Fidelity Bank (Bahamas) Limited

2009

ANNUAL REPORT

FIDELITY

FIDELITY

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Financial Highlights

SUMMARY OF RESULTS

	2009 ($000)	2008 ($000)
Revenue	14,468	13,923
Expenses	13,110	12,610
Net Income	1,357	1,313
Assets	275,530	272,491
Capital	33,149	32,969
Return on assets	0.5%	0.5%
EPS	5.0 cents	5.0 cents

CAPITAL ADEQUACY

Tier 1[1]	20.84%	25.87%
Tier 1 & 2[2]	22.57%	28.08%

[1] Minimum required 4%

[2] Minimum required 8%

Board of Directors

Sir William Allen, Chairman

Anwer J. Sunderji

Peter Andrews

Frank Crothers

Scott Elphinstone

D. Anthony Jones

Hugh Sands

Chairman's Report

Sir William Allen
Chairman

The enormous global economic challenges which emerged over two years ago continued during 2009 as the World economy registered a decline of just over one half of one per cent and the United States, our major trading partner, declined by 2.4 per cent. In 2009 the Bahamian economy shrank by 4.3 per cent after posting negative growth of 1.7 per cent in the previous year.

The outlook for 2010 is for continued negative growth for the Bahamian economy with improvements beginning to emerge however which are expected to lead to positive growth of about 2.0 per cent in 2011, according to IMF estimates.

At the national level, the need to improve the fiscal balance will drive fiscal policy in the short to medium term and that will constrain public sector spending and maintain upward pressure on taxes and tax collection which will in turn likely reinforce the prevailing moderation of credit growth. Non-performing loans in the domestic banking system are also likely to continue their rise in the short term.

There is no question that these are challenging times but the preponderance of thought is that the worst has passed, although the way forward will likely be slow and rocky. Fortunately the basic fundamentals are still good. The banking system is adequately capitalized. Liquidity is strong. Official external reserves are at an all-time high and the economic weakness has had the effect of improving the trade balance. The national debt, although high by historical standards, is still quite low by regional standards and the external component is less than one-third.

The economy is adequately positioned to benefit from a turnaround in the global economy which hopefully will become evident in the near future.

The bank has necessarily focused on cost containment and management of its non-performing loans in this adverse economic environment to ensure its readiness to derive early benefits as the economy returns to a positive growth path. It had successfully completed its restructuring in 2008, and in 2009 moved to a new banking platform from which it expects to achieve significant operational efficiencies. The bank is therefore well-positioned to benefit as economic circumstances improve, as indeed they will, in due course.

Despite the economic adversity it has still been a successful year for the bank in which it maintained its profit level of the previous year and grew its assets by $3.0 million.

On behalf of the Board of Directors I extend our thanks and appreciation to the management and staff for their dedication and hard work during the year.

We also extend our sincere appreciation to our customers and our shareholders for their continued support and confidence.

Sir William C. Allen
Chairman

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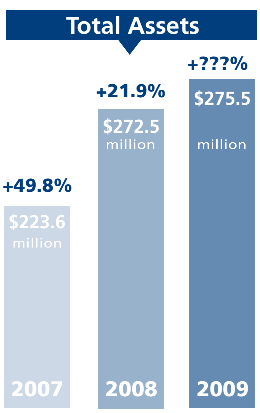
Report from the
Chief Executive Officer

Anwer J. Sunderji

2009 was a difficult year. The Bahamas is suffering from a serious slow down in the economy. Unemployment has soared and this has had a negative impact on loan delinquencies which continued to deteriorate throughout the year and into 2010.

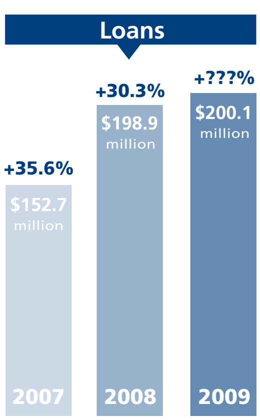
The Central Bank forecasts GDP shrinking by a further 2% in 2010 after a 5% decline in 2009. A protracted and anemic economic recovery is by far the most serious risk the bank faces as it will exacerbate asset quality further. System wide, loan delinquency in the banking industry is about 19% with non-accrual loans around 9%. The bank's delinquencies are consistent with those in the industry.

The Government's most recent budget for 2010/2011 saw several initiatives to increase revenues including a hike in bank license fees of 50%. Lower credit demand, growing delinquencies, excess liquidity and higher costs will have a negative impact on 2010 profitability.



For 2009, the bank reported a profit of $1.3 million, despite deteriorating asset quality resulting in a tripling of bad debt provisions. A hiring freeze in early 2009, coupled with an aggressive enforcement of operating standards, resulted in head count being reduced by about 15%. This reduction in overhead expenses and an increase in the bank's loan portfolio in 2008 helped the bank mitigate the sharp increase in loan loss reserves.

While the net income for the year was little changed from 2008, it masks the considerable improvement in performance as represented by the operating income (income before bad debt provisions and depreciation) of $4.1MM achieved in 2009 compared to $2.6MM in 2008, an increase of some 60%.

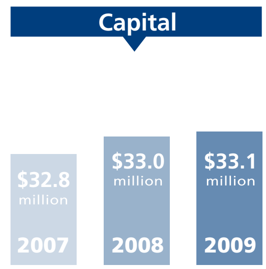


The bank's liquidity deteriorated during 2009 but improving foreign exchange reserves and lower credit demand helped the bank to retrieve and exceed normal liquidity benchmarks by early 2010. In March 2010, the bank had approximately $13MM in excess liquidity.

Credit demand remains muted in general although the bank has successfully launched a campaign to grow its government salary deduction consumer loan book.

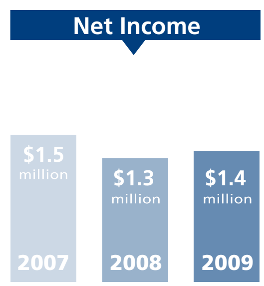
Report from the
Chief Executive Officer *continued...*

The objective is to keep the total loan book flat for the year (net of amortization) at about $200MM while changing the mix to increase consumer loans by $10MM. This will boost operating income (800 bps wider spread on the new loans) which should assist the bank in providing for continuing increase in loan loss provisions for of 2010. An added benefit of this strategy is that the new loans have a term of no more than six years and will likely be refinanced within 2 years. The shortening of maturity will assist the bank in better matching asset liability durations.



The more significant benefit of this strategy is that it appears (surprisingly) that consumer installment loans have a lower delinquency ratio, based on Central Bank statistics. This may be because a significant portion of the loans extended are to civil servants and secured by salary deduction.

With growing delinquencies and slower growth, it seems very likely that credit will be re-priced as banks attempt to repair their balance sheets after the losses they will sustain from the deteriorating loan book. It is estimated that Bahamian banking industry profitability, including Fidelity's, will be severely impacted in 2010 and 2011. The bank expects to remain modestly profitable for 2010.



The bank's focus in 2010 remains on managing risk during these uncertain times, containing expenses, managing asset quality and improving interest spreads. Our expectations are that our balance sheet will not grow with the domestic economy in recession and that there is not much room in further expense reduction. We are focused on improving our bottom line, notwithstanding the growing loan loss provisions, by expanding our spreads through a greater concentration on consumer installment loans.

We take this opportunity to thank our hard working employees, our customers and our patient shareholders as we continue our efforts to improve shareholder value.

Anwer J. Sunderji
Chief Executive Officer

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Management Discussion & Analysis

During 2009, total assets of the Bank increased by $3.0 million, or 1.1% to $275.5 million from $272.5 million in 2008 with total loans increasing by $1.2million, or 0.6%, compared to an increase of $46.7 million, or 30.1%, in 2008.

The Bank reported net income of $1,326,915 or 4.6 cents per share as compared with net income for 2008 of $1,312,606 or 4.6 cents per share. Net income for 2009 was less than budgeted and was severely impacted by the increase in non performing loans and the resulting impact on interest income and provisions for loan losses.

The return on assets for the year was 0.5% compared with 0.5%for 2008.

Dividends of 4 cents per share were paid in 2009 same as in 2008.

CAPITAL ADEQUACY

The banks tier 1 capital is comprised of ordinary share capital, retained earnings and minority interest while the banks tier 2 capital is comprised of tier 1 capital plus revaluation reserves. Using the risk weightings in accordance with the Basle Accord guidelines on capital adequacy, the Banks ratios of risk weighted assets to tier 1 and tier 2 capital as at 31 December 2009 were 21.77% (2008: 20.84%) and 23.51% (2008 22.57%).

The Central Bank guidelines require banks to have a minimum risk-weighted tier 2 capital of 8% with tier 1 capital of at least 4%.

ANALYSIS OF LOAN PORTFOLIO

During 2009, the Bank increased its mortgage loans by $2.3 million (2008: $32.2 million), or 26.0% (2007: 29.4%).

Consumer and other loans remained static for the year due to reduced demand for credit and inability of potential borrowers to qualify

At the end of 2009, mortgage loans comprised 77.8% (2008: 77.4%) of total loans with consumer and other loans comprising the balance of 22.2% (2008: 22.6%) which was less than the bank's targeted ratio.

Total non-performing loans amounted to $18.6 million (2008: $6.7 million) or 9.1% (2008: 3.34%) of total loans. Provision for loan losses represent 1.71% (2008: 1.17%) of the total loan portfolio.

DEPOSIT BASE

During 2009, total deposits grew by $5.7 million (2008: $47.7 million), or 2.7 %, (2008: 29.4%).
Liquidity in the banking system remained high throughout 2009 as credit demand declined significantly

OPERATING REVENUES

Net Interest Income

Net interest income increased slightly from $8.8 million in 2008 to $9.4 million in 2009. The net interest margin, on average total assets decreased from 3.5% in 2008 to 3.4% in 2008.

Non-Interest Income

Non-interest revenues, remained static at $5.1 million in 2009 compared with 2008. At the end of 2009, non-interest revenues comprised 35.0% (2008: 36.9%) of total revenues.

OPERATING EXPENSES

Operating expenses have stabilised in 2009. . Excluding loan loss provision charges, expenses were $11.8 million (2008: $12.4 million) a decrease of $0.6 million (2008 an increase of: $2.3 million) or (5.1%) (2008: 23.0%). The decrease in expenses is the result

- Hiring freeze at all levels in 2009
- Salary freeze for most staff level with a reduction in salaries for senior executives
- Completion of 2008 program of upgrading software , premises and staff and successful move to a new banking platform in mid 2009.

The Bank expects costs to stabilise going forward enabling the bank to reap the reward of its investment strategy.

LOAN LOSS PROVISIONS

Non Performing loans increased steadily throughout the year as the Bahamian economy contracted in line with the USA economy.
Non-performing loans as a percentage of total loans were 9.09 % at the end of 2009 (2008: 3.34 %). The level of loan loss provisions, as a percentage of non-performing loans, decreased from 35 % in 2008 to 18.8 % at the end of 2009 .Mortgages represent $13.0 million of the non performing loans with the balance comprising consumer loans and overdrafts. The bank is of the view that the security on the mortgages is sufficient to ensure that losses on its mortgage book are limited.

The Bank continues to focus on managing its non-performing loans. 2010 is expected to be a challenging year and improvement will only be seen when the USA economy improves.

NEW PRODUCTS & TECHNOLOGY

The Bank successfully moved to a new banking platform in mid 2009 and expects to achieve significant operational efficiencies from this .The Bank has now completed its technology platform and products and will focus on gaining market share and operational efficiencies moving forward.

SUMMARY

2009 has been a challenging year for the bank. Success in some areas, namely cost control and technology have been offset by major increases in loan loss provisions arising from the deterioration in the non performing loan book. Managing the loan book will be the major challenge for 2010 and success in this area will be heavily dependent on improvement in the global economy.

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Fidelity Bank (Bahamas) Limited

We have audited the accompanying consolidated financial statements of Fidelity Bank (Bahamas) Limited (the Bank) and its subsidiary (together, the Group), which comprise the consolidated balance sheet as of 31 December 2009, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the financial position of the Group as of 31 December 2009, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers.

Chartered Accountants
30 April 2010

FIDELITY BANK (BAHAMAS) LIMITED
(Incorporated under the laws of the Commonwealth of The Bahamas)

Consolidated Balance Sheet as of 31 December 2009
(Amounts expressed in Bahamian dollars)

	2009 $	2008 $
ASSETS		
Cash on hand and at banks (Note 3)	28,479,649	18,646,538
Investment securities (Note 4)	28,152,658	36,615,975
Mortgages, consumer and other loans (Note 5)	200,121,534	198,861,978
Property, plant and equipment (Note 6)	12,388,180	12,286,606
Prepayments and other assets	6,388,145	6,079,617
Total assets	**275,530,166**	**272,490,714**
LIABILITIES		
Customer deposits (Note 7)	217,035,497	210,699,878
Debt securities (Note 8)	24,898,349	28,107,262
Accrued expenses and other liabilities (Note 9)	447,404	714,906
Total liabilities	**242,381,250**	**239,522,046**
EQUITY		
Share capital (Note 10)	20,000,001	20,000,001
Revaluation surplus	2,452,416	2,526,329
Reserve for credit losses (Note 16)	2,102,818	-
Retained earnings	8,593,681	10,442,338
Total equity	**33,148,916**	**32,968,668**
Total liabilities and equity	**275,530,166**	**272,490,714**

APPROVED BY THE BOARD OF DIRECTORS AND SIGNED ON ITS BEHALF BY:

William C. Allen
Director

A Sunderland
Director

29 April 2010
Date

The accompanying notes are an integral part of these consolidated financial statements.

FIDELITY BANK (BAHAMAS) LIMITED

Consolidated Income Statement for the Year Ended 31 December 2009

(Amounts expressed in Bahamian dollars)

	2009 $	2008 $
INCOME		
Interest income		
Bank deposits and loans	19,686,780	17,312,334
Investment securities	1,188,756	1,283,413
	20,875,536	18,595,747
Interest expense	(11,156,032)	(9,812,443)
Net interest income	**9,719,504**	**8,783,304**
Non-interest income	5,054,169	5,139,846
	14,773,673	**13,923,150**
EXPENSES		
Salaries and employee benefits	5,604,650	5,771,289
General and administrative	5,065,815	5,541,219
Provision for loan losses (Note 5)	1,316,265	231,261
Depreciation and amortisation (Note 6)	1,429,719	1,066,775
	13,416,449	**12,610,544**
Net income	**1,357,224**	**1,312,606**
OTHER COMPREHENSIVE INCOME		
Property, plant and equipment revaluation	(30,309)	-
	(30,309)	-
Total comprehensive income	**1,326,915**	**1,312,606**
Weighted average number of ordinary shares outstanding	**28,666,670**	**28,666,670**
Earnings per share	**$0.05**	**$0.05**

The accompanying notes are an integral part of these consolidated financial statements.

FIDELITY BANK (BAHAMAS) LIMITED

Consolidated Statement of Changes in Equity for the Year Ended 31 December 2009

(Amounts expressed in Bahamian dollars)

	Share Capital $	Revaluation Surplus $	Retained Earnings $	Reserve for Credit Losses $	Total $
As of 1 January 2008	20,000,001	2,572,037	10,230,691	-	32,802,729
Comprehensive income					
Net income	-	-	1,312,606	-	1,312,606
Other comprehensive income					
Depreciation transfer	-	(45,708)	45,708	-	-
Total comprehensive income	-	(45,708)	1,358,314	-	1,312,606
Transactions with owners					
Dividends	-	-	(1,146,667)	-	(1,146,667)
Total transactions with owners	-	-	(1,146,667)	-	(1,146,667)
As of 31 December 2008	**20,000,001**	**2,526,329**	**10,442,338**	**-**	**32,968,668**
As of 1 January 2009	20,000,001	2,526,329	10,442,338	-	32,968,668
Comprehensive income					
Net income	-	-	1,507,224	-	1,507,224
Other comprehensive income					
Property, plant and equipment revaluation	-	(30,309)	-	-	(30,309)
Depreciation transfer	-	(43,604)	43,604	-	-
Total comprehensive income	-	(73,913)	1,550,828	-	1,476,915
Transactions with owners					
Appropriation for credit losses	-	-	(2,102,818)	2,102,818	-
Dividends	-	-	(1,146,667)	-	(1,146,667)
Total transactions with owners	-	-	(3,249,485)	2,102,818	(1,146,667)
As of 31 December 2009	**20,000,001**	**2,452,416**	**8,743,681**	**2,102,818**	**33,298,916**

Dividends per share: $0.04 (2008: $0.04)

The accompanying notes are an integral part of these consolidated financial statements.

FIDELITY BANK (BAHAMAS) LIMITED

Consolidated Cash Flow Statement for the Year Ended 31 December 2009

(Amounts expressed in Bahamian dollars)

	2009 $	2008 $
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	1,357,224	1,312,606
Adjustments for:		
Interest income	(20,875,536)	(18,595,747)
Interest expense	11,156,032	9,812,443
Provision for loan losses	1,316,265	231,261
Depreciation and amortisation	1,429,719	1,066,775
Net change in unrealised appreciation/depreciation of investment securities	(253,096)	1,687,613
Realised (gains)/losses on investment securities	2,158,007	(6,859)
(Gain)/Loss on disposal of property, plant and equipment	-	(4,617)
Interest received	20,720,677	17,906,253
Interest paid	(10,492,460)	(8,839,967)
(Increase)/Decrease in operating assets		
Mandatory reserve deposits	(851,030)	(1,758,048)
Mortgages, consumer and other loans	(2,451,291)	(45,699,837)
Prepayments and other assets	(1,168,164)	(4,633,682)
Increase/(Decrease) in operating liabilities		
Customer deposits	5,690,989	46,891,911
Accrued expenses and other liabilities	(267,502)	107,890
Net cash from/(used in) operating activities	**7,469,834**	**(522,005)**
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of investment securities	(1,793,784)	(162,690)
Proceeds from sale of investment securities	8,382,519	502,359
Purchase of property, plant and equipment	(1,561,602)	(2,108,356)
Proceeds from sale of property, plant and equipment	-	69,000
Net cash from/(used in) investing activities	**5,027,133**	**(1,699,687)**
CASH FLOWS FROM FINANCING ACTIVITIES		
Repayment of loan from bank	-	(146,403)
Issuance of debt securities	-	6,850,000
Repayment of debt securities	(3,227,855)	(6,000,022)
Dividends paid	(287,031)	(1,146,667)
Net cash used in financing activities	**(3,514,886)**	**(443,092)**
Net increase/(decrease) in cash and cash equivalents	**8,982,081**	**(2,664,784)**
Cash and cash equivalents as of beginning of year	11,332,468	13,997,252
Cash and cash equivalents as of end of year	**20,314,549**	**11,332,468**

See Notes 4 and 13 for significant non-cash transactions.

The accompanying notes are an integral part of these consolidated financial statements.

1. General Information

Fidelity Bank (Bahamas) Limited (the Bank) is incorporated under the Companies Act, 1992 of the Commonwealth of The Bahamas (The Bahamas) and is licensed under the Banks and Trust Companies Regulation Act, 2000 to carry on banking business in The Bahamas. The Bank offers a full range of retail banking services, including internet and telephone banking, acceptance of deposits, granting of loans and the provision of foreign exchange services through each of its four branches in New Providence, its branch in Grand Bahama and its branch in Abaco.

The Bank has one subsidiary, West Bay Development Company Limited, a property holding company incorporated in The Bahamas, which owns a building principally occupied by the Bank and its related parties. The Bank and its subsidiary are collectively referred to as the Group.

Fidelity Bank & Trust International Limited (the Parent), a company incorporated in The Bahamas, owns 76% (2008: 75%) of the issued ordinary shares of the Bank, with the balance being held by the Bahamian public.

The registered office of the Bank is situated at #51 Frederick Street, Nassau, Bahamas. As of 31 December 2009, the Bank employed 154 (2008: 162) persons.

The shares of the Bank are listed on The Bahamas International Stock Exchange (BISX).

2. Summary of Significant Accounting Policies

The principal accounting policies adopted in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

(a) Basis of preparation

The consolidated financial statements are prepared in accordance with International Financial Reporting Standards (IFRS), and under the historical cost convention, except as disclosed in the accounting policies below.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Group's accounting policies. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results could differ from those estimates. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements are disclosed in Notes 2(d), 2(g) and 11.

In the current year, the Group adopted IAS 1 (Revised) *Presentation of Financial Statements* and the amendment to IFRS 7 *Financial Instruments: Disclosures* which became effective for fiscal periods beginning on or after 1 January 2009; and IFRIC 13 *Customer Loyalty Programmes* which became effective for fiscal periods beginning on or after 1 July 2008. IAS 1 (Revised) requires non-owner changes in equity to be presented separately from owner changes in equity, resulting in a consolidated statement of comprehensive income. The amendment to IFRS 7 requires enhanced disclosures about fair value measurements and liquidity risk. IFRIC 13 clarifies the accounting treatment for customer loyalty programmes, with consideration received from customers where services are sold together with a customer loyalty incentive being allocated between revenue for the service and revenue/deferred revenue associated with the incentive. The adoption of the revised and amended standards and interpretation did not result in any material impact on the consolidated financial statements. Corresponding information has been re-presented to conform with new disclosure requirements.

2. Summary of Significant Accounting Policies (Continued)

(a) Basis of preparation (continued)

The remaining standards and amendments and interpretations to published standards that became effective for fiscal periods beginning on or after 1 January 2009 were not relevant to the Group's operations and accordingly did not impact the Group's accounting policies or consolidated financial statements.

The application of new standards and amendments and interpretations to existing standards that have been published but are not yet effective are not expected to have a material impact on the Group's accounting policies or consolidated financial statements in the period of initial application.

(b) Principles of consolidation

Subsidiaries are all entities over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are de-consolidated from the date that control ceases.

Inter-company transactions, balances and unrealised gains on transactions between group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting polices of subsidiaries are changed where necessary to ensure consistency with the policies adopted by the Group.

(c) Foreign currency translation

i) Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency). The consolidated financial statements are presented in Bahamian dollars (B$), which is the Bank's functional and presentation currency.

ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the date of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated statement of comprehensive income. Translation differences on financial assets measured at fair value through profit or loss are included as part of the fair value gains and losses.

(d) Financial assets

The Group classifies its financial assets in the following categories: financial assets at fair value through profit or loss and loans and receivables. Management determines the classification of its financial assets at initial recognition.

2. Summary of Significant Accounting Policies (Continued)

(d) Financial assets (continued)

i) Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is classified in this category if acquired principally for the purpose of selling in the short term or if so designated by management. Investment securities have been designated as financial assets at fair value through profit or loss.

ii) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They arise when the Group provides money, goods or services directly to a debtor with no intention of trading the receivable.

Regular-way purchases and sales of financial assets are recognised on the trade date – the date on which the Group commits to originate, purchase or sell the asset. Financial assets are initially recognised at fair value plus transaction costs, except financial assets carried at fair value through profit or loss where such costs are expensed as incurred. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or when the Group has transferred substantially all risks and rewards of ownership.

Financial assets at fair value through profit or loss are subsequently carried at fair value. Fair value is based on quoted prices for investments traded in an active market (e.g. international securities exchange) or valuation techniques, including recent arm's length transactions, discounted cash flow analysis and other valuation techniques commonly used by market participants, for securities not traded in active market. Loans and receivables are subsequently carried at amortised cost less provisions for impairment.

Gains and losses arising from sales or changes in fair value of financial assets at fair value through profit or loss are recognised in the consolidated statement of comprehensive income within "non-interest income" in the period in which they arise.

(e) Non-performing assets

All loans on which principal or interest payments are overdue in excess of ninety days are classified by management as non-performing, and monitored closely for impairment.

(f) Borrowings

Borrowings, which include debt securities, are recognised initially at fair value, net of transaction costs incurred. Borrowings are subsequently recognised at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the consolidated statement of comprehensive income over the period of the borrowings using the effective interest method.

(g) Income and expense recognition

Interest income and expense are recognised in the consolidated statement of comprehensive income for all instruments measured at amortised cost using the effective interest method. Loan origination fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loans.

2. **Summary of Significant Accounting Policies (Continued)**

(g) **Income and expense recognition (continued)**

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense 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, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Fee and commission income is recognised on the completion of the underlying transaction, which is generally at the time the customer's account is charged. Dividend income is recognised in the consolidated statement of comprehensive income when the Group's right to receive payment has been established.

Other income and expenses are recognised on the accrual basis.

(h) **Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount reported in the consolidated balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(i) **Impairment of financial assets at amortised cost**

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

If there is objective evidence that an impairment loss on loans and receivables has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated statement of comprehensive income. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

(j) **Property, plant and equipment**

Property, plant and equipment, other than land and buildings, are carried at historical cost less accumulated depreciation and amortisation. Historical cost includes expenditure that is directly attributable to the acquisition of an item. Land and buildings, which comprise branches and offices for the Group's operations, are carried at fair value based upon periodic independent appraisals that are commissioned at intervals not exceeding three years, less subsequent depreciation for buildings.

2. Summary of Significant Accounting Policies (Continued)

(j) Property, plant and equipment (continued)

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All repairs and maintenance are charged to the consolidated statement of comprehensive income during the financial period in which they are incurred.

Increases in the carrying amount arising on revaluation of land and buildings are credited to "revaluation surplus" in equity. Decreases that offset previous increases of the same asset are charged against revaluation surplus directly in equity; all other decreases are charged to the consolidated statement of comprehensive income. Each year the difference between depreciation based on the revalued carrying amount of the asset charged to the consolidated statement of comprehensive income and depreciation based on the asset's original cost is transferred from revaluation surplus to retained earnings.

Land is not depreciated. Depreciation on other assets is calculated using the straight-line method to allocate costs (net of residual values) over estimated useful lives as follows:

	Estimated Useful Life
Buildings	30 - 50 years
Furniture and fixtures	3 - 10 years
Motor vehicles	3 - 5 years
Computer software and office equipment	3 - 10 years
Leasehold improvements	Lesser of lease term and 3 - 10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each balance sheet date. Assets that are subject to depreciation and amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and its value in use.

Gains and losses on disposals are determined by comparing proceeds with the carrying amount and are recognised in the consolidated statement of comprehensive income. When revalued assets are sold, amounts included in revaluation surplus are transferred directly to retained earnings.

(k) Leases

i) The Group is the lessee

The leases entered into by the Group are operating leases. The total payments made under operating leases are charged to the consolidated statement of comprehensive income on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

ii) The Group is the lessor

Leases comprise operating leases. Lease income is recognised over the term of the lease on a straight-line basis.

2. Summary of Significant Accounting Policies (Continued)

(l) Share capital

i) Share issue costs

Incremental costs directly attributable to the issue of new shares or options or to the acquisition of a business are shown in equity as a deduction from the proceeds.

ii) Dividends

Dividends on ordinary shares are recognised in equity in the period in which they are approved by the Bank's Directors. Dividends for the year that are declared after the balance sheet date are disclosed in the subsequent events note.

(m) Cash and cash equivalents

For the purposes of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and unrestricted deposits with banks that have original contractual maturities of three months or less.

(n) Provisions

Provisions for restructuring costs and legal claims are recognised when the Group has a present legal or constructive obligation as a result of past events, and it is more likely than not that an outflow of resources will be required to settle the obligation and the amount has been reliably estimated.

(o) Employee benefits

The Group's employees participate in a defined contribution pension plan of a related party, administered by trustees that include executives of the Bank.

A defined contribution plan is a pension plan under which the Group pays fixed contributions into a separate entity. The Group has no legal or constructive obligations to pay further contributions if the plan does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods. The contributions are recognised as employee benefits expense in the consolidated statement of comprehensive income when they are due. The Group has no further payment obligations once the recognised contributions have been paid.

(p) Segment reporting

A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different from those of other business segments. A geographical segment is engaged in providing products or services within a particular economic environment that are subject to risks and returns that are different from those of segments operating in other economic environments.

The vast majority of the Group's activities are retail banking and all of its activities are based in The Bahamas. Therefore the Group has only one business segment and one geographical segment that require segment reporting. As such, no segment disclosures are made in these consolidated financial statements.

2. **Summary of Significant Accounting Policies (Continued)**

(q) **Fiduciary activities**

The Group acts as custodian, trustee and in other fiduciary capacities that result in the holding or placing of assets on behalf of individuals, investment funds and other entities. These assets are excluded from these consolidated financial statements, as they do not belong to the Group.

(r) **Corresponding figures**

Where necessary, corresponding figures are adjusted to conform with changes in presentation in the current year.

3. **Cash on Hand and at Banks**

	2009 $	2008 $
Cash on hand	4,306,305	3,119,966
Deposits at banks	16,008,244	8,212,502
Cash and cash equivalents	20,314,549	11,332,468
Mandatory reserve deposits	8,165,100	7,314,070
	28,479,649	**18,646,538**

Mandatory reserve deposits are placed with the Central Bank of The Bahamas (the Central Bank) to meet requirements of the Bank's licence and are not available for use in the Group's day to day operations. Cash on hand, and mandatory reserve deposits and other deposits with the Central Bank are non-interest-bearing. Deposits at banks earn interest rates ranging from 0.00% to 3.00% (2008: 0.00% to 5.50%).

4. **Investment Securities**

Financial assets at fair value through profit or loss

The Bank ranks its investment securities based on the hierarchy of valuation techniques required by IFRS, which is determined based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Group's market assumptions. These two types of inputs lead to the following fair value hierarchy:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes equity securities and debt instruments listed on exchanges.

Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes the government debt securities and other securities with observable inputs.

Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity securities and debt instruments with significant unobservable components. This hierarchy requires the use of observable market data when available. The Group considers relevant and observable market prices in its valuations where possible.

4. Investment Securities (Continued)

	2009 $	2008 $
Level 1		
Equity securities	2,681,129	-
Level 2		
Government debt securities	19,400,900	21,378,700
Corporate debt securities	100,000	-
Equity securities	239,808	-
	19,740,708	21,378,700
Level 3		
Mutual fund shares (Note 8)	4,729,939	14,845,751
Corporate debt securities	409,740	-
Equity securities	169,289	-
	5,308,968	14,845,751
Total – all levels	27,730,805	36,224,451
Accrued interest	421,853	391,524
Total	**28,152,658**	**36,615,975**

Government securities principally comprise Bahamas Government Registered Stock with maturities ranging from 2010 to 2036 (2008: 2010 to 2033) and with interest rates ranging from 0.09% to 1.25% above the B$ Prime rate of 5.50% (2008: 5.50%). The Bank has pledged $3 million of such securities to support a credit facility of the same amount with another Bahamian commercial bank (Note 14).

As of 31 December 2009, the cost of investment securities totalled $27,938,411 (2008: $36,685,153), of which $5,565,544 (2008: $15,291,689) represented Level 3 securities.

During the year, movements in Level 3 securities comprise:

	Mutual Fund Shares $	Corporate Debt Securities $	Equity Securities $	Total $
Balance as of 1 January 2009	14,845,751	-	-	14,845,751
Purchases	264,565	409,740	169,289	843,594
Sales	(8,411,732)	-	-	(8,411,732)
Realised gains/(losses)	(2,158,007)	-	-	(2,158,007)
Net change in unrealised appreciation/depreciation	189,362	-	-	189,362
Balance as of 31 December 2009	**4,729,939**	**409,740**	**169,289**	**5,308,968**

In 2007, the Group purchased mutual fund shares from a related party, Royal Fidelity Merchant Bank & Trust Limited, as part of a transaction involving the Parent. Effective 1 January 2008, the Bank entered into a yield management agreement with the Parent to limit its exposure to changes in market prices (Note 13).

4. Investment Securities (Continued)

Under the agreement the Parent guarantees a yield of 6.00% per annum plus 25% of any gain in excess of 6.00% per annum; any remaining gain in excess of 6.00% per annum is to be remitted to the Parent. All securities, except government debt securities, are subject to the agreement.

The Group has been redeeming a portion of the mutual fund shares each month since the acquisition of the portfolio. In 2009, the Group requested the redemption of shares with fair values totalling $5 million that was settled by the relevant fund exchanging a portfolio comprising other mutual fund shares, corporate debt securities and equity securities, with a value equal to the redemption values. Certain of the securities received were subsequently sold including the Bank's own shares, which were sold to the Parent.

Effective 1 July 2009, the Group entered into an arrangement with the aforementioned related party, which serves as investment manager of the mutual fund, to rebate to the Group 50% of the investment management fees charged to the mutual fund in relation to shares of the mutual fund owned by the Group.

5. Mortgages, Consumer and Other Loans

	2009 $	2008 $
Mortgages	158,634,164	156,209,727
Consumer and other loans	45,333,857	45,468,927
	203,968,021	201,678,654
Loan origination fees	(1,402,052)	(1,370,158)
Accrued interest	1,065,604	909,180
Provision for loan losses	(3,510,039)	(2,355,698)
Total	**200,121,534**	**198,861,978**

Movements in provision for loan losses are as follows:

	2009			2008		
	Mortgages $	Consumer $	Total $	Mortgages $	Consumer $	Total $
Balance as of 1 January	1,086,116	1,269,582	2,355,698	1,294,720	837,147	2,131,867
Provision during the year	(122,750)	1,439,015	1,316,265	(208,604)	439,865	231,261
Write-offs during year	-	(161,924)	(161,924)	-	(7,430)	(7,430)
Balance as of 31 December	**963,366**	**2,546,673**	**3,510,039**	**1,086,116**	**1,269,582**	**2,355,698**

The provision for loan losses represents 1.71% (2008: 1.16%) of the total loan portfolio, inclusive of accrued interest, and 19.79% (2008: 34.98%) of total non-performing loans.

As of 31 December 2009, principal and interest balances of non-performing loans totalled $17,734,932 (2008: $6,734,209), representing 8.70% (2008: 3.34%) of the total loan portfolio.

6. Property, Plant and Equipment

	Land & Buildings $	Furniture & Fixtures $	Motor Vehicles $	Computer Software & Office Equipment $	Leasehold Improvements $	Total $
Cost or valuation:						
As of 1 January 2009	6,700,000	3,350,475	69,930	6,145,057	5,669,426	21,934,888
Additions	-	120,127		1,162,389	279,086	1,561,602
Revaluation	(400,000)	-	-	-	-	(400,000)
As of 31 December 2009	**6,300,000**	**3,470,602**	**69,930**	**7,307,446**	**5,948,512**	**23,096,490**
Accumulated depreciation/ amortisation:						
As of 1 January 2009	242,501	1,982,646	25,762	4,678,151	2,719,222	9,648,282
Charge for the year	127,190	283,356	12,353	539,245	467,575	1,429,719
Revaluation	(369,691)	-	-	-	-	(369,691)
As of 31 December 2009	**-**	**2,266,002**	**38,115**	**5,217,396**	**3,186,797**	**10,708,310**
Net book value:						
As of 31 December 2009	**6,300,000**	**1,204,600**	**31,815**	**2,090,050**	**2,761,715**	**12,388,180**
As of 31 December 2008	**6,457,499**	**1,367,829**	**44,168**	**1,466,906**	**2,950,204**	**12,286,606**

Land and buildings were revalued by an independent appraiser as of 31 December 2009.

If land and buildings were stated on an historical cost basis, the amounts would be as follows:

	2009 $	2008 $
Cost	4,443,450	4,443,450
Accumulated depreciation	(595,866)	(512,280)
Net book value	**3,847,584**	**3,931,170**

7. Customer Deposits

	2009 $	2008 $
Demand deposits	16,499,246	20,455,653
Savings deposits	33,934,328	39,158,965
Escrow deposits	825,488	768,726
Term deposits	162,725,357	147,910,086
	213,984,419	208,293,430
Accrued interest	3,051,078	2,406,448
Total	**217,035,497**	**210,699,878**

All customer deposits carry fixed interest rates ranging from 2.50% to 7.25% (2008: 2.50% to 7.25%).

8. Debt Securities

	2009 $	2008 $
Series A redeemable fixed rate (7.00%) notes; 2017	4,917,069	4,909,653
Series B redeemable floating rate (B$ Prime + 1.75%) notes; 2022	9,820,328	9,812,359
Series C redeemable fixed rate (7.00%) notes; 2013	2,966,837	2,958,803
Series D redeemable floating rate (B$ Prime + 1.75%) notes; 2015	6,913,168	6,900,833
Short-term note issued to related party	-	3,227,855
	24,617,402	27,809,503
Accrued interest	280,947	297,759
	24,898,349	**28,107,262**

During 2008, as part of a $50,000,000 note programme approved by the Directors, the Bank offered through private placement, $10,000,000 of unsecured fixed and floating rate notes consisting of Series C - $3,000,000 redeemable 7% fixed rate notes due 30 May 2013 and Series D - $7,000,000 redeemable floating rate notes (B$ Prime rate plus 1.750%) due 30 May 2015. Interest is payable semi-annually on 30 May and 30 November each year. Costs of the notes issue totalled $150,000, all of which were paid to a related party, and are being amortised on an effective yield basis over the life of the notes.

During 2007, the Bank offered, through private placement, $15,000,000 of unsecured fixed and floating rate notes consisting of Series A - $5,000,000 redeemable 7% fixed rate notes due 19 October 2017 and Series B - $10,000,000 redeemable floating rate notes (B$ Prime rate plus 1.750%) due 19 October 2022. Interest is payable semi-annually on 19 April and 19 October each year. Costs of the notes issue totalled $294,202 and are being amortised on an effective yield basis over the life of the notes.

Also during 2007, the Bank issued of a promissory note of $12,227,877 in settlement of the purchase of an investment portfolio from a related party (Note 4). The promissory note was unsecured, accrued interest at the rate of 5.50% per annum and was payable on or before 31 May 2008. In May 2008, the agreement was amended and the related party agreed to subscribe for $3 million of Series D floating rate notes issued by the Bank in partial repayment, with the balance to be repaid in monthly installments of $1,000,000 plus accrued interest commencing 4 July 2008 with interest at B$ Prime rate on the outstanding balance. The note was repaid in full during 2009.

9. Accrued Expenses and Other Liabilities

	2009 $	2008 $
Accrued expenses	447,404	524,733
Due to related parties	-	190,173
Total	**447,404**	**714,906**

10. Share Capital

	2009 $	2008 $
Authorised		
35,000,000 ordinary shares of $0.30 each	**10,500,000**	**10,500,000**
10,000,000 preference shares of $1.00 each	**10,000,000**	**10,000,000**
Issued and fully paid		
28,666,670 ordinary shares	8,600,001	8,600,001
Share premium	11,400,000	11,400,000
Total	**20,000,001**	**20,000,001**

11. Critical Accounting Estimates and Judgments in Applying Accounting Policies

The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and assumptions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Impairment losses on mortgages, consumer and other loans

The Group reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the consolidated statement of comprehensive income, the Group makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio.

This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or economic conditions that correlate with defaults on assets in a group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

12. Employee Benefits

The Group participates in a defined contribution pension plan, Fidelity Merchant Bank & Trust Limited Employees Pension Plan (the Plan), which covers all employees of the Parent's Bahamas based operations. Under the Plan, all employees contribute 5% of gross salary and the Group matches employees' contributions.

Pension expense for the year ended 31 December 2009 totalled $223,934 (2008: $262,916), and is included in salaries and employee benefits in the consolidated statement of comprehensive income.

13. Related Party Balances and Transactions

Related parties include those entities and individuals that have the ability to control or exercise significant influence over the Group in making financial or operational decisions, and entities that are controlled, jointly controlled or significantly influenced by them.

13. Related Party Balances and Transactions (Continued)

Related party balances and transactions, not disclosed elsewhere in these consolidated financial statements, are as follows:

	2009 $	2008 $
ASSETS		
Cash at banks		
Other related parties	2,821,514	2,532,340
Investment securities		
Other related parties	4,729,939	14,845,751
Other assets		
The Parent	4,914,009	4,463,327
Other related parties	71,194	523,030
LIABILITIES		
Customer deposits (excluding directors and officers)		
The Parent	1,458,061	1,559,057
Other related parties	9,190,310	5,837,306
Debt securities		
Other related parties	4,243,500	3,227,855
INCOME		
Non-interest income		
The Parent	2,690,618	2,697,688
Other related parties	186,366	140,848
EXPENSES		
Costs allocated to other related parties	(1,591,138)	(1,363,827)

Loans to and deposits from directors and officers totalled $1,783,946 (2008: $2,207,860), and $293,424 (2008: $740,978), respectively.

Included in other assets are amounts due from the Parent in relation to the yield management agreement described in Note 4. For the year ended 31 December 2009, the Group recorded income of $2,690,618 (2008: $2,697,688) pursuant to this agreement. During the year, dividends of $859,636 (2008: $859,636) payable to the Parent were applied against amounts owing to the Group from the Parent.

Amounts due from related parties included in other assets are unsecured, interest-free and have no set terms of repayment.

Non-interest income from other related parties includes income of $50,000 from the rebate arrangement described in Note 4. The Bank provides certain services to the Parent and other related parties under service agreements; incurred costs associated with these services are allocated to the respective parties and are recorded as deductions in the relevant expense accounts.

Key management compensation (excluding directors) for the year totalled $659,839 (2008: $677,273). Included in costs allocated from related parties above are costs for key management personnel compensation of related parties that have been allocated to the Group based on services provided to the Group by such personnel. Directors' compensation (including cost of attending meetings) for the year totalled $76,736 (2008: $78,020).

14. Commitments

Loan commitments

In the normal course of business, the Bank enters into various credit-related arrangements to meet the needs of customers and earn income. These financial instruments are subject to the Bank's standard credit policies and procedures. As of 31 December 2009, these credit-related arrangements were as follows:

	2009 **$**	**2008** **$**
Loan commitments	3,569,577	15,700,827

Lines of credit

The Bank has a credit facility of $3 million with another Bahamian commercial bank. The facility bears interest at 0.50% above the B$ Prime rate up to $1 million and 1.25% above the B$ Prime rate for amounts in excess of $1 million with a stand by fee of 0.25% per annum on any unused portion of the facility. The Bank has pledged investment securities in support of the credit facility (Note 4).

As of 31 December 2009, the line of credit with the commercial bank was not utilised (2008: line of credit was fully utilised and included in customer deposits).

Operating lease commitments

The future minimum rental payments required under non-cancellable operating leases as of 31 December 2009 are as follows:

	2009 **$**	**2008** **$**
2009	-	511,370
2010	436,481	436,481
2011	397,333	397,333
2012	289,000	289,000
2013	289,000	289,000
2014	38,000	38,000
2015	38,000	38,000
2016	39,000	39,000
2017	39,000	39,000
Total minimum payments	**1,565,814**	**2,077,184**

15. Contingent Liabilities

The Group is involved in various legal proceedings covering a range of matters that arise in the ordinary course of business activities. Management is of the view that no significant losses will arise as a result of these proceedings.

16. **Reserve For Credit Losses**

The reserve for credit losses was created by the appropriation of retained earnings in order to meet the requirements of the Central Bank for credit loss provisions. The reserve represents the provision required by the Central Bank in excess of amounts calculated in accordance with IFRS.

17. **Capital Management**

The Group's objectives when managing capital, which is a broader concept than 'equity' on the face of the consolidated balance sheet, are:

- To comply with the capital requirements set by the Central Bank;
- To safeguard the Group's ability to continue as a going concern so that it can continue to provide returns for its shareholders and benefits for other stakeholders; and
- To maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored by the Group's management, employing techniques designed to ensure compliance with guidelines established by the Central Bank. The required information is filed with the Central Bank on a quarterly basis.

The Central Bank requires that the Bank maintains a ratio of total regulatory capital to risk-weighted assets at or above a minimum of 8%.

The table below summaries the composition of regulatory capital and shows the capital adequacy ratio of the Group, determined in accordance with the Basle Accord, as of the consolidated balance sheet date. During 2009, the Group complied with all of the externally imposed capital requirements to which it is subject.

	2009 **$**	**2008** **$**
Tier 1 capital		
Share capital	20,000,001	20,000,001
Retained earnings	8,743,681	10,442,338
Reserve for credit losses	2,102,818	-
	30,846,500	30,442,339
Tier 2 capital		
Revaluation surplus	2,452,416	2,526,329
Total	**33,298,916**	**32,968,668**
Risk-weighted assets	**140,998,076**	**146,060,668**
Capital adequacy ratio – Tier 1	**21.88%**	**20.84%**
Capital adequacy ratio – Tier 1 and 2	**23.62%**	**22.57%**

18. Financial Risk Management

Strategy in using financial instruments

By their nature, the Group's activities are principally related to the use of financial instruments. The Group accepts deposits from customers at both fixed and floating rates, and for various periods, and seeks to earn above-average interest margins by investing these funds in high-quality assets – predominantly mortgages. The Group seeks to increase these margins by consolidating short-term funds and lending for longer periods at higher rates, while maintaining sufficient liquidity to meet all claims that might fall due.

The Group also seeks to raise its interest margins by obtaining above-average margins, net of allowances, through lending to commercial and retail borrowers with a range of credit standings. Such exposures involve not just on-balance sheet loans and advances but include guarantees and other commitments such as letters of credit, and performance and other bonds.

The principal risks which arise from the Group's core activities that must be effectively managed include credit, interest rate, price, liquidity and fiduciary risks. The Group does not use derivative instruments to manage any of these risks.

Credit risk

Credit risk is the risk that a counterparty may be unable to pay amounts in full when due. Impairment provisions are provided for losses incurred as of the consolidated balance sheet date (Note 5). Significant changes in the economy or a sector that represents a concentration in the Group's portfolio could result in losses that are different from those provided for as of the consolidated balance sheet date. Management therefore carefully manages its exposure to credit risk.

The credit committee is responsible for approving and monitoring the Group's credit exposure, which is done through review and approval of the lending policy, and limits on credit exposure to individual borrowers and sectors.

Prior to advancing funds, an assessment is made of the credit quality of each borrower. The Group does not use an automated credit scoring system. It is the Group's policy to lend responsibly and establish loans that are within a customer's ability to repay rather than relying exclusively on security.

Maximum credit exposure at the year end approximates the carrying value of all assets. The classes of financial instruments to which the Group is most exposed are loans to customers (Note 5) and certain investment securities (Note 4).

The table below provides further information on mortgages, consumer and other loans by payment due status as of 31 December.

	2009		2008	
	$m	%	$m	%
Not impaired				
- Neither past due or impaired	136.4	66.9	190.8	94.6
- Past due up to 3 months but not impaired	49.0	24.0	4.2	2.1
Impaired				
- Past due 3 – 6 months	8.2	4.0	4.2	2.1
- Past due 6 – 12 months	4.5	2.2	1.4	0.7
- Past due over 12 months	5.9	2.9	1.1	0.5
	204.0	**100.0**	**201.7**	**100.0**

18. Financial Risk Management (Continued)

Credit risk (continued)

Of the $158 million (2008: $156 million) of mortgage loans, $128 million (2008: $126 million) are supported by family residential property, $26 million (2008: $26 million) by undeveloped land and $4 million (2008: $4 million) by commercial property. Of the $45 million (2008: $45 million) consumer loans, $7 million (2008: $7 million) are cash secured, $11 million (2008: $11 million) are funded by salary deductions from employers and $5.5 million (2008: $6 million) are overdraft facilities to customers.

The average mortgage loan balance is $93,000 (2008: $89,000) and the average consumer loan balance is $20,000 (2008: $20,000) with the largest exposure to a single customer totalling approximately $1.5 million (2008: $1.4 million). Mortgage loans can extend up to 24 years, and consumer loans up to 10 years.

Non-performing loans of $17.7 million (2008: $6.7 million) are comprised of mortgage loans totalling $12.9 million (2008: $5.4 million) and consumer loans totalling $4.8 million (2008: $1.3 million).

Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees – which represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to third parties – carry the same credit risk as loans.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Group monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

Geographical concentrations of financial assets

The Group has a concentration of risk in respect of geographical area, as both customers and assets held as collateral are primarily based in The Bahamas.

Related party receivables

The Group closely monitors amounts due from related parties and requests that payments are made on a monthly basis. Amounts due from the Parent are not considered to have significant credit risk as the Parent's share of the Group's equity exceeds amounts due. Further, the Group applies dividends payable to the Parent against amounts outstanding before remitting funds to the Parent.

Interest rate risk

Interest rate risk is the risk that the future cash flows or fair value of a financial instrument will fluctuate because of changes in market interest rates. The Group takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce gains or create losses in the event that unexpected movements arise.

18. Financial Risk Management (Continued)

Interest rate risk (continued)

The Group does not attempt to hedge specifically against the impact of changes in market interest rates on cash flow and interest margins and relies on the fact that the loan portfolio is based on floating interest rates linked to the B$ Prime rate that generally reset within three months of any rate change and has financial liabilities that offset these loans but at lower floating interest rates. The Bank maintains a general policy of fixing the interest rate spread between interest earned on financial assets and interest incurred on financial liabilities.

The Group is exposed to fair value interest rate risk on $8 million (2008: $8 million) of its debt securities which are at fixed interest rates for 5 to 10 years, and does not hedge against this risk. The remaining debt securities are at floating interest rates linked to the B$ Prime rate.

The Government securities in the Group's investment portfolio are at floating rates linked to the B$ Prime rate.

Price risk

Price risk is the risk that the fair value and/or amounts realised on sale of financial instruments may fluctuate significantly as a result of changes in market price. This risk is concentrated in investments in mutual fund shares, corporate debts securities and equity securities. The price risk of the investment portfolio is managed through diversification of the portfolio, as well as the yield management agreement with the Parent described in Notes 4 and 13. The Group plans to liquidate its portfolio of investments, excluding government debt securities, as market conditions permit.

Liquidity risk

Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due or can do so at an excessive cost. The Group's liquidity policy is to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding, to retain full public confidence in the solvency of the Group and to enable it to meet all financial obligations. This is achieved by maintaining a prudent level of liquid assets, through management control of the rate of growth of the business and maintaining high levels of capital.

As additional support, the Group maintains committed credit facilities of $3 million. These facilities were unutilised as of 31 December 2009, and fully utilised as of 31 December 2008.

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period to the contractual maturity dates as of 31 December 2009.

	Repayable on demand $m	Up to 3 months $m	3 - 12 months $m	1 – 5 years $m	More than 5 years $m	Total $m
As of 31 December 2009						
ASSETS						
Cash on hand and at bank	26.2	-	2.3	-	-	28.5
Investment securities	4.7	-	4.0	6.2	13.3	28.2
Mortgage, consumer and other loans	3.0	2.5	8.3	30.4	155.9	200.1
Other assets	6.4	-	-	-	12.3	18.7
Total assets	**40.3**	**2.5**	**14.6**	**36.6**	**181.5**	**275.5**

18. Financial Risk Management (Continued)

Liquidity risk (continued)

	Repayable on demand $m	Up to 3 months $m	3 - 12 months $m	1 – 5 years $m	More than 5 years $m	Total $m
As of 31 December 2009						
LIABILITIES						
Customer deposits	55.6	47.7	101.4	12.3	-	217.0
Debt securities	-	0.3	-	9.6	15.0	24.9
Other liabilities	-	-	0.4	-	-	0.4
Total liabilities	**55.6**	**48.0**	**101.8**	**21.9**	**15.0**	**242.30**
Net liquidity gap	**(15.3)**	**(45.5)**	**(87.2)**	**14.7**	**166.5**	
As of 31 December 2008						
ASSETS						
Cash on hand and at bank	18.6	-	-	-	-	18.6
Investment securities	14.8	-	0.3	7.8	13.7	36.6
Mortgage, consumer and other loans	1.0	3.3	10.5	27.0	157.1	198.9
Other assets	6.0	-	-	-	12.4	18.4
Total assets	**40.4**	**3.3**	**10.8**	**34.8**	**183.2**	**272.5**
LIABILITIES						
Customer deposits	59.7	40.2	96.4	13.6	-	209.9
Loan from bank						
Debt securities	-	3.5	-	3.0	21.6	28.1
Other liabilities	-	-	1.5	-	-	1.5
Total liabilities	**59.7**	**43.7**	**97.9**	**16.6**	**21.6**	**239.5**
Net liquidity gap	**(19.3)**	**(40.4)**	**(87.1)**	**18.2**	**161.6**	

Regulatory authorities set limits for liquidity balances. The requirements for the Bank are 20% of demand deposits and 15% of savings and fixed deposits. During the year, the Bank was in breach of these guidelines. This breach was remedied and as of 31 December 2009, the Bank was in compliance with these requirements.

Fiduciary risk

The Group is susceptible to fiduciary risk, which is the risk that the Group may fail in carrying out certain mandates in accordance with the wishes of its customers. To manage exposure, the Group generally takes a conservative approach in its undertakings.

19. Fair Values of Financial Instruments

Financial instruments utilised by the Group comprise the recorded financial assets and liabilities disclosed in these consolidated financial statements. The Group's financial instruments are principally short-term in nature, have interest rates that reset to market rates, or are carried at fair value; accordingly, their fair value approximates their carrying value. For long-term financial liabilities with fixed interest rates, there has been no change in market rates since the issuance of the financial liabilities and therefore, the carrying value approximates fair value.

FIDELITY