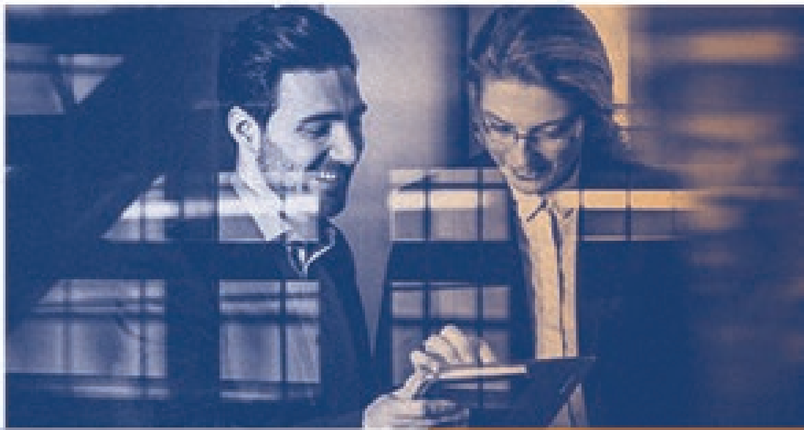
بنك البحرين والكويت

Banking without **boundaries**

Annual Report 2017



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BBK is licensed by the Central Bank of Bahrain as a Conventional Retail Bank

Designed and produced by Group Origin

Our vision

BBK will be the premier regional financial services enterprise in providing superior products and services of high quality through innovation, technology and lifelong client relationships.

Our mission

The Bank will expand its overseas presence in more locations in which it chooses to operate in order to satisfy the diversified needs of clients. We believe clients are the driving force in everything we do. We will not compromise on our absolute commitment to providing the very best in client service.

We believe our people are our number one asset, with the highest degree of competence, integrity and professionalism. We instil in our people the principles of entrepreneurship, decision-making and ownership through our commitment to training, development, delegation and performance-based reward systems.

We are determined to utilise cutting-edge technology, which we recognise as most critical in supporting our short, medium and long-term business objectives.

Our shareholders are the source of our financial strength and can expect continued growth and profitability. They are supportive and are confident of our vision of the future.

Our values

creative · passionate · pioneering · reliable

H.M. King Hamad bin Isa Al Khalifa
King of the Kingdom of Bahrain

H.H. Sheikh Sabah Al Ahmed Al Sabah
Amir of the State of Kuwait

BBK has always been a leader in banking technology. We have a series of ‘firsts’ to our credit – from ATMs to phone banking. With digital technology revolutionising so many aspects of our daily lives, connectivity is essential for our customers to benefit from banking services that embody the latest innovations.

Over the past year, we have again led the way in the banking industry, introducing high-tech advances that put our customers at the forefront of digital banking advantages.

Financial highlights

Net interest income

+5.9%

Net interest income for the year was BD 90.9 million.

Total assets

+1.6%

Total assets increased to BD 3,763 million.

Net profit

+4.0%

Net profit increased to BD 58.7 million.

	2013	2014	2015	2016	2017
Income statement highlights (BD millions)					
Net interest income	68.9	72.3	72.7	85.8	**90.9**
Other income	43.5	45.2	48.4	47.7	**52.2**
Operating expenses	54.4	46.2	49.8	53.1	**54.0**
Net profit	45.1	50.1	53.2	56.4	**58.7**
Cash dividend	10%	20%	25%	30%	**35%**
Stock dividend	10%	5%	–	–	**–**
Financial statement highlights (BD millions)					
Total assets	3,231	3,501	3,646	3,703	**3,763**
Loans and advances	1,619	1,846	1,765	1,767	**1,741**
Investments	802	824	794	812	**796**
Customer deposits	2,353	2,471	2,643	2,494	**2,624**
Term borrowings	239	241	205	206	**199**
Total equity	333	359	361	474	**501**
Profitability					
Earnings per share (fils)	44	47	50	49	**48**
Cost/income	48.41%	39.33%	41.14%	39.80%	**37.75%**
Return on average assets	1.43%	1.49%	1.44%	1.51%	**1.62%**
Return on average equity	14.56%	13.93%	14.79%	13.23%	**12.07%**
Profit per employee (BD)	45,232	48,826	52,169	54,136	**51,433**
Capital					
Capital adequacy	15.33%	15.63%	14.87%	18.48%	**20.01%**
Equity/total assets	10.31%	10.26%	9.89%	12.81%	**13.31%**
Debt/equity	71.94%	67.05%	56.74%	43.46%	**39.74%**
Liquidity and business indicators					
Loans and advances/total assets	50.10%	52.74%	48.40%	47.73%	**46.26%**
Loans and advances/customer deposits	68.79%	74.72%	66.78%	70.86%	**66.35%**
Investments/total assets	24.82%	23.53%	21.77%	21.93%	**21.15%**
Liquid assets/total assets	33.25%	29.19%	32.04%	32.61%	**34.69%**
Net yield ratio	2.39%	2.32%	2.12%	2.46%	**2.69%**
Number of employees	996	1,026	1,020	1,042	**1,141**

Dear Shareholders

I am honoured to introduce BBK’s annual report for the year ended 31 December 2017. Despite the challenging environment, we can look back on a year of significant achievements. We maintained our record of annual growth in profitability, and continued to implement the Bank’s strategic priorities.

I extend our thanks and appreciation to His Majesty King Hamad bin Isa Al Khalifa, the King of the Kingdom of Bahrain, and His Highness Sheikh Sabah Al Ahmad Al Sabah, the Amir of the State of Kuwait. And I thank the respective governments and regulatory authorities for their support and guidance.

I also thank the Board of Directors and all stakeholders for their outstanding contributions during the year. I have every confidence that their knowledge and guidance will be valuable in realising our vision for growth as we enter the closing year of our 2016-18 strategic cycle.

Murad Ali Murad
Chairman

The adoption of IFRS 9 was one of several priorities advanced during the 2016 phase of the Bank's three-year strategic cycle.

Capital adequacy

20.0%

Capital adequacy rose from 18.5 percent in 2016 to 20.0 percent in 2017.

The Board of Directors is pleased to present the 46th annual report and consolidated financial statements of BBK and its subsidiaries (the Group) for the year ended 31 December 2017.

Operating environment

There have been some signs of improvement in our operating environment, not least the rise in the oil price that is so influential in our regional economies. Nevertheless, regional political issues – and to an extent, economic issues – combined to maintain the challenging market conditions of recent times, perhaps even more so in the past year.

Towards the end of 2017, oil prices stabilised at a higher level, which would have been thought improbable not so long ago. From $36 per barrel this time last year, we are now in the $55-60 range, a major improvement.

However, this should not be taken as an indicator that our region can relax and slow down the structural economic reforms that were prompted by the decline in oil revenues. Restructuring continues to be of vital importance, particularly for Bahrain. A good example is the gradual removal of subsidies on a range of items from food to fuel, which reduces government costs while increasing revenues.

Similarly, the introduction of value added tax (VAT) will mark a significant change in the tax landscape of the GCC and assist in boosting government revenues. Businesses in Saudi Arabia and the United Arab Emirates will be required to comply with the VAT regime from January 2018. Bahrain and other GCC states are getting ready to implement VAT during 2018-19 pending official issuance of specific VAT rules and guidelines. Government revenues across the GCC region will also benefit from special taxes on tobacco products, soft drinks, and energy drinks effective from 1 January 2018.

Expected GDP growth of 2.5 to 2.8 percent in 2017 is lower than forecast and lower than the previous year, attributed by a World Bank report to weak aggregate demand and accumulated fiscal deficits. Despite austerity measures, the World Bank notes that Bahrain remains exposed to financing risks due to its limited savings, high debt levels, and low oil and bauxite prices.

Economic policy

As expected, Bahrain's government has resorted to borrowing as it goes through a period of restructuring, drawing on domestic, regional, and international sources of funding. Although the Kingdom no longer holds a national investment-grade rating, all issues have been over-subscribed, a very positive outcome for the government and the Bahrain economy.

The issues did not have to carry a premium rate to attract investors. As interest rates have gradually risen in the USA, the differential with issues by Bahrain has not been significant.

Bahrain is also now issuing treasury bills and Sukuk direct to the public, competing with banks for deposit-taking. Banks act as intermediaries for such transactions, which carry a minimum investment of about BD 10,000 and are listed on the Bahrain Bourse for ease of trading. So far, the Bank's deposit-taking has been unaffected by public issues, with BBK's figures for the year exceeding those for 2016.

The response to institutional and public issues has helped the government in restructuring and economic management, although a large balance-of-payment deficit is still in place.

Strategic initiatives

The Board of Directors has completed a detailed analysis of the Bank's entire strategic planning procedure to ensure continued relevance to the changing market environment. As a result, strategy reviews now take place every six months instead of yearly.

The adoption of International Financial Reporting Standard 9 (IFRS 9) was one of several priorities advanced during the 2016 phase of the Bank's three-year strategic cycle. Among our key business achievements were the development of our representative office in Turkey, which opened in December 2016; opening Aegila Capital Management, our joint-venture investment and advisory firm in London; relocating and opening new branches in Bahrain; completion of preparations for launching *BBK Lite*, our tailored offering for expatriate workers; and investing further in technology.

Our focus on technology has two aspects: enhancing the services we provide to customers, and increased vigilance to the ever-growing threats to cyber security.

Cash dividend

35 fils

The Board has recommended a cash dividend of 35 fils per share.

Our review of IT requirements was particularly relevant: a major initiative that matches our systems and services to the best available technology. Next year is the third and final of the current three-year strategic cycle, and technology will be an important priority. Most of global technology development has taken place in the past five years, so staying ahead is imperative for established leaders such as BBK.

Our focus on technology has two aspects: enhancing the services we provide to customers, and increased vigilance to the ever-growing threats to cyber security. The former is evident in deposit machines and our new interactive teller machines; the latter in the cyber-attacks that are becoming increasingly frequent around the world. Although BBK has not been affected, we are alert to the threat it poses for the banking industry and always ensure that we have the best protection in place.

The Bank's operation in India has recorded improved performance, expected to continue while attention is given to improve the performance of the Kuwait branch. Our representative office in Turkey is still at an early stage, but indications are good that the expected contributions to revenue will be achieved. Our well-established Dubai representative office continues to perform well.

CrediMax, our wholly owned specialist in bank card business, continues to perform very well, generating consistent demand because of the high quality of its services. External issues have stalled plans for cross-border expansion into Kurdistan and Saudi Arabia, but we still see potential there and are keeping our options open.

Invita, our wholly owned subsidiary specialising in call centre services, embedded its recently established Kuwait subsidiary and continued its diversification into serving the training and insurance sectors.

Financial highlights

In another year of excellent results, BBK achieved a net profit of BD 58.7 million for 2017, up by 4.0 percent on the previous year's BD 56.4 million, and equivalent to 48 fils earnings per share. Net interest income rose by BD 5.1 million, an increase of 5.9 percent on the BD 85.8 million reported in 2016. Total shareholders' equity rose by 5.6 percent to BD 500.8 million.

The Bank again demonstrated consistent performance in its core business, underlining the soundness of its strategy and management team. The total balance sheet strengthened to BD 3,763.1 million, an increase of 1.6 percent.

At 20.0 percent, capital adequacy is at an unprecedented level, up from 18.48 percent a year earlier. This is substantially above the minimum regulatory requirement, boosted by the successful BD 86 million perpetual bond issue in 2016. The ratio of liquid assets to total assets has strengthened to 34.69 percent, from 32.61 percent. The Board has recommended a cash dividend of 35 fils per share.

Regulatory compliance

BBK has been one of the few banks regionally to fully implement the new International Financial Reporting Standard 9 well ahead of 1 January 2018, when its requirements become formally effective. In fact, the Bank is among global leaders in early adoption of the standard, which specifies how an entity should classify and measure financial assets, financial liabilities, and some contracts to buy or sell non-financial items.

IFRS 9 is regarded as the most significant accounting development for banks today because it requires significant changes to a bank's operational and risk management processes. Recognising the importance of IFRS 9, BBK began planning and implementation two years before the effective date – a decision that has proved very valuable.

In moving from making general provision for estimated credit loss, the entire portfolio is now assessed for signs of weakness, and investment or political factors are taken into account when assessing the need for provisions. This has resulted in increased provisioning, as was expected globally, but the Bank has been able to cope with this – and absorb the cost of implementing IFRS 9 – while still achieving higher profitability.



Bahrain's Best Retail Bank **for the fifth successive year**

Global Banking and Finance Review

Appropriations

The Board of Directors recommends the following appropriations of the Bank's net profit for approval by shareholders:

	BD'000
Retained earnings as at 1 January 2017	122,830
Profit for the year 2017	58,685
Proposed appropriation for donations	(1,400)
Distribution on Perpetual Tier 1 Convertible Capital Securities	(7,103)
Other negative changes in retained earnings	(619)
Retained earnings as at 31 December 2017 available for distribution (before proposed dividend)	**172,393**
Proposed cash dividends (35% of paid-up capital, net of treasury stock)	37,761
Retained earnings as at 31 December 2017 (after proposed dividend)	**134,632**

Fitch

	Rating
Long-term issuer default rating	BB+
Short-term issuer default rating	B
Viability rating	bb+
Support rating	3
Support rating floor	BB+
Outlook	Negative

Report issue date: 2 November 2017

Fitch
Long-Term Issuer Default Rating

BB+

Moody's

	Rating
Bank deposits	B2/NP
Baseline credit assessment	b1
Adjusted baseline credit assessment	b1
Counterparty risk assessment	Ba3(cr)/NP(cr)
Senior unsecured	B1
Subordinate	(P)B2
Outlook	Negative

Report issue date: 7 August 2017

Moody's
Long-Term Bank Deposits

B2

Corporate business will remain important, but in the current environment it carries more risk, as was evident in the provisioning made for 2017.

Earnings per share

48 fils

Earnings per share for 2017 stood at 48 fils.

BBK is also well prepared to capture and report tax-residency status, to satisfy the Common Reporting Standards (CRS) as well as the USA's Foreign Account Tax Compliance Act (FATCA). Value added tax is another challenging project that the Bank aims to complete ahead of the expected implementation date in the Kingdom of Bahrain.

Supporting society

As detailed in the CSR section of this annual report, BBK continues to invest in a range of community initiatives, demonstrating our commitment to supporting Bahrain and its people.

Forward view

In the coming year, IFRS 9 will remain a focus, enabling BBK to draw maximum benefit from our investment in early adoption. We are in a position to better identify potential weaknesses and problems in our total portfolio.

Corporate business will remain important, but in the current environment it carries more risk, as was evident in the provisioning made for 2017. Our experience is not unique – it is typical of the regional banking sector and we will work with corporate customers that need help to overcome their challenges.

Global events such as the US presidential elections and the British referendum to leave the European Union have so far had little or no impact in Bahrain and we do not expect this to change in the coming year. On the positive side, the US economy is strong, with gradual upward movement in interest rates. More significantly, our region's challenges take precedence as political change and economic restructuring gather pace.

We can expect only moderate GDP growth in the coming year, but we are confident that Bahrain will come through. There is a commitment to economic reform, and the sustained over-subscription of bond issues confirms the positive nature of investor sentiment.

Appointment of auditors

At the Annual General Meeting held on 29 March 2017, Ernst & Young were re-appointed as external auditors to BBK for the financial year ending 31 December 2017.

Ratings

In November 2017, Fitch affirmed BBK's long-term issuer default rating at BB+ with a 'Negative' outlook, the same as Bahrain's sovereign rating. The agency says the rating indicates BBK's standalone strength and resilient financial performance, as reflected in the Bank's viability ratings, support ratings, and support rating floors.

BBK has maintained solid margins and consistent profitability through its well-entrenched banking franchise in Bahrain. Funding and liquidity remain satisfactory and are important rating influencers. Asset quality metrics are sound, supported by an adequate level of provisioning. Fitch does not expect a further sharp increase in impaired loans. However, it notes that the operating environment in Bahrain remains challenging and could impose additional pressure on the Bank's asset quality metrics.

Moody's reported in August 2017 that its B2 (Negative)/Not-Prime ratings of BBK's local currency deposit and senior unsecured debt illustrate BBK's standalone credit strength, as reflected in a baseline credit assessment (BCA) of b1, the same level as Bahrain's B2 (Negative) sovereign rating.

The b1 BCA indicates BBK's strong domestic franchise, which with recent efficiency improvements supports profitability, solid liquidity buffers, a resilient funding profile, and sound capital levels. BBK's long-term foreign currency deposit rating of B2 is constrained by Bahrain's B2 country ceiling for such deposits, which takes account of foreign currency transfer and convertibility risks.

Appreciation

The Board thanks BBK shareholders for their continued confidence; our clients for their loyalty and patronage; and BBK's management and employees for the hard work and commitment that underpin another year of excellent results.

On behalf of the Board of Directors

Murad Ali Murad
Chairman

Murad Ali Murad
Chairman

Chairman of the Nomination, Remuneration and Corporate Governance Committee

Chairman of the Audit and Compliance Committee

Director since 21 March 1999
(Independent)

Qualifications and experience
Fellow member of the Chartered Institute of Management Accountants, London, United Kingdom. Over 45 years' experience in the banking sector and has had his own business for the past 15 years.

Aref Saleh Khamis
Deputy Chairman

Director since 1 April 2003
(Non-executive)

Qualifications and experience
Master in Business Administration, King Fahad University of Petroleum and Minerals, Dhahran, Kingdom of Saudi Arabia. 33 years' experience in the government sector.

Nominated by:
Social Insurance Organization (SIO)

Mohamed Abdulrahman Hussain
Board Member

Chairman of the Executive Committee

Director since 2 March 2008
(Independent)

Qualifications and experience
Bachelor of Arts, Economics and Finance, University of Aleppo, Syria. Over 40 years' experience in the banking sector.

Sh. Khalifa bin Duaij Al Khalifa
Board Member

Director since 27 February 2005
(Independent)

Qualifications and experience
Master in Business Administration, Johns Hopkins University, United States of America.

Master in Social and Public Policy, Georgetown University, United States of America. 10 years' experience in the government sector (investment field) and 11 years in the diplomatic sector.

Marwan Mohammed Al Saleh
Board Member

Director since 30 December 2014
(Non-executive)

Qualifications and experience
Bachelor of Arts, Eckerd College, United States of America. 33 years in the investment sector.

Nominated by:
Kuwait Investment Authority

Dr. Zakareya Sultan AlAbbasi
Board Member

Director since 22 February 2012
(Non-executive)

Qualifications and experience
PhD., University of East Anglia, United Kingdom. 32 years' experience in the government sector (social insurance).

Nominated by:
Social Insurance Organization (SIO)

Hani Ali Al Maskati
Board Member

Chairman of the Risk Committee

Director since 29 March 2017
(Non-executive)

Qualifications and experience
Master of Business Administration, University of Hull, England. Over 30 years' experience in transaction banking.

Nominated by:
Ithmaar Bank

Edrees Musaed Ahmad
Board Member

Director since 29 March 2017
(Non-executive)

Qualifications and experience
Master of Economics, Kuwait University, State of Kuwait. Over 12 years' experience in the investment sector.

Sh. Abdulla bin Khalifa bin Salman Al Khalifa
Board Member

Director since 2 March 2008
(Non-executive)

Qualifications and experience
Bachelor of Business Administration, George Washington University, United States of America. 17 years' experience in the banking and investment sector.

Ashraf Adnan Bseisu
Board Member

Director since 29 March 2017
(Non-executive)

Qualifications and experience
Bachelor of Science in Civil Engineering, Southern Methodist University, USA; Master of Science in Management Information System, London School of Economics, UK. Over 15 years' experience in investment management and over 25 years in the insurance and financial services sector.

Nominated by:
Ithmaar Bank

Yusuf Saleh Khalaf
Board Member

Director since 6 March 2011
(Independent)

Qualifications and experience
Associate of the Association of Chartered Certified Accountants, United Kingdom, with 37 years of experience in the banking and financial services sector.

Jassem Hasan Ali Zainal
Board Member

Director since 22 November 1994
(Independent)

Qualifications and experience
Master in Civil Engineering, Kuwait University, State of Kuwait. 33 years' experience in the banking sector, 4 years in the government sector, 6 years with finance companies, 24 years with investment companies, and has had own business for 9 years.

Significant recovery in oil prices eased the pressure on state revenues but, with regional economies so dependent on government spending, the effect is still far short of previous levels. Nevertheless, BBK closed the year with 4.0 percent growth in profitability, maintaining our record of sustained year-on-year improvement.

During 2017 we faced a particularly challenging market, with political and economic issues influencing the operating environment. The Bahrain market is expecting GDP growth, although less than forecast, with negative implications for the banking sector and for customers.

Aegila is the continuation of our expansion strategy in the investment banking and private banking sectors.

Shareholders' equity

+5.6%

Ratio of liquid assets to total assets

34.7%

The ratio of liquid assets to total assets increased in 2017, from 32.6 percent in 2016.

For all banks, not least BBK, the new regulations introduced since the 2008 financial crisis have needed investment in time and money to ensure compliance with local and international guidelines. Improved systems and technology, new procedures, and more people have all added up to higher costs.

Nevertheless, many positives compensate for the new regimen. Any measures that can help minimise the impacts of a future crisis are to be welcomed, and BBK has been at the forefront in adopting one of the most important measures – International Financial Reporting Standard 9 (IFRS 9).

BBK began early in preparing for and implementing IFRS 9, enabling us to have our compliance fully tested and operational well in advance of the 1 January 2018 target. The experience has been highly worthwhile, and the benefits are already evident. The new standard takes a wider approach to identifying credit risks and potential problems, involving a three-stage analysis of a bank's total portfolio. The analysis eliminates systemic weaknesses and introduces more detailed assessment of political risks and those arising from the market environment.

The immediate impact of IFRS 9 is a greater need for early provisioning against credit risk, which facilitates more accurate and reliable management information on risk levels.

Strategy

Our overseas expansion continues, in line with one of the core principles of the Bank's 2016-18 strategic cycle. Aegila Capital Management, our new investment and advisory firm, opened in London. A joint venture between BBK and Osool Asset Management, Aegila will initially focus on opportunities in UK and European commercial real estate.

Aegila is authorised by the UK Financial Conduct Authority and is staffed by a team of talented professionals drawn from some of the world's largest and most successful investment banks, sovereign wealth funds, and private equity fund managers.

Aegila continues our expansion strategy in the investment banking and private banking sectors, aimed at broadening our service offering and increasing the weight of recurring fee-based income in the Group.

Further progress with international expansion was made with the opening in Turkey of our second representative office, a major development for BBK that enhances the Bank's international business operations.

Our people

Women's empowerment initiatives are always a top priority for BBK. Achieving gender equality at all levels is a continuous process, with emphasis on developing female managers through fast-track programmes.

Our achievements in this field were recognised in 2017 through receipt of the prestigious 'Her Royal Highness, Princess Sabeeka Bint Ibrahim Al Khalifa Award for Bahraini Women Empowerment'. The award is an important initiative to support and consolidate the status of Bahraini women. Winners are chosen for their commitment to the policy of non-discrimination and success in integrating women in national development plans, attaining higher professional status for women as they achieve executive and decision-making positions.

On the training side, BBK's e-Learning platform continues to be a vital asset in accelerating employee development. It has more than 500 tutorials and courses, including professional business skills, and is recognised as one of the best in the industry. With 'anytime, anywhere' access, the system's flexibility is vital in enabling skills transfer for the Bank's geographically dispersed workforce in the Gulf region, India, and Turkey. The platform is proving especially helpful in supporting working women, giving them access to a tool that can accommodate their needs and availability of study time.

We regard people as a highly valued asset, even maintaining links with those who are no longer members of our team. The BBK Alumni Club was formed in 2015 to strengthen the bonds between the Bank and its former employees. The club has since played a key role in showing our appreciation for the contribution of alumni to BBK's long history of success.

Technology

Sustained investment in technology leadership has always been a BBK hallmark and is an integral part of the 2016-18 strategy.

BBK was the first to introduce ATMs to Bahrain, and continued to strive to remain pioneering in banking technology. In September 2017, BBK launched the first ITM (interactive teller machine) in Bahrain. It enables users to talk directly to customer service specialists who can help them with transactions or other requirements, reducing waiting time for customers. The ITM system has been enthusiastically received by customers and more installations are planned during the next year.

New technology has also been used to reduce waiting time for our customers. 'Virtual queuing' is a smartphone application that eliminates the need to go to the banking hall, collect a queuing number, and wait for the number to be called. Customers using the app are given a specific time to visit the branch, saving time and allowing them to plan their activities more effectively. The app is another BBK 'first'. It was initially developed for doctors' surgeries and adapted by BBK for banking purposes.

Another pioneering initiative launched during the year allows our customers to withdraw cash securely and safely from any BBK ATM without using a debit card. Our ATMs are now equipped with a cardless withdrawal option, providing customers with convenient access to cash at all times.

CrediMax also contributed to the technology drive by launching MaxWallet – Bahrain's first smartphone-based digital wallet using credit cards. Produced in collaboration with MasterCard, MaxWallet is enabled by a quick response (QR) code that allows customers to pay for goods and services using their mobile phones.

MasterCard's Masterpass QR provides valuable benefits for merchants, issuers, acquirers, and end-users, being fast, secure, and cost-effective. It provides a viable alternative to cash without the need for point-of-sale equipment, enabling users to safely pay for face-to-face purchases with their phones.

Transforming payment processes is regarded as the biggest opportunity since the introduction of plastic cards many years ago. As payments increasingly shift from cash to electronic, the availability of multiple channels and devices provides opportunities for digital convergence, simplifying payments and enhancing security for customers and merchants.

BBK plans even more technology initiatives for 2018, including a number of totally new digital offerings.

Unique new format

The first pilot branch of *BBK Lite* – our new essential services retail format – is finalised and is due to open during the first quarter of 2018, bringing simplified banking services to people that have limited access to banking facilities. The format enables quick service, catering primarily to migrant workers who need salary transfers, remittances, and other banking services. The convenient location of the pilot branch saves users having to visit central Manama for banking services. More *BBK Lite* branches will follow in 2018.

Subsidiaries

CrediMax is the market leader in specialised card business and has a considerable stake of the card issuance and acquisition market. This has been achieved in the face of tough competition – more than 15 issuers and three acquirers – with 29 retail banks operating in Bahrain, all offering credit and debit cards.

Our other subsidiary, Invita, also continues to perform well and strengthen its business model. During 2018, having identified the need for a Third-Party Administrator (TPA) for motor insurance claims in Bahrain, Invita approached several insurance companies to come together to form a TPA. The result was the formation of Invita Claims Management Company (ICMC), in which Invita now has the majority shareholding.

ICMC provides more efficient claim operations for insurance companies and enhanced service for customers. It processes the claims on behalf of insurers, from initial registration to assessment of damaged vehicles, engaging repairers through its network of approved garages, and final settlements.

Internal control

BBK maintains a sound internal control system and processes, ensuring they are adequate and in place across all departments within all entities, so that the Group's assets are always safeguarded. BBK's Internal Control Unit has implemented comprehensive procedures that help identify and manage risks that could arise in the course of conducting business. These controls are reviewed at least annually.

Awards

For the fifth consecutive year, BBK was designated 'Best Retail Bank in Bahrain' by Global Banking and Finance Review. The award honours companies that stand out in particular areas of expertise in the banking and finance industry. Criteria include profitability, market share, customer relations, and product innovation. BBK was recognised once again because of its outstanding achievements, dedication to retail banking, and performing highly against the judging panel's key benchmarks.

Global Finance ranked BBK as a leader in cash management services in its annual awards for 'World's Best Treasury & Cash Management Banks and Providers 2017'. After a multi-tier assessment, BBK joined 55 banks around the world as the best in their respective countries. The recognition confirms BBK's status as Bahrain's leading provider of cash management products and services, and underlines the value of the Cashlink electronic platform. The award was presented at the SWIFT International Banking Operations Seminar (SIBOS 2017) in Toronto, regarded as one of the world's premier financial services events.

BBK also received the 2017 'Elite Quality Recognition' award by JP Morgan Chase, in recognition of the Bank's outstanding performance in MT103 Straight through Processing (STP), achieving a rate of 98.86%. This is the eighth consecutive year that BBK has qualified for the award, with Elite status since 2014. Similarly, it was awarded the Barclays Excellence Award for GBP Straight through Processing.

Security compliance meets **international benchmarks**

Interactive teller machine **is another BBK first**

BBK won an unprecedented number of industry awards during 2017.

CrediMax received the 'Most Compliant Data Integrity Award' from MasterCard, made annually to MasterCard customers demonstrating excellence in authorisation and data clearing procedures. The award underlines the continuous drive by CrediMax to lead in technology. It confirms that CrediMax maintains data integrity standards across all interfaces, programmes, services, and operations – resulting in improved authorisation response, better clearing and settlement processes, and enhanced quality of data.

Finally, as mentioned earlier, BBK's achievements in empowering women were recognised in 2017 through receipt of the prestigious 'Her Royal Highness, Princess Sabeeka bint Ibrahim Al Khalifa Award for Bahraini Women Empowerment'.

Security certification

SISA Information Security, the Middle East's leading security assessor, awarded PCI DSS v3.2 certification to BBK in 2017, after the Bank achieved one of the most stringent security standards – Payment Card Industry Data Security. Compliance with standards for payment card data and successful completion of the audit requirement illustrate the security of the Bank's system and its investment in the highest standards of safety.

Maintaining such an international benchmark is an ongoing and stringent process. BBK has laid an excellent foundation to be vigilant and ready to face any security eventuality. While acknowledging that no system can address every possible threat, achieving this standard puts BBK several steps ahead in maintaining the highest level of trust.

Conclusion

We expect 2018 to be equally challenging as its predecessor, as regional, political and economic issues continue to dominate. However, we are reasonably confident of maintaining healthy growth, based on BBK's long-standing policies of prudence, conservatism, and provisioning adequately for distressed accounts.

In line with our strategy to seek cross-border expansion, the Bank's assets are well split between Bahrain and external territories. We have a good book of business across the GCC states, and our international branches and representative offices are all sourcing assets from outside Bahrain.

A number of local investment banks have changed their strategy since the financial crisis, entering the retail banking segment. There is a clear case for consolidation as smaller banks face the same challenges as larger counterparts in complying with new regulatory requirements such as IFRS 9. Consolidation would therefore provide economies of scale.

With 80 percent of government revenues still derived from oil, initiatives to diversify revenues will certainly continue in the year ahead. The effects of removing subsidies and introducing new taxes are already being felt, with value added tax (VAT) introduced in Saudi Arabia and the UAE from January 1, 2018. Other GCC states will implement VAT during 2018-19 once their specific VAT rules are officially issued.

For BBK, priorities for 2018 will be asset quality, liquidity management of existing books, and carefully planned growth. We will further strengthen the management process, pursue the remaining objectives in the 2016-18 strategic cycle, and continue monitoring our strategic performance to leverage strengths and bridge any gaps.

Appreciation

On behalf of BBK's management team, I thank our Board of Directors for their valued guidance in the course of the year. Our thanks go also to the Central Bank of Bahrain, the Bahrain Bourse, and the regulators of the State of Kuwait, the Republic of India, the United Arab Emirates, and the Republic of Turkey.

Finally, I extend our appreciation to our loyal clients and our employees, whose dedication has contributed to the Bank's success.

Reyadh Yousif Sater
Chief Executive

Executive management

Reyadh Yousif Sater
Chief Executive

Qualifications and experience:
MBA, University of Glamorgan, United Kingdom (2001).

40 years' banking experience.

Joined BBK in 1978.

Abdulrahman Ali Saif
Deputy Chief Executive
Wholesale Banking Group

Qualifications and experience:
PhD in Economics, University of Leicester, United Kingdom (1992).

35 years' banking experience.

Joined BBK in 2008.

Mohammed Ali Malik
Deputy Chief Executive
Retail Banking Group

Qualifications and experience:
BSc in Computer Science, University of Petroleum and Minerals, Kingdom of Saudi Arabia (1984).

32 years' work experience.

Joined BBK in 2000.

Rashad Ahmed Akbari
Assistant General Manager
Operations

Qualifications and experience:
MSc in Marketing, University of Stirling, United Kingdom (1997).

31 years' work experience, of which 16 years in banking.

Joined BBK in 2000.

Raj Dugar
Assistant General Manager *
Group Chief Internal Auditor

Qualifications and experience:
ACA, Institute of Chartered Accountants of India (1987),

28 years' banking experience, of which 17 years in internal audit.

Joined BBK in 2000.

C.K. Jaidev
Assistant General Manager
International Banking

Qualifications and experience:
MBA, Indian Institute of Management, Republic of India (1989).

28 years' banking experience.

Joined BBK in 1996.

Nadeem A. Aziz Kooheji
Assistant General Manager
Corporate Banking

Qualifications and experience:
BA in Finance and International Business, University of Texas, United States of America (1988).

11 years' audit and 20 years' banking experience.

Joined BBK in 1999.

* Effective 1 March 2017
** Effective 1 August 2017

Jamal Mohamed Al Sabbagh
General Manager
Information Technology and Operations Group

Qualifications and experience:
MBA, University of Glamorgan, United Kingdom (2001).

37 years' banking experience.

Joined BBK in 1980.

Hassaan Mohammed Burshaid
General Manager
Human Resources and Administration Group

Qualifications and experience:
MSc, Human Resources Management, DePaul University, United States of America (2006).

23 years' experience in the field of human resources.

Joined BBK in 1998.

Mohammed Abdulla Isa
General Manager
Financial Planning and Control Group

Qualifications and experience:
Certified Public Accountant (CPA), American Institute of Certified Public Accountants, Delaware State Board of Accountancy, United States of America (2001).

26 years' finance experience.

Joined BBK in 2001.

Adel Abdulla Salem
Assistant General Manager
Retail Banking

Qualifications and experience:
PHD in Management, Monarch Business School - Switzerland (2015),

30 years' banking experience in retail banking, business of cards and telecoms.

Joined BBK in 2017.

Neil Sharp
Assistant General Manager
Treasury and Investment

Qualifications and experience:
Associate member of the Association of Corporate Treasurers.

31 years' banking experience in the treasury business.

Joined BBK in 2009.

C. V. Murthy
Assistant General Manager **
Risk, Credit and Compliance

Qualifications and experience:
MSc in Agricultural Economics (1984).

33 years of banking experience, of which 20 years in risk management.

Joined BBK in 2002.

Sustaining growth, **promoting national development**

BBK was honoured to receive the 'Her Royal Highness, Princess Sabeeka bint Ibrahim Al Khalifa Award for Bahraini Women Empowerment', an important initiative to support and consolidate the status of Bahraini women.

Business success and social responsibility are inter-dependent – a symbiotic union that is advantageous to both benefactor and beneficiary – building and sustaining long-term relationships. BBK is very conscious that altruism is not an end in its self, amounting to much more than merely making donations to good causes.

BBK sustains growth and promotes national economic development by supporting employees, addressing community needs, and backing Bahrain's financial sector. At the same time, the Bank earns recognition from independent authorities that testifies to the value of the Bank's social responsibility policies and the benefits they create

The Bank assists a diversity of community-related projects and good causes, providing substantial annual donations and sponsorship. In 2017, an appropriation amounting to BD 1.4 million was approved by shareholders for distribution.

Supporting employees

BBK is particularly proud that 95 percent of its employees are Bahraini nationals. The Bank recognises the value of investing in local talent through training and professional development, improving skills across the organisation and creating opportunities for career advancement. Overall, BBK is thoroughly committed to enhancing employee career development and empowering its people with greater responsibilities.

In supporting these objectives, the BBK e-Learning platform gives the Bank's geographically dispersed workforce 'anytime, anywhere' access to a higher level of professional competence. BBK e-Learning was launched in 2016 and is a growing asset in the Bank's already formidable resources for staff training.

BBK provides generous employee benefits that include share incentives, retirement programmes, and health and life insurance, reinforcing its status as an employer of choice. Employees who make outstanding contributions to the success of the Bank are recognised at an annual awards ceremony to honour their achievements.

Even former employees are encouraged to maintain links with the Bank. The Alumni Club for former employees was established so that past and present members of the BBK family could meet periodically and not lose their commonality.

Women empowering

The seriousness of BBK's commitment to empowering women is endorsed at Board of Directors level, specified in a powerful policy document that supports and complements Bahrain's Women Empowerment Strategy. The policy sets out a clear vision and encourages empowerment and gender equality at all levels. Its success is evident in the Bank's high ratio of female employees, currently standing at 38 percent, an increase of 18 percent over the last five years.

BBK's achievements in this field were recognised in 2017 through receipt of the 'Her Royal Highness, Princess Sabeeka bint Ibrahim Al Khalifa Award for Bahraini Women Empowerment'. The award was established in 2006, and has since been presented every two years. It is highly regarded as one of the important initiatives by the Kingdom in supporting and consolidating the status of Bahraini women.

The Bank's Women's Empowerment committee is responsible for developing action plans that help women reach their full potential, achieve their career goals, and maintain their work/life balance. To support the achievement of policy objectives, the Bank's annual Chief Executive Award for Women's Empowerment is an incentive for managers to support women's development and career growth.

BBK's initiatives to empower women also have an external dimension. Expanding and reinforcing relationships with women-owned ventures, including small businesses and entrepreneurs, is a strategic business priority. The Bank also helps women gain independence and education by supporting the goals of women's societies and associations in Bahrain.

Community involvement

Giving up personal time and passing on professional skills by volunteering for various community programmes is characteristic of BBK employees. During 2017, many employees gave lectures in school classrooms to support the work of InJaz Bahrain, which aims to empower young people and prepare them for today's business challenges. Such unstinting efforts are typical of the volunteering culture which the Bank's employees do so much to sustain.

Addressing community needs

A dedicated fund to support future CSR mega projects was established by BBK in 2012. The fund's value grew to BD 2.085 million during 2017, including the year's appropriation of BD 400,000 from total donations. While continuing to build up the fund, BBK is studying the needs of society and how the fund's resources can best be used to meet them. In previous years, BBK financed projects such as the BBK Health Centre in Hidd and the BBK Rehabilitation Centre.

Education

Learning features strongly in the Bank's external social responsibility work, with 30 percent of the 2017 budget allocated to education. Investment in education is part of the Bank's forward-looking philosophy, supporting young Bahraini talent on the path to becoming a new generation of informed and productive citizens.

As a long-standing Platinum Sponsor of the Crown Prince's International Scholarship Programme, BBK has committed BD 1 million to enable Bahrain's most talented young people to study at top international universities and colleges. And in a five-year commitment of BD 50,000 to the Isa bin Salman Education Charitable Trust, a scholarship fund established in 2013, the Bank contributed in helping students to pursue their studies.

Further contributions to youth empowerment include training employees' children, university students, and InJaz Bahrain students through work experience that supplements classroom learning.

SUSTAINABLE DEVELOPMENT GOALS

4 QUALITY EDUCATION

5 GENDER EQUALITY

8 DECENT WORK AND ECONOMIC GROWTH

17 PARTNERSHIPS FOR THE GOALS

The United Nations' 17 Sustainable Development Goals (SGDs) were adopted by countries all over the world, whose leaders committed to mobilise efforts to end all forms of poverty, fight inequality, and tackle climate change. BBK supports this initiative and has identified four goals that it can have a direct positive bearing on.

BBK's community contributions also have a strong emphasis on health and well-being awareness, with financial support extended consistently to medical entities and research institutes active in fighting diseases such as diabetes, sickle cell anaemia, and cancers.

Health and sport

Health and medical advancement have always been a priority and we have invested heavily through the years, continuing to support a range of worthwhile causes during 2017. These included the Mohammed Bin Khalifa Bin Salman Al Khalifa Cardiac Centre, where BBK supplied latest technology equipment that gives a three-dimensional view of the heart, helping to identify abnormal rhythm and optimise treatments.

The Bank recognises the health benefits flowing from active participation in sport, regularly increasing its investment in sport promotion. By fostering and encouraging involvement in sports, BBK helps people to become more active, while inspiring the young and aiding physical well-being for all.

During 2017, the Bank invested in gym equipment for the Muharraq Youth Centre, a state-of-the art facility that encourages young people to enhance their physical and mental health through sports and fitness.

Over decades, BBK has a proud record of donations and sponsorships that have supported football, junior tennis, and equestrianism, among others. In 2017, sponsorships included supporting Bahrain's Pro-Cycling team Merida, which participates in international cycling tours.

Customers with special needs

Integration and support for customers with special needs also ranks very highly in BBK's priorities, being the first bank to introduce ATMs for the visually impaired, as well as other special services such as sign language experts.

The Bank continues to invest in better accessibility to its facilities for those with special needs, focusing on constant enhancement that enables such customers to conduct their banking transactions independently and with as little complication as possible.

A typical example of BBK's policy in action is the Budaiya Financial Mall, where facilities for special needs customers include dedicated parking spaces, a permanent wheelchair access ramp, and tiles that guide visually impaired customers to the ATM and the Special Needs Priority Desk, lowered to cater for wheelchair users. BBK has also introduced Braille application forms, voice-over support for account opening, and an audio version of terms and conditions.

Special needs customers already have priority in the Bank's queuing system, as the reader that dispenses queue tickets is designed to recognise their special bank cards. They are also exempt from fees and charges on withdrawals at bank counters, as well as minimum account balance requirements.

Apart from its investment in facilities, BBK also allocates more than 15 percent of its total donation budget to special needs societies and associations.

Culture

The Bahrain Authority for Culture and Antiquities, and the Sheikh Ibrahim Bin Mohammed Al Khalifa Centre for Culture and Research, are the primary beneficiaries of BBK's contribution to supporting cultural organisations. The Bank also contributes to various initiatives for cultural preservation and the restoration of historical facilities, and once again co-sponsored the annual cultural and intellectual Spring of Culture movement, a festival that attracts many visitors to Bahrain.

Other philanthropic support

Renewed financial support for the Ministry of Social Development NGO Fund amounted to BD 30,000 during 2017. The fund provides grants to societies and charitable organisations for development initiatives. The Bank donated a further BD 150,000 to care homes for the elderly and organisations that benefit orphans, as well as other philanthropic societies.

Environmental initiatives

Reducing environmental impact is an ongoing project at BBK, with the Bank constantly seeking and implementing new ways to reduce its carbon footprint and contribute to environmental sustainability. Refining digital services plays an import role in the process, along with energy-saving practices and recycling of waste paper. BBK also supports the Supreme Council for Environment every year in its conservation work with Al Areen Wildlife Park.

Backing Bahrain's financial sector

BBK's status as a Domestic Systemically Important Bank (D-SIB) means that that the Bank has a major responsibility in the development of Bahrain's economy and financial sector, acting as a global ambassador for Bahrain. In this context, a leading bank initiative is to co-sponsor the annual reception for Bahraini banks at meetings of the International Monetary Fund and World Bank in Washington, a proud duty that was again carried out in 2017.

The Bank was also once again a lead sponsor of the sixth annual Euromoney GCC Financial Forum, hosted by the Bahrain Economic Development Board. More than 500 business leaders and policymakers from 24 countries attended the 2017 conference.

BBK's long-standing sponsorship of the Gulf region's first educational dealing room, established by the Bahrain Institute of Banking and Finance (BIBF), has continued, along with the Bahrain Bourse's Trade Quest competition – a stock trading simulation programme for high school students to help young Bahrainis learn about banking and investment.

Part II

Reports and disclosures

Good corporate governance is considered central to achieving the Bank's objectives, and fundamental in maintaining a leading position within the local and regional banking sectors.

BBK takes pride in ensuring exceptional standards of corporate governance are met. Our corporate governance policy is underpinned by international standards of best practice.

Initiatives in 2017

The organisational structure was further amended to ensure independence of the Compliance function, which now reports to the Board's Audit Committee, itself renamed as the Audit and Compliance Committee. The evaluation process for the Board and its committees was successfully completed, with recommendations for improvement such as focusing on strategic initiatives and continuing to update its knowledge.

The Board members were also given access to an e-learning platform to pursue further training if required. The Board approved a new Board committee, the Independent Directors' Committee, and approved its terms of reference to provide an independent view on issues discussed by the Board, and also to protect minority shareholder interests as they are not represented on the Board. The Board reviewed the Board Charter, Board Committees' Terms of Reference, the Corporate Governance framework, and other relevant policies to ensure they stay up to date and relevant.

Corporate governance philosophy

BBK shall continue its endeavour to enhance shareholders' value, protect their interests, and defend their rights by practising the pursuit of excellence in corporate life. The Bank shall not only comply with all statutory requirements – including the Corporate Governance Code of the Kingdom of Bahrain and the High Level Controls Module of the Central Bank of Bahrain – but also formulate and adhere to strong corporate governance practices.

BBK shall continuously strive to best serve the interests of its stakeholders, including shareholders, clients, employees, and the public at large.

The adoption and implementation of corporate governance is the direct responsibility of the Board of Directors, and this endeavour is in line with the policies of regulatory authorities and statutory requirements in the Kingdom of Bahrain and other countries where BBK operates.

Risk appetite statement

Risk appetite is the level and type of risk that the Bank is willing to assume in order to achieve its strategic and business objectives, keeping in perspective the obligations to its stakeholders.

The risk appetite of the Bank is both a qualitative and quantitative measure, and reflects its level of risk tolerance in normal as well as in stressed scenarios. It is expressed as a measurable key performance indicator (KPI), a tolerance limit, or as a qualitative guideline.

The Bank has a well-defined Risk Appetite Framework, that consists of the Risk Appetite Statement along with: (a) well-defined performance metrics in the form of Key Performance Indicators or KPIs; (b) risk limits, exposure criteria, restrictions and controls, lending and investment standards as laid out in the internal risk policies and procedures manual; (c) capital and liquidity benchmarks, which are monitored in the Asset Liability Management Committee meetings; (d) key business and risk management objectives, goals and strategy, which are defined in business, investment and risk management strategies; and (e) management and oversight structures in the Bank through Management and Board committees. Our risk appetite defines the desired performance levels, which, in turn, are embedded into management of the various risks within the Bank as well as the capital of the Bank. Our risk appetite is integrated into the strategic, capital, and risk management planning process across business verticals.

The Bank measures the contribution of each business vertical towards key KPIs.

The Bank aims to optimise the risk-reward for the benefit of all stakeholders, and this is reviewed and implemented through strategies (business, investment, risk management, ICAAP), which are closely reviewed annually. The Bank's primary exposure is to credit risk along with other Pillar 1 and Pillar 2 risks assumed in the normal course of its business. The risk appetite statement is also reviewed though a Risk Management Strategy document by management, and recommended for approval to the Risk Committee and the Board annually. The Bank's risk appetite requires, amongst other things:

- A high level of integrity, ethical standards, respect and professionalism in our dealings.
- Taking only those risks which are transparent and understood, and those which can be measured, monitored, and managed.
- Ensuring that the Bank has adequate levels of capital adequacy on an ongoing basis as mandated by the regulator (currently 12.5 percent), and as assessed by the Bank in its ICAAP document; that the capital requirements and capital planning are incorporated in its capital management strategy.
- Ensuring that the Bank has access to adequate levels of stable, efficient, and cost-effective funding to support liquidity and lending or investing requirements on an ongoing basis; that the Bank has in place a robust liquidity management framework and contingency plans to monitor and manage liquidity both in normal and stress liquidity conditions, in addition to monitoring key liquidity ratios (internal and regulatory) in Asset Liability Management Committee meetings on a monthly basis.
- Adhering to the core principles of lending, which are enshrined in the general lending policy of the Bank.
- Maintaining a robust credit management framework with focus on geographies where the Bank has physical presence (Kuwait, India, Dubai), GCC, and select MENA and other countries; undertaking exposures to countries within the directives of the Country Risk Committee, which reviews country risk and the Bank's strategy in those countries on a dynamic basis.
- Having in place a defined monitoring, collection and restructuring framework for effective recovery mechanism.
- Limiting exposures to high-risk activities which may culminate in tail-end risks, jeopardising the Bank's capital and creditworthiness.
- Striving for optimum profitability through income generation, cost efficiency, and low impairment.
- Widening the product basket and delivery channels for increasing customer satisfaction; assessing new credit products in a structured form for approval by appropriate authorities, so that the underlying risks, benefits, operational processes, system/technology requirements, and legal requirements are understood and managed.
- Protecting the Bank's and the customers' interests through robust operational procedures, internal controls, system support, training and operational risk management processes to mitigate operational risk.
- Ensuring full compliance with legal, statutory, and regulatory requirements; ensuring adherence to anti-money laundering (AML) and other obligations under international law; providing adequate training and guidance to mitigate compliance and AML risks.

Shareholder information

BBK's shares are listed on the Bahrain Bourse. The Bank has issued 1,081,647,952 equity shares, each with a face value of 100 fils. All shares are fully paid.

Annual Ordinary General Meeting and Extraordinary General Meeting

The Annual Ordinary General Meeting (AGM) and Extraordinary General Meeting (EGM) were held on 29 March 2017. The EGM resolved to approve increasing the Bank's branch in the State of Kuwait's paid up capital from KD 6MM to KD 15MM.

The EGM approved amendment to the Bank's Articles of Association to enable the Bank to issue perpetual convertible bonds. The shareholders approved 5 Board members appointed by major shareholders, and elected 7 more members to total 12 members on the Board. The minutes of the AGM and EGM are published in this annual report.

The Bank submits a corporate governance report to the AGM annually, covering the status on compliance with the related regulatory requirements. The Bank discloses and/or reports to the shareholders at the AGM the details under the Public Disclosure module of the Central Bank of Bahrain's Rule Book. Such disclosures include the total remuneration paid to the Board of Directors, the executive management and the external auditors. The total amount paid to directors and executive management is also contained in the annual report.

Board of Directors' information

Board composition

The Board's composition is based on the Bank's Memorandum of Association and Articles of Association, and comprises 12 members. The Board represents a mix of high-level professional skills and expertise. Furthermore, in compliance with corporate governance requirements, the Board Committees consist of members with adequate professional background and experience. Consequently, the Board has five independent Directors. The Board periodically reviews its composition and the contribution of Directors and Committees.

The appointment of Directors is subject to CBB approval. The classification of 'Executive' Directors, 'Non-Executive' Directors and 'Independent Non-Executive' Directors is as per definitions stipulated by the CBB. The current term of the Board started in March 2017 and ends in March 2020.

Directors are elected/appointed by shareholders at the AGM. Experts who are non-shareholders or promoters of the Bank may also be elected as Directors. Election or re-election of a Director at the AGM shall be accompanied by a recommendation from the Board, based on a recommendation from the Nomination, Remuneration, and Corporate Governance Committee, with specific information such as biographical and professional qualifications and other directorships held.

Group Corporate Secretary

The Board is supported by the Group Corporate Secretary, who provides professional and administrative support to the General Assembly, the Board, its Committees and members. The Group Corporate Secretary also assumes the responsibilities of the Group Corporate Governance Officer, and in this context supports the processes of performance evaluation for the Board, the Board Committees, and individual Directors as well as the process of access to independent advice and other relevant issues on a Group level. The appointment of the Group Corporate Secretary is subject to the approval of the Board.

BBK's Group Corporate Secretary is Ahmed A. Qudoos Ahmed, who joined the Bank in 2009. His qualifications include a BSc in Engineering from the University of Bahrain in 1996, he is qualified in Board Secretarial practices from George Washington University and he has attended many advance training programmes in corporate governance both in Bahrain and abroad, accumulating over 21 years of experience in the financial sector.

Directors' roles and responsibilities

The Board of Directors oversees the implementation of the Bank's strategic initiatives and its functioning within the agreed framework, in accordance with relevant statutory and regulatory structures. The Board ensures the adequacy of financial and operational systems and internal control, as well as the implementation of Corporate Ethics and the Code of Conduct.

The Board reserves a formal schedule of matters for its decision to ensure that the direction and control of the Bank rest with the Board. This includes strategic issues and planning, performance reviews, material acquisition and disposal of assets, capital expenditure, authority levels, appointment of auditors, and review of the financial statements, financing and borrowing activities including annual operating plan and budget, ensuring regulatory compliance, and reviewing the adequacy and integrity of internal controls.

The Board shall exercise judgement in establishing and revising the delegation of authority for Board Committees and Management. This delegation could be for authorisation of expenditure, approval of credit facilities, and for other corporate actions. Such delegation may be approved and expressed under various policies of the Bank. The thresholds for the identified authorities will depend upon the operating requirements of the Bank.

Shareholders

Name	Country of origin	Number of shares	% holding
Citizens of the Kingdom of Bahrain and Others	–	246,605,845	22.79
Ithmaar Bank	Kingdom of Bahrain	274,493,028	25.38
Social Insurance Organization (SIO)			
– Formerly Pension Fund Commission	Kingdom of Bahrain	203,020,288	18.77
– Formerly General Organization for Social insurance (GOSI)	Kingdom of Bahrain	144,294,820	13.34
Kuwait Investment Authority	State of Kuwait	202,229,987	18.70
Global Investment House	State of Kuwait	11,003,984	1.02

Distribution schedule of each class of equity

Category	Number of shares	Number of shareholders	% of outstanding shares
Less than 1%	246,605,845	2,377	22.79
1% to less than 5%	11,003,984	1	1.02
5% to less than 10%	–	–	–
10% to less than 20%	549,545,095	3	50.81
20% to less than 50%	274,493,028	1	25.38
50% and above	–	–	–

The issues of major capital expenditure, divestitures, mergers and acquisitions, and certain strategic investments would be within the Board's authority.

Each Director holds the position for three years, after which he must present himself to the Annual General Meeting of shareholders for reappointment. The majority of BBK Directors (including the Chairman and/or Deputy Chairman) are required to attend Board meetings in order to ensure a quorum. The Board Charter is published on the Bank's website.

Material transactions that need Board approval

Lending transactions to Directors, at a certain level of exposure, require Board approval. Also credit and investment applications exceeding certain pre-defined exposure levels require approval of the Board.

Similarly, related party transactions relating to members of the Board require approval of the Board.

Independent professional assistance

The Bank has procedures approved by the Board for allowing Board members to obtain independent professional advice relating to the affairs of the Bank or to their individual responsibilities as members, subject to approval by the Board.

Directors' induction and professional development

The Board is required to be up to date with current business, industry, regulatory, and legislative developments and trends that affect the Bank's business operations. Immediately after appointment, the Bank provides formal induction for a full day, and this year it was held on 30 March 2017.

Meetings will also be arranged with executive management. This will foster a better understanding of the business environment and markets in which the Bank operates. A continuing awareness programme is essential and it may take many different forms, through distribution of publications, workshops, presentations at Board meetings and attendance at conferences encompassing topics on directorship, business, industry, and regulatory developments. As per the Training and Competency Model of the CBB, each approved person (including members of the Board of Directors) is required to complete 15 hours of continued professional development.

Board and Committee evaluation

The Board performs a self-evaluation on an annual basis. The Board annually reviews its Charter and its own effectiveness, and initiates suitable steps for any amendments. The Board will also review self-evaluations of individual Board members and the Board Committees and consider appropriately any recommendations arising out of such evaluation. The relevant policy is published on the Bank's website.

Remuneration of Directors

The Board has adopted a remuneration policy for Directors with well-defined procedures to apply to the Directors' various remuneration and compensation components, reflective of their involvement and contributions in the activities of the Board of Directors and its ad hoc, temporary and permanent committees. The basic guideline of the policy is that participation would be considered in terms of attendance at meetings. Participation in a meeting via telephone/video conference shall be considered an attendance of the meeting. Members of the Board are treated equally when they are compensated for additional work or effort in their participation. Directors' remuneration is governed by Commercial Companies Law No 21 for the year 2001, and therefore all payments comply with the provision of the law.

Whistle-blowing policy

The Bank has a whistle-blowing policy with designated officials whom the employee can approach.

The policy provides adequate protection for the employees for any reports made in good faith. The Board's Audit Committee oversees this policy. The whistle-blowing policy is published on the Bank's website.

Key persons (KP) policy

The Bank has established a 'Key Persons' policy to ensure that key persons are aware of the legal and administrative requirements regarding holding and trading of BBK shares, with the primary objective of preventing abuse of inside information. Key persons are defined to include the Directors, executive management, designated employees, and persons under guardianship or control of Key Persons. The ownership of the Key Persons policy is entrusted to the Board's Audit Committee. The Key Persons policy is posted on the Bank's website.

Code of Conduct

The Board has an approved Code of Conduct for BBK Directors. The Board has also approved a Code of Ethics for the Executive Management and employees. These codes outline areas of conflict of interest, confidentiality, and the responsibilities of signatories to adhere to best practices. The high-level responsibility for monitoring the codes lies with the Board of Directors. The Directors' Code of Conduct is published on the Bank's website.

Relative Recruitment/Appointment Policy

The Bank has in place policies that govern the recruitment/appointment of relatives in the Bank and across its wholly owned subsidiaries. The policies are as follows:

1. Employment of relatives of first and second degrees shall be prohibited, whereas employment of relatives of third and fourth degree may be approved by the management provided it does not lead to a conflict of interest.

2. Employment of relatives at the Bank's fully owned subsidiaries of first and second degree shall be prohibited for Senior Managers and above; any exception must approved by the Chief Executive.

As part of the annual reporting, the Chief Executive must disclose to the Board of Directors on an annual basis those individuals who are occupying controlled functions and who are relatives of any other approved persons within the Bank and its wholly owned subsidiaries.

Conflict of interest

The Bank has a documented procedure for dealing with situations involving conflict of interest of Directors. In the event of the Board or its Committees considering any issues involving conflict of interest of Directors, decisions are taken by the full Board/Committees.

The concerned Director shall leave the meeting room during the discussion of these issues. These events are recorded in the Board/Committee proceedings. The Directors are required to inform the entire Board of conflicts of interest (potential or otherwise) in their activities with, and commitments to, other organisations as they arise, and to abstain from voting on the matter. This disclosure includes all material facts in the case of a contract or transaction involving the Director.

Development programmes arranged for Board members during 2017

Key: ⊙ Attended O Absent

Board of Directors	Course: "Independent board members definition – role and function" Date: 22/5/2017 2.5 hours	Course: "Impact of cyber risk and the importance of cyber security" Date: 22/5/2017 2.5 hours	Course: "The role of the Board in setting and reviewing implementation of the strategy for the organization" Date: 18/09/2017 2.5 hours	Course: "Blockchain, what it is, how it can affect our business and future outlook" Date: 18/09/2017 2.5 hours	Course: "Training on BoardWorks" Date: 20/11/2017 2.5 hours	Course: "Board performance evaluation" Date: 20/11/2017 2.5 hours	Other training hours or outside the Bank
Murad Ali Murad	⊙	⊙	⊙	⊙	⊙	⊙	–
Aref Saleh Khamis*	O	O	O	O	O	O	More than 15 hours
Mohamed A.Rahman Hussain*	⊙	⊙	⊙	⊙	O	⊙	9 hours
Jassem Hasan Ali Zainal	⊙	⊙	O	O	⊙	⊙	–
Dr. Zakareya Sultan AlAbbasi*	O	O	O	O	O	O	6 hours
Sh. Abdulla Khalifa Salman Al-Khalifa*	O	O	O	O	O	O	More than 15 hours
Sh. Khalifa Bin Duaij Al Khalifa	O	O	O	O	O	O	More than 15 hours
Marwan Mohammed Al Saleh*	⊙	⊙	⊙	⊙	O	O	More than 15 hours
Yusuf Saleh Khalaf*	⊙	⊙	⊙	⊙	O	⊙	1 hour
Edrees Musaed Ahmad*	⊙	⊙	O	O	⊙	⊙	More than 15 hours
Hani Ali Al Maskati	⊙	⊙	⊙	⊙	O	⊙	–
Ashraf Adnan Bseisu*	⊙	⊙	⊙	O	⊙	⊙	13 hours

* Attended other training sessions or sessions outside the Bank

Corporate social responsibility

BBK's contribution towards the well-being of the community is an integral part of its corporate role. This corporate social responsibility is translated by the Bank through annual appropriation of a budget allocated for donations to finance community-related projects and initiatives. The projects may vary in nature but ought to fall into any one of the following fields: charity, culture, research, education, philanthropy, environmental protection, and sports.

BBK has an approved high-level donation policy for the distribution of the donation budget. The policy outlines guiding principles and sets criteria for the evaluation and selection of donation requests, with the ultimate objective of maximising the return on both the Bank's social image and the benefit of the community.

Disclosures relating to the Board of Directors

Directors' external appointments

Murad Ali Murad		
Chairman of the Board	Bahrain Kuwait Insurance Company (BSC)	Kingdom of Bahrain
Vice Chairman	Bahrain Institute of Banking & Finance (BIBF)	Kingdom of Bahrain
Chairman of the Board	Al Janabeya Company WLL (Family Company)	Kingdom of Bahrain

Aref Saleh Khamis		
Undersecretary	Ministry of Finance	Kingdom of Bahrain
Chairman	Social Insurance Organization (SIO)	Kingdom of Bahrain
Deputy Chairman	Future Generation Fund – Ministry of Finance	Kingdom of Bahrain
Deputy Chairman	Bahrain – Qatar Causeway Foundation	Kingdom of Bahrain
Member	Rashid Equestrian & Horse Racing Club	Kingdom of Bahrain
Member	Supreme Council for Health	Kingdom of Bahrain
Member	Sh Mohammed bin Khalifa bin Salman Al Khalifa Cardiac Centre	Kingdom of Bahrain
Member	King Hamad Hospital Consultative Board	Kingdom of Bahrain

Mohamed Abdulrahman Hussain		
Vice-Chairman and Chairman of Executive Committee	Eskan Bank BSC	Kingdom of Bahrain
Board Member	Investcorp Saudi Arabia Financial Investment Company	Kingdom of Saudi Arabia
Board Member	The K Hotel WLL	Kingdom of Bahrain
Board Member and Chairman of Audit Committee	Gulf Union Insurance and Reinsurance Company BSC	Kingdom of Bahrain

Directors' external appointments (continued)

Jassem Hasan Ali Zainal		
Vice Chairman and CEO	Arzan Financial Group for Financing and Investment	State of Kuwait
Deputy Chairman and Acting CEO	Addax Investment Bank	Kingdom of Bahrain
Board Member	Kuwait International Bank	State of Kuwait
Board Member	Al-Masah Capital Limited	Dubai, UAE
Board Member	Miami International Securities Exchange LLC (MIAX)	United States of America

Dr Zakareya Sultan AlAbbasi		
Board Member	Osool Asset Management BSC	Kingdom of Bahrain
Board Member	Eskan Bank BSC	Kingdom of Bahrain

Sh Abdulla bin Khalifa bin Salman Al Khalifa		
Chief Executive Officer	Osool Asset Management BSC	Kingdom of Bahrain
Chairman	Securities & Investment Company (SICO) BSC	Kingdom of Bahrain
Board Member and Chairman of the Executive Committee	Amlak Social Insurance Organization Development Company SPC	Kingdom of Bahrain
Board Member and Chairman of the Executive Committee	Bahrain Marina Development Company SPC	Kingdom of Bahrain
Board Member and Chairman of the Executive Committee	Amanat Holdings PJSC	United Arab Emirates

Sh Khalifa bin Duaij Al Khalifa		
President	Court of HRH the Crown Prince	Kingdom of Bahrain
Board Member	Crown Prince's International Scholarship Programme	Kingdom of Bahrain
Board Member	Isa Bin Salman Educational Charitable Trusts	Kingdom of Bahrain
Board Member	Palm Capital Company WLL	Kingdom of Bahrain
Board Member	Arab Thought Foundation	Lebanon

Marwan Mohammed Al Saleh		
Director of Fixed Income	Kuwait Investment Authority	State of Kuwait

Edrees Musaed Ahmad		
Assistant Investment Manager	Kuwait Investment Authority (KIA) Employee	State of Kuwait

Hani Ali Al Maskati		
Co-Founder & Managing Partner	Cash Management Matters - CMM	Kingdom of Bahrain
Board Member Chairman of Audit committee Member of Nomination, Remuneration & Governance Committee	Al Ahlia Insurance Company	Kingdom of Bahrain
Chairman of the Audit Committee	Solidarity Saudi Takaful Company	Kingdom of Saudi Arabia
Board Member	Blu Solution Limited	British Virgin Islands

Yusuf Saleh Khalaf		
Managing Director	Vision Line Consulting WLL	Kingdom of Bahrain

Ashraf Adnan Bseisu		
Group Chief Executive	Solidarity Group Holding Company (B.S.C.)	Kingdom of Bahrain
Chairman	Solidarity First Insurance Company (P.L.C)	Hashemite Kingdom of Jordan
Vice Chairman	Solidarity General Takaful Company (B.S.C.)	Kingdom of Bahrain
Board Member	Solidarity Saudi Takaful Company	Kingdom of Saudi Arabia
Board Member	Bahrain Institute of Banking & Finance (BIBF)	Kingdom of Bahrain
Board Member	Trustees of the Human Resources Development Fund	Kingdom of Bahrain

Directors' and related parties' interests

The number of securities held by Directors as of 31 December 2017 was as follows:

Name of Director	Type of shares	31 Dec 2017	31 Dec 2016	Bonds 31 Dec 2017	Bonds 31 Dec 2016
Murad Ali Murad	Ordinary	853,977	853,977	197,778	197,778
Aref Saleh Khamis	Ordinary	–	–	–	–
Mohamed Abdulrahman Hussain	Ordinary	153,402	153,402	–	–
Jassem Hasan Ali Zainal	Ordinary	190,286	190,286	30,000	30,000
GOSI/Dr Zakareya Sultan AlAbbasi (1)	Ordinary	127,050	127,050	11,746	11,746
Sh Abdulla bin Khalifa bin Salman Al Khalifa	Ordinary	127,050	127,050	50,000	50,000
Sh Khalifa bin Duaij Al Khalifa	Ordinary	138,326	138,326	–	–
Marwan Mohammed Al Saleh	–	–	–	–	–
Kuwait Investment Authority/Mutlaq Mubark Al Sanei (2)	Ordinary	127,050	127,050	11,746	11,746
Ithmaar Bank/Elham Ebrahim Hasan (3)	Ordinary	127,050	127,050	11,746	11,746
Yusuf Saleh Khalaf	Ordinary	152,050	152,050	39,057	39,057
Ithmaar Bank/Hassan Mohammed Mahmood (3)	Ordinary	127,050	127,050	11,746	11,746

(1) Shares related to Dr Zakareya Sultan AlAbbasi are part of the whole shares of the General Organisation for Social Insurance (GOSI) ownership.
(2) Shares related to Mutlaq Mubarak Al Sanei are part of the whole shares of the Kuwait Investment Authority ownership.
(3) Shares related to Elham Ebrahim Hasan and Hassan Mohammed Mahmood are part of the whole shares of Ithmaar Bank ownership.

Related parties

Al Janabeya Company WLL (a family company owned by Mr Murad Ali and his family) owns 987,825 shares, 91,326 bonds and is related to the Chairman of the Board.

Nature and extent of transactions with related parties

None.

Approval process for related parties' transactions

The Bank has a due process for dealing with transactions involving Directors and related parties. Any such transaction will require the approval of the Board of Directors.

Material contracts and loans involving Directors

Name of the Director	Relationship with Director	Purpose of loan	Amount of loan	Interest Rate	Terms of payment of interest	Repayment of the principal	Security
Murad Ali Murad	Chairman	Personal banking needs	BD 300,000	Fixed deposit rate over 1% p.a.	On demand	On demand	100% cash collateral
Jassem Hasan Ali Zainal	Board Member	Personal banking needs	USD 66,000	LIBOR + 3%	On demand	On demand	Shares 43% plus fixed deposit of 3%
			BD 115,000	BIBOR + 3%			
Yusuf Saleh Khalaf	Board Member	Personal banking needs	BD 50,000	BIBOR + 3%	Monthly	On demand	Clean

Note: The materiality amount for such disclosures is considered above BD 100,000.

Directors' trading of BBK shares during 2017

None.

Board meetings

The Board of Directors meet at the summons of the Chairman (or Deputy Chairman in event of his absence or disability) or, if requested to do so, by at least two Directors. The Board meets at least four times a year. A meeting of the Board of Directors is deemed valid if attended by more than half of the members.

Meetings of Independent Directors

Since 2012 the Board of Directors has held separate meetings for Independent Directors. As per the Board Charter, minority shareholders look to Independent Directors for representation.

For this purpose, regular Board meetings are preceded by a meeting of Independent Directors, unless it is decided by the Independent Directors that there are no issues to discuss.

The agendas for this forum's meetings are the same as the agendas for the regular Board meetings. During these meetings the Independent Directors express their views about certain issues, especially those relating to minority shareholders. The summary of the proceedings of such meetings is recorded by the Group Corporate Secretary and shared with the Independent Directors.

Board meeting attendance

During 2017, seven Board meetings were held in the Kingdom of Bahrain in the following manner:

Key: ⊙ Attended ○ Absent ⦸ was not a member during this period

Board meetings 2017

	Quarterly meetings				Other meetings		
Members	27 Feb	24 Apr	17 Jul	23 Oct	*28 Feb	29 Mar	11 Dec
Murad Ali Murad	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Aref Saleh Khamis	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Mohamed Abdulrahman Hussain	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Jassem Hasan Ali Zainal	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Dr Zakreya Sultan AlAbbasi	⊙	○	⊙	⊙	⊙	⊙	⊙
Sh Abdulla bin Khalifa bin Salman Al Khalifa	⊙	○	⊙	⊙	⊙	⊙	⊙
Sh Khalifa bin Duaij Al Khalifa	○	⊙	○	⊙	○	⊙	⊙
Marwan Mohammed Al Saleh	⊙	⊙	○	⊙	⊙	⊙	⊙
Yusuf Saleh Khalaf	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Mutlaq Mubarark Al Sanei	⊙	⦸	⦸	⦸	○	⦸	⦸
Elham Ebrahim Hasan	⊙	⦸	⦸	⦸	⊙	⦸	⦸
Hassan Mohammed Mahmood	⊙	⦸	⦸	⦸	⊙	⦸	⦸
Edrees Musaed Ahmad	⦸	⊙	⊙	⊙	⦸	⊙	⊙
Hani Ali Al Maskati	⦸	⊙	⊙	⊙	⦸	⊙	⊙
Ashraf Adnan Bseisu	⦸	⊙	○	⊙	⦸	⊙	⊙

* The 3-year strategy review meeting was held on 28 February 2017

Major issues discussed by the Board during 2017

(Subjects that fall under the Board Committee's scope are recommended by the respective Board Committee for the Board's approval.)

Date of meeting	Subject
27 February 2017	1. Appointment or re-appointment of Share Registrar 2. Corporate Governance report to AGM 3. BBK's Sharia Supervisory Board Terms of Reference 2016 4. Quarterly Liquidity Report 5. Investment Portfolio performance 6. Financial Results for Fourth Quarter of 2016 7. Re-appointment of External Auditors and their fees 8. CBB Examination Report and Banks' Responses 9. Anti-Money Laundering annual report 2016 10. HR Policy Amendments 11. Succession Plan 12. Risk Policies for review
28 February 2017	1. The Bank's strategy for the 3-year period 2016-2018
29 March 2017	1. Board Chairmanship and Board Committees' Composition 2. Board Evaluation
24 April 2017	1. Review of the Board Charter 2. Financial Results for First Quarter of 2017 and reviewing related press release 3. Cyber Security 4. Review of the Audit Committee's Terms of Reference 5. Investment Strategy 6. Risk Policies for review

Date of meeting	Subject
17 July 2017	1. Review of the Bank's Strategy for the years 2016 to 2018 2. Financial Results for Second Quarter of 2017 and reviewing related press release 3. CBB Examination Report 2016 4. Review of the Whistle-Blowing Policy 5. Review of the Key Persons Trading Policy 6. Audit and Compliance Committee Terms of Reference 7. Quarterly Liquidity Report 8. Appointment of Chief Risk Officer 9. Risk Committee Terms of Reference 10. Risk Policies for review
23 October 2017	1. Review of the Bank's Strategy for the years 2016 to 2018 2. Financial Results for Third Quarter of 2017 and reviewing the related press release 3. Update to AML Policy and Procedures 4. Review of Corporate Governance Framework 5. Succession Planning 6. Risk Policies for review
11 December 2017	1. Stress Testing 2. CBK Inspection Report 3. Medium Term Repo Funding 4. Treasury Management Report – Buyback Treasury Shares 5. The Budget For The Year 2018

Board committees

The Board Committees are formed and their members are appointed by the Board of Directors each year after the Annual General Meeting. They are considered the high-level link between the Board and the Executive Management. The objective of these Committees is to assist the Board in supervising the actual operations of the Bank, by reviewing any issues that are submitted by the Executive Management and making recommendations to the Board for their final review.

The Board reserves the right to form temporary Committees and discontinue them from time to time, as necessary. Furthermore, members of the Board are provided with copies of the meeting minutes of the said Committees, as required by the regulators. There are no significant issues of concern to report relating to the work of the Board Committees during the year 2017.

The full text of the Terms of Reference for Board Committees (Executive Committee, Audit and Compliance Committee, Nomination, Remuneration and Corporate Governance Committee, and Risk Committee) are published on the Bank's website.

Board Committees' composition, roles and responsibilities

Executive Committee

Members	Summary terms of reference, roles and responsibilities	Summary of responsibilities
Mohamed Abdulrahman Hussain Chairman **Aref Saleh Khamis** Deputy Chairman **Sh Abdulla bin Khalifa bin Salman Al Khalifa** Member **Yusuf Saleh Khalaf** Member since March 2017 **Ashraf Adnan Bseisu** Member since March 2017 **Reyadh Yousif Safer** Member **Mutlaq Mubarak Al Sanei** Member until March 2017 **Elham Ebrahim Hasan** Member until March 2017	• Not less than 5 members are appointed for a 1-year term • Minimum number of meetings required each year: 8 (actual meetings in 2017: 13) • The Chairman and Deputy Chairman must be a Director and elected by the members of the Committee in the first meeting following the appointment of its members • The quorum shall be more than half of the members and must include the Chairman or the Deputy Chairman Attendance by proxies is not permitted • The Chairman or Deputy Chairman shall be available at the Annual General Meeting to answer questions relating to the Committee's functions • The Committee conducts an annual self-assessment of the performance of the Committee/members, and reports conclusions and recommendations to the Board	Reviews, approves and directs the executive management on matters raised to the Board of Directors such as business plans, donations, credit/ investment applications, and such other proposals within its authority, and the periodic review of the Bank's achievements

Audit and Compliance Committee

Members	Summary terms of reference, roles and responsibilities	Summary of responsibilities
Murad Ali Murad Chairman (Independent) **Jassem Hasan Zanial** Deputy Chairman (Independent) **Sh Khalifa bin Duaij Al Khalifa** Member (Independent) **Edrees Musaed Ahmad** Member since March 2017	• The Board appoints not less than 3 members for a 1-year term • The Chairman must be elected by the members of the Committee, from amongst the Independent Non-Executive Directors, in its first meeting after the appointment of the members; the majority of members should also be independent • Minimum number of meetings required each year: 4 (actual meetings in 2017: 4) • Quorum shall be more than half of the members and must include the Chairman. Attendance by proxies is not permitted • The Chairman or Deputy Chairman shall be available at the Annual General Meeting to answer questions relating to the Committee's functions • The Committee conducts an annual self-assessment of the performance of the Committee/members, and reports conclusions and recommendations to the Board	Reviews the internal audit programme and internal control system, considers major findings of internal audit reviews, investigations and management's response, ensures coordination among internal and external auditors, monitors trading activities of key persons, and ensures prohibition of the abuse of inside information and disclosure requirements Approves and periodically reviews the Internal Audit Charter Document, which defines the purpose, authority, responsibilities and other aspects of the internal audit activity

Nomination, Remuneration and Corporate Governance Committee

Members	Summary terms of reference, roles and responsibilities	Summary of responsibilities
Murad Ali Murad Chairman (Independent) **Sh Khalifa bin Duaij Al Khalifa** Deputy Chairman (Independent) **Marwan Mohammed Al Saleh** Member **Mohamed Abdulrahman Hussain** Member since March 2017 (Independent)	• The Board appoints not less than 3 members for a 1-year term. The Chairman is an Independent Director and the majority of members should also be independent • The Chairman and the Deputy Chairman must be elected by members of the Committee in its first meeting after the appointment of the members • Minimum number of meetings required each year: 2 (actual meetings in 2017: 4) • Quorum shall be more than half of the members and must include the Chairman or the Deputy Chairman. Attendance by proxies is not permitted • The Chairman or Deputy Chairman shall be available at the Annual General Meeting to answer questions relating to the Committee's functions • The Committee conducts an annual self-assessment of the performance of the Committee/members, and reports conclusions and recommendations to the Board	Assess, evaluate and advise to the Board of Directors on all matters associated with nominations and remunerations of the Directors and the Executive Management. Also, to ensure that the Bank adopts and enhances sound corporate governance practices, which are consistent with the Corporate Governance Code of the Kingdom of Bahrain and the regulatory requirements, and which also reflect best market practices in corporate governance, and makes recommendations to the Board as appropriate

Risk Committee

Members	Summary terms of reference, roles and responsibilities	Summary of responsibilities
Hani Ali Al Maskati Chairman (Non-executive) **Jassem Hasan Ali Zainal** Deputy Chairman (Independent) **Dr Zakareya Sultan AlAbbasi** Member **Edrees Musaed Ahmad** Member since March 2017	• At least 4 members are appointed for a 1-year term • The Chairman and Deputy Chairman must be a Director and elected by the members of the Committee in its first meeting following the appointment of its members • Minimum number of meetings required each year: 4 (actual meetings in 2017: 4) • The quorum shall be more than half of the members and must include the Chairman or the Deputy Chairman. Attendance by proxies is not permitted • The Chairman or Deputy Chairman shall be available at the Annual General Meeting to answer questions relating to the Committee's functions • The Committee conducts an annual self-assessment of the performance of the Committee/members and reports conclusions and recommendation to the Board	Reviews risk policies and recommends to the Board of Directors for approval. Also examines and monitors the risk issues to the Bank's business and operations and directs the management appropriately

Independent Directors Committee

Members	Summary terms of reference, roles and responsibilities	Summary of responsibilities
Murad Ali Murad Chairman (Independent) **Jassem Hasan Zanial** Member (Independent) **Sh Khalifa bin Duaij Al Khalifa** Member (Independent) **Mohammed Abdulrahman Hussain** Member (Independent) **Yusuf Saleh Khalaf** Member (Independent)	• The Committee is composed of Independent Directors • The Committee meets at least once a year • The meetings are attended by Independent Directors and the Group Corporate Secretary only • Attendance should be in person • The Committee discusses issues on the Board agenda according to its terms	Providing independent views on certain issues, especially pertaining to minority shareholders

Board Committee meetings and record of attendance

Key: ⊙ Attended ○ Absent ⊘ was not a member during this period

Executive Committee meetings in 2017

Members	5 Feb	5 Mar	*23 Mar	23 Apr	21 May	11 Jun	16 Jul	12 Sep	9 Oct	*2 Nov	*9 Nov	19 Nov	10 Dec
Mohamed Abdulrahman Hussain	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Aref Saleh Khamis	⊙	⊙	○	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Sh Abdulla bin Khalifa bin Salman Al Khalifa	⊙	⊙	○	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Mutlaq Mubarak Al Sanei	○	○	⊙	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘
Elham Ebrahim Hasan	⊙	⊙	⊙	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘
Reyadh Yousif Sater	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Ashraf Adnan Bseisu	⊘	⊘	⊘	⊙	⊙	⊙	○	⊙	⊙	⊙	⊙	⊙	○
Yusuf Saleh Khalaf	⊘	⊘	⊘	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙

* Unscheduled meetings

Audit and Compliance Committee meetings in 2017

Members	19 Feb	23 Apr	16 Jul	22 Oct
Murad Ali Murad	⊙	⊙	⊙	⊙
Sh Khalifa bin Duaij Al Khalifa	⊙	○	○	⊙
Jassem Hasan Ali Zainal	⊙	⊙	⊙	⊙
Edrees Musaed Ahmad	⊘	⊙	⊙	⊙
Hassan Mohammed Mahmood	⊙	⊘	⊘	⊘
Yusuf Saleh Khalaf	⊙	⊘	⊘	⊘

Nomination, Remuneration and Corporate Governance Committee meetings in 2017

Members	20 Feb	8 Mar	8 Oct	*19 Nov
Murad Ali Murad	⊙	⊙	⊙	⊙
Mohamed Abdulrahman Hussain	⊘	⊘	⊙	⊙
Sh Khalifa bin Duaij Al Khalifa	⊙	⊙	⊙	⊙
Marwan Mohammed Al Saleh	⊙	⊙	○	⊙

* Unscheduled meetings

Risk Committee meetings in 2017

Members	20 Feb	18 Apr	9 Jul	9 Oct
Murad Ali Murad	⊙	⊘	⊘	⊘
Jassem Hasan Ali Zainal	⊙	⊙	⊙	⊙
Dr Zakareya Sultan AlAbbasi	⊙	⊙	⊙	⊙
Yusuf Saleh Khalaf	⊙	⊘	⊘	⊘
Edrees Musaed Ahmad	⊘	⊙	⊙	⊙
Hani Ali Al Maskati	⊘	⊙	⊙	⊙

Independent Directors' Committee meetings in 2017

Members	27 Feb
Murad Ali Murad	⊙
Jassem Hasan Ali Zainal	⊙
Sh Khalifa bin Duaij Al Khalifa	⊙
Mohamed Abdulrahman Hussain	⊙
Yusuf Saleh Khalaf	⊙

Compliance and anti-money laundering

Compliance with regulatory and statutory requirements is an ongoing process. The Bank is conscious of its responsibilities in observing all regulatory provisions and best international practices in its functioning. The Bank has established an independent compliance function in keeping with Basel and CBB guidelines. The unit acts as a focal point for all regulatory compliance and for adapting other best practice compliance principles. The Bank continuously strives to improve the level of compliance in all its activities. The Bank's adopted corporate philosophy is: 'BBK shall continue its endeavour to enhance shareholders' value, protect their interests and defend their rights by practising pursuit of excellence in corporate life.' Anti-money laundering measures form an important area of the compliance function, in addition to areas of corporate governance, disclosure standards, insiders'/key persons' trading, conflict of interest, and adherence to best practices.

Starting from 2014, the Bank commenced implementation of an automated compliance system for the monitoring and management of regulatory requirements across the Bank. This system facilitates the prompt reporting of any compliance concerns or non-compliance incidents as and when they arise. In 2017, the system was rolled over to most concerned divisions as part of the system overall implementation across the Bank.

The Bank has documented an anti-money laundering programme, including periodic awareness training to employees, record-keeping, and a designated Money Laundering Reporting Officer (MLRO). The AML policy and procedures are updated annually and were last approved by the Board of Directors in October 2017.

The Bank has deployed a risk-based automated transaction monitoring system in keeping with the anti-money laundering regulations of the CBB. In 2017, an upgrade of the Bank's AML monitoring system has been initiated.

The Bank's anti-money laundering measures are regularly audited by the internal auditors, who report to the Audit and Compliance Committee of the Board. The Central Bank performs periodic inspections of the Bank's compliance with anti-money laundering regulations; the last AML/CFT examination by the Central Bank was concluded in October 2016. Additionally, the Bank's anti-money laundering measures are audited by independent external auditors every year and their report is submitted to the CBB. The overseas branches in India and Kuwait and the subsidiary, CrediMax, have designated compliance and MLRO functions to ensure implementation of local regulations and also to meet CBB requirements as applicable. The Bank is committed to combating money-laundering and, towards this end, implements all 'Prevention of Money Laundering Regulations' as stipulated in the Financial Crimes Module of the CBB Rulebook and other guidelines issued by the CBB. These regulations and guidelines are consistent with the revised FATF recommendations, 'Customer Due Diligence for Banks' paper of the Basel Committee, and best international practices.

Communication strategy

The Bank has an open policy on communication with its stakeholders, and has adopted a communication disclosure policy consistent with Basel II requirements. Shareholders are invited by the Chairman to attend the annual general meeting (AGM). The Chairman and other Directors attend the AGM and are available to answer any questions. The Bank is at all times mindful and conscious of its regulatory and statutory obligations regarding dissemination of information to its stakeholders.

The Bank provides information on all events that merit announcement, either on its website – www.bbkonline.com – or through other forms of publication. The Bank's annual report and three years' financial statements are also published on the website, as well as the Bank's Corporate Governance Report, Corporate Governance Framework, Whistle-blowing Policy, Board Charter, Code of Conduct, Key Persons' Dealing Policy, and Terms of Reference of all Board Committees. Shareholders can complete an online form, which can be found on the website, to forward any queries they may have.

The Bank uses a bulletin board for communicating with its employees on general matters, and sharing information of common interest and concern.

The Bank follows a total compensation approach to remuneration. This includes the Bank's variable remuneration policy for rewarding performance as well as providing competitive fixed remuneration for attracting and retaining talent.

In 2014, the Bank adopted regulations concerning sound remuneration practices issued by the Central Bank of Bahrain and consequently revised its variable remuneration framework. The revised policy framework and incentive components were approved by the shareholders in their Annual General Meeting on March 10th, 2015.

The key features of the remuneration framework are summarised below.

Remuneration strategy

The Bank's basic compensation philosophy is to provide a competitive level of total compensation to attract and retain qualified and competent employees. The Bank's variable remuneration policy is driven primarily by a performance-based culture that aligns employee interests with those of the shareholders of the Bank. These elements support the achievement of the objectives through balancing rewards for both short-term results and long-term sustainable performance. The strategy is designed to share the success of the Bank and to align employees' incentives with the risk framework and risk outcomes.

The quality and long-term commitment of all of the employees is fundamental to the success of the Bank. We therefore aim to attract, retain and motivate the very best people who are committed to maintaining a career with the Bank, and who will perform their role in the long-term interests of our shareholders. The Bank's reward package comprises the following key elements:

1 Fixed pay

2 Benefits

3 Annual (short term) performance bonus

4 Annual (long term) performance bonus

5 Subsidiaries Board Remuneration

A robust and effective governance framework ensures that the Bank operates within clear parameters of its compensation strategy and policy. All compensation matters, and overall compliance with regulatory requirements, are overseen by the Board Nomination, Remuneration and Corporate Governance Committee (NRCG).

The Bank's remuneration policy in particular considers the role of each employee and sets the criteria to determine whether an employee is a material risk-taker and/or an approved person in a business line, control or support function.

An approved person is an employee whose appointment requires prior regulatory approval because of the significance of his role within the Bank, and an employee is considered a material risk-taker if they are the head of a significant business line or any individuals within their control who have a material impact on the Bank's risk profile.

In order to ensure alignment between what we pay our people and our business strategy, we assess individual performance against annual and long-term financial and non-financial objectives summarised in our performance management system.

This assessment also takes into account adherence to the Bank's values, risks and compliance measures, and, above all, integrity. Altogether, performance is therefore judged not only on what is achieved over the short and long term, but also importantly on how it is achieved in order to ensure long-term sustainability of the business.

Nomination, Remuneration and Corporate Governance Committee (NRCG) role and focus

The NRCG has oversight of all reward policies for the Bank's employees. The NRCG is the supervisory and governing body for compensation policy, practices, and plans. It is responsible for determining, reviewing, and proposing variable remuneration policy for approval by the Board. It is responsible for setting the principles and governance framework for all compensation decisions. The NRCG ensures that all persons must be remunerated fairly and responsibly. The remuneration policy is reviewed on a periodic basis to reflect changes in market practices, the business plan, and risk profile of the Bank.

The responsibilities of the NRCG with regards to the Bank's variable remuneration policy, as stated in its mandate, include but are not limited to the following:

• Approve, monitor and review the remuneration system to ensure the system operates as intended.

• Review and recommend remuneration for the approval of the Board.

• Approve the remuneration amounts for each approved person and material risk-taker, as well as total variable remuneration to be distributed, taking account of total remuneration including salaries, contributions, expenses, bonuses and other employee benefits.

• Recommend the Chief Executive's remuneration for the Board of Directors' approval.

• Ensure remuneration is adjusted for all types of risks and that the remuneration system takes into consideration employees that generate same short-run profit but take different amount of risk on behalf of the Bank.

• Ensure that for material risk-takers, variable remuneration forms a substantial part of their total remuneration.

• Review the stress testing and back testing results before approving the total variable remuneration to be distributed including salaries, fees, expenses, bonuses, and other employee benefits.

• Carefully evaluate practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. The NRCG will question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payment.

• Ensure that for approved persons in risk management, internal audit, operations, financial control, and compliance functions, the mix of fixed and variable remuneration is weighted in favour of fixed remuneration.

• Recommend Board member remuneration based on their attendance and performance and in compliance with Article 188 of the Bahrain Commercial Companies Law.

• Ensure appropriate compliance mechanisms are in place to ensure that employees commit themselves not to use personal hedging strategies or remuneration and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements.

NRCG Members

As outlined in the Corporate Governance section of the annual report, the Board is satisfied that all Directors are non-executive and that the majority of the NRCG members are independent including the Chairman of the Committee. The NRCG comprises the following members:

NRCG member name	Appointment date	Number of meetings attended in 2017
Murad Ali Murad	21 March 1999	4
Sh Khalifa bin Duaij Al Khalifa	27 February 2005	4
Marwan Mohammed Al Saleh	30 December 2014	4
Mohamed Abdulrahman Hussain*	2 March 2008	2

*Became a member in the committee on 29 March 2017

The aggregate remuneration paid to NRCG members during the year in the form of sitting fees amounted to BHD 8,000 [2016: BHD 7,000].

External consultancy

A consultant was appointed during the year to review and enhance the variable remuneration polices and align them with market and best practices.

Scope of application of the remuneration policy

The variable remuneration policy is adopted on a group basis covering BBK Bahrain and BBK Kuwait. BBK India is excluded from the policy because they follow the Reserve Bank of India in this regard. Invita and CrediMax are excluded because the new guidelines are not applicable to them.

Board remuneration

The Bank's Board remuneration is determined in line with the provisions of Article 188 of the Bahrain Commercial Companies Law, 2001. The Board of Directors' remuneration will be capped so that total remuneration (excluding sitting fees) does not exceed 10 percent of the Bank's net profit after all required deductions in any financial year. Board remuneration is subject to approval of the shareholders in the annual general meeting. Remuneration of non-executive Directors does not include performance-related elements such as grants of shares, share options or other deferred stock-related incentive schemes, bonuses, or pension benefits.

Employees' variable remuneration

Variable remuneration is performance-related and consists primarily of the annual performance bonus award and long-term incentives for future performance. As a part of our staff's variable remuneration, the annual bonus rewards delivery of operational and financial targets set each year, the individual performance of the employees in achieving those targets, and their contribution to delivering the Bank's strategic objectives.

The Bank has adopted a Board-approved framework to develop a transparent link between variable remuneration and performance. The framework is designed on the basis of meeting both satisfactory financial performance and the achievement of other non-financial factors, that will, all other things being equal, deliver a target bonus pool for employees, prior to consideration of any allocation to business lines and employees individually. In the framework adopted for determining the variable remuneration pool, the NRCG aims to balance the distribution of the Bank's profits between shareholders and employees.

Key performance metrics at the Bank level include a combination of short-term and long-term measures and include profitability, solvency, liquidity, and growth indicators. The performance management process ensures that all goals are appropriately cascaded down to respective business units and employees.

In determining the amount of variable remuneration, the Bank starts from setting specific targets and other qualitative performance measures that result in a target bonus pool. The bonus pool is then adjusted to take account of risk via the use of risk-adjusted measures including forward-looking considerations.

The NRCG carefully evaluates practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. NRCG demonstrates that its decisions are consistent with an assessment of the Bank's financial condition and future prospects.

The Bank uses a formalised and transparent process to adjust the bonus pool for quality of earnings and risk profile. It is the Bank's objective to pay bonuses out of realised and sustainable profits. If the quality of earnings is not strong, the profit base could be adjusted based on the discretion of the NRCG.

For the overall Bank to have any funding for distribution of a bonus pool, threshold financial targets have to be achieved. The performance measures ensure that total variable remuneration is general considerably contracted where subdued or negative financial performance of the Bank occurs. Furthermore, the target bonus pool as determined above is subject to risk adjustments in line with the risk assessment and linkage framework.

Remuneration of control and support functions

The remuneration level of employees in the control and support functions allows the Bank to employ qualified and experienced personnel in these functions. The Bank ensures that the mix of fixed and variable remuneration for control and support function personnel is weighted in favour of fixed remuneration. The variable remuneration of control functions is based on function-specific objectives and is not determined by the financial performance of the business areas they monitor.

The Bank's performance management system plays a major role in deciding the performance of the support and control units on the basis of the objectives set for them. Such objectives are more focused on non-financial targets that include risk, control, compliance and ethical considerations as well as the market and regulatory environment, apart from value-adding tasks which are specific to each unit.

Variable compensation for business units

The variable remuneration of the business units is primarily determined by key performance objectives set through the performance management system of the Bank. Such objectives contain financial and non-financial targets, including risk control, compliance and ethical considerations, and market and regulatory requirements. The consideration of risk assessments in the performance evaluation of individuals ensures that any two employees who generate the same short-run profits but take different amounts of risk on behalf of the Bank are treated differently by the remuneration system.

Risk assessment framework

The purpose of risk linkages is to align variable remuneration to the risk profile of the Bank. In its endeavour to do so, the Bank considers both quantitative measures and qualitative measures in the risk assessment process. Both quantitative measures and human judgement play a role in determining any risk adjustments. The risk assessment process encompasses the need to ensure that the remuneration policy as designed reduces employees' incentives to take excessive and undue risks, is symmetrical with risk outcomes, and delivers an appropriate mix of remuneration that is risk aligned.

The Bank's NRCG considers whether the variable remuneration policy is in line with the Bank's risk profile and ensures that through the Bank's ex-ante and ex-post risk assessment framework and processes, remuneration practices where potential future revenues whose timing and likelihood remain uncertain are carefully evaluated.

Risk adjustments take into account all types of risk, including intangible and other risks such as reputation risk, liquidity risk and the cost of capital. The Bank undertakes risk assessments to review financial and operational performance against business strategy and risk performance prior to distribution of the annual bonus.

The Bank ensures that total variable remuneration does not limit its ability to strengthen its capital base. The extent to which capital needs to be built up is a function of the Bank's current capital position and its ICAAP.

The size of the variable remuneration pool and its allocation within the Bank takes into account the full range of current and potential risks, including:

(a) The cost and quantity of capital required to support the risks taken

(b) The cost and quantity of the liquidity risk assumed in the conduct of business

(c) Consistency with the timing and likelihood of potential future revenues incorporated into current earnings

Risk adjustments

The Bank has an ex-post risk assessment framework which is a qualitative assessment to back-test actual performance against prior risk assumptions.

In years where the Bank suffers material losses in its financial performance, the risk adjustment framework will work as follows:

- There will be considerable contraction of the Bank's total variable remuneration
- At an individual level, poor performance by the Bank will mean individual KPIs are not met and hence employee performance ratings will be lower
- Reduction in the value of deferred shares or awards
- Possible changes in vesting periods and additional deferral applied to unvested rewards
- Lastly, if the qualitative and quantitative impact of a loss incident is considered significant, a malus or claw back of previous variable awards may be considered

The NRCG, with the Board's approval, can rationalise and make the following discretionary decisions:

- Increase/reduce the ex-post adjustment
- Consider additional deferrals or increase in the quantum of non-cash awards
- Recovery through malus and claw back arrangements

Malus and claw back framework

The Bank's malus and claw back provisions allow the Bank's Board of Directors to determine that, if appropriate, unvested elements under the deferred bonus plan can be forfeited/adjusted or the delivered variable remuneration recovered in certain situations. The intention is to allow the Bank to respond appropriately if the performance factors on which reward decisions were based turn out not to reflect the corresponding performance in the longer term. All deferred compensation awards contain provisions that enable the Bank to reduce or cancel the awards of employees whose individual performance has had a materially detrimental impact on the Bank during the concerned performance year.

Any decision to take back an individual's award can only be made by the Bank's Board of Directors.

The Bank's malus and claw back provisions allow the Bank's Board to determine that, if appropriate, vested/unvested elements under the deferred bonus plan can be adjusted/cancelled in certain situations. These events include the following:

- Reasonable evidence of wilful misbehaviour, material error, negligence or incompetence of the employee causing the Bank/ the employee's business unit to suffer material loss in its financial performance, material misstatement of the Bank's financial statements, material risk management failure or reputational loss or risk due to such employee's actions, negligence, misbehaviour or incompetence during the concerned performance year.
- The employee deliberately misleads the market and/or shareholders in relation to the financial performance of the Bank during the concerned performance year.

Claw back can be used if the malus adjustment on the unvested portion is insufficient given the nature and magnitude of the issue.

Components of variable remuneration

Variable remuneration has the following main components:

Upfront cash	The portion of the variable compensation that is awarded and paid out in cash on conclusion of the performance evaluation process for each year.
Deferred cash	The portion of variable compensation that is awarded and paid in cash on a pro-rata basis over three years
Upfront short-term share awards	The portion of variable compensation that is awarded and issued in the form of shares on conclusion of the performance evaluation process for each year.
Deferred short-term share awards	The portion of variable compensation that is awarded and paid in the form of shares on a pro-rata basis over three years
Long-term performance share awards	Share-based reward schemes, under which the Bank allocates certain numbers of shares every year to executive management and senior employees based on performance, potential, and job criticality level. The plan was introduced effective 2010. It operates on a yearly basis of shares being allocated and held in a Single Person Company (SPC) in the name of the individual employee over the vesting period. Following the assessment of the performance of the Bank against the target performance conditions stipulated for the period, the ownership of the vested shares is transferred to the individual employee.
Subsidiaries Board remuneration	The portion of variable compensation that is awarded and paid out at the end of the financial year to an employee representing the Bank as director on the board of any of its wholly owned subsidiaries and/or associated companies of BBK, excluding the sitting fees.

All deferred and long-term awards are subject to malus provisions. All share awards and related dividends are released to the benefit of the employee after a six-month retention period from the date of vesting. The number of equity share awards is linked to the Bank's share price as per the rules of the Bank's Share Incentive Scheme.

Deferred compensation

All employees at senior management level and above or earning BD 100,000 per annum in Bahrain and overseas branches, excluding India, are subject to the following rules of deferral:

1 The CEO, his deputies and business line General Managers:

Element of variable remuneration	Payout percentages	Vesting period	Retention	Malus*	Claw back*
Upfront cash	40%	immediate	-	-	Yes
Deferred cash	10%	3 years	-	Yes	Yes
Deferred share awards	50%	3 years	6 months	Yes	Yes

2 All other covered staff:

Element of variable remuneration	Payout percentages	Vesting period	Retention	Malus*	Claw back*
Upfront cash	50%	immediate	-	-	Yes
Upfront share awards	10%	immediate	6 months	Yes	Yes
Deferred share awards	40%	3 years	6 months	Yes	Yes

The NRCG, based on its assessment of role profile and risk taken by an employee, could increase the coverage of employees that will be subject to deferral arrangements.

Details of remuneration paid

(a) Board of Directors

	2017	2016
Sitting fees and travel allowance	80,150	78,303
Remuneration	577,500	577,500
Others	25,018	19,510
BBK subsidiaries' Board remuneration, sitting fees and other related expenses	151,024	147,204

(b) Board of Directors of wholly owned subsidiaries

	2017	2016
Sitting fees and travel allowance	6,200	10,700
Remuneration	91,200	93,300
Others	–	–
Total	97,400	104,000

(c) Employees

1 Employee remuneration

BD 000's	2017									
		Fixed remun-eration	Sign on bonuses	Guaran-teed bonuses	Variable remuneration					
					Upfront		Deferred			
	Number of staff	Cash	(Cash/ shares)	(Cash/ shares)	Cash	Shares	Cash	Shares	Others	Total
Approved Persons Business lines	15	2,578	–	–	1,046	14	202	1,044	–	4,884
Approved Persons Control & support	9	1,306	–	–	451	77	–	324	–	2,158
Other material risk-takers	36	3,182	–	–	520	97	9	433	–	4,241
Other Staff Bahrain Operations	566	12,816	–	–	2,619	–	–	–	–	15,435
Other Staff Branches & Subsidiaries	520	7,296	–	–	580	–	–	–	–	7,876
Total	1,146	27,178	–	–	5,215	188	211	1,801	–	34,593

The net impact of other indirect staff costs amounting BD 273,700 have not been considered in the table above.

Board Remuneration and Sitting Fees received by Members of Executive Management for representing the Bank in the boards of wholly owned subsdiaries and/or associate companies of BBK amounting to BD 257,854 have been included in the table above.

BD 000's	2016									
		Fixed remun-eration	Sign on bonuses	Guaran-teed bonuses	Variable remuneration					
					Upfront		Deferred			
	Number of staff	Cash	(Cash/ shares)	(Cash/ shares)	Cash	Shares	Cash	Shares	Others	Total
Approved Persons Business lines	16	2,536	–	–	991	12	183	951	–	4,673
Approved Persons Control & support	8	1,109	–	–	420	78	–	324	–	1,931
Other material risk-takers	34	2,997	–	–	568	93	13	440	–	4,111
Other Staff Bahrain Operations	567	12,677	–	–	2,531	–	–	–	–	15,207
Other Staff Branches & Subsidiaries	421	6,431	–	–	577	–	–	–	–	7,007
Total	1,046	25,749	–	–	5,087	183	196	1,715	–	32,929

The net impact of other indirect staff costs amounting BD 266,432 have not been considered in the table above.

Board Remuneration and Sitting Fees received by Members of Executive Management for representing the Bank in the boards of wholly owned subsdiaries and/or associate companies of BBK amounting to BD 175,124 have been included in the table above.

The above table has been adjusted to reflect minor changes after publishing the annual report for 2016.

2 Deferred awards

	2017			
	Cash BD '000	Shares Number	Shares BD '000	Total BD '000
Opening balance	561	16,443,303	5,998	6,559
Awarded during the period*	211	4,349,159	1,801	2,011
Paid out/released during the period	(148)	(3,782,737)	(1,470)	(1,618)
Service, performance and risk adjustments	–	–	–	–
Bonus share adjustment	–	–	–	–
Closing balance	624	17,009,725	6,328	6,952

* The number of shares for the 2017 Deferred Awards has been calculated using the year-end closing share price at 0.414 fils per share, as the award price will be determined 14 days after the AGM.

	2016			
	Cash BD '000	Shares Number	Shares BD '000	Total BD '000
Opening balance	443	15,221,598	5,695	6,138
Awarded during the period**	195	4,636,928	1,715	1,910
Paid out/released during the period	(77)	(3,415,223)	(1,413)	(1,490)
Service, performance and risk adjustments	–	–	–	–
Bonus share adjustment	–	–	–	–
Closing balance	561	16,443,303	5,998	6,559

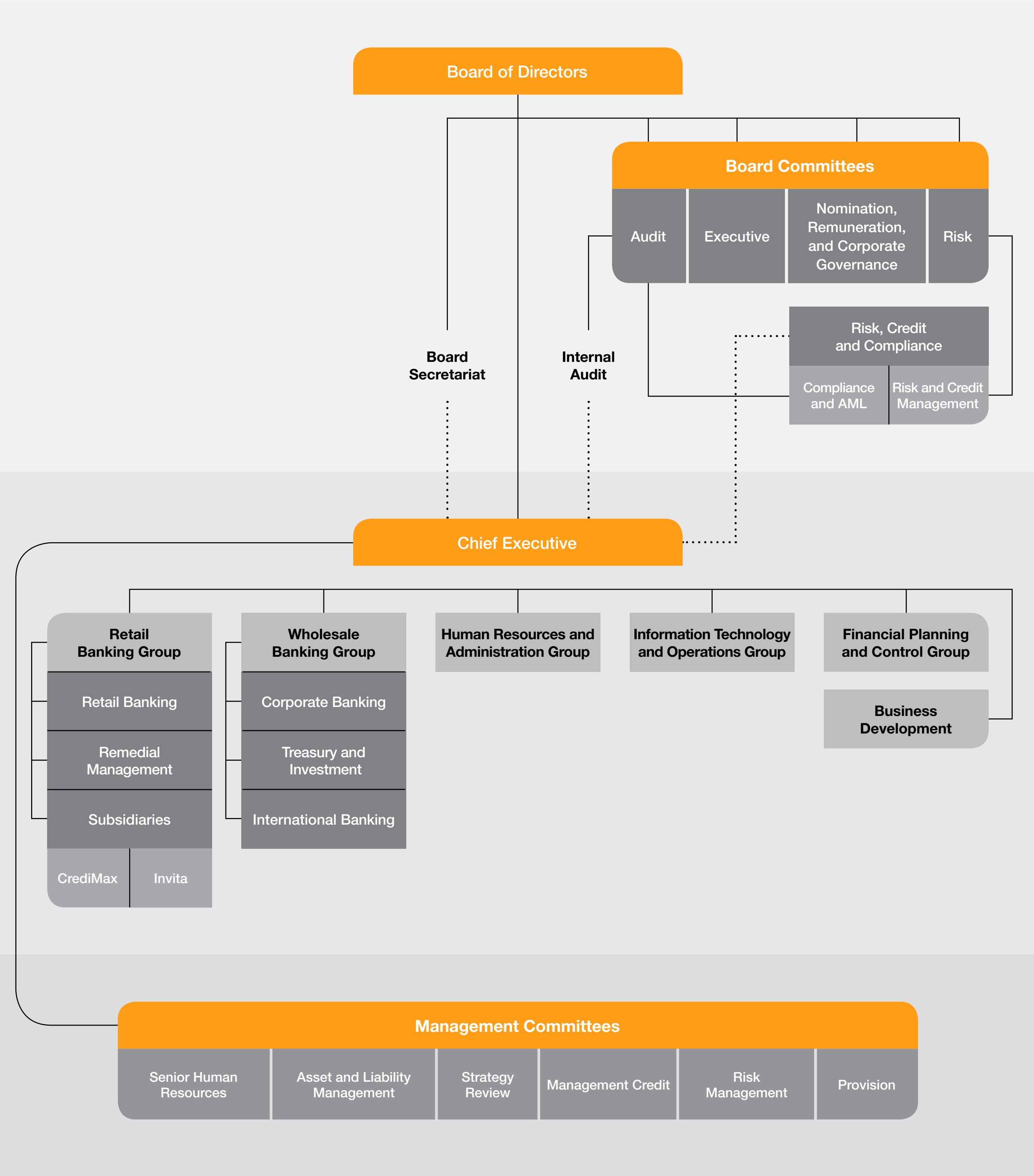
** The number of shares for the 2016 Deferred Awards have been recomputed based on the share price 14 days after the AGM of the Bank at 0.394 fils per share, and updated for the actual awards distributed to staff during 2016.

In the case of long-term incentive plan awards, the shares awarded have been included for the purposes of the table above assuming probability of vesting.

Information on share awards included above also include components of long-term performance-based incentive awards (LTIP shares). The amounts included in the tables are based on total awards granted for the performance year and may not necessarily match the accounting charge which factors probability of vesting.

Organisation information

Organisation structure



Executive management interests

The number of shares and bonds held by members of the Executive Management team as of 31 December 2017 was as follows:

Name	Type of shares	31 Dec 2017	31 Dec 2016	Bonds	
				31 Dec 2017	31 Dec 2016
Reyadh Yousif Sater	Ordinary	1,171,643	722,435	300,000	300,000
Abdulrahman Ali Saif	Ordinary	387,237	234,878	90,000	90,000
Mohammed Ali Malik	Ordinary	430,812	216,406	–	–
Jamal Mohamed Al Sabbagh	Ordinary	397,170	265,350	–	–
Hassaan Mohammed Burshaid	Ordinary	463,160	294,397	–	–
Mohammed Abdulla Isa	Ordinary	97,029	339,247	30,000	30,000
Rashad Ahmed Akbari	Ordinary	283,183	181,130	–	–
C.K. Jaidev	–	–	–	–	–
Nadeem A. Aziz Kooheji	Ordinary	30,207	54,812	–	–
C. V. Murthy	Ordinary	228,686	159,180	10,000	10,000
Neil Anthony Sharp	–	–	–	–	–
Adel Abdulla Salem	–	–	–	–	–
Raj Dugar	Ordinary	76,905	38,332	7,000	7,000

Executive Senior Management trading of the Bank's shares and bonds during 2017

Name	Trading through Bahrain Bourse	Date of trading
Abdulrahman Ali Saif	Sold 10,000 shares	28 February 2017
	Sold 67,566 shares	16 March 2017
Mohammed Ali Malik	Sold 20,000 shares	1 November 2017
	Sold 15,000 shares	2 November 2017
Mohammed Abdulla Isa	Sold 12,000 shares	13 March 2017
	Sold 53,963 shares	14 March 2017
	Sold 240,000 shares	15 March 2017
C.K. Jaidev	Sold 30,000 shares	5 February 2017
	Sold 19,810 shares	6 March 2017
	Sold 54,005 shares	7 March 2017
Nadeem A.Aziz Kooheji	Sold 20,000 shares	9 January 2017
	Sold 10,000 shares	24 January 2017
	Sold 15,000 shares	7 February 2017
	Sold 17,971 shares	15 March 2017
	Sold 10,000 shares	22 March 2017
Neil Anthony Sharp	Sold 67,584 shares	12 January 2017
	Sold 54,810 shares	4 July 2017

Management Committees

Management Committees are chaired by the Chief Executive. Committee members are heads of the relevant divisions appointed by the Committee Chairman.

Committee	Summary terms of reference, roles and responsibilities:	Frequency of meetings:
Senior Human Resources	Establishes appropriate policies, procedures and guidelines for the management of human resources.	Once every other month.
Asset and Liability Management	Establishes policies and guidelines for the overall management of the statement of financial position and its associated risks.	At least once a month.
Strategy Review	Reviews and monitors progress on strategic initiatives.	Twice a year.
Management Credit	Approves credit and investment proposals above a certain limit. Also reviews and recommends any proposal requiring Executive Committee or Board approval.	Once a week.
Risk Management	Identifies, measures, monitors and controls risk by establishing risk policies and procedures.	Once every quarter.
Provision	Reviews and establishes provisioning requirements for loans, advances and investments.	Once every quarter.

Major BBK shareholdings as of 31 December 2017

The company's ownership in other companies listed on the Bahrain Bourse (5% and above)

Name/Entity	Nationality/ Headquarters	Legal status	Ownership date	%	Number of shares 31 Dec 2016 Previous	Number of shares 31 Dec 2017 Current
Bahrain Kuwait Insurance (BKIC)	Bahrain	BSC (c)	2006	6.82%	4,879,818	**4,879,818**
Securities Investment Company	Bahrain	BSC (c)	2006	9.63%	41,250,000	**41,250,000**
Bahrain Commercial Facilities Company	Bahrain	BSC (c)	1994	23.03%	37,618,691	**37,618,691**

Major shareholders of the company's outstanding shares (5% and above)

Name/Entity	Nationality/ Headquarters	Legal status	Ownership date	%	Number of shares 31 Dec 2016 Previous	Number of shares 31 Dec 2017 Current
Ithmaar Bank	Bahrain	BSC	2008	25.38%	274,493,028	**274,493,028**
Pension Fund Commission (PFC)	Bahrain	Governmental Institution	1986	18.77%	203,020,288	**203,020,288**
Kuwait Investment Authority (KIA)	Kuwait	Investment Company	1990	18.70%	202,229,987	**202,229,987**
Social Insurance Organization (SIO)	Bahrain	Governmental Institution	1986	13.34%	144,294,820	**144,294,820**

The Bank's holdings in other companies (Quoted / unquoted in / out Kingdom of Bahrain) (10% and above)

Name/Entity	Nationality/ Headquarters	Legal status	Ownership date	%	Number of shares 31 Dec 2016 Previous	Number of shares 31 Dec 2017 Current
CrediMax	Bahrain	BSC (c)	1999	100.00%	10,000,000	**10,000,000**
Invita	Bahrain	BSC (c)	2006	100.00%	1,000,000	**1,000,000**
Global Payment Services (1)	Bahrain	WLL	2005	55.00%	10,000	**10,000**
Sakana Holistic Housing Solutions	Bahrain	BSC (c)	2006	50.00%	1,000,000	**500,000**
The Benefit Company	Bahrain	BSC (c)	1997	22.00%	6,843	**6,843**
Naseej Company	Bahrain	BSC	2009	15.15%	163,636,370	**163,636,370**
Alosra Bank	Bahrain	BSC (c)	2009	10.00%	5,000,000	**5,000,000**
Diyaar Al Harameen Al Ola Limited	Cayman Islands	WLL	2011	35.00%	16,450,000	**16,450,000**
BBK Geojit Securities KSC	Kuwait	KSC	2012	40.00%	2,000,000	**2,000,000**
Invita – Kuwait (2)	Kuwait	KSCC	2013	60.00%	600,000	**600,000**
Aegila Capital Management Limited	London	LTD	2015	50.00%	1	**1**
Bahrain Liquidity Fund	Bahrain	LTD	2016	24.27%	10,000	**10,000**
BBK Shares Incentive	Bahrain	SPC	2015	100.00%	-	**500**

(1) Shareholding through CrediMax.

(2) Shareholding through Invita

BBK offices and overseas branches

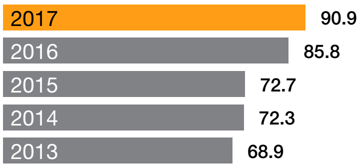
For contact details of our local and international offices and branches, please visit our website www.bbkonline.com.
The Bank is headquartered in Bahrain and also operates in Dubai, Turkey, Kuwait, and India.

Part III

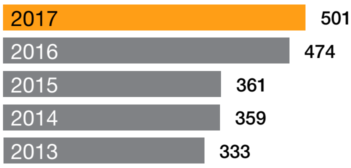
Financial information

Financial review

Net interest income
BD millions



Total equity
BD millions



Customer deposits
BD millions

Loans and advances
BD millions

Total assets
BD millions

BBK's financial performance has been achieved through our commitment to fulfil customers' evolving needs. We have focused on our strategic priorities and disciplined risk management, enabling us to deliver long-term sustainable returns to shareholders.

Overview

In spite of the tough economic conditions and turbulences, the Bank managed to maintain its high performance in 2017, achieving record profitability of BD 58.7 million attributable to shareholders for the year ended 31 December 2017, representing BD 2.3 million or 4.0 percent growth over 2016 results.

The key financial indicators of the Bank remain healthy with a return on average assets of 1.6 percent and a return on average equity of 12.1 percent. An annual return of BD 7.1 million was paid to the perpetual Tier 1 capital securities shareholders, the earnings per share decreased from 49 fils to 48 fils. The Bank's liquidity position remains stable with liquid assets to total assets at 34.7 percent (2016: 32.6 percent).

This section provides a review of our Group's financial performance, focusing on the consolidated operating results and BBK's consolidated statement of financial position, including its overseas branches, principal subsidiaries, joint ventures, associated companies, and indirect investment in associates through subsidiaries.

The consolidated financial statements have been prepared and are presented in accordance with the International Financial Reporting Standards, Bahrain Commercial Companies Law, Central Bank of Bahrain (CBB) requirements, and Financial Institutions law.

As the majority of our financial assets are loans and advances that are held on an amortised cost basis, the risk of short-term distress shocks is reduced, and thus a healthy overall financial position is upheld.

Operating results

The year 2017 was the second of BBK's three-year strategic plan in which the Bank continued its steady and consistent performance, maintaining proactive management of risks and costs while focusing on developing domestic and cross-border business opportunities.

Despite the general weakness in economic trends regionally and globally, the Net Profit for 2017 (attributable to the owners of the Bank) increased by 4.0 percent from last year, amounting to BD 58.7 million. The total operating income for the year increased by BD 9.5 million or 7.1 percent and stood at BD 143.1 million, reflecting the success in diversifying sources of income.

Continuing BBK's prudent approach to risk management and provisioning, the Bank conservatively provided for adequate provisioning levels in 2017, applying the IFRS 9 accounting standard. This standard considers expected credit losses instead of the incurred losses mandated by the previous IAS 39 to measure impaired exposures caused by market turbulence. It includes changes in the fair market value for investments as a way of protecting the Bank's overall asset exposures.

Net interest income

Net interest income increased by 5.9 percent to BD 90.9 million (2016: BD 85.8 million). This was achieved through prudent use of liquidity in high-quality investments and treasury bills, respectively reporting increases of 10.8 percent and 19.4 percent.

As a result of the strong growth in total earning assets, the net interest yield ratio increased from 2.5 to 2.7 percent.

Summary statement of profit or loss

BD millions	2017	2016	Variance BD millions	Change percent
Net interest income	**90.9**	85.8	5.1	5.9%
Other income	**52.2**	47.7	4.5	9.4%
Total income	**143.1**	133.5	9.6	7.1%
Operating expenses	**54.0**	53.1	0.9	1.6%
Provisions	**29.0**	22.6	6.4	28.1%
Profit before taxation	**60.1**	57.8	2.3	4.0%
Taxation/non-controlling interest	**(1.4)**	(1.3)	(0.1)	1.7%
Net profit	**58.7**	56.5	2.2	4.0%

Consolidated statement of financial position

BD millions	2017	2016	Variance BD millions	Change percent
Assets				
Cash and balances with central banks	**469.4**	314.4	155.0	49.3%
Treasury bills	**427.1**	401.6	25.5	6.3%
Deposits and amounts due from banks and other financial institutions	**223.8**	318.4	(94.6)	–29.7%
Loans and advances to customers	**1,740.7**	1,767.1	(26.4)	–1.5%
Investment securities	**749.0**	768.1	(19.1)	–2.5%
Investments in associated companies and joint ventures	**47.0**	43.9	3.1	6.9%
Interest receivable and other assets	**79.7**	64.8	14.9	23.0%
Premises and equipment	**26.4**	24.2	2.2	9.3%
Total assets	**3,763.1**	3,702.6	60.5	1.6%
Liabilities and Equity				
Liabilities				
Deposits and amounts due to banks and other financial institutions	**193.5**	259.9	(66.4)	–25.6%
Borrowings under repurchase agreement	**161.3**	184.0	(22.7)	–12.3%
Term borrowings	**199.0**	206.1	(7.1)	–3.4%
Customers' current, savings and other deposits	**2,623.6**	2,493.7	129.9	5.2%
Interest payable and other liabilities	**84.9**	84.6	0.3	0.4%
Total liabilities	**3,262.3**	3,228.3	34.0	1.1%
Attributable to the owners of the Bank	**498.6**	472.4	26.2	5.5%
Non-controlling interest	**2.2**	1.8	0.4	22.8%
Total equity	**500.8**	474.2	26.6	5.6%
Total liabilities and equity	**3,763.1**	3,702.6	60.5	1.6%

Other income

Other operating income consists of non-interest income, derived from business activities such as dealing in foreign currencies, investing in funds other than fixed-income funds, the sale of corporate banking and retail banking services, and investment trading.

An increase of 10.5 percent was recorded for total other income, rising to BD 46.6 million from the previous year's BD 42.2 million. Increased business volumes resulted in 6.2 percent growth in net fees and commission to BD 31.1 million (2016: BD 29.3 million). Other income relating to foreign exchange, income from associated companies and joint ventures, and investment income increased to BD 19.8 million, up 24.2 percent from 2016 BD 16.0 million.

Operating expenses

Due to the growth in business activities during the year, the Bank's operating expenses increased by 1.6 percent, from BD 53.1 million to BD 54.0 million. Staff costs increased by 3.6 percent, while other operating expenses decreased by 2.1 percent. Other operating expenses stood at BD 15.9 million (2016: BD 16.3 million). Nevertheless, the Bank's prudent cost control policy and strong revenue-generating capability enabled improvement in its cost to income ratio to 37.8 percent (2016: 39.8 percent).

Net provisions

The Bank follows the International Financial Reporting Standard 9 (IFRS 9) with regards to accounting for the impairment of financial assets. IFRS 9 replaces the incurred loss model in IAS 39 with an expected credit loss model. The new impairment model also applies to certain loan commitments and financial guarantee contracts, but not to equity investments that are subject to revaluation. Under IFRS 9, credit losses are recognised earlier than under IAS 39. The Group applies a three-stage approach to measuring expected credit losses on financial assets carried at amortised cost and debt instruments classified as FVOCI (fair value through other comprehensive income). Assets migrate through the following three stages based on the change in credit quality since initial recognition. This approach of provisioning for impairment of the Bank's financial assets is aimed at providing more realistic estimates of the impairment in the value of the assets.

The net provisions reserve amounted to BD 29.0 million for 2017, 28.1 percent higher than the previous year. The Bank's asset quality metrics improved, with the gross non-performing loans ratio decreasing to 5.8 percent (BD 107.5 million compared to BD 113.3 million in 2016). The Bank maintains a strong total provision coverage ratio of 104.5 percent (2016: 112.0 percent).

Comprehensive income

The Bank's comprehensive income stood at BD 65.0 million for the year ended 31 December 2017, compared to BD 67.3 million at the end of 2016. This was mainly driven by the significant improvement in the fair value of investment securities.

Financial position

The Group maintained a strong and liquid balance sheet, achieving growth of BD 60.5 million in the financial position (1.6 percent) to reach BD 3,763.1 million. The growth was primarily driven by an increase in cash and balances with central banks, while the surplus liquidity was prudently invested in Bahraini government debt and other debt, mostly investment-grade.

The Bank has been consistent in achieving a good balance between deposits and loans and advances. It remains a strong net lender in the inter-bank market, particularly in the GCC and MENA region. As at 31 December 2017, the ratio of net loans and advances to deposits stood at 66.3 percent (2016: 70.9 percent). This represents a slight decrease in commercial lending, but still remains a strong sign of the confidence customers have in the Bank as a financial institution in the Kingdom of Bahrain, whilst optimising the use of surplus liquidity in the market.

The overall financial position remains healthy as the majority of the financial assets are loans and advances that are held on an amortised cost basis, which reduces the risk of short-term distress shocks.

Assets

Total assets stood at BD 3,763.1 million as at 31 December 2017, an increase of 1.6 percent over 2016's BD 3,702.6 million. Loans and advances decreased slightly (1.5 percent) in line with management's strategic directions to reduce international lending exposure and focus on less risky local credit financing activities during international financial market instability. However, the excess in liquidity was deployed in high liquid assets consisting of cash and balances with central banks and treasury bills.

The investment portfolio of the Bank is classified into three categories: 'Financial assets at fair value through profit or loss' (FVTPL); 'Financial assets at fair value through other comprehensive income' (FVOCI); and 'Investments stated at amortised costs'. At the end of 2017, quoted bonds and equities constituted 81.8 percent of the gross investments (2016: 81.1 percent). The fixed income portfolio is substantially hedged against exposure to interest rate risk or highly dominated by regional governments' bonds and sukuk.

The Bank's total investment securities decreased by BD 19.1 million or 2.5 percent and stood at BD 749.0 million at the end of 2017. This was mainly due to the decrease in investment activities in selective domestic and international markets.

Investment in associated companies and joint venture represents the Bank's interest in a number of associates and joint ventures, as outlined in later sections of this report. The carrying value of these investments represents the Bank's share of the net assets of these companies.

Liabilities

Current, saving, and other deposits include the balances of interest-bearing and non-interest-bearing accounts, due to customers' on-demand and term deposits taken with different maturity dates, in various currencies and at varying rates of interest. Customer deposits stood at BD 2,623.6 million at the end of 2017 (2016: BD 2,493.7 million). The Bank continues to be successful in generating customer deposits, reflecting its success in portraying itself as a dependable and solid financial institution and leveraging its presence as a dominant player in the domestic market.

Borrowings under repurchase agreements and due to banks and financial institutions stood at BD 354.8 million (2016: BD 443.9 million). Customer deposits continue to be the major source of funding, with the ratio of customer deposits to total liabilities at 80.4 percent (2016: 77.2 percent).

Interest payable and other liabilities consist of accrued interest payable on interest-bearing deposits, accrued expenses, and provisions.

Capital adequacy

The Bank has implemented the Basel III framework for the calculation of capital adequacy since January 2015, in accordance with Central Bank of Bahrain guidelines.

Equity before appropriations stood at BD 498.6 million at the end of 2017 (2016: BD 472.4 million). The Bank continued to maintain a comfortable capital adequacy ratio of 20.0 percent (2016: 18.5 percent), well above CBB's minimum regulatory requirement of 12.5 percent.

This growth was supported by the issuance of perpetual Tier 1 capital securities in 2017, amounting to BD 86.1 million. The Group is keen to maintain strong capitalisation to support future strategic plans.

Our noticeable growth over the years is a result of our sustained culture of superior performance, our widespread participation in both local and international markets, and excellent customer service, which enables us to sustain the momentum we have built over the years and to enhance value for shareholders.

Independent auditors' report to the shareholders

Building a better working world

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Opinion

We have audited the accompanying consolidated financial statements of BBK B.S.C. ("the Bank") and its subsidiaries (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statements of profit or loss, other comprehensive income, changes in equity and cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ("ISA"). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the year ended 31 December 2017. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the Auditor's responsibilities for the audit of the consolidated financial statements section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.

Key audit matter	How the key audit matter was addressed in the audit
Impairment of carrying value of loans and advances	
The Group exercises significant judgement using subjective assumptions over both when and how much to record as loan impairment, and estimation of the amount of the impairment provision for loans and advances. Because loans and advances form a major portion of the Group's assets, and due to the significance of the judgments used in classifying loans and advances into various stages stipulated in IFRS 9 and determining related provision requirements, this audit area is considered a key audit risk. As at 31 December 2017, the Group's gross loans and advances amounted to BD 1,853 million and the related impairment provisions amounted to BD 112 million, comprising BD 46 million of provision against Stage 1 and 2 exposures and BD 66 million against exposures classified under Stage 3. The impairment provision on loans and advances is disclosed in note 7 and the impairment provision policy is presented in the accounting policies in note 3 to the consolidated financial statements.	• We gained understanding of the Group's key credit processes comprising granting, booking, monitoring and provisioning and tested the operating effectiveness of key controls over these processes; • We read the Group's impairment provisioning policy and compared it with the requirements of IFRS 9; • For provision against exposures classified as Stage 1 and Stage 2, we obtained an understanding of the Group's provisioning methodology, assessed the reasonableness of the underlying assumptions and the sufficiency of the data used. We also checked the completeness of loans and advances included in the expected credit losses calculations; • We checked the appropriateness of the Group's determination of significant increase in credit risk and the resultant basis for classification of exposures into various stages; • For a sample of exposures, we checked the appropriateness of determining exposure at default, probability of default, and loss given default used in the expected credit losses calculations; • For exposures determined to be individually impaired classified as stage 3, we tested a sample of loans and advances and examined management's estimate of future cash flows, assessed their reasonableness and checked the resultant provision calculations; and • Where relevant, we used Information System specialists to gain comfort on data integrity.

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS (continued)

Other information included in the Group's 2017 annual report

Other information consists of the information included in the Group's 2017 Annual Report, other than the consolidated financial statements and our auditor's report thereon. The Board of Directors is responsible for the other information. Prior to the date of this auditor's report, we obtained the Board of Directors' report, which will form part of the annual report, and the remaining sections of the annual report are expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon. In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information obtained prior to the date of the auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the Board of Directors for the consolidated financial statements

The Board of Directors is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS and for such internal control as the Board of Directors determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Board of Directors is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Board of Directors either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Auditor's Responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISA, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Group's internal control
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors.
- Conclude on the appropriateness of the Board of Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with the Group's Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Group's Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Group's Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

As required by the Bahrain Commercial Companies Law and Volume 1 of the Central Bank of Bahrain (CBB) Rule Book, we report that:

a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;

b) the financial information contained in the Board of Directors' report is consistent with the consolidated financial statements;

c) we are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2017 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position; and

d) satisfactory explanations and information have been provided to us by Management in response to all our requests.

The partner in charge of the audit resulting in this independent auditor's report is Ashwani Siotia.

Ernst & Young

Partner's registration no.117
19 February 2018
Manama, Kingdom of Bahrain

Consolidated statement of financial position

As at 31 December 2017

	Notes	2017 BD '000	2016 BD '000
ASSETS			
Cash and balances with central banks	4	**469,436**	314,368
Treasury bills	5	**427,130**	401,635
Deposits and amounts due from banks and other financial institutions	6	**223,824**	318,407
Loans and advances to customers	7	**1,740,651**	1,767,138
Investment securities	8	**748,985**	768,134
Investments in associated companies and joint ventures	9	**46,958**	43,923
Interest receivable and other assets	10	**79,680**	64,769
Premises and equipment	11	**26,436**	24,183
TOTAL ASSETS		**3,763,100**	3,702,557
LIABILITIES AND EQUITY			
Liabilities			
Deposits and amounts due to banks and other financial institutions		**193,472**	259,911
Borrowings under repurchase agreement		**161,314**	184,016
Term borrowings	12	**199,012**	206,109
Customers' current, savings and other deposits	13	**2,623,577**	2,493,715
Interest payable and other liabilities	14	**84,890**	84,591
Total liabilities		**3,262,265**	3,228,342
Equity			
Share capital	15	**108,165**	108,165
Treasury stock	15	**(998)**	(1,206)
Perpetual tier 1 convertible capital securities	15	**86,098**	86,098
Share premium	15	**41,016**	39,919
Statutory reserve	16	**54,082**	54,082
General reserve	16	**54,082**	54,082
Cumulative changes in fair values	17	**(8,349)**	(13,669)
Foreign currency translation adjustments		**(9,271)**	(11,558)
Retained earnings		**134,632**	122,830
Proposed Appropriations	18	**39,161**	33,666
ATTRIBUTABLE TO THE OWNERS OF THE BANK		**498,618**	472,409
Non-controlling interest		**2,217**	1,806
Total equity		**500,835**	474,215
TOTAL LIABILITIES AND EQUITY		**3,763,100**	3,702,557

Murad Ali Murad
Chairman

Aref Saleh Khamis
Deputy Chairman

Reyadh Yousif Sater
Chief Executive

The attached notes 1 to 45 form part of these consolidated financial statements

Consolidated statement of profit or loss

Year ended 31 December 2017

	Notes	2017 BD '000	2016 BD '000
Interest and similar income	19	**136,983**	128,556
Interest and similar expense		**(46,077)**	(42,708)
Net interest income		**90,906**	85,848
Share of profit of associated companies and joint ventures	9	**5,519**	5,467
Other income	20	**46,634**	42,212
Total operating income		**143,059**	133,527
Staff costs		**34,659**	33,453
Other expenses		**15,914**	16,263
Depreciation	11	**3,435**	3,430
Net provision for impairment on loans and advances to customers	7	**28,912**	23,753
Net provision/(write back) for impairment on investments	8	**98**	(1,115)
Total operating expenses		**83,018**	75,784
PROFIT BEFORE TAXATION		**60,041**	57,743
Net tax provision		**(810)**	(996)
PROFIT FOR THE YEAR		**59,231**	56,747
Attributable to:			
Owners of the Bank		**58,685**	56,410
Non-controlling interest		**546**	337
		59,231	56,747
Basic earnings per share (BD)	21	**0.048**	0.049
Diluted earnings per share (BD)	21	**0.045**	0.044

Murad Ali Murad
Chairman

Aref Saleh Khamis
Deputy Chairman

Reyadh Yousif Sater
Chief Executive

The attached notes 1 to 45 form part of these consolidated financial statements

Consolidated statement of other comprehensive income

Year ended 31 December 2017

	Notes	2017 BD '000	2016 BD '000
Profit for the year		**59,231**	56,747
Other comprehensive (loss) income			
Items that will not be reclassified to profit or loss			
Fair value through other comprehensive income reserve (equity instruments)		**(8,466)**	4,113
Items that are or may be reclassified subsequently to profit or loss			
Movement in translation reserve:			
Foreign currency translation adjustments		**2,287**	(923)
Movement in hedging reserve:			
Effective portion of changes in fair value	17	**284**	174
Net amount transferred to profit or loss			
Movement in fair value reserve			
Net change in fair value		**15,701**	8,377
Net amount transferred to profit or loss		**(3,525)**	(887)
Other comprehensive income for the year		**6,281**	10,854
Total comprehensive income for the year		**65,512**	67,601
Attributable to:			
Owners of the Bank		**64,966**	67,264
Non-controlling interest		**546**	337
		65,512	67,601

The attached notes 1 to 45 form part of these consolidated financial statements

Consolidated statement of changes in equity

Year ended 31 December 2017

	Notes	Attributable to the owners of the Bank and capital securities' holders												
		Share capital BD '000	Treasury stock BD '000	Perpetual tier 1 convertible capital securities BD '000	Share premium BD '000	Statutory reserve BD '000	General reserve BD '000	Cumulative changes in fair values BD '000	Foreign currency translation adjustments BD '000	Retained earnings BD '000	Proposed appropriations BD '000	Total BD '000	Non-controlling interest BD '000	Total equity BD '000
Restated balance at 1 January 2016		108,165	(4,728)	–	39,919	54,082	51,507	(29,184)	(10,635)	107,560	30,586	347,272	1,562	348,834
Profit for the year		–	–	–	–	–	–	–	–	56,410	–	56,410	337	56,747
Other comprehensive income		–	–	–	–	–	–	15,515	(923)	(3,738)	–	10,854	–	10,854
Total comprehensive income		–	–	–	–	–	–	15,515	(923)	52,672	–	67,264	337	67,601
Share – based payments	40	–	–	–	–	–	–	–	–	(31)	–	(31)	–	(31)
Perpetual tier 1 convertible capital securities issued		–	–	86,098	–	–	–	–	–	–	–	86,098	–	86,098
Expenses related to perpetual – tier 1 convertible capital securities issued		–	–	–	–	–	–	–	–	(180)	–	(180)	–	(180)
Distribution on Perpetual tier 1 convertible capital securities		–	–	–	–	–	–	–	–	(3,552)	–	(3,552)	–	(3,552)
Dividends paid	18	–	–	–	–	–	–	–	–	–	(26,611)	(26,611)	(93)	(26,704)
Donations		–	–	–	–	–	–	–	–	–	(1,400)	(1,400)	–	(1,400)
Movement in treasury stock	15	–	3,522	–	–	–	–	–	–	–	–	3,522	–	3,522
Unclaimed dividends	15	–	–	–	–	–	–	–	–	27	–	27	–	27
Proposed appropriations	18	–	–	–	–	–	–	–	–	(33,666)	33,666	–	–	–
Transfer to general reserve 2015		–	–	–	–	–	2,575	–		–	(2,575)	–		–
Balance at 31 December 2016		**108,165**	**(1,206)**	**86,098**	**39,919**	**54,082**	**54,082**	**(13,669)**	**(11,558)**	**122,830**	**33,666**	**472,409**	**1,806**	**474,215**
Profit for the year		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**58,685**	**–**	**58,685**	**546**	**59,231**
Other comprehensive income		**–**	**–**	**–**	**–**	**–**	**–**	**5,320**	**2,287**	**(1,326)**	**–**	**6,281**	**–**	**6,281**
Total comprehensive income		**–**	**–**	**–**	**–**	**–**	**–**	**5,320**	**2,287**	**57,359**	**–**	**64,966**	**546**	**65,512**
Share – based payments	40	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**699**	**–**	**699**	**–**	**699**
Distribution on Perpetual tier 1 convertible capital securities		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(7,103)**	**–**	**(7,103)**	**–**	**(7,103)**
Dividends paid	18	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(32,266)**	**(32,266)**	**(135)**	**(32,401)**
Donations		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(1,400)**	**(1,400)**	**–**	**(1,400)**
Movement in treasury stock		**–**	**208**	**–**	**1,097**	**–**	**–**	**–**	**–**	**–**	**–**	**1,305**	**–**	**1,305**
Unclaimed dividends		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**8**	**–**	**8**	**–**	**8**
Proposed appropriations	18	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(39,161)**	**39,161**	**–**
Balance at 31 December 2017		**108,165**	**(998)**	**86,098**	**41,016**	**54,082**	**54,082**	**(8,349)**	**(9,271)**	**134,632**	**39,161**	**498,618**	**2,217**	**500,835**

The attached notes 1 to 45 form part of these consolidated financial statements

Consolidated statement of cash flows

Year ended 31 December 2017

	Notes	2017 BD '000	2016 BD '000
OPERATING ACTIVITIES			
Profit for the year before taxation		**60,041**	57,743
Adjustments for non-cash items:			
Net provisions (write back) relating to:			
Loans and advances to customers	7	**28,912**	23,753
Investment securities	8	**98**	(1,115)
Share of profit of associated companies and joint ventures	9	**(5,519)**	(5,467)
Depreciation	11	**3,435**	3,430
Realised gains on sale of investment securities	20	**(3,965)**	(2,707)
Accrual on term borrowings		**1,412**	1,432
		84,414	77,069
(Increase) decrease in operating assets			
Mandatory reserve deposits with central banks		**(2,952)**	5,049
Treasury bills maturing after 90 days		**(25,495)**	(13,212)
Deposits and amounts due from banks and other financial institutions		**17,824**	(15,824)
Loans and advances to customers		**(2,425)**	(26,092)
Interest receivable and other assets		**(14,627)**	(7,625)
Increase (decrease) in operating liabilities			
Deposits and amounts due to banks and other financial institutions		**(66,439)**	80,507
Borrowings under repurchase agreements		**(22,703)**	9,508
Customers' current, savings and other deposits		**129,862**	(149,177)
Interest payable and other liabilities		**299**	365
Income tax paid		**(100)**	(935)
Net cash from/(used in) operating activities		**97,658**	(40,367)
INVESTING ACTIVITIES			
Purchase of investment securities		**(249,423)**	(247,605)
Redemption/sale of investment securities		**275,668**	240,940
Sale/partial repayment of capital of investment in associated companies	9	**500**	(4,492)
Dividends received from associated companies	9	**2,394**	2,103
Other movements in investment in associated companies		**(68)**	(238)
Purchase of premises and equipment		**(5,688)**	(2,807)
Net cash from/(used in) investing activities		**23,383**	(12,099)
FINANCING ACTIVITIES			
Payment of dividend and donations	18	**(33,666)**	(28,011)
Term borrowings		**(8,509)**	–
Issuance of perpetual tier 1 convertible capital securities		**–**	86,098
Payment of expenses related to issuance of perpetual tier 1 convertible capital securities		**–**	(180)
Distribution of perpetual tier 1 convertible capital securities Interest		**(7,104)**	(3,552)
Movement in treasury stock		**1,305**	3,522
Net cash (used in)/from financing activities		**(47,974)**	57,877
Foreign currency translation adjustments		**2,287**	(923)
NET CHANGE IN CASH AND CASH EQUIVALENTS		**75,354**	4,488
Cash and cash equivalents at beginning of the year		**537,604**	533,116
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	23	**612,958**	537,604

The attached notes 1 to 45 form part of these consolidated financial statements

1 ACTIVITIES

BBK B.S.C. (the "Bank"), a public shareholding company, was incorporated in the Kingdom of Bahrain by an Amiri Decree in March 1971 and registered with the Ministry of Industry and Commerce under Commercial Registration number 1234 dated 16 March 1971. The Bank operates in Bahrain under a commercial banking license issued by the Central Bank of Bahrain ("CBB") and its shares are listed on the Bahrain Bourse.

The Bank is engaged in commercial banking activities through its branches in the Kingdom of Bahrain, State of Kuwait and Republic of India and credit card operations and business process outsourcing services through its subsidiaries. The Bank's registered office is at 43 Government Avenue, P O Box 597, Manama, Kingdom of Bahrain.

The consolidated financial statements were authorised for issue in accordance with a resolution of the Bank's Board of Directors on 19 February 2018.

2 BASIS OF PREPARATION

Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and in conformity with the Bahrain Commercial Companies Law and the CBB and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Bank's memorandum and articles of association.

Accounting convention

The consolidated financial statements are prepared on a historical cost basis, except for derivative financial instruments, investment securities at fair value through other comprehensive income, trading investments and financial assets designated at fair value through statement of profit or loss, that have been measured at fair value. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges, and are otherwise carried at cost, are adjusted to record changes in fair values attributable to risks that are being hedged.

The consolidated financial statements are prepared in Bahraini Dinars which is the functional and presentation currency of the Bank.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and its subsidiaries (the "Group"), all of which have 31 December as their year end. The Bank has the following principal subsidiaries:

Name	Ownership	Country of incorporation	Activity
CrediMax B.S.C. (c)	100%	Kingdom of Bahrain	Credit card operations
Invita Company B.S.C. (c)	100%	Kingdom of Bahrain	Business process outsourcing services

CrediMax B.S.C. (c) owns 55% (2016: 55%) of the share capital of Global Payment Services W.L.L., which is established in the Kingdom of Bahrain and engaged in processing and backup services relating to credit, debit and charge cards.

Invita Company B.S.C. (c) owns 60% (2016: 60%) of the share capital of Invita Kuwait K.S.C.C. , which is established in the State of Kuwait and engaged in business processing and outsourcing services.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if and only if the Group has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns.

When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangement with the other vote holders of the investee;
- Rights arising from other contractual arrangements; and
- The Group's voting rights and potential voting rights.

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the statement of comprehensive income from the date the Group gains control until the date the Group ceases to control the subsidiary.

Profit or loss and each component of other comprehensive income (OCI) are attributed to the equity holders of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction. If the Group loses control over a subsidiary, it:

- Derecognises the assets (including goodwill) and liabilities of the subsidiary;
- Derecognises the carrying amount of any non-controlling interests;
- Derecognises the cumulative translation differences recorded in equity;
- Recognises the fair value of the consideration received;
- Recognises the fair value of any investment retained;
- Recognises any surplus or deficit in profit or loss; and
- Reclassifies the parent's share of components previously recognised in OCI to profit or loss or retained earnings, as appropriate, as would be required if the Group had directly disposed of the related assets or liabilities.

3 ACCOUNTING POLICIES

3.1 New Standards and Interpretations issued but not yet effective

The following new Standards and amendments have been issued by the International Accounting Standards Board (IASB) but are not yet mandatory as of 31 December 2017:

- IFRS 9 Financial Instrument (effective 1 January 2018, however Group has early adopted IFRS 9 for the year ended 31 December 2016).
- IFRS 15 – Revenue from Contracts with customers (effective 1 January 2018).
- IFRS 16 Leases (effective 1 January 2019).

The Group does not expect any significant impact on the Groups' financial position and results for the standards that are not yet adopted.

3.2 New Standards and Interpretations issued and effective

(i) The Group has adopted the following amended International Accounting Standards/International Financial Reporting Standards as of 1 January 2017:

- Amendments to IAS 7 : Statement of cashflows dosclosure initiative;
- Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for unrealised Losses
- Amendments to IFRS 12 Disclosure of Interests in Other Entities: Clarification of the scope of disclosure requirements in IFRS 12

The above amendments to IFRSs which are effective for annual accounting periods starting from 1 January 2017 did not have any material impact on the accounting policies, financial position or performance of the Group.

3.3 Summary of significant accounting policies

Financial assets and financial liabilities

i. Recognition and initial measurement

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue.

ii. Classification

Financial assets

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL. A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

The Group makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- The stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, realising cash flows through the sale of the assets and holding it for liquidity purposes;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed; and
- The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Group considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Group considers:

- Contingent events that would change the amount and timing of cash flows;
- Leverage features;
- Prepayment and extension terms;
- Terms that limit the Group's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- Features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Group changes its business model for managing financial assets.

Financial liabilities

The Group classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised cost.

iii. Derecognition

Financial assets

The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

If the terms of a financial asset are modified, the Group evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and a new financial asset is recognised at fair value.

A financial asset (in whole or in part) is derecognised where:
- the rights to receive cash flows from the asset have expired;
- the Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Group has transferred substantially all the risks and rewards of ownership or (b) when it has neither transferred or retained substantially all the risks and rewards and when it no longer has control over the financial asset, but has transferred control of the asset.

Financial liabilities
The Group derecognises a financial liability when its contractual obligations are discharged or cancelled ,or expire.

Financial assets designation at fair value through profit or loss
The Group designated certain financial assets as at FVTPL because the assets were managed, evaluated and reported internally on a fair value basis.

Deposits and due from banks and other financial institutions
These are stated at cost, adjusted for effective fair value hedges, less any amounts written off and provision for impairment.

Loans and Advances
Loans and advances measured at amortised cost, they are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method, and adjusted for effective fair value hedges and net of interest suspended, provision for impairment and any amounts written off.

Investment securities
The 'investment securities' includes:
- Debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;
- Debt and equity investment securities mandatorily measured at FVTPL or designated as at FVTPL; these are at fair value with changes recognised immediately in profit or loss;
- Debt securities measured at FVOCI; and
- Equity investment securities designated as at FVOCI.

For debt securities measured at FVOCI, gains and losses are recognised in OCI, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:
- Interest revenue using the effective interest method;
- Expected Credit Loss and reversals; and
- Foreign exchange gains and losses.

When debt security measured at FVOCI is impaired or derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

The Group elects to present in OCI changes in the fair value of certain investments in equity instruments. The election is made on an instrument-by-instrument basis on initial recognition and is irrevocable.

Gains and losses on such equity instruments are never reclassified to profit or loss and no impairment is recognised in profit or loss. Dividends are recognised in profit or loss, unless they clearly represent a recovery of part of the cost of the investment, in which case they are recognised in OCI. Cumulative gains and losses recognised in OCI are transferred to retained earnings on disposal of an investment.

Fair value measurement
The Group measures financial instruments, such as, derivatives at fair value at each balance sheet date. Also, fair values of financial instruments measured at amortised cost are disclosed in Note 39.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:
- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability, the principal or the most advantageous market must be accessible to by the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The fair value of financial instruments that are quoted in an active market is determined by reference to market bid priced respectively at the close of business on the statement of position date.

In case of unquoted investments, the Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

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; and

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

For assets and liabilities that are recognised in the consolidated financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

The Group's Risk Management determines the policies and procedures for fair value measurement. For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

Impairment
The Group recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:
- Financial assets that are debt instruments;
- Financial guarantee contracts issued; and
- Loan commitments issued.

No impairment loss is recognised on equity investments.

The Group measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:
- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition.

3 ACCOUNTING POLICIES (continued)

3.3 Summary of significant accounting policies (continued)

Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

Financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive);

Financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;

Undrawn loan commitments and Letter of credit: as the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and

Financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group expects to recover.

The determination of the IFRS 9 provision results from a two-step approach.

As step 1, the facilities will have to be allocated to one of the three impairment stages by determining whether a significant increase in credit risk has occurred since initial recognition or whether the facility has been credit impaired.

As step 2, the expected credit loss is calculated i.e., 12-month expected loss for all facilities in stage 1 and lifetime expected credit loss for all facilities in stage 2. The facilities in stage 3 are covered by specific provisions.

Credit-impaired financial assets

At each reporting date, the Group assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- Significant financial difficulty of the borrower or issuer;
- A breach of contract such as a default or past due event;
- The restructuring of a loan or advance by the Group on terms that the Group would not consider otherwise;
- It is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- The disappearance of an active market for a security because of financial difficulties.

In making an assessment of whether an investment in sovereign debt, other than that of the home country sovereign (i.e. Bahrain), is credit-impaired, the Group considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.

The exposure to the home country sovereign i.e. Bahrain is considered to be low risk and fully recoverable and hence no ECL is measured.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- Financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- Loan commitments and financial guarantee contracts: as a provision;
- Where a financial instrument includes both a drawn and an undrawn component, and the Group has identified the ECL on the loan commitment/off balance sheet component separately from those on the drawn component: the Group presents a loss allowance for drawn components. The amount is presented as a deduction from the gross carrying amount of the drawn component. Loss allowance for undrawn components is presented as a provision in other liabilities; and
- Debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve is presented as a provision.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Term borrowings

Financial instruments or their components issued by the Group, which are not designated at fair value through consolidated statement of profit or loss, are classified as liabilities under 'term borrowings', where the substance of the contractual arrangement results in the Group having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

After initial measurement, term borrowings are subsequently measured at amortised cost using the effective interest rate. Amortised cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the effective interest rate.

Investment in associated companies and joint ventures

The Group's investments in its associate and joint venture are accounted for using the equity method. Under the equity method, the investment in an associate or a joint venture is initially recognised at cost.

The carrying amount of the investment is adjusted to recognise changes in the Group's share of net assets of the associate or joint venture since the acquisition date. Goodwill relating to the associate or joint venture is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement 'have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.

The considerations made in determining significant influence or joint control are similar to those necessary to determine control over subsidiaries.

The statement of profit or loss reflects the Group's share of the results of operations of the associate or joint venture. Any change in OCI of those investees is presented as part of the Group's OCI. In addition, when there has been a change recognised directly in the equity of the associate or joint venture, the Group recognises its share of any changes, when applicable, in the statement of changes in equity. Unrealised gains and losses resulting from transactions between the Group and the associate or joint venture are eliminated to the extent of the interest in the associate or joint venture.

The aggregate of the Group's share of profit or loss of an associate and a joint venture is charged to the statement of profit or loss outside operating profit and represents profit or loss after tax and non-controlling interests in the subsidiaries of the associate or joint ventures.

The financial statements of the associate or joint venture are prepared for the same reporting period as the 'Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognise an impairment loss on its investment in its associate or joint venture. At each reporting date, the Group determines whether there is objective evidence that the investment in the associate or joint venture is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate or joint venture and its carrying value, then recognises the loss as 'Share of profit of an associate and a joint venture' in the consolidated statement of profit or loss.

Upon loss of significant influence over the associate or joint control over the joint venture, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate or joint venture upon loss of significant influence or joint control and the fair value of the retained investment and proceeds from disposal is recognised in profit or loss.

Premises and equipment

All items of premises and equipment are initially recorded at cost. Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment, other than freehold land which is deemed to have an indefinite life.

Collateral pending sale

The Group occasionally acquires real estate in settlement of certain loans and advances to customers. Such real estate is stated at the lower of the carrying value of the related facility and the current fair value of the collateral acquired, assessed on an individual basis. If the current fair value for any individual asset is lower, a provision is created. Gains or losses on disposal, and unrealised losses on revaluation, are recognised in the consolidated statement of profit or loss.

Deposits

All money market and customer deposits are carried at the fair value of consideration received, adjusted for effective hedges, less amounts repaid.

Repurchase and resale agreements

Securities sold under agreements to repurchase at a specified future date are not derecognised from the consolidated statement of financial position as the Group retains substantially all the risks and rewards of ownership. The corresponding cash received is recognised in the consolidated statement of financial position as an asset with a corresponding obligation to return it, including accrued interest as a liability, reflecting the transaction's economic substance as a loan to the Group. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of the agreement using the effective interest rate. When the counterparty has the right to sell or repledge the securities, the Group reclassifies those securities in its consolidated statement of financial position, as appropriate.

Conversely, securities purchased under agreements to resell at a specified future date are not recognised in the consolidated statement of financial position. The consideration paid, including accrued interest, is recorded in the consolidated statement of financial position, reflecting the transaction's economic substance as a loan by the Group. The difference between the purchase and resale prices is recorded in interest income and is accrued over the life of the agreement using the effective interest rate. If securities purchased under agreement to resell are subsequently sold to third parties, the obligation to return the securities is recorded as a short sale and measured at fair value with any gains or losses included in 'net interest income'.

Taxation

There is no tax on corporate income in the Kingdom of Bahrain. Taxation on foreign operations is provided in accordance with the fiscal regulations of the respective countries in which the Group operates.

Employees' end of service benefits

Costs relating to employees' end of service benefits are accrued in accordance with actuarial and other valuations as required by regulations applicable in each location.

Share-based payment transactions

For equity-settled shared-based payment transactions the Group measures the services received, and the corresponding increase in equity at the fair value of the services received by reference to the fair value of the equity instruments granted. The fair value of those equity instruments is measured at grant date. The fair value so calculated at the grant date is recognised as an expense in the consolidated statement of profit or loss over the vesting period, with a corresponding credit to retained earnings. When an employee leaves the Group during the vesting period the shares granted stand forfeited and any amount recognised in respect of these forfeited shares is reversed through the consolidated statement of profit or loss.

Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) and the costs to settle the obligation are both probable and able to be reliably measured.

Treasury stock

Treasury stock is deducted from equity and is stated at cost. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of own equity instruments.

Proposed dividends

Proposed dividends are included as part of equity and only recognised as liabilities when approved by the shareholders. The payment of a dividend also requires the prior approval of the CBB.

Financial guarantees

In the ordinary course of business, the Group gives financial guarantees, consisting of letters of credit, guarantees and acceptances. All such guarantees are treated as memorandum liabilities and are disclosed as part of contingent liabilities. Financial guarantees are initially recognised in the consolidated financial statements at fair value, in 'other liabilities', being the premium received. Subsequent to initial recognition, the Group's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee. Any increase in the liability relating to financial guarantees is taken to the consolidated statement of profit or loss in 'net provision for impairment'. The premium received is recognised in the consolidated statement of profit or loss in 'fee and commission income' on a straight line basis over the life of the guarantee.

Derivatives

The Group enters into derivative instruments including futures, forwards, swaps, and options in the foreign exchange and capital markets. Derivatives are stated at fair value. Derivatives with positive market values are included in 'other assets' and derivatives with negative market values are included in 'other liabilities' in the consolidated statement of financial position.

3 ACCOUNTING POLICIES (continued)

3.3 Summary of significant accounting policies (continued)

Derivatives (continued)

Certain derivatives embedded in other financial instruments are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host contract and the host contract is not carried at fair value through the consolidated statement of profit or loss. These embedded derivatives are measured at fair value with the changes in fair value recognised in the consolidated statement of profit or loss.

Hedge accounting

The Group makes use of derivative instruments to manage exposures to interest rate and foreign currency risks. In order to manage particular risks, the Group applies hedge accounting for transactions which meet the specified criteria.

At inception of the hedging relationship, the management undertake a formal designation and documentation. This includes the Group's risk management objective underlying, the hedging relationship and how that fits within the overall risk management strategy. The documentation also includes an identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the entity will assess whether the hedging relationship meets the hedge effectiveness requirements. IFRS 9 also requires documentation of the hedge ratio and potential sources of ineffectiveness.

A hedging relationship qualifies for hedge accounting if it meets all of the following effectiveness requirements:

- there is 'an economic relationship' between the hedged item and the hedging instrument;
- the effect of credit risk does not 'dominate the value changes' that result from that economic relationship; and
- the hedge ratio of the hedging relationship is the same as that resulting from the quantity of hedged item that the entity actually hedges and the quantity of the hedging instrument that the entity actually uses to hedge that quantity of hedged item.

The Group performs a hedge effectiveness assessment in a similar manner as at the inception of the hedging relationship and subsequently on every reporting period.

Classification of Hedge accounting

For the purposes of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability; and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a forecasted transaction.

Fair value hedges

In relation to fair value hedges, which meet the conditions for hedge accounting, any gain or loss from remeasuring the hedging instrument to fair value is recognised immediately in the consolidated statement of profit or loss. The hedged item is adjusted for fair value changes and the difference relating to the risk being hedged is recognised in the consolidated statement of profit or loss.

Cash flow value hedges

In relation to cash flow hedges which meet the conditions for hedge accounting the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised initially in equity and the ineffective portion is recognised in the consolidated statement of profit or loss. The gains or losses on effective cash flow hedges recognised initially in equity are either transferred to the consolidated statement of profit or loss in the period in which the hedged transaction impacts the consolidated statement of profit or loss or included in the initial measurement of the cost of the related asset or liability.

For hedges which do not qualify for hedge accounting, any gains or losses arising from changes in the fair value of the hedging instrument are taken directly to the consolidated statement of profit or loss for the year.

Discontinuation of hedges

A hedging relationship is discontinued in its entirety when as a whole it ceases to meet the qualifying criteria of the hedging relationship. Voluntary discontinuation when the qualifying criteria are met is prohibited. In the event of discontinuation, any subsequent changes in fair value of the hedging instrument are recognized in profit or loss. For effective fair value hedges of financial instruments with fixed maturities any adjustment arising from hedge accounting is amortised over the remaining term to maturity. For effective cash flow hedges, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the hedged transaction occurs. If the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the consolidated statement of profit or loss.

Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and are, accordingly, not included in the consolidated statement of financial position.

Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Group intends to settle on a net basis.

Recognition of income and expenses

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

Interest income and loan commitment fees, which are considered an integral part of the effective yield of a financial asset, are recognised using the effective yield method unless collectability is in doubt. The recognition of interest income is suspended when loans become impaired, such as when overdue by more than ninety days. Notional interest is recognised on impaired loans and other financial assets based on the rate used to discount future cash flows to their net present value based on the original effective interest rate.

Interest expense is recognised using the effective yield method.

Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

Other fees receivable are recognised when earned. Dividend income is recognised when the right to receive payment is established.

Where the Group enters into an interest rate swap to change interest from fixed to floating (or vice versa) the amount of interest income or expense is adjusted by the net interest on the swap until the hedges are effective.

Foreign currencies

i. Transactions and balances

Transactions in foreign currencies are initially recorded at the functional currency rate of exchange ruling at the date of transaction.

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange at the statement of financial position date. All differences arising on non-trading activities are taken to 'other income' in the consolidated statement of profit and loss, with the exception of differences on foreign currency borrowings that provide an effective hedge against a net investment in a foreign entity. These differences are taken directly to equity until the disposal of the net investment, at which time they are recognised in the consolidated statement of profit or loss.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined. Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operations and translated at closing rate.

ii. Group companies
As at the reporting date, the assets and liabilities of subsidiaries and overseas branches are translated into the Group's presentation currency at the rate of exchange as at the statement of financial position date, and their statements of income are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are taken directly to a separate component of equity through the consolidated statement of comprehensive income. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the consolidated statement of profit or loss.

Cash and cash equivalents
Cash and cash equivalents comprise cash and balances with central banks (excluding mandatory reserve deposits), treasury bills, deposits and due from banks and other financial institutions with original maturities of ninety days or less.

3.4 Significant accounting judgments and estimates
In the process of applying the Group's accounting policies, management has exercised judgment and estimates in determining the amounts recognised in the consolidated financial statements. The most significant uses of judgment and estimates are as follows:

Going concern
The Group's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group 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 Group's ability to continue as a going concern. Therefore, the consolidated financial statements continue to be prepared on the going concern basis.

Fair value of financial instruments
Where the fair values of financial assets and financial liabilities recorded in the consolidated statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data is not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities.

Classification of financial assets
Assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding.

Impairment of financial instruments
Assessment of whether credit risk on the financial asset has increased significantly since initial recognition and incorporation of forward-looking information in the measurement of ECL. Refer to note 32 for further details.

Impairment losses on loans and advances and investments
The Group reviews its individually significant loans and advances at each statement of financial position date to assess whether an impairment loss should be recorded in the consolidated statement of profit or loss. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the Group makes judgments about the borrower's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

4 CASH AND BALANCES WITH CENTRAL BANKS

	2017 BD '000	2016 BD '000
Cash	**18,597**	20,853
Current accounts and placements with central banks	**370,537**	216,167
Mandatory reserve deposits with central banks	**80,302**	77,348
	469,436	314,368

Mandatory reserve deposits are not available for use in the Group's day to day operations.

5 TREASURY BILLS
These are short term treasury bills issued by the Government of the Kingdom of Bahrain which are carried at amortized cost, and Republic of India which are carried at FVOCI. The impairment allowance on the same is BD 0.351 thousand (31 December 2016 BD 0.228 thousand).

At 31 December 2017, treasury bills issued by Government of the Kingdom of Bahrain includes short term Islamic Sukuk amounting BD 5,000 thousand (2016: BD 48,527 thousand).

6 DEPOSITS AND AMOUNTS DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

	2017 BD '000	2016 BD '000
Deposits with banks and other financial institutions	**190,416**	278,817
Other amounts due from banks	**33,409**	39,597
Less: Allowance for impairment	**(1)**	(7)
	223,824	318,407

7 LOANS AND ADVANCES TO CUSTOMERS

	2017 BD '000	2016 BD '000
Loans and advances to customers at amortised cost:		
Commercial loans and overdrafts	**1,337,637**	1,429,210
Consumer loans	**515,341**	464,830
	1,852,978	1,894,040
Less: Allowance for impairment	**(112,327)**	(126,902)
	1,740,651	1,767,138

7 LOANS AND ADVANCES TO CUSTOMERS (continued)

Movements in allowance for impairment are as follows:

i. Commercial loans and overdrafts

	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit- impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total ECL BD '000
2017				
Balance at 1 January	**2,623**	**38,597**	**67,331**	**108,551**
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12 month ECL	**1,600**	**(1,600)**	**–**	**–**
Transfer to lifetime ECL not credit-impaired	**(208)**	**12,099**	**(11,891)**	**–**
Transfer to lifetime ECL credit-impaired	**(16)**	**(25,062)**	**25,078**	**–**
Net remeasurement of loss allowance	**630**	**6,684**	**24,052**	**31,366**
Recoveries/write-backs	**–**	**–**	**(4,690)**	**(4,690)**
Amounts written off during the year	**–**	**–**	**(42,575)**	**(42,575)**
Foreign exchange and other movements	**–**	**215**	**721**	**936**
Balance at end of year	**4,629**	**30,933**	**58,026**	**93,588**
2016				
Balance at 1 January – on adoption of IFRS 9	2,437	42,661	51,357	96,455
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12 month ECL	2,181	(2,181)	–	–
Transfer to lifetime ECL not credit-impaired	(245)	249	(4)	–
Transfer to lifetime ECL credit-impaired	–	(10,407)	10,407	–
Net remeasurement of loss allowance	(1,750)	8,275	21,892	28,417
Recoveries/write-backs	–	–	(5,499)	(5,499)
Amounts written off during the year	–	–	(9,414)	(9,414)
Foreign exchange and other movements	–	–	(1,408)	(1,408)
Balance at end of year	2,623	38,597	67,331	108,551

ii. Consumer loans

	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit- impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total ECL BD '000
2017				
Balance at 1 January	**2,951**	**5,085**	**10,315**	**18,351**
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12 month ECL	**440**	**(440)**	**–**	**–**
Transfer to lifetime ECL not credit-impaired	**(38)**	**38**	**–**	**–**
Transfer to lifetime ECL credit-impaired	**–**	**–**	**–**	**–**
Net remeasurement of loss allowance	**799**	**1,668**	**912**	**3,379**
Recoveries/write-backs	**–**	**–**	**(1,143)**	**(1,143)**
Amounts written off during the year	**–**	**–**	**(2,322)**	**(2,322)**
Foreign exchange and other movements	**–**	**–**	**474**	**474**
Balance at end of year	**4,152**	**6,351**	**8,236**	**18,739**
2016				
Balance at 1 January – on adoption of IFRS 9	2,813	5,669	10,275	18,757
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12 month ECL	565	(565)	–	–
Transfer to lifetime ECL not credit-impaired	(90)	90	–	–
Transfer to lifetime ECL credit-impaired	–	–	–	–
Net remeasurement of loss allowance	(337)	(109)	2,413	1,967
Recoveries/write-backs	–	–	(1,132)	(1,132)
Amounts written off during the year	–	–	(1,222)	(1,222)
Foreign exchange and other movements	–	–	(19)	(19)
Balance at end of year	2,951	5,085	10,315	18,351

At 31 December 2017, interest in suspense on past due loans that are fully impaired amounts to BD 15,049 thousand (31 December 2016: BD 21,572 thousand), are treated as as a memorandum account.

The fair value of the collateral consisting of cash, securities and real estate that the Group holds relating to loans individually determined to be impaired at 31 December 2017 amounts to BD 25,712 thousand (2016: BD 54,229 thousand).

At 31 December 2017, loans and advances includes Islamic financing facilities provided by the Group to corporates amounting BD 108,525 thousand (2016: BD 109,466 thousand). These mainly consists of Murabaha and Ijarah financing facilities.

8 INVESTMENT SECURITIES

	FVTPL BD '000	FVOCI BD '000	Amortised cost BD '000	2017 Total BD '000
Quoted investments				
Government bonds	**–**	**354,128**	**13,400**	**367,528**
Other bonds	**3,184**	**206,804**	**–**	**209,988**
Equities	**–**	**35,242**	**–**	**35,242**
	3,184	**596,174**	**13,400**	**612,758**
Unquoted investments				
Government bonds	**–**	**–**	**105,458**	**105,458**
Other bonds	**82**	**584**	**69**	**735**
Equities	**–**	**29,457**	**–**	**29,457**
Managed funds	**1,196**	**–**	**–**	**1,196**
	1,278	**30,041**	**105,527**	**136,846**
	4,462	**626,215**	**118,927**	**749,604**
Allowance for impairment on debt investment	**–**	**(615)**	**(4)**	**(619)**
Balance at 31 December 2017	**4,462**	**625,600**	**118,923**	**748,985**

	FVTPL BD '000	FVOCI BD '000	Amortised cost BD '000	2016 Total BD '000
Quoted investments				
Government bonds	–	349,331	13,271	362,602
Other bonds	3,780	213,148	–	216,928
Equities	5,263	38,480	–	43,743
	9,043	600,959	13,271	623,273
Unquoted investments				
Government bonds	–	–	109,807	109,807
Other bonds	–	–	–	–
Equities	–	34,220	–	34,220
Managed funds	1,443	–	–	1,443
	1,443	34,220	109,807	145,470
	10,486	635,179	123,078	768,743
Allowance for impairment on debt investment	–	(604)	(5)	(609)
Balance at 31 December 2016	10,486	634,575	123,073	768,134

At 31 December 2017, investment securities include long term Islamic Sukuk amounting to BD 79,481 thousand (2016: BD 76,659 thousand).

Allowance for impairment

The movements in allowance for impairment of investment securities are as follows:

	Stage 1: 12-month ECL* BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total ECL BD '000
2017				
Government and other bonds at FVOCI or Amortized Cost				
Balance at 1 January	**164**	**445**	**–**	**609**
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12-month ECL	**92**	**(92)**	**–**	**–**
Transfer to lifetime ECL not credit-impaired	**(44)**	**44**	**–**	**–**
Transfer to lifetime ECL credit-impaired	**–**	**–**	**–**	**–**
Net remeasurement of loss allowance	**(87)**	**185**	**–**	**98**
Financial assets that have been derecognised	**(38)**	**(50)**	**–**	**(88)**
Write-offs	**–**	**–**	**–**	**–**
Recoveries of amounts previously written off	**–**	**–**	**–**	**–**
Balance at 31 December	**87**	**532**	**–**	**619**
2016				
Government and other bonds at FVOCI or Amortized Cost				
Balance at 1 January – on adoption of IFRS 9	162	209	22,982	23,353
Changes due to financial assets recognised in opening balance that have:				
Transfer to 12-month ECL	46	(46)	–	–
Transfer to lifetime ECL not credit-impaired	(13)	13	–	–
Transfer to lifetime ECL credit-impaired	–	–	–	–
Net remeasurement of loss allowance	(1)	292	–	291
Financial assets that have been derecognised	(30)	(23)	–	(53)
Write-offs	–	–	(21,576)	(21,576)
Recoveries of amounts previously written off	–	–	(1,406)	(1,406)
Balance at 31 December	164	445	–	609

The loss allowance of the FVOCI is not recognised in the statement of financial position because the carrying amount of debt investment securities at FVOCI is at their fair value.

* The above table includes ECL of government and other bonds measured at amortized cost of BD 4 thousand (2016: 5 thousand)

9 INVESTMENTS IN ASSOCIATED COMPANIES AND JOINT VENTURES

The Group has a 23.03% (2016: 23.03%) shareholding in Bahrain Commercial Facilities Company B.S.C. ("BCFC"), incorporated in the Kingdom of Bahrain, which is engaged in consumer financing, insurance, dealing in real estate and automobiles.

The Group has a 50% (2016: 50%) stake in Sakana Holistic Housing Solutions B.S.C. (c) ("Sakana"), a jointly controlled company incorporated in the Kingdom of Bahrain which is engaged in Islamic real estate financing, which is under liquidation.

The Group has a 22% (2016: 22%) shareholding in The Benefit Company B.S.C. (c) incorporated in the Kingdom of Bahrain which is engaged in ancillary services to provide payment systems and other related financial services for the benefit of commercial banks and their customers in the Kingdom of Bahrain.

The Group has a 40% (2016: 40%) stake in BBK Geojit securities K.S.C., a jointly controlled company incorporated in the State of Kuwait.

The Group has a 24.27% (2016: 24.27%) stake in Bahrain Liquidity Fund, an investment vehicle established in Kingdom of Bahrain to enhance liquidity in the market and to close the valuation gap between securities listed on Bahrain Bourse and their regional peers.

The Group has a 50% (2016: 50%) stake in Aegila Capital Management Limited, a joint venture company incorporated in the United Kingdom which is engaged in capital market advisory services for alternative investments with particular focus in the real estate.

The following tables illustrate the summarised financial information of the Group's interest in its associated companies and joint ventures:

	2017 BD '000	2016 BD '000
Carrying amount of investment in associated companies and joint ventures		
At 1 January	**43,923**	35,823
Acquisitions during the year	**–**	10,694
Share of profit	**5,519**	5,467
Dividends received from associated companies	**(2,394)**	(2,103)
Change in unrealised fair values – associated companies (note 17)	**342**	6
Change in Foreign exchange translation adjustments	**68**	(2)
Reclassification to FVOCI	**–**	(4,962)
Capital distribution	**(500)**	(1,000)
At 31 December	**46,958**	43,923

	2017 BD '000	2016 BD '000
Share of associated companies and joint ventures statements of financial position		
Current and non-current assets	**102,965**	94,874
Current and non-current liabilities	**(56,007)**	(50,951)
Net assets	**46,958**	43,923
Share of associated companies and joint ventures revenues		
Revenue	**11,650**	10,987

Investment in associated companies and joint ventures includes the Group investment in BCFC which is considered to be a material associate. The following table illustrates the financial information of the Group's investment in BCFC:

	2017 BD '000	2016 BD '000
Net interest income	**23,569**	21,504
Gross profit on automotive sales	**6,497**	6,671
Other operating income	**11,805**	12,866
Total operating income	**41,871**	41,041
Operating expense	**(19,081)**	(17,847)
Other expense	**(3,568)**	(2,625)
Profit for the year	**19,222**	20,569
Group's share of profit for the year	**4,427**	4,737

	2017 BD '000	2016 BD '000
Assets		
Cash and balances with banks	**2,868**	5,311
Loans and advances to customers	**290,606**	265,318
Inventories	**38,196**	26,752
Other assets	**47,911**	47,618
Total assets	**379,581**	344,999
Liabilities		
Bank overdrafts	**1,598**	1,959
Trade and other payables	**18,483**	18,851
Bank term loans	**184,344**	161,628
Bonds issued	**39,882**	39,816
Total liabilities	**244,307**	222,254
Donation reserve	**(679)**	(872)
Equity	**134,595**	121,873
Proportion of the Group's ownership	**23.03%**	23.03%
	30,997	28,067

The figures reported above for BCFC are based on 30 September reviewed financial statements adjusted for expected performance in the last quarter.

The market value of the Group's investment in BCFC is BD 25,957 thousand (2016: BD 25,205 thousand) compared to the carrying value of BD 30,997 thousand (2016: BD 28,067 thousand) as at 31 December 2017.

10 INTEREST RECEIVABLE AND OTHER ASSETS

	2017 BD '000	2016 BD '000
Interest receivable	**13,373**	14,783
Accounts receivable	**29,458**	23,002
Positive fair value of derivatives (note 26)	**7,714**	6,938
Prepaid expenses	**1,677**	1,777
Deferred tax	**1,631**	2,216
Collateral pending sale	**9,439**	4,671
Other	**16,388**	11,382
	79,680	64,769

11 PREMISES AND EQUIPMENT

	Freehold land BD '000	Properties and buildings BD '000	Furniture and equipment BD '000	Capital work in progress BD '000	Total BD '000
Net book value at 31 December 2017	**8,849**	**11,173**	**5,310**	**1,104**	**26,436**
Net book value at 31 December 2016	8,241	10,603	5,123	216	24,183

The depreciation charge for the year amounted to BD 3,435 thousand (2016: BD 3,430 thousand).

12 TERM BORROWINGS

The term borrowings were obtained for general financing purposes and comprise:

Amount of facility US$ '000	Rate of interest	Maturity Year	2017 BD '000	2016 BD '000
145,140	Libor + 1.25%	2017	**–**	8,509
129,860	Libor + 1.75%	2018	**48,212**	46,800
400,000	3.50%	2020	**150,800**	150,800
			199,012	206,109

13 CUSTOMERS' CURRENT, SAVINGS AND OTHER DEPOSITS

	2017 BD '000	2016 BD '000
Term deposits	**1,392,623**	1,362,104
Current accounts	**628,389**	571,324
Savings accounts	**532,588**	483,129
Other accounts	**69,977**	77,158
	2,623,577	2,493,715

14 INTEREST PAYABLE AND OTHER LIABILITIES

	2017 BD '000	2016 BD '000
Accrued expenses	**38,106**	36,585
Interest payable	**14,828**	13,405
Accounts payable	**14,815**	16,750
Negative fair value of derivatives (note 26)	**6,639**	9,775
Other	**9,018**	7,212
Allowance for impairment*	**1,484**	864
	84,890	84,591

* This represents allowance for impairment on financial contracts issued as of 31 December 2017, the sum of ECL provisions of BD 1,484 thousand (2016: 864 thousand).

15 EQUITY

Share capital	2017 BD '000	2016 BD '000
Authorised		
1,500,000,000 shares of BD 0.100 each	**150,000**	150,000
Issued and fully paid		
1,081,647,952 shares (2016: 1,081,647,952 shares) of BD 0.100 each	**108,165**	108,165
*Treasury stock**	**(998)**	(1,206)

* Treasury stock represents the purchase by the Bank of its own shares. At the end of the year, the Bank held 2,774,562 (2016: 6,098,267) of its own shares.

Share premium

The share premium arising on issue of ordinary shares is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the CBB.

Employee Performance Share Plan

The Group has an Employee Performance Share Plan under which shares are granted to certain eligible employees (note 40).

Unclaimed dividends

During the year, the Group transferred BD 8 thousand (2016: BD 27 thousand) to equity as unclaimed dividends by the shareholders. As per the Group policy and procedures, any unclaimed dividends in excess of 10 years are transferred to equity, however will be available to the respective shareholder for any future claims.

Perpetual tier 1 convertible capital securities

During the year 2016, the Bank completed an issue of BD 86,098 thousand Basel III compliant Additional Tier I Convertible Perpetual Capital Securities. Distribution Payment Amounts shall be payable subject to and in accordance with terms and conditions on the outstanding nominal amount of the Capital Securities at rate of 8.25 percent per annum. These securities are recognised under equity in the consolidated statement of financial position and the corresponding coupon on those securities are accounted as appropriation of profits. Expenses relating to this issuance have been included in retained earnings during 2016. Securities' holders will not have a right to claim the coupon and such event will not be considered as event of default.

16 RESERVES

Statutory reserve

The statutory reserve has been created in accordance with the Bahrain Commercial Companies Law. The Bank transfers 10% of its annual profits to its statutory reserve till such time as the reserve equals 50% of the issued share capital of the Bank. During the year, the Bank had not transferred to statutory reserve (2016: Nil) as the statutory reserve reached 50% of the issued share capital. The reserve is not available for distribution, except in circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the Central Bank of Bahrain.

General reserve

The general reserve has been built up in accordance with the provisions of the Bank's articles of association and underlines the shareholders' commitment to enhance the strong equity base of the Bank. The general reserve is distributable subject to the approval of the Central Bank of Bahrain.

17 CUMULATIVE CHANGES IN FAIR VALUES

	2017 BD '000	2016 BD '000
Fair value through other comprehensive income		
At 1 January	**(13,609)**	(28,950)
Transfer to retained earnings on sale/write off of equity securities	**(1,325)**	3,738
Transfer to P&L on sale of investment securities	**(5,019)**	(2,095)
Transferred to P&L on impairment	**98**	238
Fair value changes on investment securities at FVOCI during the year	**11,282**	13,460
At 31 December	**(8,573)**	(13,609)
Cash flow hedges		
At 1 January	**(60)**	(234)
Change in unrealised fair values	**(58)**	168
Change in unrealised fair values – associated companies (note 9)	**342**	6
At 31 December	**224**	(60)
	(8,349)	(13,669)

18 PROPOSED APPROPRIATIONS

	2017 BD '000	2016 BD '000
Cash dividend	**37,761**	32,266
Stock dividend	**–**	–
Transfer to general reserve	**–**	–
Donations	**1,400**	1,400
	39,161	33,666

The Board of Directors has proposed cash dividend of BD 0.035 per share (2016: BD 0.030 per share), net of treasury stock as of 31 December 2017. The Bank paid dividend of BD 0.030 per share (2016: BD 0.025 per share).

The above appropriations will be submitted for approval at the Annual General Assembly of the Shareholders to be held on 20 March 2018. The payment of dividend is also subject to the approval of the Central Bank of Bahrain.

19 INTEREST AND SIMILAR INCOME

	2017 BD '000	2016 BD '000
Loans and advances to customers	**94,030**	91,714
Investment securities	**25,349**	22,871
Deposits and amounts due from banks and other financial institutions	**6,661**	4,806
Treasury bills	**10,943**	9,165
	136,983	128,556

20 OTHER INCOME

	2017 BD '000	2016 BD '000
Fee and commission income	**49,253**	44,061
Dividend income	**3,828**	3,540
Realised gains on investment securities	**3,965**	2,707
Gain on foreign exchange	**5,214**	5,149
Others	**2,533**	1,539
	64,793	56,996
Fee and commission expense	**(18,159)**	(14,784)
	46,634	42,212

Included in fee and commission income is BD 42 thousand (2016: BD 67 thousand) relating to trust and other fiduciary activities.

21 BASIC AND DILUTED EARNINGS PER SHARE

Basic earnings per share

Basic earnings per share for the year are calculated by dividing the net profit for the year attributable to the owners of the Bank less distribution on perpetual tier 1 convertible capital securities, by the weighted average number of shares outstanding during the year.

Diluted earnings per share

Diluted earnings per share for the year are calculated by dividing the net profit for the year attributable to the owners of the Bank less distribution on perpetual tier 1 convertible capital securities, by the weighted average number of shares outstanding during the year plus the weighted average number of ordinary shares that would be issued on the conversion into ordinary shares:

	2017	2016
Profit for the year attributable to the owners of the Bank (BD '000)	**58,685**	56,410
(Less): Distribution on perpetual tier 1 convertible capital securities (BD '000)	**(7,103)**	(3,552)
Adjusted net profit for the year attributable to the owners of the Bank	**51,582**	52,858
Weighted average number of shares, net of treasury stock, outstanding during the year	**1,077,809,434**	1,070,557,685
Basic earnings per share (BD)	**0.048**	0.049
Weighted average number of ordinary shares adjusted for the effect of dilution	**1,293,053,214**	1,285,801,465
Diluted earnings per share (BD)	**0.045**	0.044

22 OPERATING SEGMENTS

Segment information

For management purposes the Group is organised into four major business segments:

Retail banking

Principally handling individual customers' deposits and providing consumer finance type loans, overdrafts, credit facilities and funds transfer facilities, credit cards and foreign exchange.

Corporate banking

Principally handling loans and other credit facilities, deposit and current accounts for corporate and institutional customers in Bahrain.

International banking

Principally handling loans and other credit facilities, deposit and current accounts for international corporate and institutional customers. This also covers the operations of the overseas units.

Investment, treasury and other activities

Principally providing money market, trading and treasury services as well as the management of the Group's funding operations. Investment activities involve handling investments in local and international markets, investment advisory services and funds management. Other activities also include business process outsourcing services.

These segments are the basis on which the Group reports its information to the chief operating decision maker. Transactions between segments are generally recorded at estimated market rates on an arm's length basis. Interest is charged/credited to business segments based on a transfer pricing rate which approximates the marginal cost of funds on a matched funded basis.

Segment information for the year ended 31 December 2017 was as follows:

	Retail banking BD '000	Corporate banking BD '000	International banking BD '000	Investment, treasury and other activities BD '000	Total BD '000
Interest income	**29,080**	**37,107**	**32,379**	**38,417**	**136,983**
Interest expense	**(3,159)**	**(10,094)**	**(8,937)**	**(23,887)**	**(46,077)**
Internal fund transfer price	**(1,715)**	**(1,686)**	**(6,167)**	**9,568**	**–**
Net Interest Income	**24,206**	**25,327**	**17,275**	**24,098**	**90,906**
Other Operating Income	**23,246**	**4,399**	**5,619**	**13,370**	**46,634**
Operating income before share of profit of associated companies and joint ventures	**47,452**	**29,726**	**22,894**	**37,468**	**137,540**
Net provision for impairment on loans and advances to customers	**(5,082)**	**(18,089)**	**(5,741)**	**–**	**(28,912)**
Net provision for impairment on investments	**–**	**–**	**–**	**(98)**	**(98)**
Segment result	**17,093**	**(2,344)**	**1,987**	**36,976**	**53,712**
Share of profit of associated companies and joint ventures	**5,448**	**–**	**–**	**71**	**5,519**
Profit for the year					**59,231**
Profit attributable to non-controlling interest					**(546)**
Profit for the year attributable to the owners of the Bank					**58,685**
Segment assets	**588,906**	**681,463**	**1,250,222**	**1,152,594**	**3,673,185**
Investment in associated companies and joint ventures	**35,377**	**–**	**–**	**11,581**	**46,958**
Common assets					**42,957**
Total assets					**3,763,100**
Segment liabilities	**791,506**	**856,957**	**980,667**	**584,234**	**3,213,364**
Common liabilities					**48,901**
Total liabilities					**3,262,265**

Segment information for the year ended 31 December 2016 was as follows:

	Retail banking BD '000	Corporate banking BD '000	International banking BD '000	Investment, treasury and other activities BD '000	Total BD '000
Interest income	27,160	36,519	32,702	32,175	128,556
Interest expense	(2,576)	(7,937)	(10,531)	(21,664)	(42,708)
Internal fund transfer price	(4,387)	(4,176)	(3,995)	12,558	–
Net Interest Income	20,197	24,406	18,176	23,069	85,848
Other Operating Income	21,699	3,993	5,776	10,744	42,212
Operating income before share of profit of associated companies and joint ventures	41,896	28,399	23,952	33,813	128,060
Net provision for impairment on loans and advances to customers	(1,663)	(11,688)	(10,402)	–	(23,753)
Net writeback for impairment on investments	–	–	–	1,115	1,115
Segment result	15,050	2,754	120	33,356	51,280
Share of profit of associated companies and joint ventures	5,562	–	–	(95)	5,467
Profit for the year					56,747
Loss attributable to non-controlling interest					(337)
Profit for the year attributable to the owners of the Bank					56,410
Segment assets	537,433	700,692	1,297,251	1,089,227	3,624,603
Investment in associated companies and joint ventures	31,982	–	–	11,941	43,923
Common assets					34,031
Total assets					3,702,557
Segment liabilities	734,539	792,531	885,892	765,143	3,178,105
Common liabilities					50,237
Total liabilities					3,228,342

22 OPERATING SEGMENTS (continued)

Geographic information

The Group operates in two geographic markets: Domestic (Bahrain), Others (Middle East/Africa, Europe, North America and Asia). The following tables show the distribution of the Group's revenue and non-current assets by geographical segment, allocated based on the location in which the assets and liabilities are located, for the years ended 31 December 2017 and 31 December 2016:

	Domestic BD '000	Others BD '000	Total BD '000
31 December 2017			
Net interest income	**80,040**	**10,866**	**90,906**
Share of profit in associated companies and joint ventures	**5,448**	**71**	**5,519**
Other income	**43,092**	**3,542**	**46,634**
	128,580	**14,479**	**143,059**
Non-current assets	**21,380**	**5,056**	**26,436**

	Domestic BD '000	Others BD '000	Total BD '000
31 December 2016			
Net interest income	75,413	10,435	85,848
Share of profit in associated companies and joint ventures	5,562	(95)	5,467
Other income	38,331	3,881	42,212
	119,306	14,221	133,527
Non-current assets	20,132	4,051	24,183

Non-current assets represents premises and equipment.

23 CASH AND CASH EQUIVALENTS

Cash and cash equivalents included in the consolidated statement of cash flows includes the following as at 31 December:

	2017 BD '000	2016 BD '000
Cash (note 4)	**18,597**	20,853
Current accounts and placements with central banks (note 4)	**370,537**	216,167
Deposits and amounts due from banks and other financial institutions with original maturities of ninety days or less	**223,824**	300,584
	612,958	537,604

24 RELATED PARTY TRANSACTIONS

Related parties represent major shareholders, associates and joint ventures, directors and key management personnel of the Group and entities controlled, jointly controlled or significantly influenced by such parties. Pricing policies and terms of these transactions are approved by the Group's management.

Amounts outstanding as of the statement of financial position date in respect of transactions entered into with related parties were as follows:

	Major shareholders BD '000	Associated companies and joint ventures BD '000	Directors and key management personnel BD '000	Total BD '000
2017				
Loans and advances to customers	**–**	**24,812**	**3,132**	**27,944**
Customers' current, savings and other deposits	**216,848**	**3,848**	**8,004**	**228,700**
2016				
Loans and advances to customers	–	15,521	3,325	18,846
Customers' current, savings and other deposits	208,871	3,286	8,885	221,042

For the years ended 31 December 2017 and 31 December 2016 the Group has not recorded any impairment provision on the amounts due from related parties.

The income and expense in respect of related parties included in the consolidated statement of profit or loss are as follows:

	Major shareholders BD '000	Associated companies and joint ventures BD '000	Directors and key management personnel BD '000	Total BD '000
2017				
Interest income	**–**	**992**	**30**	**1,022**
Interest expense	**3,561**	**71**	**119**	**3,751**
2016				
Interest income	–	567	120	687
Interest expense	3,127	106	115	3,348

Compensation of the key management personnel is as follows:

	2017 BD '000	2016 BD '000
Short term employee benefits	**10,562**	10,279
Others	**698**	(31)
	11,260	10,248

Key management interest in an employee share incentive scheme

For share-based payment scheme (refer to note 40 for details).

25 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The maturity profile of the assets and liabilities at 31 December 2017 and as at 31 December 2016 given below have been determined on the basis of the remaining period at the statement of financial position date to the contractual maturity date, except in the case of customer deposits. The liquidity profile of customer deposits has been determined on the basis of the effective maturities indicated by the Group's deposit retention history.

31 December 2017	Within 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 to 12 months BD '000	Subtotal BD '000	1 to 5 years BD '000	5 to 10 years BD '000	10 to 20 years BD '000	More than 20 years BD '000	Total BD '000
Assets										
Cash and balances with central banks	389,127	–	–	–	389,127	–	–	–	80,309	469,436
Treasury bills	49,929	135,727	124,197	117,277	427,130	–	–	–	–	427,130
Deposits and amounts due from banks and other financial institutions	185,205	38,619	–	–	223,824	–	–	–	–	223,824
Loans and advances to customers	247,871	158,996	121,825	160,358	689,050	729,709	237,247	45,105	39,540	1,740,651
Investment securities	29,085	29,727	12,182	7,547	78,541	305,248	226,442	26,891	111,863	748,985
Investments in associated companies and joint ventures	–	–	–	–	–	–	–	–	46,958	46,958
Interest receivable and other assets	70,241	–	–	–	70,241	9,439	–	–	–	79,680
Premises and equipment	–	–	–	–	–	23,163	304	1,257	1,712	26,436
Total assets	971,458	363,069	258,204	285,182	1,877,913	1,067,559	463,993	73,253	280,382	3,763,100
Liabilities										
Deposits and amounts due to banks and other financial institutions	168,761	24,711	–	–	193,472	–	–	–	–	193,472
Borrowings under repurchase agreement	–	–	–	40,803	40,803	120,511	–	–	–	161,314
Term borrowings	–	–	48,212	–	48,212	150,800	–	–	–	199,012
Customers' current, savings and other deposits	344,710	76,611	56,839	35,405	513,565	53,550	–	–	2,056,462	2,623,577
Interest payable and other liabilities	84,890	–	–	–	84,890	–	–	–	–	84,890
Total liabilities	598,361	101,322	105,051	76,208	880,942	324,861	–	–	2,056,462	3,262,265
Net	373,097	261,747	153,153	208,974	996,971	742,698	463,993	73,253	(1,776,080)	500,835
Cumulative	373,097	634,844	787,997	996,971		1,739,669	2,203,662	2,276,915	500,835	

31 December 2016	Within 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 to 12 months BD '000	Subtotal BD '000	1 to 5 years BD '000	5 to 10 years BD '000	10 to 20 years BD '000	More than 20 years BD '000	Total BD '000
Assets										
Cash and balances with central banks	237,020	–	–	–	237,020	–	–	–	77,348	314,368
Treasury bills	35,780	233,931	43,887	88,037	401,635	–	–	–	–	401,635
Deposits and amounts due from banks and other financial institutions	295,207	10,455	12,318	427	318,407	–	–	–	–	318,407
Loans and advances to customers	104,292	136,801	154,280	96,613	491,986	779,317	270,083	52,013	173,739	1,767,138
Investment securities	9,360	17,353	23,955	41,029	91,697	286,899	254,736	9,368	125,434	768,134
Investments in associated companies and joint ventures	–	–	–	–	–	–	–	–	43,923	43,923
Interest receivable and other assets	56,088	96	49	52	56,285	8,484	–	–	–	64,769
Premises and equipment	–	–	–	–	–	19,879	914	1,619	1,771	24,183
Total assets	737,747	398,636	234,489	226,158	1,597,030	1,094,579	525,733	63,000	422,215	3,702,557
Liabilities										
Deposits and amounts due to banks and other financial institutions	187,518	72,311	–	82	259,911	–	–	–	–	259,911
Borrowings under repurchase agreement	645	–	–	22,058	22,703	161,313	–	–	–	184,016
Term borrowings	–	–	8,509	–	8,509	197,600	–	–	–	206,109
Customers' current, savings and other deposits	406,410	241,403	61,263	28,447	737,523	66,128	–	–	1,690,064	2,493,715
Interest payable and other liabilities	57,703	3,331	1,591	1,291	63,916	20,675	–	–	–	84,591
Total liabilities	652,276	317,045	71,363	51,878	1,092,562	445,716	–	–	1,690,064	3,228,342
Net	85,471	81,591	163,126	174,280	504,468	648,863	525,733	63,000	(1,267,849)	474,215
Cumulative	85,471	167,062	330,188	504,468		1,153,331	1,679,064	1,742,064	474,215	

26 DERIVATIVES

A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in the price of one or more underlying financial instrument, reference rate or index. In the ordinary course of business, the Group enters into various types of transactions that involve derivative financial instruments. The use of derivatives is governed by the Group's policies approved by the Board of Directors. The Group enters into derivative contracts for the purpose of reducing risks from potential movements in foreign exchange rates and interest rates inherent in the Group's non-trading assets and liabilities. The Group also enters into derivative contracts for the purpose of trading.

The table below shows the positive and negative fair values of derivative financial instruments together with their notional amounts. The notional amount is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at year end but are neither indicative of the market risk nor credit risk.

31 December 2017	Positive fair value BD '000	Negative fair value BD '000	Notional amount BD '000
Derivatives held for trading			
Forward foreign exchange contracts	**147**	**647**	**104,161**
Derivatives held as fair value hedges			
Interest rate swaps	**7,467**	**5,992**	**535,170**
Derivatives held as cash flow hedges			
Interest rate swaps	**100**	**–**	**49,010**
	7,714	**6,639**	**688,341**

31 December 2016	Positive fair value BD '000	Negative fair value BD '000	Notional amount BD '000
Derivatives held for trading			
Forward foreign exchange contracts	108	137	105,635
Derivatives held as fair value hedges			
Interest rate swaps	6,672	9,638	549,716
Derivatives held as cash flow hedges			
Interest rate swaps	158	–	57,519
	6,938	9,775	712,870

Derivative product types

Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market. Foreign currency and interest rate futures are transacted in standardised amounts on regulated exchanges and are subject to daily cash margin requirements. Forward rate agreements are effectively tailor-made interest rate futures which fix a forward rate of interest on a notional amount, for an agreed period of time starting on a specified future date.

Swaps are contractual agreements between two parties to exchange interest or foreign currency differentials based on a specific notional amount. For interest rate swaps, counterparties generally exchange fixed and floating rate interest payments based on a notional value in a single currency. For currency swaps, fixed or floating interest payments and notional amounts are exchanged in different currencies.

Options are contractual agreements that convey the right, but not the obligation, to either buy or sell a specific amount of a commodity or financial instrument at a fixed price, either at a fixed future date or at any time within a specified period. The Group does not engage in the writing of options.

Derivatives held or issued for trading purposes

Most of the Group's derivative trading activities relate to back to back customer deals. In addition, the Group takes certain foreign exchange positions with the expectation of profiting from favorable movements in prices, rates or indices. Also included under this heading are derivatives which do not meet IFRS 9 hedging requirements.

Derivatives held or issued for hedging purposes

The Group has put in place systems for the measurement and management of risk. Part of the risk management process involves managing the Group's exposure to fluctuations in foreign exchange rates (currency risk) and interest rates through asset and liability management activities. It is the Group's policy to reduce its exposure to currency and interest rate risks to acceptable levels as determined by the Board of Directors. For strategies adopted to manage interest rate and currency risk, please refer notes 35 and 36 respectively.

As part of its asset and liability management the Group uses derivatives for hedging currency and interest rate movements. This is achieved by hedging specific financial instruments, forecasted transactions as well as strategic hedging against consolidated statement of financial position exposures. In all such cases the objective of the hedging relationship, details of the hedged item and hedging instrument are documented and the transactions are accounted for as fair value or cash flow hedges, as the case may be.

Fair value hedges

Fair value hedges are used by the Group to protect it against changes in the fair value of financial assets and financial liabilities due to movements in exchange rates and interest rates. The financial instruments hedged for interest rate risk include loans, fair value through other comprehensive income debt securities, debt issued and other borrowed funds. The Group uses forward foreign exchange contracts and currency swaps to hedge against specifically identified currency risks, and interest rate swaps to hedge interest rate risk.

In these hedge relationships, the main sources of ineffectiveness is the maturity mis-matches or the hedging instruments. The hedged instruments are subject to different counterparty risks, resulting in a change to hedge effectiveness measurement elements.

At 31 December 2017, the Group held the following interest rate swaps as hedging instruments in fair value hedges of interest risk.

Risk category	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	More than 5 years
Hedge of Investment Securities					
31 December 2017					
Nominal amount (BD '000)	**–**	**471**	**15,080**	**250,387**	**269,232**
Average fixed interest rate	**–**	**3%**	**3%**	**5%**	**5%**
31 December 2016					
Nominal amount (BD '000)	1,847	5,820	13,761	226,150	302,138
Average fixed interest rate	4%	6%	4%	5%	5%

The line item in the statement of financial position where the hedging instrument included is other assets.

The amounts relating to items designated as hedged items were as follows:

	2017		2016	
	Carrying amount BD '000	**Accumulated fair value hedge adjustments on the hedged item included in the carrying amount BD '000**	Carrying amount BD '000	Accumulated fair value hedge adjustments on the hedged item included in the carrying amount BD '000
Bonds [Investment securities]	**521,316**	**(4,047)**	549,057	2,230

For the year ended 31 December 2017, the Group recognised a net loss of BD 0.5 thousand (2016: net gain of BD 1 thousand), representing the loss on the hedging instruments. The total loss on hedged items attributable to the hedged risk amounted to BD 190 thousand (2016: loss of BD 21 thousand).

Cash Flow Hedges

At 31 December 2017, the Group held the following instruments to hedge exposures to changes in interest rates and foreign currency.

	Less than 1 month	1 to 3 months	3 months to 1 year	1 to 5 years	More than 5 years
Hedge of term borrowings					
31 December 2017					
Nominal amount (BD '000)	**–**	**–**	**49,010**	**–**	**–**
Average fixed interest rate	**–**	**–**	**3%**	**–**	**–**
31 December 2016					
Nominal amount (BD '000)	–	–	8,509	49,010	–
Average fixed interest rate	–	–	2%	3%	–

The line item in the statement of financial position where the hedging instrument is included is other liabilities.

The amounts relating to items designated as hedged items were as follows:

	2017		2016	
	Carrying amount BD '000	**Cash flow reserve BD '000**	Carrying amount BD '000	Cash flow reserve BD '000
Term Borrowings	**49,010**	**100**	57,519	158

27 COMMITMENTS AND CONTINGENT LIABILITIES

Credit-related commitments

Credit-related commitments include commitments to extend credit, standby letters of credit, guarantees and acceptances which are designed to meet the requirements of the Group's customers.

Commitments to extend credit represent the unused portions of contractual commitments to make loans and revolving credits, principally in the form of loans and advances, guarantees and letters of credit. With respect to credit risk on commitments to extend credit, the Group is potentially exposed to a loss in an amount equal to the total unused commitments. However, the likely amount of loss, which cannot readily be quantified, is expected to be considerably less than the total unused commitment as most of the commitments to extend credit are contingent upon the customer maintaining specific credit standards. Commitments generally have fixed expiration dates of less than one year or other termination clauses. Since commitments may expire without being drawn upon, the total contracted amounts do not necessarily represent future cash requirements.

Letters of credit, guarantees (including standby letters of credit) and acceptances commit the Group to make payments on behalf of customers contingent upon certain conditions. Standby letters of credit, which are included under guarantees, would have market risk if issued or extended at a fixed rate of interest. However, these contracts are primarily made at a floating rate.

The Group has the following credit related commitments:

31 December 2017	**On demand BD '000**	**Less than 3 months BD '000**	**3 to 12 months BD '000**	**1 to 5 years BD '000**	**Total BD '000**
Contingencies					
Letters of credit	**1,307**	**17,481**	**18,467**	**–**	**37,255**
Guarantees	**230,620**	**–**	**–**	**–**	**230,620**
					267,875
Commitments					
Undrawn loan commitments	**117,670**	**–**	**–**	**–**	**117,670**
					117,670
					385,545

31 December 2016	On demand BD '000	Less than 3 months BD '000	3 to 12 months BD '000	1 to 5 years BD '000	Total BD '000
Contingencies					
Letters of credit	3,336	18,538	16,644	–	38,518
Guarantees	228,287	–	–	–	228,287
					266,805
Commitments					
Undrawn loan commitments	127,186	–	–	–	127,186
					127,186
					393,991

The Group does not expect all its commitments to be drawn before the expiry of the commitment.

Lease commitments

Operating lease commitments – Group as lessee

The Group has entered into commercial leases on premises. Future minimum lease payments under non-cancelable operating leases as at 31 December are as follows:

	2017 BD '000	2016 BD '000
Within one year	**815**	838
After one year but not more than five years	**1,939**	1,872
More than five years	**4,039**	4,406
	6,793	7,116

28 RISK MANAGEMENT

Efficient and timely management of risks involved in the Group's activities is critical for the financial soundness and profitability of the Group. Risk management involves the identifying, measuring, monitoring and managing of risks on a regular basis. The objective of risk management is to increase shareholders' value and achieve a return on equity that is commensurate with the risks assumed. To achieve this objective, the Group employs leading risk management practices and recruits skilled and experienced people.

As with other financial institutions, the Group faces a range of risks in its business and operations including (i) credit risk; (ii) market risk (comprising of interest rate risk, currency risk and equity price risk); (iii) liquidity risk, (iv) legal risk and (v) operational risk, as detailed below.

The Board of Directors of the Bank has overall responsibility for managing risks within the Bank. Whilst the Board approves and periodically reviews risk management policies and strategies based on the recommendations of the Board Risk Committee, the management establishes procedures to implement the policies and strategies. The Risk Management Committee (RMC), the Country Risk Committee (CRC) and Asset and Liability Management Committee (ALMC), comprising Executive and Senior Management, are high level management committees responsible for the overall management of the risk profile of the Group. RMC discusses important risk related issues, policies, procedures and reviews implementation of its decisions. ALMC reviews issues relating to the statement of financial position at a micro level and also reviews issues relating to Asset Liability mismatches and liquidity. The Country Risk Committee (CRC) reviews country risk, business strategies and macro economic conditions with reference to the countries identified for doing business. The Operational Risk Management Committee (ORMC) manages the overall operational risk for the Bank by instituting CBB guidelines and Basel standards and carrying out required oversight.

28 RISK MANAGEMENT (continued)

The Risk & Credit Management Division (RCMD) is responsible for oversight of risk management within the Bank. It is responsible for looking in to risk characteristics inherent in new and existing products, activities, countries, regions, industries and making necessary recommendations to the appropriate authorities. It is also responsible for introducing or amending risk policies, procedures and exposure limits to mitigate these risks with approval from Board Risk Committee and Board or the Risk Management Committee, as applicable. The RCMD also establishes systems and processes for monitoring market and operational risks, and is also responsible for introducing risk management tools. The RCMD processes credit applications and ensures that the provisions of credit risk policies are complied with. The RCMD generates regular reports on credit risk exposures, performs credit rating reviews and monitors credit limits. The Designated Credit Officer/Designated Investment Officer in RCMD is one of the signatories in the credit/investment approval chain and provides independent view on credit & investment proposals. The Chief Risk Officer is the head of RCMD and reports to the Board Risk Committee, thereby ensuring the independence of the risk management process. In addition to the above, RCMD, in collaboration with Financial Control & Planning Division, prepares the Risk Appetite & the ICAAP document for the Bank. The ICAAP document assesses the Pillar 2 risks at length and prescribes the required level of capital buffer for the Bank. RCMD is also responsible for enusing adherance to regulatory and statutory requirements related to risk management such as introducing use of IFRS 9 guidelines, ICAAP etc. in the Bank.

The internal audit department assess whether the policies and procedures are complied with and, if necessary, suggest ways of further improving internal guidelines and procedures.

The various risks to which the Group is exposed to and how the Group manages them is discussed in the following paragraphs.

29 CREDIT RISK AND CONCENTRATION OF CREDIT RISK

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and thereby cause the other party to incur a financial loss. Concentration of credit risk arises when a number of counterparties are engaged in similar business activities, or activities in the same geographical region, or have similar economic features, fail to meet contractual obligations, due to them being affected by changes in economic, political or other conditions.

Credit risk in derivative financial instruments arises from potential counterparty default on contractual obligations and it is limited to the positive fair value in favor of the Group.

The Group attempts to control credit risk by monitoring credit exposures continuously, limiting transactions with specific counterparties, assessing the creditworthiness of counterparties, diversifying lending activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses, and by obtaining security wherever necessary and appropriate. In addition to monitoring credit limits, the Group manages credit exposures by entering into netting agreements and collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposures.

The Group has well defined policies and procedures for identifying, measuring, monitoring and controlling credit risk in all of the Group's activities, at the level of individual credit and at portfolio level. Credit limits are approved after a thorough assessment of the creditworthiness of the borrower or counterparty, including the purpose and structure of the credit, and its source of repayment. Credit proposals are reviewed by the RCMD, which is independent of business units, before approval by the appropriate approving authority is obtained. The Bank has a tiered approval authority levels depending on the extent of risk, comprising individuals with proven credit & investment credentials, Management Credit Committee and Board Committees. All policies relating to credit are reviewed by the Board Risk Committee and approved by the Board of Directors. An Executive Committee, consisting of Board of Directors, reviews and approves larger credits. In addition, all larger credits in excess of the approval authority of the Executive Committee are approved by the Board of Directors.

The Group devises specific business and risk strategies relating to corporate, retail, investments and treasury areas, within the ambit of the Group's risk policies and procedures. Any additional risks associated with such strategies are discussed in the RMC meetings and necessary risk control measures are applied through amendments to policies, procedures and circulars. The Group also draws up a comprehensive Risk Management Strategy every year and monitors the progress of that strategy.

Day-to-day monitoring of individual borrower or counterparty exposure is the responsibility of the respective business unit. The Group's Credit Administration Unit, a part of the RCMD, ensures that credit facilities are released after appropriate approval and against proper documentation. It also monitors excesses over limits, past dues, expired credits and escalates exceptions if any, for corrective action.

Counterparty credit limits are established for all customers after careful assessment of their creditworthiness and approval (as per the levels of authority prescribed in the policy). These are also subject to large credit exposure limit criteria of the Central Bank of Bahrain and the local regulators in overseas locations. Standard procedures, outlined in the Group's Risk Procedures Manual, require that all credit proposals be subjected to a detailed screening by a Designated Credit Officer/ Designated Investment Officer who is part of a three signature approval process and functions independent of the business units.

The credit growth, quality and portfolio composition are monitored continuously to maximize the risk adjusted return and reduce the level of incidence of impairment and accretion of marginal credits. The Group monitors concentration risk by establishing limits for maximum exposure to individual borrower or counterparty, country, bank and industry. Such limits are also stipulated for certain products. These limits are approved after detailed analysis and are reviewed and monitored regularly.

30 MAXIMUM EXPOSURE TO CREDIT RISK WITHOUT TAKING INTO ACCOUNT ANY COLLATERAL AND OTHER CREDIT ENHANCEMENTS

The table below shows the maximum exposure to credit risk for the components of the statement of financial position and for derivatives. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

	2017 BD '000	2016 BD '000
Balances with central banks	**450,839**	293,515
Treasury bills	**427,130**	401,635
Deposits and amounts due from banks and other financial institutions	**223,824**	318,407
Loans and advances to customers	**1,740,651**	1,767,138
Investment securities	**683,090**	688,730
Interest receivable and other assets	**66,933**	56,105
	3,592,467	3,525,530
Contingent liabilities	**267,875**	266,805
Commitments	**117,670**	127,186
	385,545	393,991
	3,978,012	3,919,521

31 CONCENTRATION OF ASSETS, LIABILITIES AND OFF STATEMENT OF FINANCIAL POSITION ITEMS

The distribution of assets, liabilities and credit commitments and contingencies by geographic region and industry sector is as follows:

	2017			2016		
	Assets BD '000	Liabilities BD '000	Credit commitments and contingencies BD '000	Assets BD '000	Liabilities BD '000	Credit commitments and contingencies BD '000
Gulf Co-operation Council countries	**3,222,728**	**2,756,671**	**340,220**	3,088,221	2,682,640	333,308
North America	**37,547**	**6,776**	**11**	61,650	5,965	615
European Union countries	**217,202**	**351,458**	**3,428**	217,846	394,225	9,799
Asia	**224,268**	**133,420**	**41,550**	243,086	132,243	42,588
Others	**61,355**	**13,940**	**336**	91,754	13,269	7,681
Total	**3,763,100**	**3,262,265**	**385,545**	3,702,557	3,228,342	393,991
Trading and manufacturing	**619,928**	**226,838**	**180,861**	629,572	94,469	176,992
Banks and other financial institutions	**655,062**	**1,240,487**	**27,018**	774,348	1,246,851	33,953
Construction and real estate	**392,225**	**62,305**	**128,840**	408,702	62,205	120,289
Government and public sector	**1,368,621**	**498,373**	**3,485**	1,196,815	698,443	2,890
Individuals	**441,848**	**914,531**	**624**	388,086	833,728	322
Others	**285,416**	**319,731**	**44,717**	305,034	292,646	59,545
Total	**3,763,100**	**3,262,265**	**385,545**	3,702,557	3,228,342	393,991

32 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS

The credit quality of financial assets is managed by the Group using internal and external credit risk ratings.

The Group follows an internal rating mechanism for grading relationships under loans and advances.

The Group utilises a scale ranging from 1 to 10 for credit relationships, with 1 to 8 denoting performing grades, 9 and 10 non-performing, in line with Basel III guidelines. Grades 1 to 3 represents high grade, 4 to 6 represents standard grade and 7 to 8 represents sub-standard grade.

All credits are assigned a rating in accordance with the defined criteria.

The Group endeavors continuously to improve upon the internal credit risk rating methodologies and credit risk management policies and practices to reflect the true underlying credit risk of the portfolio and the credit culture in the Group.

All lending relationships are reviewed at least once in a year and more frequently in the case of non-performing assets.

i. Credit quality analysis

The following table sets out information about the credit quality of financial assets measured at amortised cost and FVOCI debt investments. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

Explanation of the terms: 12-month ECL, lifetime ECL and credit-impaired are included in Note 3.3 impairment of financial assets.

	2017			
	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total BD '000
Loans and advances to customers – Commercial loans and overdrafts at amortised cost				
High (Grade 1 to 3)	**174,550**	**751**	**–**	**175,301**
Standard (Grade 4 to 6)	**725,813**	**202,911**	**–**	**928,724**
Substandard (Grade 7 to 8)	**16,464**	**120,795**	**–**	**137,259**
Non-performing (Grade 9 to 10)	**–**	**–**	**96,353**	**96,353**
	916,827	**324,457**	**96,353**	**1,337,637**
Loss allowance	**(4,629)**	**(30,933)**	**(58,026)**	**(93,588)**
Net Carrying amount	**912,198**	**293,524**	**38,327**	**1,244,049**

	2016			
	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total BD '000
Loans and advances to customers – Commercial loans and overdrafts at amortised cost				
High (Grade 1 to 3)	338,048	–	–	338,048
Standard (Grade 4 to 6)	634,153	152,974	–	787,127
Substandard (Grade 7 to 8)	8,355	195,696	–	204,051
Non-performing (Grade 9 to 10)	–	–	99,984	99,984
	980,556	348,670	99,984	1,429,210
Loss allowance	(2,623)	(38,597)	(67,331)	(108,551)
Net Carrying amount	977,933	310,073	32,653	1,320,659

32 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS (continued)

i. Credit quality analysis (continued)

	2017			
	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total BD '000
Loans and advances to customers – Consumer at amortised cost				
High (Grade 1 to 3)	**478,888**	**–**	**–**	**478,888**
Standard (Grade 4 to 6)	**–**	**12,544**	**–**	**12,544**
Substandard (Grade 7 to 8)	**–**	**12,731**	**–**	**12,731**
Non-performing (Grade 9 to 10)	**–**	**–**	**11,178**	**11,178**
	478,888	**25,275**	**11,178**	**515,341**
Loss allowance	**(4,152)**	**(6,351)**	**(8,236)**	**(18,739)**
Net Carrying amount	**474,736**	**18,924**	**2,942**	**496,602**

	2016			
	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total BD '000
Loans and advances to customers – Consumer at amortised cost				
High (Grade 1 to 3)	432,854	–	–	432,854
Standard (Grade 4 to 6)	–	8,468	–	8,468
Substandard (Grade 7 to 8)	–	10,173	–	10,173
Non-performing (Grade 9 to 10)	–	–	13,335	13,335
	432,854	18,641	13,335	464,830
Loss allowance	(2,951)	(5,085)	(10,315)	(18,351)
Net Carrying amount	429,903	13,556	3,020	446,479

	2017			
	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total BD '000
Debt investment securities at FVOCI				
High (AAA to A-)	**169,790**	**–**	**–**	**169,790**
Standard (BBB+ to B-)*	**239,283**	**161,480**	**–**	**400,763**
Total	**409,073**	**161,480**	**–**	**570,553**
Loss Allowance	**(83)**	**(532)**	**–**	**(615)**
Net Carrying amount	**408,990**	**160,948**	**–**	**569,938**
Debt investment securities at amortised cost				
High (AAA to A-)	**64,251**	**–**	**–**	**64,251**
Standard (BBB+ to B-)	**449,049**	**23,720**	**–**	**472,769**
Total	**513,300**	**23,720**	**–**	**537,020**
Loss allowance	**(4)**	**–**	**–**	**(4)**
Net Carrying amount	**513,296**	**23,720**	**–**	**537,016**
Loan commitments & Financial guarantee				
High (Grades 1 to 3)	**112,579**	**–**	**–**	**112,579**
Standard (Grade 4 to 6)	**192,760**	**31,459**	**–**	**224,219**
Substandard (Grade 7 to 8)	**6,887**	**40,407**	**–**	**47,294**
Non-performing (Grade 9 to 10)	**–**	**6**	**1,447**	**1,453**
Total	**312,226**	**71,872**	**1,447**	**385,545**
Loss allowance	**(564)**	**(844)**	**–**	**(1,408)**
Net Carrying amount	**311,662**	**71,028**	**1,447**	**384,137**

	2016			
	Stage 1: 12-month ECL BD '000	Stage 2: Lifetime ECL not credit-impaired BD '000	Stage 3: Lifetime ECL credit-impaired BD '000	Total BD '000
Debt investment securities at FVOCI				
High (AAA to A-)	183,857	–	–	183,857
Standard (BBB+ to B-) *	291,586	94,419	–	386,005
Total	475,443	94,419	–	569,862
Loss Allowance	(159)	(445)	–	(604)
Net Carrying amount	475,284	93,974	–	569,258
Debt investment securities at amortised cost				
High (AAA to A-)	83,290	–	–	83,290
Standard (BBB+ to B-)	434,042	–	–	434,042
Total	517,332	–	–	517,332
Loss allowance	(5)	–	–	(5)
Net Carrying amount	517,327	–	–	517,327
Loan commitments & Financial guarantee				
High (Grades 1 to 3)	144,149	–	–	144,149
Standard (Grade 4 to 6)	77,099	144,651	–	221,750
Substandard (Grade 7 to 8)	828	27,168	–	27,996
Non-performing (Grade 9 to 10)	–	8	88	96
Total	222,076	171,827	88	393,991
Loss allowance	(268)	(596)	–	(864)
Net Carrying amount	221,808	171,231	88	393,127

* Standard grade of debt investments at FVOCI includes unrated investments amounting to BD 1,469 thousand (2016: BD 1,549 thousand).

The following table sets out the credit analysis for non-trading financial assets measured at FVTPL.

	2017 BD '000	2016 BD '000
Debt investment securities		
High (AAA to A-)	**3,266**	3,781

The Group holds collateral and other credit enhancements against certain of its credit exposures. The following table sets out the principal types of collateral held against different types of financial assets.

Type of credit exposure

	2017 BD '000	2016 BD '000
Derivative assets held for risk management	**11,383**	11,628
Loans and advances:		
Cash	**116,785**	60,952
Mortgage lending	**819,804**	1,096,412
Financial Instruments	**30,530**	55,466

ii. Collateral and other credit enhancements
The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained are as follows:
- For commercial lending, charges over real estate properties and bank guarantees;
- For retail lending, mortgages over residential properties;
- Cash collaterals such as bank deposits; and
- Marketable securities.

The Group also obtains guarantees from parent companies for loans to their subsidiaries.

The Group monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

It is the Group's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the Group does not occupy repossessed properties for business use.

Inputs, assumptions and techniques used for estimating impairment

Refer to note 3.3 Financial assets and financial liabilities – impairment.

Significant increase in credit risk
When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and expert credit assessment and including forward-looking information.

Credit risk grades
The Group allocates each exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower. Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates. Each exposure is allocated to a credit risk grade at initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade.

Generating the term structure of Probability of Default (PD)
Credit risk grades are a primary input into the determination of the term structure of PD for exposures. The Group collects performance and default information about its Credit risk exposures analysed by credit risk grading for Corporate and days-past-due for Retail portfolio. The Group employs statistical models to analyse the data collected and generate estimates of PD of exposures and how these are expected to change as a result of the passage of time. This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, across various geographies in which the Bank has taken exposures. For most exposures, the key macro-economic indicators include: GDP growth, Real interest rates, Unemployment, Domestic Credit growth, Oil prices, Central Government Revenue as percentage to GDP and Central Government Expenditure as percentage to GDP.

Determining whether credit risk has increased significantly
In determining whether credit risk has increased significantly since initial recognition, the Group uses its internal credit risk grading system, external risk ratings, delinquency status of accounts, expert credit judgement and, where possible, relevant historical experience.

The Group may also determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis. As a backstop, the Group considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due.

The Group monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:
- The criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- The criteria do not align with the point in time when an asset becomes 30 days past due; and
- There is no unwarranted volatility in loss allowance from transfers between 12-month PD (stage 1) and lifetime PD (stage 2).

Renegotiated financial assets
The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value. Where possible, the Group seeks to restructure loans rather than to take possession of collateral, if available. This may involve extending the payment arrangements and documenting the agreement of new loan conditions. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

The accounts which are restructured due to credit reasons in past 12 months will be classified under Stage 2. The 12 months period is sufficient to test the adequacy of the cash flows to test satisfactory performance under the revised terms of restructuring.

Definition of default
The Group considers a financial asset to be in default when:
- The borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held);
- The borrower is past due more than 90 days on any material credit obligation to the Group; and
- The borrower is rated 9 or 10.

In assessing whether a borrower is in default, the Group considers indicators that are:
- Quantitative – e.g. overdue status and non-payment on another obligation of the same issuer to the Group; and
- Based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

The definition of default largely aligns with that applied by the Group for regulatory capital purposes.

Incorporation of forward-looking information
The Group employs statistical models to incorporate macro-economic factors on historical default rates. In case none of the above macro – economic parameters are statistically significant or the results of forecasted PD's are too much deviated from the present forecast of the economic conditions, qualitative PD overlay shall be used by management after analyzing the portfolio as per the diagnostic tool.

Incorporating forward looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the Expected Credit Loss (ECL) applicable to the stage 1 and stage 2 exposures which are considered as performing (Stage 3 are the exposures under default category). The methodologies and assumptions involved, including any forecasts of future economic conditions, are reviewed periodically.

32 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS (continued)

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- Probability of default (PD);
- Loss given default (LGD); and
- Exposure at default (EAD).

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

PD estimates are estimates at a certain date, which are calculated based on statistical rating models. These statistical models are based on internally compiled data comprising both quantitative and qualitative factors. Market data is used to derive the PD for banks and sovereign counterparties. If a counterparty or exposure migrates between rating PDs are estimated considering the residual maturities of exposures and estimated prepayment rates.

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the forecasted collateral value and recovery costs of any collateral that is integral to the financial asset.

LGD estimation are estimation of :

1- Cure Rate: Defined as the ratio of accounts which have fallen to default and have managed to move backward to the performing accounts.

2- Recovery Rate: Defined as the ratio of liquidation value to market value of the underlying collateral at the time of default would also account for expected recovery rate from a general claim on the individual's assets for the unsecured portion of the exposure.

3- Discounting Rate: Defined as the opportunity cost of the recovery value not being realized on the day of default adjusted for time value.

EAD represents the expected exposure in the event of a default. The Group derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortisation. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount drawn, as well as potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts.

The contractual life have been considered as maturity for ECL computation for the assets with fixed maturity whereas, for revolving and overdraft loans a maturity of 3 years (stage 2) and 1 year (stage 1) shall be considered based upon the stage under which asset lies.

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics and counterparty type that include:

- Credit risk gradings;
- Product type; and
- Geographic location of the borrower.

The groupings are subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

For portfolios in respect of which the Group has limited historical data, external benchmark information is used to supplement the internally available data. The portfolios for which external benchmark information represents a significant input into measurement of ECL are as follows.

Banks and financial institutions
Sovereign
Investment securities (debt instruments)

33 CARRYING AMOUNT OF FINANCIAL ASSETS WHOSE TERMS HAVE BEEN RENEGOTIATED

The table below shows the carrying amount for financial assets by class, renegotiated during the year.

	2017 BD '000	2016 BD '000
Loans and advances to customers		
Commercial loans	**83,884**	32,486
Consumer loans	**5,855**	7,469
	89,739	39,955

34 MARKET RISK

Market risk is defined as the risk of potential loss that may arise from adverse changes in the value of a financial instrument or portfolio of financial instruments due to movements in interest rates, foreign exchange rates, equity, commodity prices and derivatives. This risk arises from asset – liability mismatches, changes that occur in the yield curve, foreign exchange rates and changes in volatilities/implied volatilities in the market value of derivatives.

The Group has clearly defined policies for conducting investment (including trading investments) and foreign exchange business which stipulates limits for these activities. Investments are made strictly in accordance with investment acceptance criteria. The Group does not undertake any commodity trading activities. For management of market risk arising from movement in interest rates, refer to note 35.

The Group uses an internal Value-at-Risk (VaR) model for measuring general market risk in the trading book of the Group and all foreign exchange positions. The internal model was approved by the Central Bank of Bahrain. VaR is calculated using a 99% confidence level for a 10 day holding period. This implies a 1% possibility of the loss exceeding the VaR amount calculated by the model. As at 31 December, VaR calculated based on the above parameters was as follows:

	2017 BD '000	2016 BD '000
Foreign exchange	**147**	172
Interest Rate	**2**	5
	149	177

The Bank's Risk Management Department conducts backtesting in accordance with the Market Risk Capital Adequacy Regulations issued by the Central Bank of Bahrain to ensure that the VaR model and assumptions used for computing VaR numbers are reliable. Backtesting of 1 day VaR as per actual profit and loss (comparing 1 day VaR with the average actual daily profit and loss) and also hypothetical back testing (comparing 1 day VaR with derived profit and loss of static positions) is carried out on a daily basis as stipulated in the Central Bank of Bahrain Rule book. The objective is to ensure that the assumptions used for computing VaR are reasonable and provide a VaR number that is a good indicator of possible losses in trading positions. During the year, the backtesting produced satisfactory results.

The Group also conducts stress testing to identify events or influences that could greatly impact material trading positions taken by the Group. As per the Central Bank of Bahrain requirements, validation of the internal model is conducted by the Internal Audit Department of the Bank as well as by an external consultant.

35 INTEREST RATE RISK MANAGEMENT

Interest rate risk is the exposure of the Group's financial condition to adverse movements of interest rates. The Group is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off statement of financial position instruments that mature or re-price in a given period. Excessive interest rate risk can pose a significant threat to the Group's earnings and capital base. Accordingly, an effective risk management process that maintains interest rate risk within prudent levels is essential to the safety and soundness of the Group.

It is the Group's policy to keep its assets and liabilities mismatches at stable and acceptable levels to maintain a steady net interest income. The Group monitors interest rate risk based on gap/duration limits. The Group also uses 'what if' scenarios for projecting net interest income and economic value of equity of the Group. The Group uses derivative instruments such as interest rate swaps, and foreign exchange agreements to manage interest rate risk. Whilst day to day management of interest rate risk is responsibility of the Global Treasurer, ALMC also reviews the interest rate risk reports periodically.

Based on the consolidated statement of financial position as at 31 December 2017 an increase of 200 basis points in interest rates, with all variables held constant, will result in an increase in the net interest income, for the next 12 months, by approximately BD 17,738 thousand (2016: increase by BD 19,088 thousand). However, further downward movement of interest rates by 200 basis points might not be practical assumption in the current environment, given the current low levels of interest rates, and hence capping the downward movement of interest rates at 0%, the negative impact on the net interest income as at 31 December 2017 estimated at BD 16,115 thousands (2016: BD 11,528 thousands). On the other hand, the scope for interest rates increase from its current levels is most probable which the Bank shall benefit.

	Rate Shock Forecasting (+200 bps)		Rate Shock Forecasting (-200 bps)	
	2017 BD '000	2016 BD '000	**2017 BD '000**	2016 BD '000
Bahraini Dinar	**11,557**	**11,331**	11,557	7,499
US Dollar	**5,468**	**6,250**	4,269	2,400
Kuwaiti Dinar	**1,471**	**(260)**	1,047	167
Others	**(758)**	**1,766**	(758)	1,462
Total	**17,738**	**19,088**	16,115	11,528

An increase of 200 basis points in interest rates, with all other variables held constant, will result in a negative impact on equity of approximately 7.2% amounting to BD 37,955 thousand (2016: 2.8%, BD 14,126 thousand). Similarly, a decrease of 200 basis points in interest rates, with all other variables held constant, will result in a positive impact on equity of approximately 7.2% amounting to BD 37,955 thousand (2016: 2.8%, BD 14,126 thousand).

36 CURRENCY RISK

The functional currency of the Group is the Bahraini Dinar.

The Group had the following significant non-strategic net exposures denominated in foreign currencies as of the consolidated statement of financial position date:

	2017 BD '000 equivalent long (short)	2016 BD '000 equivalent long (short)
US dollar	**63,540**	83,141
Euro	**147**	488
GCC currencies (excluding Kuwaiti dinar)	**2,886**	2,582
Kuwaiti dinar	**1,039**	504
Others	**285**	1,592

As the Bahraini dinar and other GCC currencies (except the Kuwaiti dinar) are pegged to the US dollar (US$), positions in US$ and other GCC currencies are not considered to represent a significant currency risk. For currency sensitivity impact refer to VaR (note 34).

The Board of Directors has established levels of currency risk by setting limits on currency position exposures. Positions are monitored on a daily basis to ensure that they are maintained within established limits. The Group uses forward foreign exchange contracts and currency swaps to hedge against specifically identified currency risks.

37 EQUITY PRICE RISK

Equity price risk is the risk that the fair values of equities or managed funds decrease as a result of changes in the corresponding value of equity indices or the value of individual equity stocks. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

The effect on equity (as a result of a change in the fair value of equity instruments held as fair value) due to a reasonably possible change in equity indices, with all other variables held constant, is as follows:

	Effect on equity		
	% change in Index	**Total 2017 BD '000**	Total 2016 BD '000
Bahrain Bourse	± 15%	**1,374**	1,863
Other GCC and other stock exchanges	± 15%	**3,912**	4,597
		5,286	6,460

38 LIQUIDITY RISK

Liquidity risk is the risk that the Group will be unable to meet its funding requirements. Liquidity risk can be caused by market disruptions or a credit downgrade which may cause certain sources of funding to dry up immediately. To guard against this risk, the Group has diversified funding sources, assets are managed with liquidity in mind and liquidity positions are monitored, maintaining a healthy balance of cash, cash equivalents, and readily marketable securities. In addition, the Group maintains various statutory deposits with central banks and has taken lines of credit from various banks and financial institutions.

The Bank has in place a liquidity risk policy, which describes the roles and responsibilities of ALMC and Treasury, and stipulates the broad guidelines with regard to minimum liquid assets to be maintained by the Bank, gap limits under each time bucket of the maturity ladder, cumulative outflow of cash limits for each time bucket and various liquidity ratios to be maintained which are approved by the ALMC based on the Annual Liquidity Strategy.

It is the Bank's policy to keep its assets in high-quality liquid assets such as inter-bank placements, treasury bills and government bonds, to ensure that funds are available to meet maturing liabilities, undrawn facilities and deposit withdrawals as they fall due for payment. A substantial proportion of the Bank's deposits is made up of retail current, savings and fixed deposit accounts which, though payable on demand or at short notice, have traditionally formed part of a stable deposit base and a source of core funding.

The day to day management of liquidity risk is the responsibility of the Global Treasurer, who monitors the sources and maturities of assets and liabilities closely and ensures that limits stipulated by the ALMC are complied with, and that funding is not concentrated from any one source.

The Bank also draws up contingency plans to deal with extraordinary conditions of liquidity risk after comprehensive scenario analysis.

The table below summarizes the maturity profile of the Group's financial liabilities (including interest) based on contractual undiscounted repayment obligations.

31 December 2017	On Demand BD '000	Within 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 to 12 months BD '000	1 to 5 years BD '000	5 to 10 years BD '000	10 to 20 years BD '000	More than 20 years BD '000	Total BD '000
Deposits and due to banks and other financial institutions	66,154	103,880	25,108	59	46	282	–	–	–	195,529
Borrowings under repurchase agreement	–	552	492	1,230	43,155	128,652	–	–	–	174,081
Term borrowings	–	–	2,947	48,637	2,668	158,820	–	–	–	213,072
Customers' current, savings and other deposits	1,249,748	354,293	297,100	277,695	214,300	272,698	6	–	–	2,665,840
Total undiscounted financial liabilities	1,315,902	458,725	325,647	327,621	260,169	560,452	6	–	–	3,248,522
Letter of Guarantees	230,620	–	–	–	–	–	–	–	–	230,620
Undrawn loan commitments	117,670	–	–	–	–	–	–	–	–	117,670
Derivative financial instruments										
Contractual amounts payable	–	(2,789)	(4,839)	(63,630)	(20,888)	(339,168)	(239,130)	(58,546)	(69,590)	(798,580)
Contractual amounts receivable	–	2,411	4,231	63,076	19,707	331,190	233,521	52,771	66,053	772,960
	–	(378)	(608)	(554)	(1,181)	(7,978)	(5,609)	(5,775)	(3,537)	(25,620)

31 December 2016	On Demand BD '000	Within 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 to 12 months BD '000	1 to 5 years BD '000	5 to 10 years BD '000	10 to 20 years BD '000	More than 20 years BD '000	Total BD '000
Deposits and due to banks and other financial institutions	–	187,522	72,471	16	92	–	–	–	–	260,101
Borrowings under repurchase agreement	–	650	–	–	22,784	182,524	–	–	–	205,958
Term borrowings	–	–	313	8,891	3,309	211,457	–	–	–	223,970
Customers' current, savings and other deposits	1,131,845	494,365	411,937	227,023	135,748	112,706	4,471	8,944	–	2,527,039
Total undiscounted financial liabilities	1,131,845	682,537	484,721	235,930	161,933	506,687	4,471	8,944	–	3,217,068
Letter of Guarantees	228,286	–	–	–	–	–	–	–	–	228,286
Undrawn loan commitments	127,187	–	–	–	–	–	–	–	–	127,187
Derivative financial instruments										
Contractual amounts payable	–	(2,705)	(8,047)	(18,717)	(26,404)	(374,200)	(276,953)	(42,226)	(76,881)	(826,133)
Contractual amounts receivable	–	3,005	8,491	17,367	23,007	350,297	263,969	31,873	69,094	767,103
	–	300	444	(1,350)	(3,397)	(23,903)	(12,984)	(10,353)	(7,787)	(59,030)

39 FAIR VALUES OF FINANCIAL INSTRUMENTS

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

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; and

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

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy at 31 December 2017 and 31 December 2016.

31 December 2017	Level 1 BD'000	Level 2 BD'000	Level 3 BD'000	Total BD'000
Financial assets				
Bonds	**563,502**	**–**	**666**	**564,168**
Equities	**35,242**	**6,737**	**22,720**	**64,699**
Managed funds	**–**	**1,196**	**–**	**1,196**
Derivatives held for trading	**–**	**147**	**–**	**147**
Derivatives held as fair value hedges	**–**	**7,467**	**–**	**7,467**
Derivatives held as cash flow hedges	**–**	**100**	**–**	**100**
	598,744	**15,647**	**23,386**	**637,777**
Financial liabilities				
Derivatives held for trading	**–**	**647**	**–**	**647**
Derivatives held as fair value hedges	**–**	**5,992**	**–**	**5,992**
	–	**6,639**	**–**	**6,639**

31 December 2016	Level 1 BD'000	Level 2 BD'000	Level 3 BD'000	Total BD'000
Financial assets				
Bonds	563,023	2,634	–	565,657
Equities	43,742	6,066	28,153	77,961
Managed funds	–	1,442	–	1,442
Derivatives held for trading	–	108	–	108
Derivatives held as fair value hedges	–	6,672	–	6,672
Derivatives held as cash flow hedges	–	158	–	158
	606,765	17,080	28,153	651,998
Financial liabilities				
Derivatives held for trading	–	137	–	137
Derivatives held as fair value hedges	–	9,638	–	9,638
	–	9,775	–	9,775

Transfers between level 1, level 2 and level 3

During the reporting year ended 31 December 2017, there were no transfers into and out of Level 3 fair value measurements.

The table below sets out the estimated carrying values and fair values of those on and off statement of financial position financial instruments carried at amortised cost where fair values are different from the carrying amounts shown in the consolidated financial statements:

2017	Carrying value BD '000	Fair value BD '000	Difference BD '000
Financial liabilities			
Term borrowings	**199,012**	**193,941**	**(5,071)**
Financial assets			
Investment securities	**118,923**	**117,233**	**(1,690)**

2016	Carrying value BD '000	Fair value BD '000	Difference BD '000
Financial liabilities			
Term borrowings	206,109	199,596	(6,513)
Financial assets			
Investment securities	123,073	120,937	(2,136)

The above financial liabilities and assets are level 1 fair value.

The fair value of financial assets and financial liabilities approximate their carrying values, other than those disclosed in the table above.

40 SHARE-BASED PAYMENTS

The expense recognised for employee services received during the year is shown in the following table:

	2017 BD '000	2016 BD '000
Expense arising from equity-settled share-based payment transactions	**1,242**	714
Shares vested during the year	**(543)**	(745)

During 2010, the Nomination and Remuneration Committee of the Bank modified the employees stock option plans for the previously granted stock options. The existing plan was discontinued with effect from 31 March 2010. The Bank moved to a new long-term incentive plan, which is referred to as the Employee Performance Share Plan (EPSP), which will award shares (rather than options) to executives. The details of the modifications to stock option plan and EPSP are described below:

Employee Performance Share Plan (EPSP)

Shares are granted to Senior Managers and above, with more than 12 months service at the date of grant and meeting certain performance criteria. The shares granted are subject to the satisfaction of conditions relating to the Bank's net profit over a three year period and the employee being in employment at the end of the 3 year period (vesting period).

The Bank utilises its existing treasury shares for the EPSP and may also choose to issue new shares to settle the EPSP in the future. The price of the shares granted was equal to the market price of the Bank's shares on the grant date. As at 31 December 2017, there has been a transfer of 4,636,928 shares (2016: 10,398,441 shares) from treasury stock to BBK Shares Incentives S.P.C which is in line with the Employee Performance Share Plan.

40 SHARE-BASED PAYMENTS (continued)

Employee Performance Share Plan (EPSP) (continued)

The following table illustrates the number and cost per share of the shares granted during the year under the new scheme.

	2017		2016	
	Number of shares	**Cost per share BD**	Number of shares	Cost per share BD
Opening balance of shares granted but not vested	**4,636,928**	**0.354**	5,914,981	0.424
Equity shares granted during the year	**2,281,932**	**0.394**	2,851,177	0.312
Equity shares transferred to trust	**1,769,816**	**0.394**	900,000	0.312
Shares transferred to active employees	**(1,256,260)**	**0.432**	(1,798,302)	0.425

The market price of BBK B.S.C. shares at 31 December 2017 was BD 0.414 (2016: BD 0.400).

41 CAPITAL ADEQUACY

The risk asset ratio calculated in accordance with the capital adequacy guidelines approved by the Central Bank of Bahrain, for the Group is as follows:

	2017 BD '000	2016 BD '000
Capital base:		
CET1 capital	**408,784**	383,518
Additional Tier 1 capital	**86,098**	86,098
Tier 2 capital	**29,578**	30,865
Total capital base (a)	**524,460**	500,481
Credit risk weighted exposure	**2,366,212**	2,469,207
Operational risk weighted exposure	**226,425**	211,854
Market risk weighted exposure:	**28,050**	27,025
Total risk weighted exposure (b)	**2,620,687**	2,708,086
Capital adequacy (a/b * 100)	**20.01%**	18.48%
Minimum requirement	**12.50%**	12.50%

Capital management

The primary objectives of the Group's capital management policies are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

Basel III and Capital management

The Bank has adopted the new Basel III Capital Adequacy Framework (Basel III) with effect from 1 January 2015 as per the guidelines issued by the Central Bank of Bahrain which is enhancing the Bank's risk management process, supervisory review, disclosure standards and capital management.

The Bank has adopted the Standardized Approach in case of Credit Risk, the Internal Model Approach for Market Risk and the Basic Indicator Approach for Operational Risk.

The Bank has established its Internal Capital Adequacy Assessment Process (ICAAP) to provide policy guidance in Capital Planning and Capital Management. The Bank also uses Risk Adjusted Return on Capital (RAROC) model in its decision making process.

42 LEGAL AND OPERATIONAL RISK

Legal risk

Legal risk is the risk relating to losses due to legal or regulatory action that invalidates or otherwise precludes performance by the end user or its counterparty under the terms of the contract or related netting agreements.

The Group has developed preventive controls and formalised procedures to identify legal risks so that potential losses arising from non-adherence to laws and regulations, negative publicity, etc. are significantly reduced. The Group also has well established legal procedures to scrutinise product offerings and manage risks arising out of its transactions.

As at 31 December 2017, there were legal cases pending against the Group aggregating BD 795 thousand (2016: BD 814 thousand). Based on the opinion of the Group's legal advisors, the management believes that no liability is likely to arise from these cases.

Operational risk

Operational risk is the exposure to loss resulting from inadequate or failed internal processes, people and systems, or from external events. The Group has clearly defined operations procedures for each of its products and services. It also has advanced computer systems that enable it to run operations with speed and accuracy.

The operational risk department operates independently from other units of the Bank and reports to the Chief Risk Officer. It conducts regular reviews of all business areas of the Bank and reports control deficiencies and exceptions to the Bank's policies and procedures. It also recommends measures to mitigate operational risk, which are implemented by management immediately.

The Bank also has a contingency plan to take care of any failure of its computer systems. Regular back-ups are made for all important datasets, and stored outside the Bank's premises. This ensures that in case of any system failure, the Bank will be able to continue its operations without losing critical data or business transactions. As part of its disaster recovery plan, the Bank has established a back-up site which would and operate during an emergency.

The Bank has a specific Business Continuity Plan ("BCP") unit. The main objective of the BCP is to ensure that in the event of full or partial disaster, the Bank should be able to continue providing essential services to customers, minimizing any adverse effects on the Bank's business, through business impact analysis, business restoration plans and procedures, for the identified critical functions.

The Bank is using an operational risk management solution for monitoring operational risk, conducting risk and control self assessments and capturing operational loss data in accordance with Basel III/Central Bank of Bahrain guidelines.

The Bank's subsidiaries have similar contingency plans for their operations.

43 DEPOSIT PROTECTION SCHEME

Deposits held with the Bahrain operations of the Bank are covered by the Deposit Protection Scheme (the Scheme) established by the Central Bank of Bahrain regulation concerning the establishment of the Deposit Protection Scheme and Deposit Protection Board.

44 STAFF SAVING SCHEME

The scheme is a contribution saving fund between the Bank and the employee of the Bank. It was introduced in January 1996 with the objective of providing the employees with a cash benefit upon resignation, retirement or death. Participation in the scheme is discretionary and the employee may contribute any amount. The Bank guarantees a corresponding contribution of an amount that is 3% higher provided that total Bank contribution is not in excess of 10% of the employees' salary. The employee becomes eligible for the full amount of the Bank contribution once the employee has completed 5 years of service, otherwise the entitlement is proportionately calculated. The scheme is managed by a committee, consisting of members from management and representatives nominated and selected by staff.

As at 31 December 2017 the total contribution fund including the earned income stands at BD 17,044 thousand (2016: BD 15,338 thousand). Out of the total fund amount, payment of the principal amount equal to BD 14,927 thousand (2016: BD 13,496 thousand) consisting of the respective staff and Bank's contribution is guaranteed by the Bank to employees participating in the scheme within the applicable law. Out of the principal amount, BD 6,069 thousand (2016: BD 4,912 thousand) is invested in Bahraini Sovereign and GCC Bonds.

45 CLASSIFICATION OF ASSETS AND LIABILITIES

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments.

31 December 2017	Designated as at FVTPL BD '000	FVOCI – debt instruments BD '000	FVOCI – equity instruments BD '000	Amortised cost/others BD '000	Total BD '000
Cash and balances with central banks	–	–	–	469,436	469,436
Treasury Bills	–	9,037	–	418,093	427,130
Deposits and amounts due from banks and other financial institutions	–	–	–	223,824	223,824
Loans and advances to customers	–	–	–	1,740,651	1,740,651
Investment securities	4,462	560,901	64,699	118,923	748,985
Investments in associated companies and joint ventures	–	–	–	46,958	46,958
Interest receivable and other assets	–	–	–	79,680	79,680
Premises and equipment	–	–	–	26,436	26,436
Total assets	4,462	569,938	64,699	3,124,001	3,763,100
Deposits and amounts due to banks and other financial institutions	–	–	–	193,472	193,472
Borrowings under repurchase agreement	–	–	–	161,314	161,314
Term borrowings	–	–	–	199,012	199,012
Customers' current, savings and other deposits	–	–	–	2,623,577	2,623,577
Interest payable and other liabilities	–	–	–	84,890	84,890
Total liabilities	–	–	–	3,262,265	3,262,265

31 December 2016	Designated as at FVTPL BD '000	FVOCI – debt instruments BD '000	FVOCI – equity instruments BD '000	Amortised cost/others BD '000	Total BD '000
Cash and balances with central banks	–	–	–	314,368	314,368
Treasury Bills	–	7,381	–	394,254	401,635
Deposits and amounts due from banks and other financial institutions	–	–	–	318,407	318,407
Loans and advances to customers	–	–	–	1,767,138	1,767,138
Investment securities	10,486	561,875	72,700	123,073	768,134
Investments in associated companies and joint ventures	–	–	–	43,923	43,923
Interest receivable and other assets	–	–	–	64,769	64,769
Premises and equipment	–	–	–	24,183	24,183
Total assets	10,486	569,256	72,700	3,050,115	3,702,557
Deposits and amounts due to banks and other financial institutions	–	–	–	259,911	259,911
Borrowings under repurchase agreement	–	–	–	184,016	184,016
Term borrowings	–	–	–	206,109	206,109
Customers' current, savings and other deposits	–	–	–	2,493,715	2,493,715
Interest payable and other liabilities	–	–	–	84,591	84,591
Total liabilities	–	–	–	3,228,342	3,228,342

1 EXECUTIVE SUMMARY

This report has been prepared in accordance with Pillar III disclosure requirements prescribed by the Central Bank of Bahrain, herein referred to as "CBB". The report has been designed to provide BBK Group's stakeholders with detailed information on the Bank's approach in managing capital and risk, having due regard to the operating environment.

The Bank applies the Basel framework in the measurement of its capital adequacy, and in its capital management strategy and risk management framework. CBB's Basel III capital rules and guidelines became effective on 1st January 2015 as the common framework for the implementation of the Basel Committee on Banking Supervision's (Basel Committee) Basel III capital adequacy framework for banks incorporated in the Kingdom of Bahrain.

The disclosures in this report are in addition to the disclosures set out in the consolidated financial statements for the year ended 31st December 2017 presented in accordance with the International Financial Reporting Standards (IFRS). Disclosures with respect to Corporate Governance and Remuneration are provided in relevant sections of the Annual Report.

2 INTRODUCTION TO THE BASEL III FRAMEWORK

The CBB's Basel III capital framework is based on three pillars consistent with the Basel III framework developed by the Basel Committee, as follows:-

- Pillar I: calculation of the Risk Weighted Assets (RWAs) and capital requirement.
- Pillar II: the supervisory review process, including the Internal Capital Adequacy Assessment Process (ICAAP).
- Pillar III: rules for the disclosure of risk management and capital adequacy information.

Amongst the three pillars, it is Pillar I that has been affected most and largely amended with the introduction of Basel III. Additional disclosure requirements have also been introduced under Pillar III.

Pillar I

Pillar I prescribes the basis for the calculation of the regulatory capital adequacy ratio. Pillar I sets out the definitions and calculations of the RWAs, and the derivation of the regulatory total capital. Capital adequacy ratios are calculated by dividing regulatory capital by the total RWAs.

As part of Basel III implementation, while the calculation of RWAs remained almost the same as under Basel II, the definition of regulatory capital witnessed significant changes as Basel III focuses on increasing both the quantity and quality of banks' capital. To this end, Tier 1 capital "T1" must be the main component of capital, and the predominant form of T1 capital must be common shares and retained earnings. Deductions from capital and prudential filters have been harmonized and generally applied at the level of common equity. The remainder of T1 capital base must be comprised of instruments that are subordinated, have fully discretionary noncumulative dividends or coupons and have neither a maturity date nor an incentive to redeem. Certain instruments that previously qualified as regulatory capital such as innovative hybrid capital instruments are no longer accepted and the existing ones will be phased out. In addition, Tier 2 capital "T2" instruments have been harmonized with more restrictions and a limit on their contribution to total regulatory capital, and the so-called Tier 3 capital instruments, which were only available to cover market risks, were eliminated.

Furthermore, Basel III introduced a number of capital buffers to promote the conservation of capital (capital conservation buffer or "CCB") and the build-up of adequate buffers above the minimum required capital during times of good economic conditions that can be drawn down in periods of stress (countercyclical capital buffer).

CBB minimum required total capital adequacy ratio (including CCB) increased from 12 percent to 12.5 percent, compared to 10.5 percent recommended by the Basel Committee. Moreover, there are newly introduced limits and minima by the CBB under Basel III, such as minimum Common Equity Tier 1 Capital Ratio "CET1" of 9 percent (including CCB) and minimum T1 Capital Ratio of 10.5 percent (including CCB). In the event that the total capital adequacy ratio falls below 12.5 percent, additional prudential reporting requirements apply, and a formal action plan setting out the measures to be taken to restore the ratio above the minimum required level is to be formulated and submitted to the CBB. Consequently, the CBB requires BBK to maintain an effective minimum total capital adequacy ratio above 12.5 percent.

The table below summarizes the approaches available for calculating RWAs for each risk type in accordance with the CBB's Basel III capital adequacy framework:

Credit Risk	Market Risk	Operational Risk
Standardised Approach	Standardised Approach	Basic Indicator Approach
	Internal Models Approach	Standardised Approach

The approach applied by BBK for each risk type is as follows:-

i) Credit Risk

For regulatory reporting purposes, BBK is using the Standardised Approach for credit risk. Credit risk constitutes nearly 90 percent of the overall risk for the Bank. The bank has a robust credit risk management architecture which is explained in greater detail in Note 28 and 29 of the Annual Report. The credit RWAs are determined by multiplying the credit exposure by a risk weight factor dependent on the type of counterparty and the counterparty's external rating, where available.

ii) Market Risk

For the regulatory market risk capital requirement, BBK is using the Internal Model Approach based on Value-at-Risk (VaR) model. The use of the Internal Model Approach for the calculation of regulatory market risk capital has been approved by the CBB and the model is subject to periodic independent internal and external validation.

iii) Operational Risk

All banks incorporated in Bahrain are required to apply the Basic Indicator Approach for operational risk unless approval is granted by the CBB to use the Standardised Approach. The CBB's capital framework does not currently permit the use of the Advanced Measurement Approach (AMA) for operational risk. For regulatory reporting purposes, BBK is currently using the Basic Indicator Approach whereby the operational risk weighted exposures and regulatory capital requirement are calculated by applying an alpha co-efficient of 15 percent to the average gross income for the preceding three financial years.

Pillar II
Pillar II defines the process of supervisory review of an institution's risk management framework and, ultimately, its capital adequacy.

Under the CBB's Pillar II guidelines, all banks incorporated in Bahrain are required to maintain total capital adequacy ratio above 12.5 percent.

Pillar II comprises two processes:

- an Internal Capital Adequacy Assessment Process (ICAAP), and
- a supervisory review and evaluation process.

The ICAAP incorporates a review and evaluation of risk management and capital relative to the risks to which the bank is exposed. BBK has developed an ICAAP document and it addresses all components of BBK's risk management, from the daily management of more material risks to the strategic capital management of the Group. The projected growth in risk assets, operating profit, shareholders' funds and the corresponding capital requirement are estimated by the bank as part of the 3 years strategy approved by the Board. In addition, the bank also forecasts the Capital Base whenever there is likely reduction in the capital components, and necessary actions are taken in order to ensure regulatory compliance. The bank has also a Dividend Policy in place as part of capital management strategy.

The Bank uses the RAROC model in its credit decisions in order to assess risk-reward matrix for each credit exposure. The Bank has adopted a Risk Appetite Framework which is reviewed periodically. The Bank also adopts a Risk Management Strategy annually covering all types of relevant risks.

The supervisory review and evaluation process represents the CBB's review of the Group's capital management and an assessment of internal controls and corporate governance. The supervisory review and evaluation process is designed to ensure that institutions identify their material risks, allocate adequate capital, and employ sufficient management processes to support such risks. The supervisory review and evaluation process also encourages institutions to develop and apply enhanced risk management techniques for the measurement and monitoring of risks in addition to the credit, market and operational risks addressed in the core Pillar I framework. Other risk types which are not covered by the minimum capital requirements in Pillar I include liquidity risk, interest rate risk in the banking book, strategic risk, concentration risk, reputational risk, and residual risk. These are covered either by capital, or risk management and mitigation processes under Pillar II.

BBK conducts stress testing of its portfolio as part of the ICAAP process.

Pillar III
Pillar III deals with the Market Discipline guidelines of the regulator to ensure adequate disclosure of risk management practices, corporate governance standards and capital adequacy information. The banks publishes disclosures periodically and in the Annual Report.

The disclosures comprise detailed qualitative and quantitative information. The purpose of the Pillar III disclosure requirements is to complement the first two pillars and the associated supervisory review process. The disclosures are designed to enable stakeholders and market participants to assess an institution's risk appetite and risk exposures and to encourage all banks, via market pressures, to move toward more advanced forms of risk management.

Under the current regulations, partial disclosure consisting mainly of quantitative analysis is required during half year reporting, whereas full disclosure is required to coincide with the financial year end reporting.

Regulatory Reforms
The Bank is categorized as a Domestic Systemically Important Bank (DSIB). Currently, the CBB has not prescribed any Countercyclical Buffer or additional capital requirements for DSIBs.

The framework on Leverage Ratio will be part of the Pillar 1 after its introduction by the CBB.

The Bank is evaluating Expected Credit Loss as per the guidelines in IFRS 9.

3 GROUP STRUCTURE
The Group's financial statements are prepared and published on a full consolidation basis, with all subsidiaries being consolidated in accordance with IFRS. For capital adequacy purposes, all financial subsidiaries are included within the Group structure. However, the CBB's capital adequacy methodology accommodates both normal and aggregation forms of consolidation.

The principal Subsidiaries, Associates and Joint Ventures and basis of consolidation for capital adequacy purposes are as follows:-

	Domicile	Ownership	Consolidation basis
Subsidiaries			
CrediMax B.S.C. (c)	Kingdom of Bahrain	100%	Full Consolidation
Invita B.S.C. (c)	Kingdom of Bahrain	100%	Risk Weighted
Invita – Kuwait*	State of Kuwait	60%	Risk Weighted
Global Payment Services W.L.L. (GPS)**	Kingdom of Bahrain	55%	Full Consolidation
Associates			
Bahrain Liquidity Fund	Kingdom of Bahrain	24%	Risk Weighted
Bahrain Commercial Facilities Company B.S.C.	Kingdom of Bahrain	23%	Risk Weighted
The Benefit Company B.S.C (c)	Kingdom of Bahrain	22%	Risk Weighted
Joint Venture			
Sakana Holistic Housing Solutions B.S.C. (c)	Kingdom of Bahrain	50%	Risk Weighted
Aegila Capital Management Limited	United Kingdom	50%	Risk Weighted
BBK Geojit Securities KSC	State of Kuwait	40%	Risk Weighted

* Shareholding through Invita Subsidiary
** Shareholding through CrediMax Subsidiary

There are no restrictions on the transfer of funds or regulatory capital within the Group.

4 STATEMENT OF FINANCIAL POSITION UNDER THE REGULATORY SCOPE OF CONSOLIDATION

The table below shows the link between the statement of financial position in the published financial statements (accounting statement of financial position) and the regulatory statement of financial position.

	Statement of financial position as in published financial statements BD '000	Statement of financial position as per regulatory reporting BD '000	Reference
Assets			
Cash and balances with central banks	**469,436**	**469,436**	
Treasury bills	**427,130**	**427,130**	
Deposits and amounts due from banks and other financial institutions	**223,824**	**223,824**	
Loans and advances to customers	**1,740,651**	**1,740,651**	
Of which Expected Credit Loss (1.25% of Credit risk weighted assets)		(29,578)	a
Of which net loans and advances (gross of Expected Credit Loss)	1,740,651	1,770,229	
Investment securities	**748,985**	**748,985**	
Of which related to equity investments in financial entities		24,916	b
Of which investments in financial entities under CET1		22,538	c
Of which investments in financial entities under Tier 2		2,378	d
Of which related to other investments		699,153	
Investments in associated companies and joint ventures	**46,958**	**49,786**	
Of which Investment in own shares	475	475	e
Of which equity investments in financial entities	32,681	32,681	f
Of which other investments	13,802	16,630	
Interest receivable and other assets	**79,680**	**77,801**	
Of which deferred tax assets due to temporary differences	1,631	1,631	g
Of which Interest receivable and other assets	78,049	76,170	
Premises and equipment	**26,436**	**26,283**	
Total assets	**3,763,100**	**3,763,896**	
Liabilities and Equities			
Liabilities			
Deposits and amounts due to banks and other financial institutions	**193,472**	**193,472**	
Borrowings under repurchase agreement	**161,314**	**161,314**	
Term borrowings	**199,012**	**199,012**	
Customers' current, savings and other deposits	**2,623,577**	**2,625,300**	
Interest payable and other liabilities	**84,890**	**84,343**	
Total liabilities	**3,262,265**	**3,263,441**	
Equity			
Share capital	**108,165**	**108,165**	h
Treasury stock	**(998)**	**(998)**	i
Perpetual tier 1 convertible capital securities	**86,098**	**86,098**	j
Share premium	**41,016**	**41,016**	k
Statutory reserve	**54,082**	**54,082**	l
General reserve	**54,082**	**54,082**	m
Cumulative changes in fair values	**(8,349)**	**(8,349)**	
Of which cumulative changes in fair values on bonds and equities	(8,573)	(8,573)	n
Of which Fair value changes in cash flow hedges	224	224	o
Foreign currency translation adjustments	**(9,271)**	**(9,271)**	
Of which related to unconsolidated subsidiary		(71)	p
Of which related to Parent		(9,200)	q
Retained earnings	**134,632**	**134,632**	
Of which employee stock options	3,036	3,036	
Of which Retained earnings	131,596	131,596	r
Appropriations	**39,161**	**39,161**	s
ATTRIBUTABLE TO THE OWNERS OF THE BANK	498,618	498,618	
Non-controlling interest	2,217	1,837	
Total equity	**500,835**	**500,455**	
Total Liabilities and equities	**3,763,100**	**3,763,896**	

Legal entities included within the accounting scope of consolidation but excluded from the regulatory scope of consolidation:

Name	Principle activities	Total Assets	Total Equities
Invita B.S.C. (c)	Business process outsourcing services	3,756	3,209

5 CAPITAL COMPONENTS – CONSOLIDATED

Under the CBB's Basel III capital framework, total regulatory capital consists of Tier 1 capital "T1" and Tier 2 capital "T2". T1 capital is further divided into Common Equity Tier 1 capital "CET1" and Additional Tier 1 capital "AT1". CET1 capital consists of : (a) Issued and fully paid common shares that meet the criteria for classification as common shares for regulatory purposes, (b) Disclosed reserves including: i) General reserves; ii) Legal / statutory reserves; iii) Share premium; iv) Fair value reserves arising from fair valuing financial instruments; and v) Retained earnings or losses (including net profit/ loss for the reporting period, whether reviewed or audited), (c) Common shares issued by consolidated subsidiaries and held by third parties (i.e. minority interest) that meet the criteria for inclusion in CET1, and (d) Regulatory adjustments applied in the calculation of CET1. AT1 capital consists of: (a) Instruments issued by the bank that meet the criteria for inclusion in AT1, (b) Share premium resulting from the issue of instruments included in AT1, (c) Instruments issued by consolidated subsidiaries and held by third parties that meet the criteria for inclusion in AT1 and are not included in CET1, and (d) Regulatory adjustments applied in the calculation of AT1. T2 capital consists of: (a) Instruments issued by the bank that meet the criteria for inclusion in T2, (b) Share premium resulting from the issue of instruments included in T2, (c) Instruments issued by consolidated subsidiaries of the bank and held by third parties that meet the criteria for inclusion in T2 capital and are not included in T1, (d) General loan loss provisions (Expected Credit Loss), (e) Asset revaluation reserves which arise from the revaluation of fixed assets and investment properties from time to time in line with the change in market values, and (f) Regulatory adjustments applied in the calculation of T2. At present, the T2 capital of BBK consists solely of general loan loss provision (Expected Credit Loss).

The CBB applies various limits and minima to the components of the regulatory capital, as shown in the below table. There is also a restriction on the amount of general loan loss provision (also called collective impairment provision\ Expected Credit Loss) that may be included as part of T2 capital, which should be a maximum of 1.25 percent of the credit risk weighted assets.

	Optional	Minimum Ratio
Components of Consolidated CAR		
Core Equity Tier 1 (CET 1)		6.50%
Additional Tier 1 (AT1)	1.50%	
Tier 1 (T1)		8.00%
Tier 2 (T2)	2.00%	
Total Capital		10.00%
Capital Conservation Buffer (CCB)		2.50%
CAR including CCB		
CET 1 plus CCB		9.00%
Tier 1 plus CCB		10.50%
Total Capital plus CCB		12.50%

	Optional	Minimum Ratio
Components of Solo CAR		
Core Equity Tier 1 (CET 1)		4.50%
Additional Tier 1 (AT1)	1.50%	
Tier 1 (T1)		6.00%
Tier 2 (T2)	2.00%	
Total Capital		8.00%
Capital Conservation Buffer (CCB)		0.00%

In accordance with the CBB's Basel III capital adequacy framework, certain exposures are required to be deducted from regulatory capital rather than included in RWAs. The CBB's Basel III capital adequacy framework requires that most of the deductions be made from the CET1.

There are no impediments on the transfer of funds or regulatory capital within the Group other than restrictions over transfers to ensure minimum regulatory capital requirements are met for subsidiary companies.

REGULATORY CAPITAL COMPONENTS

The table below provides a detailed breakdown of the bank's regulatory capital components, including all regulatory adjustments. The table also provides reference to the comparison displayed in the previous table between accounting and regulatory statement of financial positions.

	Component of regulatory capital BD '000	Amounts subject to pre-2015 treatment BD '000	Source based on reference letters of the statement of financial positions under the regulatory scope of consolidation
Common Equity Tier 1: Instruments and reserves			
Directly issued qualifying common share capital plus related stock surplus	148,183		h+i+k
Retained earnings	170,686		p+r+s
Accumulated other comprehensive income and losses (and other reserves)	90,615		l+m+n+o+q
Common Equity Tier 1 capital before regulatory adjustments	**409,484**	**–**	
Common Equity Tier 1 capital: regulatory adjustments			
Cash flow hedge reserve	224		o
Investments in own shares	475		e
Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	–	22,538	c
Total regulatory adjustments to Common equity Tier 1	**699**	**22,538**	
Common Equity Tier 1 capital (CET1)	**408,785**		

5 CAPITAL COMPONENTS – CONSOLIDATED (continued)

	Component of regulatory capital BD '000	Amounts subject to pre-2015 treatment BD '000	Source based on reference letters of the statement of financial positions under the regulatory scope of consolidation
Additional Tier 1 capital: regulatory adjustments			
Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	86,098		j
of which: classified as equity under applicable accounting standards	86,098		
Additional Tier 1 capital before regulatory adjustments	**86,098**	**–**	
Additional Tier 1 capital: regulatory adjustments			
Total regulatory adjustments to Additional Tier 1 capital	–	–	
Additional Tier 1 capital (AT1)	**86,098**	**–**	
Tier 1 capital (T1 = CET1 + AT1)	**494,883**		
Tier 2 capital: regulatory adjustments			
Provisions	29,578		a
Tier 2 capital before regulatory adjustments	**29,578**		
Tier 2 capital: regulatory adjustments			
Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)	–	2,378	d
Total regulatory adjustments to Tier 2 capital	–	2,378	
Tier 2 capital (T2)	**29,578**		
Total capital (TC = T1 + T2)	**524,462**		
Total risk weighted assets	**2,620,687**		
Capital ratios and buffers			
Common Equity Tier 1 (as a percentage of risk weighted assets)	15.60%		
Tier 1 (as a percentage of risk weighted assets)	18.88%		
Total capital (as a percentage of risk weighted assets)	20.01%		
Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB buffer requirement, expressed as a percentage of risk weighted assets)	9.00%		
of which: capital conservation buffer requirement	2.50%		
of which: bank specific countercyclical buffer requirement	N/A		
of which: G-SIB buffer requirement	N/A		
Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)	15.60%		
National minima (where different from Basel III)			
CBB Common Equity Tier 1 minimum ratio (Excluding Capital Conservation Buffer)	6.50%		
CBB Tier 1 minimum ratio (Excluding Capital Conservation Buffer)	8.00%		
CBB total capital minimum ratio (Excluding Capital Conservation Buffer)	10.00%		
Amounts below the thresholds for deduction (before risk weighting)			
Non-significant investments in the capital of other financials	24,916		b
Significant investments in the common stock of financials	32,681		f
Deferred tax assets arising from temporary differences (net of related tax liability)	1,631		g
Applicable caps on the inclusion of provisions in Tier 2			
Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardised approach (prior to application of cap)	48,169		
Cap on inclusion of provisions in Tier 2 under standardised approach	29,578		a

6 CAPITAL ADEQUACY

The Group's policy is to maintain a strong capital base so as to preserve investor, creditor and market confidence and to sustain the future development of the business. The impact of the level of capital on shareholders' return is also recognized, as well as the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. The Group manages its capital structure and makes adjustments to the structure taking account of changes in economic conditions and strategic business plans. The capital structure may be adjusted through the dividend payout and other discretionary payments and the issue of new shares and other capital instruments.

As per its ICAAP, BBK aims to maintain a minimum total capital adequacy ratio in excess of the capital assessed as per its ICAAP document of 13.90 percent. The CBB's current minimum total capital adequacy ratio (including CCB) for banks incorporated in Bahrain is set at 12.5 percent. The total capital adequacy ratio of the Group as at 31 December 2017 was 20.01 percent.

Strategies and methods for maintaining a strong capital adequacy ratio

BBK prepares multi-year strategic projections on a rolling annual basis which include an evaluation of short term capital requirements and a forecast of longer-term capital resources.

Capital ratios – consolidated and subsidiaries above 5% of group capital

	Total capital ratio	Tier 1 capital ratio
BBK – GROUP	20.01%	18.88%
CrediMax	63.59%	63.59%

7 CREDIT RISK – PILLAR III DISCLOSURES

This section describes BBK's exposure to credit risk, and provides detailed disclosures on credit risk in accordance with the CBB's Basel III framework, in relation to Pillar III disclosure requirements.

Definition of exposure classes

BBK has a diversified on and off statement of financial position credit portfolio, the exposures of which are divided into the counterparty exposure classes defined by the CBB's Basel III capital adequacy framework for the standardised approach for credit risk. A high-level description of the counterparty exposure classes, referred to as standard portfolios in the CBB's Basel III capital adequacy framework, and the generic treatments, i.e. the risk weights to be used to derive the RWAs, are as follows:-

Sovereigns portfolio

The sovereigns portfolio comprises exposures to governments and their respective central banks. The risk weights are zero percent for exposures in the relevant domestic currency, or in any currency for exposures to GCC sovereigns. Foreign currency claims on other sovereigns are risk weighted based on their external credit ratings.

Certain multilateral development banks as determined by the CBB may be included in the sovereigns portfolio and treated as exposures with a zero percent risk weighting.

Public Sector Entities (PSE) portfolio

Claims on Bahraini PSEs, and claims on PSEs on domestic currency – which are assigned a zero percent risk weight by their respective country regulator, can be assigned a zero percent risk weight. All other PSEs are risk weighted according to their external ratings.

Banks portfolio

Claims on banks are risk weighted based on their external credit ratings. A preferential risk weight treatment is available for qualifying short term exposures. Short term exposures are defined as exposures with an original tenor of three months or less. The Bank's portfolio also includes claims on certain investment firms, which are risk weighted based on their external credit ratings, though without any option for preferential treatment for short term exposures.

Corporates portfolio

Claims on corporates are risk weighted based on their external credit ratings. A 100 percent risk weight is assigned to exposures to unrated corporates. A preferential risk weight treatment is available for certain corporates owned by the Government of Bahrain, as determined by the CBB, which are assigned a zero percent risk weight.

Regulatory retail portfolio

Claims on retail portfolio are risk weighted at 75 percent, except for past due portfolio.

Mortgage portfolio

Claims which are fully secured by first mortgages on residential property that is or will be occupied by the borrower, or that is leased, must carry a risk weighting of 75 percent. Claims secured by mortgages on commercial real estate are subject to a minimum of 100 percent risk weight. If the borrower is rated below BB-, the risk-weight corresponding to the rating of the borrower must be applied.

Equities portfolio

The equities portfolio comprises equity investments in the banking book. A 100 percent risk weight is assigned to listed equities while unlisted equities are weighted at 150 percent, unless subject to the following treatments. The amount of any significant investments in commercial entities (A "significant investment" in a commercial entity is defined as any investment in the capital instruments of a commercial entity by the bank which is equivalent to or more than 10 percent of the issued common share capital of the issuing commercial entity) above 15 percent (individually) and 60 percent (collectively) of the bank's capital (the "Total Capital materiality thresholds") must be risk weighted at 800 percent. Moreover, significant investments in the common shares of unconsolidated financial entities must be risk weighted at 250 percent.

In addition to the standard portfolios, other exposures are assigned to the following exposure classes:

Investments in funds portfolio

The risk weight for claims on corporates will be used to determine the risk weight for investments in rated funds. Unrated funds will be assigned a risk weight of 100 percent if listed, and 150 percent if not listed.

7 CREDIT RISK – PILLAR III DISCLOSURES (continued)

Past due exposures

This includes claims, for which the repayment is overdue for more than ninety days. The risk weighting applied for such loans is either 100 percent or 150 percent, depending on the level of provisions maintained against the loan.

Holding of real estate

All holding of real estate by banks (owned directly or by the way of investments in real estate companies, subsidiaries or associated companies or other arrangements such as trusts, funds or REITS) must be risk weighted at 200 percent. Premises occupied by the bank are weighted at 100 percent.

Other assets and holdings of securitisation tranches

Other assets are risk weighted at 100 percent, whereas securitization exposures are risk weighted at 20 percent to 1,250 percent, depending on the external rating.

All BBK's holding of securitizations is part of the bank's investment portfolio.

Large Exposures

The excess amount of any exposure above 15 percent of the bank's regulatory capital to any counterparty or a group of closely related counterparties must be risk weighted at 800 percent, unless it is an exempted exposure in accordance with the requirements of the CBB Rulebook.

External rating agencies

BBK uses ratings issued by Moody's and Fitch to derive the risk weightings under the CBB's Basel III capital adequacy framework. Where ratings vary between rating agencies, the highest rating from the lowest two ratings is used to represent the rating for regulatory capital adequacy purposes.

Credit risk presentation under Basel III

The credit risk exposures presented in most of this report differ from the credit risk exposures reported in the consolidated financial statements. Differences arise due to the application of different methodologies, as illustrated below:-

- Under the CBB's Basel III framework, off statement of financial position exposures are converted into credit exposure equivalents by applying a credit conversion factor (CCF). The off statement of financial position exposure is multiplied by the relevant CCF applicable to the off statement of financial exposure position category. Subsequently, the exposure is treated in accordance with the standard portfolios as referred to above in this report, in the same manner as on statement of financial position exposures.
- In case of Over-the-Counter (OTC) derivative contracts, in addition to the default risk capital requirements for counterparty credit risk, the bank must add a capital charge to cover the risk of mark-to-market losses on the expected counterparty risk (such losses being known as credit value adjustments or CVA).
- Credit risk exposure reporting under Pillar III is frequently reported by standard portfolios based on the type of counterparty. The financial statement presentation is based on asset class rather than the relevant counterparty. For example, a loan to a bank would be classified in the Bank's standard portfolio under the capital adequacy framework although is classified in loans and advances in the consolidated financial statements.
- Certain eligible collateral is applied to reduce exposure under the Basel III capital adequacy framework, whereas no such collateral netting is applicable in the consolidated financial statements.
- Based on the CBB's Basel III guidelines, certain exposures are either included in, or deducted from, regulatory capital rather than treated as an asset as in the consolidated financial statements.

8 CAPITAL REQUIREMENT FOR RISK WEIGHTED EXPOSURE

	Gross credit exposures (before risk mitigation) BD '000	Eligible financial collateral BD '000	Credit risk after risk mitigation BD '000	Risk weighted asset BD '000	Regulatory capital required 12.5% BD '000
Sovereign	1,213,110	–	1,213,110	19,615	2,452
Public Sector Entities	18,972	–	18,972	–	–
Banks	426,337	–	426,337	231,332	28,917
Corporates	1,529,467	16,069	1,513,398	1,394,605	174,326
Regulatory retail	398,830	442	398,388	298,791	37,349
Mortgage	93,829	126	93,703	70,277	8,785
Investment in securities	95,100	–	95,100	150,671	18,834
Past Due	46,168	366	45,802	48,172	6,022
Real Estate	42,242	–	42,242	70,065	8,758
Other assets and cash items	98,355	–	98,355	82,684	10,336
Total Credit Risk	**3,962,410**	**17,003**	**3,945,407**	**2,366,212**	**295,779**
Market Risk	–	–	–	28,050	3,506
Operational Risk	–	–	–	226,425	28,303
Total Risk Weighted Exposure	**3,962,410**	**17,003**	**3,945,407**	**2,620,687**	**327,588**

Credit Risk Mitigation and Collateral valuation policy

BBK employs a range of techniques to mitigate risk in its credit portfolio. Credit risk mitigation includes an objective assessment of the counterparty's capacity and willingness to meet its commitments in the normal course. The bank strives to optimize facility structure, collateral, lending covenants, terms and conditions.

The Bank has detailed policies and procedures for valuing collateral/ securities offered for various credit facilities. The collateral is valued, at minimum, quarterly or annually, based on the type of security. More frequent valuations are also considered if warranted by market volatility and declining trends in valuations are observed. The collaterals and support include mortgages, cash collaterals, marketable securities, personal and corporate guarantees and guarantees from sovereigns and financial institutions. The basis of valuation for different types of securities such as equity, debt, and real estate is also clearly defined in the policies.

9 OPERATIONAL RISK

Year	2014 BD '000	2015 BD '000	2016 BD '000	Total BD '000
Gross Income	**113,720**	**116,732**	**131,818**	**362,270**
Number of years with positive Gross Income				3
Average				**120,757**
Alpha relating the industry wide level of required capital to the industry wide level of the indicator				15%
Capital Charge under the Basic Indicator Approach-K-BIA				**18,114**
Multiplier				12.5
Risk Weighted Exposure				**226,425**

10 FUNDED AND UNFUNDED TOTAL CREDIT EXPOSURE

Total gross credit exposures	Total funded credit exposures BD '000	Total un-funded credit exposures BD '000
Sovereign	1,209,360	3,750
Public Sector Entities	18,616	356
Banks	415,433	10,904
Corporates	1,373,454	156,013
Regulatory retail	398,830	–
Mortgage	93,829	–
Investment in securities	95,100	–
Past due	46,168	–
Real estate	42,242	–
Other assets and cash items	98,355	–
Total credit risk	**3,791,387**	**171,023**

11 AVERAGE CREDIT EXPOSURE

The following are the average quarterly balances for the year ended 31st December 2017:

	BD'000
Sovereign	1,065,552
Public Sector Entities	20,287
Banks	523,398
Corporates	1,502,475
Regulatory retail	378,223
Mortgage	90,761
Investment in securities	99,137
Past Due	60,655
Real estate	40,360
Other assets and cash items	84,542
Total credit risk	**3,865,390**

12 CONCENTRATION OF CREDIT RISK BY REGION (EXPOSURES SUBJECT TO RISK WEIGHTING)

	GCC BD'000	North America BD'000	Europe BD'000	Asia BD'000	Others BD'000	Total BD'000
Cash and balances with central banks	465,496	–	–	3,940	–	**469,436**
Treasury bills	418,093	–	–	9,037	–	**427,130**
Deposits in banks and other financial institutions	163,999	27,311	14,949	17,565	–	**223,824**
Loans and advances to customers	1,559,046	–	78,619	109,783	22,792	**1,770,240**
Investments in associated companies	45,823	–	660	–	–	**46,483**
Investment securities	496,595	10,235	123,890	80,426	38,943	**750,089**
Other assets	98,437	–	397	5,351	–	**104,185**
Total funded exposure	**3,247,489**	**37,546**	**218,515**	**226,102**	**61,735**	**3,791,387**
Unfunded commitments and contingencies	149,886	80	6,336	14,708	13	**171,023**
Total credit risk	**3,397,375**	**37,626**	**224,851**	**240,810**	**61,748**	**3,962,410**

13 CONCENTRATION OF CREDIT RISK BY INDUSTRY (EXPOSURES SUBJECT TO RISK WEIGHTING)

	Trading and manufacturing BD '000	Banks and other financial institutions BD '000	Construction and real estate BD '000	Government and public sector BD '000	Individuals BD '000	Others BD '000	Total BD '000
Cash and balances with central banks	–	18,597	–	450,839	–	–	**469,436**
Treasury bills	–	–	–	427,130	–	–	**427,130**
Deposits in banks and other financial institutions	–	223,824	–	–	–	–	**223,824**
Loans and advances to customers	585,605	176,473	380,243	13,418	449,359	165,142	**1,770,240**
Investments in associated companies	–	42,102	–	–	–	4,381	**46,483**
Investment securities	44,111	196,540	18,339	477,456	–	13,643	**750,089**
Other assets	–	–	–	–	–	104,185	**104,185**
Total funded exposure	**629,716**	**657,536**	**398,582**	**1,368,843**	**449,359**	**287,351**	**3,791,387**
Unfunded commitments and contingencies	94,624	15,669	36,852	738	148	22,992	**171,023**
Total credit risk	**724,340**	**673,205**	**435,434**	**1,369,581**	**449,507**	**310,343**	**3,962,410**

14 CONCENTRATION OF CREDIT RISK BY MATURITY (EXPOSURES SUBJECT TO RISK WEIGHTING)

	Within 1 month BD '000	1 to 3 months BD '000	3 to 6 months BD '000	6 to 12 months BD '000	1 to 5 years BD '000	5 to 10 years BD '000	10 to 20 years BD '000	Above 20 years BD '000	Total BD '000
Cash and balances with central banks	389,128	–	–	–	–	–	–	80,308	**469,436**
Treasury bills	49,929	135,726	124,198	117,277	–	–	–	–	**427,130**
Deposits in banks and other financial institutions	185,205	38,619	–	–	–	–	–	–	**223,824**
Loans and advances to customers	252,085	161,699	123,896	163,084	742,113	241,279	45,872	40,212	**1,770,240**
Investments in associated companies	–	–	–	–	–	–	–	46,483	**46,483**
Investment securities	29,085	29,727	12,182	7,547	305,248	226,442	26,891	112,967	**750,089**
Other assets	68,311	–	–	–	32,601	304	1,257	1,712	**104,185**
Total funded exposure	**973,743**	**365,771**	**260,276**	**287,908**	**1,079,962**	**468,025**	**74,020**	**281,682**	**3,791,387**
Unfunded commitments and contingencies	62,534	32,229	28,258	40,810	3,150	2,916	378	748	**171,023**
Total credit risk	**1,036,277**	**398,000**	**288,534**	**328,718**	**1,083,112**	**470,941**	**74,398**	**282,430**	**3,962,410**

15 IMPAIRED LOANS AND PROVISIONS

	Principle outstanding BD '000	Impaired loans BD '000	Stage 3: Lifetime ECL credit- impaired BD '000	Net Specific charges during the period BD '000	Write off during the period BD '000
Trading and manufacturing	624,856	50,041	30,513	20,600	18,499
Banks and other financial institutions	180,319	2,379	1,839	11	–
Construction and real estate	400,838	29,214	17,977	5,076	14,614
Government and public sector	20,795	16,204	7,240	886	–
Individuals	459,540	8,466	7,773	2,313	2,347
Others	166,630	1,227	920	26	9,436
Total	**1,852,978**	**107,531**	**66,262**	**28,912**	**44,897**

16 AGEING OF IMPAIRED AND PAST DUE LOANS BY REGION

	GCC BD '000	North America BD '000	Europe BD '000	Asia BD '000	Others BD '000	Total BD '000
3 months up to 1 year	74,555	–	–	1,120	–	**75,675**
1 to 3 years	17,465	–	–	–	–	**17,465**
Over 3 years	14,377	–	–	14	–	**14,391**
Total past due and impaired loans	**106,397**	**–**	**–**	**1,134**	**–**	**107,531**
Stage 3: Lifetime ECL credit– impaired	(65,971)	–	–	(291)	–	**(66,262)**
Stage 1: 12-month ECL and stage 2 : Lifetime ECL not credit- impaired	(46,065)	–	–	–	–	**(46,065)**

17 AGEING OF IMPAIRED AND PAST DUE LOANS BY INDUSTRY

	Trading and manufacturing BD '000	Banks and other financial institutions BD '000	Construction and real estate BD '000	Government and public sector BD '000	Individuals BD '000	Others BD '000	Total BD '000
3 months up to 1 year	41,812	2,379	11,842	16,204	2,214	1,224	**75,675**
1 to 3 years	5,421	–	9,225	–	2,816	3	**17,465**
Over 3 years	2,808	–	8,147	–	3,436	–	**14,391**
Total past due and impaired loans	**50,041**	**2,379**	**29,214**	**16,204**	**8,466**	**1,227**	**107,531**
Stage 3: Lifetime ECL credit- impaired	(30,513)	(1,839)	(17,977)	(7,240)	(7,773)	(920)	**(66,262)**
Stage 1: 12-month ECL and stage 2: Lifetime ECL not credit- impaired	(15,239)	(4,592)	(9,895)	(349)	(11,693)	(4,297)	**(46,065)**

18 RESTRUCTURED LOANS

	BD'000
Loans restructured during the period	89,739
Impact of restructured facilities and loans on provisions	15,512

The above restructuring did not have any significant impact on present and future earnings and were primarily extentions of the loan tenor, revisions in interest rate, and additional collateral received.

19 MARKET RISK DISCLOSURES FOR BANKS USING THE INTERNAL MODELS APPROACH (IMA) FOR TRADING PORTFOLIOS

The "Market Risk Internal Model" is being used to measure Value-at-Risk (VaR) for calculating Capital Charge arising from Market Risk exposures (mainly Foreign Exchange and Interest Rate Risk positions) of the Trading Book. The VaR Model quantifies the maximum potential loss that could occur in the Trading book risk positions under normal market conditions, at 99% confidence level, on a 10-day horizon.

BBK maintains a prudent approach to Manage Market Risk exposures guided by Market Risk Policy and Procedure. The Position, Stoploss and VaR limits are monitored by Treasury Middle Office (reporting to Risk and Credit Administration Department and Independent of Business unit) and a daily risk report is circulated to the Senior Management.

In addition to the above, the Treasury Middle Office also carries out valuation of the Investment Portfolio independently as per the internal policies and procedures. Furthermore BBK also conducts Stress Testing and Back Testing of Market Risk positions.

The summary of VaR of the trading book for the period January 2017 to December 2017 is as follows:

VaR Results for 2017 (10 day 99%)

Global (BAHRAIN and KUWAIT)

1 January 2017 to 31 December 2017

Asset class	Limit BD '000	VaR 31 December 2017 BD '000	High VaR BD '000	Low VaR BD '000	Average VaR BD '000
Foreign exchange	641.00	147.37	270.19	87.46	159.22
Interest rate	151.00	2.03	8.87	0.11	1.22
	792.00	**149.40**	**271.35**	**88.47**	**160.44**

The Bank conducts Backtesting of VaR on a daily basis in compliance with CBB regulations to validate the internal VaR model and to check whether or not the model can predict potential losses with a fair degree of accuracy. Under Backtesting, the daily VaR numbers are compared with the mark-to-market profit or loss figures (on actual average Profit and Loss basis and also hypothetical Profit and Loss basis). If this comparison is close enough, the Backtest raises no issues regarding quality of the risk measurement model.

The Backtesting results for the period January-December 2017 confirmed that there was one occasion on which a daily trading loss exceeded VaR figure.

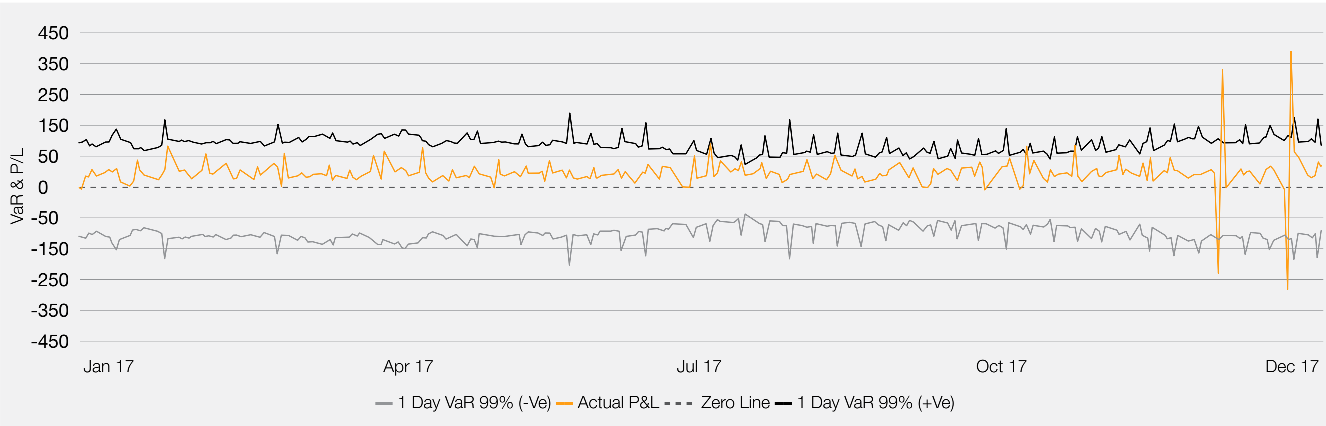
19 MARKET RISK DISCLOSURES FOR BANKS USING THE INTERNAL MODELS APPROACH (IMA) FOR TRADING PORTFOLIOS (continued)

Month end VaR (10 day 99%)

Month	VaR BD'000
January 2017	175
February 2017	231
March 2017	181
April 2017	162
May 2017	159
June 2017	137
July 2017	129
August 2017	109
September 2017	120
October 2017	158
November 2017	166
December 2017	149

The following graph shows the daily average Profit and Loss (Actual Average P & L basis) vis-à-vis one day VaR, for the review period.

Value-at-Risk Backtesting January – December 2017



20 CONCENTRATION RISK TO INDIVIDUALS WHERE THE TOTAL EXPOSURE IS IN EXCESS OF SINGLE OBLIGOR LIMIT OF 15%

	BD '000
Sovereign	914,450
Total	914,450

21 CREDIT DERIVATIVES EXPOSURE

BBK is not exposed to any credit derivatives as at 31st December 2017.

22 EQUITY POSITIONS IN THE BANKING BOOK

	BD '000
Publicly traded equity shares	40,979
Privately held equity shares	23,720
Total	64,699
Capital required	8,087

23 GAINS ON EQUITY INSTRUMENTS

	BD '000
Realised Gains/ Losses in statement of profit or loss	442
Realised Gains/ Losses in retained earnings	(1,325)
Unrealised Gains/ Losses in CET1 Capital	(20,530)