in operating assets and liabilities:		
Changes in loans and advances to banks	**736.4**	(197.8)
Changes in reverse repurchase agreements	**(69.0)**	534.8
Changes in derivative financial instruments	**(100.5)**	(80.9)
Changes in loans and advances to customers	**2,255.5**	856.4
Changes in other assets	**(214.0)**	(200.7)
Changes in deposits by banks	**(1,387.4)**	2,550.6
Changes in customer accounts	**(1,085.1)**	(2,565.1)
Changes in other liabilities	**245.9**	107.6
	(259.1)	202.5
Taxes paid	**(91.6)**	(92.1)
Net cash from/(used in) operating activities	**(350.7)**	**110.4**
Purchase of investment securities	**(1,025.2)**	(1,669.1)
Proceeds from sale or redemption of investment securities	**992.4**	1,145.9
Purchase of intangible assets	**(24.5)**	(21.0)
Proceeds from sale of intangible assets	**–**	–
Purchase of property and equipment	**(37.1)**	(64.1)
Proceeds from sale of property and equipment	**–**	–
Net cash used in investing activities	**(94.4)**	**(608.3)**
Cash flow from financing activities		
Payment of lease liabilities	**(5.3)**	(18.9)
Proceeds from issue of debt securities	**1,048.7**	976.0
Repayment of debt securities	**(976.0)**	(853.6)
Net cash from financing activities	**67.4**	**103.5**
Net decrease in cash and cash equivalents	**(377.7)**	**(394.4)**
Cash and cash equivalents at start of the year	**25,352.3**	**24,589.6**
Exchange differences in respect of cash and cash equivalents	**1,020.9**	1,157.1
Cash and cash equivalents at 31 March	**25,995.5**	**25,352.3**
Cash and cash equivalents comprise:		
Cash and balances at central banks	**25,880.0**	25,255.4
Settlement balances	**115.5**	96.9
	25,995.5	**25,352.3**

Interest received was USD 1,405.9m (2022: 914.6m) and interest paid was USD 1,197.1m (2022: USD 182.0m).

The notes on pages 91 to 152 are an integral part of these financial statements.

Notes to the financial statements
For the year ended 31 March 2023

1. Reporting entity

The Bank is a company domiciled in England and Wales. The Bank offers a wide range of wholesale banking products, including: bilateral loans, guarantees, syndicated loans, project finance, aircraft finance, shipping finance, other specialised structured finance, trade finance, leveraged finance, cash management, money markets, foreign exchange, deposit taking and derivatives as set out more fully on pages 5 and 6. The registered office is 100 Liverpool Street, London, EC2M 2AT, UK. Further information on the Bank's activities can be found in the Strategic Report.

2. Basis of preparation

(a) Statement of compliance

The Bank's financial statements have been prepared and approved by the Directors in accordance with UK-adopted international accounting standards.

(b) Basis of measurement

The Bank's financial statements are prepared on a going concern basis and under the historical cost convention as modified by the revaluation of investments, derivatives and other financial instruments, in accordance with applicable accounting standards and the Companies Act 2006.

The Directors believe that the Bank has adequate financial resources and is well placed to manage its business risks successfully despite the current uncertain outlook for the global economy and the banking sector. In addition, the Directors believe the Bank will be able to continue in operation and meet its liabilities, taking into account its current position and the principal risks faced, over a period of at least 12 months from the date of approval of these financial statements.

In making this assessment, the Directors have considered a wide range of detailed information relating to present and future conditions, including projections of profitability, liquidity and capital requirements and resources. They determined that the principal risks the Bank currently faces are those arising from recession as a consequence of the Russia / Ukraine crisis and high commodity prices and inflation, although other risks are also considered. This belief is based on consideration of a wide range of information including:

- the results of the Bank's three-year liquidity planning assessment;
- the results of the Bank's three-year capital planning assessment; and
- the results of the Bank's capital and liquidity stress testing.

The economic scenarios for the capital stress are:

- **Global Economic Downturn:** Russia-Ukraine conflict remains a key risk and US-China relations deteriorate, leading to global recession due to high levels of geopolitical risk. Central banks continue to implement tighter monetary policy controls. Emerging market economies with reliance on external debt experience capital outflows and currency depreciation, causing severe slowdown in economic activity.
- **UK and EU recession:** Deep recession in the Eurozone and UK, driven by rising cost of living as a result of increased energy costs arising from the Russia-Ukraine conflict. National budgets strained and financial markets concerned over high sovereign debt levels.
- **Japan recession:** Global recession which disproportionately impacts Japan. Tensions with China lead to supply chains being impacted and sovereign credit rating downgraded. Japan experiences a period of high inflation which is forecast to persist and Yen depreciation, and the Bank of Japan (BoJ) increases interest rates to respond.

Notes to the financial statements For the year ended 31 March 2023 continued

2. Basis of preparation continued

The economic scenarios for the liquidity stress included:

- **UK and EU market wide:** The scenario models the impact of a UK/EU market-wide effect, mainly driven by Russia and Ukraine tensions escalating due to NATO expansion, the UK and Eurozone in deep recession and national budgets are strained, causing concerns over sovereign debt.
- **Japanese stress:** The scenario models the impact of a Japanese market-wide effect driven by rising tensions in East Asia as China asserts ownership over Taiwan and risk of trade sanctions being introduced. Japan suffers a period of high inflation with risk of persistent future inflation, with the BoJ ceasing monetary easing and raises interest rates.
- **SMBC Group idiosyncratic stress:** SMBC Group idiosyncratic scenario models the situation where SMBC Group is suffering from a severe stress event which results in increased credit risk or concerns over solvency.
- **Combined stress:** The combined scenario models the situation where EMEA/UK or Japan market-wide scenario is combined with an SMBC Group idiosyncratic event.

The result of the liquidity and capital assessments, and stress tests is that the Bank remains well capitalised and it is able to continue to fund its operations.

Based on the above, the Directors conclude that the Bank has adequate resources to continue operations for a period of at least 12 months from the date of these financial statements and, therefore, it is appropriate to adopt the going concern basis.

(c) Functional and presentation currency

These financial statements are presented in US Dollars, which is also the Bank's functional currency. US Dollars is the Bank's functional currency as it is the dominant operating currency of the Bank's business. All financial information has been rounded to the nearest one million US Dollars.

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

(d) Adoption of IFRS

i) New and amended standards and interpretations

The Bank has no transactions that are affected by the newly effective standards.

ii) Future accounting standards

There are no new standards or amendments to standards which will become applicable in the future that are expected to have a significant impact on the Bank.

(e) Significant accounting judgements and estimates

The preparation of the Bank's financial statements in accordance with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgement in the process of applying the accounting policies. The most significant areas where judgements and estimates have been used, and the notes where information on these is disclosed, are as follows:

Impairment losses on loans and advances and undrawn loan commitments (note 4)

IFRS 9 impairment involves several areas of judgement as follows:

- Establishing the criteria for determining whether credit risk on the financial asset has increased significantly since initial recognition, determining the methodology for incorporating forward-looking information into the measurement of expected credit loss (ECL) and selection and approval of models used to estimate ECL.
- Determination of inputs into the ECL measurement model, including key assumptions used in estimating recoverable cash flows and incorporation of forward-looking information.
- Considerations taken into account and calculation of impairment allowances for individually significant assets in Stage 3.

The Bank reviews its problem assets held at amortised cost at each reporting date to assess whether an allowance for credit impairment should be recorded in profit and loss. In determining the ECL, management is required to exercise judgement in defining what is considered to be a significant increase in credit risk and in making assumptions and estimates to incorporate relevant information about past events, current conditions and forecasts of economic conditions. The exercise of judgement in making estimations requires the use of assumptions that are highly subjective and sensitive to the risk factors. Further information and sensitivity analyses of ECL to different economic scenarios is provided in note 4.

In addition to specific allowances against defaulted loans and advances (Stage 3), the Bank also makes provisions on performing assets based on 12-month ECLs (Stage 1) and on assets subject to a significant increase in credit risk based on lifetime ECLs (Stage 2).

Pensions (note 9)

The cost of the defined benefit pension scheme is determined using actuarial valuation. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Due to the long-term nature of the scheme, such estimates are subject to measurement uncertainty.

Fair value of financial instruments (note 5)

Where the prices of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from markets where valuations are actively quoted, they are determined using a variety of valuation techniques that include use of mathematical models. The input to these models is taken from observable market data where possible, but where this is not feasible, a degree of judgement is required in establishing fair values.

Notes to the financial statements For the year ended 31 March 2023 continued

3. Significant accounting policies

This section describes the Bank's significant accounting policies that relate to the financial statements and the notes as a whole. If an accounting policy relates to a particular note, the accounting policy is contained within the relevant note.

(a) Basis of consolidation

Subsidiaries are investees controlled by the Bank. The Bank 'controls' an investee if it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The Bank reassesses whether it has control if there are changes to one or more of the elements of control. In the normal course of business the Bank lends to structured entities in a number of different industries. The assessment undertaken by the Bank includes circumstances in which protective rights held (e.g. those resulting from a lending relationship) become substantive and lead to the Bank having power over the investee. The financial statements of any subsidiaries would be included in the consolidated financial statements from the date control commences until the date control ceases. At 31 March 2023, the Bank did not control any investees.

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured at the fair value of the consideration, including contingent consideration, given at the date of exchange. Acquisition-related costs are recognised as an expense in the income statement in the period in which they are incurred. The acquired identifiable assets, liabilities and contingent liabilities are generally measured at their fair values at the date of acquisition. Goodwill is measured as the excess of the aggregate of the consideration transferred, the amount of non-controlling interest and the fair value of the Bank's previously held equity interest, if any, over the net of the amounts of the identifiable assets acquired and the liabilities assumed.

(b) Interest and similar income and expense

Interest income and expense are recognised in the income statement for all financial assets and financial liabilities at amortised cost using the effective interest method. The effective interest method is a method of calculating the cost of a financial asset or liability and of allocating the interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period if appropriate. The application of the method has the effect of recognising income receivable on the instrument in proportion to the amount outstanding over the period to maturity or repayment. In calculating effective interest, the Bank estimates cash flows considering all contractual terms of the financial instrument but, for financial assets, excluding future credit losses. Where it is not possible to otherwise estimate reliably the cash flows or the expected life of the financial instrument, effective interest is calculated by reference to the payments or receipts specified in the contract, and the full contractual term.

(c) Fee and commission income and expense

Fee income relating to loans and advances held at amortised cost is recognised in profit and loss as either an adjustment to the effective interest rate or on an accruals basis as the service is provided. Where a fee is considered to be an adjustment to the effective interest rate, it is recognised as such over the original life of the advance or expected life if this is reliably estimated to be shorter. Where loans and advances are purchased in the secondary market and there is observable evidence that the fair value is higher than the purchase price, then the differential is recognised as profit within fees.

Fees and commissions receivable in respect of all other services provided are recognised in profit and loss when the related services are performed and when consideration is considered receivable. The performance obligations, as well as the timing of when they have been met, are identified, and determined, at the inception of the contract. The Bank's revenue contracts do not include multiple performance obligations. When the Bank provides a service to its customers, consideration is generally due immediately upon satisfaction of a service provided at a point in time or at the end of the contract period for a service provided over time.

Fees and commissions expense relates mainly to transaction and service fees, which are expensed as the service is received.

(d) Net trading income

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

(e) Financial instruments – initial recognition and subsequent measurement

Financial assets

These include loans and advances to banks and customers and investment securities.

i) Classification, initial recognition and subsequent measurement

Financial assets are classified into the following measurement categories:

- those to be measured at fair value (either through other comprehensive income (FVOCI) or through profit or loss (FVTPL)); or
- those to be measured at amortised cost.

The classification depends on the business model for managing financial assets and the contractual terms of the financial assets' cash flows.

Business model assessment

The Bank makes an assessment of the objective of the business model in which a financial asset is held based on the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. These include whether management's strategy focuses on earning contractual interest income, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of any related liabilities or expected cash outflows or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales of financial assets in prior periods, the reasons for such sales and expectations about future sales activity.

The Bank's corporate banking business comprises primarily loans to customers that are held for collecting contractual cash flows. Sales of loans from these portfolios are very rare. The exception to this is the syndications portfolio where the assets are held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets.

Investment securities are largely held for collecting contractual cash flows and selling financial assets with the exception of a small number of debt securities which are held only for collecting contractual cash flows and where sales of such assets would be infrequent.

Notes to the financial statements For the year ended 31 March 2023 continued

3. Significant accounting policies continued

Contractual terms of financial assets' cash flows

For financial assets to be held at amortised cost, the contractual terms of the financial asset must give rise to cash flows on specified dates that represent solely payments of principal and interest on the principal amount outstanding.

For the purposes of this assessment, principal is defined as the fair value of the financial assets on initial recognition and interest is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making this assessment, the Bank considers:

- contingent events that would change the amount or timing of cash flows;
- terms that may adjust the contractual coupon rate, including variable rate features;
- prepayment and extension features; and
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse features).

A prepayment feature is consistent with the solely payments of principal and interest criterion if the prepayment amount substantially represents unpaid amounts of principal and interest on the principal amount outstanding, which may include reasonable additional compensation for early termination of the contract. Additionally, for a financial asset acquired at a discount or premium to its contractual par amount, a feature that permits or requires prepayment at an amount that substantially represents the contractual par amount plus accrued contractual interest (which may include reasonable additional compensation for early termination) is treated as consistent with this criterion if the fair value of the prepayment feature is insignificant at initial recognition.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Financial assets are initially recognised at their fair value plus, in the case of financial assets not at fair value through profit and loss, any transaction costs that are incremental and directly attributable to the acquisition of the financial asset.

Fair value for financial instruments traded in an active market is based on quoted market prices or dealer price quotations (bid price for long and offer price for short positions). For other financial instruments, the fair value is determined by using appropriate valuation techniques including present-value techniques or comparison to similar instruments.

Financial liabilities

These include deposits, debt securities issued and subordinated debts which are the Bank's source of debt funding. Financial liabilities are classified as non-trading, held for trading or designated as held at fair value through profit and loss. Financial liabilities are initially recognised at their fair value minus, in the case of financial liabilities not at fair value through profit and loss, any transaction costs that are incremental and directly attributable to the issue of the financial liability. Subsequent to initial recognition, non-trading liabilities are recorded at amortised cost. Subsequent to initial recognition, liabilities held for trading or liabilities designated as held at fair value through profit and loss are accounted for as indicated in the accounting policy for financial liabilities at fair value through the profit and loss.

ii) Derecognition of financial assets and liabilities

The Bank derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or when it transfers the financial assets in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset. On derecognition of a financial asset, the difference between the carrying amount of the asset and the sum of i) the consideration received including any new asset obtained less any new liability assumed and ii) any cumulative gain or loss that has been recognised in other comprehensive income is recognised in profit and loss. Any cumulative gain or loss recognised in other comprehensive income in respect of equity investments designated as at FVOCI is not recognised in profit and loss on derecognition.

The Bank enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. If all or substantially all risks and rewards are retained, then the transferred assets are not derecognised.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

iii) Modifications of financial assets and liabilities

Financial assets

If the terms of a financial asset are modified, the Bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this instance, the original financial asset is derecognised and a new financial asset is recognised at fair value.

If the cash flows of a modified financial asset carried at amortised cost or FVOCI are not substantially different, then the modification does not result in the derecognition of the financial asset. In this case, the Bank recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognises the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit and loss. If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

Financial liabilities

The Bank derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and the new financial liability with modified terms is recognised in profit and loss.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in profit and loss.

Notes to the financial statements For the year ended 31 March 2023 continued

3. Significant accounting policies continued

Interest rate benchmark reform

If the basis for determining the contractual cash flows of a financial asset or financial liability measured at amortised cost or at FVOCI changes as a result of the interest rate benchmark reform, then the Bank updates the effective interest rate of the financial asset or financial liability to reflect the change that is required by the reform. A change in the basis for determining the contractual cash flows is required by interest rate benchmark reform if the following conditions are met:

- the change is necessary as a direct consequence of the reform; and
- the new basis for determining the contractual cash flows is economically equivalent to the previous basis.

If changes are made to a financial asset or financial liability in addition to changes to the basis for determining the contractual cash flows required by interest rate benchmark reform, then the Bank first updates the effective interest rate of the financial asset or financial liability to reflect the change that is required by interest rate benchmark reform. After that, the Bank applies the policies on accounting for modifications set out above to the additional changes.

(f) Foreign currencies

The financial statements are presented in US Dollars, which is the Bank's functional and reporting currency. Items included in the financial statements of each of the Bank's operations are measured using their functional currency, being the currency of the primary economic environment in which they operate.

Foreign currency transactions are translated into the appropriate functional currency using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are translated at the rate prevailing at the period end. Foreign exchange gains and losses resulting from the translation and settlement of these items are recognised in the income statement except for qualifying cash flow hedges.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Translation differences on equities classified as at FVTPL profit and loss are reported as part of the fair value gain or loss in the income statement.

(g) Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprises balances with original maturities of up to three months including cash and cash equivalents with central banks, and loans and advances to banks. These comprise highly liquid investments that are readily convertible into cash with an insignificant risk of changes in value.

4. Financial risk management

The risks relating to financial instruments and the way in which the Bank manages these are described below.

(a) Credit risk

Credit risk is the risk of any losses the Bank may incur due to a reduction or loss of the value of assets (including off-balance sheet assets) arising from any credit events, such as the deterioration of a borrower's financial standing.

Credit assessment

The Bank assesses and manages the credit risk of individual loans and credit portfolios on a consistent quantitative basis utilising an internal rating system.

The rating system consists of two indicators namely:

- the obligor grading, which indicates the creditworthiness of the borrower; and
- the facility grading, which indicates the probability of repayment of each facility. Facility grades are assigned based on the borrower's obligor grading and transaction terms such as guarantee, maturity and collateral.

The Bank's internal grading and borrower categories are set out in the table below, and are used for the purposes of determining the Bank's credit quality of obligors.

G grade*	**J grade***	
Code	**Code**	**Borrower's category**
G1	J1	Normal borrowers
G2	J2	Normal borrowers
G3	J3	Normal borrowers
G4	J4	Normal borrowers
G5	J5	Normal borrowers
G6	J6	Normal borrowers
(G7A, G7B)	(J7A, J7B)	Borrowers requiring caution
G7R	J7R	Substandard borrowers
G8	J8	Potentially bankrupt borrowers
G9	J9	Virtually bankrupt borrowers
G10	J10	Bankrupt borrowers

* G grade – non-Japanese borrowers, J Grade – Japanese borrowers.

The internal ratings G7R and J7R through to G10 and J10 are recognised as 'Default' in terms of EU Capital Requirements Directive IV and in line with regulatory default definition.

Credit monitoring

Credit monitoring is carried out through an ongoing reassessment of obligor grades involving:

- annual monitoring following financial results disclosures; and
- ad-hoc monitoring should credit conditions deteriorate.

Should a customer be downgraded or considered a likely candidate for future downgrade(s) to below 'Normal borrower' category, the customer is added to the special credit borrower list and reported to management.

To minimise the potential loss that may arise from any model failure and/or inadequate usage of the models and systems, the Bank has appropriate policies in place to manage its models and grading systems. The Bank's Credit Risk Control Unit performs validation of the grading models at least annually to ensure the appropriateness of the grading models.

The Bank regularly monitors the credit risks associated with wider aspects of its business, such as specific country exposure, products, industries, etc. on a portfolio basis. The Bank also undertakes regular stress tests on its portfolio to ensure adequate capital is kept at all times to cover potential losses incurred during extreme events such as the COVID-19 pandemic.

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Expected credit losses

Accounting for impairment provisions

Impairment provisions are accounted for in line with IFRS 9 'Financial Instruments – Classification and Measurement'. The Bank applies a three-stage approach to measuring ECL for the following categories of financial instruments that are not measured at FVTPL:

- Loans and advances to banks and customers measured at amortised cost.
- Debt instruments measured at amortised cost and FVOCI.
- Loan commitments.
- Financial guarantee contracts.

The Bank has grouped its financial instruments into Stage 1, Stage 2 and Stage 3, based on the implied impairment methodology, as described below:

Stage 1: 12-month ECL – For performing financial instruments where there has not been a significant deterioration in their credit quality since initial recognition, the Bank recognises an allowance for the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months.

Stage 2: Lifetime ECL – For financial instruments where there has been a significant increase in credit risk since initial recognition but they are not credit-impaired, the Bank recognises an allowance for the lifetime ECL.

Stage 3: Credit-impaired – Financial instrument exposures are assessed as credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of the instrument have occurred. For financial instruments that have been assessed as credit-impaired, the Bank recognises an allowance for the lifetime ECLs.

Determining the stage for impairment

At each balance sheet date, for loans carried at amortised cost, loan commitments, financial guarantee contracts and debt securities carried at FVOCI, the Bank assesses whether there has been a significant increase in credit risk for exposures since initial recognition by comparing the risk of default between the balance sheet date and the date of initial recognition. Credit risk is assessed either individually to financial assets, or collectively to a portfolio of similar, homogenous assets.

Significant increase in credit risk (SICR)

In order to determine whether a significant increase in credit risk of a financial instrument has taken place since its initial recognition, the Bank considers reasonable and verifiable information that is relevant and accessible without excessive cost or effort. The Bank assesses significant increase in credit risk using both quantitative and qualitative information.

Determining whether SICR takes place

The Bank follows a robust event-based framework of determining SICR. The Bank uses the quantitative factor of a change in the probability of default (PD) based on the grading of each loan as well as additional factors such as 30 days past due and whether a customer is on the Credit Alarm System (Watch List) in order to determine whether a significant increase in the credit risk of a financial instrument has taken place.

The bank has enhanced the staging model to a methodology that uses a forward-looking approach to determine the appropriate stage. The forward-looking grade calculated takes consideration of the future state of the economy. The bank applies a grading-based review on each exposure by comparing grade at origination and forward-looking grade at reporting date. The bank uses relative PD threshold based on grading as a quantitative criteria for identifying significant increase in credit risk. The threshold was assessed based on historical default data.

The Bank uses an additional criterion of 30 days past due for determining SICR. The number of days overdue is determined by counting the number of days starting from the first day when the payment was not received in full. Payment dates are determined without taking into account the grace period that can be provided to the borrower. In addition, for customers graded G/J 5 and G/J 6, inclusion in the Watch List is an indicator of SICR. This is for customers categorised as 'Normal borrowers' but determined as requiring additional monitoring due to credit deterioration.

Recognition of financial assets as impaired (Stage 3)

A financial asset is recognised as impaired if default has occurred since initial recognition.

Default definition

The definition of default for the purpose of determining ECLs has been aligned to the Capital Requirements Regulation Article 178 definition of default, to maintain a consistent approach with IFRS 9 and associated regulatory guidance. The following events generally provide objective evidence of a default situation:

- The management bodies of the borrower/group of borrowers decide to reorganise or liquidate the borrower and/or any bankruptcy proceedings or involuntary liquidation in respect of the borrower is initiated (either by the borrower itself or by any third parties) and/or an external manager, provisional manager, liquidator or commissioner is appointed.
- Delinquency exceeds three months. Delinquency is considered to be caused by the deterioration of business conditions or constrained cash flow (and including cases in which only interest is not paid, but there is no delay in repayment of the principal).
- The loan is restructured towards the more favourable conditions for a borrower, in the absence of which the borrower could not fulfil the obligations towards the Bank properly.
- Breach of financial covenants, which, in the reasonable opinion of the Bank, may result in improper fulfilment of obligations by the borrower.
- Any other event happens in relation to the borrower/group of borrowers that, in the Bank's opinion, can cause improper fulfilment of obligations by the borrower.

An exposure will migrate through the ECL stages as asset quality deteriorates. If, in a subsequent period, asset quality improves and also reverses any previously assessed significant increase in credit risk since origination, the impairment provision reverts from lifetime ECL to 12-month ECL.

The Bank recognises write-offs when the Bank assesses there is no prospect of further recoveries, typically on liquidation of the counterparty. In practice, write-offs on liquidation are infrequent.

Improvement of credit quality

If a financial asset classified in Stage 2 shows an improvement in credit quality, then this asset can be classified in Stage 1. No probation period is applied as the latest grading will reflect the customer's current financial creditworthiness with consideration of any near-term factors which could impact the customer grade already taken into account.

Movement from Stage 3 to Stage 2 or 1 is dependent on individual assessment. All relevant factors in relation to the credit worthiness of the customer will be taken into account before a customer is upgraded and moved out of Stage 3. The Stage 3 exposures with forbearance measures in place have to go through, in addition to the above requirements, a minimum cure period of two years as a normal borrower before they can be moved out of Stage 3. There have been no such movements during the year.

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Grades (credit ratings)

The Bank assigns appropriate grades to each exposure based on data that is used to predict the risk of default and by applying expert judgement on credit quality. Ratings are determined based on qualitative and quantitative factors, and indicators of the risk of default. These factors vary depending on the type of the borrower and exposure itself.

Grades are determined in a way that the risk of default increases significantly as credit quality deteriorates. For example, the difference between grades 1 and 2 is less than the difference between grades 2 and 3.

Each exposure is assigned with a particular grade at the date of the initial recognition based on the information available. These exposures are subject to continuous monitoring. So, the grade assigned to the exposure could change since the date of the initial recognition.

Monitoring usually includes the analysis of the following data:

- Information obtained as a result of analysis of the borrowers on a periodic basis: audited financial statements, management accounts, budgets, forecasts and plans.
- Credit rating agencies' data, publications and information on changes in external credit ratings.
- Bond and credit default swap quotes, if such information is available.
- Actual and expected significant changes in political, regulatory and technological environments that could influence the borrower's business.

Creation of provisions

The calculation of ECLs is based on the following metrics:

- Probability of default (PD).
- Loss given default (LGD).
- Exposure at default (EAD).

The LGD model uses the Frye-Jacob approach as the theoretical foundation and leverages the same macroeconomic variables as the PD model.

The EAD model is used to estimate lifetime EAD which will be used in the ECL calculation. This model forecasts the undrawn amount via the estimation of the Credit Conversion Factor (CCF) and calculates drawn amount of facilities with defined repayment schedule. A fallback component is added this year when no appropriate macroeconomic variables is found to forecast CCF. Under this approach, the CCF is determined for each scenario based on the quantile of the annual historical CCF distribution. Each scenario weight/probability is used to calculate the corresponding CCF.

In order to calculate ECL for loans provided to corporate clients and banks, the Bank adjusts the annual value of PD in proportion to the term of the financial instrument.

Probability of default

The PD is modelled using credit ratings transition matrices that were created based on internal and external statistics. The transition matrix shows the expected migration of a customer at a specific grade to alternative grades over a period of time. The Bank uses two sets of transition matrices to forecast PD, including transition matrices for borrowers whose parent companies are located in Japan and transition matrices for borrowers whose parent companies are residents of other countries. The value of PD is determined based on macroeconomic forecasts, including the dynamics of equity prices and GDP (2022: unemployment rates for the UK model and GDP for the EU model).

Grades are the main inputs that are used for creation of the PD for positions exposed to credit risk. The Bank collects information on the debt service quality and default level of exposures, analysed depending on jurisdiction or region, type of product and borrower, and also depending on the rating of the credit risk.

The Bank uses statistical models to analyse the collected data and to obtain estimates of the PD for the remaining period for positions exposed to credit risk and expectations of their changes in the future.

This analysis includes the estimation and calibration of correlation between changes in default levels and changes in key macroeconomic factors. The Bank uses dynamics of GDP for the EU and Japan, and unemployment rates for the UK as key macroeconomic factors to determine the PD of positions exposed to credit risk.

The Bank uses these forecasts to adjust PD estimates.

Macroeconomic forecasts

The Bank defines EU and UK Equity Price and EU and UK GDP (2022: EU GDP and UK unemployment rates) as key macroeconomic factors in the models of PD, LGD and EAD.

For each key macroeconomic factor the Bank estimates four scenarios: a base, optimistic, pessimistic (moderate) and pessimistic (severe) scenario. The base scenario is based on third party subject matter expert forecasts and is parameterised internally to give the optimistic and pessimistic scenarios. Each scenario has a probability of occurring assigned as follows:

- Optimistic: 10% (2022: 17%)
- Base: 46% (2022: 46%)
- Moderate pessimistic: 26% (2022: 24%)
- Severe stress: 18% (2022: 13%)

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Measurement of expected credit losses

ECLs are derived from probability-weighted estimates of expected loss, and are measured as follows:

- **Financial assets that are not credit-impaired at the balance sheet date:** as the present value of all cash shortfalls over the next 12 months of the financial asset discounted by the effective interest rate for assets classified as Stage 1 and as the present value of all cash shortfalls over the expected life of the financial asset discounted by the effective interest rate for assets classified as Stage 2. The cash shortfall is the difference between the cash flows due to the Bank in accordance with the contract and the cash flows that the Bank expects to receive.
- **Financial assets that are credit-impaired at the balance sheet date:** as the difference between the gross carrying amount and the present value of estimated future cash flows discounted by the effective interest rate.
- **Undrawn loan commitments:** as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive.
- **Financial guarantee contracts:** as the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Movement in ECLs is recognised as impairment loss in the income statement and for financial assets measured at amortised cost as a deduction from the gross carrying amount of the assets. In the case of debt securities measured at FVOCI, no loss allowance is recognised in the statement of financial position because the carrying amount of the assets is their fair value. However, on derecognition, the Bank recognises the impairment charge in the income statement with the corresponding amount recognised in the fair value reserve in other comprehensive income. For undrawn loan commitments and financial guarantee contracts that are recognised off balance sheet, the Bank recognises the impairment charge in the income statement with the corresponding amount recognised in other provisions on the balance sheet.

Forward-looking information

The Bank incorporates forward-looking information into both the assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and the measurement of ECL.

Methods of estimation and creation of provision for credit losses

The Bank estimates provisions for credit losses at the transaction level for all financial instruments.

Expected life

For term loans, the expected life of the transactions is based on contractual maturity.

For revolving credit facilities, a model linked to the macroeconomic variables is used to predict utilisation rates.

Use of exemptions permitted under IFRS 9

The Bank has not applied the low credit risk exemption permitted under IFRS 9.

Purchased or originated credit-impaired

Financial assets that are purchased or originated at a deep discount that reflects the incurred credit losses are considered to be purchased or originated credit-impaired (POCI). This includes the recognition of a new financial asset following a renegotiation where concessions have been granted for economic or contractual reasons relating to the borrower's financial difficulty that otherwise would not have been considered. Any changes in lifetime ECLs since initial recognition of POCI assets are recognised in profit and loss until the POCI is derecognised, even if the lifetime ECLs are less than the amount of ECLs included in the estimated cash flows on initial recognition.

As at 31 March 2023, the Bank did not hold any financial assets that are purchased or originated credit-impaired (2022: none).

Governance

The ECL models are all subject to the Bank's model governance framework.

The macroeconomic factors for the base and pessimistic scenarios are sourced from external subject matter experts whilst the optimistic scenario is derived internally. These are reviewed and challenged by internal subject matter experts. The macroeconomic factors are presented for review and approval to the Prudential Regulatory Committee, which reports into the Risk Committee. These are subsequently presented for review and final approval to the Audit Committee. The Audit Committee also reviews and considers the weightings applied to each scenario.

Management adjustments to models for impairment

Management adjustments to impairment models (post-model adjustments or PMAs) are applied in order to factor in certain conditions that are not fully incorporated into the impairment models, or to reflect additional facts and circumstances at the period end.

	2023 USDm	2022 USDm
Impairment allowance pre PMAs[1]	**95.6**	137.5
Sectors PMA	**23.2**	22.7
Uncertainty PMA	**146.3**	45.2
Condition of economy PMA	**–**	78.9
Total impairment allowance	**265.1**	284.3

1 Includes USD 9.0 million credit related to a change in the staging model with respect to using consistent probability of default data for loans at origination and at each assessment date.

The 31 March 2022 year-end coincided with the outbreak of the Russia–Ukraine conflict, an event that goes beyond the boundaries of the more typical credit cycle. Over the last 12 months, the Russia–Ukraine conflict has continued to impact on macroeconomic conditions. The conflict continues to be a threat to global security, Western political systems, the cybersphere and food and energy supply chains. Energy prices have remained elevated, which, along with increased consumer and business spending following the COVID-19 pandemic, has resulted in worldwide inflation.

As a result, the Bank has applied a number of PMAs in the year to 31 March 2023 and 31 March 2022, to reflect the additional factors that impact the impairment provisions.

Post-model adjustments 31 March 2023

As at 31 March 2023, the Bank has applied two PMAs: one covers sectors and countries, and one is focused on uncertainty regarding Russian exposures.

Notes to the financial statements
For the year ended 31 March 2023 continued

4. Financial risk management continued

Sector and country PMA – the sector overlay aims to capture idiosyncratic risks that could impact certain sectors as a result of the current economic uncertainty. High risk sectors were identified using revenue and share price performance prior to and post the commencement of the Russia–Ukraine conflict. Depending on the severity of the impact on each high risk sector, customers in these sectors have been downgraded by one or two notches. Under the severe stress scenario, eight sectors which were identified as most significantly impacted received a two-notch downgrade. A further nine sectors received a single-notch downgrade based on the moderate pessimistic scenario, and under the optimistic scenario, one sector was identified as outperforming and was subject to a one-notch upgrade.

In addition to this, a country PMA has been included to capture the bilateral trade and energy dependencies of certain countries upon Russia and the cost of living impact of these countries' fiscal and external positions to cope with the above. Countries with low country rank that don't use common currency are considered to have a weaker fiscal and external position.

A review of these countries was performed internally. For those countries with weak financial and/or external positions and that therefore are more vulnerable to financial market spillovers from the crisis, a two-notch downgrade was applied under the severe stress scenario. The remaining countries identified were subject to a one-notch downgrade under the moderate pessimistic scenario. A 1% positive/negative shift in the applied scenario will impact the PMA by approximately USD 2.4 million.

This has resulted in a PMA of USD 23.2m (2022: 22.7m).

Uncertainty PMA – the Bank had non-defaulted Russian exposures of USD 440m at 31 March 2023 (2022: USD 597m). Due to the ongoing Russia–Ukraine conflict, the Russian economy has taken a setback, resulting in an overall negative impact on Russian businesses. Considering continued geopolitical uncertainty around potential resolution of the conflict in Ukraine, increasing global economic sanctions against Russian people and corporates, and reciprocal tightening of restrictions on foreign-owned entities operating in Russia and inflexibility in payment remittance and the introduction of Type-C operations, the Bank acknowledged the heightened risks through assessment of PMAs on Russia exposures by calculating the risk of these defaulting within one year using different scenarios. A 1% positive/negative shift in the applied scenario will impact the PMA by approximately USD 2.4 million.

An uncertainty overlay for these names of USD 146.3m has been included as of 31 March 2023 (2022: 45.2m).

Post-model adjustments 31 March 2022

In addition to the two PMAs outlined above, as at 31 March 2022, the Bank also applied a PMA that considered the impact that the geopolitical situation at that time would have on the economy.

Condition of economy PMA – The credit cycle index (CCI) captures the macroeconomic impact on the probability of customers migrating to different credit grades, including the possibility of default over time, and as a result has a significant impact on the ECL outcomes.

This PMA was applied to address uncertainty in the economic forecasts as at 31 March 2022, and to address sensitivity of the models to the starting point CCI. The CCI was derived as part of the macroeconomic forecasts as at 31 March 2022.

As such, a revised CCI was estimated as at 31 March 2022 based on historic data and views of internal and external economists.

The result is that a PMA of USD 78.9m was included in the ECL as of March 2022.

Due to enhancements of the credit models that have addressed their sensitivity to CCI, this PMA has been fully released during the year ended 31 March 2023.

Maximum exposure to credit risk

The table below shows the maximum exposure to credit risk for the components of the statement of financial position, including derivatives. The maximum exposure is shown gross and does not take into account collateral or other credit enhancements.

	2023 USDm	2022 USDm
Cash and balances at central banks	**25,880.0**	25,255.4
Settlement balances	**115.5**	96.9
Loans and advances to banks	**3,223.6**	3,988.6
Loans and advances to customers	**17,712.7**	19,942.6
Reverse repurchase agreements	**1,266.9**	1,197.9
Investment securities	**1,045.1**	1,009.2
Derivative assets	**2,085.6**	1,430.4
	51,329.4	**52,921.0**
Guarantees and letters of credit	**3,353.9**	3,413.3
Commitments	**12,837.5**	15,194.9
	16,191.4	**18,608.2**
Total	**67,520.8**	**71,529.2**

Cash and balances with central banks comprises current and short-term deposits with the Bank of England of USD 11,452.4m (2022: USD 14,716.4m) and the Banque de France of USD 14,427.6m (2022: USD 10,539.0m).

Collateral held

Whilst the Bank's corporate lending is at times secured by fixed and floating charges on the assets of borrowers, the only collateral which is valued on a continuous basis is collateral in the form of cash and bonds. The value of this collateral held by the Bank, including collateral held against reverse repurchase agreements and against intra-group positions for large exposure purposes, was USD 5,237.0m (2022: USD 6,639.3m). This collateral is held against loans and advances to banks and customers, and reverse repurchase agreements of USD 3,137.2m (2022: USD 5,753.8m) and derivative assets of USD 772.4m (2022: USD 885.5m). There are no restrictions on re-pledging the collateral held against reverse repurchase agreements.

Estimates of the fair value of the collateral held are made when a loan is individually assessed for impairment. Collateral takes various forms and the value of this security will vary over time and is dependent on the types of asset and the jurisdiction of the borrowers as well as the ability to dispose of the collateral.

The Bank's estimate of the fair value of different types of collateral and other credit enhancements held as security against loans to customers that are individually impaired is USD 289.7m (2022: USD 383.5m).

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Credit quality and stage per class of financial asset

The following tables show the gross exposure and related impairments allowance by stage and grading as of 31 March 2023 and 31 March 2022.

As at 31 March 2023	Internal grading	Gross exposure Stage 1 USDm	Gross exposure Stage 2 USDm	Gross exposure Stage 3 USDm	Gross exposure Total USDm	ECL Stage 1 USDm	ECL Stage 2 USDm	ECL Stage 3 USDm	ECL Total USDm	Net exposure USDm
Cash and balances at central banks at amortised cost										
Normal borrowers	1-6	25,880.0	–	–	25,880.0	–	–	–	–	25,880.0
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8-10	–	–	–	–	–	–	–	–	–
Total		**25,880.0**	**–**	**–**	**25,880.0**	**–**	**–**	**–**	**–**	**25,880.0**
Settlement balances										
Normal borrowers	1-6	115.1	0.4	–	115.5	–	–	–	–	115.5
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8-10	–	–	–	–	–	–	–	–	–
Total		**115.1**	**0.4**	**–**	**115.5**	**–**	**–**	**–**	**–**	**115.5**
Loans and advances to banks at amortised cost										
Normal borrowers	1-6	3,003.6	256.0	–	3,259.6	1.9	34.1	–	36.0	3,223.6
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8-10	–	–	–	–	–	–	–	–	–
Total		**3,003.6**	**256.0**	**–**	**3,259.6**	**1.9**	**34.1**	**–**	**36.0**	**3,223.6**
Loans and advances to customers at amortised cost										
Normal borrowers	1-6	14,384.5	2,497.0	–	16,881.5	17.1	36.2	–	53.3	16,828.2
Borrowers requiring caution	7A, 7B	–	651.3	–	651.3	–	141.0	–	141.0	510.3
Substandard borrowers and below	7R, 8-10	–	–	396.7	396.7	–	–	22.5	22.5	374.2
Total		**14,384.5**	**3,148.3**	**396.7**	**17,929.5**	**17.1**	**177.2**	**22.5**	**216.8**	**17,712.7**
Investment securities at amortised cost										
Normal borrowers	1-6	29.3	–	–	29.3	–	–	–	–	29.3
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8-10	–	–	–	–	–	–	–	–	–
Total		**29.3**	**–**	**–**	**29.3**	**–**	**–**	**–**	**–**	**29.3**
Investment securities at FVOCI										
Normal borrowers	1-6	997.0	–	–	997.0	–	–	–	–	997.0
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8-10	–	–	–	–	–	–	–	–	–
Total		**997.0**	**–**	**–**	**997.0**	**–**	**–**	**–**	**–**	**997.0**
Off-balance sheet loans and commitments and financial guarantee contracts										
Normal borrowers	1-6	9,212.9	6,865.9	–	16,078.8	7.0	3.0	–	10.0	16,068.8
Borrowers requiring caution	7A, 7B	–	85.1	–	85.1	–	1.4	–	1.4	83.7
Substandard borrowers and below	7R, 8-10	–	–	27.5	27.5	–	–	0.6	0.6	26.9
Total		**9,212.9**	**6,951.0**	**27.5**	**16,191.4**	**7.0**	**4.4**	**0.6**	**12.0**	**16,179.4**

In addition to the ECL disclosed above, there is 0.3m ECL in relation to other financial assets.

As at 31 March 2022	Internal grading	Gross exposure Stage 1 USDm	Gross exposure Stage 2 USDm	Gross exposure Stage 3 USDm	Gross exposure Total USDm	ECL Stage 1 USDm	ECL Stage 2 USDm	ECL Stage 3 USDm	ECL Total USDm	Net exposure USDm
Cash and balances at central banks at amortised cost										
Normal borrowers	1–6	25,255.4	–	–	25,255.4	–	–	–	–	25,255.4
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8–10	–	–	–	–	–	–	–	–	–
Total		**25,255.4**	**–**	**–**	**25,255.4**	**–**	**–**	**–**	**–**	**25,255.4**
Settlement balances										
Normal borrowers	1–6	96.2	0.7	–	96.9	–	–	–	–	96.9
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8–10	–	–	–	–	–	–	–	–	–
Total		**96.2**	**0.7**	**–**	**96.9**	**–**	**–**	**–**	**–**	**96.9**
Loans and advances to banks at amortised cost										
Normal borrowers	1–6	3,372.6	623.4	–	3,996.0	0.7	6.7	–	7.4	3,988.6
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8–10	–	–	–	–	–	–	–	–	–
Total		**3,372.6**	**623.4**	**–**	**3,996.0**	**0.7**	**6.7**	**–**	**7.4**	**3,988.6**
Loans and advances to customers at amortised cost										
Normal borrowers	1–6	17,931.0	1,006.5	–	18,937.5	66.6	53.0	–	119.6	18,817.9
Borrowers requiring caution	7A, 7B	–	754.9	–	754.9	–	77.0	–	77.0	677.9
Substandard borrowers and below	7R, 8–10	–	–	492.6	492.6	–	–	45.8	45.8	446.8
Total		**17,931.0**	**1,761.4**	**492.6**	**20,185.0**	**66.6**	**130.0**	**45.8**	**242.4**	**19,942.6**
Investment securities at amortised cost										
Normal borrowers	1–6	65.4	–	–	65.4	–	–	–	–	65.4
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8–10	–	–	–	–	–	–	–	–	–
Total		**65.4**	**–**	**–**	**65.4**	**–**	**–**	**–**	**–**	**65.4**
Investment securities at FVOCI										
Normal borrowers	1–6	925.7	–	–	925.7	–	–	–	–	925.7
Borrowers requiring caution	7A, 7B	–	–	–	–	–	–	–	–	–
Substandard borrowers and below	7R, 8–10	–	–	–	–	–	–	–	–	–
Total		**925.7**	**–**	**–**	**925.7**	**–**	**–**	**–**	**–**	**925.7**
Off-balance sheet loans and commitments and financial guarantee contracts										
Normal borrowers	1–6	17,499.0	855.4	–	18,354.4	6.0	15.9	–	21.9	18,332.5
Borrowers requiring caution	7A, 7B	–	165.0	–	165.0	–	9.7	–	9.7	155.3
Substandard borrowers and below	7R, 8–10	–	–	88.8	88.8	–	–	2.9	2.9	85.9
Total		**17,499.0**	**1,020.4**	**88.8**	**18,608.2**	**6.0**	**25.6**	**2.9**	**34.5**	**18,573.7**

In addition to the ECL disclosed above, there is USD nil ECL in relation to other financial assets.

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Balance sheet credit quality

The following tables show the balance sheet by PD range as used in the ECL models.

	PD Range				PD Range			
As at 31 March 2023	**0.0% to < 3.7% USDm**	**3.7% to < 23.4% USDm**	**23.4% to 100% USDm**	**Total USDm**	**0.0% to < 3.7% %**	**3.7% to < 23.4% %**	**23.4% to 100% %**	**Total %**
Cash and balances at central banks at amortised cost	**25,880.0**	**–**	**–**	**25,880.0**	**100%**	**–**	**–**	**100%**
Settlement balances	**115.5**	**–**	**–**	**115.5**	**100%**	**–**	**–**	**100%**
Loans and advances to banks at amortised cost	**3,223.6**	**–**	**–**	**3,223.6**	**100%**	**–**	**–**	**100%**
Loans and advances to customers at amortised cost	**16,828.2**	**510.3**	**374.2**	**17,712.7**	**95%**	**3%**	**2%**	**100%**
Investment securities at amortised cost	**29.3**	**–**	**–**	**29.3**	**100%**	**–**	**–**	**100%**
Investment securities at FVOCI	**997.0**	**–**	**–**	**997.0**	**100%**	**–**	**–**	**100%**
Off-balance sheet loans and commitments and financial guarantee contracts	**16068.8**	**83.7**	**26.9**	**16179.4**	**99%**	**1%**	**–**	**100%**

	PD Range				PD Range			
As at 31 March 2022	0.0% to < 3.7% USDm	3.7% to < 23.4% USDm	23.4% to 100% USDm	Total USDm	0.0% to < 3.7% %	3.7% to < 23.4% %	23.4% to 100% %	Total %
Cash and balances at central banks at amortised cost	25,255.4	–	–	25,255.4	100%	–	–	100%
Settlement balances	96.9	–	–	96.9	100%	–	–	100%
Loans and advances to banks at amortised cost	3,988.6	–	–	3,988.6	100%	–	–	100%
Loans and advances to customers at amortised cost	18,817.9	677.9	446.8	19,942.6	94%	4%	2%	100%
Investment securities at amortised cost	65.4	–	–	65.4	100%	–	–	100%
Investment securities at FVOCI	925.7	–	–	925.7	100%	–	–	100%
Off-balance sheet loans and commitments and financial guarantee contracts	18,332.4	155.4	85.9	18,573.7	99%	1%	–	100%

Movement in impairment provisions

The following tables present a reconciliation of the opening to closing balance of the exposure and impairment allowance for financial assets at amortised cost. Transfers between stages in the tables have been reflected as if they had taken place at the beginning of the year. The movements are measured over a 12-month period.

Financial assets at amortised cost

At 31 March 2023	Gross exposure Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	**47,598.7**	**2,385.5**	**492.6**	**50,476.8**
Transfers from Stage 1 to 2	**(1,521.5)**	**1,521.5**	**–**	**–**
Transfers from Stage 2 to 1	**328.0**	**(328.0)**	**–**	**–**
Transfers to Stage 3	**(27.6)**	**–**	**27.6**	**–**
Transfers from Stage 3	**–**	**–**	**–**	**–**
Net drawdowns and movements due to exposure and risk parameter changes	**4,116.9**	**356.4**	**(65.5)**	**4,407.8**
Financial assets derecognised	**(6,085.1)**	**(530.7)**	**(58.0)**	**(6,673.8)**
Write-offs	**–**	**–**	**–**	**–**
Balance at end of year	**44,409.4**	**3,404.7**	**396.7**	**48,210.8**

At 31 March 2023	Impairment allowance Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	**67.3**	**136.7**	**45.8**	**249.8**
Transfers from Stage 1 to 2	**(0.7)**	**0.7**	**–**	**–**
Transfers from Stage 2 to 1	**0.6**	**(0.6)**	**–**	**–**
Transfers to Stage 3	**–**	**–**	**–**	**–**
Transfers from Stage 3	**–**	**–**	**–**	**–**
Net drawdowns and movements due to exposure and risk parameter changes	**(45.2)**	**76.4**	**(0.8)**	**30.4**
Financial assets derecognised	**(2.7)**	**(1.9)**	**(22.5)**	**(27.1)**
Write-offs	**–**	**–**	**–**	**–**
Balance at end of year	**19.3**	**211.3**	**22.5**	**253.1**

The above provisions and movements thereon relate to loans and advances to banks and customers.

The movement in gross exposure between the beginning and the end of the period relates to origination and derecognition in the normal course of business with no major movements arising as a result of modification.

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

At 31 March 2022	Gross exposure Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	46,288.7	3,097.8	526.5	49,913.0
Transfers from Stage 1 to 2	(1,096.7)	1,096.7	–	–
Transfers from Stage 2 to 1	551.2	(551.2)	–	–
Transfers to Stage 3	(36.1)	(44.9)	81.0	–
Transfers from Stage 3	–	16.7	(16.7)	–
Net drawdowns and movements due to exposure and risk parameter changes	4,801.9	(332.1)	(24.6)	4,445.2
Financial assets derecognised	(3,788.4)	(897.5)	(61.5)	(4,747.4)
Write-offs	–	–	(12.1)	(12.1)
Balance at end of year	**47,598.7**	**2,385.5**	**492.6**	**50,476.8**

At 31 March 2022	Impairment allowance Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	34.6	108.2	56.2	199.0
Transfers from Stage 1 to 2	(1.4)	1.4	–	–
Transfers from Stage 2 to 1	21.8	(21.8)	–	–
Transfers to Stage 3	(0.2)	(1.9)	2.1	–
Transfers from Stage 3	–	–	–	–
Net drawdowns and movements due to exposure and risk parameter changes	19.4	59.5	13.7	92.6
Financial assets derecognised	(6.9)	(8.7)	(14.1)	(29.7)
Write-offs	–	–	(12.1)	(12.1)
Balance at end of year	**67.3**	**136.7**	**45.8**	**249.8**

The following tables present a reconciliation of the opening to closing balance of the exposure and impairment allowance for loan commitments and financial guarantees.

Loan commitments and financial guarantees

At 31 March 2023	**Gross exposure Stage 1 USDm**	**Stage 2 USDm**	**Stage 3 USDm**	**Total USDm**
Balance at beginning of year	**17,499.0**	**1,020.4**	**88.8**	**18,608.2**
Transfers from Stage 1 to Stage 2	**(1,208.6)**	**1,208.6**	**–**	**–**
Transfers from Stage 2 to Stage 1	**19.6**	**(19.6)**	**–**	**–**
Transfers to Stage 3	**–**	**–**	**–**	**–**
Transfers from Stage 3	**–**	**19.0**	**(19.0)**	**–**
New drawdowns, net remeasurement and movements due to exposure and risk parameter changes	**(7,097.1)**	**4,722.6**	**(42.3)**	**(2,416.8)**
Balance at end of year	**9,212.9**	**6,951.0**	**27.5**	**16,191.4**

At 31 March 2023	Impairment allowance Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	6.0	25.6	2.9	34.5
Transfers from Stage 1 to Stage 2	(0.2)	0.2	–	–
Transfers from Stage 2 to Stage 1	0.2	(0.2)	–	–
Transfers to Stage 3	–	–	–	–
Transfers from Stage 3	–	–	–	–
New drawdowns, net remeasurement and movements due to exposure and risk parameter changes	1.0	(21.2)	(2.3)	(22.5)
Balance at end of year	**7.0**	**4.4**	**0.6**	**12.0**

At 31 March 2022	Gross exposure Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	14,611.5	897.9	96.4	15,605.8
Transfers from Stage 1 to Stage 2	(397.7)	397.7	–	–
Transfers from Stage 2 to Stage 1	196.7	(196.7)	–	–
Transfers to Stage 3	(2.7)	(8.4)	11.1	–
Transfers from Stage 3	–	0.4	(0.4)	–
New drawdowns, net remeasurement and movements due to exposure and risk parameter changes	3,091.2	(70.5)	(18.3)	3,002.4
Balance at end of year	**17,499.0**	**1,020.4**	**88.8**	**18,608.2**

At 31 March 2022	Impairment allowance Stage 1 USDm	Stage 2 USDm	Stage 3 USDm	Total USDm
Balance at beginning of year	11.8	9.1	0.3	21.2
Transfers from Stage 1 to Stage 2	(5.7)	5.7	–	–
Transfers from Stage 2 to Stage 1	2.6	(2.6)	–	–
Transfers to Stage 3	–	(2.0)	2.0	–
Transfers from Stage 3	–	–	–	–
New drawdowns, net remeasurement and movements due to exposure and risk parameter changes	(2.7)	15.4	0.6	13.3
Balance at end of year	**6.0**	**25.6**	**2.9**	**34.5**

Reconciliation of ECL movement to impairment charge for the period

	2023 USDm	2022 USDm
ECL movements since beginning of the period	54.7	94.0
Effect of disposals	(20.3)	(14.4)
Loss on disposal of impaired assets	19.0	16.4
Recovery of amounts previously written off	(4.4)	–
Foreign exchange and other movements	(1.3)	(0.2)
Impairment charge for the period	**47.7**	**95.8**

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Coverage ratios

The tables below show the coverage ratio as of 31 March 2023 and 31 March 2022.

As at 31 March 2023	Stage 1 %	Stage 2 %	Stage 3 %	Total %
Loans and advances to banks at amortised cost	0.06	13.29	–	1.10
Loans and advances to customers at amortised cost	0.12	5.64	5.68	1.21
Off-balance sheet loan commitments and financial guarantee contracts	0.08	0.06	2.29	0.07
Total	**0.10**	**2.08**	**5.46**	**0.71**

As at 31 March 2022	Stage 1 %	Stage 2 %	Stage 3 %	Total %
Loans and advances to banks at amortised cost	0.02	1.10	–	0.19
Loans and advances to customers at amortised cost	0.37	7.38	9.29	1.20
Off-balance sheet loan commitments and financial guarantee contracts	0.03	2.51	3.31	0.19
Total	**0.19**	**4.77**	**8.38**	**0.66**

The coverage ratio has increased in the year. This is largely due to an increase in the uncertainty post-model adjustment relating to Stage 2 assets classified as loans and advances to banks.

Macroeconomic variables and scenario weightings

Macroeconomic scenarios

The Bank has used a four-scenario model to calculate ECL at year-end. The base case forecast has been sourced externally and two downside scenarios and one upside scenario have been derived. An overview of the four scenarios used at the year-end is as follows:

Optimistic scenario – produced internally using in an in-house scenario generator. Assumes:

- The Russia–Ukraine conflict ends in 2023. Ceasefire agreement reached between Russia and Ukraine.
- This boosts consumer confidence and eases the squeeze on household real incomes, supporting consumption.
- Reduced uncertainty over the outlook increases demand for domestic and foreign investments for both UK and EU countries.
- Industrial strike action subsides as inflation falls and cost of living concerns diminish.

Base scenario – sourced externally. Assumes:

- The Russia–Ukraine military conflict remains a key risk for UK and EU countries, but the conflict does not escalate.
- Inflation peaked in 2022 and is expected to moderate in 2023-24 as supply and demand rebalance, driven in part by central bank monetary policy adjustments.
- A return of inflation to central bank targets is forecast by 2025.
- Industrial strike actions are occurring, but wage-price spirals are not expected as inflation is set to moderate, while inflation expectations are assumed to remain well anchored given monetary policy tightening.
- Despite the ongoing squeeze on household real incomes and consumer spending, the base forecasts do not incorporate a severe recession in 2023. Policy rate reductions are forecast from 2024.

Moderate pessimistic scenario – produced internally. Assumes:

- Russia–Ukraine conflict shows no signs of ending.
- Western countries are providing more arms to support Ukraine but still limited to a two-country war and not escalating to NATO level.
- Inflation increases and financial conditions tighten significantly further, consumers get squeezed and the cost-of-living crisis deepens as energy prices increase again.
- The introduction of restrictions to address energy supply shortages hits the industrial sector.
- Frequent industrial strike actions become more widespread in the UK and EU economies, hindering economic growth, with upward pressure on labour costs eroding competitiveness.

Severe pessimistic scenario – produced internally. The forecast for this scenario is in line with the Bank's ICAAP stress test and its severity has been benchmarked to those from the European Banking Authority (EBA) and Oxford Economics. Assumes:

- The Russia–Ukraine conflict escalates in late 2023, with expanding NATO membership (Sweden, Finland) leading to renewed aggression from Russia.
- UK and Eurozone in deep recession in early 2024 as inflation spirals. ECB and BOE respond by significantly increasing interest rates.
- Despite the introduction of government support for consumers and businesses, the continued cost-of-living crisis deepens.
- Social unrest, severe and prolonged industrial action and public demonstrations; in Europe, workers demand higher wages. UK public infrastructure is disrupted due to strikes.
- Some major UK and European banks are downgraded, and the possibility of a significant default becomes a major concern.

Scenario weightings

The Bank's ECL scenario weighting methodology is based on statistical modelling taking into consideration the average value of the three-year forecasts. To determine the weights for alternative scenarios, the Bank computes a three-year forecast average for each macroeconomic parameter, compares it to its historical values and identifies the percentile that it is closest to. The final scenario percentile is the average percentile across all parameters for each scenario. The base weight is 100% less the sum of alternative weights. The scenario weights are reviewed internally and by external economists.

The tables below show the probability weightings applied to each scenario and the key macroeconomic variables by scenario used in the ECL calculation.

	Scenario probability weighting			
	Severe pessimistic %	**Moderate pessimistic %**	**Base %**	**Optimistic %**
Scenario probability weightings as at 31 March 2023	**18%**	**26%**	**46%**	**10%**

	Scenario probability weighting			
	Severe pessimistic %	Moderate pessimistic %	Base %	Optimistic %
Revised scenario probability weightings after taking into account the COVID-19 pandemic as at 31 March 2022	13	24	46	17

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

As at 31 March 2023		Key macroeconomic variables Severe pessimistic %	Moderate pessimistic %	Base %	Optimistic %
Economic and Monetary Union GDP Real[1]	2023	**-4.2%**	**-2.2%**	**0.5%**	**2.5%**
	2024	**-3.6%**	**-1.6%**	**1.4%**	**4.0%**
	2025	**0.9%**	**1.0%**	**1.9%**	**3.0%**
	2026	**1.1%**	**0.8%**	**1.6%**	**2.3%**
Economic and Monetary Union Equity[2]	2023	**-22.9%**	**-12.3%**	**-3.2%**	**10.4%**
	2024	**-20.6%**	**-13.4%**	**-1.0%**	**26 4%**
	2025	**-7.1%**	**-4.4%**	**-1.2%**	**16.8%**
	2026	**1.2%**	**0.8%**	**0.7%**	**5.7%**
United Kingdom GDP Real[3]	2023	**-4 9%**	**-2.9%**	**-0.4%**	**3.0%**
	2024	**-3.4%**	**-1.5%**	**0.6%**	**3.5%**
	2025	**0.3%**	**0.3%**	**1.3%**	**3.0%**
	2026	**1.4%**	**1.6%**	**1.5%**	**2.2%**
United Kingdom Equity[4]	2023	**-22.0%**	**-9 5%**	**1.0%**	**13.2%**
	2024	**-19.3%**	**-10 8%**	**0.7%**	**24.7%**
	2025	**-6.4%**	**-1.8%**	**0.6%**	**15 9%**
	2026	**1.7%**	**1.2%**	**1.6%**	**4.6%**
Japan Nominal GDP[5]	2023	**0.4%**	**0.9%**	**1.8%**	**1.9%**
	2024	**1.8%**	**1.9%**	**3.6%**	**4.0%**
	2025	**3.0%**	**3.4%**	**3.6%**	**3 9%**
	2026	**3.0%**	**2.9%**	**3.2%**	**3.3%**

1 Year-on-year percentage change.
2 Year-on year percentage change, lagged by one quarter.
3 Year-on year percentage change.
4 Year-on-year percentage change, lagged by one quarter.
5 Four-quarter GBP average year-on-year percentage change.

As at 31 March 2022		Key macroeconomic variables Severe pessimistic %	Moderate pessimistic %	Base %	Optimistic %
EMU Consumer Price Index[1]	2022	-2.9	-2.2	-1.5	-1.1
	2023	0.9	0.5	0.1	0.1
	2024	–	-0.2	-0.2	-0.2
EMU nominal GDP[2]	2022	0.1	0.1	0.2	0.1
	2023	-0.1	–	0.1	-0.1
	2024	–	–	-0.1	-0.1
EMU interest rate, short term[3]	2022	1.5	1.0	0.5	0.4
	2023	-1.2	-0.7	-0.2	-0.2
	2024	–	–	–	–
UK unemployment rate[4]	2022	-0.1	-0.1	–	-0.1
	2023	-0.1	–	–	-0.1
	2024	–	-0.1	-0.1	-0.1
UK interest rate, short term[5]	2022	0.3	0.2	0.2	0.8
	2023	0.2	0.5	0.8	0.8
	2024	0.1	0.7	1.2	1.1
Japan GDP nominal financial year year-on-year growth[6]	2022	3.3	3.3	4.2	5.4
	2023	0.8	0.8	1.2	2.3
	2024	1.6	1.6	1.9	2.9

1 Year-on-year percentage change, forecast quarter on quarter.
2 Year-on-year change, forecast quarter on quarter.
3 Year-on-year change, forecast quarter on quarter lagged by one quarter.
4 Year-on-year change, forecast quarter on quarter.
5 Four-quarter average GBP level year-on-year percentage change.

ECL sensitivity analysis

The measurement of ECL involves increased complexity and judgement, including estimation of probability of default (PD), loss given default (LGD), range of unbiased future economic scenarios, estimation of expected lives, estimation of exposure at default (EAD) and assessing significant increases in credit risk.

The table below shows the ECL assuming each scenario has been 100% weighted to show the impact of alternative scenarios.

At 31 March 2023 USDm	**Weighted ECL**	**Severe pessimistic**	**Moderate pessimistic**	**Base**	**Optimistic**
Original model results[1]	**81.4**	**125.2**	**99.0**	**63.6**	**38.1**

At 31 March 2022 USDm	Weighted ECL	Severe pessimistic	Moderate pessimistic	Base	Optimistic
Original model results[1]	40.4	55.6	45.8	36.9	30.7
Model results with revised CCI (condition of economy PMA)[2]	109.5	155.1	129.1	98.9	74.1

1 The above results do not include the impact of the post-model adjustments.

2 Includes outcome from condition of economy PMA. Further details can be found on page 106.

Credit risk by sector

The exposure by major industrial sectors can be analysed as follows:

31 March 2023 USDm	**Finance and insurance**	**Government and local authorities**	**Manufacturing**	**Wholesale and services**	**Other corporate exposures**	**Transport**	**Energy and infrastructure**	**Total**
Cash and balances at central banks	**25,880.0**	**–**	**–**	**–**	**–**	**–**	**–**	**25,880.0**
Settlement balances	**115.5**	**–**	**–**	**–**	**–**	**–**	**–**	**115.5**
Loans and advances to banks	**3,223.6**	**–**	**–**	**–**	**–**	**–**	**–**	**3,223.6**
Loans and advances to customers	**1,572.1**	**188.8**	**1,451.7**	**815.7**	**9,958.7**	**1,093.6**	**2,632.1**	**17,712.7**
Reverse repurchase agreements	**534.2**	**–**	**–**	**–**	**732.7**	**–**	**–**	**1,266.9**
Investment securities	**49.2**	**995.8**	**–**	**–**	**0.1**	**–**	**–**	**1,045.1**
Derivative assets	**1,543.3**	**0.8**	**203.9**	**6.6**	**314.0**	**15.7**	**1.3**	**2,085.6**
Total on-balance sheet	**32,917.9**	**1,185.4**	**1,655.6**	**822.3**	**11,005.5**	**1,109.3**	**2,633.4**	**51,329.4**
Commitments and guarantees	**976.7**	**45.6**	**2,373.1**	**3,272.2**	**9,523.8**	**–**	**–**	**16,191.4**
Total	**33,894.6**	**1,231.0**	**4,028.7**	**4,094.5**	**20,529.3**	**1,109.3**	**2,633.4**	**67,520.8**

31 March 2022 USDm	Finance and insurance	Government and local authorities	Manufacturing	Wholesale and services	Other corporate exposures	Transport	Energy and infrastructure	Total
Cash and balances at central banks	25,255.4	–	–	–	–	–	–	25,255.4
Settlement balances	96.9	–	–	–	–	–	–	96.9
Loans and advances to banks	3,988.6	–	–	–	–	–	–	3,988.6
Loans and advances to customers	2,207.3	1,328.3	1,695.8	1,250.8	9,873.4	1,079.4	2,507.6	19,942.6
Reverse repurchase agreements	1,197.9	–	–	–	–	–	–	1,197.9
Investment securities	84.7	924.5	–	–	–	–	–	1,009.2
Derivative assets	1,139.4	7.0	36.4	11.2	218.7	17.6	0.1	1,430.4
Total on-balance sheet	33,970.2	2,259.8	1,732.2	1,262.0	10,092.1	1,097.0	2,507.7	52,921.0
Commitments and guarantees	1,670.4	25.5	2,796.0	1,249.9	12,866.4	–	–	18,608.2
Total	35,640.6	2,285.3	4,528.2	2,511.9	22,958.5	1,097.0	2,507.7	71,529.2

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

The industry exposure classifications shown above follow the same categories as used in the Bank's Pillar 3 disclosures. Finance and insurance exposure includes USD 11,452.4m to the Bank of England (2022: USD 14,716.4m) and USD 14,427.6m to the Banque de France (2022: USD 10,539.0m).

Credit risk by location

The table below analyses the geographical spread of financial assets based on country of residence of the counterparty.

31 March 2023 USDm	United Kingdom	France	Other Europe	Eastern Europe	Japan	Middle East & Africa	Other countries	Total
Cash and balances at central banks	**11,452.4**	**14,427.6**	**–**	**–**	**–**	**–**	**–**	**25,880.0**
Settlement balances	**2.1**	**–**	**32.6**	**12.5**	**15.2**	**0.4**	**52.7**	**115.5**
Loans and advances to banks	**212.7**	**2.5**	**576.9**	**92.0**	**759.5**	**1,446.7**	**133.3**	**3,223.6**
Loans and advances to customers	**6,260.3**	**3,759.9**	**2,892.9**	**271.8**	**352.7**	**2,517.9**	**1,657.2**	**17,712.7**
Reverse repurchase agreements	**988.8**	**–**	**–**	**–**	**278.1**	**–**	**–**	**1,266.9**
Investment securities	**29.5**	**–**	**995.8**	**1.2**	**–**	**–**	**18.6**	**1,045.1**
Derivative assets	**1,092.8**	**243.8**	**691.7**	**–**	**43.6**	**–**	**13.7**	**2,085.6**
Total on-balance sheet	**20,038.6**	**18,433.8**	**5,189.9**	**377.5**	**1,449.1**	**3,965.0**	**1,875.5**	**51,329.4**
Commitments and guarantees	**5,227.9**	**7,211.4**	**1,676.9**	**343.5**	**313.5**	**668.9**	**749.3**	**16,191.4**
Total	**25,266.5**	**25,645.2**	**6,866.8**	**721.0**	**1,762.6**	**4,633.9**	**2,624.8**	**67,520.8**

31 March 2022 USDm	United Kingdom	France	Other Europe	Eastern Europe	Japan	Middle East & Africa	Other countries	Total
Cash and balances at central banks	14,716.4	10,539.0	–	–	–	–	–	25,255.4
Settlement balances	–	–	43.9	17.4	0.2	0.2	35.2	96.9
Loans and advances to banks	545.2	2.4	743.9	137.8	870.0	1,035.0	654.3	3,988.6
Loans and advances to customers	6,051.4	3,599.2	3,467.8	434.0	196.8	4,245.1	1,948.3	19,942.6
Reverse repurchase agreements	883.4	–	–	–	314.5	–	–	1,197.9
Investment securities	65.5	–	924.5	1.2	–	–	18.0	1,009.2
Derivative assets	709.3	52.9	561.9	–	2.1	–	104.2	1,430.4
Total on-balance sheet	22,971.2	14,193.5	5,742.0	590.4	1,383.6	5,280.3	2,760.0	52,921.0
Commitments and guarantees	5,241.4	8,557.6	1,843.5	294.5	251.2	1,448.2	971.8	18,608.2
Total	28,212.6	22,751.1	7,585.5	884.9	1,634.8	6,728.5	3,731.8	71,529.2

The geographical exposure classifications shown above follow the same categories as used in the Bank's Pillar 3 disclosures. The above disclosures are based on country of residence, whilst the Bank's Pillar 3 disclosures use country of risk. The figures reported include balances with the Bank of England and Banque de France as disclosed above.

(b) Market risk

Market risk is the risk that movements in interest rates, foreign exchange rates or stock prices will change the market value of financial products, leading to a loss.

The Board of Directors is ultimately responsible for ensuring that the level of market risk run by the Bank is in line with its risk appetite and business model.

The Bank uses a variety of matrices to measure and control market risk. One such tool is the use of Value at Risk (VaR). VaR is a measure of the maximum expected loss in a portfolio to a given degree of confidence over a specified period. The Bank uses a 99% confidence interval and a one-day time horizon. The Bank currently uses a historical simulation which is updated monthly to generate the VaR result using data from a four-year observation period. The Bank uses VaR to control market risk both on the Trading and Banking accounts on both a standalone and a consolidated basis. The Bank has in place an ongoing programme of back-testing and analysis for the VaR model. However, VaR is not a perfect tool for risk management and cannot provide an indication of the potential losses that may occur. The Bank therefore conducts a programme of stress testing using scenarios relevant to the current portfolio composition.

Interest rate risk on the Banking book is stressed by taking the basis point value (BPV) positions and stressing them by an average of 100 basis points (bp). In addition to this, a further 200bp parallel shift stress test is carried out (as per the Prudential Sourcebook for Banks, Building Societies and Investment Firms, section 2.3.8) as part of the ICAAP submission. Stress tests are also carried out on foreign exchange positions (assuming 17% appreciation and depreciation of each currency vs. USD).

Risk management for each category is augmented by employing suitable sensitivity limits such as BPV limits which measure the potential change in portfolio fair value for an instantaneous 0.01% shift in interest rates. Using the BPV, the Bank can examine the effects to income of movements in yields applied to the Banking and Trading portfolios.

The Bank's VaR exposures during the year were:

	To 31 March 2023				To 31 March 2022			
	Maximum USDm	**Minimum USDm**	**Average USDm**	**31 March USDm**	Maximum USDm	Minimum USDm	Average USDm	31 March USDm
Trading	**0.4**	**–**	**0.1**	**0.1**	0.3	–	0.1	0.2
Banking	**3.4**	**2.4**	**2.9**	**3.2**	3.7	2.6	3.2	2.8
Total	**3.5**	**2.4**	**2.9**	**3.4**	3.6	2.5	3.2	2.8

The income sensitivity table below reports the worst case of six possible yield curve shift scenarios averaging 100bp, including 'Steepening', 'Flattening' and 'Parallel' shifts, which comprises the Market Risk Stress Test.

Income sensitivity with respect to changes in interest rates:

	Banking book		**Trading book**	
	31 March 2023 USDm	31 March 2022 USDm	**31 March 2023 USDm**	31 March 2022 USDm
Profit and loss impact	**1.0**	0.1	**6.6**	8.6

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

(c) Liquidity risk

Liquidity risk is the risk that the Bank cannot meet its liabilities or unwind or settle its positions as they become due.

Analysis of liquidity risk

Contractual maturity of financial assets and liabilities form an important source of information used by management for the management of liquidity risk.

The table below provides details on the contractual maturity of financial assets and financial liabilities. Impairment provisions on loans and advances to banks and customers are included in the Up to 3 months column.

At 31 March 2023 USDm	Up to 3 months USDm	3 to 12 months USDm	1 to 5 years USDm	Over 5 years USDm	Total USDm
Assets					
Cash and balances at central banks	**25,880.0**	–	–	–	**25,880.0**
Settlement balances	**115.5**	–	–	–	**115.5**
Loans and advances to banks	**1,901.0**	**241.9**	**1,025.4**	**55.3**	**3,223.6**
Reverse repurchase agreements	**1,266.9**	–	–	–	**1,266.9**
Derivative assets	**743.1**	**679.3**	**655.7**	**7.5**	**2,085.6**
Loans and advances to customers	**4,196.9**	**1,367.4**	**7,596.3**	**4,552.1**	**17,712.7**
Investment securities	**833.7**	**211.4**	–	–	**1,045.1**
Total financial assets	**34,937.1**	**2,500.0**	**9,277.4**	**4,614.9**	**51,329.4**
Liabilities					
Deposits by banks	**13,667.8**	**932.9**	**10,388.8**	–	**24,989.5**
Customer accounts	**17,252.3**	**1,416.7**	–	–	**18,669.0**
Derivative liabilities	**714.4**	**561.0**	**597.0**	**4.9**	**1,877.3**
Debt securities in issue	**1,014.0**	**34.7**	–	–	**1,048.7**
Total financial liabilities	**32,648.5**	**2,945.3**	**10,985.8**	**4.9**	**46,584.5**
Cumulative gap financial assets less financial liabilities	**2,288.6**	**1,843.3**	**134.9**	**4,744.9**	**4,744.9**

At 31 March 2022 USDm	Up to 3 months USDm	3 to 12 months USDm	1 to 5 years USDm	Over 5 years USDm	Total USDm
Assets					
Cash and balances at central banks	25,255.4	–	–	–	25,255.4
Settlement balances	96.9	–	–	–	96.9
Loans and advances to banks	2,831.0	476.8	618.0	62.8	3,988.6
Reverse repurchase agreements	1,197.9	–	–	–	1,197.9
Derivative assets	605.7	496.7	302.6	25.4	1,430.4
Loans and advances to customers	4,981.8	1,847.8	8,244.2	4,868.8	19,942.6
Investment securities	734.2	275.0	–	–	1,009.2
Total financial assets	35,702.9	3,096.3	9,164.8	4,957.0	52,921.0
Liabilities					
Deposits by banks	14,298.4	1,324.8	10,753.7	–	26,376.9
Customer accounts	19,264.4	489.7	–	–	19,754.1
Derivative liabilities	543.9	463.5	293.0	22.2	1,322.6
Debt securities in issue	976.0	–	–	–	976.0
Total financial liabilities	35,082.7	2,278.0	11,046.7	22.2	48,429.6
Cumulative gap financial assets less financial liabilities	620.2	1,438.5	(443.4)	4,491.4	4,491.4

The table below shows the contractual maturity analysis of interest and principal balances for liabilities, issued financial guarantee contracts and unrecognised loan commitments.

Maturity of liabilities as at 31 March 2023	**Up to 3 months USDm**	**3 to 12 months USDm**	**1 to 5 years USDm**	**Over 5 years USDm**	**Total USDm**
Deposits by banks	**13,805.8**	**1,219.4**	**11,053.2**	**–**	**26,078.4**
Customer accounts	**17,357.3**	**1,452.9**	**–**	**–**	**18,810.2**
Debt securities in issue	**1,023.8**	**35.2**	**–**	**–**	**1,059.0**
Issued financial guarantee contracts	**1,118.5**	**1,732.5**	**501.0**	**2.0**	**3,354.0**
Unrecognised loan commitments	**68.3**	**1,044.3**	**9,390.4**	**1,764.5**	**12,267.5**
	33,373.7	**5,484.3**	**20,944.6**	**1,766.5**	**61,569.1**
Derivative liabilities	**744.4**	**595.6**	**570.3**	**1.3**	**1,911.6**
Total liabilities, issued guarantees and commitments	**34,118.1**	**6,079.9**	**21,514.9**	**1,767.8**	**63,480.7**

Maturity of liabilities as at 31 March 2022	Up to 3 months USDm	3 to 12 months USDm	1 to 5 years USDm	Over 5 years USDm	Total USDm
Deposits by banks	14,324.5	1,387.7	10,918.4	–	26,630.6
Customer accounts	19,276.9	491.9	–	–	19,768.8
Debt securities in issue	977.1	–	–	–	977.1
Issued financial guarantee contracts	1,076.8	1,875.8	457.9	2.8	3,413.3
Unrecognised loan commitments	272.4	1,979.2	10,428.9	1,952.5	14,633.0
	35,927.7	**5,734.6**	**21,805.2**	**1,955.3**	**65,422.8**
Derivative liabilities	581.0	444.7	273.9	23.0	1,322.6
Total liabilities, issued guarantees and commitments	**36,508.7**	**6,179.3**	**22,079.1**	**1,978.3**	**66,745.4**

(d) Interest rate benchmark reform

There have been no changes to the Bank's risk management strategies following the IBOR reform.

Following the financial crisis, the reform and replacement of benchmark interest rates such as IBOR have become a priority for global regulators. As a result, the UK's Financial Conduct Authority (FCA) and other global regulators instructed market participants to prepare for the cessation of most LIBOR rates after the end of 2021, and to adopt 'near risk-free rates' (RFRs). The Bank has significant exposure to IBORs on its financial instruments that will be reformed as part of this market-wide initiative.

The main risks to which the Bank is exposed as a result of IBOR reform are operational – for example, the renegotiation of loan contracts through bilateral negotiation with customers, updating of contractual terms, updating of systems that use IBOR curves and revision of operational controls related to the reform. Financial risk is predominantly limited to interest rate risk. The Bank continues to have loans referencing LIBOR which could become unrepresented; this will continually be monitored, but the liquidity risk arising from this is considered low. Further information on the way in which the Bank has engaged with customers on this matter can be found in the Section 172(1) Statement on page 55.

Notes to the financial statements For the year ended 31 March 2023 continued

4. Financial risk management continued

Non-derivative financial assets and loan commitments

The Bank's exposures on loans and advances to customers include GBP, USD, EUR and JPY LIBOR.

The alternative reference rate for Sterling LIBOR is the Sterling Overnight Index Average (SONIA) and for USD LIBOR is the Secured Overnight Financing Rate (SOFR). Changes to the contractual terms of financial assets referenced to LIBOR to incorporate new benchmark rates were not yet complete as at 31 March 2023. There are some contracts, known as 'tough legacy contracts', that may be difficult to transition from LIBORs to SONIA or SOFR. These tough legacy contracts are often part of more complex or structured transactions or arrangements. The FCA has authorised broad usage of synthetic LIBOR as a temporary solution for 'tough legacy contracts' for GBP and JPY. The Bank continues to monitor total contracts utilising synthetic LIBOR fallbacks and aims to remediate to RFRs as soon as possible.

The Bank monitors the progress of transition from IBORs to new benchmark rates by reviewing the total amounts of contracts that have yet to transition to an alternative benchmark rate and the amounts of such contracts that include a fallback clause. The Bank considers that a contract is not yet transitioned to an alternative benchmark rate when interest under the contract is referenced to a benchmark rate that is still subject to IBOR reform, even if it includes a fallback clause that deals with the cessation of the existing IBOR (referred to as an 'unreformed contract'). The Bank has in place detailed plans, processes and procedures to continue to transition contracts to alternative benchmark rates which will be completed in line with official sector expectations and milestones.

Derivatives and hedge accounting

The Bank uses derivatives for trading and risk management purposes (see note 13). Some of the derivatives held for risk management purposes are designated in hedging relationships. The interest rate swaps have floating rates that reference various IBORs. The Bank's derivative instruments are governed by International Swaps and Derivatives Association (ISDA) definitions.

ISDA has reviewed its definitions in light of IBOR reform and issued an IBOR fallbacks supplement on 23 October 2020. This sets out how the amendments to new alternative benchmark rates (e.g. SOFR, SONIA) in the ISDA definitions will be accomplished. The effect of the supplement is to create fallback provisions in derivatives that describe what floating rates will apply on the permanent discontinuation of certain key IBORs or on ISDA declaring a non-representative determination of an IBOR. The supplement is effective from 25 January 2021 and from that date, all new derivatives that reference the ISDA definitions will also include the fallbacks. Further information on the impact of IBOR reform on the Bank's hedge accounting is given in note 13.

The following table shows the Bank's exposure at the year-end to significant IBORs subject to reform that have yet to transition to risk-free rates.

At 31 March 2023	**Non-derivative financial assets at carrying value USDm**	**Non-derivative financial liabilities at carrying value USDm**	**Undrawn commitments USDm**	**Derivatives notional amount USDm**
GBP LIBOR	**3.8**	**115.1**	**–**	**–**
USD LIBOR	**2,422.8**	**632.6**	**2,500.0**	**533.9**
JPY LIBOR	**83.7**	**–**	**–**	**–**

At 31 March 2022	Non-derivative financial assets at carrying value USDm	Non-derivative financial liabilities at carrying value USDm	Undrawn commitments USDm	Derivatives notional amount USDm
GBP LIBOR	589.1	133.5	–	–
USD LIBOR	6,589.1	994.4	4,300.0	670.1
JPY LIBOR	123.3	–	–	–

The Bank's exposure risk management also includes the use of the Euro Interbank Offered Rate (EURIBOR). In July 2019, the Belgian Financial Services and Markets Authority granted authorisation with respect to EURIBOR under the European Union Benchmarks Regulation. This allows market participants to continue to use EURIBOR after 1 January 2020 for both existing and new contracts. The Bank expects that EURIBOR will continue to exist as a benchmark rate for the foreseeable future. The Bank does not anticipate changing the hedged risk to a different benchmark. For these reasons, the Bank does not consider its fair value or cash flow hedges of the EURIBOR benchmark interest rate to be directly affected by interest rate benchmark reform at 31 March 2023.

5. Fair value of financial instruments

The Bank's accounting policy on fair value measurements is disclosed in accounting policy 3(e) Financial Instruments – initial recognition and subsequent measurement.

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

- **Level 1:** Quoted market price (unadjusted) in an active market for an individual instrument.
- **Level 2:** Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- **Level 3:** Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments the Bank determines fair values using valuation techniques.

Valuation techniques include net present value and discounted value models, comparison to similar instruments for which observable market prices exist, Black-Scholes, and polynomial option pricing models and binomial valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index prices, and expected price volatilities and correlations. All observable data is taken directly from Bloomberg or Reuters screens. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date, which would have been determined by market participants acting at arm's length.

The Bank uses widely recognised models for determining the fair value of common and more simple financial instruments, such as interest rate and currency swaps that use only observable market data and require little management judgement and estimation. Observable prices and model inputs are usually available in the market for listed debt and equity securities, exchange-traded derivatives and simple over-the-counter derivatives. Availability of observable market prices and model inputs reduces the need for management judgement and estimation, and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets, and is prone to changes based on specific events and general conditions in the financial markets.

Notes to the financial statements For the year ended 31 March 2023 continued

5. Fair value of financial instruments continued

For some financial instruments at fair value through other comprehensive income, the Bank uses discounted cash flow models created internally and discounted cash flow models provided by external independent parties which are assessed internally to be acceptable for the purpose of valuation. Some or all of the significant inputs into these models may not be observable in the market, and are derived from market prices or rates or are estimated based on assumptions. Valuation models that employ significant unobservable inputs require a higher degree of management judgement and estimation in the determination of fair value. Management judgement and estimation are usually required for selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instrument being valued, determination of probability of counterparty default and prepayments, and selection of appropriate discount rates.

Fair value of financial instruments carried at fair value

The following table shows the Bank's financial assets and liabilities that are held at fair value by the level in the fair value hierarchy into which the fair value measurement is categorised:

At 31 March 2023 USDm	Level 1	Level 2	Level 3	Total fair value
Financial assets				
Loans and advances to banks	–	–	–	–
Loans and advances to customers	–	–	–	–
Derivative assets	–	**2,085.6**	–	**2,085.6**
Investment securities	–	**995.8**	**20.0**	**1,015.8**
Total assets	–	**3,081.4**	**20.0**	**3,101.4**
Financial liabilities				
Derivative liabilities	–	**1,877.3**	–	**1,877.3**
Total liabilities	–	**1,877.3**	–	**1,877.3**

There are no significant movements between level 1, level 2 or level 3.

At 31 March 2022 USDm	Level 1	Level 2	Level 3	Total fair value
Financial assets				
Loans and advances to banks	–	–	–	–
Loans and advances to customers	–	–	–	–
Derivative assets	–	1,430.4	–	1,430.4
Investment securities	–	924.5	19.3	943.8
Total assets	–	2,354.9	19.3	2,374.2
Financial liabilities				
Derivative liabilities	–	1,322.6	–	1,322.6
Total liabilities	–	1,322.6	–	1,322.6

Of the total movement in level 3 assets during the year of USD 0.7m (2022: USD 6.5m), USD 0.8m (2022: USD 2.1m) relates to gains through the profit and loss account, USD 1.9m (2022: USD 4.4m) relates to purchases and USD (2.0)m relates to settlements (2022: USD nil).

For assets and liabilities which are accounted at fair value under level 3, the valuations are primarily based on Fund Manager valuations and are based on reasonable estimates. Applying reasonable alternative valuations would not lead to a significantly different valuation.

Fair value of financial instruments carried at amortised cost

The following table summarises the fair value of financial assets and liabilities measured at amortised cost, by the level in the fair value hierarchy into which the fair value measurement is categorised:

31 March 2023 USDm	Level 1	Level 2	Level 3	Total fair value	Carrying value
Assets					
Cash and balances at central banks	–	25,880.0	–	25,880.0	25,880.0
Settlement balances	–	115.5	–	115.5	115.5
Loans and advances to banks	–	–	3,263.4	3,263.4	3,223.6
Loans and advances to customers	–	–	17,966.5	17,966.5	17,712.7
Reverse repurchase agreements	–	1,266.9	–	1,266.9	1,266.9
Investment securities	–	29.3	–	29.3	29.3
Liabilities					
Deposits by banks	–	25,012.1	–	25,012.1	24,989.5
Customer accounts	–	18,666.7	–	18,666.7	18,669.0
Debt securities in issue	–	1,048.7	–	1,048.7	1,048.7

31 March 2022 USDm	Level 1	Level 2	Level 3	Total fair value	Carrying value
Assets					
Cash and balances at central banks	–	25,255.4	–	25,255.4	25,255.4
Settlement balances	–	96.9	–	96.9	96.9
Loans and advances to banks	–	–	3,983.0	3,983.0	3,988.6
Loans and advances to customers	–	–	20,259.2	20,259.2	19,942.6
Reverse repurchase agreements	–	1,197.9	–	1,197.9	1,197.9
Investment securities	–	65.3	–	65.3	65.3
Liabilities					
Deposits by banks	–	26,383.4	–	26,383.4	26,376.9
Customer accounts	–	19,753.5	–	19,753.5	19,754.1
Debt securities in issue	–	976.0	–	976.0	976.0

There were no positions classified on inception as designated at fair value through profit and loss during the year.

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements.

Assets for which fair value approximates carrying value

For financial assets and financial liabilities that are liquid or have a short-term maturity (less than three months), it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits, savings accounts without a specific maturity, and variable rate financial instruments.

Fixed rate financial instruments

The fair values of fixed rate financial assets and liabilities carried at amortised cost not hedged through fair value hedges are estimated by comparing market interest rates on initial recognition with current market rates offered for similar financial instruments including any effect of changes in market credit spreads, where material. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit risk and maturity. The fair values of quoted debt instruments issued are calculated based on quoted market prices.

Notes to the financial statements For the year ended 31 March 2023 continued

6. Personnel and other expenses

	2023 USDm	2022 USDm
Salaries and bonuses	**272.7**	273.7
Compulsory social security obligations	**59.0**	64.4
Pension costs – contribution plans	**21.7**	21.4
Pension costs – defined benefit plans	**2.1**	3.3
Other staff costs	**17.7**	22.4
Total personnel costs	**373.2**	**385.2**
Operating lease payments	**5.5**	6.5
Other operating expenses	**195.8**	159.8
Total personnel and other costs	**574.6**	**551.5**
	No.	No.
Average number of front office department employees	**526**	515
Average number of support department employees	**1,055**	967
Average number of employees	**1,581**	**1,482**

Deferred shares bonus scheme

The Bank has in place a deferred bonus scheme for certain employees. Such employees receive part of their annual bonus as a deferred award comprising 50% in cash and 50% in a scheme pegged to the SMFG share price. Any deferred awards are dependent on future service and are awarded over periods up to eight years. As at the year-end, total deferred bonuses were USD 25.4m (2022: USD 31.1m).

7. Auditor's remuneration

	2023 USDm	2022 USDm
Fees payable to the Bank's auditor for the audit of Bank's annual accounts	**1.7**	1.8
Audit-related assurance services	**0.2**	0.5
	1.9	**2.3**

Audit-related assurance services includes worked performed in relation to the Group audit and interim review work of SMFG and various regulatory assurance services. Fees amounting to USD 1.0m (2022: USD 0.6m) were paid by SMBC and SMFG.

8. Directors' emoluments

	2023 USDm	2022 USDm
Directors' fees	**0.6**	0.6
Directors' emoluments (excluding fees)	**3.3**	3.6
Post-employment benefits	**0.1**	0.1
	4.0	**4.3**

The highest paid Director received emoluments of USD 1,053,118 (2022: USD 983,463).

One Director belonged to the Bank's defined contribution pension scheme, with the Bank paying contributions of USD 122,608 (2022: Two directors with contributions of USD USD 114,199) in the year. These amounts are included within the Directors' emoluments figures above. Four Directors received a bonus (2022: Five Directors) and part of this was subject to a deferral period.

Three employees of the parent company were Directors during the year and received remuneration from the Bank as they were subject to secondment agreements. Further information on the Directors can be found in the Strategic Report on pages 41 to 43. The changes to the Directors in the year can be found in the Directors' Report on page 70.

9. Pension costs

Accounting for pension and other post-retirement benefits

The Bank operates, for the majority of employees, a defined contribution scheme. Contributions are charged to profit and loss as they become payable in accordance with the rules of the scheme.

A defined benefit scheme, the Sumitomo Mitsui Banking Corporation Europe Limited Pension Scheme, is provided to a small number of staff. The assets of the scheme are held separately from the assets of the Bank and are administered by trustees. This scheme is closed to new members.

The cost of providing benefits under the defined benefit scheme is determined using the projected-unit credit method, which attributes entitlement to benefits to the current period (to determine current service cost) and to the current and prior periods (to determine the present value of defined benefit obligations) and is based on actuarial advice. Past service costs are recognised in profit and loss as operating expenses.

The interest element of the defined benefit cost represents the change in present value of scheme obligations arising from the passage of time, and is determined by applying the discount rate to the opening present value of the benefit obligation, taking into account material changes in the obligation during the year. The expected return on plan assets is based on an assessment, made at the beginning of the year, of long-term market returns on scheme assets, adjusted for the effect on the fair value of plan assets of contributions received and benefits paid during the year. The differences between the expected return on plan assets and the interest costs are recognised in profit and loss as other finance income or expense.

Actuarial gains and losses are recognised in full in other comprehensive income in the period in which they occur.

The defined benefit pension asset or liability in the statement of financial position comprises the total for the plan of the present value of the defined benefit obligation (using a discount rate based on high quality corporate bonds that have been rated at AA or equivalent status), less any past service cost not yet recognised and less the fair value of plan assets out of which the obligations are to be settled directly. The fair value of the assets held is based on quoted prices or observable inputs for the underlying investments. The value of any net pension asset recognised is limited to the amount that may be recovered either through reduced contributions or agreed refunds from the scheme.

A triennial funding valuation of the defined benefit scheme was undertaken with an effective date of 31 December 2020 and updated to 31 March 2023 by a qualified independent Actuary. The scheme is funded and, per the triennial valuation, there was no deficit in the pension plan.

The principal actuarial assumptions as at 31 March (expressed as weighted averages) were as follows:

	2023	2022
Discount rate	**4.8%**	2.7%
Future salary increase (weighted average)	**3.4%**	3.8%
Future pension increase	**3.2%**	3.5%
Inflation assumption (CPI)	**2.4%**	2.8%

As at 31 March 2020, an assumption for CPI inflation of 1.0% per annum below the Retail Price Index (RPI) assumption was used. As a result of the announcement by the Chancellor of the Exchequer in November 2020 that RPI will be aligned with Consumer Prices Index including owner occupiers' housing costs (CPIH) from 2030, a CPI assumption of 0.9% per annum less than RPI has been used as at 31 March 2023 (31 March 2022: 0.9% per annum less than RPI).

The discount rate applied as at 31 March 2023 reflects prevailing market yields for high quality bonds, and has risen in the year in line with macroeconomic conditions. This has the impact of lowering liability and asset valuations, and hence a net impact through Actuarial gains/(losses) on defined benefit scheme of USD 17.7m

Notes to the financial statements For the year ended 31 March 2023 continued

9. Pension costs continued

The underlying mortality assumption is based upon the standard table known as S3PA Light on year of birth usage with CMI 2021 future improvement factors with a long-term annual rate of future improvement of 1.0% p.a. (31 March 2020: same except CMI 2020). This results in the following life expectancies:

– Male aged 65 now has a life expectancy of 23.1 years from retirement (previously 23.0 years).
– Female aged 65 now has a life expectancy of 24.6 years from retirement (previously 24.6 years).

Cash flow data is used to estimate the amount which the scheme needs to reimburse the Bank at the end of the year. This reimbursement is in respect of benefit payments which the Bank has paid on behalf of the scheme since 31 December 2020.

The following table shows a reconciliation from the opening balances to the closing balances for the net defined benefit liability (asset) and its components:

	Defined benefit obligations		Fair value of plan assets		Net defined benefit (liability)/asset	
	2023 USDm	2022 USDm	2023 USDm	2022 USDm	2023 USDm	2022 USDm
Balance at beginning of year	**185.4**	227.2	**245.8**	260.3	**60.4**	33.1
Included in profit or loss						
Current service cost	**1.5**	1.8	**–**	–	**(1.5)**	(1.8)
Past service cost	**–**	–	**–**	–	**–**	–
Interest expense	**4.7**	4.3	**–**	–	**(4.7)**	(4.3)
Interest income	**–**	–	**6.2**	4.9	**6.2**	4.9
Effect of movements in exchange rates	**(10.5)**	(10.7)	**(13.8)**	(12.3)	**(3.3)**	(1.6)
	(4.3)	**(4.6)**	**(7.6)**	**(7.4)**	**(3.3)**	**(2.8)**
Included in other comprehensive income						
Actuarial (loss)/gain arising from:						
Financials	**(50.1)**	(24.6)	**–**	–	**50.1**	24.6
Demographic	**–**	–	**–**	–	**–**	–
Experience	**6.6**	(7.4)	**–**	–	**(6.6)**	7.4
Return on plan assets excluding interest income	**–**	–	**(61.2)**	(4.4)	**(61.2)**	(4.4)
	(43.5)	**(32.0)**	**(61.2)**	**(4.4)**	**(17.7)**	**27.6**
Other						
Contributions paid by employer	**–**	–	**2.4**	2.5	**2.4**	2.5
Benefits paid by fund	**(4.9)**	(5.2)	**(4.9)**	(5.2)	**–**	–
	(4.9)	**(5.2)**	**(2.5)**	**(2.7)**	**2.4**	**2.5**
Balance at end of year	**132.7**	**185.4**	**174.5**	**245.8**	**41.8**	**60.4**

The agreed contributions of pensionable salaries in respect of the future service accrual to be paid by the Bank for the year ended 31 March 2023 were 71.5% of pensionable earnings. In addition, the Bank is currently paying contributions to cover the cost of pension payments, cash lump sums on retirement, trivial commutation payments and transfer values.

The scheme is run by the Trustees of the scheme who ensure compliance with the Trust Deed and Rules of the scheme. The Trustees are required by law to fund the scheme on prudent funding assumptions under the Trust Deed and Rules of the scheme. The contributions payable by the Bank to fund the scheme are set by the Trustees after consultation with the Bank.

The Trustees use the attained age funding method which is suitable for funding a scheme open for future accruals but is closed to new entrants.

IFRIC 14 is an interpretation of existing paragraph IAS 19.65, which deals with the level of net pension asset recognisable on a company's balance sheet. IFRIC 14 also requires consideration of minimum funding requirements a company has made to its pension scheme and whether this gives rise to an additional balance sheet liability. Under the scheme's Trust Deed, the Bank has an unconditional right to a refund of surplus from the scheme in the context of IFRIC 14 paragraphs 11(b) and 12. As at 31 March 2023, there was no additional balance sheet liability arising in respect of any funding commitment the Bank has to the scheme.

The weighted average duration of the benefit payments reflected in the defined benefit obligation for the Sumitomo Mitsui Banking Corporation Europe Ltd Pension Scheme is 16 years (2022: 20 years). The decrease in duration is primarily due to the significant increase in discount rate (approximately 2%), driven by higher corporate bond yields.

The employer pays all the costs of administering the scheme and any levies required by the Pension Protection Fund and the Pensions Regulator. The expected employer contribution to the scheme for the year ending 31 March 2024 in respect of future accrual contributions is USD 2.46m.

The following list is not exhaustive but covers the main funding risks for the scheme:

- **Investment return risk:** If the assets underperform the returns assumed in setting the funding target, additional contributions may be required at subsequent valuations.
- **Investment matching risk:** The scheme invests just under 10% of its assets in equity type assets, whereas the solvency target is closely related to return on bonds. If equity type assets have fallen in value relative to the matching assets of bonds, additional contributions may be required.
- **Longevity risk:** If future improvements in mortality exceed the assumptions made then additional contributions may be required.
- **Legislative risk:** The Government, or the Courts, may introduce overriding legislation which leads to an increase in the value of scheme benefits.
- **Solvency risk:** As the funding target is not a solvency target, and the investment strategy does not exactly follow that required for a solvency target, the assets of the scheme may not be sufficient to provide all members with the full value of their benefits on a scheme wind-up. The Bank would then be required to pay the funding shortfall.

The Bank expects to pay USD 6.1m in contributions to defined benefit plans in the coming financial year to 31 March 2024.

Scheme assets were made up of the following:

	2023 USDm	2022 USDm
Equity securities	**9.3**	20.8
Government bonds	**158.1**	224.4
Cash	**7.1**	0.6
	174.5	**245.8**

Sensitivity analysis

The approximate impact on the defined benefit obligation of changes in the significant assumptions is shown below:

Assumption varied	**2023 % change in defined benefit obligation**	2022 % change in defined benefit obligation
Discount rate 1% p.a. lower	**16%**	20%
Salary increase rate 1% p.a. lower	**-1%**	-2%
Pension increase (in payment and in deferment) rate 1% p.a. lower	**-6%**	-8%
Minimum rate of improvement of mortality 0.5% p.a. lower	**-2%**	-2%

The figures assume that each assumption is changed independently of others. Therefore, the disclosures are only a guide because the effect of changing more than one assumption is not cumulative. The sensitivity analysis was calculated by re-running the figures as at the last formal valuation as at 31 December 2020 adjusted approximately for changes in the membership up to 31 March 2023. Therefore, the analysis is only approximate as at the year ended 31 March 2023.

Notes to the financial statements For the year ended 31 March 2023 continued

10. Income taxes

Accounting for income taxes

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognised in profit and loss except to the extent that they relate to items recognised directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantially enacted by the reporting date.

A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefits will be realised.

Income tax expense

Recognised in the income statement:

Recognised in the income statement	**2023 USDm**	2022 USDm
Current tax charge		
Current year	**60.2**	45.2
Overseas tax	**15.9**	16.8
Adjustment for prior years	**(0.7)**	(1.1)
Foreign exchange differences	**(1.6)**	–
	73.8	**60.9**
Deferred tax charge		
Origination and reversal of temporary differences	**11.8**	(12.0)
Adjustment for prior years	**2.6**	0.6
Deferred tax change in rate	**–**	(0.6)
	14.4	**(12.0)**
Total income tax expense	**88.2**	**48.9**

Reconciliation of effective rate of tax	**USDm**	USDm
Profit before income tax	**340.3**	180.8
Income tax using the domestic corporation tax rate of 27%[1] (2022: 27%[1])	**91.9**	48.8
Adjustment for prior years	**1.8**	(0.5)
Deferred tax change in rate	**–**	(0.6)
Expenses not deductible for tax purposes	**1.2**	–
Banking surcharge allowance	**(1.6)**	(1.7)
Overseas tax	**(3.5)**	2.9
Foreign exchange differences	**(1.6)**	–
	88.2	**48.9**

1 UK corporation tax rate of 19% plus bank surcharge rate of 8%.

Effective from 1 April 2023, the headline rate of corporation tax has increased from 19% to 25% and the banking surcharge rate of 8%, applicable to profits of banking companies under the Finance (No.2) Act 2015, has been reduced to 3%.

Deferred tax assets and liabilities are required to be valued using the tax rate which will be in force at the time when the temporary difference is expected to unwind. In line with the requirements of IAS 12, the impact of the change in the headline rate of corporation tax has been reflected in the deferred tax balances at 31 March 2023 as this has been substantively enacted by the UK Parliament. The deferred tax liability has been calculated at 28% as at 31 March 2023.

Income tax recognised in other comprehensive income:

Income tax recognised in other comprehensive income	**Before tax 2023 USDm**	**Tax (expense) /benefit 2023 USDm**	**Effect of changes in tax rate 2023 USDm**	**Net of tax 2023 USDm**	Before tax 2022 USDm	Tax (expense)/ benefit 2022 USDm	Effect of changes in tax rate 2022 USDm	Net of tax 2022 USDm
Actuarial gains/(losses) on defined benefit scheme	**17.6**	**(4.9)**	**–**	**12.7**	(27.5)	7.4	0.1	(20.0)
FVOCI	**(0.4)**	**0.1**	**–**	**(0.3)**	(0.2)	–	–	(0.2)
Cash flow hedges	**(5.0)**	**1.4**	**–**	**(3.5)**	(7.8)	2.1	0.1	(5.6)
IFRS 9 transitional adjustments	**–**	**–**	**–**	**–**	–	–	0.1	0.1
	12.3	**(3.4)**	**–**	**8.9**	**(35.5)**	**9.5**	**0.3**	**(25.7)**

Deferred tax

The components of deferred taxes disclosed on the statement of financial position are as follows:

	USDm 2023	USDm 2022
Deferred tax liability	**(27.9)**	(23.1)
Deferred tax asset	**26.0**	32.1
Net deferred tax asset	**(1.9)**	**9.0**

Movements on deferred tax assets and liabilities were as follows:

	Fixed asset temporary differences USDm	**Bonus accrual USDm**	**Pensions and other retirement benefits USDm**	**Cash flow hedge/ FVOCI/AFS USDm**	**IFRS 9 transitional adjustment USDm**	**Paris branch, IFRS 9 and upfront fees USDm**	**Total USDm**
Asset/(liability) at 1 April 2022	3.5	5.0	(17.0)	(2.6)	(3.4)	23.5	9.0
Adjustments relating to prior years	(8.4)	3.8	0.1	–	–	1.9	(2.6)
Movement through the P&L account	(4.4)	–	0.3	–	–	(7.7)	(11.8)
Movement through other comprehensive income	–	–	4.9	(1.5)	0.6	–	4.0
Exchange rate changes	–	–	–	–	–	(0.5)	(0.5)
At 31 March 2023	**(9.3)**	**8.8**	**(11.7)**	**(4.1)**	**(2.8)**	**17.2**	**(1.9)**
Asset/(liability) at 1 April 2021	4.5	3.7	(8.9)	(0.4)	(3.8)	12.1	7.2
Adjustments relating to prior years	(1.1)	1.1	–	–	–	(0.6)	(0.6)
Movement through the P&L account	0.1	0.2	(0.5)	–	–	12.8	12.6
Movement through other comprehensive income	–	–	(7.5)	(2.2)	0.4	–	(9.3)
Exchange rate changes	–	–	(0.1)	–	–	(0.8)	(0.9)
At 31 March 2022	**3.5**	**5.0**	**(17.0)**	**(2.6)**	**(3.4)**	**23.5**	**9.0**

The amount of deferred tax asset expected to be recovered after more than 12 months is USD 3.8m (2022: USD 22.6m).

Notes to the financial statements For the year ended 31 March 2023 continued

11. Loans and advances to banks and customers

Accounting for loans and advances to banks and customers

Loans and advances at amortised cost

Loans and advances at amortised cost are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and exclude those that are classified as held for trading and those that are designated as at fair value through profit and loss. Subsequent to initial recognition, loans and advances are measured at amortised cost less impairment losses where:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise to cash flows on specified date that represent solely payments of principal and interest on the principal amount outstanding.

Where exposures are hedged by derivatives designated and qualifying as fair value hedges, the carrying value of the loans and advances so hedged includes a fair value adjustment for the hedged risk only (note 13).

Loans and advances at fair value through other comprehensive income

Loans and advances are classified as at fair value through other comprehensive income where:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount.

Loans and advances at fair value through other comprehensive income are measured at fair value on the statement of financial position. Unrealised gains and losses are recognised in other comprehensive income and only on disposal is the cumulative gain or loss, previously recognised in other comprehensive income, recognised in profit and loss.

The Bank does not hold any loans and advances at fair value through other comprehensive income.

Loans and advances at fair value through profit and loss

Loans and advances held at fair value through profit and loss include all loans and advances classified as held for trading, those irrevocably designated as held at fair value through profit and loss on initial recognition, and those with contractual terms that do not represent solely payments of principal and interest on the principal amount outstanding.

Loans and advances classified at fair value through profit and loss are recorded at fair value on the statement of financial position with changes in fair value recognised in profit and loss. Financial instruments are classified as held for trading when they are held with the intention of generating short-term profits.

Finance leases

Leases in terms of which the Bank assumes substantially all risks and rewards of ownership are classified as finance leases. Upon initial recognition, the lease asset receivable is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Lease income is recognised in interest income over the term of the lease using the net investment method (before tax) which reflects a constant periodic rate of return.

	2023 USDm			2022 USDm		
	Loans to banks	**Loans to customers**	**Total**	Loans to banks	Loans to customers	Total
Gross loans and advances at amortised cost	**3,259.5**	**17,929.5**	**21,189.0**	3,996.0	20,185.0	24,181.0
Less: impairment provisions (note 4)	**(36.0)**	**(216.8)**	**(252.8)**	(7.4)	(242.4)	(249.8)
Loans and advances at amortised cost	**3,223.6**	**17,712.7**	**20,936.1**	**3,988.6**	**19,942.6**	**23,931.2**

Loans and advances to customers includes USD 862.9m (2022: USD 344.8m) of Green and Sustainability-Linked Loans.

	2023 USDm	2022 USDm
Amount included within loans and advances to customers expected to be recovered more than 12 months after the reporting date	**12,148.4**	13,139.1
Included in loans and advances to customers are the following amounts relating to leases:		
Gross investment in finance leases		
– Less than one year	**–**	97.0
	–	**97.0**
Less: Unearned finance income	**–**	–
	–	**97.0**
Net investment in finance leases		
– Less than one year	**–**	97.0
	–	**97.0**

The ECL on the lease receivables is immaterial (2022: USD 48.4m).

Finance lease income is included within net interest income. The amount recognised in the income statement during the year all related to finance income from net investment in leases and was USD 0.3m (2022: USD 1.3m). There have been no finance leases entered into during the period and one lease has ended.

Notes to the financial statements For the year ended 31 March 2023 continued

12. Investment securities

Accounting for investment securities

Debt securities at amortised cost

Debt securities at amortised cost are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and exclude those that are classified as held for trading and those that are designated as at fair value through profit and loss. Subsequent to initial recognition, debt securities are measured at amortised cost less impairment losses where:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise to cash flows on specified dates that represent solely payments of principal and interest on the principal amount outstanding.

Investment securities at fair value through other comprehensive income

Debt instruments

Investments in debt instruments that are classified as at fair value through other comprehensive income are those where:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount.

Debt instruments at fair value through other comprehensive income generally comprise securities. The assets are measured at fair value on the statement of financial position. Unrealised gains and losses are recognised in other comprehensive income and only on disposal is the cumulative gain or loss, previously recognised in other comprehensive income, recognised in profit and loss.

Equity instruments

Investments in equity instruments that are not held for trading are measured at fair value through other comprehensive income where an irrevocable election has been made on initial recognition by management. Amounts presented in other comprehensive income are not subsequently transferred to profit or loss.

Investment securities at fair value through profit and loss

Investment securities held at fair value through profit and loss include all instruments classified as held for trading, those instruments irrevocably designated as held at fair value through profit and loss on initial recognition and debt instruments with contractual terms that do not represent solely payments of principal and interest on the principal amount outstanding.

Investment securities classified at fair value through profit and loss are recorded at fair value on the statement of financial position with changes in fair value recognised in profit and loss. Financial instruments are classified as held for trading when they are held with the intention of generating short-term profits.

	2023 USDm	2022 USDm
Investment securities held at amortised cost	**29.3**	65.4
Investment securities at fair value through other comprehensive income	**997.0**	925.7
Investment securities at fair value through profit and loss	**18.8**	18.1
Total investment securities	**1,045.1**	**1,009.2**

	USDm	USDm
Debt securities held at amortised cost	**29.3**	65.4
Debt securities held at fair value through other comprehensive income	**995.8**	924.5
Equities held at fair value through other comprehensive income	**1.2**	1.2
Equities held at fair value through profit and loss	**18.8**	18.1
Total investment securities	**1,045.1**	**1,009.2**

At start of year	**1,009.2**	496.5
Exchange rate adjustments	**–**	(12.9)
Acquisitions and transfers	**1,025.1**	1,669.1
Fair value movement recognised in other comprehensive income	**0.3**	3.4
Disposals and maturities	**(992.4)**	(1,145.9)
Amortisation of discounts and premiums	**2.9**	(1.0)
At end of year	**1,045.1**	**1,009.2**

13. Derivative financial instruments and hedge accounting

Accounting for derivatives

Derivatives include interest rate swaps and futures, cross currency swaps, forward foreign exchange contracts and options on interest rates and foreign currencies. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liabilities when their fair value is negative.

Derivative instruments that do not meet the criteria to be designated as a hedge are deemed to be held for trading and are measured at fair value with the resultant profits and losses included in net trading income.

The fair value of exchange-traded derivatives is determined by reference to the quoted market price.

The fair value of over-the-counter derivatives is determined by calculating the expected cash flows under the terms of each specific contract, and then discounting these to their net present value. The expected cash flows for each contract are determined either directly by reference to actual cash flows implicit in observable market prices, or through modelling cash flows using appropriate pricing models. The effect of discounting expected cash flows back to present value is achieved by constructing discount curves derived from the market price of the most appropriate observable interest rate products such as deposits, interest rate futures and swaps.

The impact of changes in a counterparty's credit spreads (known as credit valuation adjustments) is considered when measuring the fair value of derivative assets and the impact of changes in the Bank's own credit spreads (known as debit valuation adjustments) is considered when measuring the fair value of its derivative liabilities.

Notes to the financial statements For the year ended 31 March 2023 continued

13. Derivative financial instruments and hedge accounting continued

Hedge accounting

The Bank continues to apply the requirements of IAS 39 'Financial Instruments: Recognition and Measurement' for hedge accounting purposes and consequently there have been no changes to the hedge accounting policies and practices following the adoption of IFRS 9.

Derivative financial instruments are used to hedge interest rate risk on fixed rate assets and liabillities, and foreign exchange movement risk on highly probable forecast transactions. Instruments used for hedging purposes include interest rate derivatives, cross currency interest rate derivatives and foreign exchange forwards.

The criteria required for a derivative instrument to be classified as a hedge are as follows:

- At inception of the hedge, the Bank formally documents the hedge relationship between the hedged item and the hedging instrument. This will also include the aim and objective of the risk management and the method that will be used to assess the effectiveness of the hedging relationship.
- The hedge is expected to be highly effective.
- For cash flow hedges, any forecast transactions included must be highly probable and must present an exposure to variations in cash flows that could affect the profit and loss.
- The effectiveness of the hedge (hedged item and hedging instrument) can be reliably measured.
- The hedge effectiveness is assessed on an ongoing basis and determined to have been highly effective throughout the financial reporting periods for which the hedge is designated.

The Bank applies either fair value or cash flow hedge accounting when the transaction meets the above criteria. Hedge accounting is discontinued when it is determined that the derivative ceases to be highly effective as a hedge. A hedge is regarded as highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80% to 125%. A hedge will also cease to be effective if the derivative or asset is sold, terminated, expires or matures, or when a forecast transaction is no longer deemed probable.

Interest rate benchmark reform

i) Phase 1 amendments

The Bank applies the IBOR Reform Phase 1 reliefs to hedging relationships directly affected by IBOR reform during the period before the replacement of an existing interest rate benchmark with an alternative risk-free rate (RFR). A hedging relationship is affected if IBOR reform gives rise to the following uncertainties:

- the timing and/or amount of interest rate benchmark-based cash flows of the hedged item or the hedging instrument; and/or
- an interest rate benchmark subject to the reform is designated as the hedged risk, regardless of whether the rate is contractually specified.

The reliefs require that for the purpose of determining whether a forecast transaction is highly probable, it is assumed that the IBOR on which the hedged cash flows are based is not altered as a result of the IBOR reform.

IBOR Reform Phase 1 requires that for hedging relationships affected by IBOR reform, the Bank must assume, for the purpose of assessing expected future hedge effectiveness, the interest rate is not altered as a result of IBOR reform. Also, the Bank is not required to discontinue the hedging relationship if the results of the assessment of retrospective hedge effectiveness fall outside the range of 80% to 125%, although any hedge ineffectiveness must be recognised in profit and loss, as normal.

The reliefs cease to apply once certain conditions are met. These include when the uncertainty arising from IBOR reform is no longer present with respect to the timing and amount of the benchmark-based cash flows of the hedged item, if the hedging relationship is discontinued or once amounts in the cash flow hedge reserve have been released.

ii) Phase 2 amendments

The Bank also applies IBOR Reform Phase 2 issued in August 2020.

When the basis for determining the contractual cash flows of the hedged item or hedging instrument changes as a result of IBOR reform and therefore there is no longer uncertainty arising about the cash flows of the hedged item or the hedging instrument, the Bank amends the hedge documentation of that hedging relationship to reflect the change(s) required by IBOR reform. For this purpose, the hedge designation is amended only to make one or more of the following changes:

- designating an alternative benchmark rate as the hedged risk;
- updating the description of the hedged item, including the description of the designated portion of the cash flows or fair value being hedged;
- updating the description of the hedging instrument; or
- updating the description of how the entity will assess hedge effectiveness.

The Bank amends the description of the hedging instrument only if the following conditions are met:

- it makes a change required by IBOR reform by changing the basis for determining the contractual cash flows of the hedging instrument or using another approach that is economically equivalent to changing the basis for determining the contractual cash flows of the original hedging instrument; and
- the original hedging instrument is not derecognised.

The Bank amends the formal hedge documentation by the end of the reporting period during which a change required by IBOR reform is made to the hedged risk, hedged item or hedging instrument. These amendments in the formal hedge documentation do not constitute the discontinuation of the hedging relationship or the designation of a new hedging relationship. If changes are made in addition to those changes required by IBOR reform described above, then the Bank first considers whether those additional changes result in the discontinuation of the hedge accounting relationship. If the additional changes do not result in the discontinuation of the hedge accounting relationship, then the Bank amends the formal hedge documentation for changes required by IBOR reform as mentioned above.

Notes to the financial statements For the year ended 31 March 2023 continued

13. Derivative financial instruments and hedge accounting continued

Fair value hedge accounting

For qualifying fair value hedges, the changes in fair value in respect of the hedged risk of both the hedged item and hedging derivative are recognised in profit and loss. Any ineffective portion of the hedge is immediately recognised in profit and loss under interest income.

If hedge relationships no longer meet the criteria for hedge accounting or the hedging derivative is sold, terminated, expires or matures, hedge accounting is discontinued. For fair value hedges of interest rate risk, the fair value adjustment to the hedged item is amortised over the remaining period to maturity of the previously designated hedge relationship using the effective interest rate method. If the hedged item is derecognised, the unamortised fair value adjustment is recognised immediately in profit or loss.

Cash flow hedge accounting

For qualifying cash flow hedges in respect of financial assets and liabilities, the effective portion of the change in the fair value of the hedging derivative is initially recognised in other comprehensive income and is released to profit and loss in the same periods during which the hedged item affects profit and loss. Any ineffective portion of the hedge is immediately recognised in profit and loss under net trading income.

Analysis of derivatives

The following tables show the notional amounts and fair values of the Bank's derivatives at 31 March 2023 and 31 March 2022.

	2023 Notional contract amount USDm	**2023 Fair value derivative assets USDm**	**2023 Fair value derivative liabilities USDm**	2022 Notional contract amount USDm	2022 Fair value derivative assets USDm	2022 Fair value derivative liabilities USDm
Trading derivatives						
Foreign exchange derivatives						
Forward foreign exchange	**269,128.7**	**1,708.8**	**(1,834.1)**	211,178.6	1,358.2	(1,295.9)
Currency options	**15,409.7**	**191.5**	**(42.0)**	686.9	5.9	(5.9)
Total trading derivatives	**284,538.4**	**1,900.3**	**(1,876.1)**	**211,865.5**	**1,364.1**	**(1,301.8)**
Derivatives held for risk management						
Foreign exchange derivatives						
Currency swaps – Fair value hedges	**–**	**–**	**–**	–	–	–
Currency swaps – Cash flow hedges	**650.4**	**100.2**	**(0.2)**	680.3	43.9	(14.2)
Total foreign exchange derivatives	**650.4**	**100.2**	**(0.2)**	**680.3**	**43.9**	**(14.2)**
Interest rate derivatives						
Interest rate swaps – Fair value hedges	**2,014.6**	**85.1**	**(1.0)**	1,882.1	22.4	(6.6)
Total interest rate derivatives	**2,014.6**	**85.1**	**(1.0)**	**1,882.1**	**22.4**	**(6.6)**
Total derivatives held for risk management	**2,665.0**	**185.3**	**(1.2)**	**2,562.4**	**66.3**	**(20.8)**
Total derivatives	**287,203.4**	**2,085.6**	**(1,877.3)**	**214,427.9**	**1,430.4**	**(1,322.6)**

Hedge accounting

As part of its asset and liability management, the Bank uses derivatives as fair value and cash flow hedges to protect it against changes in the fair value of financial assets and financial liabilities due to movements in interest rates and against variability in cash flows arising from movements in foreign exchange rates. Derivatives often involve at their inception only a mutual exchange of promises with little or no transfer of consideration. These instruments frequently involve a high degree of leverage and can be volatile. Due to this, the Bank maintains very tight control over their use and whenever a derivative hedge is used, it is imperative that the critical terms of the hedging instrument and the hedged item are closely aligned.

The Bank applies hedge accounting to manage interest rate and foreign exchange risk. Further details of how these risks arise and how they are managed by the Bank are discussed in note 4(b).

In order to hedge the risks to which the Bank is exposed, the hedging instruments employed are interest rate and cross currency interest rate swaps. Swaps are contractual agreements between two parties to exchange streams of payments over time based on specified notional amounts, in relation to movements in specified underlying indices such as an interest rate or foreign currency rate.

Interest rate swaps relate to contracts taken out by the Bank with other financial institutions in which the Bank either receives or pays a floating rate of interest in return for paying or receiving, respectively, a fixed or alternative floating rate of interest. The payment flows are usually netted against each other, with the difference being paid by one party to the other.

In a cross currency interest rate swap, the Bank pays the principal amount in one currency and receives the principal amount in the other currency at the start of the deal with the reverse at the maturity of the deal. Interim cash flows of interest are then exchanged on the same basis as an interest rate swap in that the Bank either receives or pays a floating rate of interest in one currency, in return for paying or receiving, respectively, a fixed rate of interest in the other currency.

The hedging instruments share the same risk exposure as the hedged items, being interest rate and currency risk. Before hedge accounting is applied, the Bank determines whether an economic relationship exists between the hedged item and the hedging instrument based on an evaluation of the qualitative characteristics of these items and the hedged risk, and considers whether the critical terms of the hedged item and hedging instrument are closely aligned.

Hedge effectiveness is determined with reference to changes in the fair value of the hedged item compared with the fair value of the hedge on a cumulative basis. The hedge is considered effective if the results are in the range of 80% to 125%.

Sources of hedge ineffectiveness may arise from the following:

- mismatches between the contractual terms of the hedged item and hedging instrument, including differences in maturities or basis differences between the hedged item and the hedging instrument; or
- changes in credit risk of the hedging instrument.

Notes to the financial statements For the year ended 31 March 2023 continued

13. Derivative financial instruments and hedge accounting continued

Interest rate benchmark reform

Following the financial crisis, the reform and replacement of benchmark interest rates such as IBOR has become a priority for global regulators. Since the changes are market driven, there is currently some uncertainty around the timing and precise nature of these changes.

The Bank's risk exposure is directly affected by interest rate benchmark reform, across its fair value hedge accounting activities where IBOR-linked derivatives are designated as a fair value hedge of fixed interest rate assets.

The Bank's risk exposure is predominantly to GBP, USD, EUR and JPY LIBOR.

Fair value hedges

The financial instruments hedged for interest rate risk include fixed rate loans and bonds. The Bank uses interest rate swaps to hedge interest rate risk (including currency swaps). Interest rate risk arises as the Bank holds a portfolio of medium- and long-term fixed rate customer loans whose fair value fluctuates due to movements in market interest rates. In such cases, changes in the fair values in respect of the hedged risk of both the hedging instrument and the hedged item are recognised in profit and loss.

The Bank hedges interest rate risk only to the extent of benchmark interest rates because the changes in fair value of fixed rate loans are significantly influenced by changes in the benchmark interest rate.

The following table shows the hedging instruments which are carried on the Bank's balance sheet within derivative assets and liabilities:

Hedge type	Risk category	Notional amount USDm	Carrying amount derivative assets USDm	Carrying amount derivative liabilities USDm	Change in fair value used as a basis to determine ineffectiveness USDm	Notional amount directly impacted by IBOR reform USDm
As at 31 March 2023						
Fair value	Interest rate risk	2,014.6	85.1	1.0	84.1	1,689.8
		2,014.6	**85.1**	**1.0**	**84.1**	**1,689.8**
As at 31 March 2022						
Fair value	Interest rate risk	1,882.1	22.4	6.6	15.8	1,621.2
		1,882.1	**22.4**	**6.6**	**15.8**	**1,621.2**

The following table summarises the significant hedge accounting exposures impacted by the IBOR reform as at 31 March 2023:

Current benchmark rate	Convergence to RFR	Notional amount of hedged items directly impacted by IBOR reform USDm	Notional amount of hedging instruments directly impacted by IBOR reform USDm
GBP London Interbank Offered Rate (LIBOR)	Reformed Sterling Overnight Index Average (SONIA)	585.6	585.6
USD LIBOR	Secured Overnight Financing Rate (SOFR)	353.5	353.5
JPY LIBOR	Tokyo Overnight Average (TONA)	750.6	750.6

The following table profiles the expected notional values of current hedging instruments:

Interest rate risk Hedge of loans and advances to customers	Maturity 31 March 2023 Less than 1 year	1 to 5 years	More than 5 years	Maturity 31 March 2022 Less than 1 year	1 to 5 years	More than 5 years
Notional amount (USDm)	**636.6**	**1,013.0**	**365.0**	297.5	1,135.2	449.4
Average fixed interest rate %	**0.3%**	**0.8%**	**2.0%**	0.3%	0.3%	1.7%

The following table shows the hedged items in fair value hedge accounting relationships:

At 31 March 2023 Hedged risk	**Hedged item statement of financial position classification**	**Carrying amount USDm**	**Accumulated fair value hedge adjustments included in carrying amount USDm**	**Change in fair value used as a basis to determine ineffectiveness USDm**	**Hedge ineffectiveness recognised in the income statement USDm**
Interest rate risk	Loans and advances to customers	1,932.6	(82.0)	(82.0)	–
		1,932.6	**(82.0)**	**(82.0)**	**–**

At 31 March 2022 Hedged risk	Hedged item statement of financial position classification	Carrying amount USDm	Accumulated fair value hedge adjustments included in carrying amount USDm	Change in fair value used as a basis to determine ineffectiveness USDm	Hedge ineffectiveness recognised in the income statement USDm
Interest rate risk	Loans and advances to customers	1,863.8	(18.3)	(18.3)	–
		1,863.8	**(18.3)**	**(18.3)**	**–**

Cash flow hedges

The Bank transacts cash flow hedges for hedging cross currency swaps and to reduce the foreign exchange risk on the cash flows arising from the Bank's forecast Sterling expenses for each financial year. The Bank enters into US Dollar–Sterling foreign exchange forward contracts to manage variability in the Bank's highly probable cash outflows in relation to Sterling expenses for each month of the financial year.

The following table shows the hedged items in cash flow hedge accounting relationships:

Hedge type	**Risk category**	**Change in fair value used as a basis to determine ineffectiveness USDm**	**Balance in cash flow hedging reserve for assets USDm**	**Hedging gains or losses recognised in other comprehensive income USDm**	**Hedge ineffectiveness recognised in income statement USDm**
As at 31 March 2023					
Cash flow hedge	Foreign exchange risk	14.2	14.2	14.2	–
		14.2	**14.2**	**14.2**	**–**
As at 31 March 2022					
Cash flow hedge	Foreign exchange risk	9.2	9.2	9.2	–
		9.2	**9.2**	**9.2**	**–**

The amount recycled from other comprehensive income due to hedged items affecting the income statement for cash flow hedges of foreign exchange rate was USD 6.7m (2022: USD (1.1)m).

Notes to the financial statements For the year ended 31 March 2023 continued

13. Derivative financial instruments and hedge accounting continued

The following table shows the movements of the cash flow hedging reserve:

	Cash flow hedging reserve USDm
At 1 April 2022	**6.7**
Hedging gains for the year	**14.2**
Amounts reclassified in relation to cash flows affecting profit or loss	**(6.7)**
Tax	**(4.0)**
At 31 March 2023	**10.2**

	Cash flow hedging reserve USDm
At 1 April 2021	1.1
Hedging gains for the year	8.9
Amounts reclassified in relation to cash flows affecting profit or loss	(1.1)
Tax	(2.2)
At 31 March 2022	**6.7**

Offsetting of financial assets and financial liabilities

In accordance with IAS 32 'Financial Instruments: Presentation', the Bank does not offset any financial assets and liabilities. It does however receive or give collateral against certain derivative transactions and reverse repurchase agreements with such collateral subject to standard industry terms including the ISDA Credit Support Annex.

In addition, the Bank also enters into ISDA and similar master netting agreements which only allow offsetting on certain events, such as following an event of default. These do not meet the criteria for offsetting in the statement of financial position.

The disclosures set out below include derivative assets, derivative liabilities and reverse repurchase agreements that are subject to enforceable master netting arrangements or similar agreements.

		Related amounts not offset				
	Gross amounts recognised in the statement of financial position USDm	Financial instruments USDm	Cash collateral USDm	Net amount USDm	Amounts not subject to enforceable netting arrangements USDm	Total USDm
At 31 March 2023						
Derivative assets	**1,751.6**	**(1,293.5)**	**(265.4)**	**192.7**	**334.0**	**2,085.6**
Reverse repurchase agreements	**1,266.9**	**(1,266.9)**	**–**	**–**	**–**	**1,266.9**
	3,018.5	**(2,560.4)**	**(265.4)**	**192.7**	**334.0**	**3,352.5**
Derivatives liabilities	**1,695.7**	**(1,293.5)**	**(365.1)**	**37.1**	**181.6**	**1,877.3**
At 31 March 2022						
Derivative assets	1,248.8	(787.0)	(165.0)	296.8	181.6	1,430.4
Reverse repurchase agreements	1,197.9	(1,197.9)	–	–	–	1,197.9
	2,446.7	**(1,984.9)**	**(165.0)**	**296.8**	**181.6**	**2,628.3**
Derivatives liabilities	**1,156.7**	**(787.0)**	**(251.2)**	**118.5**	**165.9**	**1,322.6**

14. Other assets

	2023 USDm	2022 USDm
Accrued income	**484.8**	288.3
Prepayments and other receivables	**54.2**	26.9
Cash collateral placed under Credit Support Annex	**389.9**	381.1
	928.9	**696.3**

15. Intangible assets and goodwill

Accounting for intangible assets

Intangible assets are stated at capitalised cost less accumulated amortisation and accumulated impairment losses. The carrying values of intangible assets are reviewed for impairment at each reporting date and when events or changes in circumstances indicate that the carrying value may not be recoverable. Expenditure on internally developed software is recognised as an asset when the Bank is able to demonstrate its intention and ability to complete the development and use the software in a manner which will generate future economic benefits, and can reliably measure the costs to complete the development. The capitalised costs of internally developed software include all costs directly attributable to developing the software and are amortised over its useful life.

Intangible assets are amortised on a straight-line basis over their estimated useful lives as follows:

Computer software	Up to 31 March 2021	3 years
	From 1 April 2021	5 years

Accounting for goodwill

The carrying value of goodwill is determined in accordance with IFRS 3 'Business Combinations' and IAS 36 'Impairment of Assets'.

Goodwill arising on the acquisition of subsidiaries represents the excess of the fair value of the purchase consideration over the fair value of the Bank's share of the asset acquired and the liabilities and contingent liabilities assumed on the date of acquisition.

Goodwill is reviewed annually for impairment, or more frequently when there are indications that impairment may have incurred. The test involves comparing the carrying value of the cash generating unit (CGU) including goodwill with the present value of the pre tax cash flows, discounted at a rate of interest that reflects the inherent risks of the CGU to which the goodwill relates, or the CGU's fair value if this is higher.

Goodwill

Goodwill acquired in a business combination is allocated, at acquisition, to the CGU that is expected to benefit from that business combination. The carrying amount of goodwill, which is immaterial, is USD 1.9m (2022: USD 1.9m).

Notes to the financial statements For the year ended 31 March 2023 continued

15. Intangible assets and goodwill continued

Software

The carrying amount of software is as follows:

	Internally generated software USDm	Other software USDm	Total USDm
At 1 April 2022	**19.8**	**128.3**	**148.1**
Additions	**3.0**	**21.5**	**24.5**
Disposals	**–**	**–**	**–**
At 31 March 2023	**22.8**	**149.8**	**172.6**
Accumulated amortisation			
At 1 April 2022	**12.0**	**91.3**	**103.3**
Charge for the year	**2.3**	**12.5**	**14.8**
Disposals	**–**	**–**	**–**
At 31 March 2023	**14.3**	**103.8**	**118.1**
Net book value at 31 March 2023	**8.5**	**46.0**	**54.5**
At 1 April 2021	15.7	111.5	127.2
Additions	4.1	16.8	20.9
Disposals	–	–	–
At 31 March 2022	**19.8**	**128.3**	**148.1**
Accumulated amortisation			
At 1 April 2021	9.9	79.3	89.2
Charge for the year	2.1	12.0	14.1
Disposals	–	–	–
At 31 March 2022	**12.0**	**91.3**	**103.3**
Net book value at 31 March 2022	**7.8**	**37.0**	**44.8**

The gross carrying amount of fully depreciated software still in use is USD 93.0m (2022: USD 78.1m).

16. Property and equipment

Accounting for property and equipment

Fixed tangible assets are stated at capitalised cost less accumulated depreciation and accumulated impairment losses. The carrying values of fixed tangible assets are reviewed for impairment at each reporting date and when events or changes in circumstances indicate that the carrying value may not be recoverable.

Property and equipment are depreciated on a straight-line basis over their estimated useful lives as follows:

Leasehold improvements	10 years or over the remaining life of the lease, whichever is the shorter
Computer hardware	3 years
Motor vehicles	5 years
Equipment, fixtures and fittings	5 years

Accounting for leases

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Bank uses the definition of a lease in IFRS 16.

Bank acting as a lessee

At commencement or on modification of a contract that contains a lease component, the Bank allocates consideration in the contract to each lease component on the basis of its relative standalone price.

The Bank recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to office premises.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, the Bank uses its incremental borrowing rate as the discount rate.

The Bank determines its incremental borrowing rate by analysing its borrowings from various external sources and makes certain adjustments to reflect the terms of the lease and type of asset leased.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index or a rate, initially measured using the index rate as at the commencement date;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Bank is reasonably certain to exercise, lease payments in an optional renewal period if the Bank is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Bank is reasonably certain not to terminate early.

The lease liability is measured at amortised cost using the effective interest rate method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, if the Bank changes its assessment of whether it will exercise a purchase, extension or termination option, or if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to nil.

The Bank presents right-of-use assets in property and equipment, and lease liabilities in 'other liabilities' in the statement of financial position.

Notes to the financial statements For the year ended 31 March 2023 continued

16. Property and equipment continued

The Bank has elected not to recognise right-of-use assets and lease liabilities for leases of low value assets and short-term leases, including leases of IT equipment. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term (note 6). The total recognised in the income statement for the year ended 31 March 2023 was USD 5.5m (2022: USD 6.5m).

	Right-of-use assets: Land and buildings USDm	Leasehold improvements USDm	Equipment USDm	Total USDm
Cost				
At 1 April 2022	**194.2**	**107.4**	**79.5**	**381.1**
Additions	**0.1**	**5.2**	**31.8**	**37.1**
Disposals	**(15.4)**	**(32.9)**	**(23.4)**	**(71.7)**
At 31 March 2023	**178.9**	**79.7**	**87.9**	**346.5**
Accumulated depreciation				
At 1 April 2022	**34.6**	**44.0**	**47.9**	**126.5**
Charge for the year	**19.1**	**5.6**	**12.4**	**37.1**
Disposals	**(15.2)**	**(32.9)**	**(23.4)**	**(71.5)**
At 31 March 2023	**38.5**	**16.7**	**36.9**	**92.1**
Net book value at 31 March 2023	**140.4**	**63.0**	**51.0**	**254.4**
Cost				
At 1 April 2021	194.2	63.3	59.5	317.0
Additions	–	44.1	20.0	64.1
Disposals	–	–	–	–
At 31 March 2022	**194.2**	**107.4**	**79.5**	**381.1**
Accumulated depreciation				
At 1 April 2021	11.0	42.5	44.4	97.9
Charge for the year	23.6	1.5	3.5	28.6
Disposals	–	–	–	–
At 31 March 2022	**34.6**	**44.0**	**47.9**	**126.5**
Net book value at 31 March 2022	**159.6**	**63.4**	**31.6**	**254.6**

The gross carrying amount of fully depreciated property, plant and equipment still in use is USD 26.2m (2022: USD 75.3m).

17. Debt securities in issue

	2023 USDm	2022 USDm
Certificates of deposit – held at amortised cost	**1,048.7**	976.0

All debt securities are expected to be settled no more than 12 months after the reporting date.

18. Other liabilities

	2023 USDm	2022 USDm
Lease liabilities	**161.8**	175.0
Accruals and deferred income	**390.9**	211.3
Accounts payable to parent	**–**	8.0
Cash collateral received under Credit Support Annex	**292.5**	182.4
Other liabilities	**2.1**	7.0
	847.3	**583.7**

Lease liabilities

The Bank leases various offices under non-cancellable lease arrangements to meet its operational business requirements. The Bank does not have any material subleasing arrangements. Right-of-use assets relate to property leases only: refer to note 16 for a breakdown of the carrying amount of right-of-use assets.

The total expenses recognised during the year for short-term and low value leases were USD 5.5m (2022: USD 6.1m) and USD nil (2022: USD 0.5m), respectively. The portfolio of short-term and low value leases to which the Bank is exposed at the end of the year is not dissimilar to the expenses recognised during the year.

	USDm
As at 31 March 2021	192.0
Interest expense	1.9
New leases	–
Disposals	–
Cash payments	(18.9)
As at 31 March 2022	**175.0**
Interest expense	**1.7**
New leases	**–**
Disposals	**(9.6)**
Cash payments	**(5.3)**
As at 31 March 2023	**161.8**

The undiscounted maturity analysis of lease liabilities at 31 March 2023 and 31 March 2022 is as follows:

	Up to 3 months USDm	3 to 12 months USDm	1 to 2 years USDm	2 to 3 years USDm	3 to 4 years USDm	4 to 5 years USDm	Over 5 years USDm	Total USDm
31 March 2023								
Lease payments	**1.0**	**5.8**	**15.1**	**15.1**	**15.1**	**14.6**	**106.2**	**172.9**
Finance charges	**(0.4)**	**(1.3)**	**(1.6)**	**(1.4)**	**(1.3)**	**(1.1)**	**(4.0)**	**(11.1)**
Net present values	**0.6**	**4.5**	**13.5**	**13.7**	**13.8**	**13.5**	**102.2**	**161.8**
31 March 2022								
Lease payments	**2.4**	**2.9**	**7.3**	**16.0**	**16.0**	**16.0**	**128.0**	**188.6**
Finance charges	**(0.5)**	**(1.3)**	**(1.8)**	**(1.7)**	**(1.5)**	**(1.4)**	**(5.4)**	**(13.6)**
Net present values	**1.9**	**1.6**	**5.5**	**14.3**	**14.5**	**14.6**	**122.6**	**175.0**

The Bank is not exposed to any additional cash flows in respect of variable lease payments or extension and termination options. Additionally, the Bank does not have any significant sale and lease back transactions and does not have any restrictions or covenants imposed by the lessor on its property leases which restrict its business.

Notes to the financial statements For the year ended 31 March 2023 continued

19. Contingent liabilities

Accounting for contingent liabilities

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is uncertain or cannot be reliably measured. Contingent liabilities are not recognised but are disclosed unless they are remote.

The Bank is a defendant in a LIBOR-related legal case alleging certain of the Bank's practices and actions were improper. Management believes that the Bank will be successful in resolving these matters to the extent that it is able to assess them. At the reporting date, the amount at risk is not reasonably estimable. This is an area of significant judgement and the potential liability could be material to the results at the point they are recognised in future periods.

20. Called up share capital

	USDm
Issued, allotted and fully paid share capital (Ordinary shares of USD 1,000 and GBP 1)	
At 31 March 2022	3,200.1
Additions	–
At 31 March 2023	**3,200.1**

The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision and adopted by the Prudential Regulation Authority in supervising banks.

The Bank's capital is managed to ensure the Bank complies with external requirements and, in order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payments to shareholders, return capital or issue capital securities. There were no changes to the objectives, policies or process for the management of capital in the year. During the year, there were no breaches of the Bank's capital adequacy requirement which required reporting to the Prudential Regulation Authority.

The Bank's available regulatory capital as at year-end was USD 5,083.0m (2022: USD 4,886.8m) calculated as total equity per financial statements less regulatory adjustments as per the requirements laid down in the Capital Requirements Regulation.

The following table provides a reconciliation of the Bank's balance sheet position to the Bank's regulatory capital position:

	2023 USDm	2022 USDm
Shareholders' equity per financial statements	**5,189.4**	4,946.2
Reserves not included in Tier 1 capital – Cash flow hedge	**(10.2)**	(6.7)
Deductions and other adjustments	**(96.2)**	(52.7)
Tier 1 capital after deductions	**5,083.0**	**4,886.8**

21. Guarantees and commitments

Accounting for guarantees

In the course of its business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. 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. Financial guarantees are initially recognised in the financial statements at fair value, being the premium received. Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amortised premium or the provision in line with the policy in note 4. The premium receivable is recognised in profit and loss in fees and commissions income using the effective interest rate method over the life of the guarantee. Any increase in the liability relating to financial guarantees is taken to profit and loss.

	2023 Contract amount USDm	2022 Contract amount USDm
Guarantees and letters of credit	**3,353.9**	3,413.3
Undrawn formal standby facilities, credit lines and other commitments to lend	**12,837.5**	15,194.9

Undrawn commitments includes USD 1,999.3m (2022: USD 1,849.2m) in relation to green and sustainability facilities.

Guarantees and letters of credit commit the Bank to make payments on behalf of customers upon the occurrence of an event, generally related to the import or export of goods.

Commitments to extend credit represent contractual commitments to make loans and revolving credits. Since commitments may expire without being drawn upon; the total contract amounts do not necessarily represent future cash requirements.

Guarantees, letters of credit and commitments carry the same credit risk as loans and are subject to the expected credit loss requirements of IFRS 9. Further further details please refer to note 4.

22. Assets pledged

Assets are pledged as collateral to secure liabilities or as security deposits on derivatives. The following table summarises the nature and carrying amount of assets pledged against liabilities held.

	2023 USDm	2022 USDm
Loans and advances to customers	**250.4**	417.1
Other assets	**386.5**	381.1
Total	**636.9**	**798.2**

The loans and advances to customers were pledged to the Banque de France. These assets allow the Bank to draw additional liquidity as of the year-end of USD 250.4m (2022: USD 417.1m). The other assets have been pledged as security deposits on derivatives.

Notes to the financial statements For the year ended 31 March 2023 continued

23. Related parties

Two or more parties are considered to be related when one party has direct or indirect control over the other party; or the parties are subject to common control from the same source; or one party has influence over the financial and operating policies of the other party to the extent that the other party might be inhibited from pursuing at all times its own separate interests.

Key management personnel are the Directors of the Company. There were no loans or deposits with or to key management personnel (and their connected persons) of the Bank. Key management personnel compensation is as follows:

	2023 USDm	2022 USDm
Short-term employee benefits	**3.3**	2.9
Post-employment benefits	**0.1**	0.1
Total	**3.4**	**3.0**

The Bank has entered into a Keep Well Deed under which the Bank and SMBC agree to certain financial arrangements, including the obligation of the parent to maintain tangible net worth in the Bank at all times sufficient to cover the Bank's obligations arising through any of its business activities.

Amounts receivable from related parties of the Bank are as follows:

	2023		2022	
	Loans and advances USDm	**Other assets USDm**	Loans and advances USDm	Other assets USDm
Amounts due from parent company	**1,360.9**	**1,160.4**	2,289.9	496.0
Amounts due from other related parties	**24.0**	**9.9**	254.3	152.0
Total	**1,384.9**	**1,170.3**	**2,544.2**	**648.0**

Loans and advances are made in the ordinary course of business and on the same terms as comparable transactions with third parties. Other assets predominantly include derivative assets and other receivables.

Amounts payable to related parties of the Bank are as follows:

	2023		2022	
	Deposits USDm	**Other liabilities USDm**	Deposits USDm	Other liabilities USDm
Amounts due to parent company	**21,549.5**	**592.5**	21,094.4	218.2
Amounts due to other related parties	**96.0**	**12.3**	720.7	29.7
Total	**21,645.5**	**604.8**	**21,815.1**	**247.9**

The Bank receives collateral consisting of cash (part of amounts due to the parent company) of USD 3,909.6m (2022: USD 5,253.3m), from SMBC, to mitigate large exposures on intra-group positions. Deposits are taken in the ordinary course of business and on the same terms as comparable transactions with third parties.

Guarantees received from related parties of the Bank are as follows:

	2023 USDm	2022 USDm
Guarantees received on customer accounts	**1,610.0**	2,918.6
Guarantees received on the Bank's liabilities	**318.9**	363.1

Amounts recognised in the statement of comprehensive income in respect of related party transactions are as follows:

2023	**Parent companies USDm**	**Other related parties USDm**	**Total USDm**
Interest income	**28.9**	**0.7**	**29.6**
Interest payable	**(450.4)**	**(0.3)**	**(450.7)**
Fees and commissions receivable	**498.1**	**1.4**	**499.5**
Fees and commissions payable	**(2.4)**	**(0.6)**	**(3.0)**
Net trading	**–**	**(0.1)**	**(0.1)**
Other expenses	**(49.3)**	**–**	**(49.3)**
Total	**24.9**	**1.1**	**26.0**

2022	Parent companies USDm	Other related parties USDm	Total USDm
Interest income	2.9	20.6	23.5
Interest payable	(56.5)	17.0	(39.5)
Fees and commissions receivable	287.2	160.1	447.3
Fees and commissions payable	(0.6)	(1.3)	(1.9)
Net trading	–	(0.2)	(0.2)
Other expenses	(32.3)	(2.3)	(34.6)
Total	**200.7**	**193.9**	**394.6**

24. Country-by-country report

The Capital Requirements (Country-by-country Reporting) Regulations 2013 came into effect on 1 January 2014. The requirements impose certain reporting obligations on credit institutions and investments firms within the UK and within the scope of EU Capital Requirements Directive IV. The Bank's country-by-country report is presented below.

Notes to the financial statements
For the year ended 31 March 2023 continued

24. Country-by-country report continued

Country-by-country disclosure

2023

Activity	Geographical location	**Turnover USDm**	**Profit or loss before income tax USDm**	**Cash tax USDm**	**Average headcount**
Corporate banking	UK	**921.7**	**252.5**	**70.7**	**1,492**
Corporate banking	France*	**103.8**	**87.8**	**20.9**	**89**
Intra-group adjustments		**(11.1)**	**–**	**–**	**–**
		1,014.4	**340.3**	**91.6**	**1,581**

2022

Activity	Geographical location	Turnover USDm	Profit or loss before income tax USDm	Cash tax USDm	Average headcount
Corporate banking	UK	784.7	172.8	85.4	1,404
Corporate banking	France*	99.5	8.0	6.7	78
Intra-group adjustments		(13.4)			
		870.8	**180.8**	**92.1**	**1,482**

* The activity in France is carried out through the Bank's branch in Paris.

Basis of preparation

1. Activities:
   Corporate banking – refers to provision of credit and other banking services to corporate customers.

2. Geographical location – the country where the branch is established.

3. Turnover includes interest income, interest expense, fees and commissions income, fees and commissions expense and net trading (loss)/income. This is in line with the financial statements.

4. Cash tax – refers to cash amount of all corporation tax paid in each location during the period 1 April to 31 March each year, including Group relief.

5. Public subsidies – refers to direct support by the Government. The Bank does not receive any public subsidies.

25. Parent companies

The Bank is a subsidiary undertaking of Sumitomo Mitsui Financial Group Inc, which is the ultimate parent company incorporated in Japan. SMFG is the ultimate controlling party.

The largest group in which the results of the Company are consolidated is that headed by Sumitomo Mitsui Financial Group Inc. SMFG's consolidated financial statements can be obtained from its registered office at 1-1-2 Marunouchi, Chiyoda-ku, Tokyo 100-0005, Japan.

The smallest group in which they are consolidated is that headed by Sumitomo Mitsui Banking Corporation, the Bank's immediate parent. The consolidated financial statements of SMBC can be obtained from its registered office at 1-1-2 Marunouchi, Chiyoda-ku, Tokyo 100-0005, Japan.

Forward-looking statements

This document contains certain forward-looking statements with respect to the financial condition, results of operations, and business of the Bank and SMBC Group. Forward-looking statements may be made in writing but also may be made verbally by members of the management of SMBC Group in connection with this document.

Words such as 'may', 'will', 'continue', 'aim', 'target', 'projected', 'expect', 'anticipate', 'intend', 'plan', 'goal', 'believe', 'seek', 'estimate', 'achieve', 'potential' and variations of these words are intended to identify forward-looking statements. The Bank and SMBC Group makes no commitment to revise or update publicly any forward-looking statements.

Forward-looking statements may be affected by, among other things, changes in legislation; the development of standards and interpretations under IFRS; the outcome of current and future legal proceedings and regulatory investigations; the policies and actions of governmental and regulatory authorities; SMBC Group's ability to manage the impacts of climate change effectively; geopolitical risks; and the impact of competition.

A number of these factors are beyond the control of the Bank and SMBC Group. As a result, the Bank and SMBC Group's actual financial position, future results, capital distributions, capital, leverage or other regulatory ratios, or other financial and non-financial metrics or performance measures may differ materially from the statements or guidance set forth in the Bank's and SMBC Group's forward-looking statements.

SMBC