Audited Consolidated Financial Statements

Atlantic Security Bank

Year ended December 31, 2012
with Independent Auditors' Report

CONTENTS

Independent Auditors' Report....................1
Consolidated Statement of Financial Position....................3
Consolidated Statement of Income....................4
Consolidated Statement of Comprehensive Income....................5
Consolidated Statement of Changes in Shareholder's Equity....................6
Consolidated Statement of Cash Flows....................7
Notes to the Consolidated financial statements.................... 8 - 45

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Independent Auditors' Report

The Board of Directors
Atlantic Security Bank

We have audited the accompanying financial statements of Atlantic Security Bank (the "Bank") which comprise the statement of financial position as at December 31, 2012, and the statement of income, statement of comprehensive income, statement of changes in shareholder's equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

This report is made solely to the directors, as a body. Our audit work has been undertaken so that we might state to the directors those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the directors as a body, for our audit work, for this report, or for the opinions we have formed.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these 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 about whether the financial statements are free from material misstatement.

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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 auditor considers 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 financial statements present fairly, in all material respects, the financial position of Atlantic Security Bank as at December 31, 2012, and of its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

Ernst & Young Ltd.

March 20, 2013

Atlantic Security Bank
Consolidated Statement of Financial Position
December 31, 2012

(Amounts expressed in thousands of US$ dollars)

Notes		**2012 US$ 000**	2011 US$ 000
	ASSETS		
	Cash and cash equivalents		
	Cash	**34**	26
8	Interest - bearing deposits with banks	**33,848**	48,811
8	Overnight placements	**102,377**	28,164
	Total cash and cash equivalents	**136,259**	77,001
5, 8	Other interest - bearing deposits with banks	**495**	2,693
6, 8	Risk portfolio, net	**1,603,605**	1,417,743
15	Derivatives financial instruments	**408**	180
	Premises and equipment, net	**329**	255
8	Accumulated interest receivable	**22,887**	20,119
8	Other assets	**4,489**	5,538
	TOTAL ASSETS	**1,768,472**	1,523,529
	LIABILITIES AND SHAREHOLDER'S EQUITY		
	Liabilities		
	Deposits		
8	Non interest - bearing - demand	**464,998**	390,403
	Interest - bearing		
8	Demand	**88,659**	66,672
8	Time	**843,187**	863,572
7	Other borrowed funds	**136,246**	-
15	Derivatives financial instruments	**575**	1,491
8	Accumulated interest payable	**12,145**	8,400
8	Other liabilities	**2,876**	3,754
	Total Liabilities	**1,548,686**	1,334,292
12, 13, 15	**Commitments and contingencies**		
	Shareholder's Equity		
11	Share capital	**70,000**	70,000
6	Reserve for valuation of available for sale financial assets	**41,106**	13,959
	Retained earnings	**108,680**	105,278
	Total Shareholder's Equity	**219,786**	189,237
	TOTAL LIABILITIES AND SHAREHOLDER'S EQUITY	**1,768,472**	1,523,529

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

Dionisio Romero P.
Director

Raimundo Morales D.
Director

Atlantic Security Bank
Consolidated Statement of Income
For the year ended
December 31, 2012

(Amounts expressed in thousands of US$ dollars)

Notes		**2012**	2011
		US$ 000	US$ 000
	Interest and dividend income		
	Interest on deposits with banks and overnight placements	**222**	329
	Interest and dividends on investment	**31,788**	33,271
	Interest on loans	**40,882**	34,942
8	Total interest and dividend income	**72,892**	68,542
	Interest expense		
	Interest on deposits	**34,482**	32,030
	Interest on borrowed funds	**358**	193
8	Total interest expense	**34,840**	32,223
	Net interest and dividend income	**38,052**	36,319
6	Provision for loan losses	**-**	(131)
	Net interest income after provision for loan losses and dividend	**38,052**	36,188
	Non-interest income (expense)		
8	Fees and commission income	**12,837**	14,027
8	Fees and commission expense	**(3,654)**	(2,456)
6	Net realized gains on sales of financial assets	**7,705**	6,937
6	Impairment losses of financial assets	**-**	(1,000)
8,15	Gains (loss) on derivatives financial instruments	**577**	(4,438)
	Foreign currency translation loss	**(76)**	(181)
6	Impairment losses of financial assets reversals	**545**	203
	Other	**1,266**	(164)
	Total non-interest income, net	**19,200**	12,928
	Operating expenses		
	Salaries and employee benefits	**4,150**	3,658
8	General and administrative expenses	**4,556**	4,215
	Intangible amortization	**-**	11
	Depreciation and amortization	**144**	141
	Total operating expenses	**8,850**	8,025
	Net profit	**48,402**	41,091

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

Atlantic Security Bank
Consolidated Statement of Comprehensive Income
For the year ended
December 31, 2012

(Amounts expressed in thousands of US$ dollars)

Note		**2012** **US$ 000**	2011 US$ 000
	Profit for the year	**48,402**	41,091
	Other comprehensive income		
6	Net gain (loss) on available for sale financial assets	**27,147**	(11,869)
	Total comprehensive income for the year	**75,549**	29,222

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

Atlantic Security Bank
Consolidated Statement of Changes in Shareholder's Equity
For the year ended
December 31, 2012

(Amounts expressed in thousands of US$ dollars)

Note		*Share Capital US$ 000*	*Valuation of Available for Sale Financial Assets US$ 000*	*Retained Earnings US$ 000*	*Total Shareholder's Equity US$ 000*
	At January 1, 2011	70,000	25,828	109,187	205,015
6	Net change in fair value of available for sale financial assets	-	(11,869)	-	(11,869)
	Dividends paid	-	-	(45,000)	(45,000)
	Net profit	-	-	41,091	41,091
	At December 31, 2011	70,000	13,959	105,278	189,237
6	**Net change in fair value of available for sale financial assets**	**-**	**27,147**	**-**	**27,147**
	Dividends paid	**-**	**-**	**(45,000)**	**(45,000)**
	Net profit	**-**	**-**	**48,402**	**48,402**
	At December 31, 2012	**70,000**	**41,106**	**108,680**	**219,786**

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

Atlantic Security Bank
Consolidated Statement of Cash Flows
For the year ended
December 31, 2012

(Amounts expressed in thousands of US$ dollars)

	2012	2011
	US$ 000	US$ 000
Cash flows from operating activities		
Net profit	**48,402**	41,091
Adjustments to reconcile net profit to net cash flows:		
Interest expense	**34,840**	32,223
Interest and dividend income	**(73,419)**	(68,542)
Provision relating to risk portfolio	**(545)**	916
Gain on sale of financial assets	**(7,705)**	(6,937)
Net (gain) loss on derivatives financial assets	**(50)**	4,438
Depreciation and amortization	**144**	141
Intangible amortization	**-**	11
Operating results before working capital changes	**1,667**	3,341
Loans	**(194,814)**	(137,898)
Other interest-bearing deposits with banks	**2,198**	4,730
Deposits	**76,196**	202,952
Net changes in other assets provided and other liabilities	**(972)**	(378)
Net cash flows generated from operations	**(115,725)**	72,747
Interest paid	**(31,096)**	(32,891)
Interest and dividends received	**70,651**	65,729
Net cash flows (used in) provided by operating activities	**(76,170)**	105,585
Cash flows from investing activities		
Purchases of financial assets	**(512,482)**	(563,735)
Sales of financial assets	**548,081**	497,234
Purchases of reverse repurchase agreement	**8,800**	(3,900)
Acquisition of premises and equipment	**(218)**	(94)
Net cash flows provided by (used in) investing activities	**44,181**	(70,495)
Cash flows from financing activities		
Proceeds from borrowing funds	**136,246**	-
Payment of borrowing funds	**-**	(3,425)
Dividends paid	**(45,000)**	(45,000)
Net cash flows provided by (used in) financing activities	**91,246**	(48,425)
Net increase (decrease) in cash and cash equivalents	**59,258**	(13,335)
Cash and cash equivalents at January 1	**77,001**	90,336
Cash and cash equivalents at December 31	**136,259**	77,001

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

1. Corporate Information

Atlantic Security Bank (the Bank) is a wholly-owned subsidiary of Atlantic Security Holding Corporation (ASHC), incorporated under the laws of the Cayman Islands and operates under a Category "B" Banking and Trust license from the Government of the Cayman Islands. The Bank has also been granted a Mutual Fund Administrators license under the Mutual Funds Law of the Cayman Islands. The Bank is incorporated and domiciled in the Cayman Islands.

The ultimate parent company of ASHC is Credicorp Ltd., which is a limited liability company and is incorporated and domiciled in Bermuda. Credicorp Ltd. has a primary listing on the New York Stock Exchange under quote symbol "BAP" with further listing in the Peruvian Stock Exchange.

The Bank provides investment banking, financial advisory, trading and investment services to Latin American customers. The Bank has a Branch in the Republic of Panama ("Panama Branch"), operating under an international license granted by the Banking Superintendency of Panama, allowing banks to conduct, exclusively from an office in Panama, transactions which are intended to take effect outside the country.

ASB Trust Company, Ltd., is a controlled subsidiary of Atlantic Security Bank (ASB) incorporated on March 31st, 2012. The company was created in order to establish a proper corporate vehicle to develop trust–related products and services for ASB's clients. The company has not been operating since inception.

The consolidated financial statements were approved for issuance according to resolution of the Board of Directors of Atlantic Security Bank on March 20, 2013.

2. Statement of Compliance

The consolidated financial statements of Atlantic Security Bank have been prepared in accordance with International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board ("IASB").

3. Basis of Preparation of Consolidated Financial Statements

3.1 Basis of presentation

The consolidated financial statements have been prepared on an historical cost basis, except for the measurement at fair value of investments, derivative financial instruments and available-for-sale financial assets. The carrying values of such recognized assets and liabilities that are hedged items are adjusted to record variations in the fair values attributable to the risks that are being hedged. The consolidated financial statements are prepared in United States of America dollars (US$) and all values are rounded to the nearest thousand (US$000) except when otherwise indicated. The Banks presents its consolidated statements of financial position in order of liquidity.

3. Basis of Preparation of Consolidated Financial Statements (continued)

3.2 Basis of consolidation

The consolidated financial statements cover the accounts of Atlantic Security Bank its wholly owned subsidiaries (the Group). All significant intercompany balance and transactions have been eliminated in consolidation.

3.3 Changes in accounting policies and disclosures

Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Bank consolidated financial statements are disclosed below. The Bank intends to adopt these standards, if applicable, when they become effective.

IAS 1 *Presentation of Items of Other Comprehensive Income – Amendments to IAS 1*

The amendments to IAS 1 Presentation of Consolidated financial statements require companies preparing consolidated financial statements in accordance with IFRSs to group together items within OCI (other comprehensive income) that may be reclassified to the profit or loss section of the income statement. The amendments also reaffirm existing requirements that items in OCI and profit or loss should be presented as either a single statement or two consecutive statements. Annual periods beginning on or after 1 July 2012.

IAS 19 *Employee Benefits* (Revised)

The amendments to IAS 19 Employee Benefits, will provide investors and other users of consolidated financial statements with a much clearer picture of a company's current and future obligations resulting from the provision of defined benefit plans, and how these obligations will effect a company's financial position, financial performance and cash flows. This standard becomes effective for periods beginning on or after 1 January 2013.

IAS 28 *Investments in Associates and Joint Ventures* (as revised in 2011)

This Standard supersedes IAS 28 Investments in Associates and prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. Applicable to annual reporting periods beginning on or after 1 January 2013.

3. Basis of Preparation of Consolidated Financial Statements (continued)

IAS 32 *Offsetting Financial Assets and Financial Liabilities — Amendments to IAS 32*

These amendments clarify the meaning of “currently has a legally enforceable right to set-off”. The amendments also clarify the application of the IAS 32 offsetting criteria to settlement systems (such as central clearing house systems) which apply gross settlement mechanisms that are not simultaneous. These amendments are not expected to impact the Bank’s financial position or performance and become effective for annual periods beginning on or after 1 January 2014.

IFRS 1 *Government Loans – Amendments to IFRS 1*

These amendments require first-time adopters to apply the requirements of IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance,* prospectively to government loans existing at the date of transition to IFRS. Entities may choose to apply the requirements of IFRS 9 (or IAS 39, as applicable) and IAS 20 to government loans retrospectively if the information needed to do so had been obtained at the time of initially accounting for that loan. The exception would give first-time adopters relief from retrospective measurement of government loans with a below-market rate of interest. The amendment is effective for annual periods on or after 1 January 2013. The amendment has no impact on the Bank.

IFRS 7 *Disclosures — Offsetting Financial Assets and Financial Liabilities — Amendments to IFRS 7*

These amendments require an entity to disclose information about rights to set-off and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity’s financial position. The new disclosures are required for all recognised financial instruments that are set off in accordance with IAS 32 *Financial Instruments: Presentation*. The disclosures also apply to recognised financial instruments that are subject to an enforceable master arrangement or similar agreement, irrespective of whether they are set off in accordance with IAS 32. These amendments will not impact the Bank’s financial position or performance and become effective for annual periods beginning on or after 1 January 2013.

3. Basis of Preparation of Consolidated Financial Statements (continued)

IFRS 9 *Financial Instruments: Classification and Measurement*

IFRS 9, as issued, reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard was initially effective for annual periods beginning on or after 1 January 2013, but *Amendments to IFRS 9 Mandatory Effective Date of IFRS 9 and Transition Disclosures*, issued in December 2011, moved the mandatory effective date to 1 January 2015. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Bank's financial assets, but will not have an impact on classification and measurements of financial liabilities. The Bank will quantify the effect in conjunction with the other phases, when the final standard including all phases is issued.

IFRS 10 *Consolidated Financial Statements,* IAS 27 *Separate Financial Statements*

IFRS 10 replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements. It also addresses the issues raised in SIC-12 *Consolidation — Special Purpose Entities*.

IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 will require management to exercise significant judgement to determine which entities are controlled and therefore are required to be consolidated by a parent, compared with the requirements that were in IAS 27. Based on the preliminary analyses performed, IFRS 10 is not expected to have any impact on the currently held investments of the Bank.

This standard becomes effective for annual periods beginning on or after 1 January 2013.

IFRS 11 *Joint Arrangements*

IFRS 11 replaces IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly-controlled Entities — Non-monetary Contributions by Venturers*. IFRS 11 removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method.

The standard is effective for annual periods beginning on or after 1 January 2013. Replaces IAS 31 Interests in Joint Ventures. IFRS 11 provides for a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities.

3. Basis of Preparation of Consolidated Financial Statements (continued)

IFRS 12 ***Disclosure of Interests in Other Entities***

IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. A number of new disclosures are also required, but has no impact on the Bank financial position or performance. This standard becomes effective for annual periods beginning on or after 1 January 2013.

IFRS 13 ***Fair Value Measurement***

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The Bank is currently assessing the impact that this standard will have on the financial position and performance, but based on the preliminary analyses, no material impact is expected. This standard becomes effective for annual periods beginning on or after 1 January 2013.

IAS 1 ***Presentation of Consolidated Financial Statements***

This improvement clarifies the difference between voluntary additional comparative information and the minimum required comparative information. Generally, the minimum required comparative information is the previous period.

IAS 16 ***Property Plant and Equipment***

This improvement clarifies that major spare parts and servicing equipment that meet the definition of property, plant and equipment are not inventory.

IAS 32 ***Financial Instruments, Presentation***

This improvement clarifies that income taxes arising from distributions to equity holders are accounted for in accordance with IAS 12 *Income Taxes*.

IAS 34 ***Interim Financial Reporting***

The amendment aligns the disclosure requirements for total segment assets with total segment liabilities in interim consolidated financial statements. This clarification also ensures that interim disclosures are aligned with annual disclosures.

These improvements are effective for annual periods beginning on or after 1 January 2013.

3.1 Significant accounting judgments and estimates

Judgment

The preparation of the consolidated financial statements in conformity with International Financial Reporting Standards requires Management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on Management's best knowledge of current events and actions, actual results may ultimately differ from those estimates.

The Bank's management has made as assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future. Furthermore, the management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the consolidated financial statements continue to be prepared on the going concern basis.

Estimates

Impairment of financial assets

The Bank periodically reviews its individually significant loans and investments, in order to assess whether an impairment loss should be recorded in the statement of income. In particular, judgment by Management is required in the estimation of the amount and timing of future cash flow when determining the impairment loss. Such estimates are based on assumptions about a number of factors and actual results may differ, resulting in futures changes to the allowance.

In addition to specific allowances against individually significant loans and advances, the Bank also makes a collective impairment allowance which, although not identified as requiring a specific allowance, do have a risk exposure of default when originally granted. This takes into consideration factors such as any deterioration in country risk, industry and clearly identified structural weaknesses or deterioration in cash flows.

The Bank also records impairment charges on available for sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is significant or prolonged requires judgment. In marking this judgment, the Bank evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investments is less than its cost.

The impairment loss on available for sale investments is disclosed in more detail in Note 6.

4. Summary of Significant Accounting Policies

Fair value of financial instruments

Financial instruments are used by the Bank to manage market risk, facilitate customer transactions, hold proprietary positions and meet financing objectives. Fair value is determined by the Bank based on available listed market prices or broker price quotations. Assumptions regarding the fair value of each class of financial assets and liabilities are fully described in Note 10 to the consolidated financial statements.

Cash and cash equivalents

For presentation purposes, in its statement of cash flows, the Bank considers as cash and cash equivalents all highly liquid instruments with original maturities of three months or less. As of December 31, 2012 and 2011, cash and cash equivalents are represented by deposits with banks and overnight placements.

Financial assets

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and receivables, available for sale and held to maturity investments. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

Those categories are used to determine how a particular financial asset is recognized and measured in the consolidated financial statements.

Financial assets at fair value through profit or loss. This category has two subcategories:

- Designated upon initial recognition. The first includes any financial asset that is designated on initial recognition as one to be measured at fair value with fair value changes in profit or loss.

- Held for trading. The second category includes financial assets that are held for trading. All derivatives (except those designated hedging instruments) and financial assets acquired or held for the purpose of selling in the short term or for which there is a recent pattern of short-term profit taking are held for trading.

Available-for-sale financial assets (AFS) are any non-derivative financial assets designated on initial recognition as available for sale. AFS assets are measured at fair value in the statement of financial position. Fair value changes on AFS assets are recognized directly in equity, through the statement of comprehensive income, except for interest on AFS assets (which is recognized in income on an effective yield basis), impairment losses, and (for interest-bearing AFS debt instruments) foreign exchange gains or losses. The cumulative gain or loss that was recognized in equity is recognized in profit or loss when an available-for-sale financial asset is derecognized.

4. Summary of Significant Accounting Policies (continued)

Loans and receivables are non-derivative financial assets with fixed or determinable payments, originated or acquired, that are not quoted in an active market, not held for trading, and not designated on initial recognition as assets at fair value through profit or loss or as available-for-sale. Loans and receivables are measured at amortized cost using the effective interest rate method.

The Bank seeks to use collateral, where possible, to mitigate its risks on financial assets. The collateral comes in various forms such as cash, securities, letters of credit/guarantees. The fair value of collateral is generally assessed, at a minimum, at inception and based on the Bank's monthly reporting schedule, however, some collateral, for example, cash or securities relating to margining requirements, is valued daily. To the extent possible, the Bank uses active market data for valuing financial assets, held as collateral.

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments that an entity intends and is able to hold to maturity and that do not meet the definition of loans and receivables and are not designated on initial recognition as assets at fair value through profit or loss or as available for sale. Held-to-maturity investments are measured at amortized cost. If an entity sells a held-to-maturity investment other than in insignificant amounts or as a consequence of a non-recurring, isolated event beyond its control that could not be reasonably anticipated, all of its other held-to-maturity investments must be reclassified as available-for-sale for the current and next two financial reporting years.

Financial Liabilities

The Bank recognizes, in compliance to IAS 39, two classes of financial liabilities:

- Financial liabilities at fair value through profit or loss.
- Other financial liabilities measured at amortized cost using the effective interest method.

Initial recognition and measurement

The Bank uses a classification of financial asset or a financial liability depending on the purposes for which they were acquired and their characteristics. All financial assets or liabilities are recorded at their fair value plus, in the case of financial assets and financial liabilities not at fair value through profit and loss, any directly attributable incremental costs of acquisition or issue. Financial assets and liabilities carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the statement of income. A regular way purchase or sale of financial assets and liabilities is recognized and derecognized using either trade date or settlement date accounting. The Bank has adopted the method of trade accounting to recognize its financial assets and liabilities; this method has been applied consistently for all purchases and sales of financial assets and liabilities that belong to the same category of financial asset and liabilities.

4. Summary of Significant Accounting Policies (continued)

Financial assets and all financial liabilities have been recognized on the statement of financial position, including all derivatives as described in 'Derivative financial instruments' section.

Measurement subsequent to initial recognition

Subsequently, the Bank measures their financial assets and liabilities (including derivatives) at fair value, with the following exceptions:

Loans and receivables, held-to-maturity investments, and non-derivative financial liabilities, which have been measured at amortized cost using the effective interest method.

Financial assets and liabilities that are designated as a hedged item or hedging instrument are subject to measurement under the hedge accounting requirements.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. For its available-for-sale financial assets the Bank uses quoted market prices in an active market or dealer price, which are the best evidence of fair value, where they exist, to measure the financial instrument. The fair value of investment funds are determined by reference to the net asset values of the funds as provided by respective administrators of such funds the net asset value review in order to determined the reported balance is appropriate or it may be necessary to make adjustments.

Amortized cost is calculated using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or liability.

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Bank has transferred substantially all risks and rewards of ownership. When securities classified as available for sale are sold or impaired, the accumulated fair value adjustments recognized in equity are included in the statement of income as gains and losses from investment securities.

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as derecognition of the original liability, and the difference in the respective carrying amounts is recognized in profit or loss.

4. Summary of Significant Accounting Policies (continued)

Loans and borrowings

After initial recognition, interest bearing loans and borrowings are subsequently measured at amortized cost using the effective interest rate method.

Interest income and expense

Interest income and expense is recognized in the statement of income for all interest-bearing instruments on an accrual basis applying the effective yield method to the actual purchase price. Interest income includes coupons earned on fixed income investment and accredited discount on debt instruments. When a loan becomes of doubtful collection, it is written down to recoverable amount and interest income is thereafter recognized at the rate of interest which had been used to discount the future cash flows for the purpose of determining the recoverable amount.

Fees and commissions income

Fees and commissions are generally recognized on an accrual basis once service has been rendered. Loan origination fees are deferred and recognized over the life of the loan.

Foreign currency operations

The Bank's transactions are performed mostly in U.S. Dollars, its functional and reporting currency. Foreign currency transactions are translated into U.S. Dollars at the prevailing exchange rates on the date of the transaction. Foreign exchange gains or losses resulting from the settlement of such transactions and from the translation of monetary assets are measured at the date of the statement of financial position and liabilities denominated in foreign currencies are recognized in the income statement.

Translation differences on debt securities and other financial assets measured at fair value are included as foreign exchange income in the statement of income with the exception of difference on foreign borrowing that provide an effective hedge against a net investment in a foreign security which are taken directly to other comprehensive income until the disposal of net investment, at which time they are recognized in the statement of income.

Derivative financial instruments

The Bank makes use of derivative financial instruments, such as options, short selling, futures, forward foreign currency contracts, interest rate swaps and credit default swaps to manage exposure to interest rate, foreign currency and credit risk, including those arising from forecast transactions. In order to manage particular risks, the Bank applies a different accounting basis taking into account the use of derivative financial instruments as trading purposes.

4. Summary of Significant Accounting Policies (continued)

Derivative financial instrument operations are recognized initially at fair value. The fair value of derivative financial instruments is calculated by reference to current interest and exchange rates.

The changes in fair value are recorded as assets when the fair value is positive and as liabilities when it is negative. The gain or loss related to changes in fair value is recorded in the statement of income.

Premises and equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation and amortization are calculated on a straight-line basis over the useful life of the assets as follows:

Furnitures and office equipments	2 to 3 years
Vehicles	5 years
Leasehold improvement	5 years

The carrying values of premises and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable.

Intangible asset

Costs associated with maintaining computer software programs are recognized as an expense as incurred. Costs that are directly associated with identifiable and unique software products controlled by the Bank and will generate economic benefits exceeding costs beyond one year, are recognized as intangible asset.

Expenditures which enhance or extend the performance of computer software programmers beyond their original specifications are recognized as a capital improvement and therefore added to the original cost of the software. Computer software costs recognized as assets are amortized using the straight-line method over their useful lives, not exceeding 5 years.

Fiduciary activities

Assets and income arising from fiduciary activities, together with related undertakings to deliver such assets to customers, are excluded from these consolidated financial statements if the Bank acts in a fiduciary capacity such as a nominee, trustee or agent.

Income taxes

The Bank operations are tax exempted in both the Cayman Islands and in the Republic of Panama.

5. Other Interest – Bearing Deposits with Banks

	December 31	
	2012	2011
	US$ 000	US$ 000
Banco de Credito and subsidiaries		
(a subsidiary of Credicorp Ltd.)	**219**	219
Other financial institutions	**276**	2,474
	495	2,693

6. Risk Portfolio, Net

	December 31	
	2012	2011
	US$ 000	US$ 000
Reverse repurchased agreement	**7,500**	16,300
Available-for-sale financial assets, net	**793,453**	792,607
Held to maturity financial assets, net	**1,527**	2,724
Loan portfolio, net	**801,125**	606,112
	1,603,605	1,417,743

Reverse repurchase agreement

At December 31, 2012, the Bank held investments in securities under reverse repurchase agreements for US$7.5 million (2011 US$16.3 million), maturing through January 2, 2013, with an annual average interest rate of 0.24% .

6. Risk Portfolio, Net (continued)

Financial Assets

	2012			
	Cost US$000	Gross unrealized gain US$000	Gross unrealized loss US$000	Fair value US$000
Available for sale				
Federal Agencies notes - U.S.	**10,462**	**316**	**-**	**10,778**
U.S. Corporate bonds	**336,740**	**14,898**	**(2,646)**	**348,992**
Non - U.S. Corporate bonds	**330,537**	**13,072**	**(1,497)**	**342,112**
Equity securities (including funds)	**49,732**	**8,319**	**(7,728)**	**50,323**
Sovereign debt	**40,474**	**837**	**(63)**	**41,248**
Subtotal	**767,945**	**37,442**	**(11,934)**	**793,453**
Held to maturity				
U.S. Corporate bonds	**1,527**	**-**	**-**	**1,527**
Subtotal	**1,527**	**-**	**-**	**1,527**
Less:				
Provision for impairment of financial assets	**(15,598)**	**-**	**15,598**	**-**
	753,874	**37,442**	**3,664**	**794,980**

	2011			
	Cost US$000	Gross unrealized gain US$000	Gross unrealized loss US$000	Fair value US$000
Available for sale				
Federal Agencies notes - U.S.	13,669	372	(3)	14,038
U.S. Corporate bonds	412,327	7,559	(11,647)	408,239
Non - U.S. Corporate bonds	251,466	5,013	(1,782)	254,697
Equity securities (including funds)	52,888	5,966	(9,104)	49,750
Sovereign debt	65,535	584	(236)	65,883
Subtotal	795,885	19,494	(22,772)	792,607
Held to maturity				
U.S. Corporate bonds	2,724	-	-	2,724
Subtotal	2,724	-	-	2,724
Less:				
Provision for impairment of financial assets	(17,237)	-	17,237	-
	781,372	19,494	(5,535)	795,331

6. Risk Portfolio, Net (continued)

Fair value for available-for-sale assets portfolio is represented by quoted market prices in an active market or dealer price where investments are not actively traded, which are the best evidence of fair value, where they exist, to measure the financial assets. The fair value of investment funds are determined by reference to the net asset values of the funds as provided by respective administrators of such funds.

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation techniques:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities.

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

	December 31, 2012			
	Level 1	Level 2	Level 3	Total
	US$000	US$000	US$000	US$000
Financial assets				
Derivatives held for trading				
Interest rate swaps	-	153	-	153
Futures	26	-	-	26
Credit default swaps	-	229	-	229
Total	26	382	-	408
Available for sale				
Debt securities	696,879	32,409	15,369	744,657
Equity securities (including mutual funds)	21,070	-	29,253	50,323
Total	717,949	32,409	44,622	794,980
	717,975	32,791	44,622	795,388
Financial liabilities				
Derivatives held for trading				
Forward foreign currency contracts - sale	-	92	-	92
Interes rate swaps	-	337	-	337
Credit default swaps	-	146	-	146
Total	-	575	-	575

6. Risk Portfolio, Net (continued)

The following table shows a reconciliation of the opening and closing amount of level 3 financial asset which are recorded at fair value:

	At January 1, 2012 US$000	Total gains/ (losses) recorded in profit or loss US$000	Total gains/ (losses) recorded in equity US$000	Purchases US$000	Sale US$000	Transfers from level 2 to level 3 US$000	At December 31, 2012 US$000
Available for sale							
Debt securities	2,724	-	-	7,757	-	4,888	15,369
Equity securities (including mutual funds)	12,164	-	838	3,258	(101)	13,094	29,253
Total	14,888	-	838	11,015	(101)	17,982	44,622

During 2012 due to the change in the available information of certain securities available for sale quoted prices in active markets based on a conservative approach as they do not met all the criteria for classification in Level 2 and became less liquid, the Bank transferred those securities from Level 2 to Level 3.

	December 31, 2011			
	Level 1	Level 2	Level 3	Total
	US$000	US$000	US$000	US$000
Financial assets				
Derivatives held for trading				
Futures	-	3	-	3
Credit default swaps	-	177	-	177
Total	-	180	-	180
Available for sale				
Debt securities	711,479	31,378	2,724	745,581
Equity securities (including mutual funds)	19,204	18,382	12,164	49,750
Total	730,683	49,760	14,888	795,331
Financial liabilities				
Derivatives held for trading				
Forward foreign currency contracts - sale	-	393	-	393
Interes rate swaps	-	329	-	329
Futures	179	-	-	179
Credit default swaps	-	590	-	590
Total	179	1,312	-	1,491

6. Risk Portfolio, Net (continued)

The following table shows a reconciliation of the opening and closing amount of level 3 financial asset which are recorded at fair value:

	At January 1, 2011 US$000	Total gains/ (losses) recorded in profit or loss US$000	Total gains/ (losses) recorded in equity US$000	Purchases US$000	Sale US$000	At December 31, 2011 US$000
Available for sale						
Debt securities	11,307	-	(295)	-	(8,288)	2,724
Equity securities (including mutual funds)	14,442	73	321	-	(2,672)	12,164
Total	25,749	73	26	-	(10,960)	14,888

For the Level 3 investments, the Bank use consensus pricing from brokers, from industry publications and other industry materials that includes unobservable inputs (those inputs for which there is little or no current observable data available). The Bank is conscious that the fair value could be adjusted for increase or decrease to reported value using possible alternative assumption, but since the prices used by the broker had revealed that these prices have resulting very close to the fair value or execution value the sensitivity analysis is not relevant to be presented.

Amounts reported in the income statements relating to gains on available-for-sale financial assets are detailed as follows on December 31:

	2012 US$ 000	2011 US$ 000
Realized gains on sales of financial assets	**7,705**	6,937

At December 31, the financial assets, available-for-sale investment and held to maturity are summarized as follows:

	2012 US$ 000	2011 US$ 000
Balance at January 1st	**795,331**	739,189
Purchases	**512,482**	563,735
Sales and written-off, net	**(539,980)**	(495,724)
Gain (loss) from changes in fair value	**27,147**	(11,869)
Balance at December 31	**794,980**	795,331

6. Risk Portfolio, Net (continued)

The table below presents an analysis of the available-for-sale investments and held to maturity investments by rating agency designation at December 31, based on Standard & Poor's rating or its equivalent:

	2012					
Available for sale	**Federal Agencies Notes-U.S. US$000**	**US - Corporate Bonds US$000**	**Non - US Corporate Bonds US$000**	**Sovereign Debt US$000**	**Equities Securities & Funds US$000**	**Total US$000**
AAA	**2,006**	**-**	**7,463**	**401**	**-**	**9,870**
AA- to AA+	**2,710**	**6,596**	**15,379**	**2,131**	**-**	**26,816**
A- to A+	**-**	**97,232**	**62,926**	**-**	**-**	**160,158**
BBB- to BBB+	**-**	**124,786**	**161,515**	**1,964**	**5,945**	**294,210**
Lower than BBB-	**-**	**119,841**	**68,755**	**5,459**	**523**	**194,578**
Unrated	**6,062**	**538**	**26,075**	**31,292**	**43,854**	**107,821**
	10,778	**348,993**	**342,113**	**41,247**	**50,322**	**793,453**
Held to Matiurity						
AAA	**-**	**1,527**	**-**	**-**	**-**	**1,527**
Total	**10,778**	**350,520**	**342,113**	**41,247**	**50,322**	**794,980**

	2011					
Available for sale	Federal Agencies Notes-U.S. US$000	US - Corporate Bonds US$000	Non - US Corporate Bonds US$000	Sovereign Debt US$000	Equities Securities & Funds US$000	Total US$000
AAA	-	10,038	14,204	1,391	-	25,633
AA- to AA+	3,764	10,079	10,985	-	-	24,828
A- to A+	-	109,083	58,121	1,541	-	168,745
BBB- to BBB+	-	156,927	121,037	14,866	4,428	297,258
Lower than BBB-	-	121,391	31,417	6,132	-	158,940
Unrated	10,274	721	18,933	41,953	45,322	117,203
	14,038	408,239	254,697	65,883	49,750	792,607
Held to Matiurity						
AAA	-	2,724	-	-	-	2,724
Total	14,038	410,963	254,697	65,883	49,750	795,331

6. Risk Portfolio, Net (continued)

Loan portfolio, net

The loan portfolio by customers' activity at December 31 is detailed as follows:

	December 31	
	2012	2011
	US$ 000	US$ 000
Corporate:		
Manufacturing	**109,143**	94,499
Commercial	**226,601**	145,233
Financial services	**92,125**	91,058
Agriculture	**68,806**	44,844
Real estate and construction	**128,393**	104,518
Mining and other related activities	**6,064**	2,749
Transportation and communications	**70,391**	64,141
Education, health and other services	**11,687**	7,030
Fishing	**72,731**	48,758
	785,941	602,830
Other activity	**15,810**	4,108
	801,751	606,938
Less: provision for loan losses	**(626)**	(826)
	801,125	606,112

As of December 31, 2012 there are loans guaranteed with cash amounted to US$539,431 (2011 – US$515,223). These loans were matched in amount and maturity.

The distribution for loan portfolio by type of interest rates is as follows:

	December 31	
	2012	2011
	US$ 000	US$ 000
Fixed interest rates	**665,377**	520,028
Floating interest rates	**136,374**	86,910
	801,751	606,938

6. Risk Portfolio, Net (continued)

A summary of the loan portfolio by the geographic location of the borrowers and the respective collateral is as follows:

		Loan Collaterals			
	Carrying value US$000	U.S. securities and real estate US$000	U.S. dollar deposits US$000	Other collateral US$000	Unsecured portion US$000
Bermuda	**18,000**	**-**	**3,000**	**-**	**15,000**
Chile	**1,850**	**-**	**1,850**	**-**	**-**
United State of America	**1,500**	**1,500**	**-**	**-**	**-**
Venezuela	**339**	**-**	**-**	**339**	**-**
Spain	**1,654**	**-**	**-**	**-**	**1,654**
British Virgin Islands	**13,279**	**2,629**	**35**	**9,865**	**750**
Mexico	**600**	**-**	**-**	**-**	**600**
Panama	**16,256**	**1,215**	**2,167**	**10,874**	**2,000**
Peru	**738,993**	**25,457**	**532,179**	**102,635**	**78,722**
Switzerland	**131**	**-**	**-**	**131**	**-**
Cayman Islands	**8,910**	**575**	**-**	**8,335**	**-**
Colombia	**39**	**-**	**-**	**39**	**-**
Canada	**200**	**-**	**200**	**-**	**-**
	801,751	**31,376**	**539,431**	**132,218**	**98,726**

6. Risk Portfolio, Net (continued)

	Loan Collaterals				
	Carrying value US$000	U.S. securities and real estate US$000	U.S. dollar deposits US$000	Other collateral US$000	Unsecured portion US$000
Bermuda	8,000	-	3,000	-	5,000
Chile	1,850	-	1,850	-	-
United State of America	5,565	1,500	-	-	4,065
Spain	2,452	-	-	-	2,452
British Virgin Islands	6,119	3,129	1,540	1,450	-
Mexico	600	-	-	-	600
Panama	22,888	4,495	11,203	180	7,010
Peru	553,799	16,827	497,311	35,416	4,245
Switzerland	326	-	119	207	-
Cayman Islands	5,139	1,520	-	3,619	-
Canada	200	-	200	-	-
	606,938	27,471	515,223	40,872	23,372

Provision

Changes in the provision for impairment of financial assets and provision for loan losses are as follows:

	2012		
	Provision for Impairment of Financial Assets **US$000**	***Provision for Loan Losses*** **US$000**	***Total*** **US$000**
Balance at January 1st	**17,237**	**826**	**18,063**
Reversals	**(345)**	**(200)**	**(545)**
Write-off	**(1,294)**	**-**	**(1,294)**
Balance at December 31	**15,598**	**626**	**16,224**

6. Risk Portfolio, Net (continued)

	2011		
	Provision for Impairment of Financial Assets US$000	*Provision for Loan Losses* US$000	*Total* US$000
Balance at January 1st	36,589	898	37,487
Increase	1,000	131	1,131
Reversals	(12)	(203)	(215)
Write-off	(20,340)	-	(20,340)
Balance at December 31	17,237	826	18,063

7. Other Borrowed Funds

As of December 31, 2012 the Bank maintained in repurchase agreements with values amounted to US$21,739 and US$104,507 with maturity of February 19, 2013 and March 4, 2013 and an annual rate of 1.10%; and working capital US$10,000 with maturity of January 28, 2013 and an annual rate of 1.5127%. However in 2011 the Bank no maintained no balance in other borrowed funds.

The following table details other borrowed funds:

	December 31	
	2012 **US$ 000**	2011 US$ 000
Amount at the end of the year	**136,246**	-
Average during the year	**44,961**	11,959
Maximum at any month end	**168,853**	45,792

8. Balances and Transactions with Related Parties

The term "related parties" is defined by Management to encompass other affiliated parties over which control or significant influence exists through common ownership, management or directorships. In the ordinary course of its business the Bank has incurred transactions with related parties such as shareholders, non-consolidated companies, directors and key management personnel.

8. Balances and Transactions with Related Parties (continued)

	December 31			
	2012		2011	
	Directors, key management personnel and other related parties US$000	**Affiliates US$000**	Directors, key management personnel and other related parties US$000	Affiliates US$000
Statement of financial position				
Assets:				
Interest-bearing deposits with banks	**-**	**196,925**	-	4,465
Overnight placements	**-**	**70,000**	-	12,000
Other interest-bearing deposits with banks	**-**	**219**	-	219
Risk portfolio:				
Investments in financial instruments, mutual funds managed by the Bank and other related parties	**686**	**-**	1,343	-
Loans	**18,192**	**70,481**	35,153	77,396
Accumulated interest receivable	**411**	**2,842**	428	1,582
Other assets	**707**	**55**	-	290
Liabilities:				
Deposits (demand and time)	**252,041**	**19,298**	135,390	16,326
Accumulated interest payable	**3,254**	**25**	1,897	25
Other liabilities	**-**	**485**	-	744

For the years ended December 31, 2012 and 2011, the Bank has not made any provision for doubtful debts relating to amounts owed by related parties. The loans that counted on tangible guarantees as financial goods and values amounted to US$9,282 in 2012 (2011: US$30,015).

	December 31			
	2012		2011	
	Directors, key management personnel and other related parties US$000	**Affiliates US$000**	Directors, key management personnel and other related parties US$000	Affiliates US$000
Off-balance sheet:				
Forward currency contracts	**-**	**3,000**	-	3,000
Commitments for letter of credit	**-**	**20,437**	-	25,422
Investment on behalf of customers	**632,003**	**-**	580,549	-
Statements of income:				
Interest and dividend income	**1,146**	**3,690**	876	16,954
Interest expense	**3,711**	**31**	3,369	11
Losses on derivative financial instrument	-	**104**	-	403
Fee and commission income	**-**	**-**	-	430
Fee and commission expense	**-**	**1,259**	-	1,390
General and administrative expenses	-	**345**	-	410

8. Balances and Transactions with Related Parties (continued)

As of December 31, 2012, the Bank does not has loans receivable on related parties. However in 2011, the Bank had loans receivable from related parties by $4,416, which are not included in the statement of financial position due to the fact that full risk participations have been sold off to customers without recourse to the Bank.

As of December 31, 2012, the other interest-bearing deposits with banks include deposits with Banco de Credito de Peru, S. A. and Subsidiaries for US$219, and guarantee revolving credit line loans with Banco de Credito de Peru, S. A. and Subsidiaries US$55,481 (2011: US$77,396), where full risk participation has been sold off to customers without recourse to the Bank and the full amount is guaranteed by deposits received from customers.

9. Risk Management

The Bank's operations are exposed to a wide variety of financial risks: market risk (including currency risk, fair value interest rate risk, cash flow interest rate risk and price risk), credit risk and liquidity risk. Overall risk management programmes focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Bank's financial performance.

Market risk

The Bank takes on exposure to market risk, which is the risk that the fair value or future cash flow of financial instruments, will fluctuate because of changes in market prices. Market risk arises from open positions in interest rate, currency and equity products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credits spreads, foreign exchange rates and equity prices.

The Bank´s Asset/Liability Committee (ALCO) is responsible for managing and monitoring all of the Bank's risk exposures. Risk exposures are managed through control limits established for position size and overall risk exposure limits. In addition, the Bank maintains proper segregation of duties, with credit review and risk-monitoring functions performed by bodies that are independent from business producing units.

Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Bank is able to manage these risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

9. Risk Management (continued)

Credit risk

The Bank seeks to minimize and control its risk exposure by establishing a variety of separate but complementary financial, credit, operational and legal reporting schemes. The Bank's Executive Committee, duly authorized by the Board of Directors, determines the type of business in which the Bank engages and also approves guidelines for accepting customers, outlines the terms on which customer business is conducted and establishes the parameters for the risks that the Bank is willing to accept.

The Bank takes on exposure to credit risk, the risk that a counterparty will be unable to pay all amounts in full when due. The Bank structures the credit risk levels it accepts by placing limits on the amount of risk accepted in relation to one borrower, or group of borrowers, or geographical segment. Such risks are monitored on a revolving basis and subject to periodic review. Limits on levels of credit by product and country are reviewed and approved quarterly by the Board of Directors.

Financial assets which potentially expose the Bank to concentrations of credit risk consist primarily of cash and cash equivalents, interest-bearing deposits with banks, certain available-for-sale securities, loans and other assets. Cash and cash equivalents and interest-bearing deposits with banks are placed either with related parties or reputable financial institutions. An analysis of the Bank's available-for-sale securities and loans according to its credit risk rating is provided in Note 6.

Exposure to credit risk is managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations, and by adjusting lending limits as appropriate. Exposure to credit risk is also managed in part by obtaining collateral, corporate and personal guarantees.

Credit related commitments

The primary purpose of these instruments is to ensure that funds are available to customers as required. Guarantees and stand-by letters of credit, which represent irrevocable assurances that the Bank will execute payments in the event that a customer cannot meet its obligations to third parties, carry the same risk as loans. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore carry less risk than a direct borrowing.

The Bank's credit policies and procedures to approve credit commitments, guarantees and commitments. To purchase and sell securities are the same as those applicable to extension of credits which are on balance sheet and take into account their collateral and other security, if any.

9. Risk Management (continued)

Interest rate risk

The Bank is exposed to cash flow and fair value interest rate risk in the course of major operations. To manage these exposures the Bank has established a variety of separate but complementary financial, investment, operational and credit reporting schemes to determine the current position on financial assets and liabilities and how its impacted for a change in the interest rate risk.

The price risk factor that mainly affects the value of the Bank investment portfolio is interest rates. Interest Rate Risk Management is an integral component of the Asset/Liability Management (ALM) methodology in use by the Bank, which models and measures the effect that interest rate risk has over the Bank's income in the short-term.

The Bank's investment portfolio is managed through a long term investment (buy and hold) strategy and not as of a proprietary trading book, hence, its exposure to market price risk in the short-term is not considered to be relevant.

The Bank takes on exposure to the effects of fluctuations at the prevailing level of market interest rates on its financial position and cash flows. Interest margins may increase as a result of such changes, but may reduce or create losses in the event that unexpected movement materializes.

The table below summarizes the Bank's exposures to interest rate risk. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by the earlier of contractual repricing or maturity dates.

9. Risk Management (continued)

				2012			
	Up to	**1 to 3**	**3 to 12**	**1 to 5**	**Over**	**Non interest**	
Assets	**1 month**	**months**	**months**	**years**	**5 years**	**bearing**	**Total**
	US$000	**US$000**	**US$000**	**US$000**	**US$000**	**US$000**	**US$000**
Cash and cash equivalents	**136,030**	**195**	**-**	**-**	**-**	**34**	**136,259**
Due from banks	**-**	**170**	**325**	**-**	**-**	**-**	**495**
Financial assets	**23,656**	**31,747**	**65,284**	**421,745**	**177,309**	**75,239**	**794,980**
Loans	**104,562**	**135,636**	**248,643**	**269,784**	**50,000**	**-**	**808,625**
Other assets	**-**	**-**	**-**	**-**	**-**	**28,112**	**28,112**
	264,248	**167,748**	**314,252**	**691,529**	**227,309**	**103,385**	**1,768,471**
Liabilities							
Deposits:							
Non-interest bearing	**-**	**-**	**-**	**-**	**-**	**464,998**	**464,998**
Interest bearing	**236,177**	**163,358**	**474,447**	**7,863**	**50,000**	**-**	**931,845**
Borrowed funds	**10,000**	**126,246**	**-**	**-**	**-**	**-**	**136,246**
Other liabilities	**-**	**-**	**-**	**-**	**-**	**15,597**	**15,597**
	246,177	**289,604**	**474,447**	**7,863**	**50,000**	**480,595**	**1,548,686**
Total interest sensitivity gap	**18,071**	**(121,856)**	**(160,195)**	**683,666**	**177,309**		

				2011			
	Up to	1 to 3	3 to 12	1 to 5	Over	Non interest	
Assets	1 month	months	months	years	5 years	bearing	Total
	US$000	US$000	US$000	US$000	US$000	US$000	US$000
Cash and cash equivalents	72,691	250	34	4,000	-	26	77,001
Due from banks	871	658	310	854	-	-	2,693
Financial assets	41,534	54,999	65,223	442,649	157,477	49,749	811,631
Loans	66,021	96,815	139,494	253,782	50,000	-	606,112
Other assets	-	-	-	-	-	26,092	26,092
	181,117	152,722	205,061	701,285	207,477	75,867	1,523,529
Liabilities							
Deposits:							
Non-interest bearing	-	-	-	-	-	390,403	390,403
Interest bearing	212,476	144,187	453,775	69,806	50,000	-	930,244
Other liabilities	-	-	-	-	-	13,645	13,645
	212,476	144,187	453,775	69,806	50,000	404,048	1,334,292
Total interest sensitivity gap	(31,359)	8,535	(248,714)	631,479	157,477		

9. Risk Management (continued)

The sensitivity to a reasonable possible change in interest rates, with all other variables held constant, of the Bank's statement of income were demonstrates as follows:

Financial Margin Sensitivity	**2012** Sensitivity Increase 100 bps	**2012** Sensitivity Decrease 100 bps	2011 Sensitivity Increase 100 bps	2011 Sensitivity Decrease 100 bps
	US$000	**US$000**	US$000	US$000
Assets:				
Due from banks	**(412)**	**7**	(466)	272
Loans	**(4,336)**	**4,303**	(2,845)	2,843
Financial assets	**(807)**	**653**	(1,137)	865
	(5,555)	**4,963**	(4,448)	3,980
Liability				
Deposits	**5,689**	**(3,659)**	5,010	(2,674)
	5,689	**(3,659)**	5,010	(2,674)
Total interest sensivity gap	**134**	**1,304**	562	1,306

The table below summarizes the weighted average interest rates for assets and liabilities as of December 31:

	***2012* % End of year**	***2012* % During the year**	*2011 % End of year*	*2011 % During the year*
Assets:				
Interest-bearing deposits with banks	**0.48**	**0.30**	0.36	0.30
Financial assets	**4.07**	**3.99**	3.61	3.70
Loans	**5.61**	**5.94**	7.16	6.60
Liabilities				
Deposits	**3.74**	**3.48**	3.65	3.51
Borrowed funds	**1.10**	**0.82**	-	1.11

Liquidity risk

Prudent liquidity risk management implies maintaining sufficient cash and marketable securities, the availability of funding through an adequate amount of committed credit facilities and the ability to close out market positions. Due to the dynamic nature of the underlying businesses, the Bank treasury maintains flexibility in funding by maintaining availability under committed credit lines. Management monitors rolling forecasts of the Bank's liquidity on the basis of expected cash flow.

9. Risk Management (continued)

The Bank is exposed to daily calls on available cash resources from overnight deposits, current accounts, maturing deposits, loan draw downs and guarantees. The Bank does not maintain cash resources to meet all of these needs, as experience with its specific customer base shows that a minimum level of reinvestment of maturing can be predicted with a high degree of certainty. As of December 31, 2012 and 2011, the Bank holds a substantial amount of securities which Management considers as secondary liquidity source.

The table below analyzes the Bank's assets and liabilities into relevant maturity groupings based on the time remaining from balance sheet date to the contractual maturity date.

			2012			
Assets	**Up to 1 month US$000**	**1 to 3 months US$000**	**3 to 12 months US$000**	**1 to 5 years US$000**	**Over 5 years US$000**	**Total US$000**
Cash and cash equivalents	**136,064**	**195**	**-**	**-**	**-**	**136,259**
Due from banks	**-**	**170**	**105**	**220**	**-**	**495**
Financial assets	**18,910**	**41,973**	**69,432**	**444,908**	**186,124**	**761,347**
Loans	**73,001**	**119,509**	**244,569**	**302,691**	**68,855**	**808,625**
Other assets	**4,033**	**8,065**	**12,096**	**3,918**	**-**	**28,112**
	232,008	**169,912**	**326,202**	**751,737**	**254,979**	**1,734,838**
Liabilities						
Deposits:						
Non-interest bearing	**209,249**	**69,750**	**-**	**185,999**	**-**	**464,998**
Interest bearing	**187,415**	**176,657**	**199,083**	**310,827**	**57,863**	**931,845**
Borrowed funds	**10,000**	**126,246**	**-**	**-**	**-**	**136,246**
Other liabilities	**2,354**	**4,616**	**6,924**	**1,703**	**-**	**15,597**
	409,018	**377,269**	**206,007**	**498,529**	**57,863**	**1,548,686**
Net liquidity gap	**(177,010)**	**(207,357)**	**120,195**	**253,208**	**197,116**	**186,152**

9. Risk Management (continued)

	2011					
Assets	Up to 1 month US$000	1 to 3 months US$000	3 to 12 months US$000	1 to 5 years US$000	Over 5 years US$000	Total US$000
Cash and cash equivalents	72,717	250	34	4,000	-	77,001
Due from banks	871	658	310	854	-	2,693
Financial assets	39,535	56,663	68,335	463,411	162,519	790,463
Loans	59,384	75,919	369,886	50,940	49,983	606,112
Other assets	3,608	7,216	10,825	1,530	2,913	26,092
	176,115	140,706	449,390	520,735	215,415	1,502,361
Liabilities						
Deposits:						
Non-interest bearing	175,681	58,560	-	156,162	-	390,403
Interest bearing	151,359	155,299	194,758	378,828	50,000	930,244
Other liabilities	2,272	4,544	6,829	-	-	13,645
	329,312	218,403	201,587	534,990	50,000	1,334,292
Net liquidity gap	(153,197)	(77,697)	247,803	(14,256)	165,415	168,069

The matching and controlled miss-matching of the maturities and interest rates of assets and liabilities is fundamental to the Management of the Bank. It is unusual for banks ever to be completely matched since business transacted is often for uncertain terms and of different types. An unmatched position potentially enhances profitability, but also increases the risk of losses.

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

Liquidity required to support calls under guarantees and stand-by letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under agreement. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash needs, since many of these commitments will expire or terminate without actually being funded.

Capital risk

The Bank monitors its capital adequacy using ratios based on industry best practices and the recommendations issued by the Basel Committee on Banking Regulations and Supervisory Practices. The capital adequacy ratio measures capital adequacy by comparing the Bank's eligible capital, net with its risk exposure in the statements of financial position assets, off-balance sheet commitments positions at a weighted amount including an additional scope about risk sensitive approaches to credit risk and operational risk capital requirements. These internal ratios are based on both an Earnings-at-Risk model and a Net Economic Value Sensitivity model, which are part of the Bank's ALM (Asset/Liability Management) methodology. These models yield an estimate of the potential loss that might occur if the Bank's statements of financial position structure remained unchanged during specific periods of time and market volatility affects its risk exposure.

9. Risk Management (continued)

The Bank is subject to regulatory capital requirements established by the Cayman Islands Monetary Authority (“CIMA”). Failure to meet minimum capital requirements can initiate certain actions by the regulators that, if undertaken, could have a direct material effect on the Bank’s consolidated financial statements. Under capital adequacy guidelines used by CIMA and prescribed under The Banks and Trust Companies Law (Revised) of the Cayman Islands, the Bank must meet specific capital guidelines that involve quantitative measures of the Bank’s assets, liabilities, and certain off-balance sheet items as calculated under regulatory accounting practices. The Bank’s capital amounts and classification are also subject to qualitative judgments by CIMA about components and risk weightings.

The Cayman Island Monetary Authority (CIMA) had implemented the Basel II Framework, which describes a comprehensive measure and minimum standard for capital adequacy that seeks to improve on the existing Basel I rules by aligning regulatory capital requirements more closely to the underlying risks that banks face. The implementation of the Basel II accord, which consists of 3 'Pillars', go well beyond the mechanistic calculation of minimum capital levels set by Basel I, allowing Banks to use their own models to calculate regulatory capital while seeking to ensure that Banks establish a culture with risk management.

CIMA proposed to apply the Basel II Framework in two phases leveraging a practical measured approach. The first phase of the implementation was completed on December 31, 2011 and implemented throughout the 2012. It’s comprised the following Pillar 1 approaches:

- Credit Risk – Standardized
- Market Risk – Standardized
- Operational Risk – Basic Indicator Approach and The Standardized Approach

The Pillar 1 provides a methodology for determining minimum capital requirements similar to Basel I, under Basel I this calculation related only to credit risk, with a calculation for market risk, Basel II adds a further charge to allow for operational risk.

The approaches used by the Bank to calculate its capital requirements covers the credit risk and operational risk of the Bank’s operations and the specific risks of open positions in currencies, debt, and equity securities included in the risk portfolio. Assets are weighted according to broad categories of notional credit risk, the credit risk weighting has been determined by the external credit ratings assigned to the borrower and the operational risk has been determined using the standardized approach method. The Capital Ratio is determined dividing eligible regulatory capital by total risk-weighted assets.

The first phase of the Basel II implementation will also include Pillar 2 – Supervisory Review Process and Pillar 3 - Market Discipline. However, given the scope of Pillar II and Pillar III and the possible impact to banks, CIMA will implement these on March, 2013.

9. Risk Management (continued)

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios of capital.

The Bank's actual capital amount and its risk asset ratio, pursuant to CIMA reporting schedules as well as CIMA's minimum requirements, are presented in the following table:

Statements of financial positions and off-balance sheet positions (Net of provisions)	*Base Amount US$000*	*Risk Weighted Assets US$000*
Credit Risk		
Cash items	34	-
Claims on Sovereigns	38,380	6,441
Claims on Non Central Government Public Sector Entities (PSEs)	4,486	1,486
Claims on Multilateral Development Banks (MDBs)	17,637	4,647
Claims on Banks and Security Firms	348,514	136,109
Claims on Corporates and Security Firms	464,300	464,860
Claims on Retail Portfolio	809,205	146,155
Claims secured on Higher Risk Categories & Other Assets	49,588	49,588
Total Balance Sheet items	**1,732,144**	**809,286**
Off-Balance sheets items	60,755	17,749
Counterparty Credit Risk	15,425	483
Securitizations	33,509	16,840
Total Credit Risk	**1,841,833**	**844,358**
Operational Risk		
Standardized Approach		**133,370**
Market Risk		**4,143**
Total Risk Weighted Assets		**981,871**
Capital Constituents		
Net Tier 1 and Net Tier 2 Capital		**164,884**
Capital Adecuacy Ratio as of December 31, 2012		**16.79%**
Capital Adecuacy Ratio as of December 31, 2011		19.36%
Minimum capital adequacy regulatory ratio		**12%**

The Bank does not apply market risk approach as result to designate all its balance positions as banking book.

9. Risk Management (continued)

The second phase of the CIMA Basel II implementation will be considered for implementation on March 2013. It will include considering the implementation of advanced approaches, specifically Pillar 1 – Credit Risk – Advanced Approaches (IRB), Operations Risk – Advanced Measurement Approaches (AMA) and Market Risk – Internal Risk Management Models.

10. Fair Value of Financial Instruments

Fair value is the amount at which a financial instrument could be realized in a current transaction between parties at arm's length, other than in a forced sale or liquidation, and is best evidenced by a quoted market price, should it exist.

For quoted investments, market prices are used to determine the fair value of such investments. The fair value of investment funds is determined by reference to the net asset values of the funds as provided by the respective administrators of such funds.

The following summary presents the methodologies and assumptions used to estimate the fair value of the Bank's financial instruments:

- *Cash and due from banks, interest bearing deposits with banks, federal funds sold and overnight placements.* The fair values of these financial assets are considered to approximate their respective carrying values due to their short-term nature.

- *Available-for-sale-securities.* The fair value of investments that are actively traded in organized financial markets is determined by reference to quoted market bid prices at close of business of the statements of financial position date. For investments where there is no active market, fair value is determined using valuation techniques. Such techniques include recent arm's length market transactions; reference to the current market value of another instrument which is substantially the same; discounted cash flow analysis or other valuation models.

- *Loans.* The fair value of the loan portfolio approximates its carrying value due to either the short-term nature of loans and/or the fact that the loan portfolio is composed mainly of cash collateral loans.

- *Deposits, purchased funds and other borrowed funds.* The fair value of these financial liabilities approximates their respective carrying values due to either their short-term nature and/or the fact that their interest rates are comparable to those available for liabilities with similar terms and conditions.

10. Fair Value of Financial Instruments (continued)

	2012		2011	
Assets	**Carrying Value US$000**	**Fair Value US$000**	Carrying Value US$000	Fair Value US$000
Cash and cash equivalents	**136,259**	**136,259**	77,001	77,001
Due from banks	**495**	**495**	2,693	2,693
Financial assets	**802,480**	**802,480**	811,631	811,631
Loans	**801,125**	**800,801**	606,112	606,073
Other assets	**28,112**	**28,112**	26,092	26,092
	1,768,471	**1,768,147**	1,523,529	1,523,490
Liabilities				
Deposits:				
Non-interest bearing	**464,998**	**464,998**	390,403	390,403
Interest bearing	**931,846**	**931,846**	930,244	930,244
Borrowed funds	**136,246**	**136,246**	-	-
Other liabilities	**15,596**	**15,596**	13,645	13,645
	1,548,686	**1,548,686**	1,334,292	1,334,292

11. Share Capital

The number of authorized, issued and outstanding ordinary shares of the Bank as of December 31, 2012 was 70,000,000 (2011 – 70,000,000) shares.

12. Commitments and Contingencies

The consolidated financial statements do not reflect various commitments and contingencies which arise in the normal course of business and which involve elements of credit and liquidity risk. Among them are commercial letters of credit, stand by letters of credit and guarantees plus commitments to purchase and sell securities. The commitments and contingencies consist of:

	December 31,	
	2012	2011
	US$ 000	US$ 000
Commercial letters of credit	**1,550**	1,550
Stand by letters of credit and guarantees	**30,877**	36,492

Commercial and stand-by letters of credit and guarantees include exposure to credit risk in the event of nonperformance by customers. Risks also arise from the possible nonperformance by the counterparty to the transactions.

12. Commitments and Contingencies (continued)

Since stand-by letters of credit and guarantees have fixed maturity dates and many of them expire without being drawn upon, they do not generally present a significant liquidity risk to the Bank.

Legal contingency

Madoff Trustee Litigation

On September 22, 2011, the Trustee for the liquidations of Bermard L. Madoff Investment Securities LLC (BLMIS), and the substantively consolidated state of Bermard L. Madoff ("the Madoff Trustee") filed a complaint against Credicorp's subsidiary Atlantic Security Bank (ASB) in U.S. Bankruptcy Court Southern District of New York, for an amount of approximately US$120 million ("the Complaint"), which corresponds to the funds that ASB managed in Atlantic US Blue Chip Fund and that were redeemed between the end of 2004 and the beginning of 2005 from Fairfield Sentry Limited in Liquidation (hereafter "Fairfield"), a feeder fund that invested in BLMIS.

The Complaint further alleges that the Madoff Trustee filed an adversary proceeding against Fairfield, seeking to avoid and recover the initial transfers of monies from BLMIS to Fairfield; that on June 7 and 10, 2011, the Bankruptcy Court approved a settlement among the Madoff Trustee, Fairfield and others; and that the Madoff Trustee is entitled to recover the sums sought from ASB as "subsequent transfers" of "avoided transfers" from BLMIS to Fairfield that Fairfield subsequently transferred to ASB. The Madoff Trustee has filed similar actions against other alleged "subsequent transferees" that invested in Fairfield and its sister entities which, in turn, invested and redeemed funds from BLMIS.

ASB counsel and the Trustee agreed that ASB has until April 24, 2013 to move, answer or otherwise respond to the Complaint.

Management believes that ASB has substantial defenses against the Madoff Trustee's claims alleged in the Complaint and intends to contest these claims vigorously. Management considers, among other substantial defenses, that the Complaint considers only the amounts withdrawn, without taking into account the amounts invested in Fairfield. Furthermore, ASB after redeeming said funds from Fairfield re-invested them in BLMIS, through another vehicle, that resulted in a net loss in the funds that ASB managed on behalf of its clients for approximately US$78 million as of December, 2008.

12. Commitments and Contingencies (continued)

Fairfield Liquidator Litigation

On April 13, 2012, Fairfield and its representative, Kenneth Krys (the "Fairfield Liquidator"), filed an adversary proceeding against ASB pursuant to Chapter 15 of the U.S. Bankruptcy Code, in the U.S Bankruptcy Court for the Southern District of New York, styled as Fairfield Sentry Limited (In Liquidation) v. Atlantic Security Bank, Adv. Pro. No. 12-01550 (BRL) (Bankr. S.D.N.Y.) ("Fairfield v. ASB Adversary Proceeding"). The complaint sought to recover the amount of approximately US$115 million, reflecting ASB's redemptions of certain investments in Fairfield, together with investment returns thereon. These are essentially the same moneys that Madoff Trustee seeks to recover in the Madoff Litigation described above.

Thereafter, the Fairfield v. ASB Adversary Proceeding was procedurally consolidated by the Bankruptcy Court with other adversary actions by the Fairfield Liquidator against former investors in Fairfield. Pursuant to that consolidation, and by stipulation of the parties, the Bankruptcy Court's previously entered stay of all proceedings in the Fairfield Liquidator adversary actions (except for the filing of amended complaints) in light of the pending litigation in the British Virgin Island courts calling into question the Fairfield Liquidator's ability to seek recovery of funds invested with and redeemed from Fairfield, was applied in the Fairfield v. ASB Adversary Proceeding, thereby indefinitely extending ASB's time to answer or move until the stay is lifted. On January 14, 2013, the Fairfield Liquidator filed an Amended Complaint in the Fairfield v. ASB Adversary Proceeding seeking the same amount of recovery as in the original complaint but adding additional allegations and causes of action. The Bankruptcy Court stay remains in effect, and ASB's time to answer or move remains stayed indefinitely pending further order of the Bankruptcy Court.

Management believes that ASB has substantial defenses against the Fairfield Liquidator's claims alleged in the Amended Complaint and intends to contest these claims vigorously.

13. Fiduciary Activities

The Bank provides custody, trustee, investment management and advisory services to third parties which involve the Bank in making allocation and purchase and sale decisions in relation to a wide range of financial instruments. Such assets as are held in a fiduciary capacity are not included on these consolidated financial statements. These services might give rise to the risk that the Bank might be accused of failing to fulfill fiduciary duties and responsibilities.

Assets managed on behalf of customers by the Bank comprised of investment securities and loans totaling US$3,961,373 in 2012 (2011 - US$3,193,560).

These assets include mutual funds with net assets of US$631,027 according to statements of net assets prepared by the funds' management at December 31, 2012 (2011 - US$580,549).

14. Concentration of Assets and Liabilities

At December 31, the geographic concentration of significant assets (cash and cash equivalents, interest–bearing deposits with banks and risk portfolio) and liabilities (deposits, purchased funds and other borrowed funds) is as follows:

	2012	
	Assets	**Liabilities**
	US$000	**US$000**
Latin America and the Caribbean	**1,073,508**	**1,389,523**
United States of America	**542,756**	**141,213**
Other countries	**124,096**	**2,354**
	1,740,360	**1,533,090**

	2011	
	Assets	Liabilities
	US$000	US$000
Latin America and the Caribbean	830,019	1,247,154
United States of America	577,602	1,823
Other countries	89,816	71,670
	1,497,437	1,320,647

15. Derivative Financial Instruments

The Bank uses the following derivative instruments for hedging and trading purposes. The table below shows the fair values of derivative financial instruments recorded as assets or liabilities, together with their notional amounts. The notional amount, is recorded as gross amount, is the amount of the derivative's underlying asset, referenced to rates or indexes and is the basis upon which changes in the value of derivatives are measured. The notional amount indicates the volume of transactions outstanding at year end and is indicative of neither the market risk nor the credit risk.

	2012			*2011*		
	Assets US$000	***Liabilities US$000***	***Notional Amount US$000***	*Assets US$000*	*Liabilities US$000*	*Notional Amount US$000*
Derivarives held for trading						
Forward foreign currency contracts - sale	**-**	**92**	**7,497**	-	393	17,928
Interes rate swaps	**153**	**337**	**4,541**	3	329	13,341
Futures	**26**	**-**	**8,400**	-	179	33,000
Credit default swaps	**229**	**146**	**28,316**	177	590	18,456
	408	**575**	**48,754**	180	1,491	82,725

15. Derivative Financial Instruments (continued)

For the year ended December 31, 2012, the Bank recognized a net gain of US$50 (2011: net loss US$4,456), representing the net loss in derivative financial instruments held for trading and economic hedging purposes.

As of December 31, 2012 and 2011, the Bank has positions in the following types of derivatives:

Swaps

An agreement between two parties (known as counterparties) where one stream of future interest payments is exchanged for another based on a specified principal amount. Interest rate swaps often exchange a fixed payment for a floating payment that is linked to an interest rate (most often the LIBOR). A company will typically use interest rate swaps to limit or manage exposure to fluctuations in interest rates, or to obtain a marginally lower interest rate than it would have been able to get without the swap.

Credit default swaps are contractual agreements between two parties to make payments with respect to defined credit events, based on specified notional amount. The Bank purchases and sells credit default swaps from and to counterparties in order to mitigate the risk of default by the counterparty on the underlying security referenced by the swap and for yield enhancement purposes.

Forwards and futures

Forward and futures contracts are contractual agreements to buy or sell a specified financial instrument at a specific price and date in the future. Forwards are customized contracts transacted in the over–the–counter market. Futures contracts are transacted in standardized amounts on regulated exchanges and are subject to daily cash margin requirements.

The main differences in the risk associated with forward and futures contracts are credit risk and liquidity risk. The Bank has credit exposure to the counterparties of forward contracts. The credit risk related to future contracts is considered minimal because the cash margin requirements of the exchange help ensure that these contracts are always honored.

Forward contracts are settled gross and are, therefore, considered to bear a higher liquidity risk than the futures contracts which are settled on a net basis. Both types of contracts result in market risk exposure.

15. Commitments and Contingencies (continued)

Short sale

Short selling is a mechanism that serves as leasing financial instruments to a third party to repurchase in a given period, winning, or losing the price difference between two dates. The goal is to sell the papers at the beginning of the operation and when the price drops, buy it cheaper. Short sales are primarily short-term transactions to take advantage of the fact that markets tend to experience declines in prices faster than increases in their prices.

Derivative financial instruments held or issued for trading purposes

Most of the Bank's derivative trading activities are related to its investment portfolio, in order to reduce its exposure to risk. These are normally contracted in the over-the-counter market. The Bank may also take positions with the expectation of profiting from favorable movements in prices, rates or indexes. Also, under this hedging are included any derivatives which do not meet IAS 39 hedging requirements.