



Bank Leumi (UK) plc

Regulatory Disclosures – Pillar 3

Background

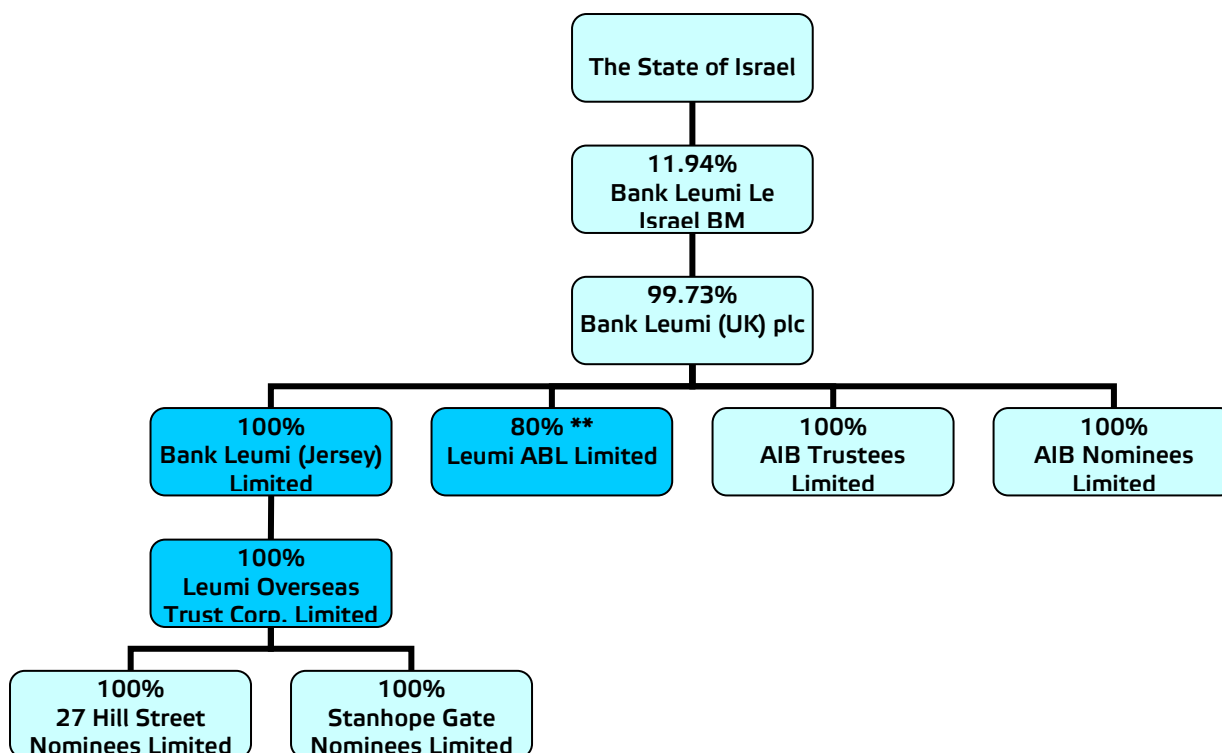
Since the 1st January 2008, Bank Leumi (UK) plc has been operating under the Capital Requirements Directive (Basel II) regime and has adopted the standardised approach for assessing the capital requirement for credit risk, and the basic indicator approach for operational risk.

This information has been prepared to satisfy the qualitative disclosure requirements as set out in Chapter 11 of the FSA's Prudential Sourcebook for Bank's (BIPRU). The quantitative disclosure requirements can be found within the later sections of this disclosure as well as the Bank's audited accounts. Copies of these financial reports have been posted on the Bank's website.

These disclosures are made based on positions, policies and procedures that were in place as at the 31st December 2008. This information will be updated on an annual basis, or where significant changes have been made that would materially effect the detail of this disclosure.

Scope of Application

These disclosures are made on a consolidated basis on behalf of Bank Leumi (UK) plc which is a UK incorporated company that is authorised and regulated by the FSA, it is a part of the wider Bank Leumi le-Israel group:



Those entities highlighted represent the main trading subsidiaries of BANK LEUMI (UK) PLC.

For accounting purposes the financial results of Bank Leumi (UK) plc and its subsidiaries are consolidated on a full basis.

From a regulatory prudential perspective Bank Leumi (UK) plc has an approved solo-consolidation waiver granted by the FSA to allow solo-consolidation treatment in respect of itself and its subsidiary Leumi ABL Limited. There is a requirement to calculate and maintain regulatory capital on both a group and solo-consolidated basis.

Bank Leumi (Jersey) limited is regulated by the Jersey Financial Services Commission and has separate regulatory capital requirements. Apart from maintaining their regulatory requirements we can not foresee any material practical or legal impediments to the transfer of capital resources, or the repayment of liabilities within the Bank Leumi (UK) plc Group.

Risk Management Objectives,

Bank Leumi (UK) plc's approach to risk is aimed at ensuring that all significant risks are identified and managed efficiently and appropriately on a timely basis. Risk management is based on certain principles and objectives:

- To clearly apportion management of all risks to risk owners
- To separate risk management functions from risk monitoring functions
- To clearly identify reporting lines
- To align group related functions under the same reporting lines wherever possible to allow for efficiency and the cross-sharing of knowledge.

Risk Management Structure

Group Risk Structure

On a group basis Bank Leumi delegates certain day to day risk management and reporting functions within subsidiary companies to locally based risk committees and/or directly to locally based Board of Directors. Risk issues are where necessary escalated via the Risk Management structure with Bank Leumi (UK) plc.

To facilitate the risk management process, Bank Leumi (UK) plc has established a risk management committee structure.



Risk Management Committee (RMC)

The RMC has prime responsibility for the Bank Leumi (UK) plc Group's risk management structure and strategy. This includes the annual assessment of the Bank's overall risk appetite; the identification, management and apportionment of risk to relevant risk owners; and the review and agreement of the regular Group assessments of compliance, fraud and embezzlement and legal risks, and approval of the resulting documentation prior to submission to the Board for approval. It also considers risks extant in subsidiaries.

Credit Risk Management Committee (CRMC)

The CRMC is responsible for credit risk within the Bank and meets to sanction specific credit applications, and to discuss and monitor wider credit risk issues such as industry sectors, country risk, and other concentrations. It recommends the Bank's credit risk policies to the Board. All policies that form a part of our credit risk appetite are reviewed at least annually.

Market Risk Management Committee (MRMC)

All market risks, including interest rate risk, liquidity risk and basis exposure is the responsibility of the MRMC. The committee reviews and recommends the Bank's market risk policies to the Board. This committee meets weekly.

Due to the limited exposure to market risks, Bank Leumi (UK) plc does not employ sophisticated modelling techniques, however the Risk Control section have extended their independent monitoring of this area especially in relation to derivative transactions.

Operational Risk management Committee (ORMC)

The ORMC is responsible for the Bank's operational risks. The committee recommends the Bank's operational risk policies to the Board for approval. The Director of Finance & Operations has been apportioned with the day to day management responsibility of operational risk.

A monthly report is additionally submitted to the Executive Committee of the Board detailing any problem issues.

Risk Control Department

Bank Leumi (UK) plc has created a single independent department to monitor and control risks. The Risk Control Department is divided into four separate sections:

- The Compliance Section (regulatory risk).
- Risk Control (market risk).
- Loan Review (credit risk).
- Intensive Care and Bad Debts (credit risk).

The Risk Control department remains responsible for monitoring that risk is contained within pre-set parameters. It is also responsible for highlighting changes in risk profiles throughout the Bank that may become apparent from their monitoring duties, or from outside/external events that may affect the Bank.

Credit Risk Monitoring Department

A new department was established at the beginning of 2009 with a principal responsibility to independently monitor credit risk. Its main responsibilities are:

- The independent analysis of credit proposals to include their recommendation on the proposal.
- The review of the content and format of credit applications.
- Quality control of credit proposals.
- Development of credit training.
- Responsibility for the Credit Grading system.
- Input into Credit Policy and Procedures.
- Development of risk/reward pricing guidelines.
- Independent monitoring of collateral positions.
- Monitoring of various sectoral exposures against limits.

The independent credit analysis function ensures that there is independent pre-approval analysis of all credit risks taken.

Credit Risk

Bank Leumi's qualitative Credit Risk Appetite can be summarised as:

- **Knowledge of the customer/counterparty:** New customer business must be properly introduced from a known and trusted source, or there must be some demonstrable reason for a prospective customer approaching the Bank for facilities.
- **Experience of sectors/activities:** Any lending into new areas is agreed only after a full assessment/analysis and after reference to the Credit Committee of the Board.
- **Security:** Lending is generally backed by tangible security, and/or is secured by pledges over a trading customer's debtors and stock, and/or represents transactional finance which allows the Bank to have some control over the title

to assets being financed. Unsecured facilities are only made available to customers of the highest standing.

- **Short Term:** The Bank is essentially a short term lender. Facilities are generally repayable on demand and reviewed at least annually. In certain circumstances a commitment to a term facility is given but, other than for Executive Mortgages, this is treated as an exception to policy and contained within a maximum seven year term.

Credit Policy

The Bank has a comprehensive Credit Policy which sets out the business areas to which finance may be provided, the type of finance which should be provided and the nature of security that should be held. It also defines acceptable loan to value ratios.

Credit Grading

The Bank employs a comprehensive Credit Grading system which allocates Credit Grades to all borrowing customers and is an important component of Credit Policy. Each grade is calculated using a matrix determined by the nature of the customer's activity and is built up using a combination of subjective and objective criteria. Linked to this Grade is Collateral Co-efficient which represents the extent to which a facility is secured. Full details are contained within the Credit Grading Procedures.

Responsibility for the design, maintenance, validation and interrogation of the Credit Grading system rests with Risk Control Department rather than the Business Lines, thus ensuring that the integrity and independence of the system is maintained.

Credit Risk Mitigation

In accordance with the requirements of the Capital Requirements Directive Bank Leumi (UK) plc only recognises certain specified types of financial collateral for providing capital relief. This includes: cash held by the Bank; debt securities issued by central governments, central banks, institutions all of which are rated by a recognised external rating agency; equities or convertible bonds that are included in a main index; and gold.

Bank Leumi (UK) plc utilises the simple method for credit risk mitigation purposes.

Large Exposures Policy

The policy applies to exposures to non-bank customers, banks, Bank Leumi le-Israel Group, counterparties connected to the bank, own-account investments, economic sectors and countries.

As the Bank reports to the FSA on both a solo consolidated basis and a consolidated basis, the policy applies to both the Bank and its subsidiary companies; the Capital Resources within the policy statement refers to either the solo consolidated or the consolidated entity, as appropriate.

Exposures to Customers

The Credit Committee must specifically ratify each of the exposures to individual borrowers or groups of related borrowers in excess of 10% of the Capital Resources and report them to the Board.

Policy states that exposures will not exceed 20% of the Capital Resources other than in exceptional circumstances meeting the criteria set out in the policy statement.

The total of all such Large Exposures, net of specifically charged cash collateral or specific provision, must not exceed our internal limit of 450% of the Capital Resources (the clustering ratio).

Exposures to Banks

Bank limits are formally reviewed by the Market Risk Management Committee at least annually in consultation with our parent company's (Bank Leumi le-Israel B.M.) International Division, and ratified by the Credit Committee. However in view of current market conditions all exposures are under constant monitoring with regular discussions held with our Parent Company.

Monitoring & Review

All relevant personnel within the Bank are aware of the importance of monitoring exposures on a daily basis and of the significance of the Large Exposure Policy. These issues are set out clearly within the Bank's Internal Procedures.

All facilities, whether current or term, are reviewed at least annually and are submitted to the level of authority appropriate for the size of the total obligor. In addition, a separate Loan Review function reviews facilities in accordance with a Loan Review Plan agreed by the Credit Committee, completely independent of the normal credit approval chain within the Bank. Loan Review reports directly to the Credit Committee and the Managing Director & CEO.

To control exposures on a group basis, procedures are in place that requires subsidiaries to seek the approval of Bank Leumi (UK) plc to any exposure, or common or connected exposure that is likely to exceed £3m.

Country Exposure Policy

For determining exposures, credit risk is the amount which the Bank considers to be 'at risk' in any particular transaction, before consideration is given to such issues as the amount of collateral held. In most cases, credit risk equates to exposure, but in the case of forward foreign exchange facilities, credit risk is treated as 1% of the nominal trading limits (exposure) marked.

The Bank may incur Country Risk by undertaking the following types of business in all countries for which an appropriate Country Limit is marked:

- Direct lending to commercial and personal customers
- Provision of trade finance facilities
- Lending to other banks and financial institutions
- Purchase of corporate and sovereign risk for the Bank's own account.

Country Exposure Limits

Country Limits are discussed and agreed by the Credit Risk Management Committee and submitted to the Credit Committee of the Board for approval. All limits are reviewed annually and more frequently whenever prudential considerations dictate.

Monitoring and Controlling Country Exposure

A report detailing total credit risk analysed by country and by type of risk is produced on a monthly basis and presented to the Credit Risk Management Committee and to the Credit Committee of the Board. Where there are concerns relating to any particular country or region, relevant exposures are monitored more frequently.

External Credit Assessments

Bank Leumi (UK) plc uses external credit assessments provided by Moody's who are recognised by the FSA as an eligible external credit assessment institution (ECAI) for the purpose of calculating credit risk requirements under the standardised approach.

External credit assessments are used in relation to the following asset classes:

- Central Governments and Central Banks
- Institutions
- Corporate

Market Risk

Market Risk Appetite

Bank Leumi seeks to engage in activities with only limited market risk exposure. It will only engage in transactions and instruments which would have a limited detrimental effect upon the profit and loss of the Bank's treasury area. The Bank will not enter into new products or markets without fully considering the market risks.

If the Bank engages in derivative transactions for customers the Bank's policy is to close the position in the market thereby eliminating any market risk save for the resulting counterparty exposure. We will only write an option or derivative for the Bank's own account if we hold the underlying product to which the transaction refers, or unless otherwise authorised within the Trading Book Policy.

The types of derivative in which the Bank will trade are limited to F/X options; interest rate/currency swaps; interest rate caps and/or floors; forward rate agreements; and equity options.

Liquidity Policy

The bank must be capable of meeting its obligations or liabilities as they fall due. The bank must provide appropriate liquidity to meet its obligations or liabilities on a usual business day and also at times when markets are stressed or other adverse circumstances could give the bank a greater risk of meeting an unusual level of obligations.

The Bank has historically maintained customer liabilities at a level exceeding customer assets, and has therefore been largely unaffected by recent liquidity issues in the wholesale market.

The bank's obligations mainly consist of deposits at sight or short notice term deposits, commitments to lend, etc.

This capacity is provided by:

1. Holding sufficient cash or liquefiable assets subject to the qualification that marketable assets vary in price.
2. Securing an appropriately matching future profile of cash flow from maturing assets, subject to the qualification that there may be shortfalls in practice if borrowers are unable to repay.
3. Maintaining an adequately diversified deposit base in terms of both maturities and range of counterparties.

Monitoring and Management

The Market Risk Management Committee (MRMC) is responsible for ensuring compliance with the Liquidity policy and for liquidity management generally and in a crisis situation.

The Liquidity position is monitored on a daily basis and is reported to The Market Risk Management Committee on a weekly basis. Projections of the effects of known movements of funds on liquidity are provided. Measurement is based on a cash flow approach inserting assets and liabilities into a maturity ladder and calculating the time band mismatch as a percentage of deposit liabilities.

Interest Rate Risk Policy

The Bank manages interest rate risk in two ways:

1. Limiting an overall loss due to an unexpected pre-set percentile change in the yield curve to an agreed percentage of the Bank's capital base (known as the hard limit).
2. Monitoring and measuring interest rate risk by slotting assets/liabilities into individual time bands and setting limits against those timebands. These limits represent a mismatch of positions which are considered acceptable risk within the total size of the book (known as the soft limits).

Status reports are submitted to the Market Risk Management Committee on a weekly basis for review. In the case of the first "hard" limit, where the limit is broken it is reported to the Board. The second limit for mismatched positions is classified as a "soft" limit where any breaches are dealt with by the MRMC, since individual mismatch position breaches would only give rise to a minimal loss which would fall within the overall maximum loss as defined in 1 above.

Operational Risk

Operational Risk Appetite

Bank Leumi has a low risk appetite for operational risk. The Bank will not enter into new markets, customer types or instruments without fully considering the operational aspects of such. The bank will not enter into structures or transactions, which incur significant operational risks.

The bank makes appropriate investments in technology, capital and staff to ensure that its operational risks are adequately managed.

Operational risk is monitored to continually assess any upwards trends of processing errors, late settlements and other events that can result in operational risk, so that they are identified, investigated and rectified.

Compliance risk appetite

The Bank Leumi (UK) plc Group has a low compliance risk appetite and seeks to ensure:

- Relations with its regulators are clear, open and honest.
- Response to regulatory issues is timely
- Involvement of the Board, Executive and Senior management in compliance matters

The Group does not wish to take regulatory risk. In order to monitor compliance issues the RMC will receive regular reports on issues arising from the compliance monitoring of both the Bank and of its subsidiaries, including a monthly report from the MLROs' of the Bank and of its (Jersey) subsidiaries.

Additionally the Risk Control Manager will provide regular reports to the Audit Committee, and hence to the Board. When necessary, the Risk Control Manager will escalate compliance issues direct to the Board itself.

Assessment of Adequacy of Internal Capital

The Bank's capital adequacy position is measured daily against the regulatory requirement as set by the FSA as per our Individual capital Guidance (ICG) In addition a capital buffer is maintained to ensure that a comfortable margin is maintained at all times to meet growth and any sudden variations.

To ensure that the Bank continues to maintain sufficient capital, as part of the ongoing ICAAP process the Bank's three year plan is modelled to assimilate the capital requirement that would result from the projections within the plan being met. The plan and the resulting capital requirement are then stressed to ascertain the effect of the business plan projections being exceeded.

Additionally certain adverse business scenarios are considered to measure the effect on capital. Such scenarios include a dramatic downturn in the property market; adverse economic trends in both the domestic market, globally, and specifically those overseas markets where the bank has business concentrations.

CAPITAL RESOURCES

The table below summarises the composition of regulatory capital as at 31 December 2008. The group complied with the capital requirements (as set by the FSA) throughout the year, including the make up of the capital to comply with BIPRU 2.2.46.

	As at 31.12.2008 Group
	£000's
Core tier 1 Capital	
Called up ordinary share capital	10,960
Share Premium account	27,100
Profit & Loss reserve	63,504
Minority Interests	40
	<hr/> 101,604
Deductions from core tier 1 capital	
Goodwill on acquisition	(460)
	<hr/> 101,144
Upper tier 2 Capital	
Perpetual subordinated debt	27,000
Collective provision	5,520
	<hr/> 32,520
Lower tier 2 Capital	
Dated subordinated debt	45,466
	<hr/> 77,986
Total tier 2 capital	<hr/> 77,986
Total Regulatory Capital	<hr/> <hr/> 179,130

CAPITAL RESOURCES – Tier 2

The perpetual subordinated loans have an indefinite maturity period, and any repayment of capital at the option of the Bank can be made at the earliest of the fifth anniversary of the date of drawn down of the loan. Advance notification of one month is required to be given to the Financial Services Authority before commencing repayments.

The dated subordinated loan notes, all of which are issued by the parent company, are callable with a notice period of five years and one day given by either the Bank or the Parent company. They can be called at the next interest payment date and after notice is given the redemption will take place following the expiration of five years and one day.

			As at 31.12.2008 Group
	Interest Rate	Interest Fixing	£000's
Upper Tier 2 Capital			
Undated perpetual subordinated debt	6.792%	3 monthly	17,000
Undated perpetual subordinated debt	10.160%	3 monthly	5,000
Undated perpetual subordinated debt	6.873%	6 monthly	5,000
			27,000
Lower tier 2 Capital			
Dated subordinated debt	3.797%	6 monthly	3,578
Dated subordinated debt	3.672%	6 monthly	1,249
Dated subordinated debt	3.547%	6 monthly	30,639
Dated subordinated debt	6.179%	6 monthly	7,500
Dated subordinated debt	9.160%	3 monthly	2,500
			45,466

The rights of the subordinated loan holders are subordinated to the claims of all other creditors of the Bank.

CAPITAL ADEQUACY

The Group's Pillar 1 capital requirement based on 8% of its risk-weighted assets is derived from capital held against risks from the following exposure classes.

	As at 31.12.2008
	Capital Requirement
	£000's
Credit Risk	
Central government or central banks	252
Regional governments or local authorities	-
Administrative bodies and non-commercial undertakings	-
Multilateral development banks	-
International organisations	-
Institutions	5,927
Corporates	33,668
Retail	-
Mortgages secured on real estate properties	16,226
Past due items	4,478
Items belonging to regulatory high risk categories	-
Covered bonds	-
Securitisation positions	-
Short term claims on institutions or corporates	34,320
CIUs	-
Other items	558
	95,429
Operational Risk	5,781
Trading book	
Interest rate PRR	-
Equity PRR	-
Option PRR	-
Counterparty risk capital component	3,230
Concentration risk component	-
Commodity PRR	-
Foreign currency PRR	94
	3,324
Total capital requirement	104,534

Counterparty Credit Risk

The Bank uses derivative instruments to hedge to its exposure to market risk, for example, for foreign exchange and interest rate risk. Counterparty credit risk is the risk that one of the counterparties to a derivative instrument that the Bank holds could default. The risk is mitigated by offsetting the amounts due to the same counterparties ('Netting benefits').

Counterparty credit risk for the Bank is minimal representing only 3% of the total Pillar 1 capital requirement. Therefore on the grounds of materiality, no further detail will be provided on this risk.

CREDIT RISK AND DILUTION RISK

Tables 1 to 4 are based on regulatory credit risk exposure values.

The exposure definition recommended by the BBA Pillar 3 working party and used below is: Exposure at Default (EAD) pre Credit Risk Mitigation (CRM), i.e the regulatory exposure value after the application of Credit Conversion Factors (CCFs) but before CRM. This may differ to statutory reported balance sheet carrying values.

Table 1: Total period end and average exposures after individual impairment and prior to credit risk mitigation by exposure class.

	Exposure as at 31.12.08	Average exposure to 31.12.08
	£000's	£000's
Central government or central banks	15,739	13,327
Institutions	169,137	137,056
Corporates	543,333	470,603
Secured on real estate properties	285,278	314,683
Past due items	49,908	41,899
Short term claims on institutions and corporates	640,556	572,525
Collective Investment Undertaking	-	2,452
Total	1,703,951	1,552,545

Table 2: Period end Geographic distribution of exposure classes

	UK	EU	USA	Israel	Rest of World	Total
	£000's	£000's	£000's	£000's	£000's	£000's
Central government or central banks	-	-	-	15,739	-	15,739
Institutions	92,020	2,711	24,343	32,359	17,704	169,137
Corporates	297,490	139,908	55,032	20,284	30,619	543,333
Secured on real estate properties	258,480	1,038	4,946	-	20,814	285,278
Past due items	21,395	1,369	-	-	27,144	49,908
Short term claims on institutions and corporates	327,982	272,983	686	9,006	29,899	640,556
Total	997,367	418,009	85,007	77,388	126,180	1,703,951

Table 3: Distribution of the exposures by industry or counterparty type

	Central government or central banks	Institutions	Corporates	Secured on real estate	Past due items	Short term claims on institutions and corporates	Total
	€000's	€000's	€000's	€000's	€000's	€000's	€000's
Governments	15,739	-	-	-	-	-	15,739
Banks & Building Societies	-	128,214	-	-	-	212,271	340,485
Financial Services / Institutions	-	40,923	154,650	19,601	1,559	159,816	376,549
Property / Real estate	-	-	48,172	251,115	31,793	134,113	465,193
Retail	-	-	9,017	1	734	2,221	11,973
Wholesale Distributions	-	-	232,407	6,301	14,211	66,943	319,862
Individuals	-	-	58,866	8,187	1,515	26,671	95,239
Other	-	-	40,221	73	96	38,521	78,911
Total	15,739	169,137	543,333	285,278	49,908	640,556	1,703,951

Table 4: Distribution of the exposures by residual maturity

	< 1 year	1 - 5 years	> 5 years	Total
	€000's	€000's	€000's	€000's
Central government or central banks	15,739	-	-	15,739
Institutions	90,104	79,033	-	169,137
Corporates	513,613	29,720	-	543,333
Secured on real estate properties	176,629	102,643	6,006	285,278
Past due items	49,908	-	-	49,908
Short term claims on institutions and corporates	622,947	17,609	-	640,556
Total	1,468,940	229,005	6,006	1,703,951

Tables 5 to 8 are produced on the same basis as the statutory disclosures in the 2008 annual Report & Accounts.

Table 5: Impaired and past due exposures; value adjustments & provisions; charges for value adjustments by significant industry or counterparty type

	Impaired Loans	Past Due Loans	Value adjustments and provisions
	£000's	£000's	£000's
Commercial Banking:			
Secured on real estate	27,226	-	35
Corporates	56,077	2,203	29,551
Total	83,303	2,203	29,586

Table 6: Geographical analysis of impaired exposures and provisions

	UK	EU	USA	Israel	Total
	£000's	£000's	£000's	£000's	£000's
Impaired Loans	44,953	31,486	6,856	8	83,303
Value adjustments and provisions	(14,597)	(8,125)	(6,856)	(8)	(29,586)
Total	30,356	23,361	-	-	53,717

Table 7: Allowances and movements for impairment of loans against credit losses

	Customers Specific	Customers Collective	Total
	£000's	£000's	£000's
As at 1st January 2008	4,363	2,718	7,081
Charge against profits (net of recoveries)	21,291	2,802	24,093
Recoveries	33	-	33
Amount written off	553	-	553
FX Difference	503	-	503
As at 31st December 2008	25,637	5,520	31,157

Table 8: The Income Statement charge/(credit) comprises

	Customers Specific	Customers Collective	Total
	£000's	£000's	£000's

Impairment charge (credit)	21,324	2,802	24,126
Recoveries	(33)	-	(33)
Total Income statement charge/(credit)	21,291	2,802	24,093

CREDIT RISK – STANDARDISED APPROACH

The group calculates credit risk for exposure on its loans and deposits under the standardised approach.

In addition, for the purposes of calculating non-retail credit risk requirements under the standardised approach, the group uses Moody's as its external credit assessment institute (ECAI).

The external rating is mapped to the prescribed credit quality assessment scale that in turn produces standard risk weightings.

The standardised credit risk exposure classes for which ECAI's are used are:-

- Central Government or Central Banks
- Institutions
- Corporates

The following tables 9 to 12 summarise the exposures to rated counterparties.

Table 9: Central Governments or Central Banks

Credit Quality Step (CQS)	Risk Weight	Exposure	Exposure after Credit Risk Mitigation
		£000's	£000's
1	0%	-	-
2	20%	15,739	15,739
3	50%	-	-
4	100%	-	-
5	100%	-	-
6	150%	-	-
		<u>15,739</u>	<u>15,739</u>

Table 10: Corporates

Credit Quality Step (CQS)	Risk Weight	Exposure	Exposure after Credit Risk Mitigation
		£000's	£000's
1	20%	-	-
2	50%	-	5,394
3	100%	10,734	5,340
4	100%	-	-
5	150%	-	-
6	150%	-	-

10,734	10,734
--------	--------

Table 11: Institutions original effective maturity of more than 3 months

Credit Quality Step (CQS)	Risk Weight	Exposure	Exposure after Credit Risk Mitigation
		£000's	£000's
1	20%	96,184	96,184
2	50%	46,846	46,846
3	50%	3,830	3,830
4	100%	-	-
5	100%	3,431	3,431
6	150%	-	-
		150,291	150,291

Table 12: Institutions short term effective maturity of 3 months or less

Credit Quality Step (CQS)	Risk Weight	Exposure	Exposure after Credit Risk Mitigation
		£000's	£000's
1	20%	148,684	148,684
2	20%	-	-
3	20%	-	-
4	50%	-	-
5	50%	-	-
6	150%	-	-
		148,684	148,684

INTEREST RATE RISK

Interest rate risk can be defined as the risk that arises from re-pricing mismatches in the Bank's books in an unstable interest rate period.

The Bank's general policy in relation to interest rate risk is to impose strict limits on re-pricing mismatches which will reduce possible losses.

The bank monitors the interest rate sensitivity gap on a regular basis, calculating the net exposure by major currency and by re-pricing band, categorised by the earlier of contractual re-pricing or maturity dates. The net exposure is determined as the Bank's money market position in cash (spot and forward) and securities, and after setting off the impact of interest rate swaps which hedge against specific positions. The net exposures are compared to limits imposed by the MRMC.

The possible loss in the event of 1% movement in interest rates is calculated on a weekly basis. The possible loss is monitored compared to a limit of 1.5% of the Bank's capital. At

31st December 2008 the possible loss was £0.3 million (2007: £0.3 million) compared with a limit of £2.5 million (2007: £1.8 million).

MARKET RISK

The group uses the maturity approach for general market risk.

Table 13: Capital requirement of market risk

	Capital Requirement	
	Trading book	All activities
	£000's	£000's
Interest rate risk	-	-
Equity position risk	-	-
Option position risk	-	-
Collective investment position risk	-	-
Counterparty risk capital component position risk	-	-
Concentration risk capital component	-	-
Component position risk	-	-
Foreign currency position risk	94	94
Commodity position risk	-	-
Total	94	94

CREDIT RISK MITIGATION

The following table shows the values of collateral and guarantees used as credit risk mitigation within the Pillar 1 Calculations

Table 14: Collateral used as part of credit risk mitigation

	Financial Collateral	Other Eligible Collateral	Guarantees	Totals
	£000's	£000's	£000's	£000's
Standardised approach				
Central government or central banks	-	-	-	-
Institutions	-	-	-	-
Corporates	89,532	27,321	20,778	137,631
Secured on real estate properties	3,391	185	2,655	6,231
Past due items	5	-	275	280
Short term claims on institutions and corporates	38,864	-	4,710	43,574
Total	131,792	27,506	28,418	187,716

