BBK

بنك البحرين والكويت

Leading

WITH EXCELLENCE

Annual Report 2016

Contents

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

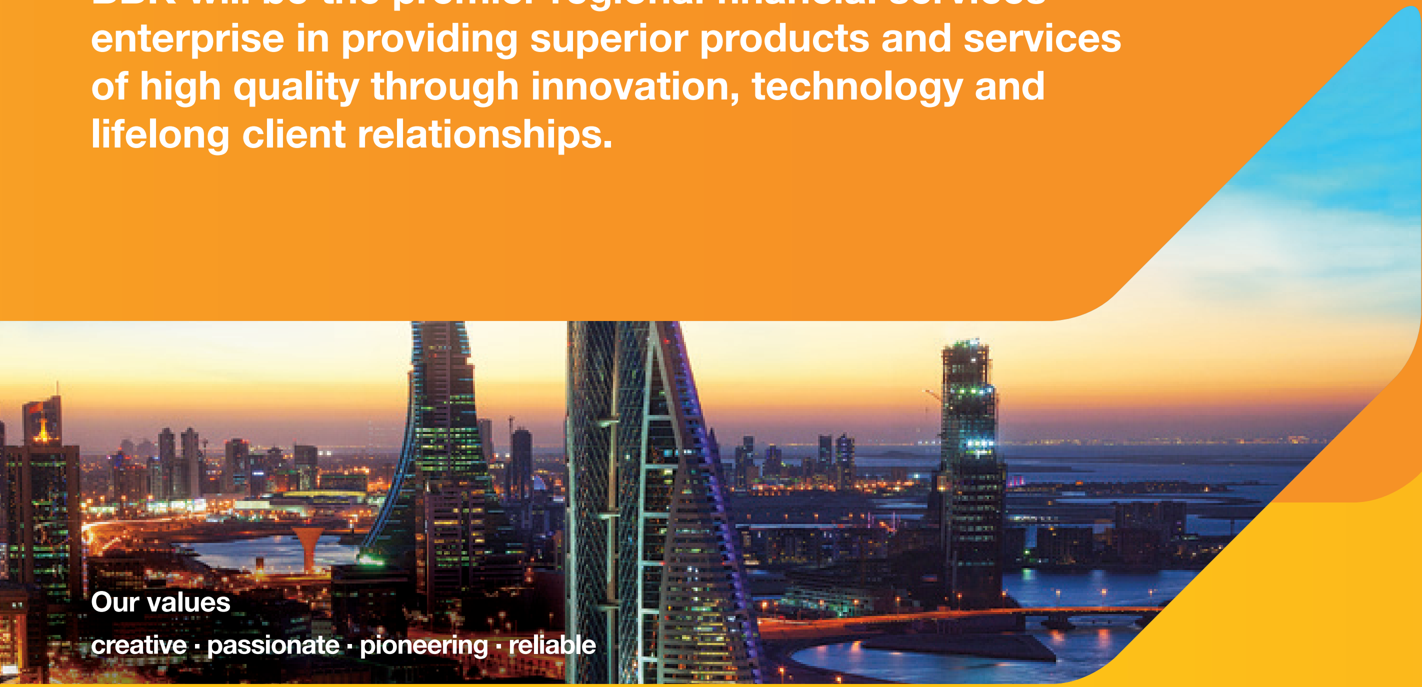
Designed and produced by Origin Communications Group

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

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 values

creative · passionate · pioneering · reliable

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.

Net interest income

+18.0%

Net interest income for the year was BD 85.8 million.

Total assets

+1.5%

Total assets increased to BD 3,703 million.

Net profit

+6.0%

Net profit increased to BD 56.4 million.

	2012	2013	2014	2015	2016
Income statement highlights (BD millions)					
Net interest income	65.8	68.9	72.3	72.7	**85.8**
Other income	42.9	43.5	45.2	48.4	**47.7**
Operating expenses	50.6	54.4	46.2	49.8	**53.1**
Net profit	42.4	45.1	50.1	53.2	**56.4**
Cash dividend	10%	10%	20%	25%	**30%**
Stock dividend	10%	10%	5%	–	**–**
Financial statement highlights (BD millions)					
Total assets	3,108	3,231	3,501	3,646	**3,703**
Loans and advances	1,499	1,619	1,846	1,765	**1,767**
Investments	772	802	824	794	**812**
Customer deposits	2,205	2,353	2,471	2,643	**2,494**
Term borrowings	238	239	241	205	**206**
Total equity	290	333	359	361	**474**
Profitability					
Earnings per share (fils)	46	44	47	50	**49**
Cost/income	46.54%	48.41%	39.33%	41.14%	**39.80%**
Return on average assets	1.46%	1.43%	1.49%	1.44%	**1.51%**
Return on average equity	16.34%	14.56%	13.93%	14.79%	**13.23%**
Profit per employee (BD)	38,789	45,232	48,826	52,169	**54,136**
Capital					
Capital adequacy	14.29%	15.33%	15.63%	14.87%	**18.48%**
Equity/total assets	9.32%	10.31%	10.26%	9.89%	**12.81%**
Debt/equity	82.18%	71.94%	67.05%	56.74%	**43.46%**
Liquidity and business indicators					
Loans and advances/total assets	48.23%	50.10%	52.74%	48.40%	**47.73%**
Loans and advances/customer deposits	67.98%	68.79%	74.72%	66.78%	**70.86%**
Investments/total assets	24.85%	24.82%	23.53%	21.77%	**21.93%**
Liquid assets/total assets	36.50%	33.25%	29.19%	32.04%	**32.61%**
Net yield ratio	2.50%	2.39%	2.32%	2.12%	**2.46%**
Number of employees	1,092	996	1,026	1,020	**1,042**

Leading WITH STRATEGY

Dear Shareholders

It is my pleasure and privilege to introduce BBK's annual report for the year ended 31 December 2016.

This was the first year of our new three-year strategic cycle, and we can reflect with some satisfaction on what has been achieved – both in terms of results and in preparing for the future. The business environment has continued to be difficult at home and abroad, but BBK has maintained the consistent performance that has been our hallmark for so long, as detailed in this report.

I take this opportunity to 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. I also extend thanks to their respective governments and regulatory authorities for their support and guidance.

I thank the Board of Directors and all stakeholders for their outstanding contributions during the year. I have every confidence that their counsel and expertise will be equally valuable in realising the vision for growth contained in our new 2016-18 strategic cycle.

Murad Ali Murad
Chairman

The Board of Directors is honoured to present the 45th annual report and consolidated financial statements of BBK and its subsidiaries (the Group) for the year ended 31 December 2016.

Operating environment

Both regionally and worldwide, economic conditions have been uncertain to say the least, and there are few prospects of immediate improvement. Nevertheless, BBK has performed well, particularly considering the prevailing circumstances.

The current macro-economic cycle could last another two to three years, and with it will come structural changes in the economy of Bahrain and the rest of the Gulf. We are already seeing reductions in subsidies and will begin to pay more for services provided by governments in the region. For example, value added tax is expected to be introduced in 2018 and other taxes may also be levied – a further illustration of the structural changes that are taking place.

Bahrain's government will also continue to rely on national debt. A considerable number of various kinds and tenors of bonds have been issued, all very successful even though Bahrain no longer has an investment-grade rating. Low interest rates globally have helped to contain yield, other than at the short end of the market such as three to six-month treasury bills, so overall costs have been at an acceptable level.

The GCC contribution to Bahrain has helped to keep economic activity at a reasonable level, with much of the funds going to infrastructural projects such as roads, housing, hospitals and airport expansion. We believe that GDP growth will be lower than last year's 3.0 percent, still a fair achievement in the circumstances, but with the GCC contribution now having largely run its course, next year could be very different.

In an international context, Bahrain has fared relatively well, avoiding the drastic action that other countries have had to take. We are fortunate to have been able to manage reasonably well with limited resources. This does not mean it hasn't been difficult – and will continue to be. Oil prices, the slowdown in the Chinese economy and Brexit are all factors that have not been conducive to growth or expansion.

Oil producers have been increasing output, and falling demand adds to the pressure on price. The expected 6.0-6.5 percent growth rate in China almost looks like a recession after a protracted period of double-digit growth. In time, we will also feel the effects of Brexit, as will the UK, the EU, and many other countries, depending on what kind of agreement they can arrange. This all adds to uncertainties, locally and globally.

As for our own planned new venture, an investment company in the UK, we believe London will continue as a major financial centre, regardless of the outcome.

A year of achievement

Against this domestic and global background of difficulty and uncertainty, BBK returned a very commendable across-the-board performance.

From an internal perspective, our transition of management leadership has been smooth. Abdulkarim Bucheery retired as Chief Executive in March 2016, succeeded by Reyadh Sater, a highly experienced member of BBK's executive team with many years of distinguished service. And close to the year-end, we reorganised and refined BBK's structure, establishing two main business groups – Wholesale and Retail – and appointing two Deputy Chief Executives.

The success of the transition is evident from our results for the year, and is probably the number one highlight of our performance and achievements over the period.

The second highlight is our very successful perpetual bond issue. We tapped difficult market conditions and raised a BD 86 million addition to our Tier 1 capital, improving our capital adequacy ratio from 14.87 percent to around 18.48 percent. This was a very satisfactory result as the increase in capital helps us fund the Bank's ambitious strategy of expansion and diversification, while also boosting capital adequacy as per Basel III requirements.

Capital adequacy ratio

18.48%

The BD 86 million addition to BBK's Tier 1 capital improved the Bank's capital adequacy ratio from 14.87 percent to around 18.48 percent.

Shareholders' equity

+31.5%

Shareholders' equity rose from BD 360.7 million in 2015 to BD 474.2 million in 2016.

The Board of Directors has resolved to implement IFRS 9. It does not become effective until 2018, so BBK is one of the first banks in the region, if not the first, to implement it.

The third highlight is our focus on the first year of our new three-year strategic cycle for 2016-18. We established a representative office in Turkey and built on our existing branches in India, focusing on quality rather than quantity and making our activities there more profitable. In Bahrain we have been able to join in various government financing requirements by participating in new bond issues. The increased yield from these issues has contributed to significant growth in interest income, reinforced by deposit interest rates not moving higher at the same pace, thus containing our cost of funding.

We are also diversifying our sources of funding, as deposits continue to be very important. We have negotiated with customers to extend the duration of their deposits, in some cases by up to three years. We have also tapped the repo market. As a result, our balance sheet profile is stronger, with a spread of maturity dates. This has enabled us to maintain a very comfortable level of liquidity, a factor which we closely monitor – not only our own situation, but overall market conditions such as US Dollar liquidity.

In such a difficult environment, some of the Bank's customer relationships have been under pressure, needing restructuring or more financing to help them trade through the uncertain times. Customers need time to restructure and assistance to manage in an uncertain economic climate. Our provisions reinforce our responsibilities in this area, as a bank and to our region.

Nevertheless, due to difficult market conditions, most industries have encountered stressed financial performance, which impacts most financial institutions. In light of this, we aim to maintain an acceptable level of non-performing loans. This is another challenge that we monitor constantly.

Financial highlights

BBK achieved a net profit of BD 56.4 million for 2016, surpassing the previous year by BD 3.2 million, a 6.0 percent improvement. Net interest income rose to BD 85.8 million, up by 18.08 percent from the previous year's BD 72.7 million, and shareholders' equity rose by 31.5 percent to BD 474.2 million.

The Bank delivered consistent underlying performance in its core business, demonstrating the soundness of its strategy and management team. The total balance sheet strengthened to BD 3,702.6 million by the end of 2016, an increase of 1.5 percent.

As a result of the successful perpetual bond issue, BBK's capital was boosted by BD 86 million, raising the capital adequacy ratio substantially above the minimum regulatory requirement. The ratio of liquid assets to total assets strengthened to 32.6 percent, from 32.0 percent. The Board has recommended a cash dividend of 30 fils per share.

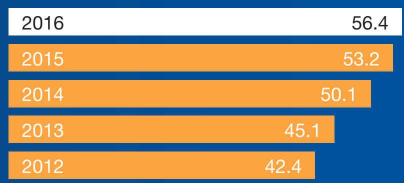
Compliance leadership

The Board of Directors has resolved to implement International Financial Reporting Standard 9 (IFRS 9), following the approval of the Central Bank of Bahrain. The new standard has been promulgated by the International Accounting Standards Board and sets out requirements for recognising and measuring risks on various financial assets. It does not become effective until 2018, so BBK is one of the first banks in the region, if not the first, to implement it. BBK is also among the first banks in the world to adopt IFRS 9.

We are also focusing on further improvements to our corporate governance practice. One of the key advances in this area during 2016 was to have our risk management function reporting directly to the Board Risk Committee, rather than within the Bank's internal executive management structures. This is another first for BBK, after applying the same practice several years ago to audit reporting.

The Bank delivered consistent underlying performance in its core business, demonstrating the soundness of its strategy and management team.

Net profit
(BD millions)



Our plan to establish a joint-venture wholesale investment firm in London is at an advanced stage of implementation.

Appropriations

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

	BD'000
Retained earnings as at 1 January 2016 (restated)	107,560
Profit for the year 2016	56,410
Proposed appropriation for donations	(1,400)
Other negative changes in retained earnings	(7,474)
Retained earnings as at 31 December 2016 available for distribution (before proposed dividend)	**155,096**
Proposed cash dividends (30% of paid-up capital, net of treasury stock)	32,266
Retained earnings as at 31 December 2016 (after proposed dividend)	**122,830**

Fitch

	Rating
Long-term issuer default rating	BB+
Short-term issuer default rating	B
Viability rating	bb+
Support rating	3
Support rating floor	BB+
Senior unsecured debt	BB+
Subordinated debt	BB
Outlook	Stable

Report issue date: 15 November 2016

Moody's

	Rating
Bank deposits (foreign currency)	Ba3/NP
Bank deposits (domestic currency)	Ba2/NP
Baseline credit assessment	ba2
Adjusted baseline credit assessment	ba2
Counterparty risk assessment	Ba1(cr)/NP(cr)
Senior unsecured	Ba2
Subordinate	Ba3
Outlook	Negative

Report issue date: 11 November 2016

Fitch
Long-Term Issuer Default Rating

BB+

Moody's
Long-Term Bank Deposits

Ba3

Backing Bahrain

BBK continues to provide opportunities to qualified and accomplished Bahraini employees. Our organisational structure relies on Bahrainis to take additional responsibility and assume management positions for more functional areas. This is not only to recognise their skills, but is crucial to succession planning. We are developing people who can grow with the Bank, essential as we have some very good managers approaching retirement age. In managing succession and planning ahead, we look first to talent within the Bank.

As detailed in the CSR section of this report, we also continue to invest heavily in our community, further demonstrating our commitment to supporting Bahrain and its people.

BBK received the Distinguished Projects Award at the 33rd GCC Social Affairs and Development Conference in Saudi Arabia. The BBK Health Centre in Hidd was a significant contributory project in this achievement. Financed and equipped by the Bank at a cost of BD 4 million, the Hidd centre is a unique model of advanced healthcare services and the latest medical technology.

Looking ahead

Overall, we are confident that the Bank is in a very strong position to manage its various resources – human and financial – to be able to achieve its strategy and the growth we seek, despite extremely uncertain conditions and a difficult environment.

There are no signs that this environment is going to change soon, but we are well diversified as far as risk is concerned. We are also very diversified in revenue streams – and virtually every stream is doing well, whether CrediMax, Invita, Kuwait, India, or other cross-border operations. All are generating acceptable bottom-line results, and we have every reason to expect this to continue as our 2016-18 strategic cycle advances.

Appointment of auditors

At the Annual General Meeting held on 28 March 2016, Ernst & Young were re-appointed as external auditors to BBK for the financial year ending 31 December 2016.

Ratings

On 15 November 2016, Fitch affirmed BBK's long-term issuer default rating (IDR) at BB+ with a 'stable' outlook. The agency says this rating is driven by the Bank's standalone strength and supported by its satisfactory and resilient financial performance, as reflected in BBK's viability ratings, support ratings, and support rating floors.

Despite the weakening operating environment in Bahrain, BBK has maintained solid margins and consistent profitability through its well-established franchise. Funding and liquidity indicators remain satisfactory and are important rating drivers. Asset quality metrics are sound.

On 11 November 2016, Moody's reported that its Ba2 (Negative)/Not-Prime ratings of BBK's local currency deposit and senior unsecured debt capture the Bank's stand-alone credit strength as reflected in a baseline credit assessment (BCA) of ba2, which is at the same level as the Ba2 (Negative) Bahraini sovereign rating.

The ba2 BCA captures BBK's strong domestic franchise, which, in addition to recent efficiency improvements, supports profitability; solid liquidity buffers and a resilient funding profile; and improved capital levels.

Appreciation

The Board acknowledges the long-term contribution of our outgoing Chief Executive, Abdulkarim Bucheery, and we wish him well in his retirement.

We also extend gratitude to BBK's shareholders for their continued confidence, to our clients for their loyalty and patronage, and to BBK's management and employees for the hard work and commitment that underpins another year of excellent results for the Bank.

On behalf of the Board of Directors

Murad Ali Murad
Chairman

BBK received the Distinguished Projects Award at the 33rd GCC Social Affairs and Development Conference in Saudi Arabia.

Murad Ali Murad
Chairman

Chairman of the Nomination, Remuneration and Corporate Governance Committee

Chairman of the Risk Committee

Director since 21 March 1999
(Independent and non-executive)

Qualifications and experience
Fellow member of the Chartered Institute of Management Accountants, London, United Kingdom. Over 44 years' experience in the banking sector and has own business for the past 14 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. 32 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 and non-executive)

Qualifications and experience
Bachelor of Arts, Economics and Finance, University of Aleppo, Syria. Over 35 years' experience in the banking sector.

Sh. Khalifa bin Duaij Al Khalifa
Board Member

Director since 27 February 2005
(Independent and non-executive)

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. 9 years' experience in the government sector (investment field) and 10 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. 32 years in the investment sector.

Nominated by:
Kuwait Investment Authority

Mutlaq Mubarak Al Sanei
Board Member

Director since 6 March 2011
(Non-executive)

Qualifications and experience
Bachelor of Economics, Kuwait University, State of Kuwait. Over 30 years' experience in the management of diversified investments across the Middle East and North Africa and around 7 years in the management of real estate and tourism projects in North Africa.

Jassem Hasan Ali Zainal
Board Member

Chairman of the Audit Committee

Director since 22 November 1994
(Independent and non-executive)

Qualifications and experience
Master in Civil Engineering, Kuwait University, State of Kuwait. 26 years' experience in the banking sector, 4 years in the government sector, 8 years with finance companies, 8 years with investment companies and has own business for 8 years.

Dr. Zakareya Sultan AlAbbasi
Board Member

Director since 22 February, 2012
(Non-executive)

Qualifications and experience
PhD., University of East Anglia, United Kingdom. 31 years' experience in the government sector (Social Insurance).

Nominated by:
Social Insurance Organization (SIO)

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. 16 years' experience in the banking and investment sector.

Elham Ebrahim Hasan
Board Member

Director since 6 March 2011
(Non-executive)

Qualifications and experience
Bachelor of Science in Accountancy, University of Cairo, Egypt. Certified Public Accountant from Boston, MA, United States of America. 31 years' experience in the auditing field (primarily auditing banks and financial institutions).

Nominated by:
Ithmaar Bank

Yusuf Saleh Khalaf
Board Member

Director since 6 March 2011
(Independent and non-executive)

Qualifications and experience
Associate of the Association of Chartered Certified Accountants, United Kingdom, with experience of 36 years in the banking and financial services sector.

Hassan Mohammed Mahmood
Board Member

Director since 1 September 2010
(Non-executive)

Qualifications and experience
Bachelor of Commerce, University of Bangalore, India. Over 19 years' experience in audit and consultancy and over 19 years in Islamic finance.

Nominated by:
Ithmaar Bank

Leading

WITH INNOVATION

Our representative office in Turkey opened during the year, prominently located in downtown Istanbul.

BBK faced a very challenging year, as did all banks – locally, regionally, and internationally – not least because of the many difficulties facing governments, especially in our domestic and regional environments.

Low oil prices are at the core, oil being the primary source of income for all the GCC states. Expenditure levels have to be financed somehow, and governments are faced with the option of using reserves – far from ideal – or borrowing, again adding extra costs through interest.

Rating agencies' downgrades of Bahrain and Oman have led to more expensive finance charges, with governments having to pay a higher yield when raising capital. BBK's status as a Domestic Systemically Important Bank (D-SIB) means that we are linked to government ratings and have to bear a corresponding increase in the cost of funding.

Government demand has to some extent affected market liquidity, increasing the pressure on banks. This is not confined to 2016 and will continue for as long as oil prices remain at current depressed levels. Liquidity management has therefore been a top priority for BBK, and we have taken the necessary action to ensure that our liquidity is not only maintained but reinforced.

Consequently, we have very healthy liquidity levels, an asset that is as crucial to our future as it is to the banking sector as a whole. I believe we have dealt very effectively and efficiently with liquidity during 2016, underpinning our performance. This is evident in our bottom-line results, which show profit growth of 6 percent at year-end.

Strategic cycle

The past year was the first in our new strategic cycle, covering the period 2016-18. We have identified many new opportunities, adopting a policy of gradual rather than aggressive implementation. Two of these are particularly important.

The first entails developing a relatively untapped market. Bahrain has a large population of foreign workers who require specific services. We have analysed this segment and evaluated its potential for growth. An internal taskforce has been established to investigate further and determine the form that BBK's tailored offering may take.

The Bank already leads the market in several retail segments – consumer loans and car loans, for example. We are capitalising on these successes and reinforcing our leadership – hence the strategic focus on new products and services, defining prospective new segments and their needs. Plans are at an early stage, but by the first quarter of 2017 we expect to announce further progress with the initiatives that are under way to further diversify and innovate within Bahrain.

The increase in net interest income achieved in 2016 indicates good balance sheet management, focusing strategically on the local market and reducing exposure to thinly priced paper. Instead we have concentrated on the more profitable segments, such as retail, which has yielded returns superior to blue-chip holdings.

Retail lending has helped boost income growth and we aim to further expand our portfolio. We also have liquidity in short-term treasury bills, offering rates that are now almost three-fold those of two years ago, in turn contributing to growth in interest income.

Strategically, high liquidity always bears a cost for banks. But considering the operating environment and the challenges facing local and regional economies, we believe that being very liquid is a positive for BBK. Consequently, we plan to maintain this position, making sure we are always prepared and ready for the unforeseen.

Our 2016-18 strategy is based on progressive implementation, choosing our moves in the context of economic realities as the environment does not encourage aggressive short-term implementation.

With this in mind, we are examining the potential for affluent services. We recognise that our retail customers sometimes need investment products – often of an international nature – and we may be able to introduce them to certain opportunities. We are therefore continuing to assess the kind of services we can offer, as a precursor to introducing them to the local market.

In terms of cross-border operations, our representative office in Turkey, prominently located in downtown Istanbul, began operations. A highly qualified Turkish woman was appointed to head the office, maintaining our long-standing policy of gender impartiality in deciding on appointments or promotions.

Close to the year-end, we reorganised and refined BBK's structure, establishing two main business groups – Wholesale and Retail – and broadening the responsibilities of the support functions.

Leading WITH PERFORMANCE

We built on our existing branches in India, focusing on quality rather than quantity and making our activities there more profitable.

Perpetual bond

Another major event was the successful issue of our perpetual bond for Tier 1 capital, the first of its kind in Bahrain and, as far as we know, the first in the entire Middle East. The offer closed at the end of April and raised BD 86 million, enabling us to meet and exceed the new capital requirements stipulated by Basel III and the Central Bank of Bahrain.

The success of the bond issue resulted in BBK taking third place in the 2016 'Financial Institution Financing Deal of the Year' category at the Bonds, Loans & Sukuk Middle East Awards. BBK was the only conventional bank to be shortlisted.

As a D-SIB, the Central Bank requires BBK to maintain specific levels of capital. The perpetual bond uptake resolved this issue and at the same time positioned us well to implement our 2016-18 strategic cycle, which is heavily dependent on liquidity and capital resources.

Unlike last year's capital markets issue to replace maturing debt, which was open to international investors, the perpetual bond was restricted to shareholders, giving them the privilege of a relatively high yield. The 8.25 percent issue rate is fixed for the first five years, with an option to renew then at a return determined by prevailing market rates.

Organisational restructuring

Driven by our new strategy, a new organisation structure was announced, aimed at fostering the Bank's three-year strategy (2016-2018), and achieving the future vision and expectations of the Bank's shareholders and stakeholders.

The changes resulted in two business groups being established – Wholesale and Retail – each headed by a newly appointed Deputy Chief Executive.

The Wholesale Group's responsibilities include Corporate Banking, Treasury and Investment as well as our overseas operations, namely the four branches in India, Kuwait branch, and the UAE and Turkey representative offices.

As its name implies, the Retail Banking Group is responsible for Retail banking services, in addition to Remedial management and a number of strategic projects of the Bank.

The support divisions – Human Resources & Administration, Information Technology & Operations, and Financial Planning & Control – have each been converted to Groups, assuming broader responsibilities to cover overseas branches. All these Groups report directly to the Chief Executive, as the Support Group has been eliminated as part of the restructuring.

Our people

We have continued to develop the Bank's number one asset – our employees – by launching the BBK e-Learning platform, recognised as one of the best programmes of its kind in the industry. The platform houses the world's most widely used financial e-learning library, containing more than 500 tutorials and courses in banking and financial services, as well as professional business skills.

It also enables 'anytime, anywhere' access to learning for our geographically dispersed workforce. The flexibility and convenience of the system will help enormously in accelerating the learning and development of all employees, especially in supporting working women by giving them a convenient developmental tool that also enables them to maintain a healthy work/life balance.

Our Women's Empowerment initiatives remain a top priority. Promoting gender equality at all levels and accelerating the development of female managers through fast-track programmes has been highly effective.

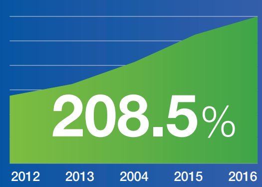
The formation of the BBK Alumni Club in 2015 has strengthened the bonds between the Bank and its former employees, showing appreciation of their role in the development of Bahrain's financial sector and in BBK's successful journey. The second reunion of the Alumni Club was held in December and was well attended. During the reunion, the Chief Executive announced a bundle of benefits for the BBK Alumni members and also honoured former female employees who served the Bank for more than 35 years.

Perpetual bond

BD 86m

BBK closed its perpetual bond for Tier 1 capital at BD 86 million, the first of its kind in Bahrain.

Online financial transactions



BBK online financial transactions have more than doubled over the last five years.

Technology
During 2016 we successfully tested the Bank's business continuity centre, which confirms that BBK is ready to respond effectively in the event of an adverse incident, minimising potential damage and maintaining essential customer services.

We also migrated to the new release of branch automation across all BBK locations in Bahrain and Kuwait. The new platform not only enables our employees to provide customers with improved online transactions, but supports business continuity by using a very robust IT architecture. In line with this, we updated various technologies in our data centres, allowing faster provisioning and scalability of the Bank's services. The Treasury back-office system was also upgraded to the latest release.

BBK remains at the forefront in meeting the Central Bank of Bahrain's requirements for new services. All pending electronic funds transfer system services were launched on the internet banking channel, at the same time making the changes necessary to ensure that SMS transaction advices are issued for all account and card-based transactions.

We have also revamped BBK's mobile banking channel. With a rich user interface accessible through the browsers of a wide range of smart phone devices, customers can now enjoy the convenience of being able to access the banking channel anytime and anywhere, with a more pleasant 'banking on the go' experience.

Our in-house technology teams worked to improve efficiency across a number of identified operational areas. The high standards of information security within the Bank were underlined by a successful review of BBK's ISO 27001-2013 certification.

Operational excellence
BBK was awarded 2016 Elite Quality Recognition by JP Morgan Chase for our outstanding performance in achieving a best-in-class 98.8 percent for MT103 straight-through processing (STP). MT103 is a message format used by the Society for Worldwide Interbank Financial Telecommunication (SWIFT) to conduct international wire transfers, telegraphic transfers, and large-value transfer system payments. STP is the automated process of payments that increases processing speed, minimises routing errors, and lowers operational and transaction costs.

This is the seventh year in a row that BBK has qualified for this award, presented to financial institutions that meet JP Morgan's stringent processing criteria. Less than 1 percent of JP Morgan's funds transfer clients received the award in the last year.

Distribution networks
In December we opened a new BBK branch in the Sanad area of Bahrain, having opened the long-awaited Hidd branch earlier in the year. The Sanad branch replaces the former Refinery branch, giving customers a more convenient location, improved space, and better accessibility. BBK now has a total of 17 branches and financial malls.

Subsidiaries
CrediMax is still exploring cross-border expansion, specifically in neighbouring markets. CrediMax also officially launched its new partnership with China's UnionPay. UnionPay cards are now accepted by CrediMax point-of-sale machines, and CrediMax is the first issuer and acquirer of UnionPay cards in Bahrain.

Invita, on the other hand, is now establishing a subsidiary in partnership with insurance companies specialised in car insurance claims between insurance companies. This initiative forms an important part of the strategic cycle for 2017.

Part of Invita's strategic goal to diversify its business and maximise income stream, it launched the Invita Training Centre (ITC), an internationally accredited service that provides organisations and individuals with world-class foundation-level training programmes. ITC is one of the few training centres in Bahrain to hold ISO 9001:2008 certification for quality management.

Our plan to establish a joint-venture wholesale investment firm in London is at an advanced stage of implementation. We are currently recruiting the management and technical team, after which we will start operation.

Risk, credit and compliance reporting
In line with corporate governance best practice, BBK's risk and credit function reports directly to the Board's Risk Committee, and the Compliance and Anti-Money Laundering function reports directly to the Board's Audit committee.

Internal control
The main role of the Internal Control Unit (ICU) is to ensure that adequate internal controls are in place in all departments and that the assets of the Bank are safeguarded. ICU has implemented well-designed and comprehensive systems and procedures that protect the Bank from risks that could arise in the course of doing business. Controls are reviewed at least annually.

Conclusion
Efficiency will continue to be a primary focus for BBK as we progress through our three-year strategic cycle. We will concentrate on using our resources as effectively as possible, working hard to produce better results with what we've got. During 2016, we were successful in reducing our cost to income ratio – itself indicative of efficiency improvement – and maintaining this trend will be a continuing goal.

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 would like to extend our appreciation to our loyal clients and our employees, whose dedication have contributed to the Bank's success journey.

Reyadh Yousif Sater
Chief Executive

Leading

WITH SERVICES

This is the seventh year in a row that BBK has qualified for the Elite Quality Recognition award, presented to financial institutions that meet JP Morgan's stringent processing criteria.

Reyadh Yousif Sater
Chief Executive *

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

39 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).

34 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).

31 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).

30 years' work experience, of which 15 years in banking.

Joined BBK in 2000.

C.K. Jaidev
Assistant General Manager
International Banking

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

27 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).

10 years' audit and 19 years' banking experience.

Joined BBK in 1999.

* Effective 1 April 2016
** Effective 28 December 2016

Jamal Mohamed Al Sabbagh
General Manager **
Information Technology and Operations Group

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

36 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).

22 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).

25 years' finance experience.

Joined BBK in 2001.

Amit Kumar
Assistant General Manager
Risk, Credit and Compliance

Qualifications and experience:
MBA, Indian Institute of Management, Republic of India (1983).

33 years' banking experience.

Joined BBK in 1994.

Neil Sharp
Assistant General Manager **
Treasury and Investment

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

30 years' banking experience in the Treasury business.

Joined BBK in 2009.

In 2016, the Bank received the Distinguished Projects Award at the GCC Social Affairs & Development conference, in Riyadh, Saudi Arabia. The award cited the Bank's many philanthropic projects, most notably the BBK Health Centre in Hidd, a unique model of advanced health care services which was financed and equipped to the value of BD 4 million.

Leading
WITH DEVELOPMENT

BBK is always conscious of the link between business success and social responsibility – a duty that is mutually beneficial and integral to sustaining long-term relationships. By supporting employees, addressing community needs, and backing Bahrain's financial sector, BBK sustains growth while promoting national economic development.

Every year the Bank allocates substantial donations and sponsorships that benefit a wide range of community-related projects and causes. For 2016, BBK's shareholders approved an appropriation amounting to BD 1.4 million.

BBK's proactive approach to social responsibility is regularly recognised by awards from independent authorities. In 2016, the Bank received the Distinguished Projects Award at the GCC Social Affairs & Development conference, in Riyadh, Saudi Arabia. The award cited the Bank's many philanthropic projects, most notably the BBK Health Centre in Hidd, a unique model of advanced health care services which was financed and equipped to the value of BD 4 million.

Supporting employees

BBK is committed to enhancing employee career development and empowering its people with greater responsibilities. The Bank is particularly proud that 96 percent of its employees are Bahraini nationals – investing in local talent through training and professional development aims to improve skills across the organisation and create opportunities for career advancement.

In supporting these objectives, a highlight of 2016 was the launch of the BBK e-Learning Platform, implemented in association with a world-leading financial e-learning library. The platform gives BBK's geographically dispersed workforce 'anytime, anywhere' access to a higher level of professional competence.

As an employer of choice, BBK provides generous employee benefits that include stock options, retirement programmes, and health and life insurance. The Bank also rewards employees who have contributed to the success of the Bank over many years, recognising them at an annual awards ceremony. The Bank also has an Alumni Club for former employees, maintaining the ties between past and present members of the BBK family.

Empowering women

Women represent 35 percent of the BBK workforce. The Bank's policy to empower women is a high-level document approved by the Board of Directors. Aiming to support and complement Bahrain's Women Empowerment Strategy, the policy sets out a clear vision and encourages empowerment and gender equality at all levels.

To achieve the objectives of the policy, the Bank's Women's Empowerment committee develops initiatives and programmes to help women reach their full potential and achieve their career goals while maintaining their work/life balance. To encourage this, the annual Chief Executive Award for Women's Empowerment recognises managers who support women's development and career growth.

Externally, the Bank continues to expand and reinforce business relationships with women-owned ventures, including small businesses and entrepreneurs. BBK also supports women's societies and associations in Bahrain in their goals of helping women gain independence and education.

Community involvement

BBK employees are encouraged to volunteer for various programmes that benefit the community. A typical example is volunteering in InJaz Bahrain, which aims to empower young people and prepare them for today's business challenges. During 2016, a number of BBK employees devoted their time to pass on skills and experience by giving classroom lectures in schools.

A highlight of 2016 was the launch of the BBK e-Learning Platform, implemented in association with a world-leading financial e-learning library.

Education CSR budget

36%

The Bank allocated 36 percent of the annual CSR budget to education in 2016 – up from 20 percent in 2015.

Support for the elderly and orphans

BD 65k

In 2016, BD 65,000 was donated to care homes for the elderly, with similar support for organisations that benefit orphans.

Addressing community needs

In 2012 BBK established a dedicated fund to support future CSR mega projects such as the BBK Health Centre in Hidd and the BBK Rehabilitation Centre. The fund's value grew to BD 1.685 million during 2016, 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.

Education

The Bank's emphasis on learning carries through into its external social responsibility work, where 36 percent of the budget is allocated to education – up from 20 percent in 2015. By investing in education, BBK helps pave the way for future generations and supports the development of young Bahraini talent.

In 2016, the Bank renewed its commitment as a Platinum Sponsor of the Crown Prince's International Scholarship Programme. BBK has committed BD 1 million to the initiative, which enables Bahrain's most talented young people to study at top international universities and colleges. As part of a five-year commitment, the Bank has also invested BD 50,000 in the Isa Bin Salman Fund, a scholarship fund established in 2013 to help students 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.

Health and sport

Over the years, health and wellbeing have been at the forefront of BBK's community contributions. The Bank donates to medical entities and research institutes active in fighting diseases such as diabetes, sickle cell anaemia, and cancers.

The Bank has increased its investment in sport and promotes the health benefits of participating. Through donation or sponsorship, BBK is proud to have maintained decades of support for football, junior tennis, and equestrianism, among others. In 2016, sponsorships included supporting Bahrain's Pro-cycling team, which participates in international cycling tours. By promoting such sports, BBK encourages people to become more active, inspires the young, and promotes physical wellbeing.

Customers with special needs

The Bank has always prioritised integration and support for this segment of the community. As well as allocating more than 15 percent of the total donation budget to special needs societies and associations, BBK continues to invest in better accessibility to the Bank's facilities for those with special needs. After being the first to introduce ATMs for the visually impaired, and other special services such as sign language experts, the Bank has focused on constantly enhancing the experience of special needs customers, enabling them to conduct their banking transactions independently.

The Budaiya Financial Mall is a typical example. 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.

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

Culture

The Bank supports the Bahrain Authority for Culture and Antiquities and the Sheikh Ebrahim Bin Mohammed Al-Khalifa Centre for Culture and Research, and contributes to various initiatives for cultural preservation and the restoration of historical facilities. In 2016, BBK again co-sponsored the Spring of Culture, an annual festival that boosts the cultural and intellectual movement and attracts many visitors to Bahrain.

Other philanthropic support

BBK has renewed its support to the Ministry of Social Development NGO Fund, which provides grants to a range of societies and charitable organisations for development initiatives, donating BD 30,000 during 2016. A further BD 65,000 was donated to care homes for the elderly, as well as to organisations that benefit orphans.

Environmental initiatives

BBK continuously refines its digital services to reduce its environmental impact. The Bank follows energy-saving practices and recycles waste paper to reduce its carbon footprint and contribute to environmental sustainability. It also supports the Supreme Council for Environment every year in its conservation work with Al Areen Wildlife Park.

Backing Bahrain's financial sector

Being designated as a Domestic Systemically Important Bank (D-SIB) means that BBK fulfils a major role in the development of Bahrain's economy and financial sector. On the world stage, the Bank acts as a global ambassador for Bahrain. Once again, BBK co-sponsored the annual reception for Bahraini banks at the 2016 International Monetary Fund and World Bank meetings in Washington.

The Bank was also a lead sponsor of Euromoney's fifth annual GCC Financial Forum, hosted by the Bahrain Economic Development Board. The 2016 conference attracted more than 500 business leaders and policymakers from 24 countries.

BBK continues to sponsor the region's first educational dealing room, established by the Bahrain Institute of Banking and Finance to help young Bahrainis learn about banking and investment. It also sponsors the Bahrain Bourse's TradeQuest competition – a stock trading simulation programme for high school students – by providing monetary assistance and delegating a portfolio manager to advise the participating teams.

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 2016

BBK implemented initiatives to enhance corporate governance practices at the Bank, including amending the organisational structure so that the Risk Management function reports directly to the Risk Committee of the Board, and the Compliance and AML function reports directly to the Audit Committee of the Board. Also reviewing all Bank policies, especially risk management policies. The evaluation process for the Board, its committees and Board members was successfully completed during the year and was concluded with recommendations for improvement. Furthermore, the Bank continued to publish enhanced disclosures in the annual report in line with best corporate governance practices and regulatory requirements. The Board reviewed the Board charter and Board Committees' Terms of Reference.

A full training schedule was approved by the Board for the year 2016, and the attendance of Board members was monitored.

The Bank fully implemented the new international accounting standards IFRS9 in 2016, and was one of the first banks in the region to do so.

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) was held on 28 March 2016 and the Extraordinary General Meeting (EGM) was held on 28 January 2016.

The EGM resolved to approve increasing the Bank's capital through offering 100 million Bahraini Dinars worth of perpetual convertible capital securities to existing shareholders, on a rights privileged subscription basis, to meet the higher regulatory capital requirements under Basel III and to fund the Bank's future strategic initiatives. The offering was well received and the participation rate was 86.1 percent. Distribution payment amounts shall be payable, subject to the terms and conditions, on the outstanding nominal amount of the capital securities semi-annually on 2 May and 2 November each year, and the first distribution was paid on 2 November 2016. The minutes of the AGM and the 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 2014 and ends in March 2017.

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.

Corporate Secretary

The Board is supported by the Corporate Secretary, who provides professional and administrative support to the General Assembly, the Board, its Committees and members. The Corporate Secretary also assumes the responsibilities of the 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. The appointment of the Corporate Secretary is subject to the approval of the Board.

BBK's 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, and he has since attended many advance training programmes in corporate governance both in Bahrain and abroad, accumulating over 20 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.

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

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	–	–	–

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 will affect the Bank's business operations. Immediately after appointment, the Bank will provide a formal induction.

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 2016

Programmes	Date	Duration
The Euromoney GCC Financial Forum	23-24 February 2016	9 hours
Corporate Governance – from a strategic point of view	19 April 2016	5 hours
Future of payments	27 December 2016	2 hours 30 minutes
IFRS9 overview	25 and 27 December 2016	5 hours

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
Chairman of the Board of Trustees	Human Resources Development Fund in Banking Sector	Kingdom of Bahrain
Member	Council of Vocational Training in Banking Sector	Kingdom of Bahrain
Chairman of the Board	AlJanabya 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	Qatar-Bahrain 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

Jassem Hasan Ali Zainal		
Acting 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	Automated System Company	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		
CEO	Social Insurance Organization (SIO)	Kingdom of Bahrain
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	Bahrain Financing Company (BFC) Group	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

Directors' external appointments (continued)

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
Board Member	Gatehouse Bank PLC	United Kingdom

Mutlaq Mubarak Al Sanei		
General Manager	Kuwait Authority for Partnership Projects	State of Kuwait
Chairman	Health Assurance Hospitals Company	State of Kuwait

Elham Ebrahim Hasan		
Managing Partner	Elham Hasan SPC	Kingdom of Bahrain
Chairman	Taaheal Healthcare	Kingdom of Bahrain
Board Member	BNP Paribas Investment Company	Kingdom of Saudi Arabia
Board Member	Solidarity Group Holding BSC	Kingdom of Bahrain
Board Member	Mumtalakat	Kingdom of Bahrain
Board Member	Edamah	Kingdom of Bahrain

Yusuf Saleh Khalaf		
Managing Director	Vision Line Consulting WLL	Kingdom of Bahrain
Board Member	Eskan Bank	Kingdom of Bahrain
Board Member	SICO Investment Bank	Kingdom of Bahrain

Hassan Mohammed Mahmood		
Board Member	Faisal Finance (Maroc) SA	Morocco
Board Member	Overland Capital Group Inc	United States of America
Board Member	Egyptian Investment Company	Egypt
Board Member	Islamic Investment Company of Gulf (Bahamas) Limited – (Until 31st March 2016)	Bahamas
Board Member	Gulf Financing Investment Company	Egypt
Board Member	Egyptian Company for Business Trade	Egypt
Board Member	Ithraa Capital	Kingdom of Saudi Arabia

Directors' and related parties' interests

The number of securities held by Directors as of 31 December 2016 was as follows:

Name of Director	Type of shares	31 Dec 2016	31 Dec 2015	Bonds 31 Dec 2016	Bonds 31 Dec 2015
Murad Ali Murad	Ordinary	853,977	853,977	197,778	–
Aref Saleh Khamis	Ordinary	–	–	–	–
Mohamed Abdulrahman Hussain	Ordinary	153,402	133,402	–	–
Jassem Hasan Ali Zainal	Ordinary	190,286	190,286	30,000	–
GOSI/Dr Zakareya Sultan Al Abbasi (1)	Ordinary	127,050	127,050	11,746	–
Sh Abdulla bin Khalifa bin Salman Al Khalifa	Ordinary	127,050	127,050	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	–
Ithmaar Bank/Elham Ebrahim Hasan (3)	Ordinary	127,050	127,050	11,746	–
Yusuf Saleh Khalaf	Ordinary	152,050	127,050	39,057	–
Ithmaar Bank/Hassan Mohammed Mahmood (3)	Ordinary	127,050	127,050	11,746	–
Hassan Mohammed Mahmood	Ordinary	73,525	63,525	30,000	–

(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 owns 987,825 shares, 91,326 bonds and is related to the Chairman of the Board.

Nature and extent of transactions with related parties during 2016

On April 2016, Al Janabeya Company WLL (a family company owned by Mr Murad Ali and his family) purchased a total of 91,326 bonds.

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%			

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

Directors' trading of BBK shares during 2016

Name of Director	Trading through Bahrain Bourse	Date of trading
Murad Ali Murad	Purchased 197,778 bonds	April 2016
Mohamed Abdulrahman Hussain	Purchased 20,000 shares	28 January 2016
Jassem Hasan Ali Zainal	Purchased 30,000 bonds	April 2016
GOSI/Dr Zakareya Sultan Al Abbasi	Purchased 11,746 bonds	April 2016
Sh Abdulla bin Khalifa bin Salman Al Khalifa	Purchased 50,000 bonds	April 2016
Kuwait Investment Authority/Mutlaq Mubarak Al Sanei	Purchased 11,746 bonds	April 2016
Ithmaar Bank/ Elham Ebrahim Hasan	Purchased 11,746 bonds	April 2016
Yusuf Saleh Khalaf	Purchased 25,000 shares	20 March 2016
	Purchased 39,057 bonds	April 2016
Ithmaar Bank/ Hassan Mohammed Mahmood	Purchased 11,746 bonds	April 2016
Hassan Mohammed Mahmood	Purchased 10,000 shares	1 February 2016
	Purchased 30,000 bonds	April 2016

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 Corporate Secretary and shared with the Independent Directors.

Board meeting attendance

During 2016, 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 2016

Members	Quarterly meetings				Other meetings		
	8 Feb	18 Apr	18 Jul	24 Oct	7 Mar	28 Mar	26 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	⊙	⊙	○	⊙	⊙	○	⊙
Mutlaq Mubarak Al Sanei	⊙	○	⊙	⊙	⊙	⊙	⊙
Elham Ebrahim Hasan	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Yusuf Saleh Khalaf	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Hassan Mohammed Mahmood	⊙	⊙	⊙	⊙	⊙	⊙	⊙

Major issues discussed by the Board during 2016 (Subjects that fall under the Board Committee's scope are recommended by the respective Board Committee for Board's approval)

Date of the meeting	Subject
8 February 2016	1. AGM and EGM Invitation and Recommendation to distribute 2015 dividends 2. Perpetual Convertible Capital Instrument Issuance 3. Anti-Money Laundering annual report 2015 4. Financial Results for Fourth Quarter of 2015 5. Budget 2016 6. INR Hedging Options 7. Board Remuneration for the year 2015 8. Corporate Governance report to AGM 9. Succession Plan 10. Nominating candidates for Committees and subsidiary Boards 11. Amendments to the Organisational Structure for BBK 12. Appointment of a CE for Kuwait Branch 13. List of employees included under the Remuneration policy 14. Islamic Sharia Supervisory Board – SSB 15. Employee Performance Share Plan 16. Risk Policies for review
7 March 2016	1. KYC requirements from Board members 2. Amendments to the Organisational Structure for BBK 3. Amendments of NRCGC Terms of Reference 4. Invita Board Remuneration 5. Merit bonus of the Bank Executive Management and CEs of its wholly owned subsidiaries 6. Job objectives of the Chief Executive for 2016 7. BBK Perpetual Convertible Capital Instrument
28 March 2016	1. Board Chairmanship and Board Committees Composition 2. Board Evaluation for the year 2015 3. Board Evaluation Results from the year 2011 to 2015 4. Amendments to the Organisational Structure for BBK
18 April 2016	1. Review of the Bank's Corporate Governance Framework 2. Review of the Board Charter 3. Update on the strategic intiatives of the branch in Kuwait and of CrediMax 4. Review of the performance of the BBK Financial Malls 5. Financial Results for First Quarter of 2016 and reviewing the related press release 6. Investment Strategy 7. Liquidity Management Framework 8. Risk Management Strategy 9. Internal Capital Adequacy Assessment Process ICAAP for the year 10. Risk Policies for review – amendment

Date of the meeting	Subject
18 July 2016	1. Board Training Session options 2. Share-registrar agreement with Bahrain Bourse 3. Quarterly Liquidity Report 4. Half Yearly Investment Portfolio performance 5. Financial Results for Second Quarter of 2016 and reviewing the related press release 6. CBB Examination Report 2015 7. Update to AML policy and procedures – 2016 8. Revising the terms of reference of the Risk Committee, taking into consideration the changes in the organisation structure 9. Risk Policies for review
24 October 2016	1. Schedule of Meetings of the Board of Directors and its Committees 2017 2. Quarterly Liquidity Report 3. Financial Results for Third Quarter of 2016 and reviewing the related press release 4. Business Initiative Approval – Invita's TPA Initiative 5. Presentation and discussion of the legal structure for Qatar 6. Board Membership Criteria 7. Amendments to the Board Charter and Board Committees' Terms of Reference 8. Remuneration Policies Amendments – Kuwait Branch 9. Compensation Benchmarking Study 10. Risk Policies for review – amendment
26 December 2016	1. Matters related to the Board during 2017 2. Treasury Management Report – Buyback Treasury Shares 3. Budget 2017 4. Country Strategies – KSA, Oman, Turkey and Qatar 5. NPL Management Update 6. IFRS9 7. New risk policies and policy amendments as a result of implementing IFRS9 8. Compensation Benchmarking Study

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 2016.

The full text of the Terms of Reference for Board Committees (Executive Committee, Audit 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
Mohammed Abdulrahman Hussain Chairman **Aref Saleh Khamis** Deputy Chairman **Sh Abdulla bin Khalifa bin Salman Al Khalifa** Member **Mutlaq Mubarak Al Sanei** Member **Abdulkarim Ahmed Bucheery** Member until March 2016 **Elham Ebrahim Hasan** Member **Reyadh Yousif Safer** Member since March 2016	• Not less than 5 members are appointed for a 1-year term. • Minimum number of meetings required each year: 8 (actual meetings in 2016: 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 Committee

Members	Summary terms of reference, roles and responsibilities	Summary of responsibilities
Jassem Hasan Ali Zainal Chairman (Independent) **Yusuf Saleh Khalaf** Deputy Chairman (Independent) **Sh Khalifa bin Duaij Al Khalifa** Member (Independent) **Hassan Mohammed Mahmood** Member	• 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 2016: 5). • 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** Member (Independent) **Marwan Mohammed Al Saleh** Member	• 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 2016: 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
Murad Ali Murad Chairman (Independent) **Jassem Hasan Ali Zainal** Deputy Chairman (Independent) **Dr Zakareya Sultan Al Abbasi** Member **Yusuf Saleh Khalaf** Member (Independent)	• 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 2016: 5). • 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.

Board Committee meetings and record of attendance

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

Executive Committee meetings in 2016

Members	*17 Jan	7 Feb	*17 Feb	6 Mar	17 Apr	22 May	19 Jun	17 Jul	4 Sep	25 Sep	23 Oct	27 Nov	25 Dec
Mohamed Abdulrahman Hussain	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Aref Saleh Khamis	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Sh Abdulla bin Khalifa bin Salman Al Khalifa	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Mutlaq Mubarak Al Sanei	○	⊙	⊙	⊙	○	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Abdulkarim Ahmed Bucheery	⊙	⊙	⊙	⊙	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘	⊘
Elham Ebrahim Hasan	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙
Reyadh Yousif Sater	⊘	⊘	⊘	⊘	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙	⊙

* Unscheduled meetings

Audit Committee meetings in 2016

Members	7 Feb	17 Apr	17 Jul	23 Oct	*25 Dec
Jassem Hasan Ali Zainal	⊙	⊙	⊙	⊙	⊙
Sh Khalifa bin Duaij Al Khalifa	⊙	⊙	⊙	⊙	⊙
Yusuf Saleh Khalaf	⊙	⊙	⊙	⊙	⊙
Hassan Mohammed Mahmood	⊙	⊙	⊙	⊙	⊙

* Unscheduled meetings

Nomination, Remuneration and Corporate Governance Committee meetings in 2016

Members	8 Feb	6 Mar	24 Oct	*26 Dec
Murad Ali Murad	⊙	⊙	⊙	⊙
Sh Khalifa bin Duaij Al Khalifa	⊙	⊙	⊙	⊙
Marwan Mohammed Al Saleh	⊙	⊙	⊙	⊙

* Unscheduled meetings

Risk Committee meetings in 2016

Members	17 Jan	10 Apr	13 Jul	16 Oct	*25 Dec
Murad Ali Murad	⊙	⊙	⊙	⊙	⊙
Yusuf Saleh Khalaf	⊙	⊙	⊙	⊙	⊙
Dr Zakareya Sultan AlAbbasi	⊙	⊙	⊙	⊙	⊙
Jassem Hasan Ali Zainal	⊙	⊙	⊙	⊙	⊙

* Unscheduled meetings

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. During 2016, the system was rolled over to some concerned divisions as part of the systems's 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/procedure is updated annually and was last approved by the Board of Directors and Chief Executive in July 2016.

The Bank has deployed a risk-based automated transaction monitoring system in keeping with the anti-money laundering regulations of the CBB.

The Bank's anti-money laundering measures are regularly audited by the internal auditors, who report to the Audit 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
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

The aggregate remuneration paid to NRCG members during the year in the form of sitting fees amounted to BHD 7,000 [2015: BHD 5,500].

External consultancy

A consultant was appointed during the year to undertake a remuneration benchmarking study of BBK's Variable Remuneration and provide recommendations regarding compensation and pay practices to ensure alignment with local and regional markets.

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. 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. There are two forms of employee long-term incentive plans: 1 Employee Stock Options Plan This plan was introduced in 1999 and options were granted yearly until 2009. The plan ended on 31 December 2016. 2 Employee Performance Shares Plan 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 Grade 24 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

	2016	2015
Sitting fees and travel allowance	78,303	77,550
Remuneration	577,500	577,500
Others	19,510	32,992
BBK subsidiaries' Board remuneration, sitting fees and other related expenses	147,204	198,643

(b) Board of Directors of wholly owned subsidiaries

	2016	2015
Sitting fees and travel allowance	10,700	13,300
Remuneration	93,300	138,648
Others	–	9,155
Total	104,000	161,103

(c) Employees

1 Employee remuneration

BD 000's	2016									
		Fixed remuneration	Sign on bonuses	Guaranteed 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	–	–	947	12	172	882	–	4,550
Approved Persons Control & support	8	1,109	–	–	420	78	–	324	–	1,931
Other material risk-takers	34	2,997	–	–	566	93	12	437	–	4,104
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	–	–	5,041	183	183	1,644	–	32,800

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.

BD 000's	2015									
		Fixed remuneration	Sign on bonuses	Guaranteed bonuses	Variable remuneration					
					Upfront		Deferred			
	Number of staff	Cash	(Cash/shares)	(Cash/shares)	Cash	Shares	Cash	Shares	Others	Total
Approved Persons Business lines	16	2,820	–	–	1,039	27	193	1,069	–	5,148
Approved Persons Control & support	11	1,442	–	–	460	72	10	357	–	2,342
Other material risk-takers	29	2,562	–	–	519	96	10	433	–	3,620
Other Staff Bahrain Operations	567	12,023	–	–	1,769	_	_	_	–	13,791
Other Staff Branches & Subsidiaries	398	5,868	–	–	699	_	_	_	–	6,567
Total	1,021	24,715	–	–	4,486	195	213	1,860	–	31,469

The net impact of other indirect staff costs amounting to BD 122,208 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 248,796 have been included in the table above.

The total amount of remuneration includes severance payments during the year amounting to BD 387,120, of which the highest paid to a single person amounted to BD 324,000.

2 Deferred awards

	2016			
	Cash	Shares		Total BD '000
	BD '000	Number	BD '000	
Opening balance	443	15,221,598	5,695	6,138
Awarded during the period*	183	4,567,409	1,827	2,010
Paid out/released during the period	(77)	(3,415,223)	(1,413)	(1,490)
Service, performance and risk adjustments	–	–	–	–
Bonus share adjustment	–	–	–	–
Closing balance	549	16,373,784	6,109	6,659

* The number of shares for the 2016 Deferred Awards has been calculated using the year-end closing share price at 0.400 fils per share, as the award price will be determined 14 days after the AGM.

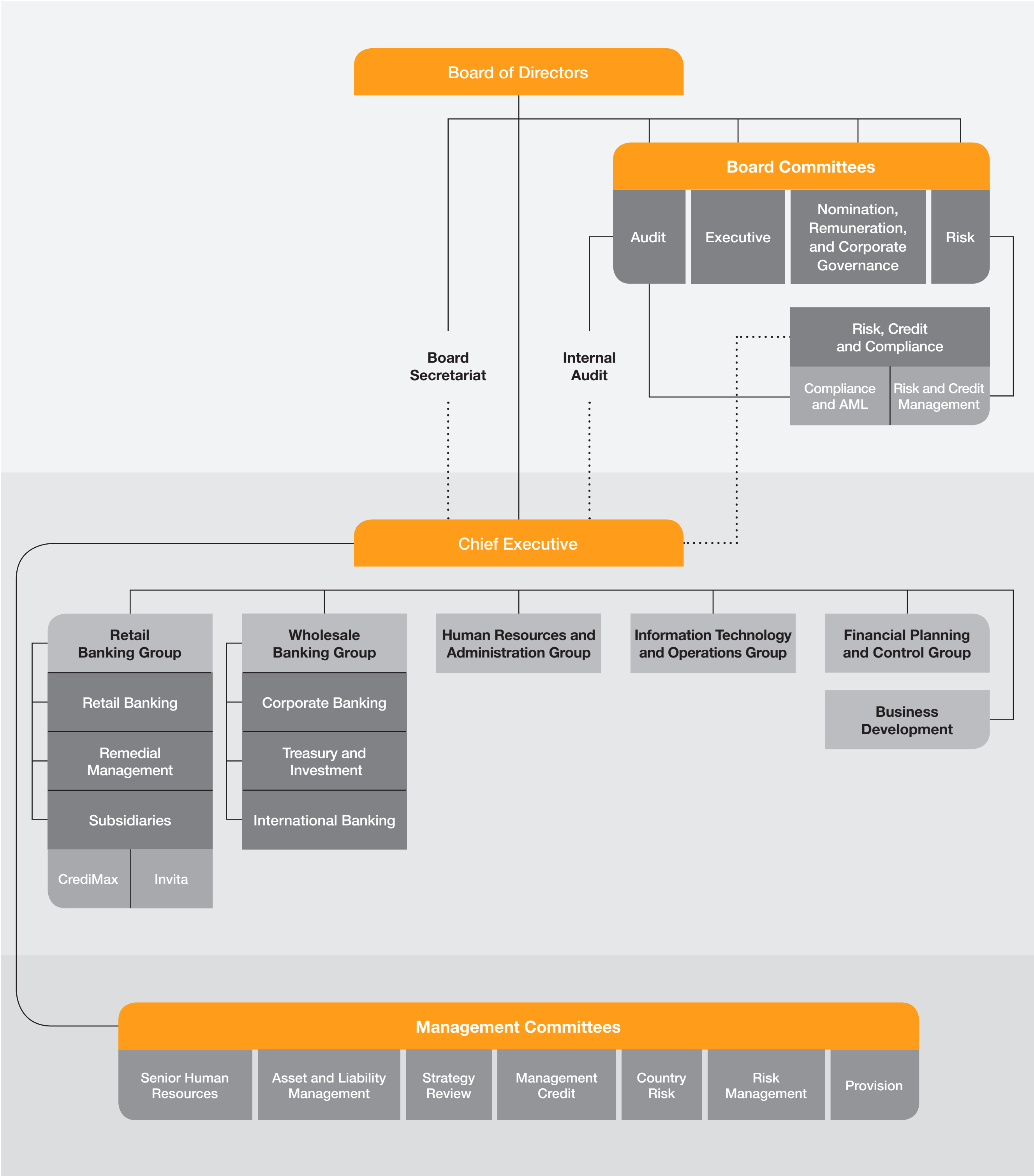
	2015			
	Cash	Shares		Total
	BD '000	Number	BD '000	BD '000
Opening balance	230	10,178,027	4,293	4,523
Awarded during the period**	213	6,605,344	2,061	2,274
Paid out/released during the period		(1,777,770)	(746)	(746)
Service, performance and risk adjustments	–	–	–	–
Bonus share adjustment	–	215,997	88	88
Closing balance	443	15,221,598	5,695	6,138

** The number of shares for the 2015 Deferred Awards have been recomputed based on the share price 14 days after the AGM of the Bank at 0.312 fils per share, and updated for the actual awards distributed to staff during 2015.

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 structure



The new structure has been effective since December 28, 2016.

Executive management interests

The number of shares and bonds held by members of the Executive Management team as of 31 December 2016 was as follows:

				Bonds	
Name	Type of shares	31 Dec 2016	31 Dec 2015	31 Dec 2016	31 Dec 2015
Reyadh Yousif Sater	Ordinary	722,435	421,608	300,000	–
Abdulrahman Ali Saif	Ordinary	234,878	68,103	90,000	–
Mohammed Ali Malik	Ordinary	216,406	79,179	–	–
Jamal Mohamed Al Sabbagh	Ordinary	265,350	156,476	–	–
Hassaan Mohammed Burshaid	Ordinary	294,397	133,943	–	–
Mohammed Abdulla Isa	Ordinary	339,247	180,435	30,000	–
Rashad Ahmed Akbari	Ordinary	181,130	106,796	–	–
C.K. Jaidev	Ordinary	–	–	–	–
Nadeem A. Aziz Kooheji	Ordinary	54,812	–	–	–
Amit Kumar	Ordinary	307,505	164,112	24,163	–
Neil Anthony Sharp	Ordinary	–	–	–	–

Executive Senior Management trading of the Bank's shares and bonds during 2016

Name	Trading through Bahrain Bourse	Date of trading
Reyadh Yousif Sater	Purchased 300,000 bonds	April 2016
Abdulrahman Ali Saif	Purchased 90,000 bonds	April 2016
Hassaan Mohammed Burshaid	Purchased 50,000 bonds	April 2016
	Sold 50,000 bonds	29 September 2016
Mohammed Abdulla Isa	Purchased 60,000 bonds	April 2016
	Sold 30,000 bonds	8 September 2016
C.K. Jaidev	Sold 48,087 shares	11 July 2016
Amit Kumar	Purchased 24,163 bonds	April 2016
Neil Anthony Sharp	Sold 80,902 shares	1 March 2016
	Sold 21,136 shares	11 July 2016

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.
Country Risk	Reviews country reports/ratings/strategies of the identified countries and presents recommendations for undertaking exposures to the Board for their approval.	Once every other month.
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 2016

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 2015 Previous	Number of shares 31 Dec 2016 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 2015 Previous	Number of shares 31 Dec 2016 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 2015 Previous	Number of shares 31 Dec 2016 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%	2,000,000	**1,000,000**
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 (2)	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 (3)	Kuwait	KSC	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**

(1) Shareholding through CrediMax.
(2) Due to closure of Capinnova Investment Bank on 30 September 2013.
(3) 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

Overview

Our strong financial performance is a result of our commitment to meeting our customers' evolving needs, focusing on our strategic priorities and prudent risk management practices, which enable us to deliver sustainable returns to shareholders.

The Bank continued its robust performance in 2016, achieving record profitability, in the face of strong economic headwinds, of BD 56.4 million for the year ended 31 December 2016, representing BD 3.2 million or 6.0 percent growth over 2015 results.

Key financial indicators remain healthy with Return on Average Assets at 1.5 percent and Return on Average Equity at 13.2 percent. Earnings per share decreased from 50.2 fils to 49.4 fils from the previous year, mainly because of the interim return of BD 3.6 million paid to the perpetual tier 1 capital securities shareholders. The Bank's liquidity position remains comfortable with liquid assets to total assets at 32.6 percent as at 2016 compared to 32.0 percent in 2015.

This section provides a review of our enterprise financial performance for 2016 that focuses on the consolidated operating results and the consolidated statement of financial position of BBK including its overseas branches, its principal subsidiaries, joint ventures, associated companies, and the indirect investment in associates through subsidiaries.

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

Operating results

The year 2016 was the first year 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 general weakness in economic trends regionally and globally, Net Profit, attributable to the owners of the Bank, for 2016 amounted to BD 56.4 million, up by 6.0 percent compared to the previous year. Total operating income for the year increased by BD 12.4 million or 10.2 percent and stood at BD 133.5 million, reflecting success in diversifying sources of income.

Continuing BBK's prudent approach to risk management and provisioning, the Bank has conservatively provided for adequate provisioning levels in 2016, opting to adapt the new 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

The increase in net profit was underpinned by an 18.1 percent rise in net interest income to BD 85.8 million for 2016 (2015: BD 72.7 million). The net interest income increase was achieved through prudent deployment of liquidity in high-quality investments and treasury bills, reporting an increase of 13.9 percent and 87.7 percent respectively.

As a result of a strong growth in total earning assets, the net interest yield ratio for 2016 showed an increase to 2.5 percent compared to 2.1 percent reported last year.

Other income

Other operating income consists of non-interest income, which is earned from business activities such as dealing in foreign currencies, investment in funds other than fixed-income funds, the sale of corporate banking and retail banking services, investment trading and share of profit / loss in associated companies and joint ventures.

Total other income recorded for the year of BD 42.2 million showed a decrease of 4.5 percent compared to the previous year's BD 44.2 million. Increased business volumes resulted in a growth in fees and commission for the year of 3.1 percent, and stood at BD 29.0 compared to BD 28.4 million reported in 2015. However, other income relating to foreign exchange, income from associated companies and joint ventures, and investment income declined to BD 16.0 million, which represents a decrease of 8.6 percent over last year (2015: BD 17.5 million).

Summary statement of profit or loss

BD millions	2016	2015	Variance BD millions	Change percent
Net interest income	**85.8**	72.7	13.1	18.08%
Other income	**47.7**	48.4	(0.7)	-1.56%
Total income	**133.5**	121.1	12.4	10.23%
Operating expenses	**53.1**	49.8	3.3	6.64%
Provisions	**22.6**	19.5	3.1	16.01%
Profit before taxation	**57.7**	51.8	5.9	11.49%
Taxation/non-controlling interest	**(1.3)**	1.4	(2.7)	-193.81%
Net profit	**56.4**	53.2	3.2	6.01%

Operating expenses

Due to the growth in business activities, the Bank's operating expenses increased to BD 53.1 million, a growth of 6.6 percent compared to last year (2015: BD 49.8 million). Staff costs showed an increase of 6.7 percent. Other operating expenses showed an increase of 6.5 percent and stood at BD 16.3 million compared to BD 15.3 million last year. Nevertheless, the Bank's prudent cost control policy and strong revenue-generating capability allowed it to improve its cost to income ratio to 39.8 percent (2015: 41.1 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. 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 values of the assets.

As a result of the migration to IFRS 9, net provisions reserve amounted to BD 22.6 million for 2016, 16.0 percent higher than the same period last year. While asset quality metrics deteriorated with gross non-performing loans ratio increasing to 6.0 percent and stood at BD 113.3 million as of 2016 (2015: BD 82.7 million), the Bank maintains a strong total provision coverage ratio of 112.0 percent (2015: 119.5 percent).

Comprehensive income

Comprehensive income stood at BD 67.3 million as of end of December 2016, compared to BD 20.1 million reported in the corresponding period of 2015. This was driven mainly from the significant improvement in the fair value of investment securities.

Financial position

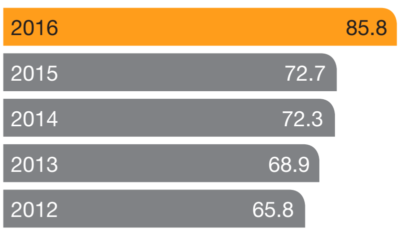
The Group maintained a strong and liquid balance sheet, achieving growth in the financial position by BD 56.1 million or 1.5 percent, and reached BD 3,702.6 million at the end of 2016. The growth was primarily driven by an increase in investments in associated companies and joint ventures, while the surplus liquidity was prudently utilised and invested in Bahraini government debt and other, mostly investment-grade, debt.

Growth across retail and corporate segments has been robust, with the Bank achieving a good balance between both loans and advances and deposits. We remain a strong net lender in the inter-bank market, particularly in the GCC and MENA region. As at 31 December 2016, our net loans and advances-to-deposits ratio stood at 70.9 percent (2015: 66.8 percent). This represents a moderate increase in commercial lending opportunities, but nevertheless remains a strong sign of the confidence customers have in us as a financial institution in the Kingdom of Bahrain, whilst growing and optimising the use of surplus liquidity in the market.

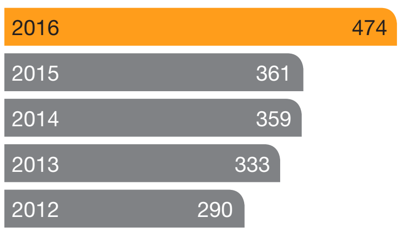
Our overall financial position remains healthy as the majority of our financial assets are loans and advances that are held on an amortised cost basis, which reduces the risk of short-term distress shocks.

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

Net interest income
BD millions



Total equity
BD millions



Assets

Total assets stood at BD 3,702.6 million as at 31 December 2016, an increase of 1.5 percent over BD 3,646.4 million recorded in the previous year. Loans and advances increased marginally during the year, by 0.1 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 turbulence. However, the excess in liquidity was deployed in high liquid assets consisting of cash and balances with central banks, treasury bills, and placement with banks and other financial institutions.

The investment portfolio of the Bank is classified into the following 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 2016, the quoted bonds and equities constitute 81.1 percent of the gross investments (2015: 85.1 percent). 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 taking into consideration the IFRS 9 classification impact has increased by BD 10.0 million or 1.3 percent and stood at BD 768.1 million at the end of 2016 mainly due to the increase 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.

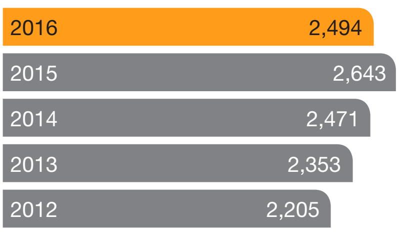
Liabilities

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 for the year ended 2016 stood at BD 2,493.7 million compared to BD 2,642.9 million in 2015. 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.

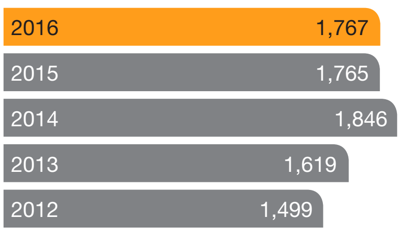
Borrowings under repurchase agreements and due to banks and financial institutions stood at BD 443.9 million compared to BD 353.9 million recorded at year-end 2015. Customer deposits continue to be the major source of funding, with customer deposits to total liabilities at 77.2 percent (December 2015: 80.4 percent).

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

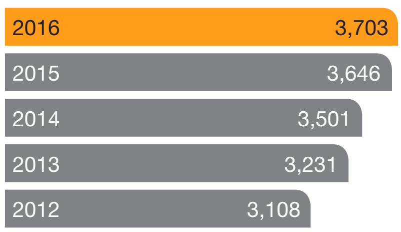
Customer deposits
BD millions



Loans and advances
BD millions



Total assets
BD millions



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 472.4 million at the end of 2016 (2015: BD 359.2 million). While there was a growth in risk weighted assets, the Bank continued to maintain a comfortable capital adequacy ratio of 18.5 percent (2015: 14.9 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 2016, which amounted to BD 86.1 million. The Group is keen to maintain a strong capitalisation in order to support future strategic plans.

Our impressive 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 will enable us to sustain the momentum we have built over the years and enhance value for shareholders.

Consolidated statement of financial position

BD millions	2016	2015	Variance BD millions	Change percent
Assets				
Cash and balances with central banks	**314.4**	286.7	27.7	9.63%
Treasury bills	**401.6**	394.1	7.5	1.91%
Deposits and amounts due from banks and other financial institutions	**318.4**	325.1	(6.7)	–2.06%
Loans and advances to customers	**1,767.1**	1,764.8	2.3	0.13%
Investment securities	**768.1**	758.1	10.0	1.32%
Investments in associated companies and joint ventures	**43.9**	35.8	8.1	22.61%
Interest receivable and other assets	**64.8**	57.0	7.8	13.69%
Premises and equipment	**24.2**	24.8	(0.6)	–2.51%
Total assets	**3,702.6**	3,646.4	56.2	1.54%
Liabilities and Equity				
Liabilities				
Deposits and amounts due to banks and other financial institutions	**259.9**	179.4	80.5	44.87%
Borrowings under repurchase agreement	**184.0**	174.5	9.5	5.45%
Term borrowings	**206.1**	204.7	1.4	0.70%
Customers' current, savings and other deposits	**2,493.7**	2,642.9	(149.2)	–5.64%
Interest payable and other liabilities	**84.6**	84.2	0.4	0.43%
Total liabilities	**3,228.3**	3,285.7	(57.4)	–1.75%
Attributable to the owners of the Bank	**472.4**	359.2	113.2	31.53%
Non-controlling interest	**1.8**	1.5	0.3	15.62%
Total equity	**474.2**	360.7	113.5	31.46%
Total liabilities and equity	**3,702.6**	3,646.4	56.2	1.54%

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 2016, 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 2016, 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 2016. 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
1. 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 2016, the Group's gross loans and advances amounted to BD 1,894 million and the related impairment provisions amounted to BD 126.9 million, comprising BD 49.3 million of provision against Stage 1 and 2 exposures and BD 77.6 million against exposures classified under Stage 3. 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; • For exposures determined to be individually impaired, 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 • For provision against exposures classified as Stage 1 and Stage 2 on early adoption of IFRS 9, we obtained an understanding of the Group's provisioning methodology, assessed the reasonableness of the underlying assumptions and the sufficiency of the data used by the management. Our procedures in this regard are discussed in further detail below under the key audit matter "Early adoption of IFRS 9".
2. Early adoption of IFRS 9	
The International Accounting Standards Board (IASB) issued *IFRS 9 – "Financial Instruments"* which replaces *"IAS 39 – Financial Instruments"* in three phases as follows: **Phase 1 –** classification and measurement of financial assets and financial liabilities; **Phase 2 –** Impairment methodology; and **Phase 3 –** Hedge accounting. Effective 1 January 2016, the Group has early adopted IFRS 9 ahead of its mandatory effective date of 1 January 2018. As permitted by IFRS 9, the requirements have been applied retrospectively without restating comparatives. Differences between previously reported carrying amounts and new carrying amounts of financial instruments as of 31 December 2015 and 1 January 2016 amounting to BD 11.9 million has been recognized in the opening retained earnings.	With respect to classification and measurement of financial assets and financial liabilities, our audit procedures comprised the following; • We read the Group's IFRS 9 based classification and measurement of financial assets and financial liabilities policy and compared it with the requirements of IFRS 9; • We obtained an understanding and checked the Group's business model assessment and the test on the contractual cash flows, which give rise to cash flows that are 'solely payments of principal and interest' [SPPI test] performed by the Group's consultant; and • We checked the appropriateness of the opening balance adjustments. With respect to impairment methodology, our audit procedures comprised the following; • We read the Group's IFRS 9 based impairment provisioning policy and compared it with the requirements of IFRS 9; • We obtained an understanding of the Group's internal rating models for loans and advances and read the rating validation report prepared by the Group's consultant to gain comfort that the discrimination and calibration of the rating model is appropriate. Further, we performed procedures to ensure the competence, objectivity and independence of the Group's consultant;

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

Key audit matters (continued)

Key audit matter	How the key audit matter was addressed in the audit
2. Early adoption of IFRS 9 (continued)	
The key changes arising from early adoption of IFRS 9 are that the Group's credit losses are now based on expected losses rather than an incurred loss model, and the change in the classification and measurement of the Group's financial assets and liabilities, which are detailed in note 3 to the consolidated financial statements. There were no significant changes arising from the early adoption of the hedge accounting requirements of IFRS 9.	• 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 the Group's staging; • We checked and understood the key data sources and assumptions for data used in the Expected Credit Loss (ECL) models (the Models) used by the Group to determine impairment provisions; • For forward looking assumptions used by the Group's management in its ECL calculations, we held discussions with management and corroborated the assumptions using publicly available information; • For a sample of exposures, we checked the appropriateness of determining Exposure at Default, including the consideration of prepayments and repayments in the cash flows and the resultant arithmetical calculations; • For Probability of Default (PD) used in the ECL calculations we checked the Through the Cycle (TTC) PDs calculation and checked the appropriateness of conversion of the TTC PDs to point in time (PIT) PDs; • We checked the calculation of the Loss Given Default (LGD) used by the Group in the ECL calculations, including the appropriateness of the use of collateral and the resultant arithmetical calculations; • We checked the completeness of loans and advances, off balance sheet items, investment securities, placements and other financial assets included in the ECL calculations as of 31 December 2016; We understood the theoretical soundness and tested the mathematical integrity of the Models; • For data from external sources, we understood the process of choosing such data, its relevance for the Group, and the controls and governance over such data; • Where relevant, we used Information System specialists to gain comfort on data integrity; • We checked consistency of various inputs and assumptions used by the Group's management to determine impairment provisions; and • We checked the appropriateness of the opening balance adjustments. With respect to hedge accounting, we read the Group's IFRS 9 based policy and compared it with the requirements of IFRS 9, further we have checked the appropriateness of the policy implementation. We assessed the financial statement disclosures arising on early adoption of IFRS 9 to determine if they were in accordance with the requirements of the Standard. Refer to the accounting policies, critical accounting estimates and judgements, disclosures of loans and advances and credit risk management in notes 3, 7 and 32 to the consolidated financial statements.

Other information included in the Group's 2016 annual report

Other information consists of the information included in the Group's 2016 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.

Auditors' 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 2016 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
27 February 2017
Manama, Kingdom of Bahrain

Consolidated statement of financial position

As at 31 December 2016

	Notes	2016 (1) BD '000	2015 BD '000
ASSETS			
Cash and balances with central banks	4	**314,368**	286,750
Treasury bills	5	**401,635**	394,090
Deposits and amounts due from banks and other financial institutions	6	**318,407**	325,096
Loans and advances to customers	7	**1,767,138**	1,764,799
Investment securities	8	**768,134**	758,107
Investments in associated companies and joint ventures	9	**43,923**	35,823
Interest receivable and other assets	10	**64,769**	56,970
Premises and equipment	11	**24,183**	24,806
TOTAL ASSETS		**3,702,557**	3,646,441
LIABILITIES AND EQUITY			
Liabilities			
Deposits and amounts due to banks and other financial institutions		**259,911**	179,404
Borrowings under repurchase agreement		**184,016**	174,508
Term borrowings	12	**206,109**	204,677
Customers' current, savings and other deposits	13	**2,493,715**	2,642,892
Interest payable and other liabilities	14	**84,591**	84,226
Total liabilities		**3,228,342**	3,285,707
Equity			
Share capital	15	**108,165**	108,165
Treasury stock	15	**(1,206)**	(4,728)
Perpetual tier 1 convertible capital securities	15	**86,098**	–
Share premium	15	**39,919**	39,919
Statutory reserve	16	**54,082**	54,082
General reserve	16	**54,082**	51,507
Cumulative changes in fair values	17	**(13,669)**	(12,304)
Foreign currency translation adjustments		**(11,558)**	(10,635)
Retained earnings		**122,830**	102,580
Proposed Appropriations	18	**33,666**	30,586
ATTRIBUTABLE TO THE OWNERS OF THE BANK		**472,409**	359,172
Non-controlling interest		**1,806**	1,562
Total equity		**474,215**	360,734
TOTAL LIABILITIES AND EQUITY		**3,702,557**	3,646,441

(1) 31 December 2016 results reflect the adoption of IFRS 9. Prior periods balances have not been restated. Refer to Note 3.3 – Accounting policies for further information.

Murad Ali Murad
Chairman

Aref Saleh Khamis
Deputy Chairman

Reyadh Yousif Sater
Chief Executive

The attached notes 1 to 44 form part of these consolidated financial statements

Consolidated statement of profit or loss

Year ended 31 December 2016

	Notes	2016 [1] BD '000	2015 BD '000
Interest and similar income	19	**128,556**	114,613
Interest and similar expense		**(42,708)**	(41,907)
Net interest income		**85,848**	72,706
Share of profit of associated companies and joint ventures	9	**5,467**	4,215
Other income	20	**42,212**	44,219
Total operating income		**133,527**	121,140
Staff costs		**33,453**	31,343
Other expenses		**16,263**	15,267
Depreciation	11	**3,430**	3,226
Net provision for impairment on loans and advances to customers	7	**23,753**	18,975
Net (write back)/provision for impairment on investments	8	**(1,115)**	538
Total operating expenses		**75,784**	69,349
PROFIT BEFORE TAXATION		**57,743**	51,791
Net tax (provision)/benefit		**(996)**	1,598
PROFIT FOR THE YEAR		**56,747**	53,389
Attributable to:			
Owners of the Bank		**56,410**	53,212
Non-controlling interest		**337**	177
		56,747	53,389
Basic earnings per share (BD)	21	**0.049**	0.050
Diluted earnings per share (BD)	21	**0.044**	0.050

(1) December 2016 results reflect the adoption of IFRS 9. Prior periods balances have not been restated. Refer to Note 3.3 – Accounting policies for further information.

Murad Ali Murad
Chairman

Aref Saleh Khamis
Deputy Chairman

Reyadh Yousif Sater
Chief Executive

The attached notes 1 to 44 form part of these consolidated financial statements

Consolidated statement of other comprehensive income

Year ended 31 December 2016

	Notes	2016 [1] BD '000	2015 BD '000
Profit for the year		**56,747**	53,389
Other comprehensive income			
Items that will not be reclassified to profit or loss			
Fair value through other comprehensive income reserve (equity instruments)	17	**4,113**	–
Items that are or may be reclassified subsequently to profit or loss			
Movement in translation reserve:			
Foreign currency translation adjustments		**(923)**	(3,376)
Movement in hedging reserve:			
Effective portion of changes in fair value	17	**174**	(304)
Net amount transferred to profit or loss			
Movement in fair value reserve (debt instruments – IFRS 9):			
Net change in fair value		**8,377**	–
Net amount transferred to profit or loss		**(887)**	–
Movement in fair value reserve (available-for-sale financial assets – IAS 39):			
Net change in fair value		**–**	(29,420)
Other comprehensive income (loss) for the year		**10,854**	(33,100)
Total comprehensive income for the year		**67,601**	20,289
Attributable to:			
Owners of the Bank		**67,264**	20,112
Non-controlling interest		**337**	177
		67,601	20,289

(1) December 2016 results reflect the adoption of IFRS 9. Prior periods have not been restated. Refer to Note 3.3 – Accounting policies for further information.

The attached notes 1 to 44 form part of these consolidated financial statements

Consolidated statement of changes in equity

Year ended 31 December 2016

		Attributable to the owners of the Bank and capital securities' holders												
	Note	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 [1] BD '000	Foreign currency translation adjustments BD '000	Retained earnings [1] BD '000	Proposed appropriations BD '000	Total [1] BD '000	Non-controlling interest BD '000	Total equity [1] BD '000
Balance at 1 January 2015		103,014	(6,951)	–	39,919	51,507	46,825	17,420	(7,259)	82,017	31,402	357,894	1,458	359,352
Profit for the year		–	–	–	–	–	–	–	–	53,212	–	53,212	177	53,389
Other comprehensive loss		–	–	–	–	–	–	(29,724)	(3,376)	–	–	(33,100)	–	(33,100)
Total comprehensive income		–	–	–	–	–	–	(29,724)	(3,376)	53,212	–	20,112	177	20,289
Share – based payments	40	–	–	–	–	–	–	–	–	269	–	269	–	269
Dividends paid	18	–	–	–	–	–	–	–	–	–	(20,179)	(20,179)	–	(20,179)
Stock dividends	18	5,151	–	–	–	–	–	–	–	–	(5,151)	–	–	–
Donations		–	–	–	–	–	–	–	–	–	(1,390)	(1,390)	–	(1,390)
Movement in treasury stock	15	–	2,223	–	–	–	–	–	–	–	–	2,223	–	2,223
Unclaimed dividends	15	–	–	–	–	–	–	–	–	243	–	243	–	243
Movement in non-controlling interest		–	–	–	–	–	–	–	–	–	–	–	(73)	(73)
Transfer to statutory reserve	16	–	–	–	–	2,575	–	–	–	(2,575)	–	–	–	–
Proposed appropriations	18	–	–	–	–	–	–	–	–	(30,586)	30,586	–	–	–
Transfer to general reserve 2014		–	–	–	–	–	4,682	–	–	–	(4,682)	–	–	–
Balance at 31 December 2015		108,165	(4,728)	–	39,919	54,082	51,507	(12,304)	(10,635)	102,580	30,586	359,172	1,562	360,734
Transition adjustment on adoption of IFRS 9 at 1 January 2016 (note 3.3)			–	–	–	–	–	(16,880)	–	4,980	–	(11,900)	–	(11,900)
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**

(1) December 2016 results reflect the adoption of IFRS 9. Prior periods have not been restated. Refer to Note 3.3 – Accounting policies for further information.

The attached notes 1 to 44 form part of these consolidated financial statements

Consolidated statement of cash flows

Year ended 31 December 2016

	Notes	2016 [1] BD '000	2015 BD '000
OPERATING ACTIVITIES			
Profit for the year before taxation		**57,743**	51,791
Adjustments for non-cash items:			
Net provisions (write back) relating to:			
Loans and advances to customers	7	**23,753**	18,975
Investment securities	8	**(1,115)**	538
Share of profit of associated companies and joint ventures	9	**(5,467)**	(4,215)
Depreciation	11	**3,430**	3,226
Realised gains on sale of investment securities	20	**(2,707)**	(4,408)
Accrual on term borrowings		**1,432**	1,439
		77,069	67,346
(Increase) decrease in operating assets			
Mandatory reserve deposits with central banks		**5,049**	(6,277)
Treasury bills maturing after 90 days		**(13,212)**	(100,790)
Deposits and amounts due from banks and other financial institutions		**(15,824)**	28,378
Loans and advances to customers		**(26,092)**	62,688
Interest receivable and other assets		**(7,625)**	1,725
Increase (decrease) in operating liabilities			
Deposits and amounts due to banks and other financial institutions		**80,507**	(133,620)
Borrowings under repurchase agreements		**9,508**	136,804
Customers' current, savings and other deposits		**(149,177)**	171,815
Interest payable and other liabilities		**365**	5,384
Income tax paid		**(935)**	(444)
Net cash (used in)/from operating activities		**(40,367)**	233,009
INVESTING ACTIVITIES			
Purchase of investment securities		**(247,605)**	(246,015)
Sale of investment securities		**240,940**	252,152
Sale/partial repayment of capital of investment in associated companies	9	**(4,492)**	3,000
Dividends received from associated companies	9	**2,103**	1,835
Other movements in investment in associated companies		**(238)**	9
Movement in non-controlling interest		**–**	(73)
Purchase of premises and equipment		**(2,807)**	(3,018)
Net cash (used in)/from investing activities		**(12,099)**	7,890
FINANCING ACTIVITIES			
Payment of dividend and donations	18	**(28,011)**	(21,569)
Term borrowings		**–**	(37,700)
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		**(3,552)**	–
Movement in treasury stock		**3,522**	2,223
Net cash from/(used in) financing activities		**57,877**	(57,046)
Foreign currency translation adjustments		**(923)**	(3,376)
NET CHANGE IN CASH AND CASH EQUIVALENTS		**4,488**	180,477
Cash and cash equivalents at beginning of the year		**533,116**	352,639
CASH AND CASH EQUIVALENTS AT END OF THE YEAR	23	**537,604**	533,116

(1) December 2016 results reflect the adoption of IFRS 9. Prior periods have not been restated. Refer to Note 3.3 – Accounting policies for further information.

The attached notes 1 to 44 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 27 February 2017.

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. **As explained in Note 3.3 the Group has early adopted IFRS 9 Financial Instruments issued in July 2014 with a date of initial application of 1 January 2016.**

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% (2015: 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% (2015: 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 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.

3.2 New Standards and Interpretations issued and effective
The Group has adopted the following new and amended International Accounting Standards/International Financial Reporting Standards as of 1 January 2016:

- Amendments to IFRS 11 Joint Arrangements: Accounting for Acquisitions of Interests;
- Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation; and
- Amendments to IAS 27: Equity Method in Separate Financial Statements.

The above amendments to IFRSs which are effective for annual accounting periods starting from 1 January 2016 did not have any material impact on the accounting policies, financial position or performance of the Group.

3.3 Early Adoption of IFRS 9
The Group has early adopted IFRS 9 Financial Instruments issued in July 2014 with a date of initial application of 1 January 2016. The requirements of IFRS 9 represent a significant change from IAS 39 Financial Instruments: Recognition and Measurement. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

The key changes to the Group's accounting policies resulting from its adoption of IFRS 9 are summarised below.

Classification of financial assets and financial liabilities
IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

Under IFRS 9,derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification. For an explanation of how the Group classifies financial assets under IFRS 9, Refer to Note 3.4 Summary of significant accounting policies – Financial assets and financial liabilities ii) classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in profit or loss, under IFRS 9 fair value changes are generally presented as follows:

Financial liabilities previously measured at amortised cost under IAS 39 have been classified and measured under IFRS 9 at amortised cost using the effective interest rate method. There have been no changes in the classification and measurement of financial liabilities on the adoption of IFRS 9.

- The amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- The remaining amount of change in the fair value is presented in profit or loss.

For an explanation of how the Group classifies financial liabilities under IFRS 9. Refer to Note 3.4 Summary of significant accounting policies – Financial assets and financial liabilities ii) classification.

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. Under IFRS 9, credit losses are recognised earlier than under IAS 39.

Key changes in the Group's accounting policy for impairment of financial assets are listed below:
The Group applies three-stage approach to measuring expected credit losses (ECL) on financial assets carried at amortised cost and debt instruments classified as FVOCI. Assets migrate through the following three stages based on the change in credit quality since initial recognition.

Stage 1: 12 months ECL
For exposures where there has not been a significant increase in credit risk since initial recognition, the portion of the lifetime ECL associated with the probability of default events occurring within next 12 months is recognised.

Stage 2: Lifetime ECL – not credit impaired
For credit exposures where there has been a significant increase in credit risk since initial recognition but that are not credit impaired, a lifetime ECL is recognised.

Stage 3: Lifetime ECL – credit impaired
Financial assets are assessed as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that asset have occurred. As this uses the same criteria as under IAS 39, the groups methodology for specific provisions remains largely unchanged.

For an explanation of how the Group applies the impairment requirements of IFRS 9. Refer to note 3.4 summary of significant accounting policies – Financial assets and financial liabilities – vii) Impairment.

Hedge accounting
The general hedge accounting requirements of IFRS 9 retain the three types of hedge accounting mechanisms in IAS 39. However, greater flexibility has been introduced to the types of transactions eligible for hedge accounting, specifically broadening the types of instruments that qualify as hedging instruments and the types of risk components of non-financial items that are eligible for hedge accounting. In addition, the effectiveness test has been overhauled and replaced with the principle of an 'economic relationship'. Retrospective assessment of hedge effectiveness is no longer required.

Transition
Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

(a) Comparative periods have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2016. Accordingly, the information presented for 2015 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2015 under IFRS 9.

(b) The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

- The determination of the business model within which a financial asset is held.
- The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
- The designation of certain investments in equity instruments not held for trading as at FVOCI.
- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Group has assumed that credit risk on the asset had not increased significantly since its initial recognition.

Impact of Adopting IFRS 9

The impact of this change in accounting policy as at 1st January 2016 has been to increase retained earnings by BD 4,980 million, and to decrease the fair value reserve by BD 16,880 million as follows:

	Retained earnings BD '000	Fair value reserve BD '000
Closing balance under IAS 39 (31 December 2015)	102,580	(12,304)
Impact on reclassification and remeasurments:		
Investment securities (debt) from available-for-sale to amortised cost	–	4,988
Investment securities (debt and equity) from available-for-sale to FVTPL	4,853	(4,853)
Investment securities (equity) from available-for-sale to FVOCI	17,381	(17,015)
	124,814	(29,184)
Impact on recognition of Expected Credit Losses:		
Expected credit losses under IFRS 9 for debt financial assets at FVOCI	(366)	–
Expected credit losses under IFRS 9 for financial assets at amortised cost	(16,888)	–
(including loan commitments and financial guarantee contracts)		
	(17,254)	–
Opening balance under IFRS 9 on date of initial application of 1 January 2016	107,560	(29,184)

Classification of financial assets and financial liabilities on the date of initial application of IFRS 9

The following table is reconciliation of original measurement categories and carrying value in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Group's financial assets and financial liabilities as at 1 January 2016.

	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount under IAS 39 BD '000	New carrying amount under IFRS 9 BD '000
Financial assets				
Cash and balances with central banks	Loans and receivables	Amortised cost	286,750	286,750
Loans and advances to customers	Loans and receivables	Amortised cost	1,764,799	1,747,926
Investment securities – debt	Held-to-maturity investments	Amortised cost	475,498	475,493
Investment securities – debt	Held-to-maturity investments	FVOCI	9,223	9,223
Investment securities – debt	Available-for-sale	Amortised cost	31,376	34,878
Investment securities – debt	Available-for-sale	FVOCI	537,293	537,293
Investment securities – debt	Available-for-sale	FVTPL	3,710	3,710
Investment securities – equity	Available-for-sale	FVTPL	23,268	23,268
Investment securities – equity	Available-for-sale	FVOCI	71,829	71,829
Deposits and amounts due from banks and other financial institutions	Loans and receivables	Amortised cost	325,096	325,086
Interest receivable and other assets	Loans and receivables	Amortised cost	56,970	58,456
Total financial assets			3,585,812	3,573,912
Financial liabilities				
Deposits and amounts due to banks and other financial institutions	Amortised cost	Amortised cost	179,404	179,404
Borrowings under repurchase agreement	Amortised cost	Amortised cost	174,508	174,508
Term borrowings	Amortised cost	Amortised cost	204,677	204,677
Customers' current, savings and other deposits	Amortised cost	Amortised cost	2,642,892	2,642,892
Interest payable and other liabilities	Amortised cost	Amortised cost	84,226	84,226
Total financial liabilities			3,285,707	3,285,707

3 ACCOUNTING POLICIES (continued)

3.3 Early Adoption of IFRS 9 (continued)

Classification of financial assets and financial liabilities on the date of initial application of IFRS 9 (continued)

The Group's accounting policies on the classification of financial instruments under IFRS 9 are set out in Note 3.4. The application of these policies resulted in the reclassifications set out in the table above and explained below.

(a) Before the adoption of IFRS 9, certain Debt securities were reclassified out of the available-for-sale categories to Held-to-maturity. On the adoption of IFRS 9, the carrying amount of those assets was adjusted so that their amortised cost under IFRS 9 was as if those assets were accounted for at amortised cost from their inception.

(b) Under IFRS 9, certain managed funds which do not meet the FVOCI criteria and debt securities where the contractual cash flows of these securities are not solely payments of principal and interest on the principal outstanding have been re-classified to FVTPL. Further, certain equity investment securities which are not strategic in nature has been re-classified from Available-for-sale (AFS) to FVTPL on adoption of IFRS 9.

(c) Certain debt securities are held by the Bank Treasury in a separate portfolio for long-term yield and for liquidity purposes. These securities may be sold, but such sales are not expected to be more than infrequent. The Bank considers that these securities are held within a business model whose objective is both to held to collect the contractual cash flows and sale. These assets are classified as measured at Fair value through other comprehensive income under IFRS 9.

The following table shows the effects of the reclassification of financial assets from IAS 39 categories into the amortised cost category under IFRS 9.

From available-for-sale financial assets under IAS 39	2016 BD '000
Fair value at 31 December 2016	**32,640**
Fair value movement that would have been recognised during 2016 in OCI if the financial assets had not been reclassified	**(2,136)**

Impairment allowances:

The following table reconciles the closing impairment allowance for financial assets in accordance with IAS 39 as at 31 December 2015 to the opening ECL allowance determined in accordance with IFRS 9 as at 1 January 2016.

	31 December 2015 BD '000	Remeasurement BD '000	1 January 2016 BD '000
Loans and receivables and held to maturity securities under IAS 39/financial assets at amortised cost under IFRS 9 (includes cash and cash equivalents, loans and advances to banks and loans and advances to customers)	98,840	16,883	115,723
Available-for-sale debt investment securities under IAS 39 reclassified to amortised cost under IFRS 9	–	5	5
Available-for-sale debt investment securities under IAS 39/debt financial assets at FVOCI under IFRS 9	22,982	366	23,348
Total	121,822	17,254	139,076

Classification of financial assets and financial liabilities

The following table provides a reconciliation between line items in the statement of financial position and categories of financial instruments

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

31 December 2015	Held-to-maturity BD '000	Loans and receivables BD '000	Available for-sale BD '000	Amortised cost/ others BD '000	Total BD '000
Cash and balances with central banks	–	286,750	–	–	286,750
Treasury Bills	394,090	–	–	–	394,090
Deposits and amounts due from banks and other financial institutions	–	325,096	–	–	325,096
Loans and advances to customers	–	1,764,799	–	–	1,764,799
Investment securities	90,633	–	667,474	–	758,107
Investments in associated companies and joint ventures	–	–	–	35,823	35,823
Interest receivable and other assets	–	–	–	56,970	56,970
Premises and equipment	–	–	–	24,806	24,806
Total assets	484,723	2,376,645	667,474	117,599	3,646,441
Deposits and amounts due to banks and other financial institutions	–	–	–	179,404	179,404
Borrowings under repurchase agreement	–	–	–	174,508	174,508
Term borrowings	–	–	–	204,677	204,677
Customers' current, savings and					
other deposits	–	–	–	2,642,892	2,642,892
Interest payable and other liabilities	–	–	–	84,226	84,226
Total liabilities	–	–	–	3,285,707	3,285,707

3.4 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 – Policy applicable from 1 January 2016

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.

3 ACCOUNTING POLICIES (continued)

3.4 Summary of significant accounting policies (continued)

ii. Classification (continued)

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

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 assets – applicable up to 31 December 2015

All financial assets are initially recognised at the fair value of consideration given, including acquisition costs associated with the investment, except in case of trading investments, where the acquisition costs are expensed in the consolidated statement of profit or loss.

For purposes of subsequent measurement financial assets are classified in four categories:

- Financial assets at fair value through profit or loss
- Loans and receivables
- Held-to-maturity investments
- Available-for-sale financial investments

The Group classifies investments as trading if they are acquired primarily for the purpose of making a short term profit.

The Group classifies debt instruments as carried at amortised cost if the debt instruments are not quoted in an active market.

The Group classifies investments which it intends and has the ability to hold to maturity as held-to-maturity.

The Group classifies financial instruments which contain embedded derivatives which cannot be separated from the host instrument as carried at fair value through statement of profit or loss.

All other investments are classified as available-for-sale.

Judgements are made in the classification of available-for-sale, held for- 'trading and held-to-maturity investments based on management's 'intention at acquisition of the financial asset.

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.

From 1 January 2016 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability.

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.

Trading investments – applicable up to 31 December 2015

Trading investments are measured at fair value with any gain or loss arising from a change in fair value being included in the consolidated statement of profit or loss in the period in which it arises. Interest earned or dividends received are included in net trading income.

Financial assets designation at fair value through profit or loss – Applicable from 1 January 2016

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

Financial assets designated at fair value through statement of profit or loss – applicable up to 31 December 2015

Financial assets classified in this category are designated by management on initial recognition when the following criteria are met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis; or
- the assets are part of a group of financial assets which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- the financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows, that would not be separately recorded.

Financial assets at fair value through statement of profit or loss are recorded in the consolidated statement of financial position at fair value. Changes in fair value are recorded in 'net gain or loss on financial assets designated at fair value through statement of profit or loss. Interest earned is accrued in interest income, while dividend income is recorded in other income. The Group has not designated any financial assets at fair value through profit or loss.

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 – Applicable from January 2016

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 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.

Investment securities – Applicable upto 31 December 2015

These include bonds, equities, managed funds and other investments. Investments in managed funds comprise investments in mutual funds, private equity, real estate and credit structured products.

These are classified as follows:

- Investments carried at amortised cost
- Available-for-sale

Investments carried at amortised cost

Debt instruments which could be classified as loans and advances and which have fixed or determinable payments but are not quoted in an active market are treated as investments and carried at amortised cost, adjusted for effective fair value hedges, less provision for impairment. Premiums and discounts on non-trading investments with fixed or determinable repayments are amortised, using the effective interest rate method, and taken to interest income.

Available-for-sale

All other investments are classified as "available-for-sale". After initial recognition, available-for-sale investments are subsequently measured at fair value, unless fair value cannot be reliably measured in which case they are measured at cost less impairment. Fair value changes which are not part of an effective hedging relationship, are reported as a separate component of equity as cumulative changes in fair value until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as "cumulative changes in fair value" within equity, is included in the consolidated statement of profit or loss for the year.

That portion of any fair value changes relating from an effective hedging relationship is recognised directly in the consolidated statement of profit or loss.

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

Policy applicable from 1 January 2016

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)

3.4 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
- 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: generally, 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 drawn 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.

Impairment and uncollectability of financial assets – applicable up to 31 December 2015

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

Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, the probability that they will enter bankruptcy or other financial reorganisation, default or delinquency in interest or principal payments and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

i. Financial assets carried at amortised cost

For financial assets carried at amortised cost (such as amounts due from banks, loans and advances to customers), the Group first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognised are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the consolidated statement of profit or loss. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of 'interest income'. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the Group.

If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to provision for impairment.

The present value of estimated future cash flows is discounted at the financial asset's original effective interest rate. The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Group's internal credit grading system, that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics such as asset type, industry, geographical location, collateral type, past due status and other relevant factors.

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

ii. Available-for-sale financial assets

For available-for-sale investments, the Group assesses at each statement of financial position date whether there is objective evidence that an investment is impaired.

In the case of debt instruments classified as available-for-sale, the Group assesses individually whether there is objective evidence of impairment based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss on the investment previously recognised in the consolidated statement of profit or loss. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of interest. If in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognised in the consolidated statement of profit or loss, the impairment loss is reversed through the consolidated statement of profit or loss.

In the case of equity investments classified as available-for-sale, objective evidence would also include a 'significant' or 'prolonged' decline in the fair value of the investment below its cost. Where there is evidence of impairment the cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the consolidated statement of income is removed from equity and recognised in the consolidated statement of profit or loss. Impairment losses on equity investments are not reversed through the consolidated statement of profit or loss. Increases in fair value after impairment are recognised directly in equity.

iii. 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.

Derecognition of financial assets and financial liabilities

Financial assets

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

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

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.

3 ACCOUNTING POLICIES (continued)

3.4 Summary of significant accounting policies (continued)

Investment in associated companies and joint ventures (continued)

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 shown on the face of 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.

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.

Hedge accounting – Policy applicable on 1 January 2016

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.
- 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.

Hedge accounting – Policy applicable up to 31 December 2015

At inception of the hedge relationship, the Group formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship.

A formal assessment is also undertaken to ensure the hedging instrument is expected to be highly effective in offsetting the designated risk in the hedged item. A hedge is regarded as highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80% to 125%. Hedges are formally assessed each quarter to reconfirm their effectiveness.

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 – Policy applicable from 1 January 2016

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.

Discontinuation of hedges – Policy applicable upto 31 December 2015

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. 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.

3 ACCOUNTING POLICIES (continued)

3.4 Summary of significant accounting policies (continued)

Recognition of income and expenses (continued)

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.

Trade date accounting and settlement date accounting

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.

3.5 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 – Policy applicable from 1 January 2016

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 – Policy applicable from 1 January 2016

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

	2016 BD '000	2015 BD '000
Cash	**20,853**	17,636
Current accounts and placements with central banks	**216,167**	186,716
Mandatory reserve deposits with central banks	**77,348**	82,398
	314,368	286,750

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 amortised cost, and Republic of India which are carried at FVOCI. The impairment allowance on the same is BD 0.228 thousand (1 January 2016 BD 0.148 thousand).

At 31 December 2016, treasury bills issued by Government of the Kingdom of Bahrain includes short term Islamic Sukuk amounting BD 48,527 thousand (2015: BD 28,138 thousand).

6 DEPOSITS AND AMOUNTS DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

	2016 BD '000	2015 BD '000
Deposits with banks and other financial institutions	**278,817**	264,359
Other amounts due from banks	**39,597**	60,737
Less: Allowance for impairment	**(7)**	–
	318,407	325,096

Allowance for impairment is on deposits with banks and other financial institutions in accordance with IFRS 9.

7 LOANS AND ADVANCES TO CUSTOMERS

	2016 BD '000	2015 BD '000
Loans and advances to customers at amortised cost		
Commercial loans and overdrafts	**1,429,210**	1,491,342
Consumer loans	**464,830**	372,297
	1,894,040	1,863,639
Less: Allowance for impairment	**(126,902)**	(98,840)
	1,767,138	1,764,799

Movements in allowance for impairment are as follows:

(i) Commercial loans and overdrafts

	2016				2015
	Stage 1: 12-month ECL	Stage 2: Lifetime ECL not credit-impaired	Stage 3: Lifetime ECL credit-impaired	Total ECL	Total
Balance at 1 January – on adoption of IFRS 9	**2,437**	**42,661**	**51,357**	**96,455**	73,770
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**	20,144
Recoveries/write-backs	**–**	**–**	**(5,499)**	**(5,499)**	(3,034)
Amounts written off during the year	**–**	**–**	**(9,414)**	**(9,414)**	(2,835)
Foreign exchange and other movements	**–**	**–**	**(1,408)**	**(1,408)**	(3,100)
Balance at end of year	**2,623**	**38,597**	**67,331**	**108,551**	84,945

(ii) Consumer loans

	2016				2015
	Stage 1: 12-month ECL	Stage 2: Lifetime ECL not credit-impaired	Stage 3: Lifetime ECL credit-impaired	Total ECL	Total
Balance at 1 January – on adoption of IFRS 9	**2,813**	**5,669**	**10,275**	**18,757**	12,983
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**	2,605
Recoveries/write-backs	**–**	**–**	**(1,132)**	**(1,132)**	(740)
Amounts written off during the year	**–**	**–**	**(1,222)**	**(1,222)**	(902)
Foreign exchange and other movements	**–**	**–**	**(19)**	**(19)**	(51)
Balance at end of year	**2,951**	**5,085**	**10,315**	**18,351**	13,895

At 31 December 2016, interest in suspense on past due loans that are fully impaired amounts to BD 21,572 thousand (31 December 2015: BD 17,680 thousand), effective 31 January 2014 the Bank has treated this 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 2016 amounts to BD 54,229 thousand (2015: BD 62,447 thousand).

At 31 December 2016, loans and advances includes Islamic financing facilities provided by the Group to corporates amounting BD 109,466 thousand (2015: BD 122,879 thousand). These mainly consists of Murabaha and Ijarah financing facilities.

8 INVESTMENT SECURITIES

	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 investments		(604)	(5)	(609)
Balance at 31 December 2016	10,486	634,575	123,073	768,134

	Available-for-sale BD '000	Carried at amortised cost BD '000	2015 Total BD '000
Quoted investments			
Government bonds	355,829	1,976	357,805
Other bonds	216,447	–	216,447
Equities	71,249	–	71,249
	643,525	1,976	645,501
Unquoted investments			
Government bonds	–	81,133	81,133
Other bonds	23,206	7,524	30,730
Equities	41,210	–	41,210
Managed funds	2,598	–	2,598
	67,014	88,657	155,671
	710,539	90,633	801,172
Allowance for impairment	(43,065)	–	(43,065)
Balance at 31 December 2015	667,474	90,633	758,107

At 31 December 2016, investment securities includes long term Islamic Sukuk amounting to BD 76,659 thousand (2015: BD 60,792 thousand).

Equity investment securities designated as at FVOCI

At 1 January 2016, the Group designated certain investments securities amounting to BD 71,829 thousand as at FVOCI. In 2015, these investments were classified as available-for-sale. Total dividends income recongnised during the year of 2016 on these investement is BD 3,161 thousand.

Allowance for impairment

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

	2016				2015
	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	Total BD '000
Government and other bonds at FVOCI or Amortised Cost					
Balance at 1 January – on adoption of IFRS 9	162	209	22,982	23,353	48,783
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	2,822
Financial assets that have been derecognised	(30)	(23)	–	(53)	
Write-offs	–	–	(21,576)	(21,576)	(1,211)
Recoveries of amounts previously written off	–	–	(1,406)	(1,406)	(2,284)
Changes in models/risk parameters	–	–	–	–	–
Foreign exchange and other movements	–	–	–	–	(45)
Balance at 31 December	164	445	–	609	48,065

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 (2015: available-for-sale) is their fair value.

* The above table includes ECL of government and other bonds measured at amortised cost of BD 5 thousand.

9 INVESTMENTS IN ASSOCIATED COMPANIES AND JOINT VENTURES

The Group has a 23.03% (2015: 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% (2015: 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% (2015: 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 35% (2015: 35%) equity stake in Diyar Al Harameen Al Ola Limited ("Diyar"), a company incorporated in the Cayman Islands. Diyar holds 100% beneficial interest in a hotel in Makkah, Kingdom of Saudi Arabia. However, due to lack of significant influence in 2016 the Group reclassified this investment to FVOCI.

The Group has a 40% (2015: 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% (2015: nil) 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 listied on Bahrain Bourse and their regional peers.

The Group has a 50% (2015: nil) stake in Aegila Capital Management Limited, a jointed 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:

	2016 BD '000	2015 BD '000
Carrying amount of investment in associated companies and joint ventures		
At 1 January	**35,823**	36,537
Acquisitions during the year	**10,694**	–
Share of profit	**5,467**	4,215
Dividends received from associated companies	**(2,103)**	(1,835)
Change in unrealised fair values – associated companies (note 17)	**6**	(85)
Change in Foreign exchange translation adjustments	**(2)**	(9)
Reclassification to FVOCI	**(4,962)**	–
Capital distribution	**(1,000)**	(3,000)
At 31 December	**43,923**	35,823

	2016 BD '000	2015 BD '000
Share of associated companies and joint ventures statements of financial position		
Current and non-current assets	**94,874**	76,577
Current and non-current liabilities	**(50,951)**	(40,754)
Net assets	**43,923**	35,823
Share of associated companies and joint ventures revenues		
Revenue	**10,987**	10,124

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:

	2016 BD '000	2015 BD '000
Net interest income	**21,504**	17,421
Gross profit on automotive sales	**6,671**	10,715
Other operating income	**12,866**	7,238
Total operating income	**41,041**	35,374
Operating expense	**(17,847)**	(18,317)
Other expense	**(2,625)**	(1,551)
Profit for the year	**20,569**	15,506
Group's share of profit for the year	**4,737**	3,571

	2016 BD '000	2015 BD '000
Assets		
Cash and balances with banks	**5,311**	2,206
Loans and advances to customers	**265,318**	222,762
Inventories	**26,752**	24,274
Other assets	**47,618**	38,278
Total assets	**344,999**	287,520
Liabilities		
Bank overdrafts	**1,959**	1,328
Trade and other payables	**18,851**	19,469
Bank term loans	**161,628**	117,503
Bonds issued	**39,816**	39,753
Total liabilities	**222,254**	178,053
Donation reserve	**(872)**	(838)
Equity	**121,873**	108,629
Proportion of the Group's ownership	**23.03%**	23.03%
	28,067	25,017

The figures reported above for BCFC are based on 30 September 2016 reviewed financial statements adjusted for expected performance in the last quarter.

The market value of the Group's investment in BCFC is BD 25,205 thousand (2015: BD 28,778 thousand) compared to the carrying value of BD 28,067 thousand (2015: BD 25,017 thousand) as at 31 December 2016.

10 INTEREST RECEIVABLE AND OTHER ASSETS

	2016 BD '000	2015 BD '000
Interest receivable	**14,783**	17,350
Accounts receivable	**23,002**	18,664
Positive fair value of derivatives (note 26)	**6,938**	2,336
Prepaid expenses	**1,777**	2,185
Deferred tax	**2,216**	2,991
Collateral pending sale	**4,671**	4,784
Other	**11,382**	8,660
	64,769	56,970

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 2016	**8,241**	**10,603**	**5,123**	**216**	**24,183**
Net book value at 31 December 2015	8,260	11,370	5,051	125	24,806

The depreciation charge for the year amounted to BD 3,430 thousand (2015: BD 3,226 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	2016 BD '000	2015 BD '000
145,140	Libor + 1.25%	2017	**8,509**	8,509
129,860	Libor + 1.75%	2018	**46,800**	45,368
400,000	3.50%	2020	**150,800**	150,800
			206,109	204,677

13 CUSTOMERS' CURRENT, SAVINGS AND OTHER DEPOSITS

	2016 BD '000	2015 BD '000
Term deposits	**1,362,104**	1,497,279
Current accounts	**571,324**	608,957
Savings accounts	**483,129**	440,189
Other accounts	**77,158**	96,467
	2,493,715	2,642,892

14 INTEREST PAYABLE AND OTHER LIABILITIES

	2016 BD '000	2015 BD '000
Accrued expenses	**36,585**	33,996
Interest payable	**13,405**	16,728
Accounts payable	**16,750**	14,634
Negative fair value of derivatives (note 26)	**9,775**	12,490
Other	**7,212**	6,378
Allowance for impairment*	**864**	–
	84,591	84,226

* This represents allowance for impairment on financial contracts issued as of 31 December 2016, the sum of ECL provisions of BD 864 and the amounts recognised at issuance less cumulative amortisation.

15 EQUITY

Share capital	2016 BD '000	2015 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 (2015: 1,081,647,952 shares) of BD 0.100 each	**108,165**	108,165
*Treasury stock**	**(1,206)**	(4,728)

* Treasury stock represents the purchase by the Bank of its own shares. At the end of the year, the Bank held 6,098,267 (2015: 17,195,500) of its own shares, inclusive of bonus shares issued during 2016.

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 27 (2015: BD 243) 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, 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 per cent. 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. 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 (2015: BD 2,575 thousand) 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

	2016 BD '000	2015 BD '000
Fair value through other comprehensive income		
At 1 January	**(12,070)**	17,350
Changes due to adoption of IFRS 9:		
Transfer to retained earnings on classification to FVTPL	**(4,853)**	–
Transfer on classification to amortised cost	**4,988**	–
Transfer from/to retained earnings on reclassification as FVOCI	**(17,015)**	–
Restated balance as at 1 January	**(28,950)**	17,350
Transfer to retained earnings on sale/write off of equity securities	**3,738**	–
Transfer to P&L on sale of investment securities	**(2,095)**	(3,813)
Transferred to P&L on impairment	**238**	1,094
Fair value changes on investment securities at FVOCI during the year	**13,460**	(26,701)
At 31 December	**(13,609)**	(12,070)
Cash flow hedges		
At 1 January	**(234)**	70
Change in unrealised fair values	**168**	(219)
Change in unrealised fair values – associated companies (note 9)	**6**	(85)
At 31 December	**(60)**	(234)
	(13,669)	(12,304)

18 PROPOSED APPROPRIATIONS

	2016 BD '000	2015 BD '000
Cash dividend	**32,266**	26,611
Stock dividend	**–**	–
Transfer to general reserve	**–**	2,575
Donations	**1,400**	1,400
	33,666	30,586

The Board of Directors has proposed cash dividend of BD 0.030 per share (2015: BD 0.025 per share), net of treasury stock as of 31 December 2016. The Bank paid dividend of BD 0.025 per share (2015: 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 29 March 2017. The payment of dividend is also subject to the approval of the Central Bank of Bahrain.

19 INTEREST AND SIMILAR INCOME

	2016 BD '000	2015 BD '000
Loans and advances to customers	**91,714**	87,094
Investment securities	**22,871**	20,075
Deposits and amounts due from banks and other financial institutions	**4,806**	2,562
Treasury bills	**9,165**	4,882
	128,556	114,613

20 OTHER INCOME

	2016 BD '000	2015 BD '000
Fee and commission income	**44,061**	40,919
Dividend income	**3,540**	3,806
Realised gains on investment securities	**2,707**	4,408
Gain on foreign exchange	**5,149**	5,260
Others	**1,539**	2,350
	56,996	56,743
Fee and commission expense	**(14,784)**	(12,524)
	42,212	44,219

Included in fee and commission income is BD 67 thousand (2015: BD 132 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 as follows:

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, 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 as follows:

	2016	2015
Profit for the year attributable to the owners of the Bank (BD '000)	**56,410**	53,212
(Less): Distribution on perpetual tier 1 convertible capital securities (BD '000)	**(3,552)**	–
Adjusted net profit for the year attributable to the owners of the Bank	**52,858**	53,212
Weighted average number of shares, net of treasury stock, outstanding during the year	**1,070,557,685**	1,060,391,006
Basic earnings per share (BD)	**0.049**	0.050
Weighted average number of ordinary shares adjusted for the effect of dilution	**1,285,801,465**	1,060,391,006
Diluted earnings per share (BD)	**0.044**	0.050

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.

22 OPERATING SEGMENTS (continued)

Segment information (continued)

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 write back of impairment of non-trading investment securities	–	–	–	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

Segment information for the year ended 31 December 2015 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	24,681	34,681	32,004	23,247	114,613
Interest expense	(2,672)	(8,600)	(8,598)	(22,037)	(41,907)
Internal fund transfer price	(6,157)	(1,971)	(3,545)	11,673	–
Net Interest Income	15,852	24,110	19,861	12,883	72,706
Other Operating Income	20,486	4,061	5,944	13,728	44,219
Operating income before share of profit of associated companies and joint ventures	36,338	28,171	25,805	26,611	116,925
Net provision for impairment on loans and advances to customers	(1,293)	(6,298)	(11,384)	–	(18,975)
Net provision of impairment of non-trading investment securities	–	–	–	(538)	(538)
Segment result	12,875	9,370	3,734	23,195	49,174
Share of profit of associated companies and joint ventures	4,215	–	–	–	4,215
Profit for the year					53,389
Loss attributable to non-controlling interest					(177)
Profit for the year attributable to the owners of the Bank					53,212
Segment assets	486,914	696,969	1,334,785	1,063,820	3,582,488
Investment in associated companies and joint ventures	27,950	–	–	7,873	35,823
Common assets					28,130
Total assets					3,646,441
Segment liabilities	679,825	975,041	853,257	729,570	3,237,693
Common liabilities					48,014
Total liabilities					3,285,707

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 2016 and 31 December 2015:

	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**

	Domestic BD '000	Others BD '000	Total BD '000
31 December 2015			
Net interest income	61,777	10,929	72,706
Share of profit in associated companies and joint ventures	4,215	–	4,215
Other income	40,553	3,666	44,219
	106,545	14,595	121,140
Non-current assets	20,659	4,147	24,806

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:

	2016 BD '000	2015 BD '000
Cash (note 4)	**20,853**	17,636
Current accounts and placements with central banks (note 4)	**216,167**	186,716
Treasury bills	**–**	5,667
Deposits and amounts due from banks and other financial institutions with original maturities of ninety days or less	**300,584**	323,097
	537,604	533,116

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
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**
2015				
Loans and advances to customers	–	4,207	1,224	5,431
Customers' current, savings and other deposits	290,287	6,180	8,895	305,362

For the years ended 31 December 2016 and 31 December 2015 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
2016				
Interest income	**–**	**567**	**120**	**687**
Interest expense	**3,127**	**106**	**115**	**3,348**
2015				
Interest income	–	320	18	338
Interest expense	3,328	100	126	3,554

Compensation of the key management personnel is as follows:

	2016 BD '000	2015 BD '000
Short term employee benefits	**10,279**	7,507
Others	**(31)**	269
	10,248	7,776

Key management interest in an employee share incentive scheme

The Bank has introduced effective 2010, a new 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 2016 and as at 31 December 2015 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 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 venture	–	–	–	–	–	–	–	–	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	

31 December 2015	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	204,352	–	–	–	204,352	–	–	–	82,398	286,750
Treasury bills	77,647	146,069	72,057	98,317	394,090	–	–	–	–	394,090
Deposits and amounts due from banks and other financial institutions	288,375	36,721	–	–	325,096	–	–	–	–	325,096
Loans and advances to customers	101,348	145,071	121,488	139,823	507,730	769,419	243,185	54,137	190,328	1,764,799
Investment securities	24,602	9,641	19,872	50,883	104,998	261,825	239,942	14,016	137,326	758,107
Investments in associated companies and joint venture	–	–	–	–	–	–	–	–	35,823	35,823
Interest receivable and other assets	47,884	63	90	54	48,091	8,879	–	–	–	56,970
Premises and equipment	–	–	–	–	–	20,022	1,216	1,728	1,840	24,806
Total assets	744,208	337,565	213,507	289,077	1,584,357	1,060,145	484,343	69,881	447,715	3,646,441
Liabilities										
Deposits and amounts due to banks and other financial institutions	137,683	28,893	9,440	3,388	179,404	–	–	–	–	179,404
Borrowings under repurchase agreement	–	–	–	–	–	174,508	–	–	–	174,508
Term borrowings	–	–	–	–	–	204,677	–	–	–	204,677
Customers' current, savings and other deposits	334,779	228,438	95,990	112,213	771,420	28,391	9	–	1,843,072	2,642,892
Interest payable and other liabilities	66,400	3,000	1,438	3,647	74,485	9,432	–	–	309	84,226
Total liabilities	538,862	260,331	106,868	119,248	1,025,309	417,008	9	–	1,843,381	3,285,707
Net	205,346	77,234	106,639	169,829	559,048	643,137	484,334	69,881	(1,395,666)	360,734
Cumulative	205,346	282,580	389,219	559,048		1,202,185	1,686,519	1,756,400	360,734	

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 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**

31 December 2015	Positive fair value BD '000	Negative fair value BD '000	Notional amount BD '000
Derivatives held for trading			
Forward foreign exchange contracts	302	360	162,509
Derivatives held as fair value hedges			
Interest rate swaps	1,991	12,078	505,932
Derivatives held as cash flow hedges			
Interest rate swaps	43	52	57,519
	2,336	12,490	725,960

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 and the hedged istruments are subject to different counterparty risks, resulting in a change to hedge effectiveness measurement elements.

At 31 December 2016, the Group held the following interest rate swaps as hedging instruments in fair value hedges of interest risk.

Risk category	Less than 1 month	1–3 months	3 months – 1 year	1–5 years	More than 5 years
Interest rate risk					
Hedge of Investment Securities					
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%**
31 December 2015					
Nominal amount (BD '000)	1,885	3,770	19,604	194,267	286,406
Average fixed interest rate	5%	5%	5%	5%	5%

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

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

	2016		2015	
	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]	**549,057**	**2,230**	514,980	9,580

For the year ended 31 December 2016, the Group recognised a net gain of BD 1 thousand (2015: net gain of BD 31 thousand), representing the gain on the hedging instruments. The total loss on hedged items attributable to the hedged risk amounted to BD 21 thousand (2015: loss of BD 286 thousand).

26 DERIVATIVES (continued)

Cash Flow Hedges

At 31 December 2016, the Group held the following instruments to hedge exposures to changes in interest rates and foreign currency.

	Less than 1 month	1–3 months	3 months – 1 year	1–5 years	More than 5 years
Interest rate risk					
Interest rate swaps					
31 December 2016					
Nominal amount (BD '000)	**–**	**–**	**8,509**	**49,010**	**–**
Average fixed interest rate	**0%**	**0%**	**2%**	**3%**	**0%**
31 December 2015					
Nominal amount (BD '000)	–	–	–	57,519	–
Average fixed interest rate	0%	0%	0%	3%	0%

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.

	2016		2015	
	Carrying amount BD '000	**Cash flow reserve BD '000**	Carrying amount BD '000	Cash flow reserve BD '000
Term Borrowings	**57,519**	**158**	57,519	(10)

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 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

31 December 2015	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	3,946	13,925	16,382	–	34,253
Guarantees	204,616	–	–	–	204,616
					238,869
Commitments					
Undrawn loan commitments	143,943	–	–	–	143,943
					143,943
					382,812

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:

	2016 BD '000	2015 BD '000
Within one year	**838**	858
After one year but not more than five years	**1,872**	1,212
More than five years	**4,406**	2,418
	7,116	4,488

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. 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) 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.

The Risk & Credit Management Division (RCMD) is responsible for oversight of 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. 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.

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. 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 Credit 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.

	2016 BD '000	2015 BD '000
Balances with central banks	**293,515**	269,114
Treasury bills	**401,635**	394,090
Deposits and amounts due from banks and other financial institutions	**318,407**	325,096
Loans and advances to customers	**1,767,138**	1,764,799
Investment securities	**688,730**	663,051
Interest receivable and other assets	**56,105**	47,010
	3,525,530	3,463,160
Contingent liabilities	**266,805**	238,869
Commitments	**127,186**	143,943
	393,991	382,812
	3,919,521	3,845,972

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:

	2016			2015		
	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	**3,088,221**	**2,682,640**	**333,308**	2,959,680	2,809,005	329,950
North America	**61,650**	**5,965**	**615**	90,196	5,217	436
European Union countries	**217,846**	**394,225**	**9,799**	219,528	314,990	11,379
Asia	**243,086**	**132,243**	**42,588**	315,379	142,972	29,640
Others	**91,754**	**13,269**	**7,681**	61,658	13,523	11,407
	3,702,557	**3,228,342**	**393,991**	3,646,441	3,285,707	382,812
Trading and manufacturing	**629,572**	**94,469**	**176,992**	613,889	151,087	164,186
Banks and other financial institutions	**774,348**	**1,246,851**	**33,953**	827,713	1,237,166	38,185
Construction and real estate	**408,702**	**62,205**	**120,289**	430,783	75,601	123,703
Government and public sector	**1,196,815**	**698,443**	**2,890**	1,141,750	756,818	3,016
Individuals	**388,086**	**833,728**	**322**	352,781	768,835	1,050
Others	**305,034**	**292,646**	**59,545**	279,525	296,200	52,672
	3,702,557	**3,228,342**	**393,991**	3,646,441	3,285,707	382,812

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, FVOCI debt investments (2016) and available-for-sale debt assets (2015). 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.

	2016				2015
	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**	Total BD '000
Loans and advances to customers – Commercial loans and overdraftsat amortised cost					
High (Grades 1 to 3)	**338,048**	**–**	**–**	**338,048**	300,306
Standard (Grade 4 to 6)	**634,153**	**152,974**	**–**	**787,127**	909,513
Substandard (Grade 7 to 8)	**8,355**	**195,696**	**–**	**204,051**	214,597
Non-performing (Grade 9 to 10)	**–**	**–**	**99,984**	**99,984**	66,926
	980,556	**348,670**	**99,984**	**1,429,210**	1,491,342
Loss allowance	**(2,623)**	**(38,597)**	**(67,331)**	**(108,551)**	(84,945)
Carrying amount	**977,933**	**310,073**	**32,653**	**1,320,659**	1,406,397

	2016				2015
	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**	Total BD '000
Loans and advances to customers – Consumer at amortised cost					
High (Grades 1 to 3)	**432,854**	**–**	**–**	**432,854**	342,837
Standard (Grade 4 to 6)	**–**	**8,468**	**–**	**8,468**	5,112
Substandard (Grade 7 to 8)	**–**	**10,173**	**–**	**10,173**	8,587
Non-performing (Grade 9 to 10)	**–**	**–**	**13,335**	**13,335**	15,761
	432,854	**18,641**	**13,335**	**464,830**	372,297
Loss allowance	**(2,951)**	**(5,085)**	**(10,315)**	**(18,351)**	(13,895)
Carrying amount	**429,903**	**13,556**	**3,020**	**446,479**	358,402

	2016				2015
	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	Total BD '000
Debt investment securities at FVOCI (2015: available-for-sale)					
High (AAA to A-)	**183,857**	**–**	**–**	**183,857**	268,927
Standard (BBB+ to B-)*	**291,586**	**94,419**	**–**	**386,005**	382,578
Substandard (CCC+ to CCC-)	**–**	**–**	**–**	**–**	–
Past due or individually impaired	**–**	**–**	**–**	**–**	23,064
Total	**475,443**	**94,419**	**–**	**569,862**	674,569
Loss Allowance	**(159)**	**(445)**	**–**	**(604)**	(23,064)
Net Carrying amount	**475,284**	**93,974**	**–**	**569,258**	651,505

* Standard grade includes unrated investments amounting to BD 1,549 thousand (2015: BD 7,058 thousand).

	Stage 1	Stage 2	Stage 3	Total 2016	Total 2015
Debt investment securities at amortised cost (2015: held-to-maturity)					
High (AAA to A-)	**83,290**	**–**	**–**	**83,290**	–
Standard (BBB+ to B-)	**434,042**	**–**	**–**	**434,042**	405,636
Substandard (CCC+ to CCC-)	**–**	**–**	**–**	**–**	–
Past due or individually impaired	**–**	**–**	**–**	**–**	–
Total	**517,332**	**–**	**–**	**517,332**	405,636
Loss allowance	**(5)**	**–**	**–**	**(5)**	–
Net Carrying amount	**517,327**	**–**	**–**	**517,327**	405,636
Loan commitments & Financial guarantee					
High (Grades 1 to 3)	**144,149**	**–**	**–**	**144,149**	124,097
Standard (Grade 4 to 6)	**77,099**	**144,651**	**–**	**221,750**	229,536
Substandard (Grade 7 to 8)	**828**	**27,168**	**–**	**27,996**	28,718
Non-performing (Grade 9 to 10)	**–**	**8**	**88**	**96**	461
Total	**222,076**	**171,827**	**88**	**393,991**	382,812
Loss allowance	**(268)**	**(596)**	**–**	**(864)**	(501)
Carrying amount (provision)	**221,808**	**171,231**	**88**	**393,127**	382,311

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

	2016 BD '000	2015 BD '000
Debt investment securities		
High (AAA to A-)	**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

	2016 BD '000	2015 BD '000
Derivative assets held for risk management	**11,628**	16,771
Loans and advances:		
Cash	**60,952**	71,586
Mortgage lending	**1,096,412**	1,097,499
Financial Instruments	**55,466**	85,426

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
- 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 vii 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.

32 CREDIT QUALITY PER CLASS OF FINANCIAL ASSETS (continued)

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.

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 Bank 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 years (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 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.

	2016 BD '000
Banks and financial institutions	**560,101**
Sovereign	**22,202**
Investment securities (debt instruments)	**1,087,475**

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.

	2016 BD '000	2015 BD '000
Loans and advances to customers		
Commercial loans	**32,486**	105,062
Consumer loans	**7,469**	7,915
	39,955	112,977

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:

	2016 BD '000	2015 BD '000
Foreign exchange	**172**	94
Interest Rate	**5**	1
	177	95

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 2016 an increase of 200 basis point in interest rates, with all variables held constant, will result in an increase in the net interest income, for the following next 12 months, by approximately BD 19,088 thousand (2015: increase by BD 18,504 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 2016 estimated at BD 11,528 thousands (2015: BD 7,167 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)	
	2016 BD '000	2015 BD '000	2016 BD '000	2015 BD '000
Bahraini Dinar	**11,331**	7,023	**7,499**	3,133
US Dollar	**6,250**	7,496	**2,400**	1,290
Kuwaiti Dinar	**(260)**	763	**167**	669
Others	**1,766**	3,223	**1,462**	2,076
Total	**19,088**	18,504	**11,528**	7,167

An increase of 200 basis point in interest rates, with all other variables held constant, will result in a negative impact on equity of approximately 2.8% amounting to BD 14,126 thousand (2015:3.8%, BD 14,591 thousand). Similarly, a decrease of 200 basis point in interest rates, with all other variables held constant, will result in a positive impact on equity of approximately 2.8% amounting to BD 14,126 thousand (2015: 3.8%, BD 14,591 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:

	2016 BD '000 equivalent long (short)	2015 BD '000 equivalent long (short)
US dollar	**83,141**	60,496
Euro	**488**	51
GCC currencies (excluding Kuwaiti dinar)	**2,582**	8,789
Kuwaiti dinar	**504**	274
Others	**1,592**	463

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 at 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 2016 BD '000**	Total 2015 BD '000
Bahrain Bourse	± 15%	**1,863**	2,263
Other GCC and other stock exchanges	± 15%	**4,597**	6,815
		6,460	9,078

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 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)**

31 December 2015	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	–	133,544	30,521	9,450	5,894	–	–	–	–	179,409
Borrowings under repurchase agreement	–	–	–	–	5,185	189,127	–	–	–	194,312
Term borrowings	–	–	619	308	3,255	224,838	–	–	–	229,020
Customers' current, savings and other deposits	1,146,028	375,422	454,149	302,021	369,262	24,920	5,874	11,730	–	2,689,406
Total undiscounted financial liabilities	1,146,028	508,966	485,289	311,779	383,596	438,885	5,874	11,730	–	3,292,147
Letter of Guarantees	204,617	–	–	–	–	–	–	–	–	204,617
Undrawn loan commitments	143,942	–	–	–	–	–	–	–	–	143,942
Derivative financial instruments										
Contractual amounts payable	–	(2,188)	(5,614)	(6,203)	(33,733)	(343,944)	(266,099)	(40,428)	(70,685)	(768,894)
Contractual amounts receivable	–	2,931	6,109	4,625	28,897	311,508	248,987	28,921	61,504	693,482
	–	743	495	(1,578)	(4,836)	(32,436)	(17,112)	(11,507)	(9,181)	(75,412)

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 2016 and 31 December 2015.

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**
Derivatives held as cash flow hedges	**–**	**–**	**–**	**–**
	–	**9,775**	**–**	**9,775**

31 December 2015	Level 1 BD'000	Level 2 BD'000	Level 3 BD'000	Total BD'000
Financial assets				
Bonds	569,612	2,664	–	572,276
Equities	60,518	7,387	–	67,905
Managed funds	–	1,870	–	1,870
Derivatives held for trading	–	179	–	179
Derivatives held as fair value hedges	–	2,114	–	2,114
Derivatives held as cash flow hedges	–	43	–	43
	630,130	14,257	–	644,387
Financial liabilities			–	
Derivatives held for trading	–	26	–	26
Derivatives held as fair value hedges	–	12,412	–	12,412
Derivatives held as cash flow hedges	–	52	–	52
	–	12,490	–	12,490

During 2015, unquoted equity and managed funds investments amounting to BD 25,284 thousand recorded at cost less impairment, were included under available-for-sale investments.

Transfers between level 1, level 2 and level 3

During the reporting year ended 31 December 2016 and 31 December 2015, 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:

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)**

2015	Carrying value BD '000	Fair value BD '000	Difference BD '000
Financial liabilities			
Term borrowings	204,677	194,859	(9,818)
Financial assets			
Investment securities	90,774	89,205	(1,569)

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:

	2016 BD '000	2015 BD '000
Expense arising from equity-settled share-based payment transactions	**714**	716
Shares vested during the year	**(745)**	(447)

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 2016, there has been a transfer of 10,398,441 shares (2015: 9,498,441 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)

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

	2016		2015	
	Number of shares	Cost per share BD	Number of shares	Cost per share BD
Opening balance of shares granted but not vested	**5,914,981**	**0.424**	5,155,397	0.415
Equity shares granted during the year	**2,851,177**	**0.312**	2,681,473	0.432
Equity shares transferred to trust	**900,000**	**0.312**	1,877,014	0.432
Shares transferred to active employees	**(1,798,302)**	**0.425**	(1,117,430)	0.400

The market price of BBK B.S.C. shares at 31 December 2016 was BD 0.400 (2015: BD 0.436).

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:

	2016 BD '000	2015 BD '000
Capital base:		
CET1 capital	**383,518**	355,631
Additional Tier 1 capital	**86,098**	–
Tier 2 capital	**30,865**	29,056
Total capital base (a)	**500,481**	384,687
Credit risk weighted exposure	**2,469,207**	2,367,734
Operational risk weighted exposure	**211,854**	204,947
Market risk weighted exposure:	**27,025**	14,762
Total risk weighted exposure (b)	**2,708,086**	2,587,443
Capital adequacy (a/b* 100)*	**18.48%**	14.87%
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 2016, there were legal cases pending against the Group aggregating BD 814 thousand (2015: 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 2016 the total contribution fund including the earned income stands at BD 15,338 thousand (2015: BD 14,577 thousand). Out of the total fund amount, payment of the principal amount equal to BD 13,496 thousand (2015: BD 13,007 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 4,912 thousand (2015: BD 3,912 thousand) is invested in Bahraini Sovereign Bonds.

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 2016 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 definition 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. In addition, 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 per cent to 12.5 per cent, compared to 10.5 per cent 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 per cent (including CCB) and minimum T1 Capital Ratio of 10.5 per cent (including CCB). In the event that the total capital adequacy ratio falls below 12.5 per cent, 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 per cent.

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% of the overall risk for the Bank. The bank has a robust credit risk management architecture which is explained in greater detail in 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 per cent 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%.

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 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.

2 INTRODUCTION TO THE BASEL III FRAMEWORK (continued)

Pillar II (continued)

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 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 framework is currently under initial monitoring period. As per the concluded consultation, the framework is proposed to be introduced with effect from January 1, 2018.

The CBB has concluded consultation on draft guidelines for Credit Grading and Classification in 2015. The CBB has also solicited views from banks on the Basel Committee's consultation document on Standardized Approach. Similarly, the bank is in the process of reviewing IFRS 9 for implementation within the prescribed timeframe. These initiatives, if and when introduced, may impact capital adequacy requirements.

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	**314,368**	**314,368**	
Treasury bills	**401,635**	**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**	
Of which collective impairment provisions	(30,865)		a
Of Which net loans and advances (gross of collective impairment provisions)	1,798,003	1,767,138	
Investment securities	**768,134**	**768,134**	
Of which related to equity investments in financial entities		37,403	
Of which investments in financial entities under CET1		28,461	b
Of which investments in financial entities under Tier 2		8,942	c
Of which related to other investments		693,328	
Investments in associated companies and joint ventures	**43,923**	**46,443**	
Of which Investment in own shares	515	515	d
Of which equity investments in financial entities	30,351	30,351	e
Of which other investments	13,057	15,577	

	Statement of financial position as in published financial statements BD '000	Statement of financial position as per Regulatory Reporting BD '000	Reference
Interest receivable and other assets	**64,769**	**63,613**	
Of which deferred tax assets due to temporary differences	2,217	2,217	f
Of which Interest receivable and other assets	62,552	61,396	
Premises and equipment	**24,183**	**23,984**	
Total assets	**3,702,557**	**3,703,722**	
Liabilities and Equities			
Liabilities			
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**	**2,495,693**	
Interest payable and other liabilities	**84,591**	**84,156**	
Total liabilities	**3,228,342**	**3,229,885**	
Equity			
Share capital	**108,165**	**108,165**	g
Treasury stock	**(1,206)**	**(1,206)**	h
Perpetual tier 1 convertible capital securities	**86,098**	**86,098**	i
Share premium	**39,919**	**39,919**	j
Statutory reserve	**54,082**	**54,082**	k
General reserve	**54,082**	**54,082**	l
Cumulative changes in fair values	**(13,669)**	**(13,669)**	
of which cumulative changes in fair values on bonds and equities	(13,608)	(13,608)	m
of which Fair value changes in cash flow hedges	(60)	(60)	n
Foreign currency translation adjustments	**(11,558)**	**(11,558)**	
of which related to unconsolidated subsidiary	–	(85)	o
of which related to Parent	–	(11,473)	p
Retained earnings	**122,830**	**122,830**	
of which employee stock options	2,337	2,337	
of which Retained earnings	120,493	120,493	q
Appropriations	**33,666**	**33,666**	r
ATTRIBUTABLE TO THE OWNERS OF THE BANK	472,409	472,409	
Non-controlling interest	1,806	1,428	
Total equity	**474,215**	**473,837**	
Total Liabilities and equities	**3,702,557**	**3,703,722**	

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	3,333	2,897

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, (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.

5 CAPITAL COMPONENTS - CONSOLIDATED (continued)

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) that may be included as part of T2 capital, which should be a maximum of 1.25 per cent 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%
Tier 2 (T2)	2%	
Total Capital		10%
Capital Conservation Buffer (CCB)		2.50%
CAR including CCB		
CET 1 plus CCB		9%
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%
Tier 2 (T2)	2%	
Total Capital		8%
Capital Conservation Buffer (CCB)		0%

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. Unlike Basel II capital adequacy framework were deductions were applied 50 per cent from T1 and 50 per cent from T2, 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	146,878		g+h+j
Retained earnings	154,072		o+q+r
Accumulated other comprehensive income and losses (and other reserves)	83,023		k+l+m+n+p
Common Equity Tier 1 capital before regulatory adjustments	**383,973**	**–**	
Common Equity Tier 1 capital: regulatory adjustments			
Cash flow hedge reserve	(60)		n
Investments in own shares	515		d
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)	–	28,461	b
Total regulatory adjustments to Common equity Tier 1	**455**	**28,461**	
Common Equity Tier 1 capital (CET1)	**383,518**		
Additional Tier 1 capital: instruments			
Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	86,098		
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)	**469,616**		
Tier 2 capital: instruments and provisions			
Provisions	30,865		
Tier 2 capital before regulatory adjustments	**30,865**		

	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
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)	–	8,942	c
Total regulatory adjustments to Tier 2 capital	–	8,942	
Tier 2 capital (T2)	**30,865**		
Total capital (TC = T1 + T2)	**500,481**		
Total risk weighted assets	**2,708,086**		
Capital ratios and buffers			
Common Equity Tier 1 (as a percentage of risk weighted assets)	14.16%		
Tier 1 (as a percentage of risk weighted assets)	17.34%		
Total capital (as a percentage of risk weighted assets)	18.48%		
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)	14.16%		
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	37,403		
Significant investments in the common stock of financials	30,351		e
Deferred tax assets arising from temporary differences (net of related tax liability)	2,217		f
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)	50,736		
Cap on inclusion of provisions in Tier 2 under standardised approach	30,865		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 per cent. The CBB's current minimum total capital adequacy ratio (including CCB) for banks incorporated in Bahrain is set at 12.5 per cent. The total capital adequacy ratio of the Group as at 31 December 2016 was 18.48 per cent.

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	18.48%	17.34%
CrediMax	63.52%	63.52%

7. CREDIT RISK – PILLAR III DISCLOSURES

This section describes the 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 per cent 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 per cent risk weighting.

Public Sector Entities (PSE) portfolio

Claims on Bahraini PSEs, and claims on PSEs on domestic currency - which are assigned a zero per cent risk weight by their respective country regulator, can be assigned a zero per cent 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 per cent 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 per cent risk weight.

Regulatory retail portfolio

Claims on retail portfolio are risk weighted at 75%, 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 per cent. Claims secured by mortgages on commercial real estate are subject to a minimum of 100 per cent 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, i.e. the available-for-sale securities portfolio. A 100 per cent risk weight is assigned to listed equities while unlisted equities are weighted at 150 per cent, 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 per cent of the issued common share capital of the issuing commercial entity) above 15 per cent (individually) and 60 per cent (collectively) of the bank's capital (the "Total Capital materiality thresholds") must be risk weighted at 800 per cent. Moreover, significant investments in the common shares of unconsolidated financial entities must be risk weighted at 250 per cent.

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 corporate will be used to determine the risk weight for investments in rated funds. Unrated funds will be assigned a risk weight of 100% if listed, and 150% if not listed.

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 per cent or 150 per cent, 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 per cent. Premises occupied by the bank are weighted at 100 per cent.

Other assets and holdings of securitisation tranches

Other assets are risk weighted at 100 per cent, whereas securitization exposures are risk weighted at 20 per cent to 1,250 per cent, 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% of the bank's regulatory capital to any counterparty or a group of closely related counterparties must be risk weighted at 800%, 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 EXPOSURES

	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	1,054,979	–	1,054,979	19,753	2,469
Public Sector Entities	24,696	–	24,696	–	–
Banks	555,954	–	555,954	328,526	41,066
Corporates	1,540,794	18,282	1,522,512	1,454,869	181,859
Regulatory retail	354,467	266	354,201	265,651	33,206
Mortgage	90,220	152	90,068	67,551	8,444
Investment in securities	102,377	–	102,377	153,727	19,216
Past Due	41,301	1,737	39,564	43,257	5,407
Real Estate	39,718	–	39,718	64,805	8,101
Other assets	68,414	–	68,414	71,740	8,968
Cash Items	17,498	–	17,498	(671)	(84)
Total Credit Risk	**3,890,418**	**20,437**	**3,869,981**	**2,469,208**	**308,652**
Market Risk	–	–	–	27,025	3,378
Operational Risk	–	–	–	211,854	26,482
Total Risk Weighted Exposures	**3,890,418**	**20,437**	**3,869,981**	**2,708,087**	**338,512**

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. FUNDED AND UNFUNDED TOTAL CREDIT EXPOSURES

Total gross credit exposures	Total funded credit exposures BD '000	Total un-funded credit exposures BD '000
Sovereign	1,054,805	174
Public sector entities	24,696	–
Banks	532,160	23,794
Corporates	1,406,041	134,753
Regulatory retail	354,459	8
Mortgage	90,220	–
Investment in securities	102,377	–
Past due	41,301	–
Real estate	39,718	–
Other assets	68,414	–
Cash items	17,498	–
Total credit risk	**3,731,689**	**158,729**

10. AVERAGE CREDIT EXPOSURES

The following are the average quarterly balances for the year ended 31st December 2016:

	BD'000
Sovereign	1,055,253
Public sector entities	24,481
Banks	597,102
Corporates	1,543,842
Regulatory retail	334,022
Mortgage	92,121
Investment in securities	102,448
Past Due	36,628
Real estate	41,299
Other assets	63,067
Cash items	16,956
Total credit risk	**3,907,219**

11. 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	311,242	–	–	3,126	–	**314,368**
Treasury bills	381,309	12,945	–	7,381	–	**401,635**
Deposits in banks & other financial institutions	188,956	35,544	54,679	39,154	74	**318,407**
Loans & advances to customers	1,595,881	38	41,391	116,018	44,251	**1,797,579**
Investments in associated companies	42,808	–	600	–	–	**43,408**
Investment securities	510,817	13,124	121,828	74,730	48,177	**768,676**
Other assets	82,927	–	49	4,640	–	**87,616**
Total funded exposures	**3,113,940**	**61,651**	**218,547**	**245,049**	**92,502**	**3,731,689**
Unfunded commitments and contingencies	126,976	200	7,258	17,106	7,189	**158,729**
Total credit risk	**3,240,916**	**61,851**	**225,805**	**262,155**	**99,691**	**3,890,418**

12. CONCENTRATION OF CREDIT RISK BY INDUSTRY (EXPOSURES SUBJECT TO RISK WEIGHTING)

	Trading and manufacturing BD '000	Banks & other financial institutions BD '000	Construction & real estate BD '000	Government & public sector BD '000	Individuals BD '000	Others BD '000	Total BD '000
Cash and balances with central banks	–	20,872	–	293,496	–	–	**314,368**
Treasury bills	–	–	–	401,635	–	–	**401,635**
Deposits in banks & other financial institutions	–	318,407	–	–	–	–	**318,407**
Loans & advances to customers	604,414	173,969	394,460	21,975	394,772	207,989	**1,797,579**
Investments in associated companies	–	43,408	–	–	–	–	**43,408**
Investment securities	35,393	220,123	20,922	480,081	–	12,157	**768,676**
Other assets	–	–	–	–	–	87,616	**87,616**
Total funded exposures	**639,807**	**776,779**	**415,382**	**1,197,187**	**394,772**	**307,762**	**3,731,689**
Unfunded commitments and contingencies	76,671	25,205	32,537	112	173	24,032	**158,729**
Total credit risk	**716,478**	**801,984**	**447,919**	**1,197,299**	**394,945**	**331,794**	**3,890,418**

13. 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	237,020	–	–	–	–	–	–	77,348	**314,368**
Treasury bills	35,780	233,931	43,887	88,037	–	–	–	–	**401,635**
Deposits in banks & other financial institutions	295,207	10,455	12,318	427	–	–	–	–	**318,407**
Loans & advances to customers	106,088	139,158	156,938	98,277	792,743	274,735	52,909	176,731	**1,797,579**
Investments in associated companies	–	–	–	–	–	–	–	43,408	**43,408**
Investment securities	9,360	17,353	23,955	41,029	286,899	254,736	9,368	125,976	**768,676**
Other assets	54,751	96	49	52	28,364	914	1,619	1,771	**87,616**
Total funded exposures	**738,206**	**400,993**	**237,147**	**227,822**	**1,108,006**	**530,385**	**63,896**	**425,234**	**3,731,689**
Unfunded commitments and contingencies	45,031	22,701	27,704	46,191	12,585	3,609	122	787	**158,729**
Total credit risk	**783,237**	**423,694**	**264,851**	**274,013**	**1,120,591**	**533,994**	**64,018**	**426,021**	**3,890,418**

14. IMPAIRED LOANS AND PROVISIONS

	Principle outstanding BD '000	Impaired loans BD '000	Stage 3: Lifetime ECL credit- impaired BD '000
Manufacturing	319,166	38,191	20,295
Mining and quarrying	16,801	–	–
Agriculture, fishing and forestry	964	10	10
Construction	148,317	16,115	8,712
Financial	177,686	–	969
Trade	294,086	4,070	4,277
Personal / Consumer finance	358,780	7,351	8,416
Credit cards	49,801	1,609	2,275
Commercial real estate financing	177,517	23,710	14,992
Residential mortgage	99,894	5,228	884
Government	22,128	–	–
Technology, media and telecommunications	131,793	17,035	16,816
Transport	21,247	–	–
Other sectors	75,860	–	–
Total	**1,894,040**	**113,319**	**77,646**

15. 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
Past Due loans	50,107	–	–	6,321	–	**56,428**
Impaired loans	109,820	–	–	3,499	–	**113,319**
Stage 3: Lifetime ECL credit- impaired	(74,062)	–	–	(3,584)	–	**(77,646)**
Stage 1: 12-month ECL and stage 2 : Lifetime ECL not credit- impaired	(48,867)	–	–	(389)	–	**(49,256)**

16. IMPAIRED AND PAST DUE LOANS BY INDUSTRY

	Trading and manufacturing BD '000	Banks & other financial institutions BD '000	Construction & real estate BD '000	Government & public sector BD '000	Individuals BD '000	Others BD '000	Total BD '000
Past Due loans	11,863	4,733	19,618	7	13,515	6,692	**56,428**
Impaired loans	36,270	–	45,053	–	31,996	–	**113,319**
Stage 3: Lifetime ECL credit- impaired	(35,639)	(969)	(24,588)	–	(16,450)	–	**(77,646)**
Stage 1: 12-month ECL and stage 2 : Lifetime ECL not credit- impaired	(16,562)	(4,767)	(10,809)	(602)	(10,817)	(5,699)	**(49,256)**

17. AGING OF IMPAIRED PAST DUE LOANS

	3 months up to 1 year BD '000	1 to 3 years BD '000	Over 3 years BD '000	Total BD '000
Impaired past due loans	41,179	33,017	39,123	**113,319**
Stage 3: Lifetime ECL credit- impaired	(18,954)	(26,715)	(31,977)	**(77,646)**
Net outstanding	**22,225**	**6,302**	**7,146**	**35,673**
Market value of collateral	2,148	6,036	46,045	**54,229**

18. RESTRUCTURED LOANS

	BD'000
Loans restructured during the period	39,955
Impact of restructured facilities and loans on provisions	2,939

The above restructuring did not have any significant impact on present and future earnings and were primarily extensions 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.

19. MARKET RISK DISCLOSURES FOR BANKS USING THE INTERNAL MODELS APPROACH (IMA) FOR TRADING PORTFOLIOS (continued)

The summary of VaR of the trading book for the period January 2016 to December 2016 is as follows:

VaR Results for 2016 (10 day 99%)

Global (BAHRAIN and KUWAIT)

1 January 2016 to 31 December 2016

Asset class	Limit BD '000	VaR 31 December 2016 BD '000	High VaR BD '000	Low VaR BD '000	Average VaR BD '000
Foreign exchange	641.00	172.11	289.77	78.27	168.87
Interest rate	151.00	5.10	7.87	0.06	1.14
	792.00	**177.21**	**290.50**	**80.32**	**170.01**

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.

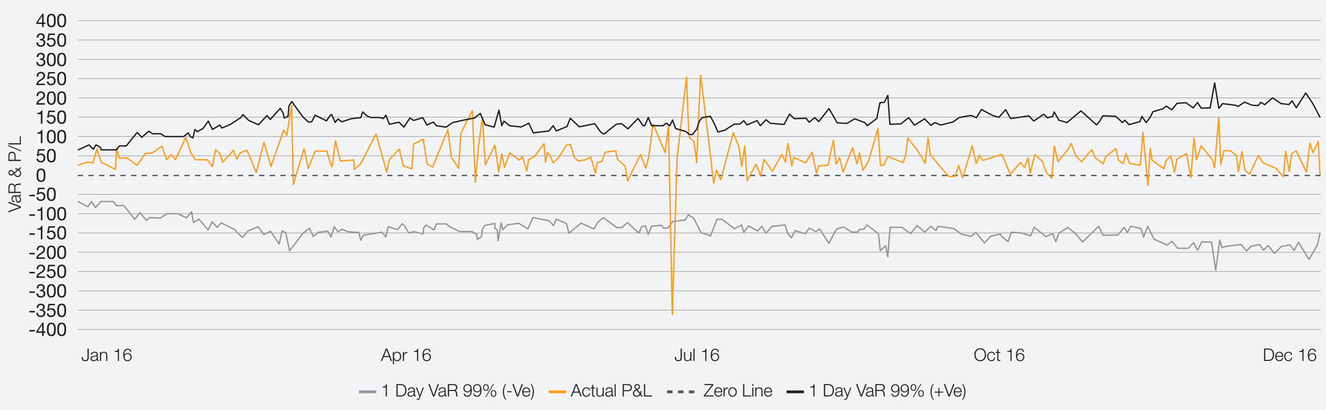
The Backtesting results for the period January-December 2016 confirmed that there was one occasion on which a daily trading loss exceeded VaR figure.

Month end VaR (10 day 99%)

Month	VaR in BD'000
January 2016	117
February 2016	209
March 2016	189
April 2016	158
May 2016	161
June 2016	145
July 2016	172
August 2016	178
September 2016	176
October 2016	183
November 2016	204
December 2016	177

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 2016



20. CONCENTRATION RISK TO INDIVIDUALS WHERE THE TOTAL EXPOSURE IS IN EXCESS OF SINGLE OBLIGOR LIMIT OF 15%

	BD '000
Sovereign	675,980
Total	675,980

21. CREDIT DERIVATIVES EXPOSURE

BBK is not exposed to any credit derivatives as at 31st December 2016.

22. EQUITY POSITIONS IN THE BANKING BOOK

	BD '000
Publicly traded equity shares	52,429
Privately held equity shares	25,531
Total	77,960
Capital required	9,745

23. GAINS ON EQUITY INSTRUMENTS

	BD '000
Realised Gains/ Losses in statement of profit or loss	1,553
Unrealised Gains/ Losses in CET1 Capital	(13,388)

Part IV

Minutes

These meetings are conducted in Arabic, hence the minutes are recorded in Arabic.