United Gulf Bank B.S.C. (c)

CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2019

United Gulf Bank B.S.C. (c)
REPORT OF THE BOARD OF DIRECTORS

The Board of Directors is pleased to submit its report and the audited consolidated financial statements of United Gulf Bank B.S.C. (c) ("the Bank" or "UGB") for the year ended 31 December 2019.

Principal activities and review of business developments
The principal activities of the Bank and its subsidiaries (together the "Group") comprise of investment and commercial banking. Investment banking include asset portfolio management, corporate finance, advisory, investment in quoted and private equity / funds, real estate, capital markets, international banking and treasury functions. Commercial banking includes extending loans and other credit facilities, accepting deposits and current accounts from corporate and institutional customers.

KAMCO merger with Global Investment House
Subsequent to acquisition of GIH in 2018, KAMCO obtained approval of the Kuwait Capital Market Authority (CMA) and the creditors of GIH to merge GIH by amalgamation with KAMCO. The Extraordinary General Meeting (EGM) of GIH, held on 18 September 2019 approved the merger between GIH and KAMCO by way of amalgamation, including the dissolution of GIH. Pursuant to which KAMCO became the merging company and GIH became the merged company. The EGM also approved the share swap ratio of 0.75522821 shares of KAMCO for every share of GIH.

Following the completion of merger all the right and obligation of GIH vested in KAMCO and the legal formalities to transfer ownership of assets and liabilities, changes to contracts where GIH was a party, cancellation of commercial license and license with the Central Bank of Kuwait (CBK) are under process as at the date of these consolidated financial statements. Further, at the close of business on 12 December 2019, GIH transferred all the assets and liabilities to KAMCO.

Results for the year
For the year ended 31 December 2019, the Bank earned a net profit of US$ 11.4 million (2018: net profit of US$ 10.1 million) and total operating income of US$ 113.7 million (2018: US$ 78.9 million).

As of 31 December 2019, total assets of the Group were US$ 923.2 million (2018: US$ 873.5 million) with total equity of shareholders at US$ 210.9 million (2018: US$ 187.0 million).

Appropriations for the year
The Board of Directors' recommendation on the allocation of the net profit for the year is as follows:

- Transfer of US$ 1,142 thousand equivalent to 10% of the Bank's net profit for the period to the Bank's Statutory Reserves;
- Transfer of US$ 1,142 thousand equivalent to 10% of the Bank's net profit for the period to the Bank's General Reserves;
- Retaining the remaining balance of net profit for the period as Retained Earnings for next year.

Auditors

Ernst & Young have expressed their willingness to continue in office and a resolution for their appointment as auditors of the Bank for the year ending 31 December 2020 has been put for approval by the Shareholders.

Signed on behalf of the Board of Directors.

Masaud Hayat
Chairman

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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF UNITED GULF BANK B.S.C. (c)

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the accompanying consolidated financial statements of United Gulf Bank B.S.C. (c) ("the Bank") and its subsidiaries (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2019, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of cash flows and consolidated statement of changes in equity 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 2019 and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). 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 Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in the Kingdom of Bahrain, 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.

Other information included in the Group's 2019 annual report

Other information consists of the information included in the Group's 2019 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 auditors' report, we obtained the Report of the Board of Directors which forms 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.

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF UNITED GULF BANK B.S.C. (c) (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

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 IFRSs and for such internal control as the Board of Directors determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

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

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

As part of an audit in accordance with ISAs, 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.

INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF UNITED GULF BANK B.S.C. (c) (continued)

Report on the Audit of the Consolidated Financial Statements (continued)

Auditor's responsibilities for the audit of the consolidated financial statements (continued)

- 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. 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

We communicate with the 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.

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 Report of the Board of Directors is consistent with the consolidated financial statements;

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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF UNITED GULF BANK B.S.C. (c) (continued)

Report on Other Legal and Regulatory Requirements (continued)

c) we are not aware of any violations of the Bahrain Commercial Companies Law, the CBB and Financial Institutions Law, the CBB Rule Book (Volume 1 and applicable provisions of Volume 6) and CBB directives, or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2019 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.

Ernst & Young

Partner's registration no. 244
26 February 2020
Manama, Kingdom of Bahrain

United Gulf Bank B.S.C. (c)

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2019

	Note	*2019* *US$ 000*	*2018* *US$ 000*
ASSETS			
Demand and call deposits with banks		**71,369**	143,510
Placements with banks		**236,110**	108,529
Investments carried at fair value through profit and loss	7	**97,778**	81,852
Investments carried at fair value through other comprehensive income	8	**131,048**	167,647
Investments carried at amortised cost		**280**	494
Loans and receivables	9	**27,778**	25,191
Other assets	10	**62,933**	61,097
Investments in associates	11	**75,774**	71,513
Investment properties	12	**102,713**	107,629
Property and equipment	13	**51,849**	39,394
Goodwill and other intangible assets	14	**65,591**	66,634
TOTAL ASSETS		**923,223**	873,490
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks and other financial institutions		**307,784**	220,879
Deposits from customers		**22,647**	32,608
Loans payable	16	**36,875**	67,033
Long term bonds	17	**131,948**	131,739
Other liabilities	18	**90,965**	106,375
TOTAL LIABILITIES		**590,219**	558,634
EQUITY			
Share capital	19	**116,132**	101,132
Share premium	19	**5,687**	5,687
Statutory reserve	19	**52,032**	50,890
General reserve	19	**31,763**	30,621
Fair value reserve	20	**(6,009)**	(10,121)
Foreign currency translation reserve	19	**(4,569)**	(4,534)
Retained earnings		**15,911**	13,318
CAPITAL AND RESERVES ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT		**210,947**	186,993
Perpetual Tier 1 capital	21	**33,000**	33,000
Non-controlling interests in equity		**89,057**	94,863
TOTAL EQUITY		**333,004**	314,856
TOTAL LIABILITIES AND EQUITY		**923,223**	873,490

Masaud Hayat Chairman	Faisal Al Ayyar Vice Chairman	Hussain Lalani Chief Executive Officer

The attached notes 1 to 34 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2019

	Note	*2019* *US$ 000*	*2018* *US$ 000*
Continuing operations			
Interest income	22	**9,964**	6,363
Investment income - net	23	**30,371**	4,812
Gain on bargain purchase of a subsidiary		**-**	23,928
		40,335	35,103
Fees and commissions - net	24	**68,337**	42,965
Foreign currency gains - net		**414**	1,621
Share of results of associates - net	11,25	**4,646**	(764)
Total income		**113,732**	78,925
Interest expense	26	**(22,170)**	(14,732)
Operating income before expenses and provisions		**91,562**	64,193
Salaries and benefits		**(45,461)**	(30,310)
General and administrative expenses		**(29,615)**	(20,277)
Operating income before provisions and tax		**16,486**	13,606
Provision for losses against unfunded participation		**-**	(805)
Expected credit losses reversals (provision)	4	**1,615**	(2,306)
Profit before tax from continuing operations		**18,101**	10,495
Taxation - net	15	**(2,027)**	95
Profit after tax from continuing operations		**16,074**	10,590
Discontinued operations			
Net profit from discontinued operations		**-**	524
Profit for the year		**16,074**	11,114
Net profit attributable to non-controlling interests		**4,654**	1,021
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT		**11,420**	10,093

Masaud Hayat
Chairman

Faisal Al Ayyar
Vice Chairman

Hussain Lalani
Chief Executive Officer

The attached notes 1 to 34 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2019

	2019	*2018*
	US$ 000	*US$ 000*
Profit for the year	**16,074**	11,114
Other comprehensive (loss) income that will not be reclassified to profit or loss in subsequent period		
Fair value reserve	**(63)**	(13,283)
	(63)	(13,283)
Other comprehensive loss that may be reclassified to profit or loss in subsequent period		
Cash flow hedges	**(1,132)**	180
Foreign currency translation reserve	**(157)**	(1,093)
Fair value reserve	**(7,853)**	(10,753)
Other comprehensive loss for the year	**(9,205)**	(24,949)
TOTAL COMPREHENSIVE INCOME (LOSS)	**6,869**	(13,835)
Total comprehensive income (loss) attributable to:		
- shareholders of the parent	**2,585**	(11,405)
- non-controlling interests	**4,284**	(2,430)
	6,869	(13,835)

The attached notes 1 to 34 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2019

	Note	2019 US$ 000	2018 US$ 000
OPERATING ACTIVITIES			
Profit before tax		**18,101**	11,019
Net profit from discontinued operations		-	(524)
Profit before tax from continuing operations		**18,101**	10,495
Adjustments for non-cash items:			
Depreciation and amortisation		**3,479**	2,105
Share of results of associates - net	11,25	**(4,646)**	764
Expected credit losses (reversals) / provisions	4	**(1,615)**	2,306
Provision for losses against unfunded participation		-	805
(Gain) loss on investments carried at fair value through profit and loss	23	**(8,617)**	794
Interest income	22	**(9,964)**	(6,363)
Gain on fair valuation of investment properties	23	**(7,294)**	(124)
Interest expense	26	**22,170**	14,732
Dividend Income	23	**(4,196)**	(1,669)
Gain due to reclassification of investment	23	**(664)**	(31)
Loss on sale of an associate	23	-	523
Gain on bargain purchase of a subsidiary		-	(23,928)
Operating profit before changes in operating assets and liabilities		**6,754**	409
Changes in operating assets and liabilities:			
Placements with banks with original maturities of more than ninety days		**(284)**	(15,526)
Investments carried at fair value through profit and loss		**(7,308)**	142
Investments carried at fair value through other comprehensive income		**29,224**	51,804
Investments carried at amortised cost		**214**	-
Loans and receivables		**(1,299)**	(3,472)
Other assets		**(4,626)**	7,805
Due to banks and other financial institutions		**86,905**	(29,332)
Deposits from customers		**(9,961)**	1,590
Other liabilities		**(10,395)**	(4,810)
Net assets of disposal group classified as held for sale		-	524
Interest received		**9,922**	6,415
Interest paid		**(18,543)**	(14,010)
Dividend Income		**4,196**	1,669
Donations		**(200)**	(200)
Directors' remuneration		**(195)**	-
Net cash from operating activities		**84,404**	3,008
INVESTING ACTIVITIES			
Deferred consideration paid on acquisition of a subsidiary		**(8,247)**	-
Investments in associates - net		**384**	5,137
Property and equipment - net		**(2,106)**	(1,793)
Investment in subsidiaries - net of cash acquired		-	(23,568)
Net cash used in investing activities		**(9,969)**	(20,224)
FINANCING ACTIVITIES			
Share capital issued		**15,000**	-
Repayment of loans		**(30,158)**	(31,625)
Interest payment on Tier 1 capital securities		**(3,513)**	(3,513)
Long term bonds		-	131,739
Net cash (used in) from financing activities		**(18,671)**	96,601
Foreign currency translation adjustments		**(400)**	422
Movement in non-controlling interests		**(208)**	(8,631)
NET CHANGE IN CASH AND CASH EQUIVALENTS		**55,156**	71,176
Cash and cash equivalents at 1 January		**237,428**	166,252
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	27	**292,584**	237,428

The attached notes 1 to 34 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
For the year ended 31 December 2019

	Attributable to shareholders of the parent										
	Share capital US$ 000	*Share premium US$ 000*	*Statutory reserve US$ 000*	*General reserve US$ 000*	*Fair value reserve US$ 000*	*Foreign currency translation reserve US$ 000*	*Retained earnings US$ 000*	*Total before non-controlling interests US$ 000*	*Perpetual Tier 1 capital US$ 000*	*Non-controlling interests US$ 000*	*Total equity US$ 000*
Balance at 1 January 2019	101,132	5,687	50,890	30,621	(10,121)	(4,534)	13,318	186,993	33,000	94,863	314,856
Profit for the year	-	-	-	-	-	-	11,420	11,420	-	4,654	16,074
Other comprehensive loss	-	-	-	-	(8,800)	(35)	-	(8,835)	-	(370)	(9,205)
Total comprehensive (loss) income for the year	-	-	-	-	(8,800)	(35)	11,420	2,585	-	4,284	6,869
Issue of share capital (Note 19)	15,000	-	-	-	-	-	-	15,000	-	-	15,000
Transfer upon disposal of investments carried at fair value through other comprehensive income	-	-	-	-	8,215	-	(8,215)	-	-	-	-
Interest payment on Tier 1 capital	-	-	-	-	-	-	(3,513)	(3,513)	-	-	(3,513)
Transfers during the year	-	-	1,142	1,142	-	-	(2,284)	-	-	-	-
Dilution in ownership in a subsidiary (note 5)	-	-	-	-	4,697	-	5,185	9,882	-	(9,882)	-
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	(208)	(208)
Balance at 31 December 2019	**116,132**	**5,687**	**52,032**	**31,763**	**(6,009)**	**(4,569)**	**15,911**	**210,947**	**33,000**	**89,057**	**333,004**
Balance at 1 January 2018	101,132	5,687	49,881	29,612	12,867	(3,871)	7,659	202,967	33,000	26,902	262,869
Transition adjustment on adoption of IFRS 9 at 1 January 2018	-	-	-	-	3,037	-	(4,093)	(1,056)	-	465	(591)
	101,132	5,687	49,881	29,612	15,904	(3,871)	3,566	201,911	33,000	27,367	262,278
Profit for the year	-	-	-	-	-	-	10,093	10,093	-	1,021	11,114
Other comprehensive loss for the year	-	-	-	-	(20,835)	(663)	-	(21,498)	-	(3,451)	(24,949)
Total comprehensive (loss) income for the year	-	-	-	-	(20,835)	(663)	10,093	(11,405)	-	(2,430)	(13,835)
Transfer upon disposal of investments carried at fair value through other comprehensive income	-	-	-	-	(5,190)	-	5,190	-	-	-	-
Interest payment on Tier 1 capital	-	-	-	-	-	-	(3,513)	(3,513)	-	-	(3,513)
Transfers during the year	-	-	1,009	1,009	-	-	(2,018)	-	-	-	-
Acquisition of a subsidiary	-	-	-	-	-	-	-	-	-	78,557	78,557
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	(8,631)	(8,631)
Balance at 31 December 2018	101,132	5,687	50,890	30,621	(10,121)	(4,534)	13,318	186,993	33,000	94,863	314,856

The attached explanatory notes 1 to 34 form part of these consolidated financial statements

1 INCORPORATION AND PRINCIPAL ACTIVITIES

Incorporation

United Gulf Bank B.S.C. (c) ("UGB" or "the Bank") is a closed joint stock company incorporated in the Kingdom of Bahrain in 1980, under Commercial Registration number 10550. The address of the Bank's registered office is UGB Tower, Diplomatic Area, P.O. Box 5964, Manama, Kingdom of Bahrain.

The Bank operates in the Kingdom of Bahrain under a Wholesale Banking License issued by the Central Bank of Bahrain ("the CBB").

Activities

The principal activities of the Bank and its subsidiaries (together the "Group") comprise of investment and commercial banking. Investment banking include asset portfolio management, corporate finance, advisory, investment in quoted and private equity / funds, real estate, capital markets, international banking and treasury functions. Commercial banking includes extending loans and other credit facilities, accepting deposits and current accounts from corporate and institutional customers.

The Bank's parent company is United Gulf Holding Company B.S.C. ("UGH") which owns 100% shares of the Bank and ultimate holding company is Kuwait Projects Company (Holding) K.S.C. ("KIPCO"). UGH is incorporated in the Kingdom of Bahrain as a joint stock company and is listed on the Bahrain Bourse. KIPCO is incorporated in the State of Kuwait and is listed on the Kuwait Stock Exchange (Boursa Kuwait).

These consolidated financial statements were authorised for issue by the Board of Directors on 26 February 2020.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and the relevant provisions of the CBB and Financial Institutions Law and the Bahrain Commercial Companies Law, and the CBB Rulebook (Volume 1 and applicable provisions of Volume 6) and CBB directives.

Basis of preparation

The consolidated financial statements have been prepared on a historical cost basis, except for derivative financial instruments, investment properties, other financial assets held for trading and financial assets designated at fair value through profit or loss (FVTPL) and equity instruments at fair value through other comprehensive income (FVOCI) all of which have been measured at fair value.

Certain of the prior year figures have been reclassified to conform to the presentation adopted in the current year. Such reclassification did not affect the previously reported net profit or the total equity of the Group.

Presentation and functional currency

The consolidated financial statements have been presented in United States Dollar (US$) which is also the functional currency of the Group and are rounded to the nearest US$ thousands except when otherwise indicated.

New and amended standards and interpretations

The accounting policies used in the preparation of these consolidated financial statements are consistent with those used in previous year, except for the adoption of the following new standards or amendments to existing standards applicable to the Group, and which are effective for annual periods beginning on or after 1 January 2019:

IFRS 16 Leases (IFRS 16)

IFRS 16 supersedes IAS 17 Leases, IFRIC 4 Determining whether an Arrangement contains a Lease, SIC-15Operating Leases-Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. The standard sets out the principles for the recognition, measurement, presentation and disclosure of leases and requires lessees to recognise most leases on the statement of financial position.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

New and amended standards and interpretations (continued)

IFRS 16 Leases (IFRS 16) (continued)
Lessor accounting under IFRS 16 is substantially unchanged from IAS 17. Lessors will continue to classify leases as either operating or finance leases using similar principles as in IAS 17. Therefore, IFRS 16 did not have an impact for leases where the Group is the lessor.

The Group adopted IFRS 16 using the modified retrospective method of adoption with the date of initial application of 1 January 2019. Under this method, the standard is applied retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application. The Group elected to use the transition practical expedient allowing the standard to be applied only to contracts that were previously identified as leases applying IAS 17 and IFRIC 4 at the date of initial application. The Group also elected to use the recognition exemptions for lease contracts that, at the commencement date, have a lease term of 12 months or less and do not contain a purchase option ('short-term leases'), and lease contracts for which the underlying asset is of low value ('low-value assets').

The Group is primarily a lessor, and all lease contracts where the Group is a lessee are either short-term leases or the underlying assets are low-value assets.

Short-term leases and leases of low-value assets
The Group applies the short-term lease recognition exemption to its short-term leases (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of office equipment that are considered of low value. Lease payments on short-term leases and leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

Amendments to IAS 28: Long-term interests in associates and joint ventures
The amendments clarify that an entity applies IFRS 9 to long-term interests in an associate or joint venture to which the equity method is not applied but that, in substance, form part of the net investment in the associate or joint venture (long-term interests). This clarification is relevant because it implies that the expected credit loss model in IFRS 9 applies to such long-term interests.

The amendments also clarified that, in applying IFRS 9, an entity does not take account of any losses of the associate or joint venture, or any impairment losses on the net investment, recognised as adjustments to the net investment in the associate or joint venture that arise from applying IAS 28 *Investments in Associates and Joint Ventures.*

Annual Improvements 2015-2017 Cycle

IFRS 3 Business Combinations
The amendments clarify that, when an entity obtains control of a business that is a joint operation, it applies the requirements for a business combination achieved in stages, including remeasuring previously held interests in the assets and liabilities of the joint operation at fair value. In doing so, the acquirer remeasures its entire previously held interest in the joint operation.

An entity applies those amendments to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 January 2019, with early application permitted. These amendments had no impact on the consolidated financial statements of the Group as there is no transaction where a joint control is obtained.

Several other amendments and interpretations apply for the first time in 2019, but do not have an impact on the consolidated financial statements of the Group.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation
The consolidated financial statements include the financial statements of the Bank and its subsidiaries as at 31 December 2019. The reporting dates of the subsidiaries and the Bank are identical and the subsidiaries' accounting policies conform to those used by the Bank for like transactions and events in similar circumstances.

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. 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. 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 financial statements 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:

a) Derecognises the assets (including goodwill) and liabilities of the subsidiary;
b) Derecognises the carrying amount of any non-controlling interest;
c) Derecognises the cumulative transaction differences, recorded in equity;
d) Recognises the fair value of consideration received;
e) Recognises the fair value of any investment retained;
f) Recognises any surplus or deficit in the consolidated statement of income; and
g) Reclassifies the parent's share of a component previously recognised in OCI to consolidated statement of income or retained earnings, as appropriate, as would be required if the Group had directly disposed of the related assets or liabilities.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation (continued)

The principal subsidiaries of the Bank are as follows:

Name of the subsidiary	*Country of incorporation*	*Ownership at 31 December 2019*	*2018*	*Year of incorporation*
Held directly				
KAMCO Investment Company K.S.C.P. [KAMCO]	Kuwait	**60%**	86%	1998
United Gulf Financial Services Company-North Africa	Tunisia	**84%**	84%	2008
United Gulf Realty International, Ltd [UGRIL]	British Virgin Islands	**100%**	100%	2012
United Gulf Asset Company S.P.C.	Bahrain	**100%**	100%	2017
Held through KAMCO				
Al Dhiyafa United Real Estate Company W.L.L.	Kuwait	**100%**	100%	2007
Al Jazi Money Market Fund	Kuwait	**51%**	51%	2007
Al Tadamon United Holding Co	Kuwait	**100%**	96%	2017
Al Zad Real Estate W.L.L.	Kuwait	**100%**	99%	2007
Bukeye Power Project Advisory Co	U.S.A.	**50%**	50%	2017
Bukeye Power Project Manager Ltd	Jersey	**100%**	100%	2017
Carnation Advisory Company LLC	U.S.A.	**75%**	75%	2018
Carnation Manager limited	U.K.	**100%**	100%	2018
First Brokerage	Kuwait	**93%**	-	1985
Flint Advisor Company LLC	Jersey	**46%**	46%	2017
Flint Manager Ltd	U.S.A.	**100%**	100%	2017
Global Investment House	Kuwait	**-**	71%	1998
Global DIFC	Kuwait	**100%**	-	2013
Global Saudi	Saudi Arabia	**100%**	-	2016
KAMCO Egypt Holding Ltd	U.A.E.	**100%**	100%	2018
Kamco GCC Opportunistic Fund	Kuwait	**100%**	100%	2013
KAMCO Investment Company (DIFC) Limited	U.A.E.	**100%**	100%	2016
KAMCO MENA Plus (DIFC)	U.A.E.	**100%**	100%	2019
KAMCO Mena Plus Fixed Income Fund	Kuwait	**-**	38%	2016
Kubbar United Real Estate Co	Kuwait	**100%**	-	2017
Kuwait Private Equity Opportunity Fund	Kuwait	**73%**	73%	2004
Nawasi United Holding Co	Kuwait	**100%**	96%	2017
North Africa Real Estate Co.	Kuwait	**100%**	100%	2014
Plans United Real Estate Co	Kuwait	**100%**	-	2017
Project Plaza Investor Inc	U.S.A.	**100%**	-	2019
S17P02V Holding Ltd	U.A.E.	**-**	100%	2018
Shuroq Investment Services	Oman	**77%**	-	1998

Business combinations

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non controlling interest in the acquiree either at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition costs incurred are expensed and included in administrative expenses.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the acquisition date fair value of the acquirer's previously held equity interest in the acquiree is remeasured to fair value at the acquisition date through the consolidated statement of income. It is then considered in the determination of goodwill.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Business combinations (continued)
Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability that is a financial instrument and within the scope of IAS 39 Financial Instruments: Recognition and Measurement, is measured at fair value with the changes in fair value recognised in the consolidated statement of income.

Goodwill and other Intangible assets

Goodwill
Goodwill represents the excess of the cost of acquisition over the Group's share of the fair value of the net identifiable assets of the acquired subsidiary or associate at the date of the acquisition. Goodwill arising on the acquisition of an associate is included in the carrying amount of the respective associate and, therefore, is not separately tested for impairment. Goodwill arising on the acquisition of a subsidiary is recognised as a separate asset in the consolidated statement of financial position.

Goodwill acquired in a business combination is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interests, and any previous interest held, over the Bank's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired.

If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the Group re-assesses whether it has correctly identified all of the assets acquired and all of the liabilities assumed and reviews the procedures used to measure the amounts to be recognised at the acquisition date. If the re-assessment still results in an excess of the fair value of net assets acquired over the aggregate consideration transferred, then the gain is recognised in the consolidated statement of income.

After initial recognition, goodwill is stated at cost less any accumulated impairment losses. Goodwill of subsidiaries is allocated to cash-generating units and is tested annually for impairment. If the recoverable amount of the cash generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro-rata on the basis of the carrying amount of each asset in the unit. The recoverable amount of a cash-generating unit is the higher of the cash-generating unit's fair value less costs to sell, and its value in use. Any impairment loss recognised for goodwill is not reversed in a subsequent period.

On disposal of a part of a subsidiary, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

Other Intangible assets
Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and accumulated impairment losses.

The useful lives of intangible assets are assessed as either finite or infinite.

Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the consolidated statement of income in the expense category that is consistent with the function of the intangible assets.

An intangible asset is derecognised upon disposal (i.e., at the date the recipient obtains control) or when no future economic benefits are expected from its use or disposal. Any gain or loss arising upon derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated statement of income.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments in associates
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.

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

The Group's investments in its associates are accounted for using the equity method.

Under the equity method, the investment in an associate 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 since the acquisition date. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

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

The financial statements of associates are prepared for the same reporting period as that of 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 investments in its associates. At each reporting date, the Group determines whether there is objective evidence that an investment in an associate is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value, then recognises the loss as 'Share of results of associates' in the consolidated statement of income.

Upon loss of significant influence over an associate, the Group measures and recognises any retained investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognised in the consolidated statement of income.

Financial instruments
A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Date of recognition
Financial assets and liabilities, with the exception of loans and receivables, due to banks and other financial institutions and deposits from customers, are initially recognised on the trade date, i.e., the date that the Group becomes a party to the contractual provisions of the instrument. This includes regular way trades: 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. Loans and receivables are recognised when funds are transferred to the customers' accounts. The Group recognises due to banks and other financial institutions and deposits from customers when funds are transferred to the Group.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Initial measurement
The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. At initial recognition, the Group measures a financial asset or financial liability at its fair value plus or minus, in the case of a financial asset or financial liability not at FVTPL, transaction costs that are incremental and directly attributable to the acquisition or issue of the financial asset or financial liability, such as fees and commissions. Transaction costs of financial assets and financial liabilities carried at FVTPL are expensed in consolidated income. Immediately after initial recognition, an ECL is recognised for financial assets measured at amortised cost and investments in debt instruments measured at FVOCI, which results in an accounting loss being recognised in the consolidated statement of income when an asset is newly originated.

When the fair value of financial assets and liabilities at initial recognition differs from the transaction price, the Group accounts for the Day 1 profit or loss as follows:

(a) When the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses data only from observable markets, the difference is recognised as a day 1 gain or loss.
(b) In all other cases, the difference is deferred and the timing of recognition of deferred day 1 profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or when the instrument is derecognised.

Measurement categories of financial assets and liabilities
The Group classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost.
- Fair value through other comprehensive income (FVOCI); or
- Fair value through profit or loss (FVTPL);

The Group classifies and measures its derivative and trading portfolio at FVTPL. The Group may designate financial instruments at FVTPL, if so doing eliminates or significantly reduces measurement or recognition inconsistencies.

Financial liabilities, other than loan commitments and financial guarantees, are measured at amortised cost or at FVTPL when they are derivative instruments.

Financial assets

Classification and subsequent measurement
The classification requirements for financial assets is as below:

Debt type Instrument: Classification and Subsequent measurement:
Classification and subsequent measurement of debt instruments depend on:
(i) the Group's business model for managing the asset; and
(ii) the cash flow characteristics of the asset i.e. solely payments of principal and interest (SPPI) test.

Based on these factors, the Group classifies its debt instruments into one of the following three measurement categories:

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent SPPI, and that are not designated at FVTPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any ECL allowance recognised. Interest income from these financial assets is included in 'Interest income' using the EIR method.

- FVOCI: Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent SPPI, and that are not designated at FVTPL, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortised cost which are recognised in consolidated statement of income. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to consolidated income and recognised in 'Investment income - net' as 'Gain on disposal of non-trading securities'. Interest income from these financial assets is included in 'Interest income' using the EIR method.

- FVTPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at FVTPL and is not part of a hedging relationship is recognised in consolidated profit or loss and presented in the consolidated statement of income within 'Investment income - net' as 'Gain on trading securities' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Investment income - net' as 'Gain on disposal of non-trading securities'. Interest income from these financial assets is included in 'Interest income' using the EIR method.

Business model

The Group determines its business model at the level that best reflects how it manages groups of financial assets to achieve its business objective. The business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'held for trading' business model and measured at FVTPL. The business model assessment is not carried out on an instrument-by-instrument basis but at the aggregate portfolio level and is based on observable factors such as:

- 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, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realizing cash flows through the sale of the assets;
- How the asset's and business model performance is evaluated and reported to key management personnel and Asset and Liability Committee (ALCO);
- How risks are assessed and 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.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Group's original expectations, the Group does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

Financial assets that are held for trading 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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

SPPI test
As a second step of its classification process the Group assesses the contractual terms of financial assets to identify whether they meet the SPPI test.

Principal for the purpose of this test is defined as the fair value of the financial asset at initial recognition and may change over the life of the financial asset (for example, if there are repayments of principal or amortisation of the premium/discount).

Interest is the consideration for the time value of money, credit risk, other basic lending risks and a profit margin that is consistent with a basic lending arrangement.

In assessing whether the contractual cash flows are SPPI, 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:

- the currency in which the financial asset is denominated, and the period for which the interest rate is set;
- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms; and
- terms that limit the Group's claim to cash flows from specified assets (e.g. non-recourse asset arrangements).

Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at FVTPL.

The Group reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent.

Equity type instruments: classification and subsequent measurement
Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

Equity instruments at FVOCI
Upon initial recognition, the Group may elect to classify irrevocably some of its equity investments as equity instruments at FVOCI when they meet the definition of Equity under *IAS 32 Financial Instruments: Presentation* and are not held for trading. Such classification is determined on an instrument-by-instrument basis. Fair value gains and losses are recognised in other comprehensive income and are not subsequently reclassified to consolidated income, including on disposal. Equity investments at FVOCI are not subject to impairment assessment. Equity investments at FVOCI are included in non-trading investments in the statement of financial position. All other equity investments which the Group has not irrevocably elected at initial recognition or transition, to classify at FVOCI, are recognised at FVTPL.

Financial asset at FVTPL
The Group classifies financial assets at fair value through profit and loss when they have been purchased or issued primarily for short-term profit making through trading activities or form part of a portfolio of financial instruments that are managed together, for which there is evidence of a recent pattern of short-term profit taking. Held-for-trading assets are recorded and measured in the statement of financial position at fair value. 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. Changes in fair values gain and losses, financing income and dividends are recorded in consolidated statement of income according to the terms of the contract, or when the right to payment has been established.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial assets (continued)

Financial asset at FVTPL (continued)
Dividends are recognised in the consolidated statement of income as 'Investment income - net' when the Group's right to receive payments is established.

Impairment
The Group assesses on a forward-looking, basis the ECL associated with its debt instrument assets carried at amortised cost and FVOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

To calculate ECL, the Group estimates the risk of a default occurring on the financial instrument during its expected life. ECLs are estimated based on the present value of all cash shortfalls over the remaining expected life of the financial asset, i.e., the difference between: the contractual cash flows that are due to the Group under the contract, and the cash flows that the Group expects to receive, discounted at the effective interest rate of the loan or an approximation thereof.

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: estimates the expected portion of the loan commitment that are drawn down over the expected life of the loan commitment; and calculates the present value of cash shortfalls between the contractual cash flows that are due to the entity if the holder of the loan commitment draws down that expected portion of the loan and the cash flows that the entity expects to receive if that expected portion of the loan is drawn down; and
- financial guarantee contracts: estimates the ECLs based on the present value of the expected payments to reimburse the holder for a credit loss that it incurs less any amounts that the guarantor expects to receive from the holder, the debtor or any other party. If a loan is fully guaranteed, the ECL estimate for the financial guarantee contract would be the same as the estimated cash shortfall estimate for the loan subject to the guarantee.

For the purposes of calculation of ECL, the Group categorises its FVOCI debt securities, loans and receivable and loan commitments and financial guarantee contracts into Stage 1, Stage 2 and Stage 3, based on the applied impairment methodology, as described below:

- Stage 1 – Performing: when loans are first recognised, the Group recognises an allowance based up to 12-month ECL.
- Stage 2 – Significant increase in credit risk: when a loan shows a significant increase in credit risk, the Group records an allowance for the lifetime ECL.
- Stage 3 – Impaired: the Group recognises the lifetime ECL for these loans.

For the purposes of categorisation into above stages, the Group has established a policy to perform an assessment at the end of each reporting period of whether credit risk has increased significantly since initial recognition by considering the change in the risk of default occurring over the remaining life of the financial instrument.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment (continued)

Measurement of ECL (continued)
The Group records impairment for FVOCI debt securities, depending on whether they are classified as Stage 1, 2, or 3, as explained above. However, the ECL does not reduce the carrying amount of these financial assets in the statement of financial position, which remains at fair value. Instead, an amount equal to the allowance that would arise if the asset were measured at amortised cost is recognised in OCI as an accumulated impairment amount, with a corresponding charge to profit or loss.

No impairment is recorded on equity investments.

Stage 1
The Group measures loss allowances at an amount up to 12-month ECL for Stage 1 customers. All financial assets are classified as Stage 1 on initial recognition date. Subsequently on each reporting date the Group classifies following as Stage 1:

- debt type assets that are determined to have low credit risk at the reporting date; and
- on which credit risk has not increased significantly since their initial recognition.

Stage 2
IFRS 9 requires financial assets to be classified in Stage 2 when their credit risk has increased significantly since their initial recognition. For these assets, a loss allowance needs to be recognised based on their lifetime ECLs.

The Group considers whether there has been a significant increase in credit risk of an asset by comparing the rating migration upon initial recognition of the asset against the risk of a default occurring on the asset as at the end of each reporting period. In each case, this assessment is based on forward-looking assessment that takes into account a number of economic scenarios, in order to recognise the probability of higher losses associated with more negative economic outlooks.

It is the Group's policy to evaluate additional available reasonable and supportive forward-looking information as further additional drivers.

Stage 3
Financial assets are included in Stage 3 when there is objective evidence that the loan is credit impaired. At each reporting date, the Group assesses whether financial assets carried at amortized cost and debt financial assets carried at FVOCI are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have 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 reorganization; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment. In addition, a loan that is overdue for 90 days or more is considered impaired.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment (continued)

Stage 3 (continued)
In making an assessment of whether an investment in sovereign debt 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 country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

Other than originated credit-impaired loans, loans are transferred from out of Stage 3 if they no longer meet the criteria of credit-impaired after a probation period of 12 months.

Forward looking information
The Group incorporates forward-looking information in the measurement of ECLs.

The Group considers forward-looking information such as macroeconomic factors (e.g., GDP growth, oil prices, country's equity indices and unemployment rates) and economic forecasts.

The Group uses internal information coming from internal economic experts, combined with published external information from government and private economic forecasting services. These forward looking assumptions undergo an internal governance process before they are applied for different scenarios.

Presentation of allowance for ECL in the statement of financial position
Loss allowances for ECL are presented in the consolidated statement of financial position as follows:
- financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: as a provision under other liabilities; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the consolidated 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 cumulative changes in fair value reserve.

Limitation of estimation techniques
The models applied by the Group may not always capture all characteristics of the market at a point in time as they cannot be recalibrated at the same pace as changes in market conditions. Interim adjustments are expected to be made until the base models are updated. Although the Group uses data that is as current as possible, models used to calculate ECLs are based on data that is up to date except for certain factors for which the data is updated once it is available and adjustments are made for significant events occurring prior to the reporting date.

Experienced credit adjustment
The Group's ECL allowance methodology requires the Group to use its experienced credit judgement to incorporate the estimated impact of factors not captured in the modelled ECL results, in all reporting periods.

For more details on the impairment calculations and policy refer to note 4 to these consolidated financial statements.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivatives and hedging activities
A derivative is a financial instrument or other contract with all three of the following characteristics:

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided that, in the case of a non-financial variable, it is not specific to a party to the contract (i.e., the 'underlying').
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts expected to have a similar response to changes in market
- It is settled at a future date.

The Group enters into derivative transactions with various counterparties. These include interest rate swaps and forward foreign exchange contracts. Derivatives are initially recognised at fair value on the date on which the derivative contract is entered into and are subsequently remeasured at fair value. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated and qualifies as a hedging instrument, and if so, the nature of the item being hedged. The Group designates certain derivatives as either:

(a) Hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedges);
(b) Hedges of highly probable future cash flows attributable to a recognised asset or liability (cash flow hedges); or
(c) Hedges of a net investment in a foreign operation (net investment hedges).

The Group documents, at the inception of the hedge, the relationship between hedged items and hedging instruments, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

(a) Fair value hedge
Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the consolidated statement of income, together with changes in the fair value of the hedged asset or liability that are attributable to the hedged risk.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective interest method is used is amortised to profit or loss over the period to maturity and recorded as net interest income.

(b) Cash flow hedge
The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income. The gain or loss relating to the ineffective portion is recognised immediately in the consolidated statement of income.

Amounts accumulated in equity are recycled to the consolidated statement of income in the periods when the hedged item affects income or loss. They are recorded in the income or expense lines in which the revenue or expense associated with the related hedged item is reported.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised in the periods when the hedged item affects income or loss. When a forecast transaction is no longer expected to occur (for example, the recognised hedged asset is disposed of), the cumulative gain or loss previously recognised in other comprehensive income is immediately reclassified to the consolidated statement of income.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivatives and hedging activities (continued)

(c) Net investment hedge
Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised directly in other comprehensive income; the gain or loss relating to the ineffective portion is recognised immediately in the consolidated statement of income. Gains and losses accumulated in equity are included in the consolidated statement of income when the foreign operation is disposed of as part of the gain or loss on the disposal.

The Group did not have any impact on its retained earnings or profit or loss due to change in hedge accounting under IFRS 9.

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 loan, 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 amounts 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 cross-currency swaps, notional amounts are exchanged in different currencies. For cross-currency interest rate swaps, notional amounts and fixed and floating interest payments 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.

Derivative related credit risk
Credit risk in respect of derivative financial instruments arises from the potential for a counterparty to default on its contractual obligations and is limited to the positive fair value of instruments that are favourable to the Group. The majority of the Group's derivative contracts are entered into with other financial institutions and there is no significant concentration of credit risk in respect of contracts with positive fair value with any individual counterparty at the date of the statement of financial position.

Derivatives held or issued for trading purposes
Most of the Group's derivative trading activities relate to entering into forward contracts with external counterparties on behalf of UGHC.

Derivatives held or issued for hedging purposes
The Group has adopted a comprehensive system 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. The Board has established levels of currency risk by setting limits on currency position exposures. Positions are monitored on an ongoing basis and hedging strategies used to ensure positions are maintained within established limits. The Board has established levels of interest rate risk by setting limits on the interest rate gaps for stipulated periods. Interest rate gaps are reviewed on an ongoing basis and hedging strategies used to reduce the interest rate gaps to within the limits established by the Board of Directors.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivatives held or issued for hedging purposes (continued)
As part of its asset and liability management the Group uses derivatives for hedging purposes in order to reduce its exposure to currency and interest rate risks. This is achieved by hedging specific financial instruments, forecasted transactions as well as strategic hedging against overall statement of financial position exposures. For interest rate risk this is carried out by monitoring the duration of assets and liabilities using simulations to estimate the level of interest rate risk and entering into interest rate swaps and futures to hedge a proportion of the interest rate exposure, where appropriate. Since strategic hedging does not qualify for special hedge accounting related derivatives are accounted for as trading instruments.

The Group uses forward foreign exchange contracts and currency swaps to hedge against specifically identified currency risks. In addition, the Group uses interest rate swaps to hedge against the interest rate risk arising from specifically identified loans and securities bearing fixed interest rates. In all such cases the hedging relationship and objective, including details of the hedged item and hedging instrument, are formally documented and the transactions are accounted for as hedges.

The Group applies hedge accounting in three separate hedging strategies, as follows:

Interest rate risk on fixed rate debt type instruments (fair value hedge)
The Group holds a portfolio of long-term variable and fixed rate loans / securities and therefore is exposed to changes in fair value due to movements in market interest rates. The Group manages this risk exposure by entering into pay fixed / receive floating interest rate swaps.

Only the interest rate risk element is hedged and therefore other risks, such as credit risk, are managed but not hedged by the Group. The interest rate risk component is determined as the change in fair value of the long-term variable / fixed rate loans and securities arising solely from changes in LIBOR (the benchmark rate of interest). Such changes are usually the largest component of the overall change in fair value. This strategy is designated as a fair value hedge and its effectiveness is assessed by comparing changes in the fair value of the loans attributable to changes in the benchmark rate of interest with changes in the fair value of the interest rate swaps.

The Group establishes the hedging ratio by matching the notional of the derivatives with the principal of the portfolio being hedged. Possible sources of ineffectiveness are as follows:

(i) differences between the expected and actual volume of prepayments, as the Group hedges to the expected repayment date taking into account expected prepayments based on past experience;
(ii) hedging derivatives with a non-zero fair value at the date of initial designation as a hedging instrument; and
(iii) counterparty credit risk which impacts the fair value of uncollateralised interest rate swaps but not the hedged items.

Net investment in foreign operation (net investment hedge)
The Group has investments in foreign operations which are consolidated in these financial statements. The foreign exchange rate exposure arising from this investment is hedged through the use of forward exchange contracts. These contracts are designated as net investment hedges to hedge the equity of the foreign operations. The Group establishes the hedging ratio by matching the contracts with the net assets of the foreign operations.

Hedge ineffectiveness
Hedge effectiveness is determined at the inception of the hedge relationship, and through periodic prospective effectiveness assessments to ensure that an economic relationship exists between the hedged item and hedging instrument. For hedges of exposures to fluctuations in foreign exchange rates, the Group enters into hedge relationships where the critical terms of the hedging instrument match exactly with the terms of the hedged item. The Group therefore performs a qualitative assessment of effectiveness.

In hedges of foreign currency exposures, ineffectiveness may arise if the timing of the cash flows changes from what was originally estimated, or if there are changes in the credit risk of the Bank or the derivative counterparty.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Hedge ineffectiveness (continued)
The Group enters into interest rate swaps that have similar critical terms as the hedged item, such as reference rate, reset dates, payment dates, maturities and notional amount. In cases, where the Group does not hedge 100% of its loans, the hedged item is identified as a proportion of the outstanding loans up to the notional amount of the swaps. As all critical terms matched during the year, the economic relationship was 100% effective.

Hedge ineffectiveness for interest rate swaps is assessed using the same principles as for hedges of foreign currency. It may occur due to the credit value/debit value adjustment on the interest rate swaps which is not matched by the loan, and differences in critical terms between the interest rate swaps and loans.

There was no ineffectiveness during 2019 or 2018 in relation to the interest rate swaps.

Interest income
Under both IFRS 9 and IAS 39, interest income is recorded using the effective interest rate (EIR) method for all financial instruments measured at amortised cost, financial instruments designated at FVTPL. Interest income on interest bearing financial assets measured at FVOCI under IFRS 9, similarly to interest bearing financial assets classified as available-for-sale or held to maturity under IAS 39 are also recorded by using the EIR method. The EIR is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset.

Fair value measurement
A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

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.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

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: valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable; and
Level 3: valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurement (continued)

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.

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.

The Group measures financial instruments, such as, derivatives, and non-financial assets such as investment properties, at fair value at each reporting date.

For financial instruments traded in an active market, fair value is determined by reference to quoted market bid prices for assets and quoted market offer prices for liabilities, without deduction for transaction costs. The fair value of investments in managed funds or similar investment vehicles, where available, are based on last published bid price.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indications that a market is inactive are when there is a wide bid-offer spread or significant increase in the bid-offer spread or there are few recent transactions.

For financial instruments where there is no active market, fair value is determined using appropriate valuation techniques. Such techniques may include the following:

- brokers' quotes
- recent arm's length market transactions
- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics
- option pricing models
- other valuation methods

Financial instruments with no active market and where fair value can not be reliably determined are stated at cost less provision for any impairment.

The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount payable on demand.

The fair value of forward foreign exchange contracts is determined using forward exchange rates at the statement of financial position date with the resulting value discounted back to present value.

The fair value of interest rate swaps is determined by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

Derecognition

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

(a) the right to receive cash flows from the asset have expired;
(b) the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement; or
(c) the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition (continued)

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. 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. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to consolidated statement of income.

Investment properties

All properties held for rental or for capital appreciation purposes, or both, are classified as investment properties. Where a property is partially occupied by the Group and the portions could be sold separately, the Group accounts for the portions separately either as an investment property or property and equipment, as appropriate. If the portions cannot be sold separately, the property is classified as an investment property only if an insignificant portion is held for own use.

The Group applies the fair value model of accounting for investment properties. All investment properties are initially recorded at cost, including acquisition expenses associated with the property.

Subsequent to initial recognition, all investment properties are remeasured at fair value and changes in fair value are recognised in the consolidated statement of income. The Group engages independent valuation specialists to determine the fair value of investment properties. Fair values are determined based on an annual evaluation performed by an accredited external independent valuer applying a valuation model recommended by the International Valuation Standards Committee.

Investment properties are derecognised either when they have been disposed of or when they are permanently withdrawn from use and no future economic benefit is expected from their disposal. The difference between the net disposal proceeds and the carrying amount of the asset is recognised in profit or loss in the period of derecognition.

Transfers are made to (or from) investment property only when there is a change in use. For a transfer from investment property to owner-occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner-occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under property, plant and equipment up to the date of change in use.

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and impairment losses. When assets are sold or retired, their cost and accumulated depreciation are eliminated from the consolidated statement of financial position and any gain or loss resulting from disposal is included in the consolidated statement of income.

The carrying values of property and equipment are reviewed for impairment when events or changes in circumstances indicate the carrying value may not be recoverable. If any such indication exists and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount, being the higher of their fair value less costs to sell and their value in use.

Depreciation is provided on all property and equipment, except land and work in progress, at rates calculated to write off the cost of each asset on a straight line basis to their residual values over its expected useful life which is between 3 to 5 years for all property and equipment except for certain building fixtures and fittings which are depreciated over expected useful life of 10 years and building civil structure which is depreciated over its expected useful life of 20 years.

The assets' residual values, useful lives and methods of depreciation are reviewed at each financial year end and adjusted prospectively, if appropriate.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial liabilities
Financial liabilities comprise of due to banks and other financial institutions, deposits from customers, loans, bonds and subordinated debt and other liabilities. These are stated at amortised cost. Transaction costs are amortised over the period of the debt using the effective yield method. Deposits from customers include deposits from both external customers and other group companies.

Classification and subsequent measurement
The accounting for financial liabilities remains largely the same as it was under IAS 39, except for the treatment of gains or losses arising from an entity's own credit risk relating to liabilities designated at FVTPL. Such movements are presented in OCI with no subsequent reclassification to the consolidated statement of income.

Treasury shares and treasury share reserve
Treasury shares are own equity instruments of the Bank which are reacquired by the Bank or any of its subsidiaries. These are stated at cost and deducted from equity. Any gain or loss arising on reissuance of treasury shares is taken directly to treasury share reserve in the consolidated statement of changes in equity.

Cash and cash equivalents
Cash and cash equivalents include cash, demand and call deposits, highly liquid investments that are readily convertible into cash and placements (excluding escrow balances) with original maturities up to ninety days from the date of acquisition.

Fiduciary assets
Assets held in a fiduciary capacity are not treated as assets of the Group in the consolidated statement of financial position.

Dividends on ordinary shares
The Bank recognises a liability to make cash or non-cash distributions to its equity holders when the distribution is authorised and the distribution is no longer at the discretion of the Bank. A distribution is authorised when it is approved by the shareholders. A corresponding amount is recognised directly in equity.

Non-cash distributions are measured at the fair value of the assets to be distributed with fair value re-measurement recognised directly in equity.

Upon distribution of non-cash assets, any difference between the carrying amount of the liability and the carrying amount of the assets distributed is recognised in the consolidated statement of income.

Dividends for the year that are approved after the statement of financial position date are disclosed as an event after the statement of financial position date.

Taxes
There is no tax on corporate income in the Kingdom of Bahrain. Taxation on overseas subsidiaries is calculated on the basis of the tax rates applicable and prescribed according to the prevailing laws, regulations and instructions of the countries where these subsidiaries operate. Income tax payable on taxable profit ("current tax") is recognised as an expense in the period in which the profits arise in accordance with the fiscal regulations of the respective countries in which the Group operates.

Deferred Tax
Deferred tax is provided using the liability method on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date.

Deferred tax assets are recognised for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses. Deferred tax assets are recognised to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised, except when the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Taxes (continued)
The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are re-assessed at each reporting date and are recognised to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax liabilities are recognised for all taxable temporary differences, except:

(a) When the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
(b) In respect of taxable temporary differences associated with investments in subsidiaries and associates, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets and liabilities are measured using tax rates and applicable legislation at the reporting date.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

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 either settle on a net basis, or to realise the asset and settle the liability simultaneously.

Trade and settlement date accounting
All "regular way" purchases and sales of financial assets are recognised on the settlement date, i.e. the date the asset is delivered to the counterparty.

Employees benefits
The Group provides for end of service benefits to all its employees. Entitlement to these benefits is usually based upon the employees' length of service and the completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment. National employees of the Bank are also covered by the Social Insurance Organisation scheme and the Bank's obligations are limited to the amount contributed to the scheme.

Provisions
Provisions are recognised when the Group has a present obligation (legal or constructive) arising from a past event and the costs to settle the obligation are both probable and reliably measurable.

Foreign currencies
The consolidated financial statements have been presented in US Dollars being the functional and presentational currency of the Bank. Each entity in the Group determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

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

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Foreign currencies (continued)

Translation of foreign currency transactions and balances

Monetary assets and liabilities denominated in foreign currencies are retranslated at the functional currency rate of exchange ruling at the reporting date. Exchange differences arising on the retranslation of monetary items, are included in consolidated statement of income for the year. Non-monetary items measured at fair value in a foreign currency are retranslated using the exchange rates at the date when the fair value was determined. Exchange differences arising on the retranslation of non-monetary investments carried at fair value through profit and loss are included in the consolidated statement of income for the year. Exchange differences arising on the retranslation of investments carried at fair value through other comprehensive income, other than those which are carried at cost, are recognised directly in a fair value reserve in the consolidated statement of comprehensive income. Non–monetary items that are measured at historical cost in a foreign currency are translated using the spot exchange rates as at the date of recognition.

Translation of financial statements of foreign operations

Assets (including goodwill) and liabilities of foreign operations are translated at the exchange rates prevailing at the statement of financial position date. Income and expense items are translated at average exchange rates for the relevant period. All resulting exchange differences are taken directly to a foreign currency translation reserve in equity through consolidated OCI.

On disposal of a foreign operation, the component of consolidated OCI relating to that particular foreign operation is recognised in the consolidated statement of income.

Recognition of income and expenses

Interest income and related fees are recognised using the effective yield method, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

Recognition of interest income is suspended when the related financial asset becomes impaired. Notional interest is recognised on impaired financial assets based on the rate used to discount future cash flows to their net present value.

Commission income and other fees are recognised when earned.

Performance-based fees

For revenue from performance-based fees for the provision of services over a period of time, the Group previously accrued revenue over that period. Under IFRS 15, performance-based fees will not be recognised until it is highly probable that a significant reversal in the amount of cumulative revenue will not occur. The recognition of performance-based fees will require significant judgement and are unlikely to be recognised in full until they have crystallised or are no longer subject to clawback.

Advisory income

For revenue from advisory fees for the provision of services over a period of time, the Group previously accrued revenue over that period. Under IFRS 15, the Group applied significant judgement to identify the performance obligations in an advisory service contract and whether each service is capable of being distinct in the context of contract. Revenue from these performance obligations are recognized either at a point in time or over time when the respective performance obligations in a contract are delivered to the customer.

Rental income on investment properties is recognised on a straight line basis.

Dividend income is recognised when the Group's right to receive the dividend is established.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Contingent liabilities and contingent assets
Contingent liabilities are not recognised in the consolidated financial statements, but are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets are not recognised in the consolidated financial statements, but are disclosed when an inflow of economic benefits is probable.

Financial guarantee contracts and commitments
Financial guarantee contracts issued by the Group are those contracts that require a payment to be made to reimburse the holder for a loss it incurs because the specified debtor fails to make a payment when due in accordance with the terms of a debt instrument. Financial guarantee contracts are recognised initially as a liability at fair value, adjusted for transaction costs that are directly attributable to the issuance of the guarantee. Subsequently, the liability is measured at the higher of the best estimate of the expenditure required to settle the present obligation at the reporting date and the amount recognised less cumulative amortisation.

The premium received is recognised in the consolidated statement of profit or loss in other operating income on a straight line basis over the life of the guarantee.

Undrawn loan commitments, under which, over the duration of the commitment, the Group is required to provide a loan with pre-specified terms to the customer. Similar to financial guarantee contracts, under IAS 39, a provision was made if they were an onerous contract but, from 1 January 2019, these contracts are in the scope of the ECL requirements.

The nominal contractual value of financial guarantees and undrawn loan commitments, where the loan agreed to be provided is on market terms, are not recorded in the consolidated statement of financial position.

Significant assumptions, accounting judgements and estimates
In the process of applying the Group's accounting policies, management has made the following assumptions, judgements and estimates in determining the amounts recognised in the consolidated financial statements:

Measurement of the expected credit loss allowance (ECL)
The measurement of the ECL for financial assets measured at amortised cost and FVOCI is an area that requires the use of complex models and significant assumptions about future economic conditions, credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses), estimation of the amount and timing of the future cash flows and collateral values. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Group's ECL calculation are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Internal credit rating model, which assigns PDs to the individual ratings;
- Determining criteria for SICR;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs;
- Selection and relative weightings of forward-looking scenarios to derive the economic inputs into the ECL models;
- Establishing groups of similar financial assets for the purposes of measuring ECL; and
- Determining relevant period of exposure with respect to the revolving facilities and facilities undergoing restructuring at the time of the reporting date.

Classification of financial assets
Classification of financial assets in the appropriate category depends upon the business model and SPPI test. Determining the appropriate business model and assessing whether the cash flows generated by the financial asset meet the SPPI test is complex and requires significant judgements by management.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Significant assumptions, accounting judgements and estimates (continued)
The Group applies judgement while carrying out SPPI test and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

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, 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.

Impairment of goodwill
The Group determines whether goodwill is impaired at each reporting date. This requires an estimation of the value in use of the cash generating units to which the goodwill is allocated. Estimating the value in use requires the Group to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

Fair value of financial instruments
Where the fair values of financial assets and financial liabilities recorded in the statement of consolidated financial position cannot be derived from active markets, they are determined using valuation techniques including discounted cash flow models. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

Loans and receivables
Loans and receivables are non-derivative financial assets originated or acquired by the Group with fixed or determinable payments that are not quoted in an active market.

Loans and receivables are recognised when cash is advanced to borrowers. They are derecognised when either borrower repays their obligations, or the loans are sold or written off, or substantially all the risks and rewards of ownership are transferred.

Loans and receivables are initially measured at cost, being the fair value of the consideration given.

Following initial recognition, loans and receivables are stated at cost less any amount written off and specific and collective provisions for impairment.

When a loan is uncollectible and there is no realistic prospect of recovery, it is written off against the related provision. Subsequent recoveries and reductions in provision are credited to provision for doubtful loans in the consolidated statement of income.

3 NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE

Standards issued but not yet effective up to the date of issuance of the Group's consolidated financial statements are listed below. This listing is of relevant standards and interpretations issued, which the Group reasonably expects to be applicable at a future date. The Group intends to adopt those standards (where applicable) when they become effective:

Amendments to IFRS 3: Definition of a Business
In October 2018, the IASB issued amendments to the definition of a business in IFRS 3 Business Combinations to help entities determine whether an acquired set of activities and assets is a business or not. They clarify the minimum requirements for a business, remove the assessment of whether market participants are capable of replacing any missing elements, add guidance to help entities assess whether an acquired process is substantive, narrow the definitions of a business and of outputs, and introduce an optional fair value concentration test. New illustrative examples were provided along with the amendments.

3 NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE (continued)

Amendments to IAS 1 and IAS 8: Definition of Material
In October 2018, the IASB issued amendments to IAS 1 Presentation of Financial Statements and IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors to align the definition of 'material' across the standards and to clarify certain aspects of the definition. The new definition states that, 'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.'

Since the amendments apply prospectively to transactions or other events that occur on or after the date of first application, the Group will not be affected by these amendments on the date of transition.

4 EXPECTED CREDIT LOSSES

Movement in ECL for the year

	Stage 1 *US$ 000*	*Stage 2* *US$ 000*	*Stage 3* *US$ 000*	*Total* *US$ 000*
As at 31 December 2018	3,446	1,405	10,534	15,385
Adjustment *	10,349	766	(962)	10,153
As at 1 January 2019	13,795	2,171	9,572	25,538
Provided (reversal) during the year - net	728	(1,670)	(673)	(1,615)
Amounts written-off	(430)	-	-	(430)
Other adjustments	37	2	4	43
As at 31 December 2019	**14,130**	**503**	**8,903**	**23,536**

* During the current year, as at 1 January 2019, the Group changed the presentation of certain of its other assets and loans and advances and segregated the related credit losses from gross other assets for disclosures in the consolidated financial statements. As at 31 December 2018, the Group reported these other assets on a net basis.

5 KAMCO MERGER WITH GLOBAL INVESTMENT HOUSE (GIH)

On 21 July 2018, subsequent to acquisition of GIH, KAMCO obtained approval of the Kuwait Capital Market Authority (CMA) to merge GIH by amalgamation with KAMCO, where by the shareholders of GIH will receive shares of KAMCO in exchange. KAMCO will become legal successor of GIH's all rights and obligations on the effective date of the merger.

The Extraordinary General Meeting (EGM) of GIH, held on 18 September 2019 approved the merger between GIH and KAMCO by way of amalgamation, including the dissolution of GIH. Pursuant to which KAMCO became the merging company and GIH became the merged company. The EGM also approved the share swap ratio as noted below.

On 29 September 2019, merger resolution was announced and published in Kuwait Gazette that granted the creditors of GIH the right to object the merger within a period of 30 days from the announcement by serving an official notification to GIH through the court.

No creditor objected the merger, therefore on 30 October 2019, a general public notice of the merger was issued by Ministry of Commerce and Industry, Kuwait ("MOCI") which included the dissolution of GIH. On 21 November 2019, the Capital Market Authority, Kuwait, approved execution of the merger between KAMCO and GIH.

On 12 December 2019, the share swap was executed and this resulted in cancelling of GIH's shareholders' register with Kuwait Clearing Company on the same date. The minority shareholders of GIH received 0.75522821 shares of KAMCO for every share of GIH.

5 KAMCO MERGER WITH GLOBAL INVESTMENT HOUSE (GIH) (continued)

Following the completion of merger all the right and obligation of GIH vested in KAMCO and the legal formalities to transfer ownership of assets and liabilities, changes to contracts where GIH was a party, cancellation of commercial license and license with the Central Bank of Kuwait (CBK) are under process as at the date of these consolidated financial statements. Further, at the close of business on 12 December 2019, GIH transferred all the assets and liabilities to KAMCO.

The Group owned 205,218,583 shares in KAMCO which represented 86.4% of KAMCO's outstanding shares prior to the merger. Subsequent to the merger, the Group effective ownership reduced to 59.95%. However, as the shares were issued at a premium, the Group recorded a gain of US$ 5,185 thousand on the remaining ownership stake in retained earnings.

6 FINANCIAL ASSETS AND LIABILITIES

The table below summarises the accounting classification of the Group's financial assets and financial liabilities:

31 December 2019	*Designated at FVTPL US$ 000*	*Designated at FVOCI US$ 000*	*Amortised cost US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	**71,369**	**71,369**
Placements with banks	-	-	**236,110**	**236,110**
Investments carried at fair value through profit and loss	**97,778**	-	-	**97,778**
Investments carried at fair value through other comprehensive income	-	**131,048**	-	**131,048**
Investments carried at amortised cost	-	-	**280**	**280**
Loans and receivables	-	-	**27,778**	**27,778**
Other assets	-	**148**	**62,174**	**62,322**
Total financial assets	**97,778**	**131,196**	**397,711**	**626,685**
Due to banks and other financial institutions	-	-	**307,784**	**307,784**
Deposits from customers	-	-	**22,647**	**22,647**
Loans payable	-	-	**36,875**	**36,875**
Long term bonds	-	-	**131,948**	**131,948**
Other liabilities	**360**	**269**	**90,336**	**90,965**
Total financial liabilities	**360**	**269**	**589,590**	**590,219**

31 December 2018	*Designated at FVTPL US$ 000*	*Available-for-sale US$ 000*	*Amortised cost / Loans and receivables US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	143,510	143,510
Placements with banks	-	-	108,529	108,529
Investments carried at fair value through profit and loss	81,852	-	-	81,852
Investments carried at fair value through other comprehensive income	-	167,647	-	167,647
Investments carried at amortised cost	-	-	494	494
Loans and receivables	-	-	25,191	25,191
Other assets	-	1,280	58,931	60,211
Total financial assets	81,852	168,927	336,655	587,434
Due to banks and other financial institutions	-	-	220,879	220,879
Deposits from customers	-	-	32,608	32,608
Loans payable	-	-	67,033	67,033
Long Term bonds	-	-	131,739	131,739
Other liabilities	168	208	105,999	106,375
Total financial liabilities	168	208	558,258	558,634

7 INVESTMENTS CARRIED AT FAIR VALUE THROUGH PROFIT AND LOSS

	2019	*2018*
	US$ 000	*US$ 000*
Quoted equities	**13,545**	12,278
Quoted debt securities	**12,245**	6,941
Unquoted equities	**4,335**	3,210
Unquoted debt securities	**825**	-
Managed funds *	**66,828**	59,423
	97,778	81,852

*Managed funds primarily represent funds that invests in unlisted companies and limited partnership interests. The fund managers have created these legal structures for tax efficiency and to meet other investors' requirements. The underlying investments in these funds are primarily in quoted debt and equity instruments in Kuwait and other international markets.

8 INVESTMENTS CARRIED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	2019	*2018*
	US$ 000	*US$ 000*
Unquoted equities	**99,855**	121,418
Quoted equities	**30,187**	45,219
Other managed funds	**1,006**	1,010
	131,048	**167,647**

9 LOANS AND RECEIVABLES

	2019				*2018*
	Stage 1	*Stage 2*	*Stage 3*	*Total*	
	US$ 000	*US$ 000*	*US$ 000*	*US$ 000*	*US$ 000*
Loans to customers	**23,740**	**335**	**8,915**	**32,990**	32,566
Staff loans	**4,843**	**-**	**-**	**4,843**	4,028
	28,583	**335**	**8,915**	**37,833**	36,594
Less: Expected credit losses	**(817)**	**(335)**	**(8,903)**	**(10,055)**	(11,403)
	27,766	**-**	**12**	**27,778**	25,191

The movement in the expected credit losses is as follows:

	Stage 1	*Stage 2*	*Stage 3*	*Total*
	US$ 000	*US$ 000*	*US$ 000*	*US$ 000*
As at 31 December 2018	697	172	10,534	11,403
Adjustment *	-	766	(962)	(196)
As at 1 January 2019	697	938	9,572	11,207
Provided (reversal/recoveries) during the year - net	111	(605)	(673)	(1,167)
Other movements	9	2	4	15
As at 31 December 2019	817	335	8,903	10,055

* During the current year, as at 1 January 2019, the Group changed the presentation of certain of its loans and advances and segregated the related credit losses from gross other assets for disclosures in the consolidated financial statements. As at 31 December 2018, the Group reported these other assets on a net basis.

9 LOANS AND RECEIVABLES (continued)

The table below shows the credit quality of loans and receivables:

	Neither past due nor impaired US$ 000	*Past due and impaired US$ 000*	*Total US$ 000*
31 December 2019			
Loans to customers	**24,075**	**8,915**	**32,990**
Staff loans	**4,843**	**-**	**4,843**
Total	**28,918**	**8,915**	**37,833**

	Neither past due nor impaired US$ 000	*Past due and impaired US$ 000*	*Total US$ 000*
31 December 2018			
Loans to customers	22,032	10,534	32,566
Staff loans	4,028	-	4,028
Total	26,060	10,534	36,594

No ECL is recognised against the Group's exposures to staff loans as these are fully collateralized.

10 OTHER ASSETS

	2019 US$ 000	*2018 US$ 000*
Due from customers	**64,126**	50,677
Accounts receivable	**11,213**	10,897
Prepayments	**611**	886
Interest receivable	**148**	106
Derivative assets (Note 30)	**148**	1,280
Gross other assets	**76,246**	63,846
Less: Expected credit losses	**(13,313)**	(2,749)
	62,933	61,097

The table below reconciles the movement of the ECL from 1 January 2019 and 31 December 2019:

	Stage 1 US$ 000	***Stage 2 US$ 000***	***Stage 3 US$ 000***	***Total US$ 000***
As at 31 December 2018	**2,749**	-	-	**2,749**
Adjustment *	**10,349**	-	-	**10,349**
As at 1 January 2019	**13,098**	-	-	**13,098**
Provided during the year - net	**617**	-	-	**617**
Amounts written-off	**(430)**	-	-	**(430)**
Other movements	**28**	-	-	**28**
As at 31 December 2019	**13,313**	-	-	**13,313**

* During the current year, as at 1 January 2019, the Group changed the presentation of certain of its other assets and segregated the related credit losses from gross other assets for disclosures in the consolidated financial statements. As at 31 December 2018, the Group reported these other assets on a net basis.

11 INVESTMENTS IN ASSOCIATES

		Activity	Carrying value 2019 US$ 000	Ownership 2019 %	Carrying value 2018 US$ 000	Ownership 2018 %
a)	Kamco Investment Fund	Fund	**30,807**	**23**	24,357	23
b)	KAMCO Real Estate Yield Fund	Fund	**13,745**	**38**	14,549	30
c)	N.S. 88	Real estate	**11,424**	**20**	11,570	20
d)	Manafae Investment Company	Islamic investment	**10,951**	**33**	11,202	33
e)	United Capital Transport Co K.S.C.C.	Transport	**8,419**	**40**	9,269	40
f)	Others	Various	**428**	**-**	566	-
			75,774		71,513	

The Group has no share of any contingent liabilities or capital commitments, as at 31 December 2019 and 2018 on behalf of its associates.

a) The Group holds a 23% (2018: 23%) equity interest in KAMCO Investment Fund ("KIF") through its subsidiary KAMCO.

b) The Group holds a 38% (2018: 30%) equity interest in KAMCO Real Estate Yield Fund through its subsidiary KAMCO. The increase in equity interest is due to redemption of the fund's units by other unit holders during the year.

c) The Group owns 20% of N.S. 88 through its subsidiary KAMCO (2018: 20%).

d) The Group owns 33% of Manafae Investment Company through its subsidiary KAMCO (2018: 31%).

e) United Capital Transport Company K.S.C.C. (UniCap) was incorporated in State of Kuwait in 2011. The Group owns a 40% equity interest through its subsidiary KAMCO (2018: 40%). UniCap is a dedicated leasing solutions provider to governments, international oil companies and varied construction, mining and industrial services businesses.

f) Others includes associates with carrying values of under US$ 1 million and mainly include Adhari Park Development with group ownership of 20% (2018: 20%), Fina Corporation 49% (2018: 40%), Lotus Financial Investments 45% (2018: Nil) and United Real Estate Company - Syria 20% (2018: 20%).

In accordance with IAS 36 Impairment of Assets, the Group's recoverable amount of these associates (i.e. value in use) was in excess of their carrying values and accordingly no impairment was recognised against these investments during the year ended 31 December 2019 (2018: same).

11 INVESTMENTS IN ASSOCIATES (continued)

Investments in associates that are not individually significant

As at 31 December 2019 and 2018, all of the Group's investments in associates were not individually significant. The aggregate summarised financial information of the Group's associates that are not individually significant are provided below:

	2019 *US$ 000*	*2018* *US$ 000*
Summarised statement of financial position as of 31 December:		
Total assets	**394,302**	274,625
Total liabilities	**(14,514)**	(5,328)
Equity	**379,788**	269,297
Carrying amount of investments	**75,774**	71,513
Summarised statement of income for the year ended 31 December:		
Revenue	**29,506**	1,824
Profit (loss) for the year	**21,879**	(1,414)
Other comprehensive income for the year	**-**	-
Total comprehensive income (loss) for the year	**21,879**	(1,414)
Group's share of profit (loss) for the year	**4,646**	(764)

12 INVESTMENT PROPERTIES

	2019 *US$ 000*	*2018* *US$ 000*
At 1 January	**107,629**	105,093
Reclassification to Property and Equipment	**(12,734)**	-
Revaluation gain (note 23)	**7,294**	124
Foreign currency translation and other adjustments	**524**	241
Acquired on acquisition of subsidiary	**-**	2,171
At 31 December	**102,713**	107,629

As at 1 January 2019, the Group determined that there is a change in use of a land and building amounting to US$ 12,734 thousand, and the land and building meets the definition of a owner-occupied property under IAS 16 Property, Plant and Equipment. The Group reclassified the land and building from investment properties to property and equipment.

The fair value of the land and building, as of the date of transfer, has been considered to be the deemed cost for subsequent accounting in accordance with IAS 16. The building will be depreciated over 20 years on a straight line basis from the date of transfer.

Investment properties comprise of land and buildings owned by the Group. These are stated at fair values, determined based on independent valuations performed by external professional valuers at the year end.

Valuations of investment properties were conducted by independent appraisers with a recognised and relevant professional qualification and recent experience of the location and category of investment property being valued. The discounted future cash flow method or property market value method have been used as deemed appropriate considering the nature and usage of the properties. The Group's investment properties are categorised in level 3 of the fair value hierarchy as at 31 December 2019 and 2018.

Significant increases (decreases) in estimated rental value and rent growth per annum in isolation would result in a significantly higher (lower) fair value of the properties. Significant increases (decreases) in the long-term vacancy rate and discount rate (and exit yield) in isolation would result in a significantly lower (higher) fair value.

13 PROPERTY AND EQUIPMENT

2019	*Land* *US$ 000*	*Buildings* *US$ 000*	*Furniture and fixtures* *US$ 000*	*Computers and vehicles* *US$ 000*	*Total* *US$ 000*
Cost					
Balance as at 1 January 2019	**16,767**	**55,152**	**19,361**	**17,351**	**108,631**
Reclassification to Property and Equipment (note 12)	**2,734**	**10,000**	**-**	**-**	**12,734**
Additions during the year	**-**	**20**	**1,654**	**432**	**2,106**
Disposals during the year	**-**	**-**	**(2,863)**	**(56)**	**(2,919)**
Exchange rate and other movements	**-**	**-**	**(3)**	**-**	**(3)**
At 31 December 2019	**19,501**	**65,172**	**18,149**	**17,727**	**120,549**
Depreciation					
Balance as at 1 January 2019	**-**	**(35,654)**	**(17,455)**	**(16,128)**	**(69,237)**
Charge for the year	**-**	**(1,296)**	**(633)**	**(457)**	**(2,386)**
Disposals during the year	**-**	**-**	**2,863**	**56**	**2,919**
Exchange rate and other movements	**-**	**-**	**4**	**-**	**4**
At 31 December 2019	**-**	**(36,950)**	**(15,221)**	**(16,529)**	**(68,700)**
Net book value:					
At 31 December 2019	**19,501**	**28,222**	**2,928**	**1,198**	**51,849**
At 31 December 2018	16,767	19,498	1,906	1,223	39,394

14 GOODWILL AND OTHER INTANGIBLE ASSETS

2019	*Goodwill* *US$ 000*	*Customer relationships* *US$ 000*	*Licenses with indefinite useful lives* *US$ 000*	*Total* *US$ 000*
Cost				
Balance as at 1 January 2019	**52,092**	**11,328**	**3,627**	**67,047**
Exchange rate and other movements	**82**	**(33)**	**1**	**50**
At 31 December 2019	**52,174**	**11,295**	**3,628**	**67,097**
Amortisation and impairment				
Balance as at 1 January 2019	**-**	**(413)**	**-**	**(413)**
Amortisation	**-**	**(1,093)**	**-**	**(1,093)**
At 31 December 2019	**-**	**(1,506)**	**-**	**(1,506)**
2018				
Cost				
Balance as at 1 January 2018	52,390	-	-	52,390
Acquired on the acquisition of a subsidiary	-	11,328	3,627	14,955
Foreign currency translation adjustments	(298)	-	-	(298)
At 31 December 2018	52,092	11,328	3,627	67,047
Amortisation and impairment				
Balance as at 1 January 2018	-	-	-	-
Amortisation	-	(413)	-	(413)
At 31 December 2018	-	(413)	-	(413)
Net book value:				
At 31 December 2019	**52,174**	**9,789**	**3,628**	**65,591**
At 31 December 2018	52,092	10,915	3,627	66,634

14 GOODWILL AND OTHER INTANGIBLE ASSETS (continued)

Goodwill

The goodwill remaining as of 31 December relates to KAMCO (a subsidiary) and is allocated to the asset management and investment banking operating segment, a cash generating unit (a CGU). The recoverable amount of the CGU is determined based on a value in use calculation using cash flow projections from financial budgets approved by the Group's senior management covering a five year period. The key assumptions used in the value in use calculation include a perpetuity growth rate of 2% (2018: 3%) and discount factor of 8.3% (2018: 9.5%). There was no goodwill impairment identified in 2019 or 2018 as the recoverable amount of the CGU was higher than its net book value.

The calculation of value in use for the CGU is sensitive primarily to market risk premium, growth risk rate, risk free rate and country risk premium.

The sensitivity of the value in use calculation to changes in key assumptions used in the impairment assessment of goodwill is disclosed below:

	Impact of change	
	+10%	**-10%**
Key assumptions		
Growth rate	**7,633**	**(7,167)**
Discount factor	**(34,724)**	**45,233**

These changes do not result in impairment of goodwill.

Other intangible assets

Customer relationships with finite useful lives have a useful economic life of 10 years each and are amortised on a straight line basis.

15 TAXATION

The Group's subsidiaries in the United States of America were subject to income tax in their respective jurisdictions.

a) Deferred tax liabilities

Deferred tax liabilities relate to the following:

	2019	*2018*
	US$ 000	*US$ 000*
Revaluation of investment properties at fair value	**4,573**	2,666
	4,573	2,666

Reconciliation of deferred tax liabilities is as follows:

	Opening balance	*Recognised in consolidated statement of income*	*Closing balance*
	US$ 000	*US$ 000*	*US$ 000*
2019			
Revaluation of investment properties at fair value	**2,666**	**1,907**	**4,573**
	2,666	**1,907**	**4,573**
2018			
Excess of capital allowances over depreciation	390	(390)	-
Revaluation of investment properties at fair value	2,859	(193)	2,666
	3,249	(583)	2,666

15 TAXATION (continued)

b) Income tax (charge) credit

The major components of income tax (charge) credit for the year ended 31 December are as follows:

	2019	*2018*
	US$ 000	*US$ 000*
Consolidated statement of income		
Current income tax (charge) credit	**(3,934)**	678
Movement in deferred tax liabilities recognised in statement of income	**1,907**	(583)
Income tax (charge) credit reported in the consolidated statement of income - net	**(2,027)**	95

The Group offsets tax assets and liabilities if and only if it has a legally enforceable right to set off current tax assets and current tax liabilities and the deferred tax assets and deferred tax liabilities relate to income taxes levied by the same tax authority.

16 LOANS PAYABLE

31 December 2019	*Currency**	*Subsidiaries US$ 000*	*Total US$ 000*
Maturing within one year			
3 months or less but over 1 month	KWD	**9,896**	**9,896**
1 year or less but over 3 months	KWD	**16,494**	**16,494**
		26,390	**26,390**
Maturing after one year			
More than 2 years	US$	**10,485**	**10,485**
		10,485	**10,485**
		36,875	**36,875**
31 December 2018			
Maturing within one year			
1 month or less	KWD	6,994	6,994
3 months or less but over 1 month	KWD	16,326	16,326
1 year or less but over 3 months	KWD	16,467	16,467
		39,787	39,787
Maturing after one year			
More than 1 year & less than 2 years	KWD	16,467	16,467
More than 2 years	US$	10,779	10,779
		27,246	27,246
		67,033	67,033

* KWD represents Kuwaiti Dinar.

17 LONG TERM BONDS

	2019	*2018*
	US$ 000	*US$ 000*
Fixed interest rate of 6.00% per annum and maturing on 26 July 2023, (KWD 14.9 million)	**49,151**	49,073
Floating interest at CBK discount rate + 2.75% per annum (capped at 7% per annum) and maturing on 26 July 2023, (KWD 25.1 million)	**82,797**	82,666
	131,948	131,739

18 OTHER LIABILITIES

	2019 US$ 000	2018 US$ 000
Staff related payables	**27,427**	35,812
Accrued expenses	**12,844**	13,767
Deferred income	**10,117**	13,898
Provisions for legal liabilities	**9,899**	9,899
Interest payable	**4,672**	1,045
Deferred tax (Note 15)	**4,573**	2,666
Dividends payable	**3,655**	2,505
Derivative financial liabilities (Note 30)	**629**	376
Deferred consideration payable	**-**	8,264
Other payables	**17,149**	18,143
	90,965	106,375

19 EQUITY

a) Share capital

	31 December 2019 US$ 000	31 December 2018 US$ 000
Authorised share capital		
Number of shares (in thousands)	**500,000**	500,000
Par value (US$)	**0.50**	0.50
	250,000	250,000
Issued and fully paid up share capital		
Number of shares (in thousands)	**232,263**	202,263
Par value (US$)	**0.50**	0.50
	116,132	101,132

During the year, the Bank increased its share capital by US$ 15 million by issuing 30,000,000 new shares of US$ 0.50 each through a rights issue subscribed by cash. The capital increase was approved by the CBB on 6 March 2019 and by the shareholders in the Extraordinary General Assembly Meeting on 24 March 2019.

b) Share premium
Share premium represents a non-distributable reserve arising from the exercise of the Bank's Employee Share Option Plan. The reserve is credited with the difference between the proceeds from the exercise of share options and the par value of the shares issued under the plan.

c) Statutory reserve
In accordance with the Bahrain Commercial Companies Law and the Bank's articles of association, 10% of the profit for the year is transferred to a statutory reserve until such time as the reserve reaches 50% of the Bank's paid-up 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 CBB.

d) General reserve
The Directors have approved a transfer of 10% (2018: 10%) of the profit of the Group for the year to general reserve in accordance with the Bank's Articles of Association.

e) Dividend paid
No dividend was announced or paid during the years ended 31 December 2019 or 2018.

f) Foreign currency translation reserve
The foreign currency translation reserve represents the net foreign exchange gain or loss arising from translating the financial statements of the Bank's foreign subsidiaries and associated companies from their functional currencies into United States Dollars.

20 FAIR VALUE RESERVE

	Note	2019 US$ 000	2018 US$ 000
Investments carried at fair value through other comprehensive			
Balance at 1 January		**(11,401)**	11,767
Transferred to Retained earnings upon the sale of FVOCI investments		**8,215**	(5,190)
Transferred to non-controlling interests upon dilution in a subsidiary	5	**4,697**	-
Net movement in unrealised fair values during the year		**(7,668)**	(21,015)
Transition adjustment on adoption of IFRS 9		**-**	3,037
Balance at 31 December		**(6,157)**	(11,401)
Cash flow hedges			
Balance at 1 January		**1,280**	1,100
Net movement in the fair values during the year		**(1,132)**	180
Balance at 31 December		**148**	1,280
		(6,009)	(10,121)

21 PERPETUAL TIER 1 CAPITAL

On 28 March 2016, the Bank issued Perpetual Additional Tier 1 Capital (the "AT1 Capital") amounting to US$ 33,000 thousand.

The AT1 Capital constitutes subordinated obligations of the Bank and is classified as equity in accordance with IAS 32: *Financial Instruments – Classification*. The AT1 Capital does not have a maturity date and bears interest on its nominal amount from the date of issue at a fixed annual rate.

The AT1 Capital is redeemable by the Bank at its sole discretion on or after 28 March 2021 or on any interest payment date thereafter subject to the prior consent of the CBB.

The Bank at its sole discretion may elect not to distribute interest and this is not considered an event of default. If the Bank does not pay interest on the AT1 Capital (for whatever reason), then the Bank must not make any other distribution on or with respect to its other shares that rank equally with or junior to the AT1 Capital.

22 INTEREST INCOME

	2019 US$ 000	2018 US$ 000
Loans and receivables	**1,266**	1,084
Investments carried at fair value through profit and loss	**1,506**	595
Placements with banks	**7,166**	3,532
Demand and call deposits with banks	**26**	1,152
	9,964	6,363

23 INVESTMENT INCOME - NET

	2019 US$ 000	2018 US$ 000
Gain (loss) on investments carried at fair value through profit and loss	**8,617**	(794)
Unrealized gain on investment properties	**7,294**	124
Dividend income	**4,196**	1,669
Rental income from investment properties	**4,039**	3,945
Gain on sale of investments	**2,390**	-
Gain due to reclassification of investment	**664**	31
Loss on sale of associates	**-**	(523)
Others	**3,171**	360
	30,371	4,812

24 FEES AND COMMISSIONS - NET

	2019 US$ 000	2018 US$ 000
Credit related fees, commissions and other income - net	**22,326**	21,381
Management fees from fiduciary activities	**40,773**	14,965
Advisory fees	**5,238**	6,619
	68,337	42,965

25 SHARE OF RESULTS OF ASSOCIATES - NET

	2019 US$ 000	2018 US$ 000
Kamco Investment Fund	**6,412**	1,737
United Capital Transport Company	**(874)**	(1,944)
Manafae Investment Company	**(419)**	(423)
KAMCO Real Estate Yield Fund	**(296)**	21
N.S. 88	**(177)**	(392)
Kuwait Education Fund	**-**	237
	4,646	(764)

26 INTEREST EXPENSE

	2019 US$ 000	2018 US$ 000
Loans payable	**4,451**	3,975
Long term bonds	**7,692**	3,353
Due to banks and other financial institutions	**8,759**	6,617
Deposits from customers	**1,268**	787
	22,170	14,732

27 CASH AND CASH EQUIVALENTS

	2019 US$ 000	2018 US$ 000
Demand and call deposits with banks excluding mandatory reserves	**71,051**	143,192
Placements with original maturities of ninety days or less	**221,533**	94,236
Cash and cash equivalents gross of expected credit losses	**292,584**	237,428
Placements with original maturities of more than ninety days	**14,745**	15,526
Expected credit losses	**(168)**	(1,233)
Cash and cash equivalents net of expected credit losses	**292,416**	236,195

The movement in the expected credit losses is as follows:

	Stage 1 US$ 000	Stage 2 US$ 000	Stage 3 US$ 000	Total US$ 000
As at 1 January 2019	-	**1,233**	-	**1,233**
Reversal during the year - net	-	**(1,065)**	-	**(1,065)**
As at 31 December 2019	-	**168**	-	**168**

28 RELATED PARTY TRANSACTIONS

Related parties represent the parent, associates and joint ventures, directors and key management personnel and entities which are controlled, jointly controlled or significantly influenced by any of the above mentioned parties.

The income and expenses in respect of related parties transactions during the year and included in the consolidated financial statements are as follows:

	2019			
	Parent US$ 000	***Associates US$ 000***	***Other related parties US$ 000***	***Total US$ 000***
Gain on investments carried at fair value through other comprehensive income	**-**	**-**	**(3)**	**(3)**
Fees and commissions - net*	**3,750**	**2,154**	**8,487**	**14,391**
Dividend income	**-**	**-**	**566**	**566**
Rental income	**-**	**-**	**2,275**	**2,275**
Interest income	**-**	**-**	**1,772**	**1,772**
Interest expense	**(758)**	**-**	**(6,071)**	**(6,829)**
Others	**-**	**-**	**563**	**563**

	2018			
	Parent US$ 000	*Associates US$ 000*	*Other related parties US$ 000*	*Total US$ 000*
Gain on investments carried at fair value through profit and loss	-	-	15	15
Fees and commissions - net	6,800	3,290	9,499	19,589
Dividend income	-	-	836	836
Rental income	-	-	2,711	2,711
Interest income	-	-	2,272	2,272
Interest expense	(547)	-	(4,562)	(5,109)
Others	(12)	-	(1,243)	(1,255)

Equity transactions with related parties during the year included in the consolidated statement of changes in equity are as follows:

	2019 US$ 000	*2018 US$ 000*
Interest payment on Perpetual Tier 1 Capital.	**(531)**	(531)

All related party transactions are on terms that are mutually agreed between the counterparties.

*The Bank and its parent entered into arrangement for service sharing between the two group entities. In line with the arrangement, the Bank will provided certain services and incur certain expenses on behalf of its parent.

28 RELATED PARTY TRANSACTIONS (continued)

The year-end balances in respect of related parties included in the consolidated financial statements are as follows:

	2019			
	Parent US$ 000	*Associates US$ 000*	*Other related parties US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	**1,689**	**1,689**
Placements with banks	-	-	**25,270**	**25,270**
Investments carried at fair value through profit and loss	-	-	**3,084**	**3,084**
Investments carried at fair value through other comprehensive income	-	-	**91,280**	**91,280**
Loans and receivables	-	-	**7,441**	**7,441**
Other assets	-	**3,621**	**7,098**	**10,719**
Due to banks and other financial institutions	-	-	**(214,811)**	**(214,811)**
Deposits from customers	**(8,032)**	**(673)**	**(5,687)**	**(14,392)**
Other liabilities	**(2)**	-	**(3,275)**	**(3,277)**
Perpetual Tier 1 Capital	-	-	**(10,000)**	**(10,000)**
Off statement of financial position items:				
Letters of guarantee	-	-	**150**	**150**
Loan related commitments	-	-	**3,195**	**3,195**

	2018			
	Parent US$ 000	*Associates US$ 000*	*Other related parties US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	21,120	21,120
Placements with banks	-	-	21,546	21,546
Investments carried at fair value through other comprehensive income	-	-	98,652	98,652
Loans and receivables	-	-	4,101	4,101
Other assets	102	1,716	9,083	10,901
Due to banks and other financial institutions	-	-	(135,908)	(135,908)
Deposits from customers	(14,365)	-	(7,074)	(21,439)
Other liabilities	-	-	(4,335)	(4,335)
Perpetual Tier 1 Capital	-	-	(10,000)	(10,000)
				-
Off statement of financial position items:				-
Letters of guarantee	-	-	150	150
Loan related commitments	-	-	3,195	3,195

All related party transactions are on terms that are mutually agreed between the counterparties. All related party exposures are performing.

The ultimate parent has committed to acquire certain FVOCI investment from the Group at its carrying value of US$ 28 million.

28 RELATED PARTY TRANSACTIONS (continued)

Compensation of key management personnel was as follows:

	2019 ***US$ 000***	*2018* *US$ 000*
Short term employee benefits	**8,304**	5,991

29 COMMITMENTS AND CONTINGENCIES

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.

Letters of credit, guarantees (including standby letters of credit) and acceptances committed by the Group to make payments on behalf of customers if certain conditions are met under the terms of the contract.

The Group has the following credit and investment related commitments:

	2019 ***US$ 000***	*2018* *US$ 000*
Credit-related commitments:		
Letters of guarantee	**2,237**	2,162
	2,237	2,162
Investments and loan related commitments *	**5,152**	5,157
	7,389	7,319

* Investment related commitments represent commitments for capital calls of fund structures. These commitments can be called during the investment period of the fund which is normally 1 to 5 years.

30 DERIVATIVES

In the ordinary course of business the Group enters into various types of transactions that involve derivative financial instruments.

The table below shows the positive and negative fair values of derivative financial instruments. The notional amount is that 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 and are not indicative of either market or credit risk.

				Notional amounts by term to maturity		
31 December 2019	*Positive fair value US$ 000*	*Negative fair value US$ 000*	*Notional amount Total US$ 000*	*Within 3 months US$ 000*	*3 - 12 months US$ 000*	*1 - 5 years US$ 000*
Derivatives held for trading *						
Forward foreign exchange contracts	**1,886**	**(2,246)**	**815,428**	**465,436**	**340,183**	**9,809**
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	**7**	**(276)**	**114,776**	**78,670**	**26,294**	**9,812**
Derivatives used as cash flow hedges						
Interest rate swaps	**148**	**-**	**75,000**	**-**	**75,000**	**-**
31 December 2018						
Derivatives held for trading *						
Forward foreign exchange contracts	1,171	(1,339)	767,694	420,762	327,311	19,621
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	377	(585)	186,165	153,641	32,524	-
Derivatives used as cash flow hedges						
Interest rate swap	1,280	-	75,000	-	-	75,000

* The Group uses foreign currency denominated borrowings and forward currency contracts to manage some of its transaction exposures. These currency forward contracts are not designated as cash flow, fair value or net investment in foreign operations hedges and are entered into for periods consistent with currency transaction exposures.

Forward foreign exchange contracts are contractual agreements to either buy or sell a specified currency, at a specific price and date in the future, and are customised contracts transacted in the over-the-counter market.

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.

Hedge of net investments in foreign operations

The Bank has designated certain forward foreign exchange contracts to hedge against changes in the value of its investments in foreign operations for an amount of US$ 191 million (KWD 50 million and EUR 24 million) [2018: US$ 181 million (KWD 46 million and EUR 24 million)]. Gains or losses on the retranslation of these forward foreign exchange contracts are transferred to equity through other comprehensive income to offset any gains or losses on the translation of the net investments in foreign operations.

30 DERIVATIVES (continued)

Cash flow hedges
The Group is exposed to variability in interest cash flows on liabilities which bear interest at a variable rate. The Group uses interest rate swaps as cash flow hedges of these interest rate risks. A schedule indicating as at 31 December, the periods when the net cash flows are expected to occur and when they are expected to affect the consolidated statement of income is as follows:

	2019		*2018*	
	Within 1 year US$ 000	***1-5 years US$ 000***	*Within 1 year US$ 000*	*1-5 years US$ 000*
Net cash outflows (liabilities)	**376**	**-**	1,141	391
Other comprehensive income	**148**	**-**	1,280	-

31 RISK MANAGEMENT

a) Introduction
Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is considered critical to the Group's continuing profitability.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. They are monitored through the Group's strategic planning process.

The major risks to which the Group is exposed while conducting its business and operations, and the means and organisational structure it employs to manage them strategically for building shareholder value, are outlined below.

Risk management structure
Each subsidiary within the Group is responsible for managing its own risks and has its own Board Committees, including Audit and Executive Committees in addition to other management committees such as Credit/ Investment Committee and Asset and Liability Committees (ALCO), or equivalent, with responsibilities generally the same as the Bank's committees.

The Board's role is to approve investment strategies of the Bank. However, it has delegated authority for the day-to-day decision making to the Executive Committee so that risk can be effectively managed within the Bank.

The Board of Directors has delegated the executive management of the Bank to the Chief Executive Officer (who is not a Director) and has appointed several Board Committees to work with them and to form and define policies and approve procedures for all of the Bank's activities.

The Executive Management of the Bank is headed by the Chief Executive Officer who is broadly responsible for the day to day conduct of the Bank's business in line with the Board's approved policies and procedures and complements and facilitates the Board in meeting its responsibility towards all stakeholders. He is assisted by the six members of the Bank's management team, each of whom is responsible for his or her respective department. Several management committees have been formed which are chaired by the Chief Executive Officer.

Executive Committee
The Executive Committee comprises of four directors including the Chairman, Vice Chairman and two other directors. Board meetings are held through circulation to approve all proposals not within the Investment Committee's risk authority, as well as to act on all matters within the Board's remit.

31 RISK MANAGEMENT (continued)

a) Introduction (continued)

Risk management structure (continued)

Investment Committee

The Investment Committee is mainly responsible for approving or recommending approval to the Executive Committee limits for individual exposures, investments and concentrations towards banks, countries, industries, risk rating classes, or other special risk asset categories. In addition, the Committee also monitors the overall risk profile of the Bank and recommends provision levels to the Executive Committee. The Investment Committee is constituted by a majority motion passed in the Executive Committee. Currently the Committee consists of four members.

Audit Committee

The Audit Committee is appointed by the Board and consists of four members who are Directors, including three independent Directors. The Audit Committee assists the Board in carrying out its responsibilities with respect to assessing (a) the quality and integrity of financial reporting, (b) the audit thereof, (c) the soundness of the internal controls of the Bank, (d) the risk assessment of the Bank's activities, and (e) the methods for monitoring compliance with laws, regulations and supervisory and internal policies.

Risk and Compliance

The Risk and Compliance Committee is responsible for the monitoring and assessment of risks facing the Bank, the review of compliance with internal and external guidelines, the review and recommendation of provisioning requirements, the assessment of the impact on the Bank from new regulatory requirements, and review of Investment Committee decisions. The Committee comprises of six senior executives of the Bank including the Chief Executive Officer. Additionally, the Head of Internal Audit and Quality Assurance participates in the Committee meetings in the capacity of an observer.

Asset and Liability Committee

The Asset and Liability Committee establishes policies and objectives for the asset and liability management of the Bank's statement of financial position in terms of structure, distribution, risk and return and its impact on profitability. It also monitors the cash flow, tenor and cost/yield profiles of assets and liabilities and evaluates the Bank's financial position both from interest rate sensitivity and liquidity points of view, making corrective adjustments based upon perceived trends and market conditions, monitoring liquidity, monitoring foreign exchange exposures and positions. The Committee comprises of six senior executives of the Bank including the Chief Executive Officer.

Management Committee

The Management Committee acts as the steering committee of the Bank as well as a management forum to discuss any relevant issues. It meets on a weekly basis and consists of the Chief Executive Officer and all Department Heads as well as Internal Audit. It also serves to follow up on a weekly basis on the daily conduct of the Bank's business activities. The Committee is headed by the Chief Executive Officer.

Key Persons Committee

The Key Persons Committee comprises three members of senior management. The Committee is mainly responsible for the supervision of adequacy of compliance with the CBB and Bahrain Bourse guidelines on key persons trading (insider trading).

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected geographies and industry sectors. In addition, the Bank monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

31 RISK MANAGEMENT (continued)

a) Introduction (continued)

Nominating and Remunerations Committee
The Nominating and Remuneration Committee (NRC) assists the Board in assessing the skills set of Board members and is responsible to oversee the preparation of appropriate nomination documents and notifications proposing candidates for directorships. It reviews the independence of directors on an annual basis, supervises the preparation of induction materials and orientation sessions, makes recommendations to the Board regarding the management structure and ensures that there is a succession plan in place. The NRC comprises of three members, all of whom are independent.

The NRC also recommends/ reviews the remuneration policies for the Board of Directors and senior management and submits recommendations for shareholders' approval.

Risk mitigation
As part of its overall risk management, the Group uses derivatives and other instruments to manage exposures resulting from changes in interest rates and foreign currency transactions.

The risk profile is assessed before entering into hedge transactions, which are authorised by the appropriate level of seniority within the Group.

Where warranted, the Group enters into legally enforceable netting arrangements covering its money market and foreign exchange trading activities whereby the only net amounts may be settled at maturity. With regard to the credit risk in the off statement of financial statement exposures, third party guarantees are obtained wherever possible as a risk mitigation measure.

Concentration risk
Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentrations of risk, the Group's policies and procedures include specific guidelines to focus on country and counterparty limits and maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly. Robust limit structures put in place by the Board ensures effective monitoring and control of concentration risk and any limit breaches are immediately rectified and reported to the Board.

b) Credit risk
Credit risk arises from the extension of credit facilities in the Group's banking and trading activities as well as in investment activities where there is a possibility that a counterparty may fail to honour its commitment whenever an investment may fail.

Credit risk is mitigated through:

(i) Establishing an appropriate credit risk environment;
(ii) Operating under a sound credit and investment approval process;
(iii) Maintaining appropriate credit administration, measurement and monitoring processes; and
(iv) Ensuring adequate controls over the credit risk management process.

The Group has well defined policies approved at the individual board level. These provide carefully documented guidelines for credit risk management. There is a two tier committee structure to approve and review credit and investment risk. The Investment Committee comprises of the Chief Executive Officer, Head of Treasury and the Chief Financial Officer. The Head of Credit and Risk Management acts as a non-voting member to the Committee. Exposures beyond Investment Committee limits are approved by the Board's Executive Committee or by the Board of Directors.

31 RISK MANAGEMENT (continued)

b) Credit risk (continued)

Maximum exposure to credit risk without taking account of any collateral or other credit enhancements

The table below shows the Group's maximum exposure to credit risk for the components of on and off statement of financial position exposure. The maximum exposure shown is gross before the effect of mitigation through the use of collateral arrangements, but after any expected credit losses.

	2019 *US$ 000*	*2018* *US$ 000*
Demand and call deposits with banks	**71,369**	143,510
Placements with banks	**236,110**	108,529
Investments carried at FVTPL	**13,070**	6,941
Investments carried at amortised cost	**280**	494
Loans and receivables	**27,778**	25,191
Other assets	**62,174**	58,931
Letters of guarantee	**2,237**	2,162
Derivative financial assets	**148**	1,280
	413,166	347,038

Risk concentrations of the maximum exposure to credit risk

Concentration of risk is managed by client/counterparty, by geographical region and by industry sector. The maximum credit exposure to any single client or counterparty as of 31 December 2019 was US$ 61.8 million (2018: US$ 31.3) before taking account of collateral or other credit enhancements.

An analysis of the Group's financial assets by geographical region, before taking into account collateral held or other credit enhancements, is as follows:

	G.C.C. *US$ 000*	*Middle East and North Africa* *US$ 000*	*Europe* *US$ 000*	*Americas* *US$ 000*	*Others* *US$ 000*	*Total* *US$ 000*
Demand and call deposits with banks	**35,361**	**1,957**	**837**	**33,214**	-	**71,369**
Placements with banks	**206,383**	**29,727**	-	-	-	**236,110**
Investments carried at FVTPL	**13,070**	-	-	-	-	**13,070**
Investments at amortised cost	-	**280**	-	-	-	**280**
Loans and receivables	**23,803**	**3,975**			-	**27,778**
Other assets	**30,615**	**26,363**	**3,100**	**2,096**	-	**62,174**
Letters of guarantee	**165**	**2,072**			-	**2,237**
Derivative financial assets	**148**	-	-	-	-	**148**
31 December 2019	**309,545**	**64,374**	**3,937**	**35,310**	-	**413,166**
Demand and call deposits with banks	119,762	192	474	23,082	-	143,510
Placements with banks	85,267	23,262	-	-	-	108,529
Investments carried at FVTPL	6,941	-	-	-	-	6,941
Investments at amortised cost	-	494	-	-		494
Loans and receivables	17,816	7,375	-	-	-	25,191
Other assets	51,061	6,735	2	1,133	-	58,931
Letters of guarantee	15	343	1,647	157	-	2,162
Derivative financial assets	1,280	-	-	-	-	1,280
31 December 2018	282,142	38,401	2,123	24,372	-	347,038

31 RISK MANAGEMENT (continued)

b) Credit risk (continued)

Risk concentrations of the maximum exposure to credit risk (continued)

An industry sector analysis of the Group's financial assets, before taking into account collateral held or other credit enhancements, is as follows:

At 31 December 2019	*Trading & Manufacturing* *US$ 000*	*Banks and other financial institutions* *US$ 000*	*Construction and real estate* *US$ 000*	*Individuals* *US$ 000*	*Others* *US$ 000*	*Total* *US$ 000*
Demand and call deposits with banks	-	**71,369**	-	-	-	**71,369**
Placements with banks	-	**236,110**	-	-	-	**236,110**
Investments carried at FVTPL	**2,761**	**6,632**	**2,068**	-	**1,609**	**13,070**
Investments at amortised cost	-	-	-	-	**280**	**280**
Loans and receivables	-	**2,892**	-	**20,948**	**3,938**	**27,778**
Other assets	-	**9,098**	**2,231**	**14**	**50,831**	**62,174**
Letters of guarantee	-	**2,237**	-	-	-	**2,237**
Derivative financial assets	-	**148**	-	-	-	**148**
	2,761	**328,486**	**4,299**	**20,962**	**56,658**	**413,166**
At 31 December 2018						
Demand and call deposits with banks	-	143,510	-	-	-	143,510
Placements with banks	-	108,529	-	-	-	108,529
Investments carried at FVTPL	-	6,941	-	-	-	6,941
Investments at amortised cost	-	494	-	-	-	494
Loans and receivables	-	1,516	-	23,283	392	25,191
Other assets	-	53,485	-	10	5,436	58,931
Letters of guarantee	-	2,162	-	-	-	2,162
Derivative financial assets	-	1,280	-	-	-	1,280
	-	317,917	-	23,293	5,828	347,038

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 mainly include charges over trading securities.

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

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

31 RISK MANAGEMENT (continued)

b) Credit risk (continued)

Credit risk exposure for each credit rating

	Investment grade	*Non-investment grade*	*Unrated**	*Total*
	US$ 000	*US$ 000*	*US$ 000*	*US$ 000*
At 31 December 2019				
Demand and call deposits with banks	**70,921**	**318**	**130**	**71,369**
Placements with banks	**210,839**	**-**	**25,271**	**236,110**
Investments carried at FVTPL	**13,070**	**-**	**-**	**13,070**
Investments at amortised cost	**-**	**-**	**280**	**280**
Loans and receivables	**-**	**-**	**27,778**	**27,778**
Other assets	**2,601**	**-**	**59,573**	**62,174**
Letters of guarantee	**-**	**-**	**2,237**	**2,237**
Derivative financial assets	**148**	**-**	**-**	**148**
	297,579	**318**	**115,269**	**413,166**

* Includes exposures to counterparties not rated by credit rating agencies

At 31 December 2018				
Demand and call deposits with banks	143,071	318	121	143,510
Placements with banks	85,267	-	23,262	108,529
Investments at FVTPL	6,941	-	-	6,941
Investments at amortised cost	-	-	494	494
Loans and receivables	-	-	25,191	25,191
Other assets	2,330	-	56,601	58,931
Letters of guarantee	-	-	2,162	2,162
Derivative financial assets	1,280	-	-	1,280
	238,889	318	107,831	347,038

It is the Group's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risk and the comparison of credit exposures across all business lines, geographic regions and products. All externally rated credit risk exposures are rated by the relevant External Credit Assessment Institutions ("ECAIs").

Additionally, the internal risk ratings of the Group's externally unrated credit risk exposures which are largely subjective, are tailored to the various categories and are derived in accordance with the internal rating policy and practices. The attributable internal risk ratings are assessed and updated on a regular basis.

31 RISK MANAGEMENT (continued)

b) Credit risk (continued)

Credit risk exposure for each credit rating (continued)
The table above reflects the risk ratings of the credit risk exposures rated by the relevant ECAIs. All of the externally unrated credit risk exposures have been classified under "Unrated" category.

Restructured 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, the loan is no longer considered past due. The Group has not restructured any loans as of 31 December 2019 (31 December 2018: Same).

Restructured loans have a minimum cool-off period of 12 months, from the date when the condition(s) that caused an account to move to Stage 2 or Stage 3 ceases to exist, and provided that up to date payments are received with no arrears.

Offsetting financial assets and financial liabilities
The disclosures set out in the table below include financial assets and financial liabilities that are offset in the Group's statement of financial position:

	Loans receivables US$ 000	*Customer deposits US$ 000*
31 December 2019		
Gross amounts of recognised financial asset / liability	**285,000**	**285,000**
Gross amounts offset in the consolidated statement of financial position	**(285,000)**	**(285,000)**
Net amount of financial asset / (liability) presented in the consolidated statement of financial position	-	-
31 December 2018		
Gross amounts of recognised financial asset / liability	285,000	285,000
Gross amounts offset in the consolidated statement of financial position	(285,000)	(285,000)
Net amount of financial asset / (liability) presented in the consolidated statement of financial position	-	-

c) Market risk
Market risk is defined as the risk of losses in the value of on-or-off statement of financial position financial instruments caused by a change in market prices or rates, (including changes in interest rates and foreign exchange rates). The Group's policy guidelines for market risk have been vetted by the Board of Directors in compliance with the rules and guidelines provided by the CBB. The CBB guidelines introduced a risk measurement framework whereby all locally incorporated banks in Bahrain are required to measure and apply capital charges in respect of their market risk in addition to capital requirements for credit risk and operational risk.

The market risk subject to capital charge normally arises from changes in value due to market forces in the following exposures:

- Interest rate instruments and securities in the trading book; and
- Foreign exchange throughout the banking book.

The Group has entered into interest rate swaps and forward foreign exchange contracts for hedging and trading purposes.

31 RISK MANAGEMENT (continued)

c) Market risk (continued)

Interest rate risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within the established limits.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Group's consolidated statement of income based on the consolidated statement of financial position as of 31 December:

Currency	***Increase in basis points 2019***	***Sensitivity of net interest income 2019 US$ 000***	*Increase in basis points 2018*	*Sensitivity of net interest income 2018 US$ 000*
Kuwaiti Dinar	**+ 25**	**(94)**	+ 25	(260)
United States Dollar	**+ 25**	**180**	+ 25	(104)
Euro	**+ 25**	**(13)**	+ 25	(4)
Pound Sterling	**+ 25**	**1**	+ 25	-
Others	**+ 25**	**29**	+ 25	286

The decrease in the basis points will have an opposite impact on the net interest income.

The sensitivity of the consolidated statement of income is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate financial assets and financial liabilities held at 31 December 2019, including the effect of hedging instruments.

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group considers the United States Dollar as its functional currency. Positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits.

The table below indicates the effect on profit before tax for the positions as at statement of financial position date as a result of change in the currency rate with all other variables held constant.

Currency	***Change in currency rate in % 2019***	***Effect on profit before tax 2019 US$ 000***	***Effect on equity 2019 US$ 000***	*Change in currency rate in % 2018*	*Effect on profit before tax 2018 US$ 000*	*Effect on equity 2018 US$ 000*
Kuwaiti Dinar	+2	**(2,265)**	**1,137**	+2	(16,280)	19,615
	-2	**2,265**	**(1,137)**	-2	16,280	(19,615)
Euro	+2	**(624)**	**538**	+2	(1,425)	24,037
	-2	**624**	**(538)**	-2	1,425	(24,037)
Pound Sterling	+2	**11**	-	+2	17	-
	-2	**(11)**	-	-2	(17)	-

31 RISK MANAGEMENT (continued)

c) Market risk (continued)

Equity price risk

Equity price risk arises from the change in fair values of equity investments. The Group manages this risk through diversification of investments in terms of geographical distribution and industry concentration.

The geographical distribution of the Group's equity investments is as follows:

Geographical distribution

At 31 December 2019	***Middle East/ Africa US$ 000***	***Europe US$ 000***	***North America US$ 000***	***Others US$ 000***	***Total US$ 000***
Investments carried at fair value through profit and loss					
Quoted equities	**13,512**	**-**	**1**	**32**	**13,545**
Unquoted equities	**496**	**909**	**2,930**	**-**	**4,335**
Managed funds	**54,403**	**8,535**	**3,890**	**-**	**66,828**
	68,411	**9,444**	**6,821**	**32**	**84,708**
Investments carried at fair value through other comprehensive income					
Quoted equities	**30,187**	**-**	**-**	**-**	**30,187**
Unquoted equities	**68,651**	**26,914**	**4,277**	**13**	**99,855**
Managed funds	**1,006**	**-**	**-**	**-**	**1,006**
	99,844	**26,914**	**4,277**	**13**	**131,048**
Total	**168,255**	**36,358**	**11,098**	**45**	**215,756**

At 31 December 2018	*Middle East/ North Africa US$ 000*	*Europe US$ 000*	*North America US$ 000*	*Others US$ 000*	*Total US$ 000*
Investments carried at fair value through profit and loss					
Quoted equities	10,584	879	783	32	12,278
Unquoted equities	280	-	2,930	-	3,210
Managed funds	42,706	9,916	6,801	-	59,423
	53,570	10,795	10,514	32	74,911
Investments carried at fair value through other comprehensive income					
Quoted equities	45,219	-	-	-	45,219
Unquoted equities	76,565	40,109	3,182	442	120,298
Managed funds	1,124	-	973	33	2,130
	122,908	40,109	4,155	475	167,647
Total	176,478	50,904	14,669	507	242,558

At the reporting date, the exposure to listed equity securities at fair value was US$ 43,732 thousand (2018:US$ 57,497 thousand). A decrease of 10% on the market indices of MENA stock exchanges could have an impact of approximately US$ 4,373 thousand (2018: US$ 5,750 thousand) on the income or equity attributable to the Group, depending on whether the decline is significant or prolonged. The majority of the equities in the MENA region are quoted on the Boursa Kuwait.

31 RISK MANAGEMENT (continued)

d) Liquidity risk

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2019 based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

At 31 December 2019	On demand US$ 000	1 - 3 months US$ 000	3 - 12 months US$ 000	1 - 5 years US$ 000	Over 5 years US$ 000	Total US$ 000
Financial liabilities						
Due to banks and other financial institutions	103,362	24,555	183,474	-	-	311,391
Deposits from customers	17,587	5,078	-	-	-	22,665
Loans payable	-	9,999	16,951	11,304	-	38,254
Long term bonds	-	-	-	159,219	-	159,219
Other liabilities	-	19,359	71,606		-	90,965
Total non-derivative undiscounted financial liabilities	120,949	58,991	272,031	170,523	-	622,494
Derivatives						
Net cash outflows on interest rate swaps	-	-	376	-	-	376
Gross settled foreign currency derivatives	-	544,106	366,477	19,621	-	930,204
Off-statement of financial position items						
Letters of guarantee	2,237	-	-	-	-	2,237
Investment and loan related commitments	-	-	-	5,152	-	5,152

The Group expects that not all of contingent items or commitments will be drawn before expiry of the commitments.

31 RISK MANAGEMENT (continued)

d) Liquidity risk (continued)

At 31 December 2018	On demand US$ 000	1 - 3 months US$ 000	3 - 12 months US$ 000	1 - 5 years US$ 000	Over 5 years US$ 000	Total US$ 000
Financial liabilities						
Due to banks and other financial institutions	120,879	-	100,000	-	-	220,879
Deposits from customers	31,145	1,463	-	-	-	32,608
Loans payable	-	23,320	16,467	27,246	-	67,033
Long term bonds	-	-	-	131,739	-	131,739
Other liabilities	-	63,601	-	42,774	-	106,375
Total non-derivative undiscounted financial liabilities	152,024	88,384	116,467	201,759	-	558,634
Derivatives						
Net cash outflows on interest rate swaps	-	571	571	390	-	1,532
Gross settled foreign currency derivatives	-	846,491	87,747	19,621	-	953,859
Off statement of financial position items						
Letters of guarantee	2,162	-	-	-	-	2,162
Investment and loan related commitments	-	-	-	5,157	-	5,157

The Group expects that not all of contingent items or commitments will be drawn before expiry of the commitments.

31 RISK MANAGEMENT (continued)

d) Liquidity risk (continued)

In order to ensure that the Group can meet its financial obligations as they fall due, there is a close monitoring of its assets / liabilities position. Besides other functions, the Asset-Liability Committee evaluates the statement of financial position both from a liquidity and an interest rate sensitivity point of view. The whole process is aimed at ensuring sufficient liquidity to fund its ongoing business activities and to meet its obligations as they fall due. A diversified funding base has evolved in deposits raised from the interbank market, deposits received from customers and medium term funds raised through syndicated and commodity based murabaha transactions. These, together with the strength of its equity and the asset quality, ensure that funds are made available on competitive rates.

The maturity analysis of assets and liabilities analysed according to when they are expected to be recovered or settled are as follows:

At 31 December 2019

	Less than 12 months US$ 000	*Over 12 months US$ 000*	*Total US$ 000*
Demand and call deposits with banks	**71,051**	**318**	**71,369**
Placements with banks	**236,110**	**-**	**236,110**
Investments carried at fair value through profit and loss	**97,778**	**-**	**97,778**
Investments carried at fair value through other comprehensive income	**30,187**	**100,861**	**131,048**
Investments carried at amortised cost	**-**	**280**	**280**
Loans and receivables	**22,988**	**4,790**	**27,778**
Other assets	**62,933**	**-**	**62,933**
Investments in associates	**-**	**75,774**	**75,774**
Investment properties	**-**	**102,713**	**102,713**
Property and equipment	**-**	**51,849**	**51,849**
Goodwill and other intangible assets	**-**	**65,591**	**65,591**
Total assets	**521,047**	**402,176**	**923,223**
Due to banks and other financial institutions	**307,784**	**-**	**307,784**
Deposits from customers	**22,647**	**-**	**22,647**
Loans payable	**26,390**	**10,485**	**36,875**
Long term bonds	**-**	**131,948**	**131,948**
Other liabilities	**90,965**	**-**	**90,965**
Total liabilities	**447,786**	**142,433**	**590,219**
Net	**73,261**	**259,743**	**333,004**

31 RISK MANAGEMENT (Continued)

d) Liquidity risk (continued)

At 31 December 2018

	Less than 12 months US$ 000	*Over 12 months US$ 000*	*Total US$ 000*
Demand and call deposits with banks	143,192	318	143,510
Placements with banks	108,529	-	108,529
Investments carried at fair value through profit and loss	81,852	-	81,852
Investments carried at fair value through other comprehensive income	45,252	122,395	167,647
Investments carried at amortised cost	-	494	494
Loans and receivables	21,169	4,022	25,191
Other assets	61,097	-	61,097
Investments in associates and joint venture	-	71,513	71,513
Investment properties	-	107,629	107,629
Property and equipment	-	39,394	39,394
Goodwill	-	66,634	66,634
Total assets	461,091	412,399	873,490
Due to banks and other financial institutions	220,879	-	220,879
Deposits from customers	32,608	-	32,608
Loans payable	39,787	27,246	67,033
Long term bonds	-	131,739	131,739
Other liabilities	63,601	42,774	106,375
Total liabilities	356,875	201,759	558,634
Net	104,216	210,640	314,856

The Group is also required to comply with the liquidity requirements as stipulated by the CBB, which became effective during the year 2019. These requirements relate to maintaining a minimum of 100% net stable funding ratio (NSFR) and 100% liquidity coverage ratio (LCR). As at 31 December 2019, the Group's NSFR and LCR ratios were at 118% and 273% respectively.

e) Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. When controls fail to perform operational risk can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group has established a board approved framework for operational risk management which comprehensively outlines operational risk appetite for the Bank and provides operational risk management procedures. The Framework is supported by a dedicated operational risk system covering Loss Data Collection, Risk and Control Self Assessment and Key Indicator modules which have been rolled out in the Bank. While, the Group cannot expect to eliminate all operational risks, but through dedicated operational risk framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

32 FAIR VALUE MEASUREMENT

The Group uses the hierarchy for determining and disclosing the fair value of financial instruments as disclosed in Note 2.

Management has assessed that financial assets comprising of demand and call deposits with banks, placements with banks, and loans and receivables maturing within one year, and financial liabilities comprising of on-demand customer deposits, amounts due to banks and loans payable falling due within one year approximate their carrying values largely due to the short term maturities of these instruments.

The following table provides the fair value measurement hierarchy of the Group's assets and liabilities.

Quantitative disclosures fair value measurement hierarchy for assets as at 31 December 2019:

	Fair value measurement using			
	Level 1	*Level 2*	*Level 3*	*Total*
	US$ 000	*US$ 000*	*US$ 000*	*US$ 000*
Assets measured at fair value				
Investments carried at fair value through profit and loss				
Quoted equities	13,545	-	-	13,545
Quoted debt securities	12,245	-	-	12,245
Unquoted equities	-	-	4,335	4,335
Unquoted debt securities	-	-	825	825
Managed funds	3,494	49,193	14,141	66,828
Investments carried at fair value through other comprehensive income				
Quoted equities	2,284	-	27,903	30,187
Quoted managed funds	-	-	-	-
Unquoted equities	-	-	99,855	99,855
Unquoted managed funds	-	-	1,006	1,006
Derivatives				
Interest rate swaps	-	148	-	148
Investment properties	-	-	102,713	102,713
	31,568	49,341	250,778	331,687
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	-	(629)	-	(629)
	-	(629)	-	(629)

32 FAIR VALUE MEASUREMENT (continued)

Quantitative disclosures fair value measurement hierarchy for assets as at 31 December 2018:

	Fair value measurement using			
	Level 1 US$ 000	*Level 2 US$ 000*	*Level 3 US$ 000*	*Total US$ 000*
Assets measured at fair value				
Investments carried at fair value through profit and loss				
Equities - quoted	9,615	-	-	9,615
Debt securities - quoted	6,661	-	-	6,661
Unquoted equities	-	-	4,089	4,089
Managed funds	-	42,892	18,595	61,487
Investments carried at fair value through other comprehensive income				
Equities - quoted	45,219	-	-	45,219
Equities - unquoted	-	-	121,418	121,418
Managed funds	-	-	1,010	1,010
Derivatives				-
Interest rate swap	-	1,280	-	1,280
Investment properties	-	-	107,629	107,629
	61,495	44,172	252,741	358,408
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	-	(376)	-	(376)
	-	(376)	-	(376)

Transfers between Level 1, Level 2 and Level 3

During the year ended 31 December 2019 there were no transfers between Level 1 and Level 2 fair value measurements and no transfers into or out of Level 3 fair value measurement.

Reconciliation of fair value measurement of investments in level 3 of the fair value hierarchy:

	As at 1 January 2019 US$'000	***Net purchases, sales, transfer and settlement US$'000***	***(Loss) gain recorded in the statement of income US$'000***	***Loss recognised in OCI US$'000***	***As at 31 December 2019 US$'000***
Investments carried at fair value through profit and loss					
Equities - unquoted	**4,089**	**-**	**246**	**-**	**4,335**
Debt securities - unquoted	**-**	**825**	**-**	**-**	**825**
Managed funds	**18,595**	**(2,188)**	**(2,266)**	**-**	**14,141**
	22,684	**(1,364)**	**(2,019)**	**-**	**19,301**
Investments carried at fair value through other comprehensive income					
Equities - unquoted	**121,418**	**(10,529)**	**-**	**(11,034)**	**99,855**
Managed funds	**1,010**	**-**	**-**	**(4)**	**1,006**
	122,428	**(10,529)**	**-**	**(11,038)**	**100,861**
Investment properties	**107,629**	**(12,734)**	**7,818**	**-**	**102,713**

33 CAPITAL ADEQUACY

The Bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision ("BIS rules/ratios") as adopted by the CBB.

Capital management

The primary objectives of the Group's capital management are to ensure that the Group complies with capital requirements of the CBB and that the Group maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value. In order to maintain or adjust the capital structure, the Bank may adjust the amount of dividend payment to shareholders, or issue equity securities. No changes were made in the capital management objectives, policies and processes from previous years.

The risk asset ratio calculated in accordance with the capital adequacy guidelines issued by the CBB, for the Group is as follows:

	2019	*2018*
	US$ 000	*US$ 000*
Capital base:		
Tier 1	**177,943**	147,347
Tier 2	**15,658**	6,219
Total capital base (a)	**193,601**	153,566
Credit risk weighted exposure	**878,011**	944,533
Market risk weighted exposure	**11,450**	10,375
Operational risk weighted exposure	**93,188**	38,413
Total risk weighted exposure (b)	**982,649**	993,321
Capital adequacy (a/b * 100)	**19.70%**	15.46%
Minimum requirement	**12.5%**	12.5%

Regulatory capital consists of Tier 1 capital, which comprises share capital, share premium, statutory reserve, general reserve, treasury share reserve, foreign currency reserve, retained earnings and non-controlling interests less goodwill. The other component of regulatory capital is Tier 2 capital, which includes subordinated long term debt and fair value reserves.

34 TRANSITION FROM LIBOR TO ALTERNATIVE RISK-FREE RATES

As communicated by the CBB, the London Interbank Offered Rate ("LIBOR") used to price US$ denominated financial instruments will be replaced by Secured Overnight Financing Rate ("SOFR") or other recognised benchmark rates internationally. While LIBOR is intended to be discontinued after end-2021, a transition to alternative risk-free rates will potentially have legal, technological, accounting and regulatory implications.

The Bank is currently in the process of assessing the impact of such a transition and developing an approach to address arising risks. An initial impact assessment analysis is being submitted to the CBB as of the date of these financial statements that describes the process, timelines and appropriate legal solutions to deal with the transition.

Impact on hedging relationships

Interest Rate Benchmark Reform Amendments to IFRS 9, IAS 39 and IFRS 7 include a number of reliefs, which apply to all hedging relationships that are directly affected by interest rate benchmark reform.

As a result of interest rate benchmark reform, there may be uncertainties about the timing and or amount of benchmark-based cash flows of the hedged item or the hedging instrument during the period before the replacement of an existing interest rate benchmark with an alternative risk-free interest rate. These amendments are effective for annual periods beginning on or after 1 January 2020, with early application permitted. The Group is currently assessing the impact of this standard and will apply from the effective date.