Bank of Cyprus Public Company Ltd

Pillar 3 Disclosures 2007

CONTENTS

1. Introduction

Bank of Cyprus Public Company Ltd ('the Bank', 'the Company') is the holding company of the Bank of Cyprus Group ('the Group'). The principal activities of the Group are the provision of banking, financial services and insurance business.

This report has been prepared in accordance with the requirements of the Directive to banks for the calculation of the capital requirements and large exposures of banks of 2006 and 2007 ('the Directive') issued by the Central Bank of Cyprus ('CBC'). The Directive implements the European Union's Capital Requirements Directive ('CRD').

1.1 Scope of Application

Bank Details

The requirements of the Directive, apply to the Group on a consolidated basis, as well as to the following companies on an individual basis:

- Bank of Cyprus Public Company Ltd
- Bank of Cyprus (Channel Islands) Ltd
- Bank of Cyprus Australia Ltd
- LLC CB 'Bank of Cyprus'
- Mortgage Bank of Cyprus Ltd

Differences in the basis of consolidation for financial reporting and prudential purposes

For financial reporting purposes, all subsidiaries are fully consolidated. However, for prudential purposes, the book value of the Group's insurance subsidiaries, as well as its property and hotel business subsidiaries, is deducted from the capital base. The treatment for accounting and prudential purposes of the various Group entities is presented in Appendix 1 (p.26) of the report.

Exemption from the requirements of the Directive on an individual basis

The Group makes use of the provisions laid down in paragraph 13 of unit A of the Directive in relation to the exemption of banking subsidiaries from its requirements on an individual basis in the case of Mortgage Bank of Cyprus Ltd ('MBOC') for the following reasons:

- MBOC has a banking licence issued by the CBC.
- MBOC is supervised by the CBC.
- MBOC is included in the consolidated supervision of the CBC.
- MBOC is 100% owned by the Bank.
- There is no current or foreseen material, practical or legal impediment as to the prompt transfer of own funds or the repayment of liabilities by the parent company.
- The Bank has stated to the CBC that it guarantees the liabilities of MBOC.
- The risk management procedures of the Bank also cover MBOC.

The Group has also successfully applied to the CBC for the inclusion of Kyprou Leasing SA in the calculation of the capital requirements of the Bank on an individual basis, on the grounds that the requirements of paragraph 14 of Unit A of the Directive are satisfied, namely:

- It is substantially funded by the Bank.
- The risk management procedures of the Bank cover Kyprou Leasing SA.
- Kyprou Leasing SA is 100% owned by the Bank.

2. Risk Management Objectives and Policies

2.1 Risk Management Organisation

Risk is inherent to the Group's business and activities. The Group's ability to identify, assess, monitor and manage each type of risk to which the Group is exposed is an important factor in its financial stability, performance, reputation and future success. The Group's principal risks are credit, market and operational risk. The Group's approach to risk management is built on formal governance processes and relies on individual responsibility and collective oversight, enabled by comprehensive reporting.

There are three risk management divisions (credit, market and operational) which report to the Group General Manager Risk Management ('GGMRM').

The three risk management divisions have the responsibility of developing the framework for the appropriate risk governance measuring and monitoring methods for risk management covering the entire Group. Through the realization of this objective, it is expected that both the losses arising from these risks and the relevant capital requirement, will be reduced. In addition, each division is responsible for ensuring that the Group complies with the Directive in its respective area.

Local risk management units have also been established where necessary within the banking units of the Group, which report to the relevant risk management divisions at Group level. Risk related issues are reported to the Group Executive Risk Committee consisting of the following members:

- A. Eliades – Group Chief Executive Officer
- Y. Kypri – Group Chief General Manager
- A. Jacouris – Group General Manager International Business & Operations
- V. Shiarly- Group General Manager Domestic Banking
- C.Hadjimitsis- Group General Manager Finance and Strategy
- N. Karydas – Group General Manager Risk Management
- I. Seiradakis –General Manager Bank of Cyprus Greece
- A.Jacovides- Manager Group Operational Risk Management

The Group Executive Risk Committee convenes quarterly, whilst risk management committees also operate within the Banking entities in Greece, the UK and Australia.

Market risks are reviewed at least monthly by the Group Asset and Liability Committee (ALCO). Group ALCO approves the policies and limits relating to the management of market and other treasury related risks (such as liquidity risk and counterparty credit risk). At its monthly meeting, the Group ALCO views consolidated reports that indicate the Group's liquidity position and exposure to market risks.

The Board Risk Committee which convenes at least quarterly ratifies all major policies and limits.

The first Internal Capital Adequacy Assessment Process ('ICAAP') report required by the CBC was prepared for the year 2007. As required by the Directive (Pillar II), the report includes a detailed analysis of all the risks and a description of the control framework for the minimization of those risks.

The strategies and processes for managing risks, as well as the measurement systems used and the hedging and mitigating strategies, are analysed below by risk division.

2.2 Credit Risk Management

The Group places great importance on the effective management of credit risk. This is achieved through a combination of highly trained and specialized personnel and appropriate systems, through which the creditworthiness of existing and new customers is assessed and the pricing of credit facilities is determined.

Measurement and Assessment

One important aspect of credit risk management is the development of new and the constant upgrading of existing systems for the assessment of the creditworthiness of Group customers.

In the retail banking sector, credit scoring systems are used for new customers and behavioral scoring systems for existing customers, which are continuously upgraded, so that the level of risk undertaken can be carefully assessed.

In the corporate banking sector, the final version of the new Integrated Rating System for the risk assessment for both medium-sized enterprises and corporate customer sectors was completed during 2008. The Bank expects that during 2009, this system will be formally applied for the efficient calculation of the customer's creditworthiness as well as the calculation of the overall credit risk. Specifically, the Borrower Rating will be calculated, that is, an assessment of the credit-worthiness of the customer which is calculated on the basis of the business' financial information, the quality its management, market trends/outlook, behaviour of the business' bank accounts and the bank facilities of the guarantors/owners of the business. The Transaction Rating will then be calculated, i.e. the rating that reflects the Bank's overall credit risk arising from the customer taking into account all relevant factors, including the collateral held by the Bank. The objective is to use this application in a way that will comply with the more advanced approaches of the Directive for calculating credit risk (Internal Rating Based ('IRB') approach).

Loan Sanctioning Policy

The Group has set specific limits for the various loan approval levels, which are exercised by qualified officers or committees within a predefined framework. There are also appropriate credit risk policies for each market/sector based on an evaluation of the credit risk and changing economic environment. Specific guidelines for the sound growth of the Group's loan portfolio are given by Credit Risk Policy Management Department on a regular basis. Relevant instructions are also issued to ensure that, as far as possible, loans are properly priced on an individual customer basis. The relevant CBC guidelines are also taken into account which include Lending guidelines for the acquisition of immovable property including residential property.

Efficient Management, Monitoring and Control of Customer Advances

The ultimate objective of the efficient management of the Group's advances portfolio is to enable prompt corrective action to be taken as soon as arrears/irregularities appear on customer debit accounts, so as to restrict loan impairment. In this context, an integrated, automated collection/settlement system is used for the timely handling of overdue debit accounts in the retail sector. At the same time, all loan portfolios are closely and systematically monitored and controlled centrally by specialized Group departments, as well as regionally by the Business/Corporate Centres, and appropriate prompt corrective action is taken. Recoveries accounts are also handled effectively at both central and regional level.

Credit Risk with correspondent Banks and Countries

The Group ALCO has approved a model for setting credit limits for correspondents and countries based primarily on their credit rating as determined by recognised international credit rating agencies.

Group Market Risk Management ('GMRM') monitors, on a daily basis, changes to the ratings of correspondents and countries, for which the Group has limits, and notifies the Group's banking units of any changes to their limits.

Policies for hedging and mitigating credit risk

The Group has implemented different methods in order to achieve effective mitigation of Credit Risk. Some of the most important methods are listed below:

- Determining which sectors of the economy the Bank is not willing to finance
- Setting of sanctioning limits for all line Managers and Credit Committees
- Setting of thresholds relating to Loan to Value Ratios as well as procedures relating to taking collaterals especially residential/ commercial mortgage.
- Credit Scoring Rating for retail customers and MRA Credit Rating for corporate customers are linked with approval/ rejection criteria
- Issuing circulars and guidelines concerning the granting of credit
- Ad- hoc approvals of corporate clients' lending.

2.3 Market Risk Management

GMRM is responsible for measuring and monitoring the following risks at Group level:

- Market risk (mainly interest rate risk and exchange rate risk)
- Liquidity risk
- Credit risk with correspondent banks and countries

The Group ALCO sets out the policy for the management of these risks and approves the acceptable level of risk and limits, which are ratified by the Board Risk Committee.

The monitoring of these risks at local banking units is carried out by market risk officers in the various countries in which the Group operates, who report directly to GMRM which is responsible for monitoring market risk at Group level.

During 2007, the Group ALCO approved market risk limits for the new units of the Group in Russia and Romania that are monitored daily. During 2008, the framework for monitoring market risks in Ukraine will also be put in place.

Interest Rate Risk

In order to control the risk from changes in interest rates, there are limits on the maximum reduction of net interest income, of each banking unit, that can take place each year, for the next three years. These limits have been set as a percentage of Group capital (1,5%) and as a percentage of Group net interest income (5%) and have been allocated to the various banking units in accordance with their contribution to net interest income. Small limits have also been set for open interest rate positions in the over three-year period.

During 2007, the Group began measuring the impact of a 2% change in interest rates on the economic value of the Group. The Group ALCO has set a maximum limit for this change equal to 10% of Group regulatory capital (calculated in accordance with CBC provisions).

Exchange Rate Risk

In order to limit the risk of loss from adverse fluctuations in exchange rates, the Group ALCO has approved open position limits for each currency or group of currencies and for the overall open currency position. These limits are smaller than the maximum permissible by the CBC.

For the foreign exchange trading book (which operates only in Cyprus) the Group ALCO has approved daily and monthly stop loss limits, as well as Value at Risk ('VaR') limits. These limits are monitored daily by GMRM. Value at Risk is calculated using the variance/co-variance method with 99% confidence interval and a one-day holding period. Historical data on exchange rates over the last five years is used. During 2007, the realised losses did not exceed the Value at Risk on any day.

Liquidity risk

GMRM monitors the Group's liquidity position and ensures adherence to the various limits (e.g. liquidity mismatch limits) set by the Group ALCO and the regulatory authorities in the countries where the Group operates. During 2007, the Group ALCO approved the various assumptions and limits of two liquidity crisis scenarios: bank-specific crisis and market crisis.

Policies for hedging and mitigating market risk

The Group aims to minimize market risks, through hedging. Only minimal open positions are allowed for both foreign exchange (FX) and interest rate risk.

FX risk is mostly hedged in the spot market. The Local Treasury departments outside Cyprus, hedge their position (arising out of customer transactions) with The Group Treasury in Nicosia and only transact with other market participants in limited cases (e.g. when there is a bank holiday in Cyprus). The Group Treasury in Nicosia then covers its FX position by entering into FX deals with other banks. Other instruments used to hedge FX risk include FX forwards and FX swaps.

Interest rate risk is also managed centrally at Group level. Group Treasury either provides fixed rate funding to other banking units that grant fixed rate loans, or accepts fixed rate funding from banking units to hedge their fixed rate deposits. Interest rate risk is also hedged using interest rate swaps ('IRS') between the various banking units of the Group as well as with external counterparties. The Group also hedges a percentage of non-rate sensitive deposits, such as current accounts, by investing in fixed rate bonds (structural hedging).

Every month, GMRM carries out tests to ensure that hedges are still effective. For structural hedging the amount of structural hedging assets is compared to the amount that should be hedged (based on the level of deposits and the assumptions approved by the Group ALCO). The average tenor of hedging assets is also compared to the targeted average tenor, in order to ensure that hedging is within the Group ALCO approved parameters.

For over three year positions there are strict position limits. Any position not hedged is immediately identified since it violates the open position limits

For fair value hedges, the change in the fair value of the hedging item is compared with the change in the fair value of the hedging instrument in order to establish that they continue to be in the 80% to 125% range. In the case of bonds, the credit spread effect is ignored, in order to take into account the mark to market impact from interest rate changes only.

For cash flow hedges, the initial effectiveness testing is assessed to confirm that there are no changes in the expected cash flows and that hedging continues to be effective.

2.4 Operational risk management

The Group Operational Risk Management Division is working on the development of specialized methods for measuring operational risk, with a view to the proper monitoring of operational risks and the timely identification of any shortcomings. This is a long term task, since, beyond the set up / adoption of the necessary infrastructure and systems, most importantly, the right culture has to be promoted within the organization. This is an essential element for the effective management of the relevant risks.

Potential losses from operational risks may occur in all the Group's activities as a result of inefficiency or failure of internal processes or systems caused either by external events or human error. Consequently, under the umbrella of operational risks a wide range of possible cases are included, which are not easily predictable. Nonetheless, with proper operational risk management it is possible to limit any adverse consequences.

Within this framework, data on operational risk events is being collected from all group units on a specialised system. This data is already being utilised so as to improve the management of operational risks and, where possible, for preventive purposes.

In addition, the more long term task of analyzing and codifying the procedures of the Group, from the point of view of better operational risk management continues. In parallel, the number of key risk indicators monitored is being enriched. The collection of relevant data continue, so as to aid the monitoring and assessment of operational risks. The above currently take place in Cyprus and in Greece. The aim is to gradually cover all the Group companies.

Policies for hedging and mitigating operational risk

Part of the mitigation strategies that the Group follows, as far as operational risk is concerned, is having appropriate insurance coverage. This is being reviewed each year to ensure that the Group's needs are met. Finally, the major project of implementing a business continuity plan is in progress, aiming to ensure that services can resume immediately in the case of a disruption.

3. Own funds

The own funds of Bank of Cyprus Group as at 31/12/2007 were £1.287.879 thousand as shown below:

Original Own Funds (Tier 1)	**£000**
Share Capital	283.112
Share Premium	402.873
Reserves	272.466
Hybrid Capital Securities	100.183
50% of Book value of non-banking subsidiaries	(66.334)
Intangible Assets	(10.348)
Total Tier 1	**981.952**
Additional Own Funds (Tier 2)	
Revaluation Reserves	138.930
Subordinated Loan Stock	233.331
50% of Book value of non-banking subsidiaries	(66.334)
Total Tier 2	**305.927**
Total own funds	**1.287.879**

The own funds for all subsidiaries, as at 31/12/2007, were in excess of the minimum required by the Directive.

3.1 Original Own Funds

Share Capital

As at 31/12/2007 the share capital of the Bank comprised of 566.223 thousand shares with a nominal value of €0,50 each.

Hybrid capital securities
Hybrid capital securities have no maturity date, but may be redeemed in whole at the option of the Bank, subject to the prior consent of the CBC, at their nominal amount together with any outstanding interest payments, five years after their issue date or on any interest payment date thereafter. The amount of £100.183 thousand included in original own funds consists of:

	£000
Capital Securities Series B	29.883
Capital Securities 12/2007	70.300
	100.183

Capital Securities Series B were issued in Cyprus pounds in March 2004 and are listed on the Cyprus Stock Exchange. They carry a floating interest rate, which is reset every three months. The interest rate is equal to the base rate of Bank of Cyprus Public Company Ltd at the beginning of each three-month period plus 1,00% per annum. Interest is payable quarterly.

Capital Securities 12/2007 were issued in December 2007 in Cyprus pounds and are listed on the Cyprus Stock Exchange. Their interest rate is fixed at 6,00% per annum for the first six months and floating thereafter, equal to the three-month Euribor plus 1,25% per annum. Interest is payable quarterly.

Additional own funds

Subordinated loan stock
The subordinated loan stock issued by the Bank is not secured and the rights and claims of loan stockholders are subordinated to the claims of depositors and other creditors of the Bank, but have priority over those of the shareholders of the Bank.

The Bank issued €200 million Subordinated Bonds 2008/2013 in October 2003, bearing a floating interest rate and maturing in October 2013. The Bank has the option to call the bonds in whole during or after October 2008. The interest rate of the bonds was set at the three-month Euribor plus 1,00% per annum until October 2008 and it will increase to, plus 2,20% per annum thereafter. The bonds are listed on the Luxembourg Stock Exchange. At 31 December 2007, the amount of €200 million Subordinated Bonds 2008/2013 outstanding amounted to €199,1 million.

In May 2006, the Bank issued €200 million floating rate Subordinated Bonds 2011/2016 maturing in May 2016. The Bank has the option to call the bonds in whole during or after May 2011. The bonds bear an interest rate set at the three-month Euribor plus 0,60% per annum until May 2011 and will increase to plus 1,60% per annum thereafter. The bonds are listed on the Luxembourg Stock Exchange. At 31 December 2007, the amount of the €200 million Subordinated Bonds 2011/2016 outstanding amounted to €196 million.

Practical or legal impediments to the prompt transfer of own funds or repayment of liabilities among the parent undertaking and its subsidiaries

In the event of a crisis, the Bank may encounter difficulties in drawing dividends from the non-EU overseas subsidiaries, namely:

- Bank of Cyprus (Channel Islands) Ltd
- Bank of Cyprus Australia Ltd
- LLC CB 'Bank of Cyprus'

This may be due to the possible insistence of local regulators for the maintenance of capital ratios well in excess of these required by the CBC for these subsidiaries.

Apart from the above, there are no current or foreseen material practical or legal impediments to the prompt transfer of own funds or repayment of liabilities among the parent company and its subsidiaries. Any distributions beyond the local capital adequacy requirements will be subject to local regulatory authorities' approval.

4. Minimum required own funds for credit, market and operational risk

4.1 Group's approach to assessing the adequacy of its internal capital

The different methods used to assess the adequacy of the internal capital for the different categories of risks are described below.

Standardised approach for credit risk

The necessary mechanism for the capital calculation with the Standardised Approach has been completed. The foundations have been laid for the implementation of the IRB foundation approach for Credit Risk.

The following table shows the 8% of the risk-weighted group exposure amounts as at 31/12/2007 for each of the exposure classes specified in paragraph 23 of Unit A.

	£000
Central governments or central banks	643
Regional governments or local authorities	859
Administrative bodies and non – commercial undertakings	297
Institutions	79.515
Corporate	385.969
Retail	242.480
Covered Bonds	1.438
Securitisation Positions	50
Other assets	23.256
	734.507

Minimum capital requirements for trading book activities related to position risk, settlement risk and counterparty risk and where applicable concentration risk

The minimum capital requirements calculated in accordance with paragraph 19(b) of Unit A of the Directive for trading book activities is as follows:

	Capital Requirement £000
Traded debt instruments	2.447
Equity shares	312
	2.759

Minimum capital requirements in relation to operational risk

The minimum capital requirement in relation to operational risk calculated in accordance with the Standardised Approach (paragraph 48 of Unit A of the Directive) amounts to £75.403 thousand.

5. Counterparty credit risk

As at 31 December 2007, the Group did not have any repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions or margin lending transactions outstanding. Hence the section below only discusses the credit risk arising from derivative instruments.

5.1 Internal capital and credit limits for counterparty credit exposures

Limits for derivative transactions are assigned for a select number of counterparties, all rated A1 or above. These limits are approved by the Group ALCO. The derivative limit (for the Expected Replacement Cost (ERC) of the contract), counts within the overall limit of the counterparty and is set at 15% of the total limit. There is also a limit for the maximum notional amount of contracts with each counterparty, which is 20 times the ERC limit.

Credit risk arising from entering into derivative transactions with counterparties is measured using the mark-to-market method. According to this method, the current replacement cost of all contracts with positive amounts is obtained and an add-on is applied to this amount for potential future credit exposure, according to specific factors depending on the type of transaction and duration. This figure is used both for calculating the capital required for the credit risk of those transactions and for credit limit monitoring.

5.2 Policies for securing collateral and establishing credit reserves

Until the year-end the Group had signed Credit Support Annexes (‘CSAs’) to the International Swaps and Derivatives Association (‘ISDA’) agreement with four counterparties out of twenty. In 2008 it is expected that more such agreements will be entered into. As at the year-end, the threshold amounts in the CSAs were not reached, thus the Group has not obtained collateral from any counterparty. In any case, all the counterparties with which we enter into derivative transactions are rated A1 and above.

5.3 Policies with respect to wrong-way risk exposures

This risk is not currently measured. It is not anticipated to be significant since a change in market rates (interest rates and FX rates which are the main underlying factors of our derivative transactions) is not expected to materially increase the probability of default (PD) of our counterparties. It should also be noted that since the Bank uses the standardised approach, it does not measure the PDs of counterparties.

5.4 Amount of collateral the bank would have to provide given a downgrade in its credit rating

Currently the only instance where the Group would have to provide additional collateral in the event of a downgrade, involves derivative transactions under ISDA agreements, where a CSA has been signed. Out of the four agreements signed, only two such agreements in place provide for additional collateral in the event of a downgrade. In the event of an up to two notch downgrade, the amount of additional collateral to be provided amounts to €3,2 million (see Table below).

Increase in Collateral in the case of 2 notches downgrade in Rating (ISDA Agreements)				
Bank	Moody's Rating	Threshold Amount (USD million)	Threshold Amount (EUR million)	Difference (EUR million)
Goldman Sachs International	A2 A3-Baa1	15 10	9,5 6,3	3,2
Nomura International Plc	A1 to A3 Baa1	n/a n/a	15 15	0

5.5 Gross positive fair value of contracts

The gross positive fair value of the Group derivative contracts (mainly IRS and FX contracts) is presented in the Table below. This is the total of the positive mark-to-market of all contracts (including net accrued interest). It should be noted that there are no legally enforceable netting agreements in place. The collateral agreements where in place have not yet reached the threshold amount (thus no collateral has been provided). Thus, the “Gross positive fair value” of the derivative contracts in place is equal to the "Net derivatives credit exposures".

	Gross Positive Fair Value as at 31 Dec 2007
	£000
Cyprus	22.857
Greece	3.045
UK	6.664
Group	**32.566**

5.6 Mark- to-market method and exposures

The mark-to-market of IRSs is calculated using the Bloomberg system. The methodology used is as follows:

- The fixed payments are calculated for all future payment dates based on the fixed rate of the IRS.
- The floating payments are also calculated for all future payment dates based on the rates implied by the forward curve.
- The net position of the fixed and floating payments is calculated and discounted to present value using the relevant discount factors.

FX forwards and FX swaps are marked to market as follows:

The forward leg of each contract is taken, and each currency is converted into Cyprus pounds using the forward rate corresponding to the remaining period to the maturity date of the contract (i.e. the period between the valuation date and the maturity date). The difference between the CYP amount of the two currencies discounted to the valuation date using the risk free rate, is the profit or loss on the contract as follows:

If PV (CYP equivalent of purchase amount – CYP equivalent of sale amount) > 0 => profit

If PV (CYP equivalent of purchase amount – CYP equivalent of sale amount) < 0 => loss

The table below indicates the measures for exposure value under the mark-to-market methodology. The exposure values are calculated as the:

- The positive mark to market after taking into account the accrued interest and
- Add on amount, which is equal to a percentage of the nominal amount of each deal based on its duration.

Exposures under mark-to-market method as at 31 Dec 2007	
	£000
Cyprus	
Institutions	34.067
Corporates	1.802
	35.869
Greece	
Institutions	3.484
Corporates	2.043
	5.527
Greece	
Institutions	6.617
Corporates	34
	6.651
Group	
Institutions	44.168
Corporates	3.879
	48.047

6. Bank's exposure to credit risk and impairment risk

Past due loans and advances are defined as all loans and advances where the counterparty has failed to make a payment when it is contractually due.

At each balance sheet date the Group assesses whether there is any objective evidence that loans and advances are impaired. A loan is impaired if there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the loan (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the loan or the group of loans, that can be reliably estimated.

For loans and advances to customers, the Group first assesses whether objective evidence of impairment exists for loans and advances that are individually significant. Furthermore, a collective impairment assessment is made for loans and advances that are not individually significant and for losses that have been incurred but are not yet identified relating to loans and advances that have been assessed individually and for which no provision has been made.

The collectability of individually significant loans and advances is evaluated based on the customer's overall financial condition resources, payment record, the prospect of support from creditworthy guarantors and the realisable value of any collateral.

There is objective evidence that a loan is impaired when it is probable that the Group will not be able to collect all amounts due according to the original contract terms, unless such loans are secured or other factors exist whereby the Group expects that all amounts due will be collected.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the carrying amount of the loan and the present value of the estimated future cash flows (excluding future credit losses not yet incurred) including the cash flows which may arise from guarantees and tangible collateral, irrespective of the outcome of foreclosure. The carrying amount of the loan is reduced through the use of a provision account and the amount of the loss is recognised in the income statement. Loans together with the associated provisions are written off when there is no realistic prospect of future recovery. Loans are monitored continuously and are reviewed for impairment every six months. If, in a subsequent period, the amount of the estimated impairment loss decreases and the decrease is due to an event occurring after the impairment was recognised, when the creditworthiness of the customer has improved to such an extent that there is reasonable assurance that all or part of the principal and interest according to the original contract terms of the loan will be collected timely, the previously recognised impairment loss is reduced by adjusting the impairment provision account. If a previously written-off loan is subsequently recovered, any amounts previously charged are credited in the income statement.

The present value of the estimated future cash flows is discounted using the loan's original effective interest rate. If a loan bears a variable interest rate, the discount rate used for measuring any impairment loss is the current reference rate plus the margin specified in the initial contract.

For the purposes of a collective evaluation of impairment, loans are grouped based on similar credit risk characteristics taking into account the type of loan and the industry, geographic location, collateral type, past-due amounts and other relevant factors.

Future cash flows for a group of loans and advances that are collectively evaluated for impairment are estimated on the basis of historical loss experience for loans with similar credit risk characteristics to those of the group. Historical loss experience is adjusted on the basis of current observable data to reflect the impact of current conditions that did not affect the period on which the historical loss experience is based and to remove the impact of conditions in the historical period that do not currently exist. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

6.1 Total amount of exposures

Credit exposure by type as at 31 Dec. 2007					
Type	Retail Customers	Corporate Customers	Financial Institutions	Governments and Local Authorities	**Total**
	£000	£000	£000	£000	**£000**
Bank Loans & Overdrafts	5.006.231	6.002.420	-	65.272	**11.073.923**
Acceptances, Endorsements & Documentary Credits	149.628	51.896	-	23	**201.547**
Guarantees	252.295	558.211	-	80	**810.586**
Unutilized Loan Commitments	1.183.955	820.053	-	9.251	**2.013.259**
Interbank Placements	-	-	3.597.827	519.637	**4.117.464**
Securities	-	19.456	1.353.019	962.472	**2.334.947**
Derivatives	-	1.836	30.730	-	**32.566**
Others	-	-	-	95.712	**95.712**
Total	6.592.109	7.453.872	4.981.576	1.652.447	**20.680.004**

6.2 Geographic distribution of the exposures

Credit Exposure by Geographical Area as at 31 Dec. 2007					
	Retail Customers	Corporate Customers	Financial Institutions	Governments and Local Authorities	**Total**
	£000	£000	£000	£000	**£000**
European Union:					
Cyprus	3.088.499	3.911.834	212.402	891.963	**8.104.698**
Greece	2.865.962	2.844.903	143.216	484.208	**6.338.289**
UK	310.653	369.333	646.006	409	**1.326.401**
Romania	7.859	156.040	2.266	3.929	**170.094**
Other	-	-	58.814	176.407	**235.221**
Rest of Europe					
Including Russia	174.947	93.672	319.425	237	**588.281**
Australia & New Zealand	3.322	146	211.340	1.482	**216.290**
North America & Canada	9.541	15.629	535.679	-	**560.849**
Other	127.482	97.486	2.914.913	-	**3.139.881**
Total	6.588.265	7.489.043	5.044.061	1.558.635	**20.680.004**

6.3 Distribution of the exposures by industry or counterparty types

Exposure broken down by NACE as at 31 Dec.2007					
Description	Retail Customers	Corporate Customers	Financial Institutions	Governments & Local Authorities	**Total**
	£000	£000	£000	£000	**£000**
Agriculture, Hunting	59.790	63.995	-	-	**123.785**
Fishing	5.940	23.358	-	-	**29.298**
Mining & Quarrying	25.956	61.171	-	-	**87.127**
Manufacturing	573.355	752.553	-	-	**1.325.908**
Electricity, Gas	15.935	30.374	-	-	**46.309**
Construction	480.902	1.277.619	-	-	**1.758.521**
Wholesale & Retail	945.817	1.364.953	-	124	**2.310.894**
Hotels & Restaurants	240.602	980.186	-	-	**1.220.788**
Transport	172.350	221.449	-	14	**393.813**
Financial Intermediation	160.563	443.617	-	-	**604.180**
Real Estate	655.358	1.364.671	-	-	**2.020.029**
Public Administration	6.972	28.367	-	1.523.484	**1.558.823**
Education	19.659	19.940	-	-	**39.599**
Health & Social Work	72.947	34.227	-	-	**107.174**
Personal Service Activities	109.428	301.044		35.013	**445.485**
Private Individuals	3.181.967	380.490	-	-	**3.562.457**
Financial Institutions	-	-	5.044.062	-	**5.044.062**
Territorial Organizations	950	802	-	-	**1.752**
Total	6.728.491	7.348.816	5.044.062	1.558.635	**20.680.004**

6.4 Residual maturity breakdown of all the exposures

Credit Exposure by Maturity as at 31 Dec. 2007					
	Retail, Customers	Corporate Customers	Financial Institutions	Governments & Local Authorities	**Total**
	£000	£000	£000	£000	**£000**
Less than 1 year	897.044	1.106.827	3.907.351	473.335	**6.384.557**
1 to 5 years	2.405.625	3.361.846	823.235	731.581	**7.322.287**
5 to 10 years	760.112	978.260	268.316	266.925	**2.273.613**
More than 10 years	2.660.203	1.907.390	45.160	86.794	**4.699.547**
Total	6.722.984	7.354.323	5.044.062	1.558.635	**20.680.004**

6.5 Security breakdown

Credit exposure and value of security as at 31 Dec. 2007					
	Retail, Customers	Corporate Customers	Financial Institutions	Governments & Local Authorities	**Total**
	£000	£000	£000	£000	**£000**
Credit Exposure	6.592.109	7.453.872	4.981.576	1.652.447	**20.680.004**
Value of Security	(3.095.392)	(3.543.733)	(57.000)	(50.960)	**(6.747.085)**
Total Unsecured Credit Exposure	3.496.717	3.910.139	4.924.576	1.601.487	**13.932.919**

Security by type as at 31 Dec.2007					
	Retail Customers	Corporate Customers	Financial Institutions	Governments & Local Authorities	**Total**
	£000	£000	£000	£000	**£000**
Real Estate Property	2.791.077	3.092.747	-	744	**5.884.568**
Cash	195.922	169.376	57.000	107	**422.405**
Securities/ Bonds	39.453	207.972	-	-	**247.425**
Life Insurance	-	-	-	-	**0**
Guarantees	67.971	72.485	-	50.109	**190.565**
Other Securities	969	1.153	-	-	**2.122**
Total	3.095.392	3.543.733	57.000	50.960	**6.747.085**

6.6 Impaired exposures and past due exposures

Impaired and past due loans and advances by geographical areas as at 31 Dec.2007			
	Neither past due nor impaired	Past due but not impaired	**Impaired**
	£000	£000	**£000**
Cyprus	4.975.168	523.454	**282.823**
Greece	3.891.947	596.829	**146.254**
United Kingdom	669.140	66.743	**7.928**
Australia	204.806	30.042	**7**
Romania & Russia	7.635	10.025	**-**
	9.748.696	1.227.093	**437.012**

Provision for impairment of loans and advances by geographical area as at 31 Dec.2007				
	Cyprus	Greece	Other Countries	**Total Provision for Impairment**
	£000	£000	£000	**£000**
At 1 January 2007	338.854	115.726	7.128	**461.708**
Exchange adjustment	3	1.252	(84)	**1.171**
Applied in writing off:				
- interest on previous years' impaired loans and advances	(121.488)	(16.368)	(850)	**(138.706)**
- impaired loans and advances	(17.914)	(12.962)	(178)	**(31.054)**
Interest accrued on impaired loans and advances	(11.665)	(5.515)	(266)	**(17.446)**
Collection of loans and advances previously written off	24.243	6.259	-	**30.502**
Charge for the year	14.836	17.564	303	**32.703**
At 31 December 2007	**226.869**	**105.956**	**6.053**	**338.878**
Individual impairment	**162.685**	**57.666**	**4.605**	**224.956**
Collective impairment	**64.184**	**48.290**	**1.448**	**113.922**

7. The standardised approach

7.1 Exposure classes for which External Credit Assessment Institutions ('ECAI') or Export Credit Agencies ('ECA') are used

The Group uses external ratings from Moody's. These ratings are used for all relevant exposure classes, which are the following:

- Claims or contingent claims on central government or central banks
- Claims or contingent claims on regional governments or local authorities
- Claims or contingent claims on multilateral development banks
- Claims or contingent claims on institutions
- Claims or contingent claims on corporates (*it should be noted that most corporate are unrated)*
- Claims in the form of covered bonds
- Short-term claims on institutions and corporates
- Securitization positions
- Claims in the form of collective investment undertakings ("CIU") – *no exposure as at the year-end*

7.2 Transfer of credit assessments onto items not included in the trading book

The exposures are classified into the above exposure classes, and are then ranked into respective credit quality steps, that determine the risk-weight to be used in accordance with the provisions of the Directive.

In the case of financial institutions, the credit quality step is determined, according to the rating of the country under whose supervision they operate. It should be noted that all exposures with financial institutions with original maturity of three months or less, are risk-weighted 20%, unless the counterparty is unrated and the risk-weight assigned to its country is higher.

7.3 Association of external rating of each nominated ECAI or ECA with credit quality steps

The Group complies with the standard association published by the CBC, regarding the association of the external rating of each nominated ECAI or ECA with the credit quality steps prescribed in Annex VI of the Directive.

<u>For Financial Institutions *</u>

Risk weight	Moody's rating of central government
20%	Aaa to Aa3
50%	A1 to A3
100%	Baa1 to Baa3
100%	Ba1 to Ba3
100%	B1 to B3
150%	equal or lower than Caa1

* The above association also applies for regional governments or local authorities and for multilateral development banks (unless they are specifically stated in the CBC rules to be 0% risk-weighted).

For Sovereigns

Risk weight	Moody's rating of central government
0%	Aaa to Aa3
20%	A1 to A3
50%	Baa1 to Baa3
100%	Ba1 to Ba3
100%	B1 to B3
150%	equal or lower than Caa1

For Corporates

Risk weight	Moody's rating of central government
20%	Aaa to Aa3
50%	A1 to A3
100%	Baa1 to Baa3
100%	Ba1 to Ba3
150%	B1 to B3
150%	equal or lower than Caa1

7.4 Exposure before and after credit risk mitigation

The exposure before and after credit risk mitigation associated with each credit quality step mostly for financial institutions and governments, as at the year-end was as follows:

Rating	TOTAL Exposure £000
Aaa - Aa3	4.626
A1- A3	1.487
Baa1 - Baa3	53
NR	338
Items in course of collection	44
TOTAL	**6.548**

As at the year-end there was no credit risk mitigation available for exposures with banks and sovereigns and corporate bonds/derivatives. Therefore, the above amounts indicate the exposures both before and after credit risk mitigation.

8. Operational risk

8.1 Approaches for the assessment of own funds requirements

The Group follows the Standardised Approach for the calculation of own funds requirements for operational risk for which the approval of the CBC was obtained.

8.2 Relevant internal and external factors considered in the bank's measurement approach

As the Group is using the Standardised Approach it is exempt from utilising data on internal and external factors for capital calculation (required for banks that use the Advanced Measurement Approach). Nonetheless, as required for the Standardised Approach, internal loss data is collected in an in-house developed database. Where available, external data is considered as part of the Group's overall risk assessment. The internal data is submitted to the CBC together with the Capital calculation as required.

9. Exposures in equities not included in the trading book

The Group holds equity securities mainly for the purposes of capital appreciation. At 31 December 2007, the Group also had certain equity securities obtained from customers in satisfaction of debt as well as certain venture capital investments.

Listed equity securities are measured at fair value, being the market value of these securities on a recognised stock exchange. Unlisted securities are also measured at fair value, which are determined using valuation models. These models are periodically reviewed by qualified personnel.

There have been no significant changes to these practices in 2007 compared to 2006.

Of the total equity securities held by the Group as at 31 December 2007, £45.039 thousand were classified as available for sale and £1.650 thousand were classified as at fair value through profit or loss.

The balance sheet value of the Group's equity securities not included in the trading book at 31 December 2007 is £46.689 thousand, analysed as follows:

	£000
Listed on the Cyprus Stock Exchange	42.964
Listed on European stock exchanges	1.116
Unlisted venture capital investments	1.650
Other unlisted	959
Total	**46.689**

There is no difference between the fair value and the balance sheet value of equity securities.

The cumulative realised gains from disposals of equity securities during 2007 amounted to £8.667 thousand and were included in the income statement. The total unrealised gains on revaluation of non-trading equity securities amounted to £34.106 thousand and were included in the revaluation reserves of the Group.

10. Exposure to interest rate risk on positions not included in the trading book

The Group ALCO sets limits on the maximum allowable interest rate risk in the banking book, for each banking unit. The exposure is measured as follows:

Impact on Net Interest Income

The maximum loss limits apply for each year, for the first three years. They were set as a percentage of Group capital (1,5%) and as a percentage of net interest income of the Group (5%) and were allocated to the various banking units of the Group based on their contribution to net interest income. Small limits for open interest rate positions have been approved for periods more than three years.

The table below indicates how the net interest income of the Group, over a one-year period, will be affected from a reasonably possible change in the interest rates of the main currencies:

Change in rates	Cyprus pounds	Euro	USD	GBP	Other currencies	Total
	£000	£000	£000	£000	£000	**£000**
2007						
+0,5% in all currencies	**6.218**	**1.040**	**711**	**513**	**277**	**8.466**
-1,5% in USD and -0,5% in other currencies	**(6.294)**	**(1.080)**	**(3.112)**	**(533)**	**(347)**	**(10.659)**

The total change in net interest income differs from the sum of the changes for each individual currency, as it has been calculated based on the actual correlation coefficients between the interest rates of the various foreign currencies, and perfect positive correlation between the interest rate of the foreign currencies and the Cypriot pound.

Impact on the Economic Value of equity

The impact on the Economic Value of equity is measured for Group positions, for a 200 basis points change in interest rates. The Group ALCO has set a maximum limit of 10% of Group Capital for this change. The change in the economic value of the Group as at the end of December 2007 amounted to €105 million (4,8% of Group regulatory capital, calculated in accordance with CBC rules).

Measuring the interest rate effect

The following methodology is used to measure the interest rate effect:

The assets and liabilities in each currency are placed in time bands, according to the number of days remaining from the reporting date until their next repricing date. The difference between assets and liabilities repricing in each time band, 'the gap' is then calculated. The gaps are the starting point in calculating both the impact on net interest income and on economic value from a certain change in interest rates.

A rate change is applied on the gap of each time zone for the number of days from the middle of the time zone to the year-end in order to calculate the impact on net interest income. Moreover, a factor (provided in the Basel document "Principles for the management and supervision of interest rate risk) for the standardised interest rate shock and corresponding to a 2% rate change) is applied on the gap of each time zone in order to calculate the impact on Economic Value.

The interest rate effect, on interest income is measured according to the following scenarios:

I. For a 1% increase and a 1% decrease in rates assuming a parallel shift of the yield curve.
II. Using interest rate changes for each currency and time period as suggested by the yield curves.

The overall interest rate effect is calculated in two ways:

a) As the average of the interest rate affects using the assumption of positive and zero correlations, since we know from historic data that actual correlations lie between 0 and 1.
b) Using the actual correlations of 1-month interest rates.

Daily monitoring – for the purpose of monitoring compliance with the maximum loss limit on a daily basis, the interest rate effect is calculated using method I above and a) only – that is to say a 1% parallel shift in both directions will be used and the average of the zero and positive correlations will be applied.

Monthly monitoring – All the above methods will be used. In the case of operations in Australia, Channel Islands, Russia and Romania monitoring for the time being will be monthly– methods I and II above will be used. As the operations grow and become more complex, more frequent monitoring will be carried out.

All the interest rate effects calculated using the above methodologies should be within the overall limit for each banking unit.

Concentration limits per currency

In order to avoid excessive variations in the Group net interest income caused by the change in the interest rate of a particular currency, it is prudent to limit the maximum interest rate effect by establishing concentration limits per currency. These limits are related to the size of the assets and liabilities of each currency. Concentration limits are set for the Bank's operations in Cyprus and Greece. No concentration limits are set for the other operations (in the UK, the Channel Islands, Australia, Russia and Romania) due to the size of their balance sheets.

11. Market Risk Trading Books

The Group has a low market risk appetite. There are very small limits for undertaking market risk in trading books.

FX Trading book

There is a trading book in FX, which is operated in the Cyprus dealing room only. The following limits are available:

Stop-Loss limits

Daily	£50.000
Monthly	£100.000
Value at Risk limit	**£150.000**

Moreover, there are position limits for intra-day and overnight positions.

During 2008, the actual losses on any given day did not exceed the Value at Risk limit.

Capital Markets Trading book

In Cyprus there is also a capital markets trading book, that includes credit and interest rate risk positions.

The following limits apply:

Stop Loss limits

Daily	£100.000
Monthly	£200.000
Yearly	£500.000

Position limits

Credit Risk positions	£160 million
Interest Rate Risk positions	£40 million

Equities Trading book

In addition to the above, some equities listed in the Cyprus Stock Exchange are held in a trading book in the books of the Cyprus operations of the Bank and its subsidiary CISCO. The intention is to gradually dispose of these equities and close the trading book.

Capital Requirement

As at the year-end 2007, the capital required to support market risks amounted to only CYP 2.759.000 and was made up of:

Position risk	£2.447.000
Equity risk	£312.000
FX risk *	£-

* the FX position was less than 2% of the capital base.

It should be noted that the standardised method is used for calculating market risk for the above positions. The maturity method is used for the measurement of interest rate risk.

APPENDIX 1

The list of Group companies as at 31 December 2007 by country of incorporation is set out below:

Company Name	Activities	Consolidation method	
		Accounting purposes	**Prudential purposes**
Cyprus			
Bank of Cyprus Public Company Ltd	Commercial banking	C	C
Mortgage Bank of Cyprus Ltd	Commercial banking	C	C
The Cyprus Investment and Securities Corporation Ltd (CISCO)	Investment banking	C	C
General Insurance of Cyprus Ltd	General insurance	C	D
EuroLife Ltd	Life insurance	C	D
Kermia Ltd	Property trading and development	C	D
Kermia Properties & Investments Ltd	Property trading and development	C	D
Kermia Hotels Ltd	Hotel business	C	D
BOC Ventures Ltd	Management of venture capital investments	C	C
Tefkros Investments Ltd	Investment fund	C	C
Bank of Cyprus Mutual Funds Ltd	Distribution of mutual funds	C	D
JCC Payment Systems Ltd	Credit card transactions processing	PC	PC
Cytrustees Investment public Company Ltd	Closed - end investment company	C	D
Interfund Investments Plc	Closed - end investment company	Associate (Equity Method)	D
Greece			
Bank of Cyprus Public Company Ltd (branch)	Commercial banking	C	C
Kyprou Leasing SA	Leasing	C	C
Kyprou Commercial SA	Financing of motor vehicles and other consumer products	C	C
Kyprou Securities SA	Investment banking	C	C
Kyprou Mutual Fund Management Company (Kyprou AEDAK)	Management of mutual funds	C	C
Kyprou Properties SA	Property management	C	D
Kyprou Insurance Services Ltd	General insurance brokers	C	D
Kyprou Zois (branch of EuroLife Ltd)	Life insurance	C	D
Kyprou Asfalistiki(branch of General Insurance of Cyprus Ltd)	General insurance	C	D
United Kingdom			
Bank of Cyprus United Kingdom (branch)	Commercial banking	C	C
Channel Islands			
Bank of Cyprus (Channel Islands) Ltd	Commercial banking	C	C
Tefkros Investments (CI) Ltd	Investment Fund	C	C
Australia			
Bank of Cyprus Australia Ltd	Commercial banking	C	C
Romania			
Bank of Cyprus Romania (branch)	Commercial banking	C	C
Cyprus Leasing Romania IFN SA	Leasing	C	C
Russia			
LLC CB ‘Bank of Cyprus’	Commercial banking	C	C
Cyprus Leasing LLC	Leasing	C	C

C: Fully Consolidated
D: Deducted from Capital Base
PC: Proportionally Consolidated