

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

**INTERIM CONDENSED CONSOLIDATED
FINANCIAL STATEMENTS**

30 JUNE 2018 (REVIEWED)

REPORT ON REVIEW OF INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS TO THE BOARD OF DIRECTORS OF UNITED GULF BANK B.S.C. (c)

Introduction

We have reviewed the accompanying interim condensed consolidated financial statements of United Gulf Bank B.S.C. (c) (the "Bank") and its subsidiaries (together the "Group") as at 30 June 2018, comprising the interim consolidated statement of financial position as at 30 June 2018 and the related interim consolidated statements of income, comprehensive income, cash flows and changes in equity for the six-month period then ended and explanatory notes. The Board of Directors of the Bank is responsible for the preparation and presentation of these interim condensed consolidated financial statements in accordance with International Accounting Standard 34 *Interim Financial Reporting* (IAS 34). Our responsibility is to express a conclusion on these interim condensed consolidated financial statements based on our review.

Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410, *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing. Consequently, it does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34.



1 August 2018
Manama, Kingdom of Bahrain

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

INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 30 June 2018 (Reviewed)

	<i>Reviewed 30 June 2018</i>	<i>Audited 31 December 2017</i>	<i>Reviewed 30 June 2017</i>
<i>Note</i>	<i>US\$ 000</i>	<i>US\$ 000</i>	<i>US\$ 000</i>
ASSETS			
Demand and call deposits with banks	44,551	97,993	405,881
Placements with banks	94,420	68,577	167,748
Investments carried at fair value through statement of income	37,057	19,288	23,899
Non-trading investments	158,393	221,586	424,418
Loans and receivables	3,849	4,218	988,415
Other assets	27,877	31,820	128,103
Investments in associates	77,533	77,512	720,188
Investment properties	106,491	106,093	104,899
Property and equipment	2,497	1,679	32,420
Goodwill	52,390	52,390	51,868
Assets held for sale	-	-	63,022
TOTAL ASSETS	605,158	680,114	3,118,459
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks and other financial institutions	209,240	250,211	733,417
Deposits from customers	28,541	31,018	900,033
Loans payable	78,085	98,658	777,998
Subordinated debt	-	-	50,000
Other liabilities	38,288	37,358	88,102
Liabilities directly associated with assets held for sale	-	-	38,734
TOTAL LIABILITIES	352,134	417,245	2,588,284
EQUITY			
Share capital	101,132	101,132	208,651
Treasury shares	-	-	(18,131)
Share premium	5,687	5,687	11,459
Statutory reserve	49,881	49,881	100,514
General reserve	29,612	29,612	80,999
Treasury shares reserve	-	-	14,248
Fair value reserve	1,248	12,887	(39,640)
Foreign currency translation reserve	(3,646)	(3,871)	(35,136)
Retained earnings	11,714	7,659	88,059
CAPITAL AND RESERVES ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT	195,628	202,987	411,023
Perpetual Tier 1 capital	33,000	33,000	33,000
Non-controlling interests	24,396	26,802	106,152
TOTAL EQUITY	253,024	262,889	550,175
TOTAL LIABILITIES AND EQUITY	605,158	680,114	3,118,459



Maseaud Hayat
Chairman



Faisal Al Ayyar
Vice Chairman



Hussain Lalani
Acting Chief Executive Officer

The attached notes 1 to 11 form part of these Interim condensed consolidated financial statements.

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

INTERIM CONSOLIDATED STATEMENT OF INCOME

For the six-month period ended 30 June 2018 (Reviewed)

	Three-month period ended 30 June		Six-month period ended 30 June	
	2018	2017	2018	2017
	US\$ '000	US\$ '000	US\$ '000	US\$ '000
Continuing operations				
Investment income - net	808	3,323	5,318	11,734
Interest income	1,039	799	2,132	1,788
	1,847	4,122	7,450	13,502
Fees and commissions	10,346	7,307	18,283	14,980
Foreign currency translation gains (losses) - net	(984)	(237)	443	(212)
Share of results of associates - net	1,104	377	1,290	174
Total income	12,313	11,589	27,468	28,424
Interest expense	(2,440)	(3,738)	(5,692)	(7,398)
Operating income before expenses and provisions	9,873	7,833	21,774	21,026
Salaries and benefits	(4,868)	(5,298)	(10,044)	(10,705)
General and administrative expenses	(3,290)	(2,789)	(7,131)	(6,662)
Operating income (loss) before provisions and tax	1,715	(254)	4,599	3,659
Provisions for loans and receivables	-	(2,083)	-	(2,260)
Provision for impairment on investments	-	523	-	(462)
Provision for losses against unfunded participation	-	-	(731)	-
Taxation - net	(160)	12	619	(1,165)
Net profit (loss) for the period from continuing operations	1,555	(1,802)	4,487	(228)
Net income from discontinued operations	460	4,501	460	8,083
Net profit for the period	2,005	2,699	4,937	7,835
Net profit (loss) for the period attributable to:				
Non-controlling interests				
- from continuing operations	62	153	166	208
- from discontinued operations	61	1,125	61	1,529
	123	1,278	227	1,735
Shareholders of the parent				
- from continuing operations	1,493	(1,955)	4,321	(434)
- from discontinued operations	389	3,376	389	6,534
	1,882	1,421	4,710	6,100



Masaud Hayat
Chairman



Faisal Al Ayyar
Vice Chairman



Hussain Lalani
Acting Chief Executive Officer

The attached notes 1 to 11 form part of these Interim condensed financial statements.

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

INTERIM CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

For the six-month period ended 30 June 2018 (Reviewed)

	<i>Three-month period ended 30 June</i>		<i>Six-month period ended 30 June</i>	
	<i>2018</i>	<i>2017</i>	<i>2018</i>	<i>2,017</i>
	<i>US\$ 000</i>	<i>US\$ 000</i>	<i>US\$ 000</i>	<i>US\$ 000</i>
NET PROFIT FOR THE PERIOD	2,005	2,699	4,937	7,835
Other comprehensive (loss) income for the period to be reclassified to profit or loss in subsequent periods:				
Foreign currency translation reserve	(2,461)	511	(1,046)	2,616
Fair value reserve	(1,895)	9,833	(9,836)	19,454
Share of other comprehensive income (loss) of associates - net	-	(2,247)	-	(7,436)
Cash flow hedges	27	(413)	630	(361)
Other comprehensive (loss) income for the period to be reclassified to profit or loss in subsequent periods	(4,329)	7,684	(10,252)	14,273
TOTAL COMPREHENSIVE (LOSS) INCOME FOR THE PERIOD	(2,324)	10,383	(5,315)	22,108
Total comprehensive (loss) income attributable to:				
- shareholders of the parent	(2,163)	8,645	(4,531)	18,766
- non-controlling interests	(161)	1,738	(784)	3,342
	(2,324)	10,383	(5,315)	22,108

The attached notes 1 to 11 form part of these interim condensed financial statements.

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

INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS

For the six-month period ended 30 June 2018 (Reviewed)

	Note	Six-months period ended 30 June	
		2018 US\$ 000	2017 US\$ 000
OPERATING ACTIVITIES			
Net profit (loss) for the period from continuing operations		4,487	(228)
Net income from discontinued operations		450	8,063
Net profit for the period		4,937	7,835
Adjustments for non-cash items:			
Depreciation		502	1,660
Gain on investments carried			
at fair value through statement of income		(311)	(3,380)
Share of results of associates - net		(1,290)	(19,613)
Net gain arising from non-current assets classified as held for sale		-	(920)
Provisions for loans and receivables		-	500
Provisions for impairment on investments		-	462
Provisions for losses against unfunded participation		731	-
(Gain) loss on sale of associates & subsidiaries		(31)	8
Gain on fair valuation of investment properties		(1,398)	(3,000)
Gain on sale of non-trading investments		(56)	-
Interest income		(2,131)	(27,937)
Interest expense		5,692	30,248
Dividend income		(1,432)	(5,351)
Operating income (loss) before working capital changes		5,213	(19,488)
Changes in operating assets and liabilities:			
Placements with banks with original maturities of more than ninety days		-	(202,758)
Investments carried at fair value through statement of income		(17,478)	24,860
Non-trading investments		55,878	(2,321)
Loans and receivables		267	187,889
Other assets		2,902	(17,969)
Due to banks and other financial institutions		(40,971)	7,196
Deposits from customers		(2,477)	(85,177)
Other liabilities		(1,212)	3,936
Interest received		1,870	32,177
Interest paid		(4,281)	(30,412)
Dividends received		1,432	5,351
Directors' remuneration		-	(195)
Donations		-	(200)
Net cash flows from (used in) operating activities		1,143	(97,111)
INVESTING ACTIVITIES			
Net assets of disposal group classified as held for sale		-	37,243
Investments in associates - net		1,269	1,026
Investment properties - net		-	(573)
Property and equipment - net		(1,320)	(1,964)
Acquisition of non-current assets classified as held for sale		-	(60,611)
Net cash flows used in investing activities		(51)	(24,879)
FINANCING ACTIVITY			
Repayment of term loans		(22,593)	125,873
Interest paid on perpetual Tier 1 Capital		(1,752)	(1,752)
Net cash flows (used in) from financing activity		(24,345)	124,121
Foreign currency translation adjustments		225	2,340
Movement in non-controlling interests		(2,733)	1,970
NET CHANGE IN CASH AND CASH EQUIVALENTS		(25,761)	6,441
Cash and cash equivalents at 1 January		166,252	357,067
CASH AND CASH EQUIVALENTS AT 30 JUNE	5	140,491	363,508

The attached notes 1 to 11 form part of these interim condensed consolidated financial statements.

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INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
For the six-month period ended 30 June 2018 (Reviewed)

	Attributable to shareholders of the parent						Total before non-controlling interests			Non-controlling interests		Total equity US\$ '000	
	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	Foreign currency translation	Retained earnings US\$ '000	Perpetual capital US\$ '000	Tier 1 capital US\$ '000	Total equity US\$ '000	
Balance at 1 January 2018	101,132	-	5,687	49,881	29,612	-	12,867	(3,871)	7,659	202,967	33,000	26,902	262,869
Transition adjustment on adoption of IFRS 9 at 1 January 2018 (note 4)	-	-	-	-	-	-	3,037	-	(4,093)	(1,056)	-	465	(591)
Profit for the period	101,132	-	5,687	49,881	29,612	-	15,904	(3,871)	3,566	201,911	33,000	27,367	262,278
Other comprehensive (loss) income for the period	-	-	-	-	-	-	-	-	4,710	4,710	-	227	4,937
Total comprehensive (loss) income for the period	-	-	-	-	-	-	(8,160)	(1,081)	-	(9,241)	-	(1,011)	(10,252)
Transfer upon disposal of non-Trading investments	-	-	-	-	-	-	(8,160)	(1,081)	4,710	(4,531)	-	(784)	(5,315)
Interest payment on Tier 1 capital	-	-	-	-	-	-	-	-	(5,190)	-	5,190	-	-
Transfer upon reclassification (note 4A)	-	-	-	-	-	-	-	-	(1,752)	(1,752)	-	-	(1,752)
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	-	-
Balance at 30 June 2018	101,132	-	5,687	49,881	29,612	-	1,248	(3,646)	11,714	195,628	33,000	24,396	253,024
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
Profit for the period	-	-	-	-	-	-	-	-	6,100	6,100	-	1,735	7,835
Other comprehensive income for the period	-	-	-	-	-	-	-	-	10,326	2,340	-	12,666	14,273
Total comprehensive income for the period	-	-	-	-	-	-	-	-	10,326	2,340	6,100	18,766	-
Interest payment on Tier 1 capital	-	-	-	-	-	-	-	-	-	(1,752)	(1,752)	-	3,342
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	-	(1,752)
Balance at 30 June 2017	208,651	(18,131)	11,459	100,514	80,999	14,248	(39,640)	(35,136)	88,059	411,023	33,000	106,152	550,175

The attached notes 1 to 11 form part of these interim condensed consolidated financial statements.

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

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL

As at 30 June 2018 (Reviewed)

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 (Boursa Kuwait).

These interim condensed consolidated financial statements were authorised for issue by the Board of Directors on 1 August 2018.

2 SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

The interim condensed consolidated financial statements of the Group for the six-month period ended 30 June 2018 are prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting*.

These interim condensed consolidated financial statements do not contain all the information and disclosures required for full set of financial statements prepared in accordance with International Financial Reporting Standards, and should be read in conjunction with the Group's consolidated financial statements for the year ended 31 December 2017. In addition, results for the six-month period ended 30 June 2018 are not necessarily indicative of the results that may be expected for the financial year ending 31 December 2018.

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

Significant accounting policies

The accounting policies adopted in the preparation of these interim condensed consolidated financial statements are consistent with those followed in the preparation of the Group's consolidated financial statements for the period ended 31 December 2017, except for new standards and interpretations effective as of 1 January 2018. The Group has not early adopted any standard, interpretation or amendment that has been issued but is not yet effective.

In these interim condensed consolidated financial statements, the Group has applied IFRS 7 (revised) Financial instruments: Disclosures (IFRS 7R), IFRS 9 Financial Instruments (IFRS 9) and IFRS 15 Revenue from contracts with customers (IFRS 15). The nature and impact of each amendment is described below:

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

New standards, interpretations and amendments adopted by the Group

IFRS 9 Financial Instruments

IFRS 9 replaces IAS 39 Financial instruments: recognition and measurement (IAS 39) for annual periods on or after 1 January 2018 bringing together all three aspects of the accounting for financial instruments: classification and measurement; impairment; and hedge accounting. This resulted in changes in accounting policies and adjustments to the amounts previously recognised in the interim condensed consolidated financial statements.

The Group has not restated comparative information for 2017 for financial instruments in the scope of IFRS 9. Therefore, the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Consequently, for notes and disclosures, the consequential amendments from IFRS 7R have also been applied to the current period. The comparative period notes and disclosures repeat those disclosures made in the prior year. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018.

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

Classification and measurement of financial assets

Under IFRS 9, the classification and measurement category of all financial assets, except equity instruments and derivatives, is assessed based on a combination of the entity's business model for managing the financial assets and its contractual cash flow characteristics.

The IAS 39 measurement categories of financial assets (fair value through profit or loss (FVTPL), available for sale (AFS), held-to-maturity (HTM) and amortised cost) have been replaced by:

- Debt instruments at amortised cost
- Debt instruments at fair value through other comprehensive income (FVOCI), with gains or losses recycled to profit or loss on derecognition
- Equity instruments at FVOCI, with no recycling of gains or losses to profit or loss on derecognition
- Financial assets at fair value through profit or loss (FVTPL)

The above designation of equity investments at FVOCI (i.e. election to present subsequent changes in fair value of an equity investment that is neither held for trading nor contingent consideration recognised by an acquirer in a business combination to which IFRS 3 applies in other comprehensive income) and debt investment that meets the amortised cost or FVOCI criteria as FVTPL (only if doing so eliminates or significantly reduces an accounting mismatch), through an irrevocable election / designation at initial recognition of a financial asset.

The Group's classification of its financial assets is explained in detail in note 9. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in note 4.

Classification and measurement of financial liabilities

Classification of financial liabilities remained largely unchanged for the Group. Financial liabilities continue to be measured at amortised cost.

Impairment of financial assets

IFRS 9 impairment requirements are based on expected credit loss (ECL) model as compared to the incurred loss model approach under IAS 39. Key changes to the Group's accounting policy for impairment of financial assets are listed below:

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

New standards, interpretations and amendments adopted by the Group (continued)

IFRS 9 Financial Instruments (continued)

Impairment of financial assets (continued)

Under IFRS 9, the Group applies a three-stage approach to measuring ECL on all loans and debt type financial assets (including loan commitments and financial guarantee contracts) accounted for at amortised cost and FVOCI. Assets migrate through the following three stages based on the change in the credit quality since initial recognition:

i) Stage 1: 12 months ECL

For exposures where there has not been a significant increase in credit risk (SICR) since initial recognition and that are not credit impaired upon origination, the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months is recognised.

ii) Stage 2: Lifetime ECL - not credit impaired

For exposures where there has been a SICR since initial recognition but that are not credit impaired, a lifetime ECL is recognised.

iii) Stage 3: Lifetime ECL - credit impaired

Financial assets are assessed as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that asset have occurred. As this uses the same criteria as under IAS 39, the Group's methodology for specific provisions remains unchanged. For financial assets that have become credit impaired, a lifetime ECL is recognised and interest income is suspended and recognised on cash receipt basis.

For more details on the accounting policies, refer section summary of changes in significant accounting policies. The quantitative impact of applying IFRS 9 as at 1 January 2018 is disclosed in note 4.

IFRS 7(revised) Financial instruments: Disclosures (IFRS 7R)

To reflect the differences between IFRS 9 and IAS 39, IFRS 7 Financial instruments: Disclosures was updated and the Group has adopted it, together with IFRS 9, for the year beginning 1 January 2018. Changes include transition disclosures as shown in note 4.

Reconciliations from opening to closing ECL allowances are presented in note 4.

IFRS 7R also requires additional and more detailed disclosures for hedge accounting. However, the adoption of IFRS 9 for hedge accounting did not have a material impact on the hedging activities / accounting of the Group, therefore, these will be disclosed in the annual consolidated financial statements for the year ending 31 December 2018.

IFRS 15 Revenue from contracts with customers (IFRS 15)

The Group adopted IFRS 15 Revenue from contracts with customers (IFRS 15) resulting in a change in the revenue recognition policy of the Group in relation to its contracts with customers.

IFRS 15 was issued in May 2014 and is effective for annual periods commencing on or after 1 January 2018. IFRS 15 outlines a single comprehensive model of accounting for revenue arising from contracts with customers and supersedes current revenue guidance, which is found currently across several standards and interpretations within IFRS. It established a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The adoption of this standard will result into change in accounting policies as discussed below:

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

New standards, interpretations and amendments adopted by the Group (continued)

IFRS 15 Revenue from contracts with customers (IFRS 15) (continued)

Performance-based fees

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

Advisory income

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

The Group has opted for the modified retrospective application permitted by IFRS 15 upon adoption of the new standard. Modified retrospective application also requires the recognition of the cumulative impact of adoption of IFRS 15 on all contracts as at 1 January 2018 in equity. There were no adjustments to opening retained earnings and other account balances on the adoption of IFRS 15.

Several other amendments to standards and interpretations applied for the first time in 2018, however, they did not impact the interim condensed consolidated financial statements of the Group.

New standards, interpretations and amendments issued but not yet effective

The main standard that is issued, but not yet effective, up to the date of issuance of the Group's interim condensed consolidated financial statements is IFRS 16, which is effective from 1 January 2019. The Group intends to adopt the standard, if applicable, when it becomes effective. The Group is assessing the impact of implementation of the standards.

Summary of changes in significant accounting policies

Based on the adoption of new standards explained above and in note 4, the following accounting policies are applicable effective 1 January 2018 replacing / amending or adding to the corresponding accounting policies set out in annual consolidated financial statements for the year ended 31 December 2017.

Financial instruments

Date of recognition

Financial assets and liabilities, with the exception of loans and receivables, due to banks and other financial institutions and deposits from customers, are initially recognised on the trade date, i.e., the date that the Group becomes a party to the contractual provisions of the instrument. This includes regular way trades: purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place. Loans and receivables are recognised when funds are transferred to the customers' accounts. The Group recognises due to banks and other financial institutions and deposits from customers when funds are transferred to the Group.

Initial measurement

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments.

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Initial measurement (continued)

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

When the fair value of financial assets and liabilities at initial recognition differs from the transaction price, the Group accounts for the difference as follows:

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

Measurement categories of financial assets and liabilities

From 1 January 2018, the Group classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

- Amortised cost
- FVOCI
- FVTPL

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

Before 1 January 2018, the Group classified its financial assets as loans and receivables (amortised cost), FVTPL, available-for-sale or held-to-maturity (amortised cost), as explained in the annual consolidated financial statements for the year ended 31 December 2017.

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

Financial assets

Classification and subsequent measurement

From 1 January 2018, the Group has applied IFRS 9 and classified its financial assets in the following measurement categories:

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

The classification requirements for financial assets is as below:

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Summary of changes in significant accounting policies (continued)

Financial assets (continued)

Classification and subsequent measurement (continued)

Classification and subsequent measurement of debt instruments depend on:

- (i) the Group's business model for managing the asset; and
- (ii) the cash flow characteristics of the asset i.e. solely payments of principal and interest (SPPI) test.

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

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent SPPI, and that are not designated at FVTPL, are measured at amortised cost. The carrying amount of these assets is adjusted by any ECL allowance recognised and measured as described in note 4. Interest income from these financial assets is included in 'Interest income' using the EIR method.
- FVOCI: Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent SPPI, and that are not designated at FVTPL, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest revenue and foreign exchange gains and losses on the instrument's amortised cost which are recognised in interim consolidated statement of income. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to consolidated income and recognised in 'Investment income - net' as 'Gain on disposal of non-trading securities'. Interest income from these financial assets is included in 'Interest income' using the EIR method.
- FVTPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at FVTPL and is not part of a hedging relationship is recognised in consolidated profit or loss and presented in the interim consolidated statement of income within 'Investment income - net' as 'Gain on trading securities' in the period in which it arises, unless it arises from debt instruments that were designated at fair value or which are not held for trading, in which case they are presented separately in 'Investment income - net' as 'Gain on disposal of non-trading securities'. Interest income from these financial assets is included in 'Interest income' using the EIR method.

Business model

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

- The stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realizing cash flows through the sale of the assets;
- How the asset's and business model performance is evaluated and reported to key management personnel and Asset and Liability Committee (ALCO);

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Summary of changes in significant accounting policies (continued)

Financial assets (continued)

Business model (continued)

- How risks are assessed and managed; and
- The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

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

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

SPPI test

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

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

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

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

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

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

The Group reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and none occurred during the period.

Equity instruments

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

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Summary of changes in significant accounting policies (continued)

Financial assets (continued)

Financial asset at FVTPL

The Group classifies financial assets at fair value through profit and loss when they have been purchased or issued primarily for short-term profit making through trading activities or form part of a portfolio of financial instruments that are managed together, for which there is evidence of a recent pattern of short-term profit taking. Held-for-trading assets are recorded and measured in the statement of financial position at fair value. In addition, on initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise. Changes in fair values, financing income and dividends are recorded in consolidated statement of income according to the terms of the contract, or when the right to payment has been established.

Equity instruments at FVOCI

Upon initial recognition, the Group may elect to classify irrevocably some of its equity investments as equity instruments at FVOCI when they meet the definition of Equity under IAS 32 Financial Instruments: Presentation and are not held for trading. Such classification is determined on an instrument-by-instrument basis. Fair value gains and losses are recognised in other comprehensive income and are not subsequently reclassified to consolidated income, including on disposal. Equity investments at FVOCI are not subject to impairment assessment. Dividends are recognised in the interim consolidated statement of income as 'Investment income - net' when the Group's right to receive payments is established. Equity investments at FVOCI are included in non-trading investments in the statement of financial position.

Financial Liabilities

Classification and subsequent measurement

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

Impairment

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

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

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

Derivatives and hedging activities

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

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

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Summary of changes in significant accounting policies (continued)

Derivatives and hedging activities

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

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

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

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

(a) Fair value hedge

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

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

(b) Cash flow hedge

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

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

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

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Summary of changes in significant accounting policies (continued)

Derivatives and hedging activities (continued)

(c) Net investment hedge

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

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

Interest income

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

Significant accounting judgements, estimates and assumptions

In preparing these interim condensed consolidated financial statements, significant judgements made by management in applying accounting policies and key sources of estimation were the same as those that were applied to the annual consolidated financial statements for the year ended 31 December 2017 except for new judgements and estimates explained below:

Measurement of the expected credit loss allowance (ECL)

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

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

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

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

Significant accounting judgements, estimates and assumptions (continued)

Classification of financial assets

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

The Group applies judgement while carrying out SPPI test and considers relevant factors such as the currency in which the financial asset is denominated, and the period for which the interest rate is set.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

3 BASIS OF CONSOLIDATION

These interim condensed consolidated financial statements include the interim condensed financial statements of the Bank and its subsidiaries as at 30 June 2018. 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.

The principal subsidiaries of the Bank are as follows:

Name of the subsidiary	Country of incorporation	Legal ownership		Year of incorporation
		30 June 2018	31 December 2017	
<i>Held directly</i>				
KAMCO Investment Company K.S.C.P. [KAMCO]	Kuwait	86%	86%	1998
United Gulf Financial Services Company-North Africa	Tunisia	84%	83%	2008
United Gulf Asset Company S.P.C.	Bahrain	100%	100%	2017
United Gulf Realty International, Ltd	British Virgin Islands	100%	100%	2012
<i>Held through KAMCO</i>				
Al Dhiyafa United Real Estate Company W.L.L.	Kuwait	100%	100%	2007
Al Jazi Money Market Fund	Kuwait	51%	51%	2007
Al Tadamon United Holding Co	Kuwait	96%	96%	2017
Al Zad Real Estate W.L.L.	Kuwait	99%	99%	2007
Bukeye Power Project Advisory Co	U.S.A.	50%	50%	2017
Bukeye Power Project Manager Ltd	Jersey	100%	100%	2017
Carnation Advisory Company LLC	U.S.A.	75%	-	2018
Carnation Manager limited	U.K.	100%	-	2018
Flint Advisor Company Llc	Jersey	46%	46%	2017
Flint Manager Ltd	U.S.A.	100%	100%	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	78%	71%	2016
Kuwait Private Equity Opportunity Fund	Kuwait	73%	73%	2004
Nawasi United Holding Co	Kuwait	96%	96%	2017
North Africa Real Estate Co.	Kuwait	100%	100%	2014

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

4 TRANSITION DISCLOSURES

(a) The Group performed a detailed analysis of its business models for managing financial assets and analysis of their cash flow characteristics.

The following table reconciles the carrying amounts of financial assets and financial liabilities, from their previous measurement category in accordance with IAS 39 to their new measurement categories upon transition to IFRS 9 on 1 January 2018:

Financial assets	IAS39 carrying amount	Reclassifi- cation	Remeasure- ment	IFRS 9 carrying amount	Classifica- tion under IFRS9
	US\$ '000	US\$ '000	US\$ '000	US\$ '000	
Demand and call deposits with banks	97,993	-	(1)	97,992	Amortised cost
Placements with banks	68,577	-	(204)	68,373	Amortised cost
Investments carried at fair value through statement of income	19,268	(3,704)	-	15,564	FVTPL
Non-trading investments	-	3,704	-	3,704	FVOCI
Non-trading investments	221,566	(72,828)	-	148,738	FVOCI
Investments carried at fair value through statement of income	-	44,832	-	44,832	FVTPL
Loans and receivables	4,216	27,996	(1,005)	31,207	Amortised cost
Other assets	31,820	-	(157)	31,663	Amortised cost
Total assets	443,440	-	(1,367)	442,073	

Adoption of IFRS 9 did not result in any change in classification or measurement of financial liabilities.

(b) Impact on retained earnings and other reserves

	Retained earnings	Other reserves
Closing balance under IAS 39 (31 December 2017)	7,659	12,867
Reclassifications and remeasurement of investments under IFRS 9	(2,726)	3,037
Recognition of expected credit losses under IFRS 9	(1,367)	-
Opening balance under IFRS 9 (1 January 2018)	3,566	15,904

(c) Reconciliation of impairment allowance balance from IAS 39 to IFRS 9

The following table reconciles the prior period's closing loan loss provisions measured in accordance with IAS 39 incurred loss model to the new impairment allowance measured in accordance with the IFRS 9 ECL model at 1 January 2018:

Measurement category	Loan loss allowance under IAS 39	Remeasure- ment	ECL under IFRS 9
Demand and call deposits with banks	-	1	1
Placements with banks	-	204	204
Loans and receivables	2,535	1,005	3,540
Other assets	-	157	157
Total	2,535	1,367	3,902

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

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

4 TRANSITION DISCLOSURES (continued)

An analysis of movement in ECL allowances during the period is as follows:

	Stage 1 US\$ 000	Stage 2 US\$ 000	Stage 3 US\$ 000	Total US\$ 000
As at 1 January 2018	362	3,540	-	3,902
Net transfers between stage 1, 2 and 3	(304)	(1,270)	1,574	-
Amount written off	-	-	(1,574)	(1,574)
As at 30 June 2018	58	2,270	-	2,328

The following explains how applying the new classification requirements of IFRS 9 led to changes in classification of certain financial assets held by the Group as shown in the table above:

(A) Debt instruments previously classified as available for sale

The Group holds a portfolio of debt instruments that were classified as available for sale under IAS 39. The Group has reassessed the debt instruments under IFRS 9. As a result, these instruments, which amounted to US\$ 27,996 thousand were classified as amortised cost from the date of initial application.

During the period, based on certain amendments to an initial credit facility agreement, the repayment of the debt instrument will be made in kind with the issuance of ordinary shares of the counter party at the fair value of the shares at the date of maturity. The Group has reassessed the classification of the debt instrument and as at 30 June 2018 the Group reclassified its investment as an equity instruments measured at FVOCI, as permitted under IFRS 9.

(B) Designation of equity instruments at FVOCI

The Group has elected to irrevocably designate investments of US\$ 3,704 thousand that were previously classified as FVTPL, at FVOCI as permitted under IFRS 9. The changes in fair value of such securities will no longer be reclassified to profit or loss when they are disposed of.

(C) Designation of equity instruments at FVTPL

The Group has elected to designate certain of its investments at a carrying value of US\$ 44,832 thousand as FVTPL as permitted under IFRS 9 from the initial date of application. These investments were previously classified as available-for-sale. Any changes in fair value of these securities will be recognised in the profit or loss.

5 CASH AND CASH EQUIVALENTS

	Reviewed 30 June 2018 US\$ 000	Audited 31 December 2017 US\$ 000	Reviewed 30 June 2017 US\$ 000
Demand and call deposits with banks excluding mandatory reserves	44,233	97,675	196,530
Placements with original maturities of ninety days or less	96,258	68,577	166,978
Cash and cash equivalents gross of expected credit losses	140,491	166,252	363,508
Expected credit losses as per IFRS 9	(1,838)	-	-
Cash and cash equivalents net of expected credit losses	138,653	166,252	363,508

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

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL As at 30 June 2018 (Reviewed)

6 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.

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NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS
As at 30 June 2018 (Reviewed)

7 RELATED PARTY TRANSACTIONS

The Group enters into transactions with its parent, associated companies, directors, senior management and entities which are either controlled or significantly influenced by such parties.

The income and expenses in respect of related party transactions during the six-month period are included in the interim condensed consolidated financial statements and are as follows:

	<i>Reviewed</i>			<i>Reviewed Six-month period ended 30 June 2017</i>	
	<i>Six-month period ended 30 June 2018</i>				
	<i>Major shareholder</i>	<i>Associates</i>	<i>Other</i>		
	<i>US\$'000</i>	<i>US\$'000</i>	<i>US\$'000</i>	<i>US\$'000</i>	
Gain on investments carried at fair value through statement of income - net					
Fees and commissions - net	2,967	1,225	8	8	
Dividend income	-	-	5,340	9,532	
Rental income	-	-	859	859	
Loss on sale of investments in associated and subsidiary companies					
Gain on foreign currencies	-	-	1,225	1,225	
Interest income	-	-	-	-	
Interest expense	(332)	-	917	917	
Others - net	-	(512)	(2,081)	(2,413)	
			(512)	(11,461)	
			694	694	

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

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
As at 30 June 2018 (Reviewed)

7 RELATED PARTY TRANSACTIONS (continued)

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

	<i>Reviewed</i>			<i>Reviewed</i>		
	<i>30 June 2018</i>			<i>31 December 2017</i>		
	<i>Major shareholder</i> <i>US\$ 000</i>	<i>Associates</i> <i>US\$ 000</i>	<i>Other related parties</i> <i>US\$ 000</i>	<i>Total</i> <i>US\$ 000</i>	<i>Audited</i> <i>US\$ 000</i>	
Demand and call deposits with banks	-	-	4,477	4,477	2,170	2,045
Placements with banks	-	-	21,151	21,151	22,777	23,052
Investments carried at fair value through statement of income	-	-	9,277	9,277	2,209	2,237
Non-trading investments	-	-	102,811	102,811	94,270	29,242
Loans and receivables	-	-	2,658	2,658	5,652	29,770
Other assets	-	50	14,096	14,096	9,569	27,724
Due to banks and other financial institutions	(12,882)	-	(133,834)	(133,834)	(134,689)	(219,181)
Deposits from customers	-	-	(11,225)	(24,107)	(18,902)	(20,540)
Loans payable	-	-	-	-	(14,078)	(451,024)
Subordinated debt	-	-	-	-	-	(50,000)
Other liabilities	(1,465)	-	(4,517)	(5,982)	(4,778)	(8,182)
Perpetual Tier 1 Capital	-	-	10,000	10,000	(10,000)	(10,000)
<i>Off statement of financial position items:</i>						
Letters of guarantee	-	-	150	150	150	150
Funds managed or advised by the Group	-	-	-	-	-	41,675

Except as mentioned below, all related party exposures are performing.

During the period, ECL, relating to an exposure with a related party, amounting to US\$ 1,574 thousand was transferred to stage 3 and written off.

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

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As at 30 June 2018 (Reviewed)

8 COMMITMENTS, CONTINGENCIES AND OTHER OFF STATEMENT OF FINANCIAL POSITION ITEMS

Commitments

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

Letters of credit, letters of guarantee (including standby letters of credit) and acceptances commit 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:

	Reviewed 30 June 2018 US\$ 000	Audited 31 December 2017 US\$ 000	Reviewed 30 June 2017 US\$ 000
Credit-related commitments:			
Letters of credit	-	-	45,014
Letters of guarantee	150	812	10,318
	<u>150</u>	<u>812</u>	<u>55,332</u>
Investments and loan related commitments	4,017	4,017	201,677
	<u>4,167</u>	<u>4,829</u>	<u>257,009</u>

Investment-related commitments represent capital commitments to fund structures. These commitments can be called by the fund during the investment period of the fund, which is normally between 1 to 5 years.

9 DERIVATIVES

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

	Notional amounts		
	Reviewed 30 June 2018 US\$ 000	Audited 31 December 2017 US\$ 000	Reviewed 30 June 2017 US\$ 000
<i>Derivatives held for trading:</i>			
Forward foreign exchange contracts *	455,685	427,968	202,926
<i>Derivatives used as hedge of net investments in foreign operations</i>			
Forward foreign exchange contracts	109,199	245,114	751,581
<i>Derivatives used as cash flow hedges</i>			
Interest rate swap	75,000	145,000	195,000

* 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.

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

As at 30 June 2018 (Reviewed)

10 FINANCIAL INSTRUMENTS

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

30 June 2018	Held for trading	Designated at FVTPL	FVOCI	Amortised cost	Total US\$ 000
	US\$ 000	US\$ 000		US\$ 000	
Demand and call deposits with banks	-	-	-	44,551	44,551
Placements with banks	-	-	-	94,420	94,420
Investments carried at fair value through statement of income	32,916	4,141	-	-	37,057
Non-trading investments	-	-	158,393	-	158,393
Loans and receivables	-	-	-	3,949	3,949
Other assets	-	245	-	26,388	26,633
Total financial assets	32,916	4,386	158,393	169,308	365,003
Due to banks and other financial institutions	-	-	-	209,240	209,240
Deposits from customers	-	-	-	28,541	28,541
Loans payable	-	-	-	76,065	76,065
Other liabilities	-	-	-	38,288	38,288
Total financial liabilities	-	-	-	352,134	352,134

31 December 2017	Designated at fair value through statement of income		Available- for-sale	Amortised cost / Loans and receivables	Total US\$ 000
	Held for trading	US\$ 000	US\$ 000	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	-	-	-	30,840	30,840
Total financial assets	17,983	1,285	221,566	201,626	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

The fair values of financial instruments on statement of financial position are not significantly different from their carrying values included in the interim condensed consolidated financial statements.

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NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

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11 FAIR VALUE MEASUREMENT

Fair value hierarchy

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.

Fair values of quoted securities are derived from quoted market prices in active markets, if available. For unquoted securities, fair value is estimated using appropriate valuation techniques. Such techniques may include using recent market transactions; reference to the current fair value of another instrument that is substantially the same; discounted cash flow analysis or other valuation models.

The fair values of the funds that are listed on active markets are determined by reference to their quoted bid prices. The fair values of unlisted funds are based on net asset values which are determined by the fund manager using the quoted market prices of the underlying assets, if available, or other acceptable methods such as a recent price paid by another investor or the market value of a comparable company.

The Group uses the following hierarchy for determining and disclosing the fair value of the Group's assets and liabilities by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly; and

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

The following table shows an analysis of the Group's assets and liabilities recorded at fair value by level of the fair value hierarchy at 30 June 2018:

	<i>Level 1</i> US\$ 000	<i>Level 2</i> US\$ 000	<i>Level 3</i> US\$ 000	<i>Total</i> US\$ 000
Assets measured at fair value				
Investments carried at fair value through statement of income				
Equities - quoted	21,536	-	-	21,536
Debt securities - quoted	10,250	-	-	10,250
Equities - unquoted	-	-	2,930	2,930
Managed funds	-	1,211	1,130	2,341
Non-trading investments				
Equities - quoted	31,875			31,875
Equities - unquoted	-	48,575	76,783	125,358
Real estate managed funds - unquoted	-	-	179	179
Other managed funds	-	-	981	981
Derivatives				
Held for trading	-	158	-	158
Used as hedge of net investments in foreign operations	-	87	-	87
Interest rate swap	-	1,730	-	1,730
Investment properties	-	-	106,491	106,491
	63,661	51,761	188,494	303,916

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As at 30 June 2018 (Reviewed)

11 FAIR VALUE MEASUREMENT (continued)

The following table shows an analysis of the Group's assets and liabilities recorded at fair value by level of the fair value hierarchy at 31 December 2017:

	Level 1 US\$ 000	Level 2 US\$ 000	Level 3 US\$ 000	Total US\$ 000
Assets measured at fair value				
Investments carried at fair value through statement of income				
Equities - quoted	6,305	-	-	6,305
Debt securities - quoted	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
Real estate managed funds - unquoted	-	25,011	10,342	35,353
Derivatives				
Interest rate swap	-	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)

Transfers between Level 1, Level 2 and Level 3

During the six-month period ended 30 June 2018 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.