CAF BANK LTD PILLAR 3 DISCLOSURE

30 April 2018

CAF Bank

Company number 1837656

CONTENTS

Overview

Purpose of this disclosure

This document is prepared in accordance with the Pillar 3 requirements which are set out under the Capital Requirements Directive and Regulation (CRD IV) and aim to promote market discipline through regulatory disclosure requirements. These requirements enable market participants to access key information relating to a bank's regulatory capital and risk exposures in order to increase transparency and confidence about a bank's exposure to risk and the overall adequacy of its regulatory capital.

General

CAF Bank Limited publishes its Pillar 3 Disclosure annually. This Pillar 3 report is based upon the Bank's financial statements for the year ended 30 April 2018 and is prepared on a solo basis.

CAF Bank Limited is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

This document should be read in conjunction with CAF Bank's annual report and financial statements for the corresponding financial year, which, together with other information, is available on the Bank's website www.cafonline.org/cafbankannualaccounts

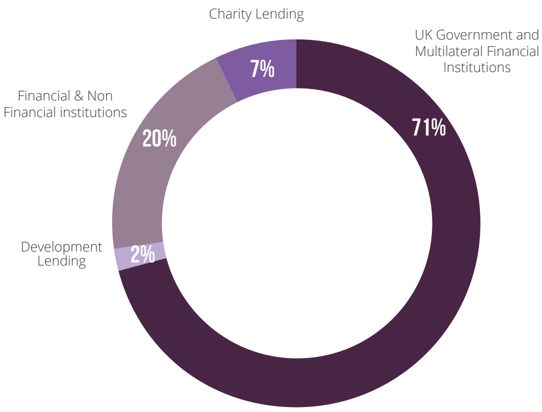
Principal activities

CAF Bank Limited provides banking services to charities, social purpose organisations and philanthropically minded individuals. The Bank offers transactional current and deposit accounts and loans and advances to UK customers. Customers have access to HSBC and RBS branches across England, Scotland and Wales.

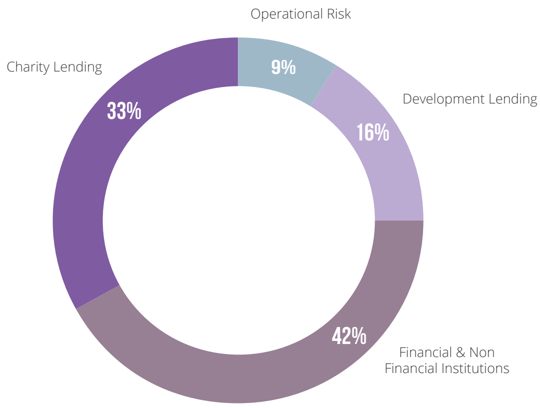
CAF Bank is a wholly owned subsidiary of the Charities Aid Foundation (CAF).

Capital and Exposures at 30th April 2018

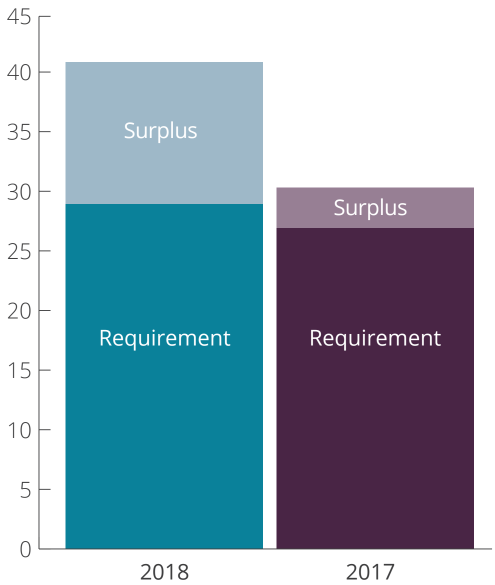
Exposures



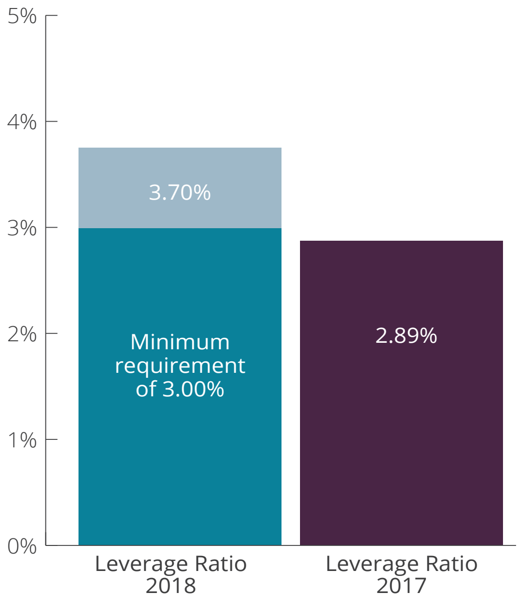
Risk Weighted Assets



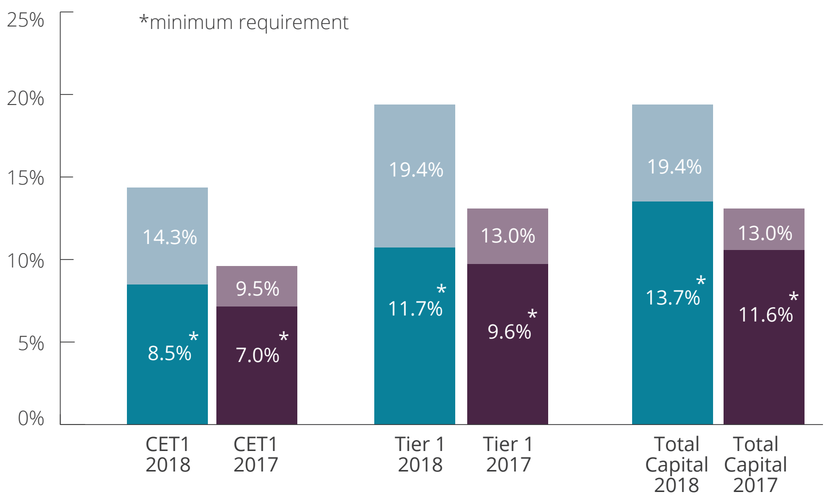
Capital Resources (£m)



Leverage Ratio



Capital Ratios



Capital resources

Capital management

CAF Bank aims to at all times to maintain an adequate level of capital to support the development of its business and to meet regulatory capital requirements.

Business and capital plans are drawn up annually covering a three year period and approved by the Board. The plans ensure that adequate levels of capital are maintained by the Bank to support its strategy. This is integrated with the Bank's annual planning process.

The capital plan takes the following into account:

- current and anticipated future regulatory capital requirements;
- increases in demand for capital due to business development, including planned lending growth;
- potential demand for capital from market shocks or stresses;
- available supply of capital and capital raising options;
- achieving a minimum required leverage ratio; and
- internal controls and governance for managing the Bank's risk, operations and capital.

The Bank undertakes a detailed capital adequacy assessment to support its capital requirements. Each material risk is assessed, relevant mitigants considered, and appropriate levels of capital determined. The capital adequacy assessment is a key part of the Bank's risk and planning framework and a minimum capital requirement is assessed and agreed with the PRA. The Bank's internal capital adequacy assessment is regularly updated under two Pillars.

Minimum capital requirement: Pillar 1

In calculating minimum capital requirements under Pillar 1, CAF Bank adopts the Standardised Approach to credit risk and Basic Indicator Approach to operational risk. The following table outlines the Bank's minimum capital requirement as at 30 April 2018.

Pillar 1 capital requirement	2018	2017
	£000	£000
Risk weighted assets	194,326	217,896
Operational Risk Add-on	18,311	16,370
Total Risk Exposure Amount	212,637	234,266
Total Pillar 1 capital requirement (8%)	**17,011**	**18,741**
Comprising:		
Credit Risk	15,546	17,431
Operational Risk	1,465	1,310
Total Pillar 1 capital requirement	**17,011**	**18,741**

An analysis of the credit risk capital requirement is shown in the table below:

Pillar 1 capital requirement: Credit Risk	2018	2017
	£000	£000
Central government and Multilateral Development Banks	-	-
Financial institutions	5,679	8,696
Corporates	1,489	2,031
Loans to charities	6,102	4,700
Loans to personal customers	2,699	2,527
Other items (debtors and prepayments)	62	9
SME deduction	(485)	(532)
Total Pillar 1 capital requirement: Credit Risk	15,546	17,431

Minimum capital requirement: Pillar 2

Pillar 2 is designed to assess the adequacy of a firm's capital resources by considering all material risks to the business, including those not covered or adequately addressed by Pillar 1, taking into account the impact of stress tests conducted across a variety of different scenarios which the Bank may be exposed to. Requirements under Pillar 2 encourage firms to develop, operate and evolve better risk management techniques for monitoring, measuring and managing material risks.

CAF Bank has assessed its risks and allocated capital over and above that required for Pillar 1 for the risks shown in the following table. Each risk type is described in the Principal Risks section.

Pillar 2A

Risk type	2018 Capital addition		2017 Capital addition	
	£000	%	£000	%
Market and interest rate risk	1,361	0.6%	1,874	0.8%
Operational risk	2,254	1.1%	2,343	1.0%
Concentration Risk	4,465	2.1%	1,171	0.5%
Total	8,080	3.8%	5,388	2.3%

The amounts identified above relating to Pillar 2A capital represent additional capital equivalent to 3.8% of Total Risk Exposure Amount (CAF Bank's 'ICG').

Pillar 2B

CAF Bank assesses an additional amount of capital as a buffer ('Pillar 2B') against risks it may become exposed to over the forward looking planning horizon. Such risks include a downgrade in credit ratings of wholesale counterparties, bail in losses affecting counterparties, loan losses and an increase in market interest rates. Following implementation of CRR, CAF Bank is progressively introducing Capital Conservation and Countercyclical buffers.

Capital Conservation Buffer rates are set in the CRR.

The Countercyclical Capital Buffer is a weighted average of the buffer rates applicable to the jurisdictions in which CAF Bank is invested. CAF Bank monitors the buffer rates published by the Bank of England. The Countercyclical Capital Buffer requirement at 30 April 2018 is 0% of Total Risk Exposure Amount.

Pillar 2B Capital Requirement (as % of Total Risk Exposure Amount)	
Capital Conservation Buffer	1.9%
Countercyclical Capital Buffer	0.0%

Total capital requirements

Following implementation of CRR, the above minimum capital requirements are aggregated and expressed as a percentage of the Bank's Total Risk Exposure Amount.

CRR places greater emphasis on the highest quality of capital (known as Common Equity Tier 1) and strengthens the criteria used to determine what can be used as CET1.

Minimum capital requirement (% of Total Risk Exposure Amount)					2018
	CRD IV minimum requirement	Pillar 2A	Capital Conservation Buffer	Countercyclical Buffer	Minimum Requirement
Common Equity Tier 1 (CET1)	4.5%	2.1%	1.9%	0.0%	8.5%
Tier 1 (CET1 + Additional Tier 1)	6.0%	3.8%	1.9%	0.0%	11.7%
Total Capital (Tier 1 + Tier 2)	8.0%	3.8%	1.9%	0.0%	13.7%
	£000	£000	£000	£000	£000
Common Equity Tier 1 (CET1)	9,569	4,525	3,987	-	18,081
Tier 1 (CET1 + Additional Tier 1)	12,758	8,080	3,987	-	24,825
Total Capital (Tier 1 + Tier 2)	17,011	8,080	3,987	-	29,078

Capital resources

The Bank's capital resources and Total Risk Exposure Amounts are shown in the following table. The main features and terms of the various components of the capital resources are described in the Capital Instruments section.

CAF Bank's capital position has been strengthened during 2017/18 following investment by CAF of a further £8m in Ordinary Share Capital and £3m in Additional Tier 1 capital ('AT1').

	2018		2017	
	£000	% of Total Risk Exposure	£000	% of Total Risk Exposure
Common Equity Tier 1 Capital				
Called up ordinary share capital	29,350		21,350	
Qualifying distributable reserves	1,000		1,000	
Common Equity Tier 1 Capital	30,350	14.3%	22,350	9.5%
Other Tier 1 Capital				
Additional Tier 1 capital	11,000		8,000	
Total Tier 1 Capital	41,350	19.4%	30,350	13.0%
Total Capital resources	41,350	19.4%	30,350	13.0%
Total Risk Exposure Amount	212,637	100.0%	234,266	100.0%
Risk weighted assets	194,326		217,896	
Operational Risk Add-on	18,311		16,370	
Total Risk Exposure Amount	212,637		234,266	

Total capital position

CAF Bank's capital resources and total capital requirement outlined above are summarised in the table below.

Capital Surplus	2018		2017	
	%	£000	%	£000
Total Capital Resources				
CET1	14.3%	30,350	9.5%	22,350
Total T1	19.4%	41,350	13.0%	30,350
Total capital	19.4%	41,350	13.0%	30,350
Total Capital Requirement				
CET1	8.5%	18,081	7.0%	16,488
Total T1	11.7%	24,825	9.6%	22,372
Total capital	13.7%	29,078	11.6%	27,058
Capital Surplus				
CET1	5.8%	12,269	2.5%	5,862
Total T1	7.8%	16,525	3.4%	7,978
Total capital	5.8%	12,272	1.4%	3,292

Leverage ratio

CRR requires firms to calculate a non-risk adjusted Leverage Ratio, to supplement risk-based capital requirements. The Leverage Ratio measures the relationship between the capital resources of the firm and its total assets. The purpose is to constrain the build up of excessive leverage.

Leverage is calculated as Tier 1 capital divided by total on and off balance sheet assets adjusted for deductions.

A transition period was established from January 2013 to December 2017 during which firms monitored their leverage against a minimum ratio of 3%. The following table outlines the Bank's leverage ratio as at 30 April 2018.

CAF Bank Leverage Ratio	2018	2017
End-point	3.7%	2.9%

Capital instruments issued by CAF Bank

Tier 1 capital

CAF Bank's Tier 1 capital is further comprised of CET1 capital (ordinary share capital and distributable reserves) and Other Tier 1 capital (Additional Tier 1 capital).

CET1 capital

Description	Terms	2018	2017
		£000	£000
Tier 1 capital			
Ordinary shares	Permanent	29,350	21,350
Distributable reserves		1,000	1,000
Total		30,350	22,350

CAF Bank issued a further £8m of Ordinary share capital to CAF in January 2018.

Ordinary share capital is fully paid-up with the proceeds of issue immediately and fully available. There is no obligation to pay a dividend. The capital is available for unrestricted and immediate use to cover risks and losses, and enable the organisation to continue trading.

Other T1 capital

Description	Coupon	Terms	2018	2017
			£000	£000
Tier 1 capital				
Additional tier 1	9.0%	Perpetual, non-cumulative	11,000	8,000
Total			11,000	8,000

CAF Bank issued a further £3m of Additional Tier 1 capital to CAF in January 2018. The principal terms of the capital are as follows:

- Perpetual, repayable at CAF Bank's election after 5 years with the prior consent of the PRA;
- Non-cumulative 9% per annum coupon, cancellable at the discretion of the CAF Bank Board;
- Irrevocable conversion to voting ordinary shares either at a trigger level of 7% Common Equity Tier 1 capital, or at such time as the CAF Bank Board considers it reasonably foreseeable that a trigger event will occur; and
- In the event of conversion, £1 par value of AT1 capital will convert to £1 nominal value of ordinary share capital, such ordinary shares being identical to existing ordinary shares in all respects.

Governance

Governance Structure

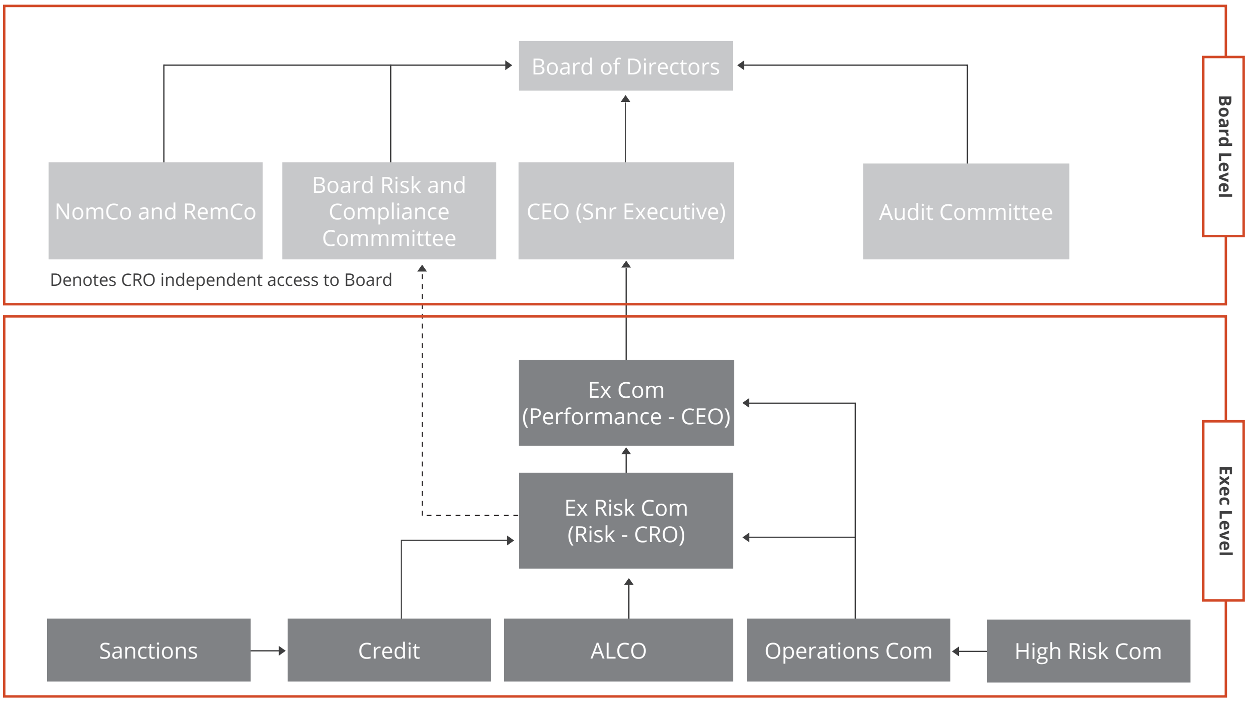
The Board exercises its accountabilities through its own activities and through delegation of responsibilities to the CEO and his Executive Committee. The Board receives reports from the CEO and reviews the work of the Executive Committee.

In addition, the Board has established three sub-committees to assist it in monitoring the business, reviewing policies, systems, and controls, and consideration and setting of risk appetite.

These are:

i Board Risk and Compliance Committee;
ii. Audit Committee; and
iii. Nominations and Remuneration Committee.

Each sub-committee is subject to its own terms of reference and has authority to review relevant policies (in line with the Policy Approval Protocol), systems, controls and reporting, making recommendations to the Board for approval.



Board composition

The Board consists of ten non-executive directors and two executive directors at 30 April 2018.

None of the Directors have interests in the shares of the Bank or any associated undertaking or trust.

The CAF Bank Board is responsible for:

a) development of the firm's strategy, operating plans and budgets, monitoring MI and providing challenge to the senior management against performance;
b) defining the Bank's risk appetite and implementing and maintaining policies to provide an effective and appropriate governance and control structure for managing the business;
c) setting an appropriate 'tone from the top' and ensuring alignment of values and behaviours in the Bank relating to the conduct of its business;
d) overseeing, monitoring and challenging the current and future operating activities of the Bank;
e) overseeing the conduct of business to ensure that systems, procedures and internal controls are adequate to ensure compliance with applicable regulations and regulatory limits/ ratios;
f) monitoring and managing sensitive matters such as reputational risk and brand issues;
g) reviewing, challenging and approving annually the capital funding (ICAAP) and liquidity (ILAAP) policies and assessments and approving the gifting of annual profits to its parent, the Charities Aid Foundation;
h) reviewing, challenging and approving annually the Recovery and Resolution Plan;
i) approving the composition, membership and terms of reference of Board sub-committees;
j) reviewing reports from Board sub-committees taking action as appropriate;
k) reviewing and approving where appropriate the recommendations from Board sub-committees; and
l) reviewing regulatory correspondence from the PRA and FCA and ensuring management take appropriate action on regulatory matters affecting the firm.

The Board Risk and Compliance Committee (BRCC)

The Board Risk Committee is chaired by a Non-Executive Director and comprises three other Non-Executive Directors. The main responsibilities of the Committee include ensuring:

- The development and maintenance of the Bank's risk management framework;
- Ensuring the Bank's strategy, principles, policies and resources are aligned to the Bank's risk appetite, as well as to regulatory and industry best practices;
- Compliance with legislation, regulation and internal policy; and
- Reviewing policies and recommending these to the Board.

The Board Audit Committee

The Audit Committee is chaired by a Non-Executive Director and comprises two other Non-Executive Directors. The responsibilities of the Committee include:

- Monitoring the integrity of the annual published report and accounts and Pillar 3 disclosures;
- Reviewing reports from the Bank's External Auditors including their audit plan, and monitoring the effectiveness of the external audit;
- Reviewing the Bank's internal control and risk management systems;
- Setting the annual audit plan and considering the work of Internal Audit, and monitoring, reviewing and challenging the effectiveness of the Bank's Internal Audit function, which is outsourced; and
- The Chair of the Committee also oversees the adoption of whistleblowing across the Bank.

The Nominations and Remuneration Committee

The Nominations and Remuneration Committee, comprising the Chair, CAF Chief Executive and CAF Bank CEO is responsible for:

- Reviewing the Board's effectiveness, Board nominations and retirements;
- Monitoring conflicts of interest;
- Succession planning; and
- Remuneration policy and practice.

The Executive Committee

The purpose of the Executive Committee is to assist the CEO in the performance of their duties, including:

- Cascading the 'culture and tone' set by the Board in relation to the conduct of the Bank's business;
- Development and implementation of strategy, operational plans, policies, procedures and budgets;
- Monitoring of operating and financial performance;
- Prioritisation and allocation of resource and monitoring competitive forces in each area of operation; and
- Reviewing the Bank's conduct of business to ensure products and processes are effective and compliant with applicable regulation.

Executive Risk Committee

The purpose of Executive Risk Committee is to enable the Chief Risk Officer to discharge their duties, under delegated authorities, including:

- The development, implementation and maintenance of the Bank's overall risk management framework and adherence to risk appetite metrics and statements;
- Ensuring the identification, assessment and control of principal risks;
- Act as the senior risk committee receiving reports from, and point of escalation for, the Asset and Liability Committee, Credit Committee and Operations Committee;
- Monitoring the Compliance function to ensure compliance with legislation, regulation and internal policy; and
- Establishing and maintaining appropriate policies.

The Credit Committee

The purpose of the Credit Committee is to provide oversight of the Bank's credit activities:

- Monitoring portfolio performance against approved policies and limits;
- Reviewing policies and recommending changes to the Executive Risk Committee;
- Reviewing credit reports covering each specific business line; and
- Reviewing the quality of new lending, credit performance, arrears and non-performing loans and review the detailed composition of the credit portfolios.

The Sanctions Committee

The purpose of the Sanctions Committee is to:

- Approve or decline applications for credit from customers based on customers' creditworthiness in line with appetite, policy and approval levels.

The Asset and Liability Committee (ALCo)

The purpose of ALCo is to:

- Oversee the Bank's liquidity, funding and market risks, treasury, regulatory and capital requirement within the risk appetite set by the Board;
- Develop the Bank's forward looking asset and liability strategy;
- Review policies and recommend these to the Executive Risk Committee;
- Oversee, review and make recommendations on the Bank's ILAAP and ICAAP documents which are then presented to Executive Risk Committee for review;
- Monitor the financial risks faced by the Bank including counterparty placements and investments; and
- Develop and review product pricing.

Operations Committee

The purpose of the Operations Committee is to:

- Review the level of customer service delivered through analysis of management information relating to service level agreements and complaints;
- Seek continued operational improvements and efficiencies;
- Review outsourcing arrangements, ensuring compliance with outsourcing policy; and
- Review systems and controls and in particular operational risk controls and new or emerging risks, ensuring these are appropriate and escalate significant issues.

Risk management

Risk Management Framework

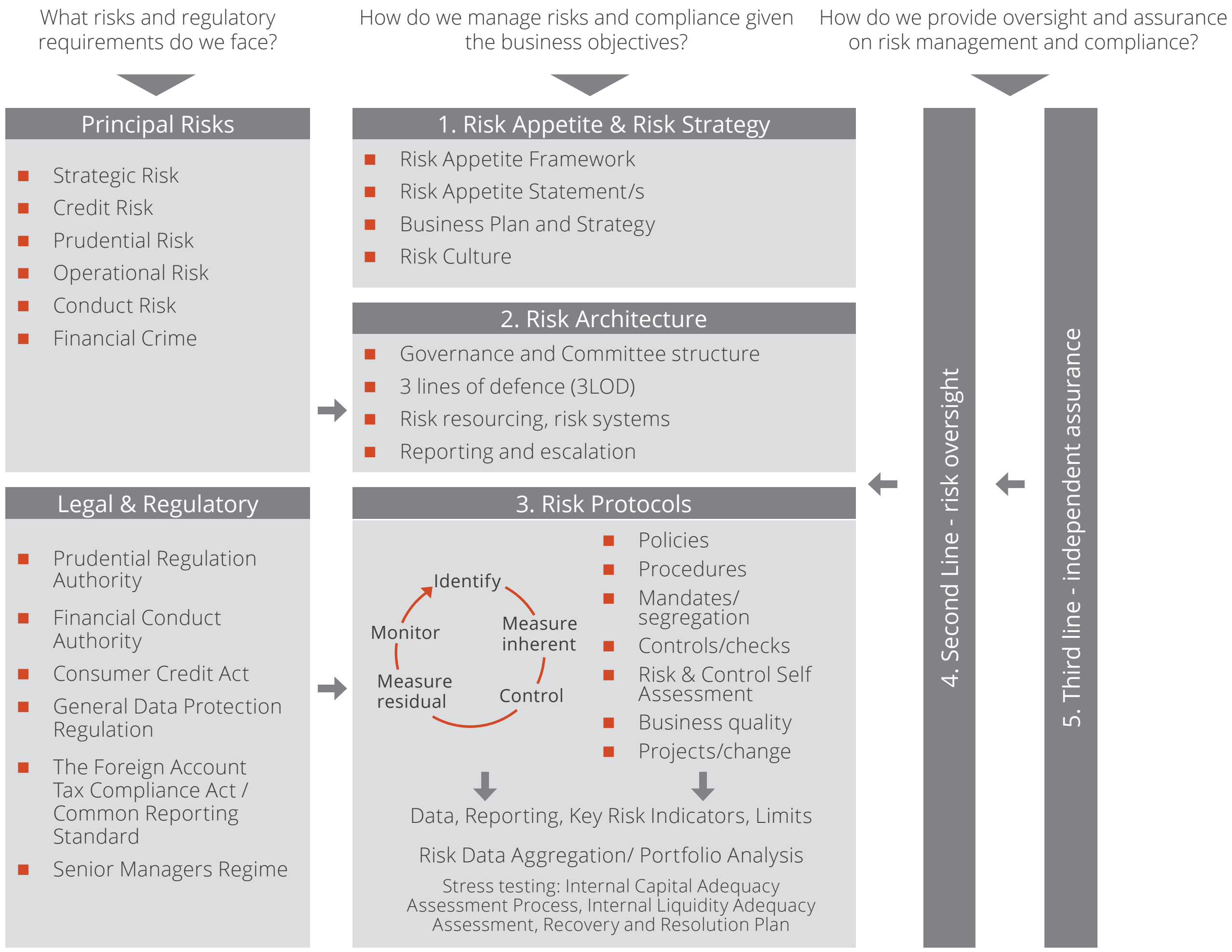
The Risk Management Framework (RMF) outlines the means by which the Board and senior management establish and implement the strategy of the Bank in relation to its risk appetite. This is the process of identification, assessment, measurement, control and monitoring of risks to which the Bank is exposed. The RMF explains how the Bank adheres to the monitoring of its risk appetite as well as the policies, procedures, governance, systems and tools that it uses to enable effective risk management at the Bank.

The RMF is reviewed and approved by the Board annually following recommendation by the Board Risk and Compliance Committee. The CEO and the Chief Risk Officer ensure that business objectives and practices are fully aligned with the RMF.

The senior executives and managers of the Bank ensure that the RMF is embedded in its day-to-day management and control activities, with a clear separation between First Line of Defence (1LOD) and Second Line of defence (2LOD) activities. The RMF is subject to assurance reviews undertaken by Internal Audit and these are made available to external stakeholders as and when required.

The RMF is supported by detailed policies and procedures. These combine to ensure that risks are managed in a manner which is consistent with the size and nature of the Bank's operations, are aligned to regulatory requirements and reflect industry best practice, as reflected below:

Risk Management Framework



The RMF includes the three lines of defence model which ensures a clear delineation of responsibilities between control over day to day operations, risk oversight and control and independent assurance of the Bank's activities.

This model provides clarity for individuals and functions about their role, where responsibilities and accountabilities lie and is a core component of the RMF. The emphasis on the responsibilities of each line of defence is as follows:

First line of defence – Business lines and centralised functions

- To run the business in a safe but profitable manner to enable sustainability – within the Risk Appetite Framework and Statements;
- To identify, measure, control and monitor risks within each area of the business, and to report and escalate issues as necessary and to evidence control;
- To implement and adhere to the mandates, policies and processes of the Bank;
- To identify and assess new or emerging risks as internal activities or the external environment changes.

Second line of defence – Oversight functions (Risk, Compliance and Anti-Money Laundering)

- To support a structured approach to risk management by implementing and maintaining a RMF and Bank-wide risk policies, and to monitor their proper execution in the 1LOD;
- To provide independent oversight and guidance on risks relevant to the Bank's strategy and activities;
- Maintain an aggregate view of risk and monitoring performance in relation to the Bank's risk appetite;
- Monitoring changes in and compliance with to external regulation, and promoting best practices.

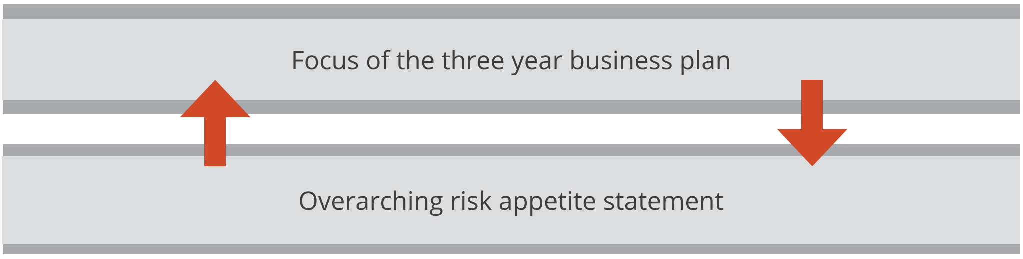
Third line of defence - Internal Audit (the Internal Audit function is outsourced to Mazars LLP)

- To provide independent assurance to the Board via the Audit Committee that the 1LOD and 2LOD are operating effectively in discharging their responsibilities.

Central to the Risk Governance and to the Three Lines of Defence model is the Chief Risk Officer (CRO). The Bank has appointed a CRO (approved by the PRA and FCA) to be responsible to the Board for oversight of bank-wide risk management. The CRO is independent of the 1LOD and has unfettered access to the Board (usually through the Chair of the BRCC); and on a day to day basis reports to the CEO.

Risk appetite statement

In articulating its risk appetite, the Bank has taken into consideration the expectations of its stakeholders; the need for regulatory compliance at all times; the preservation of its franchise and reputation and its desire for controlled and sustainable profits, in line with its values. An overarching Risk Appetite Statement (RAS) governs the Bank's approach to the risks it is willing to assume in support of its Business Plan. Accordingly, the overarching Risk Appetite Statement is aligned to the Business Plan and Strategy:



CAF Bank, a bank owned by a charity is developing a more robust business model that seeks to maintain an appropriate balance between its mission to support charities and providing a return to CAF in a low interest environment.

The Bank will take appropriate but controlled risk to support income and lending book growth, to remain sustainable, whilst remaining the safe, trusted and ethical bank of choice that is "helping charities make a better society".

The Bank's principal risks are credit risk, capital risk, liquidity risk, market and interest rate risk, operational risk, financial crime risk and conduct risk. Identifying and monitoring current and emerging risks is integral to our approach to risk management.

Strategic Risk

Strategic risk is the risk that can affect the Bank's ability to achieve its strategic and business objectives. From a strategic perspective, CAF Bank was established to further the charitable mission of its parent, the Charities Aid Foundation as well as provide a financial return on CAF's investment in the Bank. The Bank is continuing to diversifying from being entirely reliant on wholesale treasury income into lending and growing fee income.

Credit Risk

Credit risk is the risk of financial loss arising from a borrower or counterparty failing to meet their financial obligations to the Bank to repay in accordance with agreed terms. Credit risk arises primarily from investing funds with wholesale counterparties and lending to charities and personal customers.

Wholesale assets

Wholesale counterparties are reviewed and approved by the Asset and Liability Committee (ALCo) in accordance with policies and criteria approved by the Board. The Bank sets criteria which include credit rating, counterparty lending limits, group exposures, and country exposure limits. New investments with financial and non-financial institutions should not exceed £10m and £5m respectively.

The Bank uses the Standardised Approach to assess capital required for credit risk, with risk weightings based on the lower of the two highest of Fitch, S&P and Moody's ratings in accordance with the credit quality assessment scale.

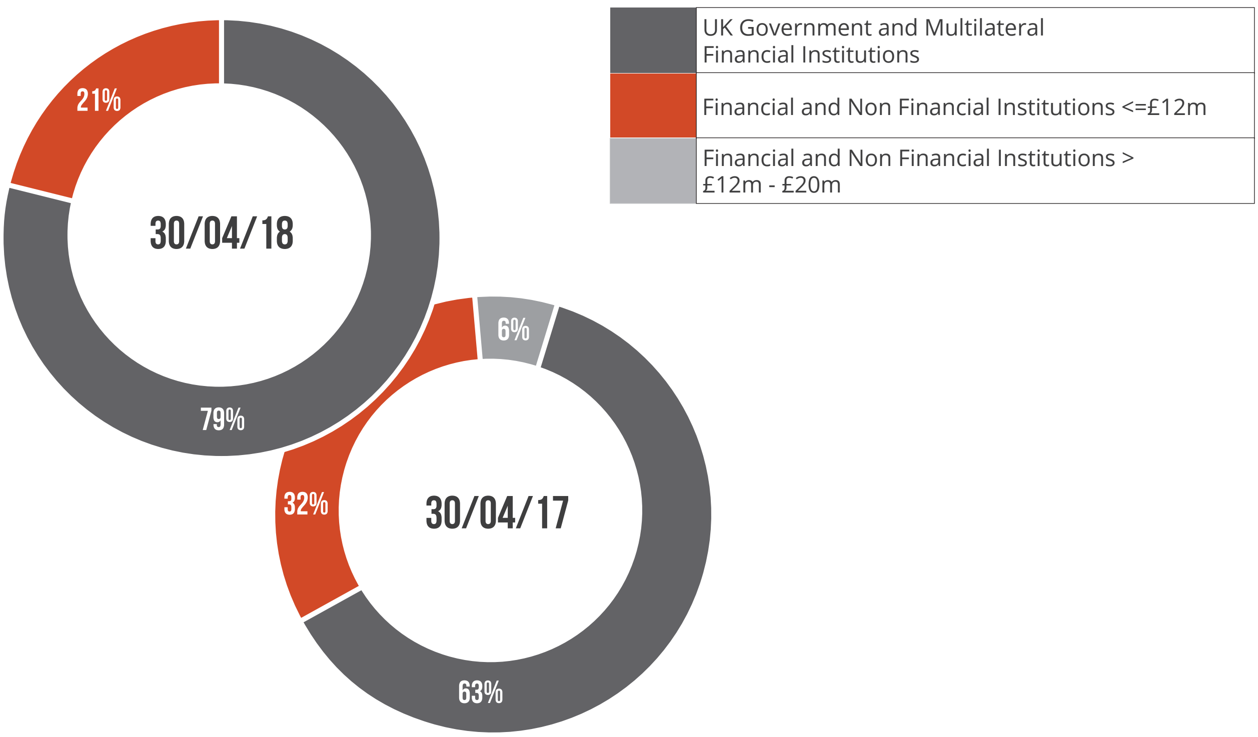
Treasury assets by class

	2018		2017	
	Book Value £000	**Market Value £000**	**Book Value £000**	**Market Value £000**
Listed:				
UK government	25,171	25,266	26,364	26,799
Multilateral financial institutions	350,934	349,560	368,604	370,396
Fixed coupon corporate bonds	98,865	99,035	145,252	146,739
Floating rate corporate bonds	97,538	98,072	174,526	175,355
	572,508	571,933	714,746	719,289
Unlisted:				
Certificates of deposit	10,000	10,111	20,000	20,225
Debt securities	582,508	582,044	734,746	739,514
Balances at Bank of England	415,346	415,346	203,278	203,278
Loans and advances to banks	12,268	12,268	22,341	22,341
	1,010,122	1,009,658	960,365	965,133

Treasury assets by credit rating

	2018		2017	
Category (Fitch equivalent lowest credit rating)	**Book Value £000**	**% of Book %**	**Book Value £000**	**% of Book %**
UK Government	440,517	43.61%	229,642	23.91%
AAA	322,874	31.96%	358,050	37.28%
AA+	40,608	4.02%	32,395	3.37%
AA	4,577	0.45%	9,620	1.00%
AA -	32,037	3.17%	104,393	10.87%
A+	20,073	1.99%	38,056	3.96%
A	114,803	11.37%	113,849	11.85%
A-	26,319	2.61%	51,666	5.38%
BBB+	4,378	0.43%	12,173	1.27%
BBB	3,936	0.39%	10,521	1.10%
	1,010,122	100.00%	960,365	100.00%

Treasury assets by exposure value



Lending

CAF Bank has in place a system of limits and controls to manage credit risk on its loan portfolio. Loan applications are reviewed by a credit assessment team and presented for approval to the Sanctions Committee, a sub-committee of the Credit Committee, in accordance with policies and criteria approved by the Board. Lending is secured on property and subject to maximum limits on loan to value ratios.

The policies include maximum exposure values and limits to manage concentration risk by sector. Exposure to geographical area is monitored. At 30 April 2018, the largest loan was £4.69m (2016/17: £5m). The maximum aggregate exposures to any one sector and geographical area were 46% and 26% respectively (2016/17 34% and 36% respectively).

Loans, overdrafts and BACS facilities are subject to regular monitoring of loan performance and individual annual review. Administration of the loan book is outsourced to Link Mortgage Services Ltd who provide regular management information on a loan by loan and aggregated basis. A provision of £641k has been made at 30 April 2018 reflecting losses that have been incurred but not yet identified (2016/17: £522k). No overdrafts were written off during the year (2016/17: £5k). No loans were in arrears at 30 April 2018 (2016/17: one).

	2018	**2017**
	£000	£000
Gross loans and advances to customers	92,866	72,916
Undrawn overdraft and loan commitments	12,359	14,285
	105,225	87,201
Amounts included within the above:		
Secured on property	103,812	86,173
Unsecured:		
Loans	148	255
Overdrafts	1,265	773
	105,225	87,201

As at 30 April 2018 the average loan to value ratio across the lending portfolio was 45%.

Liquidity and Funding Risk

Liquidity risk is the risk that the Bank does not have sufficient financial resources to meet its obligations as they fall due, or can secure them only at excessive cost. Liquidity risk arises from mismatches in the timing of cash flows. Funding risk arises when the liquidity needed to fund illiquid asset positions cannot be obtained at the expected terms and when required.

Liquidity and Funding risk is measured, monitored and reported daily and against intra-day triggers and limits approved by the Board within the Bank's Liquidity Policy. The liquidity position is monitored by ALCo and the Executive Risk Committee. The Bank undertakes regular stress testing of its liquidity position and behavioural analysis of its liabilities and assets.

CAF Bank holds liquidity buffer eligible assets of £781m (2016/17: £598m). Liquidity buffer assets comprise investments in the Bank of England Reserve Account, UK Gilts, Treasury Bills and multilateral development banks:

	2018 Book Value	**2017 Book Value**
	£000	£000
Balances at Bank of England	415,346	203,278
UK government	25,171	26,364
Multilateral financial institutions	340,750	368,604
	781,267	598,246

Market and Interest Rate Risk

Market and interest rate risk is the risk from adverse movements in external markets, e.g. interest rate movements, changes in investment values or currency movements that will reduce our income or the value of our assets. This includes interest rate risk in our banking book (IRRBB) which is the risk arising from a mismatch between the duration of assets and liabilities.

CAF Bank does not undertake proprietary trading activities. Investments are held to maturity and valued at cost with any premium or discount amortised over the remaining term. All the Bank's assets and liabilities are denominated in sterling.

Market and interest rate risk is measured by monitoring mismatches between assets and liabilities assessed on a behavioural basis which may result from movements in market interest rates over a specified time period within Board approved limits. IRRBB is measured weekly and monitoring is carried out by ALCo and the Board Risk and Compliance Committee.

Non-maturity (on-demand) deposits are behaviourally adjusted as follows:

£0 - £249,999	2 - 3 years
£250,000 - £999,999	1 - 2 years
Over £1m	6 - 12 months

Assets and liabilities analysed by interest rate pricing time periods:

As at 30 April 2018	Next day £000	Up to 3 months £000	3 months to 6 months £000	6 months to 1 year £000	1 year to 5 years £000	Over 5 years £000	Other items £000	Total £000
Assets								
Balances at Bank of England	414,756	590	-	-	-	-	-	415,346
Loans and advances to banks	4,268	8,000	-	-	-	-	-	12,268
Loans and advances to customers	91,425	-	-	-	-	-	-	91,425
Debt securities	-	150,329	15,721	127,126	288,835	-	497	582,508
Prepayments and accrued income	-	240	-	-	-	-	4,469	4,709
	510,449	159,159	15,721	127,126	288,835	-	**4,966**	**1,106,256**
Liabilities								
Customer accounts	600,581	-	-	47,058	387,766	-	14,021	1,049,426
Repurchase agreements	10,142	-	-	-	-	-	-	10,142
Other liabilities	-	-	-	-	-	-	5,288	5,288
Accruals and deferred income	-	-	-	-	-	-	50	50
Shareholders' funds	-	-	-	-	-	-	41,350	41,350
	610,723	-	-	47,058	387,766	-	60,709	1,106,256
Interest rate sensitivity gap	(100,274)	159,159	15,721	80,068	(98,931)	-	(55,743)	-
Impact of 2% change in interest rates	-	(155)	(115)	(1,169)	1,376	-	-	(63)

As at 30 April 2017	Next day £000	Up to 3 months £000	3 months to 6 months £000	6 months to 1 year £000	1 year to 5 years £000	Over 5 years £000	Other items £000	Total £000
Assets								
Balances at Bank of England	202,751	527	-	-	-	-	-	203,278
Loans and advances to banks	4,341	10,000	-	5,000	3,000	-	-	22,341
Loans and advances to customers	71,705	-	-	-	-	-	-	71,705
Debt securities	-	215,565	88,064	142,448	288,669	-	-	734,746
Prepayments and accrued income	-	-	-	-	-	-	7,715	7,715
	278,797	226,092	88,064	147,448	291,669	-	**7,715**	**1,039,785**
Liabilities								
Customer accounts	582,092	-	-	42,837	368,409	-	10,295	1,003,633
Repurchase agreements	-	-	-	-	-	-	-	-
Other liabilities	-	-	-	-	-	-	5,676	5,676
Accruals and deferred income	-	-	-	-	-	-	126	126
Shareholders' funds	-	-	-	-	-	-	30,350	30,350
	582,092	-	-	42,837	368,409	-	46,447	1,039,785
Interest rate sensitivity gap	(303,295)	226,092	88,064	104,611	(76,740)	-	(38,732)	-
Impact of 2% change in interest rates	-	184	(652)	(1,538)	3,108	-	-	1,102

Operational Risk

Operational risk is the risk of financial loss and or reputational damage resulting from inadequate or failed internal processes, people and systems or from external events.

The Bank continues to develop systems and controls to reduce the likelihood of failure associated with operational risks. The reporting of the Bank's operational risk profile continues to be enhanced. This highlights key areas of concern, enabling increased focus.

During the year ended 30 April 2018 operational losses totalled £37k (2016/17: £31k).

Cyber threats are escalating from an increasingly sophisticated criminal community. We have and continue to invest in strengthening defences.

CAF Bank has also enhanced the level of 'know your customer' reviews undertaken in line with industry practice.

The Bank is developing its Operational Resilience to protect the Bank against internal and external events that can disrupt service to our customers.

CAF Bank uses the Basic Indicator Approach to assess operational risk capital requirements.

Financial Crime

The Bank defines "Financial crime" to include any offence involving fraud or dishonesty, or handling the proceeds of crime. We seek to protect our customers and the Bank from the risks of financial crime by identifying inherent risks and operating only with appropriate systems and controls to detect and prevent harm. We will not conduct business with individuals or entities we believe are engaged in illicit behaviour. We seek to minimise the Bank's and our customers' exposure to loss from fraud.

CAF Bank complies with all relevant laws and regulation taking into account supervisory and approved industry guidance. Work to prevent fraud, money laundering, terrorist financing, breach of sanctions, tax evasion and bribery/corruption is led by the Bank's CEO with the support of dedicated Know Your Customer and Fraud Prevention teams. Oversight is provided by the Money Laundering Reporting Officer and Chief Risk Officer.

Bank losses to fraud in the year ended 30 April 2018 were £30k (2016/17: £13k).

Capital Risk

Capital risk is the risk that the Bank has insufficient capital to cover stressed conditions, regulatory requirements or growth plans.

An overriding principle is that the Bank operates at all times at levels that are above regulatory minima. The Board views that a strong capital position aids the long term strategy of controlled growth.

Conduct Risk

Conduct Risk is the risk of delivering unfair customer outcomes that may cause customer detriment, reputational damage and/or undermining the integrity of the market through the Bank's actions, behaviour, inappropriate culture and/or the conduct of business. Conduct risk is managed through behaviours and customer centric decisions, to deliver appropriate customer outcomes through the Bank's products and services.

Remuneration

CAF Bank is subject to the Remuneration Code (the Code). The aim of the Code is to ensure that all firms within scope have risk focused remuneration policies that are consistent with and promote effective risk management and do not expose them to excessive risk. The Bank's policies and procedures, covering salaries, bonuses and pension arrangements, comply with the requirements of the Code.

Remuneration Code Staff (Code Staff) are "employees whose professional activities have a material impact on the firm's risk profile, including any employee who is deemed to have a material impact on the firm's risk profile in accordance with Regulation (EU) 604/2014 of 4 March 2014 (Regulatory technical standards to identify staff who are material risk takers)".

The Bank has no 'risk takers' or staff engaged in control or significant influence functions that are not among its senior management. Total aggregate fixed remuneration of the Bank's five Code Staff for 2017/18 is £582k. Amounts of variable remuneration are not material.

Remuneration is overseen by the Nominations and Remuneration Committee, which determines the remuneration and employment policies and practice. Non-Executive Directors are not remunerated.

As a bank, we offer an ethical and fair approach to doing business, and support our customers to deliver social impact and achieve a fairer society. The total remuneration paid to 96 staff assigned wholly to CAF Bank in the financial year 2017/18 was £3,487k. In line with our core principles, bonuses do not amount to a significant element of total compensation. Bonuses are paid as a one-off lump sum through the parent company's payroll scheme and are non-pensionable. No other bonus or one-off payments are made. Staff are invited to join CAF's contributory pension scheme.

Cautionary note on forward-looking statements

This document may contain certain forward-looking statements with respect to the financial condition, results of operations and business of CAF Bank Ltd. Generally, words such as 'may', 'could', 'will', 'expect', 'intend', 'estimate', 'anticipate', 'believe', 'plan', 'seek', 'continue', 'project', 'should', 'probability', 'risk', 'value-at-risk', 'target', 'goal', 'objective', 'endeavour', 'outlook', 'optimistic' and 'prospects' or similar expressions or variations on such expressions identify forward-looking statements.

Any forward-looking statement represents the Bank's current expectations or beliefs, as well as assumptions about future expectations or beliefs concerning future events, and involves known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. There are several factors which could cause actual results to differ materially from those expressed or implied in forward looking statements. Among the factors that could cause actual results to differ materially from those described in the forward looking statements are: changes in the global, political, economic, business, competitive, market and regulatory forces, future exchange and interest rates, changes in tax rates and future business combinations or dispositions.

For further risks and uncertainties faced by the Bank that may impact the statements set out in this document, please read the Bank's Annual Report and Accounts for the year ended 30th April 2018 and any other interim or updated information published by CAF Bank.

Forward-looking statements contained within this document apply only as at the date of this document. Except as required by the Prudential Regulatory Authority, Financial Conduct Authority or other applicable law or regulation, CAF Bank does not have any obligation to update or revise publicly any forward-looking statement, whether as a result of new information, further events or circumstances or otherwise, and expressly disclaims any obligation to do so.

2453C/0618

CAF Bank