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

CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2017

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INDEPENDENT AUDITORS' 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 2017, and the consolidated statements of income and other comprehensive income, cash flows and 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 2017 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 Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information included in the Group's 2017 annual report

Other information consists of the information included in the Group's 2017 Annual Report, other than the consolidated financial statements and our auditor's report thereon. The Board of Directors is responsible for the other information. Prior to the date of this auditors' report, we obtained the Directors' report 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.

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INDEPENDENT AUDITORS' 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.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors.

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INDEPENDENT AUDITORS' 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)

- 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 opinion.

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.

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

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;

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

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

Ernst + Young

Partner's registration no. 121
27 February 2018
Manama, Kingdom of Bahrain

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2017

	Note	2017 US$ 000	2016 US$ 000
ASSETS			
Demand and call deposits with banks		97,993	176,880
Placements with banks		68,677	187,350
Investments carried at fair value through statement of income	5	19,268	45,178
Non-trading investments	6	221,566	404,436
Loans and receivables	7	4,216	1,184,804
Other assets	8	31,820	112,735
Investments in associates	9	77,512	709,043
Investment properties	10	106,093	101,326
Property and equipment		1,679	32,117
Goodwill	11	52,390	51,868
TOTAL ASSETS		680,114	3,005,737
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks and other financial institutions		250,211	726,222
Deposits from customers		31,018	985,210
Loans payable	13	98,658	652,125
Subordinated debt	14	-	50,000
Other liabilities	15	37,358	62,724
TOTAL LIABILITIES		417,245	2,476,281
EQUITY			
Share capital	16	101,132	208,651
Treasury shares	16	-	(18,131)
Share premium	16	5,687	11,459
Statutory reserve	16	49,881	100,514
General reserve	16	29,612	80,999
Treasury shares reserve	16	-	14,248
Fair value reserve	17	12,867	(49,986)
Foreign currency translation reserve	16	(3,871)	(37,476)
Retained earnings		7,659	83,711
CAPITAL AND RESERVES ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT		202,967	394,009
Perpetual Tier 1 capital	18	33,000	33,000
Non-controlling interests in equity		26,902	102,447
TOTAL EQUITY		262,869	529,456
TOTAL LIABILITIES AND EQUITY		680,114	3,005,737

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

The attached notes 1 to 32 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF INCOME AND OTHER COMPREHENSIVE INCOME

For the year ended 31 December 2017

	Note	*2017* *US$ 000*	*2016* *US$ 000*
Continuing operations			
Interest income	19	4,431	3,310
Investment income - net	20	23,810	9,753
		28,241	13,063
Fees and commissions - net	21	25,391	19,830
Foreign currency losses - net		(409)	(3,886)
Share of results of associates - net	22	(2,922)	3,841
Total income		50,301	32,848
Interest expense	23	(15,232)	(11,703)
Operating income before expenses and provisions		35,069	21,145
Salaries and benefits		(15,862)	(12,635)
General and administrative expenses		(9,730)	(7,978)
Operating income before provisions and tax		9,477	532
Impairment loss on investments	6,9	(462)	(2,933)
Provision for doubtful loans and other assets - net	7,8	(2,895)	894
Taxation - net	12	(1,018)	(20)
Net profit (loss) for the year from continuing operations		5,102	(1,527)
Net profit from discontinued operations		3,268	2,400
Net profit before reclassification adjustments		8,370	873
Reclassification adjustments	16 (h)	(87,765)	-
(Loss) profit for the year		(79,395)	873
Other comprehensive income:			
Reclassification adjustments	16 (h)	87,765	-
		8,370	873
Foreign currency translation reserve		6,029	(2,806)
Fair value reserve		4,950	6,062
Transfer to consolidated statement of income upon disposal		(1,880)	2,681
Share of other comprehensive loss of associates - net		-	(11,690)
Cash flow hedges		256	655
Other comprehensive income (loss) for the year		9,355	(5,098)
TOTAL COMPREHENSIVE INCOME (LOSS) FOR THE YEAR		17,725	(4,225)
(Loss) profit for the year		(79,850)	6,259
Other comprehensive income (loss) for the year		96,438	(4,393)
Total comprehensive income attributable to shareholders of the parent		16,588	1,866
Profit (loss) for the year		455	(5,386)
Other comprehensive income (loss) for the year		682	(705)
Total comprehensive income (loss) attributable to non-controlling interests		1,137	(6,091)

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

The attached notes 1 to 32 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2017

	Note	2017 US$ 000	2016 US$ 000
OPERATING ACTIVITIES			
Net (loss) profit for the year		(79,395)	873
Reclassification adjustments	16 (h)	87,765	-
Net profit from discontinued operations		(3,268)	-
Net profit for the year from continuing operations		5,102	873
Adjustments for non-cash items:			
Depreciation		797	5,309
Share of results of associates - net	22	2,922	(41,080)
Provisions for doubtful loans - net	7	2,895	8,255
Impairment loss on investments	6,9	462	2,933
(Gain) loss on investments carried at fair value through statement of income	20	(3,902)	229
Gain on fair valuation of investment properties	20	(2,732)	-
Gain on sale of an associate and subsidiaries	20	(2,668)	(2,824)
Gain on sale of non-trading investments	20	(4,369)	-
Gain due to reclassification of investment	20	(2,971)	-
Interest income	19	(23,810)	(48,503)
Interest expense	23	15,232	52,932
Dividend income	20	(1,907)	(7,230)
Other non-cash items	11	(719)	453
Taxation		1,018	-
Operating loss before changes in operating assets and liabilities		(14,650)	(28,653)
Changes in operating assets and liabilities:			
Placements with banks with original maturities of more than ninety days		6,845	5,699
Investments carried at fair value through statement of income		29,812	5,254
Non-trading investments		187,165	(17,056)
Loans and receivables		1,178,460	(161,130)
Other assets		74,289	10,138
Due to banks and other financial institutions		(476,011)	(111,938)
Deposits from customers		(954,192)	523,124
Other liabilities		(13,924)	5,107
Net assets of disposal group classified as held for sale		3,268	862
Interest received		28,687	46,140
Interest paid		(26,279)	(49,894)
Dividends received	20	1,907	7,230
Donations		(200)	(200)
Directors' remuneration		(195)	(220)
Net cash from operating activities		24,982	234,463
INVESTING ACTIVITIES			
Investments in associates - net		681,837	25,073
Investment properties - net		(1,035)	896
Property and equipment - net		29,641	4,268
Net cash from investing activities		710,443	30,237
FINANCING ACTIVITIES			
Share Capital issued (Restructuring)		(277,775)	-
Repayment of loans		(553,467)	(62,443)
Issue of perpetual Tier 1 capital		-	33,000
Interest payment on Tier 1 capital securities		(3,513)	(1,793)
Repayment of subordinated debt		(50,000)	(93,270)
Net cash used in financing activities		(884,755)	(124,506)
Foreign currency translation adjustments		33,605	(2,586)
Movement in non-controlling interests		(75,090)	(1,498)
NET CHANGE IN CASH AND CASH EQUIVALENTS		(190,815)	136,110
Cash and cash equivalents at 1 January		357,067	220,957
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	24	166,252	357,067

The attached notes 1 to 32 form part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2017

	Attributable to shareholders of the parent												
	Share capital US$ 000	*Treasury shares US$ 000*	*Share premium US$ 000*	*Statutory reserve US$ 000*	*General reserve US$ 000*	*Treasury share 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 2017	208,651	(18,131)	11,459	100,514	80,999	14,248	(49,966)	(37,476)	83,711	394,009	33,000	102,447	529,456
Net profit for the year before reclassification adjustments	-	-	-	-	-	-	-	-	7,915	7,915	-	455	8,370
Reclassification adjustments	-	-	-	-	-	-	59,826	27,939	(87,765)	-	-	-	-
Other comprehensive income	-	-	-	-	-	-	3,007	5,666	-	8,673	-	682	9,355
Total comprehensive income for the year	-	-	-	-	-	-	62,833	33,605	(79,850)	16,588	-	1,137	17,725
Capital reduction	(107,519)	18,131	(5,772)	(50,633)	(36,387)	(14,248)	-	-	(7,689)	(204,117)	-	-	(204,117)
Transfers during the year	-	-	-	-	(15,000)	-	-	-	15,000	-	-	-	-
Interest payment on Tier 1 capital	-	-	-	-	-	-	-	-	(3,513)	(3,513)	-	-	(3,513)
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	(76,682)	(76,682)
Balance at 31 December 2017	**101,132**	**-**	**5,687**	**49,881**	**29,612**	**-**	**12,867**	**(3,871)**	**7,659**	**202,967**	**33,000**	**26,902**	**262,869**
Balance at 1 January 2016	208,651	(18,131)	11,459	99,888	80,373	14,248	(48,159)	(34,890)	80,497	393,936	-	109,331	503,267
Profit (loss) for the year	-	-	-	-	-	-	-	-	6,259	6,259	-	(5,386)	873
Other comprehensive loss	-	-	-	-	-	-	(1,807)	(2,586)	-	(4,393)	-	(705)	(5,098)
Total comprehensive (loss) income for the year	-	-	-	-	-	-	(1,807)	(2,586)	6,259	1,866	-	(6,091)	(4,225)
Perpetual Tier 1 capital (note 18)	-	-	-	-	-	-	-	-	-	-	33,000	-	33,000
Interest payment on Tier 1 capital	-	-	-	-	-	-	-	-	(1,793)	(1,793)	-	-	(1,793)
Transfers during the year	-	-	-	626	626	-	-	-	(1,252)	-	-	-	-
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	(793)	(793)
Balance at 31 December 2016	208,651	(18,131)	11,459	100,514	80,999	14,248	(49,966)	(37,476)	83,711	394,009	33,000	102,447	529,456

The attached explanatory notes 1 to 32 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 ("UGHC") which owns 100% shares of the Bank and ultimate holding company is Kuwait Projects Company (Holding) K.S.C. ("KIPCO"). UGHC 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.

Restructuring
On 7 September 2017, the Bank's directors announced the reorganisation of the Bank's operations following which the Bank's Board of Directors, the CBB and the Bank's shareholders approved the reorganisation plan in an Extraordinary General Meeting held on 25 September 2017. In this regard, UGHC acquired entire shareholding of UGB via a share swap offer of 1 new UGHC share for 2 shares of UGB. Subsequent to the share swap, UGHC shares were listed on the Bahrain Bourse. Moreover, the portfolio of the core investments managed by UGB has been transferred to UGHC.

UGB has been delisted from the Bahrain Bourse but remains a wholesale conventional bank governed by CBB. The regulated banking activities and assets under management including investment banking along with related liabilities are retained at UGB level.

As at 31 December 2017, UGHC is the Bank's parent company and holds 100% shares of UGB and KIPCO being the ultimate parent company owns 98% of UGHC's outstanding shares (31 December 2016: 98% of the Bank's outstanding shares).

These consolidated financial statements were authorised for issue by the Board of Directors on 27 February 2018.

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 Central Bank of Bahrain and Financial Institutions Law and the Bahrain Commercial Companies Law, and the CBB Rulebook (Volume 1 and applicable provisions of Volume 6) and relevant CBB directives.

Basis of preparation
The consolidated financial statements have been prepared under the historical cost convention as modified by the remeasurement at fair value of investments carried at fair value through statement of income, non-trading investments, investment properties and derivative financial instruments.

Presentation and functional currency
The consolidated financial statements have been presented in US Dollars (US$) being the functional currency of the Group and are rounded to the nearest US$ thousands except when otherwise indicated.

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 loss or the total equity of the Company. For more details, please refer to the paragraph on Restructuring in note 1 above.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

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 amendments to IFRS, applicable to the Group, and which are effective from 1 January 2017:

2.1 Standards effective for the year

Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative
The amendments require entities to provide disclosure of changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses).

Amendments to IAS 7 Statement of Cash Flows
In January 2016, the IASB issued amendments to IAS 7 Statement of Cash Flows with the intention to improve disclosures of financing activities and help users to better understand the reporting entities' liquidity positions. Under the new requirements, entities will need to disclose changes in their financial liabilities as a result of financing activities such as changes from cash flows and non-cash items (e.g., gains and losses due to foreign currency movements). The amendment is effective from 1 January 2017.

Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses
The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of deductible temporary difference related to unrealised losses. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. The Group applied amendments retrospectively. However, their application has no effect on the Group's financial position and performance as the Group has no deductible temporary differences or assets that are in the scope of the amendments.

Annual Improvements 2012-2016 Cycle
These improvements include:

Amendments to IFRS 12 Disclosure of Interests in Other Entities: Clarification of the scope of disclosure
The amendments clarify that the disclosure requirements in IFRS 12, other than those in paragraphs B10–B16, apply to an entity's interest in a subsidiary, a joint venture or an associate (or a portion of its interest in a joint venture or an associate) that is classified (or included in a disposal group that is classified) as held for sale. As at 31 December 2017, the Group did not have any held for sale assets and that these amendments did not affect the Group's consolidated financial statements.

Significant accounting policies are set out below:

Principles of consolidation
The consolidated financial statements include the financial statements of the Bank and its subsidiaries as at 31 December 2017. 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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation (continued)

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

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

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

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

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

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.

The principal subsidiaries of the Bank are as follows:

Name of the subsidiary	*Country of incorporation*	*Ownership at 31 December 2017*	*Ownership at 31 December 2016*	*Year of incorporation*
Held directly				
KAMCO Investment Company K.S.C.P. [KAMCO]	Kuwait	86%	86%	1998
United Gulf Financial Services Company-North Africa	Tunisia	83%	85%	2008
United Gulf Realty International, Ltd [UGRIL]	British Virgin Islands	100%	100%	2012
FIMBank Group [FIMBank]	Malta	0%	61%	1994
Hatoon Real Estate Company	Kuwait	0%	98%	2008
Syria Gulf Investment Company	Syria	0%	99%	2007

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation (continued)

Name of the subsidiary	*Country of Incorporation*	*Ownership at 31 December 2017*	*Ownership at 31 December 2016*	*Year of Incorporation*
Held through KAMCO				
Al Dhiyafa United Real Estate Company W.L.L.	Kuwait	100%	100%	2007
Al Jazi Money Market Fund	Kuwait	51%	48%	2007
Al Tadamon United Holding Co	Kuwait	96%	0%	2017
Al Zad Real Estate W.L.L.	Kuwait	99%	99%	2007
Bukeye Power Project Advisory Co	U.S.A.	50%	0%	2017
Bukeye Power Project Manager Ltd	Jersey	100%	0%	2017
Flint Advisor Company Llc	Jersey	46%	0%	2017
Flint Manager Ltd	U.S.A.	100%	0%	2017
Kamco GCC Opportunistic Fund	Kuwait	100%	100%	2013
KAMCO Investment Company (DIFC) Limited	U.A.E.	100%	100%	2016
KAMCO Mena Plus Fixed Income Fund	Kuwait	71%	51%	2016
Kuwait Private Equity Opportunity Fund	Kuwait	73%	71%	2004
Nawasi United Holding Co	Kuwait	96%	0%	2017
North Africa Real Estate Co.	Kuwait	100%	100%	2014
Orange Real Estate Co. W.L.L.	Kuwait	0%	100%	2005
Held through FIMBank				
India Factoring and Finance Solutions Private Limited	India	0%	86%	2010
CIS Factors Holdings B.V.	Russia	0%	100%	2009
FIM Holdings (Chile) S.p.a.	Chile	0%	100%	2014
Latam Factors S.A.	Chile	0%	51%	2014
London Forfaiting Company Limited	United Kingdom	0%	100%	2009
London Forfaiting International Limited	United Kingdom	0%	100%	2009
London Forfaiting Americas Inc.	United States of America	0%	100%	2009
London Forfaiting do Brasil Ltd.	Brazil	0%	100%	2009
FIM Factors B.V.	Netherlands	0%	100%	2009
Menafactors Limited	United Arab Emirates	0%	100%	2009
FIM Business Solutions Limited	Malta	0%	100%	2009
FIM Property Investment Limited	Malta	0%	100%	2010
The Egyptian Company for Factoring S.A.E.	Egypt	0%	100%	2016

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
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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Investments in associates (continued)
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.

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurement (continued)
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 (Note 29)

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.

Investments carried at fair value through statement of income
Investments classified as carried at fair value through the statement of income comprise of two categories 'investments held for trading' and 'investments designated at fair value through statement of income'.

An investment is classified as 'held for trading' if it is acquired or incurred principally for the purpose of selling in the near term or if on initial recognition is part of a portfolio of identifiable financial investments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking. Derivatives which are not used as hedge are also categorised as held for trading.

Investments designated at fair value through statement of income are investments that are not classified as held for trading but are managed, and their performance is evaluated on a fair value basis in accordance with the Group's investment strategy.

These investments are initially recognised at fair value. Transaction costs are immediately expensed in the consolidated statement of income. Subsequent to initial recognition, investments designated at fair value through statement of income are remeasured at fair value and gains and losses arising from such remeasurement are included in the consolidated statement of income.

Non-trading investments
These are classified as follows:

- Held to maturity; and
- Available-for-sale

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Non-trading investments (continued)

Held to maturity
Investments with fixed or determinable payments and fixed maturities are classified as held to maturity when the Group has the positive intention and ability to hold these investments to maturity. These investments are initially recognised at fair value, including directly attributable transaction costs.

After initial recognition investments held to maturity are carried at amortised cost using the effective interest rate method. Any gain or loss on such investments is recognised in the consolidated statement of income when the investment is derecognised or impaired. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortisation is included in 'interest income' in the consolidated statement of income. The losses, if any, arising from impairment of such investments are recognised in the consolidated statement of income.

Investments available-for-sale
Investments available-for-sale include equity investments and debt securities. Investments available-for-sale are those non-derivative financial assets that are designated as available-for-sale or are not classified as investment at fair value through statement of income, investments held to maturity or loans and receivables.

These investments are initially recognised at fair value, including directly attributable transaction costs.

After initial recognition, available-for-sale investments are measured at fair value with gains and losses being recognised in the consolidated OCI until the investment is derecognised or determined to be impaired at which time the cumulative gains or losses previously reported in the consolidated OCI are recognised in the consolidated statement of income. Investments whose fair value cannot be reliably measured are carried at cost less impairment losses, if any.

Dividends are included in 'dividend income'. Interest income on available-for-sale investments is recorded in 'interest income' in the consolidated statement of income, using the effective interest yield method.

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.

Derivatives and hedge accounting
The Group makes use of derivative instruments to manage exposure to foreign currency risk and interest rate risk. In order to manage a particular risk, the Group applies hedge accounting to transactions which meet the specified criteria. The Group enters into derivative instruments, mainly forward foreign exchange contracts, interest rate and forward currency swaps in the foreign exchange markets.

Derivatives embedded in host contracts are accounted for as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contracts and the host contracts are not held for trading or designated at fair value though profit or loss. These embedded derivatives are measured at fair value with changes in fair value recognised in profit or loss. Reassessment only occurs if there is either a change in the terms of the contract that significantly modifies the cash flows that would otherwise be required or a reclassification of a financial asset out of the fair value through profit or loss.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivatives and hedge accounting (continued)
Derivatives are initially recognised and subsequently measured at fair value with transaction costs taken directly to the consolidated statement of income. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative. Derivatives with positive fair values (unrealised gains) are included in other assets and derivatives with negative fair values (unrealised losses) are included in other liabilities in the consolidated statement of financial position.

Any gains or losses arising from changes in the fair value of derivatives are taken directly to the consolidated statement of income, except for the effective portion of cash flow hedges, which is recognised in consolidated OCI and later reclassified to the consolidated statement of income when the hedge item affects the consolidated statement of income.

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

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

For the purpose of hedge accounting, hedges are classified into three categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability; (b) cash flow hedges which hedge exposure to variability in cash flows of a recognised asset or liability or a forecasted transaction; and (c) hedge of net investment in a foreign operation.

Fair value hedges
In relation to fair value hedges, that qualify for hedge accounting, any gain or loss from remeasuring the hedging instrument to fair value, as well as related changes in fair value of the item being hedged, are recognised immediately in the consolidated statement of income. At 31 December 2017 and 2016 there were no hedges classified as fair value hedges.

Cash flow hedges
In relation to cash flow hedges the effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised directly in the fair value reserve in the consolidated OCI. The gain or loss relating to the ineffective portion is recognised in the consolidated statement of income.

When the hedged cash flow affects the consolidated statement of income, the gain or loss on the hedging instrument is recycled in the corresponding income or expense line of the consolidated statement of income. When the hedging instrument expires or is sold, terminated or exercised or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at the time remains in equity and is recognised when the hedged forecast transaction is ultimately recognised in the consolidated statement of income. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the consolidated statement of income.

Hedge of net investments in foreign operations
Hedges of a net investment in a foreign operation are accounted for in a way similar to cash flow hedges. On the disposal of the foreign operation, the cumulative value of any such gains or losses recognised in equity through consolidated OCI is transferred to the consolidated statement of income.

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

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivatives and hedge accounting (continued)

Hedge of net investments in foreign operations (continued)
Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. For discontinued fair value hedges of financial instruments with fixed maturities any adjustment arising from hedge accounting is amortised over the remaining term to maturity. For discontinued cash flow hedges or hedges of net investments in foreign operations, any cumulative gain or loss on the hedging instrument recognised in equity remains in equity until the hedged transaction occurs. If the hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the consolidated statement of 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.

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

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.

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

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.

Impairment of financial assets
An assessment is made at each statement of financial position date to determine whether there is objective evidence that a specific financial asset may be impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicates that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults. If such evidence exists, an impairment loss, is recognised in the consolidated statement of income.

Financial assets carried at amortised cost
A financial asset is considered impaired when there is an objective evidence of credit-related impairment as a result of one or more loss event(s) that occurred after the initial recognition of the asset and those loss events have an impact on the estimated future cash flows of the financial asset or group of financial assets and can be reliably estimated.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets (continued)
A specific provision for credit losses, due to impairment of a loan or any other financial asset held at amortised cost, is established if there is objective evidence that the Group will not be able to collect all amounts due. The amount of the specific provision is the difference between the carrying amount and the estimated recoverable amount. The estimated recoverable amount is the present value of expected cash flows, including amounts estimated to be recoverable from guarantees and collateral, discounted based on the original effective yield basis.

In addition to a specific provision for credit losses, a provision for collective impairment is made on a portfolio basis for credit losses where there is an objective evidence that unidentified losses exist at the reporting date. These are based on any deterioration in the risk rating (i.e. downward migration of risk ratings) of the financial asset since it was originally granted. This provision is estimated based on various factors including credit ratings allocated to a borrower or group of borrowers, the current economic conditions, the experience the Group has had in dealing with a borrower or group of borrowers and available historical default information.

The carrying amount of the asset is adjusted through the use of a provision for impairment account and the amount of the adjustment is included in the consolidated statement of income.

Investments available-for-sale
For available-for-sale financial assets, the Group assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

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

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of income. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the consolidated statement of income, the impairment loss is reversed through the consolidated statement of income.

Impairment of non-financial assets
Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised in the consolidated statement of income for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell, and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units). The impairment test also can be performed on a single asset when the fair value less costs to sell or the value in use can be determined reliably. Non-financial assets other than goodwill that suffer impairment are reviewed for possible reversal of the impairment at each reporting date.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

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.

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 the statement of income are included in the consolidated statement of income for the year. Exchange differences arising on the retranslation of available for sale equity investments, 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.

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial guarantee contracts
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.

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:

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.

Classification of investments
Management decides on acquisition of an investment whether it should be classified as carried at fair value through statement of income, held to maturity or available-for-sale.

The Group classifies investments as held for trading if they are acquired primarily for the purpose of making short term profit. Classification of investments designated as fair value through statement of income depends on how management monitors the performance of these investments.

For those deemed to be held to maturity, management ensures that the requirements of IAS 39 are met and in particular the Group has the intention and ability to hold these to maturity.

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

The key assumptions concerning the future and other key sources of estimation uncertainty at the statement of financial position date, that have a risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

Impairment of investments
The Group treats available-for-sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires considerable judgment.

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.

Impairment losses on loans and receivables
The Group reviews its loans and receivables on a quarterly basis to assess whether a provision for impairment should be recorded in the consolidated statement of income. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Significant assumptions, accounting judgements and estimates (continued)

Collective impairment provisions on loans and receivables
In addition to specific provisions against individually significant loans and receivables, the Group also makes a collective impairment provision against loans and receivables, which although not specifically identified against a loan, have a greater risk of default than when originally granted. This collective provision is based on any deterioration in the internal grade of the loan since it was granted. The amount of the provision is based on the historical loss pattern for loans within each grade and is adjusted to reflect current economic changes.

These internal gradings take into consideration factors such as any deterioration in country risk, industry, technological obsolescence as well as identified structural weaknesses or deterioration in 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.

3 PROSPECTIVE CHANGES IN ACCOUNTING POLICIES

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:

IFRS 9 Financial Instruments

Introduction
In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments that replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

Classification and measurement
From a classification and measurement perspective, the new standard will require all financial assets, except equity instruments and derivatives, to be assessed based on a combination of the entity's business model for managing the assets and the instruments' contractual cash flow characteristics. The IAS 39 measurement categories will be replaced by: fair value through profit or loss (FVPL), fair value through other comprehensive income (FVOCI), and amortised cost. IFRS 9 will also allow entities to continue to irrevocably designate instruments that qualify for amortised cost or fair value through OCI instruments as FVPL, if doing so eliminates or significantly reduces a measurement or recognition inconsistency. Equity instruments that are not held for trading may be irrevocably designated as FVOCI, with no subsequent reclassification of gains or losses to the statement of profit or loss.

The accounting for financial liabilities will largely be the same as the requirements of IAS 39, except for the treatment of gains or losses arising from an entity's own credit risk relating to liabilities designated at FVPL. Such movements will be presented in OCI with no subsequent reclassification to the income statement, unless an accounting mismatch in profit or loss would arise.

3 PROSPECTIVE CHANGES IN ACCOUNTING POLICIES (continued)

New standards and interpretations issued but not yet effective (continued)

IFRS 9 Financial Instruments (continued)

Classification and measurement (continued)
The following is the outcome of an initial high level impact assessment performed by the Group during 2016:

- The majority of loans and advances to banks and customers, that are classified as loans and advances under IAS 39 are expected to be measured at amortised cost under IFRS 9;
- Financial assets held for trading and financial assets designated at FVPL are expected to continue to be measured at FVPL;
- The majority of the debt securities classified as available for sale under IAS 39 are expected to be measured at amortised cost or FVOCI. Some securities, however, will be classified as FVPL, either because of their contractual cash flow characteristics or the business model within which they are held; and
- Debt securities classified as held to maturity are expected to continue to be measured at amortised cost.

Hedge accounting
The Group believes that all existing hedge relationships that are currently designated in effective hedging relationships will still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the Group does not expect a significant impact as a result of applying IFRS 9.

Impairment of financial assets
IFRS 9 will also fundamentally change the loan loss impairment methodology. The standard will replace IAS 39's incurred loss approach with a forward-looking Expected Credit Loss (ECL) approach. The Group will be required to record an allowance for expected losses for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. The allowance is based on the expected credit losses associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination, in which case, the allowance is based on the probability of default over the life of the asset.

The Group is currently working on establishing 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.

- To calculate ECL, the Group will estimate 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.

Under IFRS 9, the Group expects to group its loans into Stage 1, Stage 2 and Stage 3, based on the applied impairment methodology, as described below:

- Stage 1 – Performing loans: when loans are first recognised, the Group recognises an allowance based on 12-month expected credit losses.
- Stage 2 – Underperforming loans: when a loan shows a significant increase in credit risk, the Group records an allowance for the lifetime expected credit loss.
- Stage 3 – Impaired loans: the Group recognises the lifetime expected credit losses for these loans. In addition, in Stage 3 the Group recognises interest income on receipt basis.

During the year, the Group performed a detailed impact assessment taking into consideration the above impairment methodology.

3 PROSPECTIVE CHANGES IN ACCOUNTING POLICIES

New standards and interpretations issued but not yet effective (continued)

IFRS 15 Revenue from Contracts with Customers
In May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, effective for periods beginning on 1 January 2018 with early adoption permitted. IFRS 15 defines principles for recognising revenue and will be applicable to all contracts with customers. However, interest and fee income integral to financial instruments and leases will continue to fall outside the scope of IFRS 15 and will be regulated by the other applicable standards (e.g., IFRS 9, and IFRS 16 Leases).

Revenue under IFRS 15 will need to be recognised as goods and services are transferred, to the extent that the transferor anticipates entitlement to goods and services. The standard will also specify a comprehensive set of disclosure requirements regarding the nature, extent and timing as well as any uncertainty of revenue and corresponding cash flows with customers.

The Group does not anticipate early adopting IFRS 15 and does not expect any material impact on the consolidated financial statements of the Group.

IFRS 16 Leases
The IASB issued the new standard for accounting for leases - IFRS 16 Leases in January 2016. The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognise most leases on their balance sheets as lease liabilities, with the corresponding right-of-use assets. Lessees must apply a single model for all recognised leases, but will have the option not to recognise 'short-term' leases and leases of 'low-value' assets. Generally, the profit or loss recognition pattern for recognised leases will be similar to today's finance lease accounting, with interest and depreciation expense recognised separately in the statement of profit or loss.

IFRS 16 is effective for annual periods beginning on or after 1 January 2019. Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date. Lessees must adopt IFRS 16 using either a full retrospective or a modified retrospective approach.

The Group does not anticipate early adopting IFRS 16 and does not expect any material impact on the consolidated financial statements of the Group.

4 FINANCIAL ASSETS AND LIABILITIES

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

31 December 2017	*Held for trading US$ 000*	*Designated at fair value through statement of income US$ 000*	*Available-for-sale US$ 000*	*Amortised cost / Loans and receivables US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	-	97,993	97,993
Placements with banks	-	-	-	68,577	68,577
Investments carried at fair value through statement of income	17,983	1,285	-	-	19,268
Non-trading investments	-	-	221,566	-	221,566
Loans and receivables	-	-	-	4,216	4,216
Other assets	-	1,100	-	29,740	30,840
Total financial assets	17,983	2,385	221,566	200,526	442,460
Due to banks and other financial institutions	-	-	-	250,211	250,211
Deposits from customers	-	-	-	31,018	31,018
Loans payable	-	-	-	98,658	98,658
Other liabilities	115	-	-	37,243	37,358
Total financial liabilities	115	-	-	417,130	417,245

31 December 2016	*Held for trading US$ 000*	*Designated at fair value through statement of income US$ 000*	*Available-for-sale US$ 000*	*Amortised cost / Loans and receivables US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	-	176,880	176,880
Placements with banks	-	-	-	187,350	187,350
Investments carried at fair value through statement of income	26,050	19,128	-	-	45,178
Non-trading investments	-	-	404,436	-	404,436
Loans and receivables	-	-	-	1,184,804	1,184,804
Other assets	-	845	-	107,825	108,670
Total financial assets	26,050	19,973	404,436	1,656,859	2,107,318
Due to banks and other financial institutions	-	-	-	726,222	726,222
Deposits from customers	-	-	-	985,210	985,210
Loans payable	-	-	-	652,125	652,125
Subordinated debt	-	-	-	50,000	50,000
Other liabilities	5,478	-	-	57,246	62,724
Total financial liabilities	5,478	-	-	2,470,803	2,476,281

5 INVESTMENTS CARRIED AT FAIR VALUE THROUGH STATEMENT OF INCOME

	2017 US$ 000	2016 US$ 000
Investments held for trading		
Quoted equities	**6,305**	15,485
Quoted debt securities	**11,678**	10,565
Investments designated at fair value through statement of income		
Credit linked notes	**-**	17,800
Managed funds	**1,285**	1,328
	19,268	45,178

Managed funds primarily represent funds invested through 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.

6 NON-TRADING INVESTMENTS

Non-trading investments comprise available-for-sale investments as follows:

	2017 US$ 000	2016 US$ 000
Quoted		
Debt securities	**-**	161,842
Equities	**42,081**	57,825
Total quoted	**42,081**	219,667
Unquoted		
Equities	**143,117**	121,281
Other managed funds	**36,074**	51,514
Real estate managed funds	**294**	11,974
Total unquoted	**179,485**	184,769
Total non-trading investments	**221,566**	404,436

Included under non-trading investments are unquoted available-for-sale investments, primarily representing nominal equity stakes up to 1.1% (2016:13.9%) in various geographically and sectorally dispersed companies, amounting to US$ 61,294 thousand (2016: US$ 43,789 thousand) for which fair value cannot be determined with sufficient accuracy, as future cash flows are not determinable. Accordingly, these investments are carried at cost less provisions for impairment.

The movement in provision for non-trading investments was as follows:

	2017 US$ 000	2016 US$ 000
At 1 January	**22,467**	21,502
Charge for the year	**462**	1,300
Reversed upon disposal	**(6,927)**	(335)
Net movement during the year	**(6,465)**	965
At 31 December	**16,002**	22,467
Gross amount of individually impaired investments	**17,030**	39,887

7 LOANS AND RECEIVABLES

	2017 US$ 000	2016 US$ 000
Forfaiting assets	-	538,226
Factoring assets	-	220,597
Loans to customers	**4,077**	168,612
Loans to banks	-	173,766
Syndication loans	-	124,024
Staff loans	**2,674**	3,115
	6,751	1,228,340
Less: Provision for impairment	**(2,535)**	(43,536)
	4,216	1,184,804

The movement in the provision for impairment is as follows:

	2017		
	Specific US$ 000	Collective US$ 000	Total US$ 000
At 1 January	**28,913**	**14,623**	**43,536**
Provided during the year - net	-	**2,129**	**2,129**
Written-off during the year	-	**(2,107)**	**(2,107)**
Transferred under restructuring	**(28,913)**	**(12,110)**	**(41,023)**
Balance at 31 December	-	**2,535**	**2,535**

	2016		
	Specific US$ 000	Collective US$ 000	Total US$ 000
At 1 January	34,078	10,082	44,160
Provided (written-back) during the year - net	2,388	5,867	8,255
Written-off during the year	(8,161)	-	(8,161)
Other adjustments	608	(1,326)	(718)
Balance at 31 December	28,913	14,623	43,536

	2017 US$ 000	2016 US$ 000
Gross amount of loans, individually determined to be impaired	-	70,527

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

	Neither past due nor impaired US$ 000	Past due but not impaired US$ 000	Past due and impaired US$ 000	Total US$ 000
31 December 2017				
Loans to customers	**4,077**	-	-	**4,077**
Staff loans	**2,674**	-	-	**2,674**
Total	**6,751**	-	-	**6,751**

7 LOANS AND RECEIVABLES (continued)

	Neither past due nor impaired US$ 000	*Past due but not impaired US$ 000*	*Past due and impaired US$ 000*	*Total US$ 000*
31 December 2016				
Forfaiting assets	505,397	7,238	25,591	538,226
Factoring assets	220,597	-	-	220,597
Loans to customers	149,680	-	18,932	168,612
Loans to banks	165,328	-	8,438	173,766
Syndication loans	106,458	-	17,566	124,024
Staff loans	3,115	-	-	3,115
Total	1,150,575	7,238	70,527	1,228,340

8 OTHER ASSETS

	***2017* US$ 000**	*2016 US$ 000*
Due from customers	**16,379**	29,497
Deferred tax asset (Note 12)	-	41,884
Accounts receivable	**13,203**	31,410
Prepayments	**980**	4,065
Interest receivable	**158**	5,034
Derivative assets (Note 27)	**1,100**	845
	31,820	112,735

Due from customers and accounts receivable are stated net of provision of US$ 77 thousand (2016: US$ 157 thousand). During the year, provisions of US$ 766 thousand were made against doubtful receivables (2016: reversal of US$ 170 thousand).

9 INVESTMENTS IN ASSOCIATES

		Activity	***Carrying value 2017* US$ 000**	***Ownership 2017* %**	*Carrying value 2016 US$ 000*	*Ownership 2016 %*
a)	Kamco Investment Fund	Fund	**22,750**	**23**	-	-
b)	Kuwait Education Fund	Fund	**14,139**	**34**	19,552	34
c)	United Capital Transport Co K.S.C.C.	Transport	**15,038**	**40**	16,530	40
d)	Manafae Investment Company	Islamic investment	**12,870**	**31**	12,855	31
e)	N.S. 88	Real estate	**12,280**	**20**	12,292	20
f)	Arab Leadership Academy	Training institute	**414**	**15**	408	15
g)	United Real Estate Company - Syria	Real estate	**21**	**20**	22	20
h)	Al Sharq Financial Brokerage Co.	Brokerage and investment business	-	-	7,501	19
i)	Meena Homes Real Estate Company	Real estate	-	-	806	20
j)	Burgan Bank S.A.K.	Commercial banking	-	-	484,095	15

9 INVESTMENTS IN ASSOCIATES (continued)

		Activity	*Carrying value 2017 US$ 000*	*Ownership 2017 %*	*Carrying value 2016 US$ 000*	*Ownership 2016 %*
k)	United Real Estate Company	Real estate	-	-	67,084	10
l)	North Africa Holding Company	Investments	-	-	49,027	44
m)	Assoufid B.V.	Holding, finance and project-development	-	-	33,677	40
n)	Syria Gulf Bank	Commercial banking	-	-	4,033	31
o)	Brasilfactors	Factoring and Forfaiting	-	-	1,161	50
p)	Takaud Savings & Pensions Company	Pension funds	-	-	-	50
			77,512		709,043	

The Group has no share of any contingent liabilities or capital commitments, as at 31 December 2017 and 2016 on behalf of its associates.

a) During the year, the Group acquired an additional 3.82% equity interest in KAMCO Investment Fund ("KIF") (previously classified as a financial assets available for sale) through its subsidiary KAMCO, for a cash consideration of US$ 4,306 thousand. Accordingly, the Group's equity interest in KIF increased from 19.16% to 22.98%. Following the acquisition of additional equity interest, the Group determined that it exercises significant influence over KIF and hence became an associate of the Group. As a result, the Group has recognised a gain on previously held equity interest of US$ 3,431 thousand in the consolidated statement of income.

b) Kuwait Education Fund is a fund incorporated in the State of Kuwait in 2007. As of 31 December 2017, the Bank owns 34% through its subsidiary KAMCO (2016: 34%).

c) United Capital Transport Company K.S.C.C. (UniCap) was incorporated in State of Kuwait in 2011. The Bank owns a 40% (2016: 40%) equity stake through its subsidiary KAMCO. UniCap is a dedicated leasing solutions provider to governments, international oil companies and varied construction, mining and industrial services businesses.

d) The Bank indirectly owns 31% (2016: 31%) of Manafae Investment Company through its subsidiary KAMCO.

e) The Bank indirectly owns 20% (2016: 20%) of N.S. 88 through its subsidiary KAMCO, formerly known as Savannah SPV.

f) Arab Leadership Academy is a training institute incorporated in the State of Kuwait in 2007. As of 31 December 2017, the Bank owns 15% (2016: 15%) through its subsidiary KAMCO. The Group has significant influence by appointment of directors on the Board of Directors of Arab Leadership Academy.

g) United Real Estate Company - Syria is a closed company incorporated in the Syrian Arab Republic. At 31 December 2017, the Bank directly owns 20% (2016: 20%) of its equity stake.

h) During the year, the Group's effective interest in Al Sharq Financial Brokerage Company K.S.C. (Closed) ("Al Sharq") through its subsidiary KAMCO diluted to 7.33% as a result of subscription of rights issue by the other shareholders. Accordingly, upon loss of significant influence, the Group has reclassified its investment in Al Sharq to financial assets available for sale. Upon reclassification, the Group has fair valued its previously held interest in Al Sharq and recorded a loss of US$ 460 thousand in the consolidated statement of income.

9 INVESTMENTS IN ASSOCIATES (continued)

i) During the year, the Group sold its entire equity interest in MENA Homes Real Estate Company KSCC, an associate of the Group. As at December 2016, the Group owned 20% shares of the associate.

j) to p) UGB embarked on its corporate reorganization plan during 2017 whereby the regulated banking activities were segregated from non-regulated services. For this purpose, KIPCO, UGB's major shareholder floated a Bahraini Shareholding Company (Public) in the Kingdom of Bahrain in the name of United Gulf Holding Company B.S.C. ("UGHC") which acquired 100% shareholding of UGB (regulating banking entity). The reorganization plan, including the share swap of 1 UGHC share for every 2 UGB shares, was approved by the shareholders of UGB in an EGM on 25th September 2017 subsequent to obtaining regulatory approvals. As part of the reorganization, beneficial interest in these associates was transferred to UGHC. These investments are being held under trust with UGB as per the Bahrain Trust Law under The Royal Decree No. 23 dated 13th October 2016, pending completion of the legal process for the transfer.

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 2017 (2016: same).

Investments in associates that are individually not significant
The aggregate summarised financial information of the Group's associates that are not individually significant are provided below:

	2017	*2016*
	US$ 000	*US$ 000*
Summarised statement of financial position as of 31 December:		
Total assets	**243,037**	519,826
Total liabilities	**(2,786)**	(210,429)
Equity	**240,251**	309,397
Carrying amount of investments	**77,512**	157,864
Summarised statement of income for the year ended 31 December:		
Revenue	**14,666**	103,970
(Loss) / gain for the year	**(2,879)**	9,383
Other comprehensive loss for the year	**-**	(34,489)
Total comprehensive loss for the year	**(2,879)**	(25,106)
Group's share of (loss) / profit for the year	**(1,092)**	2,254

10 INVESTMENT PROPERTIES

	2017	*2016*
	US$ 000	*US$ 000*
At 1 January	**101,326**	46,222
Acquisition	**-**	56,000
Revaluation	**2,732**	-
Foreign currency translation and other adjustments	**1,035**	(896)
At 31 December	**105,093**	101,326

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 property. The Group's investment properties are categorised in level 3 of the fair value hierarchy as at 31 December 2017 and 2016.

11 GOODWILL

	2017 US$ 000	2016 US$ 000
At 1 January	**51,868**	52,321
Foreign currency translation adjustments	**719**	(453)
Transferred as part of restructuring	**(197)**	-
At 31 December	**52,390**	51,868

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 3% (2016: 3%) and discount factor of 9.5% (2016: 10.7%). There was no goodwill impairment identified in 2017 or 2016 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	**12,169**	**(11,101)**
Discount factor	**(40,750)**	**54,811**

12 TAXATION - NET

The Group's subsidiaries in Malta, the United Kingdom, India, Chile and the United States of America were subject to income tax in their respective jurisdictions. During the year, all such subsidiaries, with the exception of UGRIL, were transferred to UGH as part of the Group's restructuring.

a) Deferred tax assets

Deferred tax assets relate to the following:

	2017 US$ 000	2016 US$ 000
Excess of capital allowances over depreciation	-	(294)
Allowances for uncollectibility	-	18,069
Changes in fair value of financial instruments	-	3,578
Investment tax credits	-	239
Unabsorbed capital allowances	-	542
Unabsorbed tax losses	-	19,750
	-	41,884

12 TAXATION (continued)

Reconciliation of deferred tax assets is as follows:

2017	*Opening balance US$ 000*	*Transferred as part of restructuring US$ 000*	*Recognised in consolidated statement of income US$ 000*	*Effects of movement in exchange rates US$ 000*	*Closing balance US$ 000*
Excess of capital allowances over depreciation	**(294)**	**294**	**-**	**-**	**-**
Allowances for uncollectibility	**18,069**	**(18,069)**	**-**	**-**	**-**
Changes in fair value of financial instruments	**3,578**	**(3,578)**	**-**	**-**	**-**
Investment tax credits	**239**	**(239)**	**-**	**-**	**-**
Unabsorbed capital allowances	**542**	**(542)**	**-**	**-**	**-**
Unabsorbed tax losses	**19,750**	**(19,750)**	**-**	**-**	**-**
	41,884	**(41,884)**	**-**	**-**	**-**
2016					
Excess of capital allowances over depreciation	(416)	-	122	-	(294)
Allowances for uncollectibility	23,610	-	(5,279)	(262)	18,069
Changes in fair value of financial instruments	163	798	2,617	-	3,578
Investment tax credits	328	-	(89)	-	239
Unabsorbed capital allowances	275	-	267	-	542
Unabsorbed tax losses	16,608	-	3,059	83	19,750
	40,568	798	697	(179)	41,884

b) Deferred tax liabilities

Deferred tax liabilities relate to the following:

	***2017* US$ 000**	*2016 US$ 000*
Excess of capital allowances over depreciation	**390**	403
Changes in fair value of financial instruments	**2,859**	1,799
	3,249	2,202

Reconciliation of deferred tax liabilities is as follows:

2017	*Opening balance*	*Recognised in consolidated statement of income*	*Closing balance*
Excess of capital allowances over depreciation	**403**	**(13)**	**390**
Changes in fair value of financial instruments	**1,799**	**1,060**	**2,859**
	2,202	**1,047**	**3,249**
2016			
Excess of capital allowances over depreciation	403	-	403
Changes in fair value of financial instruments	1,805	(6)	1,799
	2,208	(6)	2,202

12 TAXATION (continued)

c) Income tax credit

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

	2017 *US$ 000*	*2016* *US$ 000*
Consolidated statement of income		
Current income tax charge	**(2,065)**	(14)
Movement in deferred tax assets recognised in statement of income	**-**	-
Movement in deferred tax liabilities recognised in statement of income	**1,047**	(6)
Income tax credit reported in the consolidated statement of income - net	**(1,018)**	(20)

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.

13 LOANS PAYABLE

31 December 2017	***Currency****	***Bank*** ***US$ 000***	***Subsidiaries*** ***US$ 000***	***Total*** ***US$ 000***
Maturing within one year				
1 month or less	KWD	**-**	**662**	**662**
3 months or less but over 1 month	KWD	**-**	**16,501**	**16,501**
	GBP	**-**	**2,419**	**2,419**
1 year or less but over 3 months	US$	**-**	**2,749**	**2,749**
	GBP	**-**	**3,534**	**3,534**
	KWD	**-**	**28,652**	**28,652**
		-	**54,517**	**54,517**
Maturing after one year				
More than 1 year & less than 2	KWD	**-**	**16,562**	**16,562**
More than 2 years	KWD	**-**	**16,562**	**16,562**
	US$	**-**	**11,017**	**11,017**
		-	**44,141**	**44,141**
		-	**98,658**	**98,658**

31 December 2016	*Currency**	*Bank* *US$ 000*	*Subsidiaries* *US$ 000*	*Total* *US$ 000*
Maturing within one year				
1 month or less	Various	-	58,740	58,740
3 months or less but over 1 month	US$	-	40,000	40,000
1 year or less but over 3 months	US$	350,522	-	350,522
	KWD	-	60,438	60,438
		350,522	159,178	509,700
Maturing after one year				
More than 1 year & less than 2	EUR	-	15,789	15,789
	KWD	49,004	-	49,004
More than 2 years	KWD	-	16,335	16,335
	US$	50,000	11,297	61,297
		99,004	43,421	142,425
		449,526	202,599	652,125

* KWD represents Kuwaiti Dinar.

14 SUBORDINATED DEBT

As of 31 December 2016, the Group's sub-ordinated debt comprised of a 5-year loan amounting to US$ 50 million issued in 2015 by FIMBank, a subsidiary of the Group. The Group's investment in FIMBank was transferred to UGHC during the year as part of the Group's restructuring.

15 OTHER LIABILITIES

	2017 US$ 000	*2016 US$ 000*
Staff related payables	**20,019**	16,955
Accrued expenses	**3,002**	17,717
Interest payable	**322**	11,047
Dividends payable	**2,511**	2,508
Deferred tax (Note 12)	**3,249**	2,202
Derivative financial liabilities (Note 27)	**115**	5,478
Other payables	**8,140**	6,817
	37,358	62,724

16 EQUITY

a) Share capital

The Bank's authorised share capital as of 31 December 2017 comprised 1 billion shares of US$ 0.25 each (2016: 1 billion shares of US$ 0.25 each).

During the year, as part of the overall Group restructuring, the Bank reduced its share capital by 410,622,078 shares (US$ 107,519 thousand). The issued and fully paid up share capital as of 31 December 2017 comprised 404,526,082 shares of US$ 0.25 each (2016: 834,602,295 shares of US$ 0.25 each).

b) Treasury shares and treasury shares reserve

At 31 December 2017, the Bank does not hold treasury shares (2016: 19,454,135 shares). These were cancelled as part of the Group's restructuring.

c) 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.

d) 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 Central Bank of Bahrain.

e) General reserve

The Directors have approved a transfer of nil (2016:10%) of the profit of the Group for the year to general reserve in accordance with the Bank's Articles of Association. During the year, the Group transferred US$ 15,000 thousand from general reserves to retained earnings.

f) Dividend paid

No dividend was announced or paid during the years ended 31 December 2017 or 2016.

g) 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.

h) Reclassification adjustment

As part of the Group's restructuring, foreign currency losses of US$ 27,939 thousand and fair value losses of US$ 59,826 thousand were transferred to the consolidated statement of income.

17 FAIR VALUE RESERVE

	Note	*2017 US$ 000*	*2016 US$ 000*
Non-trading investments			
Balance at 1 January		**(50,811)**	(48,349)
Transferred to consolidated statement of income:			
- as part of restructuring	16 (h)	**59,826**	-
- sale of non-trading investments		**(1,880)**	2,681
Net movement in unrealised fair values during the year		**4,631**	(5,143)
Balance at 31 December		**11,766**	(50,811)
Cash flow hedges			
Balance at 1 January		**845**	190
Net movement in the fair values during the year		**256**	655
Balance at 31 December		**1,101**	845
		12,867	(49,966)

18 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 Central Bank of Bahrain.

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.

19 INTEREST INCOME

	2017 US$ 000	*2016 US$ 000*
Loans and receivables	**2,044**	1,616
Non-trading investments	**743**	958
Placements with banks	**1,243**	688
Demand and call deposits with banks	**401**	48
	4,431	3,310

20 INVESTMENT INCOME - NET

	2017 US$ 000	*2016 US$ 000*
Dividend income	**1,907**	1,774
Gain on sale of associates and subsidiaries	**2,668**	2,824
Rental income from investment properties	**4,757**	3,294
Gain on sale of non-trading investments	**4,369**	852
Gain (loss) on investments carried at fair value through statement of income	**3,902**	(3,603)
Unrealized gain on investment properties	**2,732**	-
Gain on sale due to reclassification of investment (Notes 9(a) and 9(h))	**2,971**	-
Others	**504**	4,612
	23,810	9,753

21 FEES AND COMMISSIONS - NET

	2017	*2016*
	US$ 000	*US$ 000*
Credit related fees, commissions and other income - net	**2,266**	(795)
Management fees from fiduciary activities	**15,971**	13,199
Advisory fees	**7,154**	7,426
	25,391	19,830

22 SHARE OF RESULTS OF ASSOCIATES - NET

	2017	*2016*
	US$ 000	*US$ 000*
Al Sharq Financial Brokerage Co.	**129**	(54)
Kamco Investment Fund	**(1,787)**	-
KAMCO Real Estate Yield Fund	**-**	349
Kuwait Education Fund	**1,055**	299
Manafae Investment Company	**(172)**	1,242
Meena Homes Real Estate Company	**-**	23
N.S. 88	**(2)**	722
Royal Capital Company P.S.C.	**-**	(35)
United Capital Transport Company	**(2,145)**	1,295
	(2,922)	3,841

23 INTEREST EXPENSE

	2017	*2016*
	US$ 000	*US$ 000*
Loans payable	**6,129**	5,264
Due to banks and other financial institutions	**7,548**	5,645
Deposits from customers	**1,555**	794
	15,232	11,703

24 CASH AND CASH EQUIVALENTS

	2017	*2016*
	US$ 000	*US$ 000*
Demand and call deposits with banks excluding mandatory reserves	**97,675**	169,717
Placements with original maturities of ninety days or less	**68,577**	187,350
	166,252	357,067

25 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:

	2017			
	Parent US$ 000	***Associates US$ 000***	***Other related parties US$ 000***	***Total US$ 000***
Gain on investments carried at fair value through statement of income	-	-	**48**	**48**
Gain on sale of non-trading investments	-	-	**(11)**	**(11)**
Fees and commissions - net*	**1,476**	**2,224**	**7,044**	**10,744**
Dividend income	-	-	**503**	**503**
Rental income	-	-	**2,457**	**2,457**
Interest income	-	-	**2,746**	**2,746**
Interest expense	-	-	**(19,319)**	**(19,319)**
Others	-	-	**(1,023)**	**(1,023)**

	2016			
	Parent US$ 000	*Associates US$ 000*	*Other related parties US$ 000*	*Total US$ 000*
Gain on investments carried at fair value through statement of income	-	36	1	37
Gain on sale of non-trading investments	-	-	274	274
Gain on sale of investments in associates	1,145	-	1,077	2,222
Fees and commissions - net	1,981	2,736	4,907	9,624
Dividend income	-	18	69	87
Rental income	2,246	221	-	2,467
Foreign currency translation losses - net	-	(12,529)	-	(12,529)
Interest income	-	1,899	880	2,779
Interest expense	(1,212)	(15,067)	(3,534)	(19,813)
Others	185	1,751	(959)	977
Purchase transactions				
Non-trading investments	49,449	45,000	-	94,449
Investment properties	56,000	-	-	56,000
Sale transactions				
Investments in associates**	146,000	-	-	146,000

*The Bank and UGHC have entered into an arrangement for service sharing between the two group entities. In line with the arrangement the Bank will provide certain services and incur certain expenses on behalf of UGHC.

** The Group had sold investments in associated companies of US$ 146,000 thousand and acquired certain non-trading investments of US$ 94,449 thousand and investment properties of US$ 56,000 thousand from related parties.

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

25 RELATED PARTY TRANSACTIONS (continued)

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

	2017			
	Parent US$ 000	*Associates US$ 000*	*Other related parties US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	-	**2,170**	**2,170**
Placements with banks	-	-	**22,777**	**22,777**
Investments carried at fair value through statement of income	-	-	**2,209**	**2,209**
Non-trading investments	-	-	**66,274**	**66,274**
Loans and receivables	-	-	**33,648**	**33,648**
Other assets	**2,357**	-	**7,212**	**9,569**
Due to banks and other financial institutions	-	-	**(134,689)**	**(134,689)**
Deposits from customers	-	-	**(18,902)**	**(18,902)**
Loans payable	-	-	**(14,078)**	**(14,078)**
Other liabilities	-	-	**(4,778)**	**(4,778)**
Perpetual Tier 1 Capital	-	-	**(10,000)**	**(10,000)**
Off statement of financial position items:				
Letters of guarantee	-	-	**150**	**150**

	2016			
	Parent US$ 000	*Associates US$ 000*	*Other related parties US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	5,944	180	6,124
Placements with banks	-	-	20,469	20,469
Investments carried at fair value through statement of income	-	-	2,179	2,179
Non-trading investments	-	-	26,852	26,852
Loans and receivables	-	7,545	23,354	30,899
Other assets	-	24,368	6,014	30,382
Due to banks and other financial institutions	-	(51,890)	(172,056)	(223,946)
Deposits from customers	(61)	(6,719)	(15,567)	(22,347)
Loans payable	-	(345,940)	-	(345,940)
Other liabilities	(614)	(1,670)	(2,727)	(5,011)
Subordinated debt	-	(50,000)	-	(50,000)
Perpetual Tier 1 Capital	-	-	(10,000)	(10,000)
Off statement of financial position items:				
Letters of guarantee	-	-	150	150

All related party transactions are on terms that are mutually agreed between the counterparties. All related party exposures are performing and are free of any provision for possible credit losses.

25 RELATED PARTY TRANSACTIONS (continued)

Compensation of key management personnel was as follows:

	2017 *US$ 000*	*2016* *US$ 000*
Short term employee benefits	**3,943**	8,716

26 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:

	2017 *US$ 000*	*2016* *US$ 000*
Credit related		
Letters of credit	**-**	52,044
Letters of guarantee	**812**	7,161
	812	59,205
Investment related commitments*	**4,017**	140,044
	4,829	199,249

* 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.

27 DERIVATIVES

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

			Notional amounts by term to maturity			
31 December 2017	*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	**774**	**(889)**	**427,968**	**274,505**	**153,463**	**-**
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	**-**	**-**	**245,114**	**245,114**	**-**	**-**
Derivatives used as cash flow hedges						
Interest rate swaps	**1,100**	**-**	**145,000**	**-**	**70,000**	**75,000**
31 December 2016						
Derivatives held for trading*						
Forward foreign exchange contracts	1,506	(8,827)	432,242	311,519	120,723	-
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	1,857	(14)	711,424	562,877	148,547	-
Derivatives used as cash flow hedges						
Interest rate swap	845	-	175,000	-	80,000	95,000

* 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$ 245 million (KWD 74 million) [2016: US$ 711 million (KWD 218 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.

27 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:

	2017		*2016*	
	Within 1 year US$ 000	***1-5 years US$ 000***	*Within 1 year US$ 000*	*1-5 years US$ 000*
Net cash outflows (liabilities)	**1,363**	**1,985**	1,347	873
Other comprehensive income	**1,100**	**-**	152	693

28 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 (in the case of major subsidiaries) 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 Acting 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 Acting 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 Acting 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.

28 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 Acting 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 Acting 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 Acting 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 Acting 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 Central Bank of Bahrain 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.

28 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 Acting Chief Executive Officer, Head of Treasury and the Chief Financial Officer. The Acting 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.

28 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 provision for impairment.

	2017 *US$ 000*	*2016* *US$ 000*
Demand and call deposits with banks	**97,993**	176,880
Placements with banks	**68,577**	187,350
Non-trading	**-**	161,842
Loans and receivables	**4,216**	1,184,804
Other assets	**29,740**	104,462
Letters of credit	**-**	52,044
Letters of guarantee	**812**	7,161
Derivative financial assets	**1,100**	845
	202,438	1,875,388

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 2017 was US$ 72.1 million (2016 US$ 120 million) 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*	*Asia* *US$ 000*	*Others* *US$ 000*	*Total* *US$ 000*
Demand and call deposits with banks	**22,064**	**111**	**1,963**	**73,844**	**-**	**11**	**97,993**
Placements with banks	**45,800**	**22,777**	**-**	**-**	**-**	**-**	**68,577**
Loans and receivables	**3,834**	**382**	**-**	**-**	**-**	**-**	**4,216**
Other assets	**27,715**	**1,257**	**4**	**764**	**-**	**-**	**29,740**
Letters of guarantee	**662**	**150**	**-**	**-**	**-**	**-**	**812**
Derivative financial assets	**1,100**	**-**	**-**	**-**	**-**	**-**	**1,100**
31 December 2017	**101,175**	**24,677**	**1,967**	**74,608**	**-**	**11**	**202,438**
Demand and call deposits with banks	33,250	8,342	110,218	23,603	646	821	176,880
Placements with banks	84,316	20,469	82,565	-	-	-	187,350
Non-trading investments	-	-	69,425	44,429	7,726	40,262	161,842
Loans and receivables	118,556	61,882	490,748	180,294	89,536	243,788	1,184,804
Other assets	43,132	2,979	34,890	4,004	17,793	1,664	104,462
Letters of credit	6,994	4,067	11,214	5,985	1,858	21,926	52,044
Letters of guarantee	4,748	-	1,907	105	-	401	7,161
Derivative financial assets	845	-	-	-	-	-	845
31 December 2016	291,841	97,739	800,967	258,420	117,559	308,862	1,875,388

28 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 2017	*Trading & Manufacturing US$ 000*	*Banks and other financial institutions US$ 000*	*Construction and real estate US$ 000*	*Individuals US$ 000*	*Government and public sector US$ 000*	*Others US$ 000*	*Total US$ 000*
Demand and call deposits with banks	-	97,993	-	-	-	-	97,993
Placements with banks	-	68,577	-	-	-	-	68,577
Loans and receivables	-	-	1,873	1,670	-	673	4,216
Other assets	15,283	5,366	2,298	752	-	6,041	29,740
Letters of guarantee	662	150	-	-	-	-	812
Derivative financial assets	-	1,100	-	-	-	-	1,100
	15,945	173,186	4,171	2,422	-	6,714	202,438
At 31 December 2016							
Demand and call deposits with banks	-	176,880	-	-	-	-	176,880
Placements with banks	-	187,350	-	-	-	-	187,350
Non-trading investments	4,825	94,525	-	-	62,492	-	161,842
Loans and receivables	298,156	661,416	56,179	1,916	34,811	132,326	1,184,804
Other assets	436	30,560	2,286	82	371	70,727	104,462
Letters of credit	8,618	43,426	-	-	-	-	52,044
Letters of guarantee	132	5,402	4	134	-	1,489	7,161
Derivative financial assets	-	845	-	-	-	-	845
	312,167	1,200,404	58,469	2,132	97,674	204,542	1,875,388

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 for commercial lending include charges over real estate properties, inventory, trade receivables, trading securities and bank guarantees.

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.

28 RISK MANAGEMENT (continued)

b) Credit risk (continued)

Collateral and other credit enhancements (continued)
An industry sector analysis of the Group's gross loans and advances, before and after taking into account collateral held or other credit enhancements, is as follows:

	Gross maximum exposure 2017 US$ 000	*Net maximum exposure 2017 US$ 000*	*Gross maximum exposure 2016 US$ 000*	*Net maximum exposure 2016 US$ 000*
Loans to banks	-	-	173,766	52,123
Loans to customers	4,077	4,077	168,612	140,515
Factoring assets	-	-	220,597	170,589
Forfaiting assets	-	-	538,226	538,226
Syndication loans	-	-	124,024	124,024
Staff loans	2,674	2,674	3,115	3,115
	6,751	6,751	1,228,340	1,028,592

Credit risk exposure for each credit rating

	Investment grade US$ 000	*Non-investment grade US$ 000*	*Unrated US$ 000*	*Total US$ 000*
At 31 December 2017				
Demand and call deposits with banks	97,498	318	177	97,993
Placements with banks	45,800	-	22,777	68,577
Loans and receivables	-	-	4,216	4,216
Other assets	1,406	34	28,300	29,740
Letters of guarantee	662	-	150	812
Derivative financial assets	1,100	-	-	1,100
	146,466	352	55,620	202,438
At 31 December 2016				
Demand and call deposits with banks	132,388	8,774	35,718	176,880
Placements with banks	140,565	-	46,785	187,350
Non-trading investments	161,842	-	-	161,842
Loans and receivables	88,347	247,267	849,190	1,184,804
Other assets	22,298	431	81,733	104,462
Letters of credit	-	3,215	48,829	52,044
Letters of guarantee	4,485	186	2,490	7,161
Derivative financial assets	845	-	-	845
	550,770	259,873	1,064,745	1,875,388

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.

28 RISK MANAGEMENT (continued)

b) 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 2017 (31 December 2016: US$ 17,258 thousand).

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 and receivables US$ 000	*Customer deposits US$ 000*
31 December 2017		
Gross amounts of recognised financial asset (liability)	**305,700**	**305,700**
Gross amounts offset in the consolidated statement of financial position	**(305,700)**	**(305,700)**
Net amount of financial liability presented in the consolidated statement of financial position	**-**	**-**
31 December 2016		
Gross amounts of recognised financial asset (liability)	133,450	(133,450)
Gross amounts offset in the consolidated statement of financial position	(133,450)	133,450
Net amount of financial 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 Central Bank of Bahrain. The Central Bank of Bahrain 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 purposes and does not actively trade in derivatives.

28 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 2017*	*Sensitivity of net interest income 2017 US$ 000*	*Increase in basis points 2016*	*Sensitivity of net interest income 2016 US$ 000*
Kuwaiti Dinar	+ 25	(356)	+ 25	(439)
United States Dollar	+ 25	(147)	+ 25	(404)
Euro	+ 25	13	+ 25	(1,093)
Pound Sterling	+ 25	-	+ 25	6
Others	+ 25	32	+ 25	76

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 2017, 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 % 2017*	*Effect on profit before tax 2017 US$ 000*	*Effect on equity 2017 US$ 000*	*Change in currency rate in % 2016*	*Effect on profit before tax 2016 US$ 000*	*Effect on equity 2016 US$ 000*
Kuwaiti Dinar	+2	(6,174)	2,143	+2	443	1,668
	-2	6,174	(2,143)	-2	(443)	(1,668)
Euro	+2	(59)	3	+2	8,001	-
	-2	59	(3)	-2	(8,001)	-
Pound Sterling	+2	(121)	-	+2	65	-
	-2	121	-	-2	(65)	-

28 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 2017	*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 statement of income					
Quoted equities	6,303	-	1	1	6,305
Managed funds	956	263	66	-	1,285
	7,259	263	67	1	7,590
Non-trading investments					
Quoted equities	31,514	-	10,567	-	42,081
Unquoted equities	111,629	25,609	5,879	-	143,117
Managed funds	34,129	-	2,239	-	36,368
	177,272	25,609	18,685	-	221,566
Total	184,531	25,872	18,752	1	229,156

At 31 December 2016	*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 statement of income					
Quoted equities	13,413	1,057	1	1,014	15,485
Managed funds	1,021	241	66	-	1,328
	14,434	1,298	67	1,014	16,813
Non-trading investments					
Quoted equities	46,265	-	11,560	-	57,825
Unquoted equities	92,900	21,237	7,144	-	121,281
Managed funds	57,544	5,576	368	-	63,488
	196,709	26,813	19,072	-	242,594
Total	211,143	28,111	19,139	1,014	259,407

At the reporting date, the exposure to listed equity securities at fair value was US$ 48,386 thousand (2016: US$ 73,310 thousand). A decrease of 10% on the market indices of MENA stock exchanges could have an impact of approximately US$ 4,839 thousand (2016: US$ 7,331 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 Kuwait Stock Exchange.

For unquoted investments carried at cost the impact of the changes in the equity prices will only be reflected in the consolidated statement of income when the investment is sold or deemed to be impaired.

28 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 2017 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 2017	On demand US$ 000	1 - 6 months US$ 000	6 - 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	133,661	16,757	101,423	-	-	251,841
Deposits from customers	62,395	6,323	-	-	-	68,718
Loans payable	663	40,270	14,746	49,224	-	104,903
Other liabilities	37,358	-	-	-	-	37,358
Total non-derivative undiscounted financial liabilities	234,077	63,350	116,169	49,224	-	462,820
Derivatives						
Net cash outflows on interest rate swaps	-	780	583	1,985	-	3,348
Gross settled foreign currency derivatives	-	673,082	-	-	-	673,082
Off-statement of financial position items						
Letters of guarantee	-	-	812	-	-	812
Investment related commitments	-	-	-	4,017	-	4,017

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

28 RISK MANAGEMENT (continued)

d) Liquidity risk (continued)

At 31 December 2016	*On demand US$ 000*	*1 - 6 months US$ 000*	*6 - 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	342,730	177,494	207,333	3,726	-	731,283
Deposits from customers	469,249	255,233	202,473	89,846	-	1,016,801
Loans payable	79,601	181,065	259,378	156,159	-	676,203
Subordinated debt	182	1,590	2,141	56,072	-	59,985
Other liabilities	-	-	62,724	-	-	62,724
Total non-derivative undiscounted financial liabilities	891,762	615,382	734,049	305,803	-	2,546,996
Derivatives						
Net cash outflows on interest rate swaps	-	773	574	873	-	2,220
Gross settled foreign currency derivatives	-	874,396	269,270	-	-	1,143,666
Off statement of financial position items						
Letters of credit	-	11,837	32,801	2,548	4,858	52,044
Letters of guarantee	-	2,139	479	4,543	-	7,161
Investment related commitments	-	-	-	140,044	-	140,044

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

28 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 2017

	Less than 12 months US$ 000	*Over 12 months US$ 000*	*Total US$ 000*
Demand and call deposits with banks	**97,675**	**318**	**97,993**
Placements with banks	**68,577**	**-**	**68,577**
Investments carried at fair value through statement of income	**19,268**	**-**	**19,268**
Non-trading investments	**42,081**	**179,485**	**221,566**
Loans and receivables	**1,564**	**2,652**	**4,216**
Other assets	**31,820**	**-**	**31,820**
Investments in associates	**-**	**77,512**	**77,512**
Investment properties	**-**	**105,093**	**105,093**
Property and equipment	**-**	**1,679**	**1,679**
Goodwill	**-**	**52,390**	**52,390**
Total assets	**260,985**	**419,129**	**680,114**
Due to banks and other financial institutions	**250,211**	**-**	**250,211**
Deposits from customers	**31,018**	**-**	**31,018**
Loans payable	**54,517**	**44,141**	**98,658**
Other liabilities	**37,358**	**-**	**37,358**
Total liabilities	**373,104**	**44,141**	**417,245**
Net	**(112,119)**	**374,988**	**262,869**

28 RISK MANAGEMENT (Continued)

d) Liquidity risk (continued)

At 31 December 2016

	Less than 12 months US$ 000	*Over 12 months US$ 000*	*Total US$ 000*
Demand and call deposits with banks	169,717	7,163	176,880
Placements with banks	187,350	-	187,350
Investments carried at fair value through statement of income	45,178	-	45,178
Non-trading investments	219,666	184,770	404,436
Loans and receivables	1,079,597	105,207	1,184,804
Other assets	112,735	-	112,735
Investments in associates and joint venture	-	709,043	709,043
Investment properties	-	101,326	101,326
Property and equipment	-	32,117	32,117
Goodwill	-	51,868	51,868
Total assets	1,814,243	1,191,494	3,005,737
Due to banks and other financial institutions	723,069	3,153	726,222
Deposits from customers	899,192	86,018	985,210
Loans payable	509,700	142,425	652,125
Subordinated debt	-	50,000	50,000
Other liabilities	-	62,724	62,724
Total liabilities	2,131,961	344,320	2,476,281
Net	(317,718)	847,174	529,456

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.

29 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. Non-trading investments carried at cost are disclosed in Note 6.

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 2017:

	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 statement of income				
Quoted equities	**6,305**	**-**	**-**	**6,305**
Quoted debt securities	**11,678**	**-**	**-**	**11,678**
Managed funds	**-**	**1,285**	**-**	**1,285**
Non-trading investments				
Equities - quoted	**42,081**	**-**	**-**	**42,081**
Equities - unquoted	**-**	**82,410**	**463**	**82,873**
Other managed funds	**-**	**25,011**	**10,342**	**35,353**
Derivatives				
Interest rate swaps	**-**	**1,100**	**-**	**1,100**
Investment properties	**-**	**-**	**105,093**	**105,093**
	60,064	**109,806**	**115,898**	**285,768**
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	**-**	**(115)**	**-**	**(115)**
	-	**(115)**	**-**	**(115)**

29 FAIR VALUE MEASUREMENT (continued)

Quantitative disclosures fair value measurement hierarchy for assets as at 31 December 2016:

	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 statement of income				
Quoted equities	15,485	-	-	15,485
Quoted debt securities	10,565	-	-	10,565
Credit linked notes	17,800	-	-	17,800
Managed funds	-	1,328	-	1,328
Non-trading investments				
Equities - quoted	57,825	-	-	57,825
Debt Securities - quoted	161,842	-	-	161,842
Equities - unquoted	-	78,052	474	78,526
Real estate managed funds - unquoted	-	11,673	-	11,673
Other managed funds	-	35,200	15,581	50,781
Derivatives				
Interest rate swaps	-	845	-	845
Investment properties	-	-	101,326	101,326
	263,517	127,098	117,381	507,996
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	-	(5,478)	-	(5,478)
	-	(5,478)	-	(5,478)

Transfers between Level 1, Level 2 and Level 3

During the year ended 31 December 2017 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:

	Equities	*Other managed funds*	*Debt securities*	*Investment properties*	*Total*
	US$ 000	*US$ 000*	*US$ 000*	*US$ 000*	*US$ 000*
As at 1 January 2016	478	12,599	2,968	46,222	62,267
Recognised in statement of income	-	71	-	-	71
Net purchases, sales and transfers and settlements	-	3,251	(2,968)	56,000	56,283
Remeasurement recognised in OCI	(4)	(340)	-	(896)	(1,240)
As at 1 January 2017	**474**	**15,581**	**-**	**101,326**	**117,381**
Recognised in statement of income	-	-	-	3,000	3,000
Net purchases, sales and transfers and settlements	(11)	(5,024)	-	-	(5,035)
Remeasurement recognised in OCI	-	(215)	-	767	552
As at 31 December 2017	**463**	**10,342**	**-**	**105,093**	**115,898**

30 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 Central Bank of Bahrain.

Capital management

The primary objectives of the Group's capital management are to ensure that the Group complies with capital requirements of the Central Bank of Bahrain 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 Central Bank of Bahrain, for the Group is as follows:

	2017	*2016*
	US$ 000	*US$ 000*
Capital base:		
Tier 1	**188,657**	264,123
Tier 2	**3,428**	73,751
Total capital base (a)	**192,085**	337,874
Credit risk weighted exposure	**750,074**	2,227,194
Market risk weighted exposure	**54,400**	122,725
Operational risk weighted exposure	**87,463**	84,638
Total risk weighted exposure (b)	**891,937**	2,434,557
Capital adequacy (a/b * 100)	**21.54%**	13.88%
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.

31 IFRS 9 TRANSITION DISCLOSURES

Based on 31 December 2017 data and the current implementation status of IFRS 9 as described in further detail below, the Group estimates the adoption of IFRS 9 will not lead to a material decline in the Group's total shareholders' equity, as the Group carries sufficient provisions to account for any potential impact of impairment requirements of IFRS 9.

IFRS 9 Financial Instruments
In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments that replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. IFRS 9 brings together all three aspects of the accounting for financial instruments project: classification and measurement, impairment and hedge accounting. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early application permitted. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions.

The Group plans to adopt the new standard on the required effective date and will not restate comparative information. During 2017, the Group has performed a detailed impact assessment of all three aspects of IFRS 9. This assessment is based on currently available information and may be subject to changes arising from further reasonable and supportable information being made available to the Group in 2018 when the Group will adopt IFRS 9. Overall, the Group expects no significant impact on its statement of financial position and equity. In addition, the Group will implement changes in classification of certain financial instruments.

(a) Classification and measurement
The Group does not expect a significant impact on its balance sheet or equity on applying the classification and measurement requirements of IFRS 9. It expects to continue measuring at fair value all financial assets currently held at fair value. Quoted equity shares currently held as available-for-sale (AFS) with gains and losses recorded in OCI will continued to be measured at fair value through other comprehensive income. Debt securities are expected to be measured at fair value through OCI under IFRS 9 as the Group expects not only to hold the assets to collect contractual cash flows, but also to sell a significant amount on a relatively frequent basis.

The equity shares in non-listed companies are intended to be held for the foreseeable future. Impairment losses of US$ 17,684 thousand were recognised in profit or loss during prior periods for these investments. The Group will apply the option to present fair value changes in OCI, and, therefore, the application of IFRS 9 will not have a significant impact on the Group's equity.

Loans as well as trade receivables are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. The Group analysed the contractual cash flow characteristics of those instruments and concluded that they meet the criteria for amortised cost measurement under IFRS 9. Therefore, reclassification for these instruments is not required.

(b) Impairment
IFRS 9 requires the Group to record expected credit losses on all of its debt securities, loans and trade receivables, either on a 12-month or lifetime basis. The Group will apply the simplified approach and record lifetime expected losses on all trade receivables. The Group has determined that 12-month expected losses of US$ 60 thousand are required as per IFRS 9, however the Group carries sufficient provisions to absorb any potential impact of loss allowances required as per IFRS 9.

(c) Hedge accounting
The Group determined that all existing hedge relationships that are currently designated in effective hedging relationships will continue to qualify for hedge accounting under IFRS 9. The Group has chosen not to retrospectively apply IFRS 9 on transition to the hedges where the Group excluded the forward points from the hedge designation under IAS 39. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, applying the hedging requirements of IFRS 9 will not have a significant impact on Group's financial statements.

(d) Other adjustments
In addition to the adjustments described above, on adoption of IFRS 9, other items of the primary financial statements such as deferred taxes, assets held for sale and liabilities associated with them, investments in the associate and joint venture, will be adjusted as necessary. The exchange differences on translation of foreign operations will also be adjusted.

32 DISCONTINUED OPERATIONS

Restructuring

On 7 September 2017, the Bank's directors announced the reorganisation of the Bank's operations following which the Bank's Board of Directors, the CBB and the Bank's shareholders approved the reorganisation plan in an Extraordinary General Meeting held on 25 September 2017. In this regard, UGHC acquired entire shareholding of UGB via a share swap offer of 1 new UGHC share for 2 shares of UGB. Subsequent to the share swap, UGHC shares were listed on the Bahrain Bourse. Moreover, the portfolio of the core investments managed by UGB has been transferred to UGHC.

The major classes of assets and liabilities transferred to UGHC are as follows:

	US$ 000
ASSETS	
Demand and call deposits with banks	**228,964**
Placements with banks	**38,421**
Non-trading investments	**125,462**
Loans and receivables	**1,041,114**
Other assets	**73,858**
Investments in associates	**606,412**
Property and equipment	**30,487**
Goodwill	**197**
Assets held for sale	**2,144,915**
LIABILITIES	
Due to banks and other financial institutions	**321,668**
Deposits from customers	**810,841**
Loans payable	**617,376**
Subordinated debt	**50,000**
Other liabilities	**25,237**
Liabilities directly associated with assets held for sale	**1,825,122**
Net assets directly associated with disposal group	**319,793**

The results of the disposal group for the year are presented below:

	2017 US$ 000	*2016 US$ 000*
Investment income - net	**513**	9,956
Interest income	**-**	45,193
Fees and commissions	**(3,496)**	14,655
Foreign currency translation gains (losses) - net	**-**	(1,865)
Share of results of associates - net	**29,407**	37,238
Total income	**26,424**	105,177
Interest expenses	**(18,610)**	(41,229)
Salaries, general and administrative expenses	**(6,400)**	(52,916)
Provisions and taxation	**-**	(8,552)
Net profit from discontinued operations	**1,854**	(80)
Profit from discontinued operations	**3,268**	2,400

The net cash flows received by/invested in the disposal group are presented below:

	2017 US$ 000	*2016 US$ 000*
Net cash flows (used in) from operating activities	**(120,026)**	203,636
Net cash flows from (used in) investing activities	**9,951**	(1,652)
Net cash flows from (used in) financing activities	**58,862**	(117,338)
Other movements	**(412)**	1,371
	(51,625)	86,017