ANNUAL REPORT 2016

بنك الخليج المتحد ش.م.ب.

United Gulf Bank B.S.C.

A member of the KIPCO Group

The item was made in Iran circa late 17th to early 18th century CE. The image is reproduced with the kind permission of The al-Sabah Collection, Dar al-Athar al-Islamiyyah.

Dar al-Athar al-Islamiyyah, one of Kuwaiti's leading cultural organizations, was created to manage activities related to The al-Sabah Collection. The collection includes one of the world's finest assemblages of arts from the Islamic world. The collection consists of over 30,000 priceless objects, including manuscripts, scientific instruments, carpets, fabrics, jewelry, ceramics, ivory, metalwork and glass from countries such as Spain, India, China and Iran.

This year, the annual reports of the KIPCO Group companies each feature a different piece of woven textile from The al-Sabah Collection. The images used within the reports reflect KIPCO's commitment to protecting and promoting Kuwait's heritage while helping to build the nation's future.

The Item pictured here (LNS 5 T) is a brocaded panel with metal thread, featuring displays of floral arrangements in vases. The item was made in Iran circa late 17th to early 18th century CE. The image is reproduced with the kind permission of The al-Sabah Collection, Dar al-Athar al-Islamiyyah.

H. M. KING HAMAD BIN ISA AL KHALIFA

King of the Kingdom of Bahrain

H. H. SHEIKH SABAH AL AHMAD AL JABER AL-SABAH

Amir of the State of Kuwait

Corporate Profile

UNITED GULF BANK

UGB is the merchant banking subsidiary of the KIPCO Group. Its proprietary investments include assets in commercial banking, real estate, private equity, and quoted securities. As of 31 December 2016, assets under management amounted to US$ 10.0 billion (31 December 2015: US$ 10.7 billion).

UGB's core subsidiaries and associates include: Burgan Bank, KAMCO Investment Company (KAMCO), FIMBank p.l.c., North Africa Holding Company, United Gulf Financial Services - North Africa, Takaud Savings & Pensions Company, United Capital Transport Company and United Real Estate Company.

UGB and its subsidiary KAMCO have a proven track record of successfully completing more than 60 investment banking transactions for clients since 2001, with an aggregate value of over US$ 10 billion including corporate finance, advisory, new issue placement and underwriting, corporate restructuring, bond issuance, and mergers and acquisitions.

UGB is a member of the KIPCO Group, one of the biggest holding companies in the Middle East and North Africa.

A MEMBER OF THE KIPCO GROUP

The KIPCO Group is one of the biggest holding companies in the Middle East and North Africa, with consolidated assets of US$ 32.7 billion as at 31 December 2016. The Group has significant ownership interests in over 60 companies operating across 24 countries. The Group's main business sectors are financial services, media, real estate and manufacturing. Through its core companies, subsidiaries and affiliates, KIPCO also has interests in the education and medical sectors.

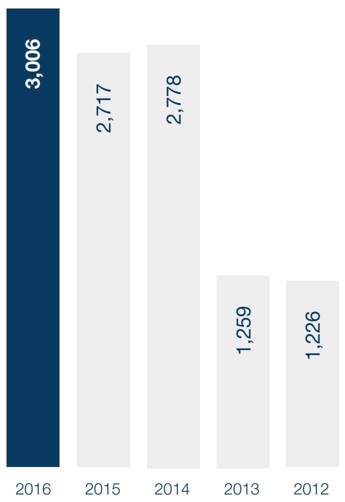
Major Subsidiaries and Affiliates

P.O. Box 5964, Diplomatic Area
UGB Tower, Manama, Kingdom of Bahrain
Tel: +973 17 533 233, Fax: +973 17 533 137
info@ugbbah.com
www.ugbbh.com

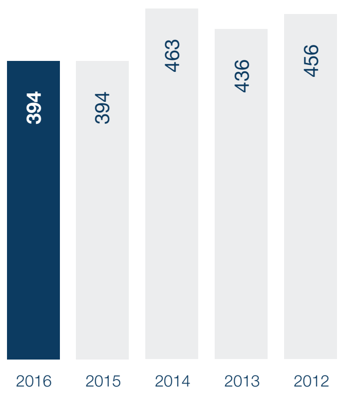
Licensed as a conventional wholesale bank by the Central Bank of Bahrain

Financial Highlights

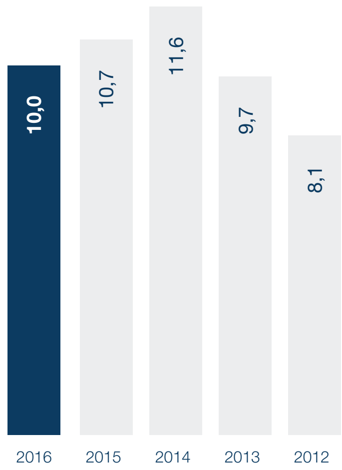
Total Assets
US$ million



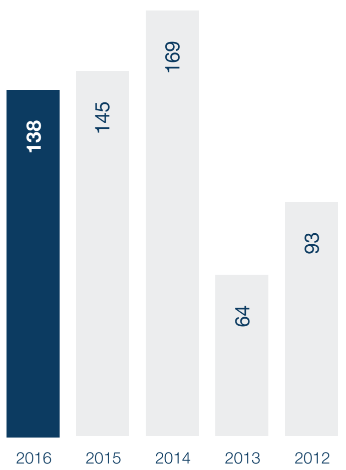
Shareholders' Equity
US$ million



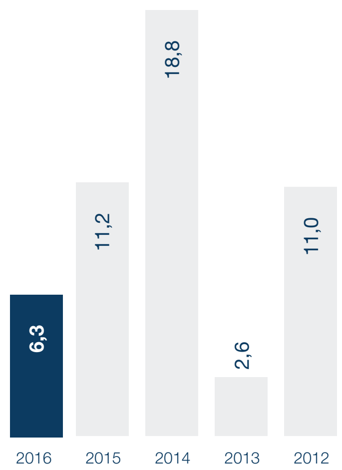
Assets Under Management
US$ billion



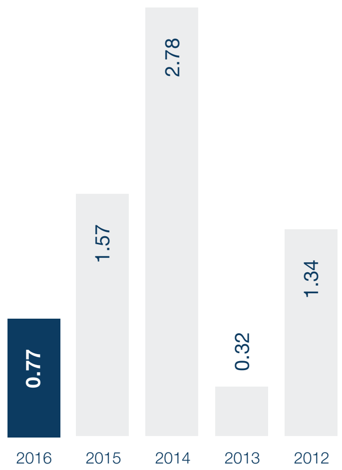
Total Income
US$ million



Net Income Attributable to Shareholders of the Parent
US$ million



Earnings per Share
US$ cents



US$
3.0 billion
Total Assets

13.9 %
Capital Adequacy Ratio

US$
10.0 billion
Assets Under Management

Financial Summary

	2016	2015	2014	2013	2012
US$ million					
Total Income	138.0	144.8	169.1	64.3	93.0
Investment income	19.7	7.7	44.2	20.0	28.9
Operating income	85.1	93.3	117.4	33.0	48.7
Shareholders' Equity	394.0	394.0	462.9	436.3	456.2
Total Assets	3,005.7	2,716.5	2,777.8	1,258.6	1,225.6
Net Income Attributable to Shareholders of the Parent	6.3	11.2	18.8	2.6	11.0
%					
Return on Average Equity	1.59%	2.62%	4.19%	0.58%	2.17%
Return on Average Assets	0.22%	0.41%	0.93%	0.21%	0.74%
Operating Expense / Operating Income	86.4%	87.3%	58.6%	72.4%	58.5%
Average Equity to Average Assets	13.8%	15.6%	22.3%	35.9%	34.0%
US$					
Book Value per share	0.4834	0.4833	0.5679	0.5352	0.5562
Earnings per share (US$ cents)	0.77	1.57	2.78	0.32	1.34
Dividend per share	-	-	-	-	-
Stock dividend per share	-	-	-	-	0.118
COMPARATIVES AVERAGES BALANCES (based on quarterly averages)					
US$ million					
Assets	2,990.9	2,645.7	2,617.8	1,258.1	1,454.3
Liabilities	2,455.0	2,122.5	2,056.4	784.6	889.9
Minority Interest	107.0	113.5	99.0	22.8	27.6
Shareholders' Equity	428.9	409.7	462.5	450.7	536.8
	2990.9	2,645.7	2,617.8	1,258.1	1,454.3
Guarantees and commercial LC	65.3	78.0	145.3	39.4	70.3
Commitments	100.5	62.4	133.9	8.1	39.2
Asset Under Management (US$ billion)	10.0	10.7	11.8	9.3	7.8

Chairman's Statement

On behalf of the Board of Directors, I have the privilege to present the annual report and consolidated financial statements of United Gulf Bank (UGB) for the year ended 31 December 2016. This proved to be an even more challenging and unpredictable period than expected. The year was marked by intensified economic and market volatility, heightened regional geo-political tensions, and unexpected global events such as Brexit.

FINANCIAL PERFORMANCE

During 2016, UGB successfully maintained profitability, a strong balance sheet and high liquidity, while continuing to control costs. Total income before interest and other expenses in 2016 was US$ 138.0 million compared with US$ 144.8 million for the previous year; while total expenses were US$ 73.5 million versus US$ 81.4 million in 2015. As a result, net profit attributable to shareholders of the parent company was US$ 6.3 million compared with US$ 11.2 million in 2015; with basic earnings per share of US 0.77 cents against US 1.38 cents for the previous year. Contributions from the Bank's associates totalled US$ 41.1 million compared with US$ 45.9 million in 2015; while total assets under management as at 31 December 2016 amounted to US$ 10.0 billion versus US$ 10.7 billion at the end of 2015.

I would like to point out that 2016 was the Bank's 26th consecutive year of profitability and the 33rd year of positive results, since its establishment in 1980. Such a performance reinforces UGB's track record as a leading asset management, merchant and investment banking, and financial services group in the MENA region.

At the end of the year, total assets stood at US$ 3.0 billion compared with US$ 2.7 billion at the end of the previous year. The Bank retained a strong balance sheet, with total equity of US$ 529.5 million compared with US$ 503.3 million at the end of 2015. UGB's consolidated capital adequacy ratio was 13.9 per cent, which exceeds the Central Bank of Bahrain's minimum requirement of 12.5 per cent. Liquidity remained healthy, with total liquid assets of US$ 621.9 million representing 20.7 per cent of the balance sheet at the end of the year. During 2016, the Bank repaid a Tier 2 Bond of US$ 100 million and a US$ 70 million Club Loan; and raised mid-term financing of US$ 100 million in aggregate through two different transactions during the first half of the year.

In June 2016, the international rating agency Capital Intelligence affirmed the long and short term foreign currency ratings (FCRs) of UGB at 'BBB' and 'A3'. The agency's revised negative outlook demonstrates the impact of weakening economic indicators due to lower oil prices and increased market volatility. Capital Intelligence noted the Bank's strong ownership combined with the demonstrated financial and liquidity support from its parent KIPCO; and highlighted UGB's demonstrated ability to repay and refinance maturing debt, its effective access to term finance, and the sound quality of its investment portfolio. We regard this as an independent validation of the actions we have taken in recent years to restructure the balance sheet, strengthen the overall quality of assets, and improve the risk profiles of the Bank's key subsidiaries and associate companies.

SUBSIDIARIES AND ASSOCIATES

The main contributors to the share of results from the Bank's subsidiaries and associates in 2016 continued to be KAMCO Investment Company (KAMCO), Burgan Bank and United Real Estate Company (URC). Notable developments during the year include KAMCO opening its first international office in Dubai International Financial Centre; and Burgan Bank completing a KWD 100 million (US$ 237 million) subordinated Tier 2 Basel III compliant bond issue, one of the first of its kind in Kuwait. URC continued to make good progress in developing its flagship Assoufid mixed use property in Marrakesh, Morocco. In addition, FIMBank returned to profitability due to the successful implementation of its consolidation strategy over the past two years. In light of continued volatile market conditions, we continued to focus on increasing our investment in real estate during 2016, through the addition of new properties and land with a view to enhancing recurring income. We also made investments in sectors that are not highly correlated to oil prices, market performance or government spending, such as media and entertainment, and healthcare.

SOUND GOVERNANCE

As in previous years, UGB continued to place the highest importance on sound corporate governance and risk management. We maintained our compliance with the latest regulatory requirements of the Central Bank of Bahrain; while enhancing our risk management practices through further automation. We also continued to implement the Bank's corporate responsibility programme, with a special emphasis on education and career development for young Bahrainis; development of the regional banking sector; women's empowerment; and charitable and community based activities.

FUTURE OUTLOOK

Looking ahead, 2017 seems set to be even more challenging and unpredictable than 2016, with many of the underlying issues and concerns continuing to affect investor sentiment. However, the recent stabilisation in oil prices, and the economic transformation plans being implemented across the region, offer a more positive outlook. As such, we remain cautiously optimistic about UGB's future prospects. During 2017, we will maintain our firm focus on managing liquidity and costs; while further diversifying our investment portfolio and enhancing recurring income. We are also reviewing options through which to optimise the Bank's capital efficiency and further strengthen our balance sheet. During the year, UGB strengthened its capital base through raising Additional Tier 1 capital of USD 33 million. For 2017, a comprehensive plan is at an advanced discussion stage to ensure the Bank maintains adequate capital to meet its growth plans, while keeping pace with a changing regulatory landscape.

ACKNOWLEDGEMENTS

On behalf of the Board of Directors, it is with deep gratitude that I acknowledge the immense support and encouragement that we receive from the Government of the Kingdom of Bahrain; the Central Bank of Bahrain, Bahrain Bourse, and Ministry of Industry, Commerce and Tourism; and the various regulatory and supervisory authorities of the different jurisdictions in which UGB operates. I express my thanks for the financial support and confidence of our shareholders; the trust and loyalty of our clients; and the collaboration of our business partners. Finally, I would like to pay tribute to the professionalism and commitment of the Bank's Management team and staff, and their positive contribution to another challenging but successful year for UGB.

MASAUD M J HAYAT
Chairman of the Board of Directors

Board of Directors

MASAUD M. J. HAYAT

Chairman

Chairman of the Executive Committee

Chief Executive Officer, Banking Sector, Kuwait Projects Company (Holding) - Kuwait
Chairman and Chairman of the Executive Committee, Tunis International Bank - Tunisia
Chairman, Syria Gulf Bank - Syria
Vice Chairman and Chairman of the Executive Committee, Gulf Bank Algeria - Algeria
Vice Chairman and Chairman of the Executive Committee, Bank of Bagdad - Iraq
Vice Chairman, FIMBank p.l.c. - Malta
Vice Chairman, Royal Capital PJSC - UAE
Board Member, Burgan Bank - Kuwait
Board Member, Jordan Kuwait Bank - Jordan
Board Member, KAMCO Investment Company K.S.C. (Public) - Kuwait
Board Member, North Africa Holding Company - Kuwait
Board Member, Mashare'a Al Khair Est. - Kuwait
Over 40 years of experience in the financial sector
Degree in Economics, Kuwait University; Diploma in Banking Studies, Institute of Banking Studies, Kuwait.

FAISAL HAMAD M. AL AYYAR

Vice Chairman

Member of the Executive Committee and Member of the Board Audit Committee

Vice Chairman (Executive), Kuwait Projects Company (Holding) - Kuwait
Chairman, Panther Media Group - Dubai, UAE
Vice Chairman, Gulf Insurance Group - Kuwait
Vice Chairman, Jordan Kuwait Bank - Jordan
Vice Chairman, Mashare'a Al-Khair Est. - Kuwait
Board Member, Saudia Dairy & Foodstuff Co. - Saudi Arabia
Board Member, Gulf Egypt for Hotels & Tourism Co - Egypt
Trustee, American University of Kuwait - Kuwait
Honorary Chairman, Kuwait Association for Learning Differences - Kuwait
Award Winner, Kuwait Financial Forum 2009, for contributions to the Kuwait investment sector and success in global financial markets
Award Winner, Tunis Arab Economic Forum 2007
Recipient of Lifetime Achievement Award, Beirut Arab Economic Forum 2007
Recipient of the Arab Bankers Association of North America (ABANA) Achievement Award in 2005
Over 30 years of experience in the financial sector
Graduated as a fighter pilot with the Kuwait Air Force in the USA.

SAMER KHANACHET

Executive Director

Member of the Executive Committee

Group Chief Operating Officer, Kuwait Projects Company (Holding) - Kuwait
Chairman, Takaud Savings & Pensions Company - Bahrain
Board Member, Burgan Bank - Kuwait
Board Member, United Real Estate Company – Kuwait
Chairman, United Gulf Management, Inc. - USA
Director, United Gulf Management Ltd. - UK
Board Member, United Gulf Investments Ltd. - Cayman Islands
Trustee, American University of Kuwait - Kuwait
Member, the Corporation Development Committee and the Educational Council of the Massachusetts Institute of Technology, Cambridge, MA, USA
Past President of the Arab Bankers Association of North America - New York, NY, USA
Over 40 years of experience in the financial sector
MBA, Harvard Business School, Boston, MA, USA
BSc, Chemical Engineering and BSc, Management Science, Massachusetts Institute of Technology, Cambridge, MA, USA.

SHEIKH ABDULLAH NASSER SABAH AL AHMAD AL SABAH

Executive Director

Board Member, Kuwait Projects Company (Holding) – Kuwait
Advisor to the Chairman of the Board of Directors of Kuwait Projects Company (Holding) - Kuwait
Chairman, KAMCO Investment Company K.S.C. (Public) - Kuwait
Vice-Chairman, Al Daiya United Real Estate Company – Kuwait
Over 20 years of experience in the financial sector
Graduate of the Royal Military Academy, Sandhurst, UK
BSc, Business Administration, New York Institute of Technology, USA.

MUBARAK MOHAMMED AL-MASKATI

Independent Director

Chairman of the Nominating & Remuneration Committee and Member of the Board Audit Committee

Board Member, Royal Aviation Company - Kuwait
Former Board Member, Kuwait Projects Company (Holding), and Kuwait Aviation Services Company - Kuwait
Manager of the Amiri Fleet, Amiri Diwan
Over 30 years of experience in the financial sector
BSc, Political Studies and Economics, Pennsylvania State University, USA.

BADER AL AWADI

Independent Director

Member of the Nominating & Remuneration Committee

Independent Director and Chairman of the Board Audit Committee of Tunis International Bank, Tunis
Independent Director at Assoufid B.V., Morocco
Board Member, Manar Interholdings SL - Spain
Founder of Mada Alsharqia Real Estate Development Company, Khobar, Saudi Arabia
Over 30 years of experience in the financial sector
BSc, Industrial Engineering, University of Miami, USA
Completed the General Manager Program, Harvard Business School, Boston, USA
Completed the Program for Management Development, Harvard Business School, Boston, USA.

MOHAMMED HAROON

Independent Director

Chairman of the Board Audit Committee and Member of the Nominating & Remuneration Committee

Former Advisor to the Board of Directors, United Gulf Bank, B.S.C., Bahrain
Former Acting Chief Executive and Deputy Chief Executive Officer, United Gulf Bank, B.S.C., Bahrain.
Previously he served National Bank of Pakistan in Bahrain and in Pakistan, and Investment Corporation of Pakistan, in various management positions.
Over 47 years of experience in the financial industry
BSc (Hons), Peshawar University, Pakistan
Diploma in Banking.

Executive Management


1


2

1. HUSSAIN LALANI
Acting Chief Executive Officer

2. MOHAMMED ALQUMAISH
Assistant General Manager, Chief Audit Executive & Corporate Secretary

3. DEEPA CHANDRASEKHAR
Senior Vice President, Chief Compliance Officer & MLRO

4. SYED REHAN ASHRAF
Senior Vice President, Chief Financial Officer


3


4


5


6

5. ADEL AL ARAB
Senior Vice President, Head of Operations

6. NIRMAL PARIK
Vice President, Head of Asset Management & Investment Banking

7. ABBAS AL TOOQ
Assistant Vice President, Head of Credit & Risk Management

8. HAMID AL HASHIMI
Vice President, Head of Treasury


7


8

Executive Management
(continued)

1. HUSSAIN LALANI FCA CISA

Acting Chief Executive Officer

Mr. Lalani joined UGB in 2002 and was appointed as the Acting CEO in September 2015. His career extends over 20 years. He has worked extensively with the Board of Directors on advisory transactions in his previous capacity as the Bank's Chief Financial Officer, and partnered with business divisions to support growth and business plans. Mr. Lalani was previously employed by Ernst & Young (Bahrain) and PriceWaterhouse Coopers (Pakistan). He is a Board Member of Takaud Savings & Pensions B.S.C. (c), Bahrain; Global Banking Corporation, Bahrain; United Gulf Financial Services North Africa, Tunisia; and Assoufid B.V. He is also a Non Executive Director of Takaud Savings & Pensions (DIFC). A Chartered Accountant and a Certified Information Systems Auditor, Mr. Lalani holds a Bachelor of Commerce degree from the University of Karachi, Pakistan.

2. MOHAMMED ALQUMAISH CIA CISA MBA

Assistant General Manager, Chief Audit Executive & Corporate Secretary

Mr. Alqumaish joined UGB in September 2001. He has more than 20 years of regional, commercial and investment banking experience in internal auditing, risk assessment, compliance, corporate governance and quality assurance services. He previously worked with Ahli United Bank and Shamil Bank in Bahrain. Mr. Alqumaish is a Board member of Tunis International Bank, Tunisia and Al Ameen Real Estate Investment Company, Iraq. He is a member of the Board Audit Committees of Tunis International Bank, Tunisia; Gulf Bank Algeria, Algeria; and Syria Gulf Bank, Syria. A Certified Internal Auditor (CIA) and Certified Information Systems Auditor (CISA), Mr. Alqumaish holds an MBA from the University of Strathclyde Business School, UK.

3. DEEPA CHANDRASEKHAR APRM CAMS FICA CFE CHARTERED MCSI

Senior Vice President, Chief Compliance Officer & MLRO

Mrs. Chandrasekhar joined UGB in 2008. She has over 28 years of experience in the areas of risk management, treasury, operations, internal audit and compliance. Mrs. Chandrasekhar holds an MBA degree from the University of Alberta, Canada; as well as several professional certifications. She is a member of the Steering Committee of the Professional Risk Managers International Association (PRMIA), Bahrain Chapter; and the Advisory Council of the Chartered Institute of Securities and Investment (CISI), Bahrain Chapter. She also serves as an international moderator for the Finance Accreditation Agency, Malaysia. Mrs. Chandrasekhar is a frequent speaker at professional forums and has published several financial articles.

4. SYED REHAN ASHRAF FCA MBA

Senior Vice President, Chief Financial Officer

Mr. Ashraf joined UGB in 2005. He was appointed CFO in October 2015 after serving as Head of Credit and Risk Management since October 2007. He has more than 19 years of experience in the areas of credit, risk management, advisory, compliance and assurance services – with Islamic and conventional banks – and the big four audit firms. He previously worked with Shamil Bank, Bahrain; Deloitte & Touche, Faysal Bank, Pakistan; and PriceWaterhouse Coopers, Pakistan. A Chartered Accountant (FCA) from the Institute of Chartered Accountants of Pakistan, Mr. Ashraf also holds an MBA from DePaul University of Chicago, USA.

5. ADEL AL ARAB CRA

Senior Vice President, Head of Operations

Mr. Al-Arab joined UGB in 1994. He has over 20 years of experience in the field of operations, credit and risk management. Mr. Al-Arab holds a Bachelor of Science (BSc) degree in Business Administration from the University of Bahrain. He is a Chartered Risk Analyst (CRA) from the Global Academy of Finance and Management, USA; and was awarded the Certificate of ISMA Foundation Program from the International Securities Market Association, Zurich. Mr. Al-Arab has attended several professional courses in banking, finance, and risk management.

6. NIRMAL PARIK CFA MBA

Vice President, Head of Asset Management & Investment Banking

Mr. Parik joined UGB in 2007 and was appointed Head of Asset Management & Investment Banking in October 2015. He has more than 14 years of experience in the financial services industry in investment banking, asset management and corporate banking. Prior to joining UGB, Mr. Parik worked in ING Investment Management (I) Pvt. Ltd. and IL&FS Financial Services Ltd. He currently serves as a Board Member of International Innovative Technologies Ltd., UK. Mr. Parik is a Chartered Financial Analyst (CFA) and holds an MBA degree with specialisation in Finance from BIM Trichy, India.

7. ABBAS AL TOOQ MBA APRM

Assistant Vice President, Head of Credit & Risk Management

Mr. Al Tooq joined UGB in 1999. He assumed the role of the Head of Credit and Risk Management in October 2015. He has more than 20 years of experience in the areas of credit, risk management, operations and audit. He previously worked with Jawad Habib Coopers & Lybrand, Daiwa Middle East Bank, and The Arab Investment Company. Mr. Al Tooq holds an MBA degree from DePaul University, Chicago, USA. He also holds the Associate Professional Risk Manager (APRM) from PRMIA.

8. HAMID AL HASHIMI

Vice President, Head of Treasury

Mr. Al Hashimi joined UGB in early 2017. His experience within Treasury is over 14 years, across all asset classes including structuring, sales & trading, as well as leading the syndication team for a number of regional capital market fixed income issuances. Mr. Al Hashimi has held several positions within Treasury at various international and regional financial institutions (both conventional and Islamic) Mr. Al Hashimi holds a Bachelor's Degree with Honors in Business Administration with emphasis on Economics from the University of Bradford UK, including an in depth dissertation on the impact of e-commerce on the Treasury.

Review of Operations

STRATEGY AND BUSINESS OVERVIEW

UGB's strategic objective is to create the MENA region's premier asset management, merchant banking and investment bank. UGB seeks to be the preferred gateway to the region for its clients and global partners through the delivery of both conventional and Islamic services, backed by world class standards of support, infrastructure and processes. The Bank works with strategic partners to create opportunities that position UGB as a leading financial institution for the region.

Either directly or through its subsidiaries, associate companies and joint venture, UGB engages primarily in asset and fund management, investment banking, private equity and corporate banking. Other business activities include commercial banking, proprietary investments, savings and pensions, brokerage and treasury.

Either directly or through its subsidiaries, associate companies and joint venture, UGB engages primarily in asset and fund management, investment banking, private equity and corporate banking. Other business activities include commercial banking, proprietary investments, savings and pensions, brokerage and treasury.

ASSET MANAGEMENT AND INVESTMENT BANKING

Asset Management

Asset and fund management activities – covering local, regional and international markets – comprise discretionary and non-discretionary portfolio management; securities trading; portfolio structuring and asset allocation advice; mutual funds; investments and structuring; and alternative / structured investments.

Investment Banking

Conventional and Islamic investment banking activities cover equity and debt underwriting, private placements, capital restructuring, and mergers and acquisitions.

Private Equity

Private equity activity focuses on key growth or demand sectors such as telecommunications, media, technology, and energy.

Corporate Banking

Corporate banking advisory services include IPO and private placement advisory and execution; business valuation and financial feasibility studies; project finance; and due diligence.

OTHER BUSINESS ACTIVITIES

Commercial Banking

UGB along with its commercial banking subsidiary FIMBank plc, work closely with its associate, Burgan Bank, which manages commercial banking assets in various countries.

Savings and Pensions

UGB's associate, Takaud Savings and Pensions B.S.C. (c), is the first financial institution in the MENA region to provide a range of personal pensions and savings products.

Brokerage

UGB provides financial brokerage services for overseas clients who wish to trade on shares listed on the Bahrain Bourse. The Bank also provides clients with access to the Kuwait Stock Exchange through its associate, Al Sharq Financial Brokerage Company.

KEY BUSINESS DEVELOPMENTS AND INITIATIVES

- UGB's assets under management stood at US$ 10 billion at the end of 2016 compared with US$ 10.7 billion at the end of the previous year.
- Revenue from associated companies in 2016 decreased slightly to US$ 41.1 million compared with US$ 45.9 million in 2015. Key contributors were Burgan Bank with US$ 35.5 million and United Real Estate Company with US$ 3.3 million.
- New investments during the year include a 9.8% stake in Advanced Technology Company, the leading end-to-end total healthcare solutions provider in Kuwait; a minority stake in the MENA region; and acquisition of a prime income generating property in Kuwait.
- Since the acquisition in 2015 of a prime income generating, fully leased commercial property in Federal Street, Boston, USA, the Bank has been actively involved in the day to day management of the property, with the aim of increasing the overall value of the investment.

Review of Operations
(continued)

UGB SUBSIDIARIES AND ASSOCIATES

United Gulf Bank B.S.C.

Commercial Banking	Savings & Pensions	Brokerage	Asset Management & Investment Banking	Non Financial Operating Companies
15% Burgan Bank S.A.K., Kuwait Commercial Bank, Kuwait	50% Takaud Savings and Pensions B.S.C. (c) Pensions Company, Bahrain	19% Al Sharq Brokerage Company K.S.C. (c) Brokerage House, Kuwait	86% KAMCO Investment Company K.S.C. (Public) Asset Management, Kuwait	10% United Real Estate Company S.A.K. Real Estate, Kuwait
61% FIMBank p.l.c. Malta Commercial Bank, Malta			44% North Africa Holding Company K.S.C. (c) Investment Company, Kuwait	40% United Capital Transport Company Transport Company, Kuwait
31% Syria Gulf Bank S.A. Syria Commercial Bank, Syria			85% United Gulf Financial Services - North Africa Asset Management, Tunisia	40% Assoufid BV Real Estate, Morocco

UGB consolidated holdings, as at 31 December 2016

ASSET MANAGEMENT & INVESTMENT BANKING

KAMCO Investment Company K.S.C. (Public) (KAMCO)

UGB Consolidated Subsidiary based in Kuwait

Established in 1998, KAMCO Investment Company is a leading asset management and financial institution, with one of the largest private sector assets under management (AUM) in the GCC region. Its three principal business lines are asset management, financial services, and investment advisory research services, which are offered to a diverse local, regional and international client base. Key developments in 2016 include the opening of the Company's first international office in Dubai International Financial Centre as part of its geographic expansion policy; and acting as joint lead manager for two of the first subordinated Tier 2 Basel III compliant bond issuances in Kuwait – for Burgan Bank and Gulf Bank – both valued at KWD 100 million (US$ 237 million) each. KAMCO also acquired General Electric's Global Operation Center in the USA, in line with its strategy to provide new and innovative income generating alternative asset streams. At the end of 2016, the Company had total client AUM of over US$ 10 billion. UGB owns 86% of KAMCO, which is listed on the Kuwait Stock Exchange.

United Gulf Financial Services Company North Africa (UGFS-NA)

UGB Consolidated Subsidiary based in Tunisia

Commencing operations in 2009, United Gulf Financial Services Company North Africa is an asset management company regulated by the Tunisian Capital Market Authority – Conseil du Marché Financier (CMF). The Company is primarily involved in three main activities: fund services, portfolio management services, and corporate finance services. UGB has a total consolidated interest of 85% in UGFS-NA, whose shares are unlisted.

North Africa Holding Company (NorAH)

UGB Associate Company based in Kuwait

North African Holding Company was established in 2006 with the aim of capitalising on the significant investment opportunities arising within North African economies, by building genuine partnerships with local businesses that have demonstrated the ability, or have the potential, to deliver real value. The Company's target market spans Morocco, Algeria, Tunisia, Libya and Egypt, which together account for two thirds of the MENA population, and offer considerable untapped investment potential. Key growth sectors include real estate, industrial, logistics, healthcare, education and agribusiness. UGB has a total consolidated interest of 44% in NorAH, whose shares are unlisted.

COMMERCIAL BANKING

Burgan Bank (BB)

UGB Associate Company based in Kuwait

Established in 1975, Burgan Bank is a subsidiary of KIPCO. The Bank is Kuwait's second largest lender in terms of assets, and over the years has acquired a leading role in the commercial banking sector in the MENA region, with operations spanning Kuwait, Turkey, Jordan, Algeria, Tunisia, Iraq, Lebanon and Dubai. Its achievements in product innovation, information technology, efficiency, quality and corporate governance have been recognised by numerous awards, with several of them being unique to the region. In 2016, Burgan Bank successfully completed a KWD 100 million (US$ 237 million) subordinated Tier 2 Basel III compliant bond issue, one of the first of its kind in Kuwait. UGB has an equity stake of 15% in Burgan Bank, which is listed on the Kuwait Stock Exchange.

FIMBank plc

UGB Consolidated Subsidiary based in Malta

Established in 1994, FIMBank is an international trade finance specialist. The Bank's main business lines comprise trade commodity finance, forfaiting, factoring and treasury. FIMBank has branches in Dubai and Athens, and a representative office in London; and owns the UK registered London Forfaiting Company, which is represented across four continents. Factoring subsidiaries and joint-ventures have been established in Brazil, India, Egypt and Chile. The successful implementation of a consolidation strategy over the past two years has resulted in the Bank returning to profitability in 2016. UGB owns a 61% stake in FIMBank, whose shares are listed on the Malta Stock Exchange.

SAVINGS AND PENSIONS

Takaud Savings & Pensions (TAKAUD)

UGB Associate Company based in Bahrain

Takaud Savings & Pensions is a venture between the KIPCO Group and UGB. The objective of this new entity is to specialise in offering savings and private pension products engineered and conceived primarily for customers in the MENA region. The Company's growth strategy involves establishing specialised companies in different countries within the MENA region, or entering into strategic distribution agreements. The Bahrain head office provides market analysis, product engineering, distribution management, asset management and funds management. In 2016, the Company signed new distribution agreements with Ahli Capital, the investment arm of Al Ahli Bank of Kuwait; Amwal, the first regulated asset management firm in Qatar; and Bahrain based Takaful International, one of the pioneering Islamic insurance companies in the Middle East. As part of its thought leadership and industry awareness activities, TAKAUD hosted the inaugural Middle East Pensions Conference in 2016 under the patronage of the Central Bank of Bahrain.

Review of Operations
(continued)

BROKERAGE

Al Sharq Financial Brokerage Company (Al Sharq)

UGB Associate Company based in Kuwait

Established in 1985, Al Sharq Financial Brokerage Company has grown to become one of the largest brokerage firms in Kuwait, as measured by the number of transactions conducted on the Kuwait Stock Exchange (KSE). In 2016, Al Sharq had a market share of 19% of aggregate trades on the KSE. UGB owns 19% of the Company on a consolidated basis. Al Sharq's shares are unlisted.

NON-FINANCIAL ASSOCIATES

United Real Estate Company (URC)

UGB Associate Company based in Kuwait

Established in 1973, United Real Estate Company is involved in real estate activities that include the purchase, sale, lease and rental of land and buildings. URC handles the construction of private and public buildings and projects, and manages third party properties in Kuwait, Egypt, Lebanon, Oman, Morocco and Jordan. The Company's real estate portfolio includes commercial complexes, hotels and resorts, residential buildings, high rise office buildings, and mixed use developments. In Kuwait, these include KIPCO Tower, Marina Plaza, Marina Mall and Marina Hotel. URC is developing Abdali Mall in Jordan, Junoot in Oman, Raouche Views in Lebanon, Aswar Residences in Egypt, and Assoufid in Morocco. It has also developed Salalah Gardens Mall and Salalah Mall Residences in Oman. UGB owns a 10% stake in URC, which is listed on the Kuwait Stock Exchange.

United Capital Transport Company (UNICAP)

UGB Associate Company based in Kuwait

United Capital Transport Company was established in 2011 as a joint venture between UGB's subsidiary KAMCO and ANHAM, a leading contracting firm active throughout the MENA region, Central Asia and Europe. The Company is a leasing solutions provider to governments, international oil companies, and businesses involved in various construction, mining and industrial services. UNICAP offers timely, efficient and customer-focused equipment and logistical support services to a variety of clients and markets. Customised leasing, transportation and financing solutions are provided to vendors and customers to meet their specific needs within geographically diverse and strategically challenging markets. UGB owns 40% of UNICAP on a consolidated basis. The Company's shares are unlisted.

Assoufid B.V.

UGB Associate Company based in Morocco

Assoufid is a Morocco-based real estate development company. Its prime property is the Assoufid high end mixed use development in Marrakech. The property is spread over 222 hectares on a naturally undulating terrain, and set against the backdrop of the snow capped Atlas Mountains. The first phase is the award winning Assoufid Golf Club, which has been completed. The second phase currently underway, includes a 5-star hotel and luxury branded golf villas. UGB holds a 40% stake in the Company, whose shares are unlisted

SHARED SERVICES

Treasury

Treasury manages UGB's liquidity and funding requirements; and also implements the Bank's hedging strategies in terms of foreign exchange and interest rate exposures. In another challenging year, UGB maintained its existing long-term counterparty relationships and added a number of new counterparties, while continuing to benefit from the support it receives from the KIPCO Group. Deposits from customers increased by 113% to reach US$ 985.2 million in 2016, reflecting UGB's strong reputation in the market. The Bank retained a strong balance sheet, with a consolidated capital adequacy ratio of 13.9% which exceeds the minimum requirements of the Central Bank of Bahrain of 12.5%. Liquidity remained healthy, with total liquid assets of US$ 629.1 million representing 20.7% of the balance sheet at the end of the year. UGB continued its policy of deleveraging the balance sheet through liquidating non-accretive assets, and using the proceeds to repay borrowings. During 2016, the Bank repaid a US$ 100 Tier 2 Bond and a US$ 70 million Club Loan; and raised medium-term financing of US$ 100 million in aggregate from two different transactions during the first half of the year. UGB strengthened its capital base through raising Additional Tier 1 capital of US$ 33 million.

Operations

The main activities of the Operations function include settlement of foreign exchange and money market transactions; handling payments and funding in coordination with Treasury; and facilitating transfers. During the year, UGB continued to enhance and streamline its critical back office operating processes and procedures in order to improve efficiency and productivity. A key development in 2016 entailed upgrading the SWIFT system from the Alliance Workstation to the Alliance Web Platform SE (Server-Embedded) which hosts graphical user interface software for all Alliance products. This new platform offers a scaleable and cost-effective solution for harmonising all back-office SWIFT applications.

Human Resources

UGB places the highest importance on the professional development of its people. During 2016, the Bank continued to encourage and support staff to obtain professional qualifications. Two employees achieved Chartered Financial Analyst (CFA) and Financial Risk Manager (FRM) accreditation; while a number of other staff are pursuing their respective professional examination studies. Appropriate staff training is provided by the Bahrain Institute of Banking & Finance (BIBF) and other relevant external bodies; while mandatory regulatory-related training, such as Anti-Money Laundering, is conducted in-house. UGB's merit-based Mashare'a Al Khair Scholarship Programme continued to assist dependants of the Bank's staff to obtain degrees from accredited colleges, universities and other academic institutions. Other HR-related developments in 2016 included reviewing and revising the Bank's remuneration policy and procedures in line with latest changes to the Sound Remuneration Practices for Licensed Banks issued by the Central Bank of Bahrain. At the end of 2016, the Bank's headcount in Bahrain was 38 – on par with the previous year.

Information Technology

During 2016, UGB continued to invest in further strengthening and enhancing its information and communications technology framework. In light of increasing cyber-attacks against regional and international financial institutions, UGB appointed external consultants to assess the Bank's vulnerability to various cyber security risks. This comprehensive exercise entailed vulnerability assessment and penetration testing of external and internal networks, SWIFT environment, wireless network and corporate website. It also included detailed reviews and assessments of the infrastructure security configuration, social engineering and physical security. Based on the results, the Bank's IT Policy Manual was reviewed and updated to ensure that appropriate processes and procedures are in place to detect, monitor, mitigate and report cyber-attacks. UGB also conducted two successful tests of its business continuity planning (BCP) process during 2016 in line with regulatory requirements of the Central Bank of Bahrain (CBB). The second test involved a special simulation exercise at the offsite BCP site under the scenario of staff being unable to access their offices, and being directed to the BCP site to resume their work. In another key development, UGB's new customised enterprise risk management (ERM) system was fully implemented in 2016. The benefits of ERM include enhancement of risk management processes and procedures, and the automation of risk reports to Management and the CBB. In addition, a redesigned and re-engineered website was launched. This features enhanced user-friendliness and state-of-the-art security, together with easier accessibility from different browsers and mobile devices.

Financial Review

This review provides a detailed description of UGB's financial performance for the year ended 31 December 2016.

The notes to UGB's Consolidated Financial Statements provide additional relevant details, with some of these notes being cross referenced here. Figures contained in the Financial Performance Summary are subject to rounding adjustments and in certain instances, the sum of the numbers in a column or row may not conform exactly to the total figure given for that column or row.

REVENUES

UGB's total revenues were US$ 138.0 million in 2016 compared with US$ 144.8 million in 2015 as indicated below:

Total Revenues US$ million	2016	2015
Financial services	35.2	38.0
Real estate	7.6	7.8
Other associates	1.6	1.5
Credit related fees and commission	13.5	14.5
Management fees from fiduciary activities	13.5	13.9
Advisory fees	7.4	3.3
Interest income	48.5	56.3
Realised gain / (loss) on non - trading investments	0.9	(0.1)
Trading loss	(0.2)	(5.0)
Dividend	7.2	5.1
Gain on sale of associates and subsidiaries	2.8	2.6
Gain on bargain purchase	-	2.0
Foreign currency translation (losses) / gains	(5.8)	3.3
Other income	5.8	1.6
Total	138.0	144.8

During 2016, the decrease in total revenues is mainly attributed to foreign currency losses on the Group's Euro and Turkish Lira exposures, and a decrease in interest income. The impact is partially offset by higher advisory fees from new mandates, lower trading losses resulting from recovering regional stock markets and recovery in oil prices, and higher other income.

Financial Services

UGB's financial services related revenues are derived from its investment in associates involved in asset management and investment banking, commercial banking, and brokerage. Details of these entities are included in the Review of Operations section in this Annual Report.

Results from financial associates decreased to US$ 35.2 million compared with US$ 38.0 million in 2015. The decrease is mainly due to the sale of a 2% stake in Burgan Bank during the first quarter of 2016; while positive results from Manafae, Assoufid and North Africa Holding lessened the impact from Burgan's sale. The share of profit from Burgan Bank decreased to US$ 35.5 million from US$ 44.0 million in 2015.

The table below indicates the performance of UGB's financial associates:

Revenue - Financial Associates US$ million	2016	2015
Burgan Bank	35.5	44.0
Manafae Investment Company	1.2	(0.4)
Assoufid B.V.	0.6	(1.4)
Brasilfactors	-	(0.2)
The Egyptian Company for Factoring S.A.E.	-	(0.6)
Al Sharq Financial Brokerage Co.	(0.1)	-
CIS Factors Holding B.V.	(0.4)	-
Takaud Saving & Pensions Company	(0.8)	-
North Africa Holding Company	(0.8)	(3.4)
Total	35.2	38.0

Real Estate

UGB's real estate revenues were derived mainly from rental income from real estate properties in Kuwait and the USA; and share of income from United Real Estate Company (URC), which contributed US$ 3.3 million in 2016 compared with US$ 6.0 million in 2015. The lower value is due to the sale of an 11.6% shareholding in URC during the first quarter of 2016.

Revenues - Real Estate US$ million	2016	2015
United Real Estate Company	3.3	6.0
N.S. 88	0.7	-
KAMCO Real Estate Yield Fund	0.3	0.4
Rental income	3.3	1.4
Total	7.6	7.8

Other Associates

Profits from other associates of UGB increased slightly to US$ 1.6 million in 2016 from US$ 1.5 million in 2015.

Revenues - Non Financial Associates US$ million	2016	2015
United Capital Transport Company	1.3	1.3
Kuwait Education Fund	0.3	0.2
Total	1.6	1.5

Credit Related Fees and Commission Income

Credit related fees and commission income decreased slightly to US$ 13.5 million in 2016 from US$ 14.5 million in 2015, mainly due to exits from certain assets and jurisdictions after a re-alignment of strategy at FIMBank.

Management Fees from Fiduciary Activities

Management fees decreased moderately from US$ 13.9 million in 2015 to US$ 13.5 million in 2016, after regional stock markets stabilised during the year. The slight drop is due to a decrease in UGB's assets under management from US$ 10.7 billion in 2015 to US$ 10.0 billion in 2016.

Advisory Fees

Advisory fee income increased to US$ 7.4 million in 2016 from US$ 3.3 million in 2015, mainly due to new mandates.

Interest Income

The main source of interest income for UGB is derived from interbank placements and the loan portfolio of FIMBank p.l.c. Interest income decreased from US$ 56.3 million in 2015 to US$ 48.5 million in 2016, mainly due to a one-off income recorded in the previous year, and a general decrease in interest income at FIMBank.

Trading Loss

Trading positions recorded a loss of US$ 0.2 million in 2016 compared to loss of US$ 5.0 million for 2015. Trading losses were reduced mainly due to the slight recovery of regional stock markets during the year.

Dividend Income

Dividend income increased to US$ 7.2 million in 2016 compared to US$ 5.1 million in 2015, mainly due to dividend income received from FIMBank's investments in funds.

Foreign Currency Translation (Losses) / Gains

Foreign currency translation losses of US$ 5.8 million were recorded in 2016 compared to gains of US$ 3.3 million in 2015. This is attributed mainly to the depreciation of the Euro and Turkish Lira during the year.

EXPENSES

Interest Expense

Interest expenses increased slightly from US$ 51.6 million in 2015 to US$ 52.9 million in 2016, mainly due to a small increase in LIBOR during the year.

Operating Expenses

Operating expenses decreased by 10% to US$ 73.5 million in 2016 compared with US$ 81.4 million in 2015. Salaries and benefits decreased to US$ 48.5 million (2015: US$ 49.5 million) while general and administration expenses decreased to US$ 25.0 million (2015: US$ 31.8 million).

Operating expenses US$ million	2016	2015
Salaries and benefits	48.5	49.5
General and administrative expenses	25.0	31.8
Total	73.5	81.3

Taxation

A net income tax credit of US$ 0.6 million was recorded in 2016 compared to US$ 6.6 million in 2015. Lower income tax credit for 2016 mainly related to tax credits booked at FIMBank p.l.c. due to losses at its subsidiaries.

Provisions

UGB made total provisions of US$ 11.2 million in 2016 compared to US$ 12.8 million in 2015. Provisions for 2016 mainly resulted at FIMBank due to impairment provisions on loans and advances; through the investment in an associate of KAMCO (Al Sharq), and certain available for sale investments.

Provisions for impairment US$ million	2016	2015
Impairment loss on investments	2.9	3.2
Provision for doubtful loans and other assets - net	8.3	9.6
Total	11.2	12.8

Net Income Attributable to Parent

Net income attributable to parent decreased to US$ 6.3 million from US$ 11.2 million in 2015. Earnings per share similarly decreased to US 0.77 cents from US 1.38 cents in 2015.

CONSOLIDATED BALANCE SHEET

Consolidated Assets

UGB's consolidated assets stood at US$ 3.01 billion at the end of 2016 compared with US$ 2.72 billion at the end of 2015. A comparison of the two years is provided below.

Assets - US$ millions US$ million	2016	2015
Demand and call deposits with banks	176.9	176.8
Placements with banks	187.4	57.0
Investments carried at fair value through statement of income	45.2	50.7
Non-trading investments	404.4	285.0
Loans and receivables	1,184.8	1,032.1
Other assets	112.7	119.7
Investments in associates	709.0	854.0
Investment properties	101.3	46.2
Property and equipment	32.1	41.7
Goodwill	51.9	52.3
Assets of disposal group classified as held for sale	-	1.0
Total	3,005.7	2,716.5

Demand, Call and Placements with Banks

Demand, call and placements with banks were US$ 364.2 million in 2016 compared with US$ 233.8 million in 2015, as funds raised through customers were placed with banks under short term time deposits. Total liquid assets – comprising cash, deposits, liquid securities and other assets – represented 20.7% of the balance sheet as at year-end 2016 (end-2015: 15.7%).

Trading Investments (investments carried at fair value through the statement of income)

Investments carried at fair value through the statement of income were US$ 45.2 million in 2016 compared with US$ 50.7 million in 2015. This portfolio comprises securities held for trading and managed funds designated as held for trading. The securities held for trading portfolio consists mainly of equities listed on the Kuwait Stock Exchange.

Non-Trading Investments

Non-trading investments increased to US$ 404.4 million in 2016 compared with US$ 285 million in 2015. The total portfolio mainly comprises listed equities of US$ 57.8 million (2015: US$ 12.5 million), quoted debt securities of US$ 161.8 million (2015: US$ 134.7 million), unlisted equities of US$ 121.3 million (2015: US$ 64 million), real estate managed funds of US$ 12.0 million (2015: US$ 16.6 million) and other managed funds of US$ 51.5 million (2015: US$ 52.8 million).

The major investments classified under the non trading investments portfolio as at 31 December 2016 were:

Quoted bonds: US Treasury bonds of US$ 38.4 million, European Investment Bank bonds of US$ 40.3 million, Government of Malta bonds of US$ 13.5 million, and other corporate bonds of US$ 69.6 million as of 31 December 2016. These bonds are quoted on their respective stock exchanges in the United States, Europe and Malta, and are carried at their quoted market prices as at year end.

Advanced Technologies Company: UGB acquired a 9.8% stake in ATC 2016. ATC is a leading medical equipment and turnkey solution provider. It was established in Kuwait in 1981 and listed on the Kuwait Stock Exchange in 2007. It offers over 1,000 products to customers in the public and private sectors, focusing on medical, pharmaceutical, dental and laboratory equipment. ATC provides its products and services to over 500 health care facilities, and has approximately a 45% share of the Kuwait medical sector.

Burgan Equity Fund: This is an open ended fund managed by Burgan Bank, and focuses mainly on investing in shares of Kuwaiti companies listed on the KSE. The fund adopts a balanced investment policy. Its objective is to earn long term capital gains with minimum possible risk. UGB's investment represents an equity stake of 8.9% (2015: 9.7%).

Kuwait Energy plc: This is an independent oil and gas company actively engaged in the exploration, appraisal, development and production of hydrocarbons in the MENA region. As of 31 December 2016, UGB owned an equity stake of 1.2% (2015: 1.2%) in Kuwait Energy plc.

United Tower Holding Company: This is a real estate development company that concentrates on real estate investment, development and management activities in Kuwait. UGB's investment represents an equity stake of 7.9% (2015: 7.9%).

Global Banking Corporation (GBCORP): This is an Islamic wholesale bank incorporated in Bahrain, with an issued and paid up capital of US$ 200 million. GBCORP's business lines include private equity and venture capital, real estate and infrastructure development, asset management, advisory services in corporate finance and capital markets, and portfolio management services. The year end value represents an equity stake of 12.5% (2015: 12.5%).

Loans and Advances

Loans and advances in 2016 amounted to US$ 1,184.8 million (2015: US$ 1,032.1 million) and consisted mainly of facilities extended by FIMBank.

Details of the loan book are as follows:

Loans and Advances US$ million	2016	2015
Forfaiting assets	538.2	355.1
Factoring assets	220.6	340.8
Loans to customers	168.6	164.8
Loans to banks	173.8	114.4
Syndication loans	124.0	98.1
Staff loans	3.1	3.1
Gross loans and advances	1,228.3	1,076.3
Less: Provision for impairment	(43.5)	(44.2)
Total	1,184.8	1,032.1

Past due and impaired loans amounted to US$ 70.5 million (2015: US$ 80.9 million) against which provisions of US$ 43.5 million (2015: US$ 44.2 million) were recorded. The nonperforming loan ratio stood at 6% with a coverage ratio after cash collateral and insurance of 84%.

Investments in Associated Companies

Investments in the Bank's associated companies decreased to US$ 709 million in 2016 compared with US$ 854 million in 2015, mainly due to the sale of a 2% stake in Burgan Bank and an 11% stake in URC. The Bank's associated companies contributed a total profit of US$ 41.1 million in 2016 (2015: US$ 45.9 million), with key contributors being Burgan Bank (US$ 35.5 million) and United Real Estate Company (US$ 3.3 million).

Investment Properties

During the year, UGB acquired real estate properties in Kuwait for US$ 56 million. Rental income on these investments amounted to US$ 2.2 million.

Consolidated Liabilities

UGB's consolidated liabilities increased to US$ 2,476.3 million in 2016 compared with US$ 2,213.3 million in 2015.

Liabilities US$ million	2016	2015
Due to banks and other financial institutions	726.2	838.2
Deposits from customers	985.2	462.1
Loans payable	652.2	714.5
Subordinated debt	50.0	143.3
Other liabilities	62.7	55.0
Liabilities of disposal group classified as held for sale	-	0.2
Total	2,476.3	2,213.3

During the year, the UGB Group repaid loans of US$ 343 million and raised the new medium term borrowings of US$ 262 million.

Total Equity

As at 31 December 2016, UGB's equity increased to US$ 529.5 million (2015: US$ 503.3 million) mainly reflective of the USD 33 million additional tier 1 capital raised during Q1 2016.

Equity US$ million	2016	2015
Share capital	208.7	208.7
Treasury shares	(18.1)	(18.1)
Share premium	11.5	11.5
Statutory reserve	100.5	99.9
General reserve	81.0	80.4
Treasury share reserve	14.2	14.2
Fair value reserve	(50.0)	(48.2)
Foreign currency translation reserve	(37.5)	(34.9)
Retained earnings	83.7	80.5
Capital and reserves attributable to the shareholders of the parent	394.0	394.0
Perpetual Tier 1 capital	33.0	-
Non-controlling interests in equity	102.5	109.3
Total Equity	529.5	503.3
Total Liabilities and Equity	529.5	503.3

The major movements in equity from 31 December 2015 to 31 December 2016 were:

- Net profit of US$ 6.3 million
- Issue of Perpetual Tier 1 Capital of US$ 33 million
- Negative fair value reserve movement of US$ 1.8 million
- Negative FX revaluation reserve movement of US$ 2.6 million mainly due to deprecation of the Kuwaiti Dinar

The minority interest decreased by US$ 6.9 million mainly due to losses attributable to non-controlling interests in FIMBank p.l.c. and Takaud.

OFF-BALANCE SHEET COMMITMENTS

UGB's off-balance sheet commitments comprise guarantees, letters of credit, credit commitments, undrawn investment commitments, and bankers' acceptances; financial instruments to cover foreign exchange risks; forward purchase and sales contracts; and interest rate and currency swaps. The Bank's investments and credit-related commitments aggregated to US$ 199.2 million as at 31 December 2016 (2015: US$ 165.1 million). UGB does not trade derivatives, nor does it engage in proprietary foreign exchange trading. Further details regarding off-balance sheet commitments are provided in Note 28 to the Consolidated Financial Statements for the year ended 31 December 2016.

CAPITAL ADEQUACY

UGB's consolidated capital adequacy ratio of 13.9% at 31 December 2016 (2015: 15.0%) under the Basel III regulations as mandated by the Central Bank of Bahrain, was above the minimum requirement of 12.5%.

US$ million	2016	2015
Capital base:		
Tier 1 capital	264.12	316.35
Tier 2 capital	73.75	88.29
Total capital base (a)	337.87	404.64
Credit risk weighted exposure	2,227.19	2,576.21
Market risk weighted exposure	122.73	66.90
Operational risk weighted exposure	84.64	52.75
Total risk weighted exposure (b)	2,434.56	2,695.86
Capital adequacy (a/b * 100)	13.9%	15.0%
Minimum requirement	12.5%	12.5%

UGB's robust risk management framework provides comprehensive controls and ongoing management of major risks inherent in the Bank's business model and operational activities.

Key Developments in 2016

- UGB maintained its focus on operational consolidation and strengthening liquidity in order to achieve financial efficiency across Bank wide operations.
- The Bank completed the implementation of a new custom-designed Enterprise Risk Management (ERM) system, enhancing real time risk reporting. The system covers mainly credit, liquidity and market risk; and also has the capability to provide stress testing, limits monitoring, dashboard and heat maps, and reports with drill-down capabilities that deliver in-depth and real-time information on ERM. A fully automated Operational Risk Management (ORM) system is already in place, which enables the Bank to monitor, mitigate and report its operational risk exposures in a structured and robust manner.
- A series of meetings were held with the Central Bank of Bahrain regarding UGB's capital optimisation strategy.
- The scope of quarterly reporting to the Board, its Committees, and Management on liquidity, operational risk and investment reviews was enhanced.

Risk Philosophy

The Bank's risk philosophy is based on the following five principles:

1. Sound knowledge base, experience and judgement of Senior Management and Risk Management staff, are the cornerstone of successful risk mitigation.
2. Vigilance, discipline and attention to detail are mandatory.
3. Complete segregation of duties and reporting authorities must exist between business lines and support functions.
4. Policies and procedures must be clear, properly documented, well-communicated, understood, and implemented in both letter and spirit.
5. Well-established processes and systems provide the backbone of risk management practices at the Bank.

Responsibilities

The Board of Directors of UGB has the ultimate authority for setting the overall risk appetite, risk tolerance, parameters and limits, within which the Bank operates. The Board approves the Bank's overall risk profile and significant risk exposures, as well as the policies, procedures and controls that have been extensively documented.

The Board has delegated day-to-day decision making to the Executive Committee (EC) that comprises three Executive Directors. The EC meets between Board meetings to approve all proposals that exceed the threshold of the Investment Committee.

The Investment Committee (IC) is responsible for approving or recommending approvals to the Executive Committee; limits for individual exposures; investments; and concentrations towards banks, countries, industries, risk rating classes or other special risk asset categories.

The Risk and Compliance Committee (RCC) supervises the adoption of best practice in the areas of risk and compliance. It acts as the steering committee for risk and compliance initiatives, responsible for monitoring the progress and facilitating a smooth transition towards complete compliance with provisions of the New Capital Accord and other regulatory requirements. During 2016, the Committee met four times.

Further information on the constitution and responsibilities of these committees is disclosed in the Corporate Governance Report available on the Bank's website: www.ugbbh.com.

UGB's ability to properly identify, assess, manage, measure, monitor and report risk is critical to its financial strength and profitability. A comprehensive set of risk management policies, processes and limits are in place to provide guidelines and parameters. These are continuously updated with the objective of incorporating best practice, changes in market factors, and changes in the regulatory environment in the various jurisdictions in which the Bank operates.

Risk Management Philosophy

The overall risk management strategy of UGB focuses on optimising the risk return profile of the Bank's exposures (a portfolio approach) as well as avoiding losses. The management philosophy of the Bank for managing the main types of risk is summarised below:

Risk Type	Risk Management Philosophy
Credit risk	Discipline its lending activities and ensure that credit facilities are granted on a sound basis; and that the Bank's funds are invested in a profitable manner.
Market risk	Minimise the loss of the value of financial instruments or a portfolio of financial instruments, due to an adverse change in market prices or rates.
Interest Rate risk	Capture all material sources of interest rate risk, and assess the effect of interest rate changes on the income stream and equity of the Bank.
Liquidity risk	Identify, capture, monitor and manage the various dimensions of liquidity risk with the objective of protecting asset values and income streams, such that the interests of the Bank's shareholders are safeguarded, while maximising returns to shareholders.
Operational risk	Mitigate or insure the risk of loss arising from a failure in UGB's internal processes due to inadequate internal controls and procedures, human error, deliberate acts, and/or business interruptions caused by technology, systems or external disasters beyond the Bank's control.

TYPES OF RISK

The major types of risk to which UGB is primarily exposed include credit, market, operational, liquidity and funding, interest rate, concentration, reputational and legal risks. Details on each of these are provided in the Basel III Pillar III Risk Management and Capital Adequacy Disclosures available on the Bank's website at: www.ugbbh.com.

The following section provides a brief synopsis of the different types of risk and the processes adopted to identify, assess and monitor them.

Credit Risk

Credit risk arises mainly from the extension of credit facilities in the UGB Group's commercial banking, investment banking and trading activities, where there is a possibility that a counterparty may fail to honour its commitments.

The Bank identifies and manages credit risk inherent in all products and activities, and ensures that such risks are assessed in depth and are well understood. These activities are then subject to adequate risk management procedures and controls which are approved by the Board of Directors prior to implementation.

The Bank mitigates its credit risk through:

- Establishing an appropriate credit risk environment
- Operating under a sound credit and investment approval process
- Ensuring adequate controls over the credit risk management process
- Knowledge of target markets, borrowers and counterparties
- Maintaining appropriate credit administration, measurement and monitoring processes

The Bank's policies and procedures provide the guidelines for credit risk management. UGB manages credit risk through its limit structure, which controls the amount of risk that it is willing to accept for individual counterparties, related parties, and for geographical and industry concentrations. Exposures with respect to the adherence of these limits are monitored on a regular basis.

There is a two-tier committee structure to approve and review credit and investment risk. The Investment Committee (IC) includes the Acting Chief Executive Officer, the Head of Asset Management and Investment Banking, and the Chief Financial Officer. The Acting Head of Credit and Risk Management is a non-voting member on the Committee and acts as its secretary. Exposures beyond IC delegated limits are approved by the Board's Executive Committee or the full Board of Directors.

The credit risk inherent in trading activities is also actively managed, and in case of exposures to counterparties, is calculated daily as the sum of mark-to-market values. In certain cases, the Bank has entered into legally-enforceable netting agreements covering its money market and foreign exchange trading activities. In areas where UGB acts as an agent for commodity trading on behalf of certain Islamic financial institutions, the risk is managed through simultaneous spot and forward trading in commodities, through well established financial and commodity trading institutions that have been subjected to a detailed credit review. The Bank does not trade in derivatives.

Continuous monitoring of the Bank's assets through various reports and reviews is critical to early and timely identification of any impairment. A monthly risk asset review report is produced by the Credit and Risk Management Department and reviewed monthly by the Management Committee and quarterly by the Risk & Compliance Committee. All investments are assessed based on rating, industry and geographic exposure, in addition to a number of other parameters. The purpose of this report is also to ensure compliance with external regulatory requirements and internal risk policy guidelines. Additionally, a semi annual review of all investments is conducted for monitoring performance and highlighting any recent developments. A quarterly review of loans is prepared for the purpose of identifying impairments and providing an update on the status of each facility. The risk asset review report is reviewed on a monthly basis by Management, and quarterly by the Risk and Compliance Committee.

UGB has adopted the Standardized Approach for calculating the charge for credit risk. Non-performing loans for the Group stood at US$ 70.5 million as at 31 December 2016 (2015: US$ 80.9 million) against which a provision of US$ 43.5 million exists as at 31 December 2016 (2015: US$ 44.2 million).

The Bank has established overall credit limits at the level of individual borrowers and counterparties, as well as groups of connected or comparable counterparties. These are aggregated in a meaningful manner to indicate different types of exposures in the banking and trading book, and on and off the balance sheet. The credit limits recognise and reflect the risks associated with the near term liquidation of positions in the event of counterparty default. Limits also factor in any unsecured exposure in a liquidation scenario. All extensions of credit are made on an arm's length basis. Any credit extended to companies and individuals that are outside the approved policy parameters are avoided, or are authorised on an exception basis by the appropriate authorities. A detailed review of connected party exposure is conducted on a monthly basis and reported to Central Bank of Bahrain.

Detailed information on the Bank's credit risk exposures, including geographical distribution, industry and sector allocation, details of the collaterals and other credit enhancements, and bifurcation based on internal ratings, is provided in Note 30(b) of the Consolidated Financial Statements.

Market Risk

Market risk is defined as the risk of losses in the value of on- or off-balance sheet financial instruments caused by a change in market prices or rates (including changes in interest rates and foreign exchange rates). UGB's policy guidelines for market risk have been vetted by the Board of Directors in accordance with the rules and guidelines provided by the Central Bank of Bahrain.

UGB has adopted the Standardized Approach for the measurement of its market risk. This involves a 'building block' methodology that aggregates charges for interest rate exposure, equities, foreign exchange, commodities and options. The Bank has entered into forward contracts and interest rate swaps for hedging purposes, and does not trade in commodities or derivatives. Consequently, UGB's market risk capital adequacy requirements cover the securities trading book and the foreign exchange book.

The minimum capital charge for interest rate exposure is expressed as the sum of the specific and general market risk of each position. For the general market risk capital charge, the Bank applies the maturity method with its respective rules. Information on the interest rate sensitivity in the Bank's asset and liability structure is detailed in Note 30(c) of the Consolidated Financial Statements.

The capital charge for equities held in the Bank's trading book is also an aggregate of 'specific risk' of holding a long or short position in an individual equity; and the 'general market risk' of holding that position in the market as a whole. In case of foreign exchange risk, the open currency position is taken both in the banking and the trading book. The sensitivity towards currency movements on the Bank's equity is detailed in Note 30 (c) of the Consolidated Financial Statements.

The Bank seeks to manage the market risks that it faces through diversification of exposures across dissimilar markets, industries and products. In addition to the exercise of business judgement and management experience, UGB utilises limit structures related to positions, portfolios, maturities and maximum allowable losses, to control the extent of such risk.

Interest Rate Risk in the Banking Book

Interest rate risk in the banking book arises as a result of mismatches in the re-pricing or maturity of interest rate sensitive financial assets and liabilities. This is also known as re-pricing risk. Additionally, UGB is exposed to minimal basis risk which results from a change in the relationship between the yields/yield curves of long and short positions with the same maturity in different financial instruments. In effect, this means that the long and short positions no longer fully hedge each other.

The Bank clearly identifies the sources of interest rate risk, and the interest rate risk-sensitive products and activities. It proactively measures and monitors the interest rate risk in the banking book. UGB also periodically carries out stress tests to assess the effect of extreme movements in interest rates that could expose the Bank to high risks. A conscious effort is also made to match the amount of floating rate assets with floating rate liabilities in the banking book. All new products and transactions are evaluated with respect to their inherent interest rate risk, and the identification of mitigating factors. UGB also enters into certain transactions in order to hedge exposures arising from day-to-day banking and investment activities. These hedge transactions include instruments such as interest rate swaps (IRS) and floating rate notes (FRN), to convert a floating rate asset/liability into a fixed rate one or vice-versa. The Bank continuously monitors the effectiveness of the hedges.

Risk Management Review
(continued)

Operational Risk

Operational risk is defined as the risk of losses arising from a failure in UGB's internal processes due to inadequate internal controls and procedures, human error, deliberate acts and/or business interruptions caused by technology, systems or external disasters beyond the Bank's control.

In accordance with Basel guidelines, UGB has developed a comprehensive operational risk framework, whereby all activities and processes of the Bank are analysed and residual risks are identified, measured and reported as appropriate.

Internal control systems have been introduced that are based on the tenet of adequate segregation of duties. Exception and excess exposure reporting by the Credit and Risk Management Department, succession planning and business continuity planning, reliable management reporting, and supervision of the Internal Audit and Quality Assurance Department and the Board Audit Committee, is also adhered to by the Bank. Anti-money laundering procedures and controls are also in place to mitigate any possible misuse of the Bank's services. These are reviewed by the external auditors on a yearly basis, and their report is forwarded to the Central Bank of Bahrain as mandated by local regulations.

The management of operational risk in the Bank is the responsibility of every employee. The operational risk framework is built around a detailed Risk Control Self-Assessment (RCSA) that identifies all risks stemming from activities of each department of the Bank. The probability of occurrence and potential severity of the risks are assessed; existing controls against each probable risk event are plotted and reviewed in terms of their effectiveness; residual risks after taking into account the effectiveness of controls are documented; and action plans are developed to reduce or mitigate the residual risks. The results of the RCSA are periodically reviewed by the Risk and Compliance Committee. Heat maps are produced to alert Senior Management to areas that may be subject to an increased level of operational risk.

In line with CBB guidelines, UGB uses the Basic Indicator Approach (BIA) to calculate the capital charge for operational risk. This is prescribed as 15% of the average annual gross income of the current year and the preceding two years. The detailed working for the capital charge on operational risk is provided in the Prudential Disclosures related to Basel III - Pillar III, which are posted on the Bank's website at: www.ugbbh.com.

UGB has enhanced its Operational Risk framework by implementing a fully automated Operational Risk System. The system comprises four key modules: loss database, risk and control self-assessment, key risk indicators, and exposure monitoring. This enables the Bank to monitor, mitigate and report its operational risk exposures in a structured and robust manner on a real-time basis.

Liquidity Risk and Funding

Liquidity risk stems from the inability to procure sufficient cash flow to meet UGB's financial obligations as and when they fall due. The risk arises due to the timing differences between the maturity profile of the Bank's assets and liabilities. In order to ensure that the Bank can meet its financial obligations as they fall due, the tenors of UGB's assets and liabilities are closely monitored across different maturity time bands.

The Asset and Liability Committee evaluates the balance sheet from a structural, liquidity and sensitivity point of view. The whole process is aimed at ensuring availability of sufficient liquidity to fund the Bank's ongoing business activities; effectively managing maturity mismatches between assets and liabilities; managing market sensitivities; and ensuring the Bank's ability to fund its obligations as they fall due. Daily and weekly reports are generated, which monitor deposits by counterparties to ensure maintenance of a diversified funding base in terms of individual depositors, their ratings, geographical concentration and maturities.

A diversified funding base has evolved around the deposits raised from the interbank market, Sharia-compliant market deposits received from customers, and medium term funds raised through syndicated borrowings. Access to available but uncommitted short term funding from the Bank's established relationships, internationally and across the MENA region, provides additional comfort. As at year end 2016, UGB's solo liquidity ratio was 35% (2015: 47%).The Bank monitors this on a daily basis to ensure that the regulatory threshold of 25% is maintained at all times.

Liquidity risk is minimised by actively managing mismatches, and through diversification of assets and liabilities. The Bank uses a combination of maturity gap limits and liquidity ratio limits to ensure that liquidity risk is managed and controlled from the asset and liability perspective:

- Maturity gap limits: Assets and liabilities in the Bank's balance sheet are grouped in specific maturity time buckets. The maximum liquidity mismatch between assets and liabilities in each defined time bucket (e.g. one to seven days, eight days to one month, one to three months, three to six months, six to twelve months, one to three years, three to five years, and more than five years), is controlled by gap limits that have been set for each time bucket. The Risk Management team tracks these limits.
- Liquidity ratio limits: UGB has limits on a set of ratios which it uses proactively for monitoring liquidity risk. These include the current ratio, liquid assets as a percentage of total assets, liquid assets as a percentage of total liabilities, and short term liabilities as a percentage of total liabilities.

Information on the liquidity risk and maturity profile of UGB's asset and liability structure as at the end of 2016 is detailed in Note 30(d) of the Consolidated Financial Statements. As of this date, 60% of total assets and 86% of total liabilities were contracted to mature within one year (2015: 54% and 67% respectively). A significant portion of assets with longer-term maturities comprise readily realisable securities or listed assets with active markets.

Concentration Risk

Concentration of exposures in credit portfolios is an important aspect of credit risk that is monitored separately in UGB. This risk can be considered from either a micro (idiosyncratic) or a macro (systemic) perspective. The first type – name concentration – relates to imperfect diversification of risk in the portfolio, either because of its small size or because of large exposures to specific individual obligors/investments. The second type – sector concentration – relates to imperfect diversification across systemic components of risk, namely industry sectoral factors.

Concentration risk is captured in UGB's framework through the use of internal and external regulations that cap the maximum exposure to any single obligor/investment. There are established limits in place that set thresholds for aggregate industry, geography, and counterparty. The actual levels of exposure are monitored against approved limits and regularly reviewed by Senior Management and the Board of Directors.

The Bank pursues a set of internal policies and limits that ascertain to a large extent, that no defined exposure limits referred to in its various policies are exceeded. If any potential exposure is deemed to result in breach of regulatory and/or internal limits, the Bank obtains due approvals from the appropriate authority (Central Bank of Bahrain and/or the Bank's relevant approving authority) before executing the respective business transaction.

Legal Risk

Legal risk is defined as the loss that may arise as a result of the inability to enforce contracts and agreements entered into, the failure of these to adequately cover the risks, and liabilities the Bank may face, and their inability to protect the Bank's interests. In order to mitigate legal risk, UGB uses industry standard master agreements wherever available. Expert legal advice is sought on all legal structures and arrangements to which the Bank is a party. A retainer agreement is maintained with a Bahrain law firm for the review of standard business agreements. The advice of local and international law firms is sought for documentation related to special assignments. Proper execution and completion of all legal contracts is ensured prior to committing funds to the transactions. All legal documents are reviewed on a periodic basis to ensure their ongoing enforceability, and are maintained under dual custody.

BASEL III

The Central Bank of Bahrain issued detailed Basel III regulations with respect to capital adequacy calculations which became effective from 1 January 2015. In line with Basel Committee guidelines, CBB allows a transition period of up to 2018 for full implementation. During 2016, several meetings were held with the CBB in which UGB submitted its study on how best to optimise its capital.

MONITORING AND REPORTING

The monitoring and reporting of risk is conducted on a daily basis for market and liquidity risk, on a monthly basis for credit risk, and on a quarterly basis for operational risk. The regular forums in which risk related issues are highlighted and discussed are Management meetings, Risk and Compliance Committee meetings, and Executive Committee meetings. The Board of Directors is also regularly apprised of pertinent risk issues, including the semi-annual investment reviews and any proposed corrective actions.

INTERNAL CAPITAL ADEQUACY ASSESSMENT PROCESS

The Internal Capital Adequacy Assessment Process (ICAAP) is a requirement of the Pillar II norms of Basel III, and involves appropriate identification and measurement of risks, and maintenance of an appropriate level of internal capital in alignment with the Bank's overall risk profile and business plan. The objective of the Bank's ICAAP is to ensure that adequate capital is retained at all times to support the risks that UGB undertakes in the course of its business.

The Bank recognises that its earnings are the first line of defence against losses arising from business risks, and that capital is one of the tools to address such risks. Also important, are establishing and implementing documented procedures; defining and monitoring internal limits on the Bank's activities/exposures; strong risk management, compliance and internal control processes; as well as adequate provisions for credit, market and operational losses. However, since capital is vital to ensure continued solvency, the Bank's objective is to maintain sufficient capital such that a buffer above regulatory capital adequacy requirement is available to meet risks arising from fluctuations in asset values, revenue streams, business cycles, and expansion and future requirements. UGB's ICAAP identifies risks that are material to the Bank's business, and the capital that is required to be set aside for such risks.

The Bank seeks to achieve the following goals by implementing an effective capital management framework:

- Meet the regulatory capital adequacy requirement and maintain a prudent buffer.
- Generate sufficient capital to support the overall business strategy.
- Integrate capital allocation decisions with the strategic and financial planning process.
- Enhance Board and Senior Management's ability to understand how much capital flexibility exists to support the overall business strategy.
- Improve the Bank's understanding on capital requirements under different economic and stress scenarios.
- Build and support the link between risks and capital and tie performance to both of them.

CAPITAL SOURCES

UGB's capital is primarily derived from common shareholders' equity and retained earnings. Other sources of capital include additional tier 1 capital and subordinated long term debt.

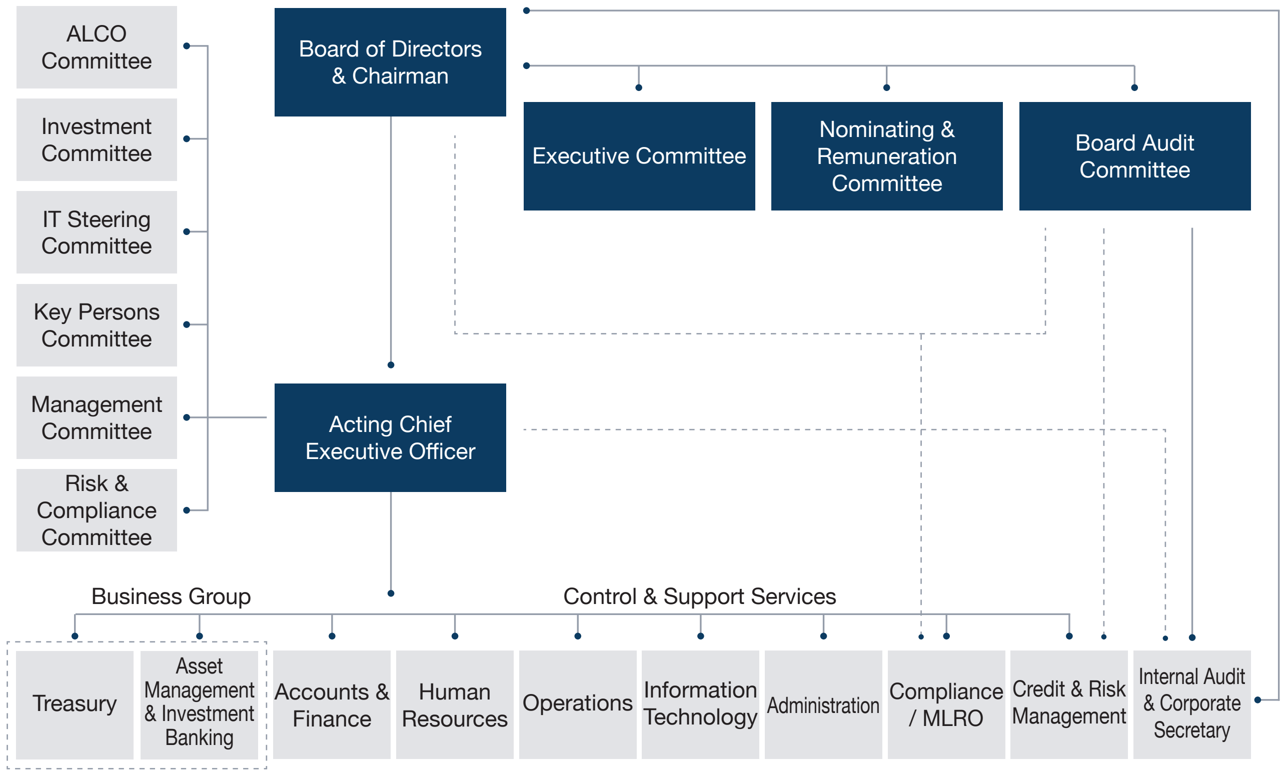
CAPITAL MANAGEMENT

The Board of Directors of the Bank is responsible for ensuring that adequate levels of capital are maintained at all times. The Board also approves and oversees the processes adopted for capital management by the Bank.

UGB has a well-established risk governance structure, with an active and engaged Board of Directors supported by an experienced senior management team, and a support services group that is independent of the business lines. Decision making is highly centralised through a number of Board and executive committees. The corporate governance framework of the Bank is a reflection of its culture, policies, stakeholder relationships, and commitment to corporate values. The Board of Directors believes that sound ethical practices, transparency of operations, and timely disclosures are critical factors in enhancing shareholder value and safeguarding the interests of all stakeholders.

UGB is committed to adopting the highest standards of corporate governance in line with global best practice.

GOVERNANCE AND ORGANISATION STRUCTURE



KEY DEVELOPMENTS IN 2016

Throughout the year, UGB continued to take steps to ensure compliance with the Higher Level Controls Module of the Rulebook of the Central Bank of Bahrain (CBB), regulations of the Bahrain Bourse, requirements of the Commercial Companies Law, and the principles of the Code of Corporate Governance of the Kingdom of Bahrain (the Code). The main activities conducted in 2016 comprised:

- Internal policies and procedures were reviewed to ensure that they are up to date.
- The Share Registry was transferred from UGB to the Central Securities Registry System of the Bahrain Bourse (dematerialized shares), in line with Resolution No. (5) of 2015 in Respect of Amending the Listing Requirements of Shareholding Companies on the Bahrain Bourse Main Board.

- In anticipation of a more intensive regulatory landscape in 2017, UGB reviewed the relevant background information to prepare for:
  - Automatic Exchange of Information (AEOI), also known as Common Reporting Standards (CRS), launched by the Organization for Economic Cooperation and Development (OECD) to which Bahrain has committed.
  - Signing by Bahrain of the GCC Accord on Value Added Tax (VAT) regulations which are expected to be introduced in mid 2018.

COMPLIANCE

In accordance with CBB requirements, UGB has a designated Chief Compliance Officer (CCO) with a dotted reporting line to the Board Audit Committee. The CCO acts as the central coordinator for all matters relating to regulatory reporting and other requirements. A framework of relevant policies and processes covering the areas of adherence to external regulations, code of conduct and conflicts of interest, are encapsulated in the Bank's Compliance Charter, Corporate Governance Guidelines and Code of Conduct. These documents have been approved by the Board of Directors, and help define, clarify, assert and enforce the role of governance within UGB.

A Compliance Report for UGB and its main operating subsidiaries, is presented every quarter by the CCO to members of the Board Audit Committee, and the Risk and Compliance Committee. Forthcoming deadlines, as well as feedback on ongoing consultations, are highlighted at quarterly Risk and Compliance Committee meetings. The Compliance function is also responsible for ensuring that all ad hoc requests for information from regulatory authorities are responded to immediately, and that corrective action is taken if required.

UGB shares a strong rapport with its local regulators – the Central Bank of Bahrain, the Bahrain Bourse, and the Ministry of Industry, Commerce and Tourism. There is proactive dialogue as and when warranted. In addition, the CBB conducts an annual Prudential Meeting with Senior Management of UGB in the presence of a Board Director. This forum involves the regulators receiving an overview of the Bank's performance; business model and strategic plan; market outlook; corporate governance and risk management; and capital adequacy framework.

During the year, UGB responded to a number of Consultation Papers issued by the CBB and the Bahrain Bourse. These included the proposed Trust Law; proposed changes to Sound Remuneration Practices; proposed Unified GCC Law of Commerce; proposed Amendments to the Offering of the Securities Module (Module OFS) of the CBB Rule Book Volume 6; and proposed amendments to the Higher Level Controls Module (Module HC) of the CBB Rule Book Volume 1.

ANTI-MONEY LAUNDERING

UGB has a designated Money Laundering Reporting Officer (MLRO) and a Deputy MLRO (DMLRO) who have been appointed following approval received from the CBB. The position of MLRO has been combined with that of the CCO. The Bank has implemented an anti-money laundering (AML) and counter terrorism financing (CFT) policy, which is reviewed on an annual basis and approved by the Board. UGB uses case studies to train staff every year to raise awareness of identifying and reporting suspicious transactions. Employees receive an overview of the Bank's AML/CFT policy and procedures, and training slides; these are also available on the Intranet. UGB follows prudent practices related to Customer Due Diligence and Beneficial Ownership using the Thomson Reuters screening tool, and Know Your Customer (KYC) principles. In accordance with regulatory requirements, the MLRO reviews the effectiveness of the AML/CFT procedures, systems and controls at least once a year. The Bank's anti-money laundering measures are reviewed annually by the independent external auditors for UGB and its main subsidiaries. Their separate assurance reports are submitted to the Compliance Directorate of the CBB.

CODE OF CONDUCT

The Board of Directors has established corporate standards for all Directors and employees. These are emphasised in the Bank's Code of Conduct which reiterates the need to uphold sensitive and confidential information; avoiding and disclosing (wherever applicable) conflicts of interest; personal accountability; honesty; harmonious relationships with clients, subsidiaries, affiliates and regulators; non-solicitation of gifts; transparent and accurate external communications; expected standards of professionalism, fairness, behaviour and language; and accurate accounting, auditing and bookkeeping.

The Board and Senior Management view the Code of Conduct as an integral part of the way they exercise their responsibilities; and how they conduct themselves with clients, shareholders, staff, and the wider community. Familiarisation sessions on the requirements of the Code of Conduct are conducted on annual basis by the Chief Compliance Officer. Board members and staff submit a written affirmation that they will abide by the tenets of the Code, and disclose any personal conflicts of interest. Any incidents of non-compliance with the Code, or lack of affirmation by any member of UGB, is escalated to the Board Audit Committee and the Board of Directors. The Code of Conduct is available on the Bank's website: www.ugbbh.com.

Corporate Governance Review
(continued)

TRANSPARENCY AND DISCLOSURE

UGB is transparent and open with its regulators, shareholders, lenders and other stakeholders. The Board of Directors has approved a Disclosure and Transparency Policy which lays down the set of disclosure standards for the Bank. The objective of this policy is to facilitate understanding and compliance with the disclosure and transparency requirements for all material and non-material information with regard to the affairs of UGB. Adequate consideration is given to regulatory requirements to which the Bank is subject. The policy was also introduced to monitor the transparency adopted, and to enhance the Bank's image through accurate and timely disclosure of information.

As part of its communications strategy, UGB's website (www.ugbbh.com) is the repository of financial information together with financial statements, relevant information on the Group/Bank, key products and services, and press releases that are issued periodically to the media. As mandated by the CBB, the detailed risk management and capital adequacy calculations that relate to Basel III have also been uploaded under 'Investor Relations'. The Bank's Corporate Governance Report as well as incorporation documents are also available on the website. UGB's website was redesigned in 2016 to enhance user-friendliness and security, and make it more easily accessible from different browsers and mobile devices.

INTERNAL AUDIT & QUALITY ASSURANCE

The independent Internal Audit department of UGB reports directly to the Board Audit Committee, and administratively to the Chief Executive Officer. Staffed by experienced and qualified professionals, the department is governed by a detailed Board approved Audit Charter. Details of its responsibilities are documented in a Board approved Policies & Procedures Manual in line with internal audit international best practice. Internal Audit has a close and direct working relationship with UGB's Executive Management and Committee, in addition to having unrestricted access to information, records, systems and personnel within the Bank.

Internal Audit carries out its responsibilities in line with a risk-based three year strategic Audit Plan. This is designed to implement a systematic, disciplined audit review approach by utilising the available audit resources in the most efficient and effective manner. It examines the adequacy and effectiveness of processes, systems and procedures within the internal controls framework – comprising Compliance, Corporate Governance, Risk Management, IT Security, Financial Control and AML amongst others – and provides recommendations in order to enhance and strengthen their reliability. On a periodic basis, the department performs follow-ups on internal control recommendations and corrective actions that have been raised, and reports their updated status to the Board Audit Committee. The department also oversees the implementation of sound governance and internal control principles and practices at the level of UGB's subsidiaries and associate companies; and provides regular support to their respective Board Audit Committees and Internal Audit functions.

The Quality Assurance function adopts a consultative role in working with head office departments, and subsidiaries and associate companies, to facilitate continuous process improvements and review new initiatives. These include regular reviews of updates to the Bank's policies and procedures, organisation chart and job descriptions; and assessing the impact of new regulations. In addition, Quality Assurance conducts ad hoc special assignments at the request of the Board and Management to ensure continuous improvement.

Corporate Social Responsibility

The Bank has long been active in a wide range of socially responsible activities including corporate philanthropy, employee involvement, and long term strategic programmes in education. This is in line with its commitment to promote thought leadership within the industry, empower students through education and training, and contribute to the social well-being and economic prosperity of the Kingdom of Bahrain.

During 2016, UGB continued to implement its corporate social responsibility programme with a special emphasis on education and career development for young Bahrainis; development of the regional banking sector; women's empowerment; and charitable and community-based activities.

EDUCATION AND CAREER DEVELOPMENT FOR YOUNG BAHRAINIS

UGB supports the philosophy that education is the best source of empowerment. The Bank provides education and career development opportunities for young Bahraini students through the following activities:

- **The Crown Prince's International Scholarship Program (CPISP)**

An annual Silver Sponsor of this major educational initiative since its inception in 2006, UGB became a Friends Sponsor in 2012, which carried a five-year commitment of US$ 50,000. In 2016, the Bank renewed its Friends Sponsorship for a further five-year term.

- **University of Bahrain Student Internships**

UGB is a founding member of this programme, which provides selected students with summer work experience and the opportunity of placement.

- **TradeQuest – The Trading Challenge**

TradeQuest is a business-education partnership that was established 19 years ago. Conducted under the aegis of the Bahrain Bourse, it provides school students with an opportunity to participate in a simulated interschool trading competition by investing in shares listed on the New York Stock Exchange, NASDAQ and the Bahrain Bourse. UGB has supported this prestigious competition for the past 15 years by sponsoring one of the participating schools. The Chief Compliance Officer is actively involved in working with the students, and guiding them through the elements of investing and risk management. The UGB supported TradeQuest school team, won the third place in the 2016-2017 competition.

In addition, the Bank's Mashare' Al Khair Scholarship Programme assists qualified UGB employees' dependants to study at accredited colleges, universities or other recognised academic institutions. The Bank also extends financial support to its staff to constantly enhance their academic and professional qualifications and fulfill their continuing professional development (CPD) commitments.

UGB has an enduring responsibility to support the well being of communities in which it operates.

DEVELOPMENT OF THE REGIONAL BANKING SECTOR

UGB contributes to the growth and development of the regional banking and financial services sector in a number of different ways:

- The Bank supports a wide range of banking-related organisations including the Bahrain Association of Banks, Union of Arab Banks, Bahrain Institute of Banking and Finance (BIBF), and International Islamic Financial Market of Bahrain.
- UGB staff are members of professional institutions and associations.
- The Bank supports the CFA Society Bahrain in promoting and maintaining the highest standards of professional excellence and integrity in the financial and investment community.
- UGB staff are invited to speak at industry seminars, think tanks and conferences.

WOMEN'S EMPOWERMENT

UGB continues to support joint initiatives by the Central Bank of Bahrain and the Supreme Council for Women to promote the role of women in Bahrain's financial and banking sector. The Bank supports the mentoring of young talented women in Bahrain's financial sector through the participation of a member of staff in the CBB - BIBF Mentoring Programme. The main objective of this programme is to inspire young students, and raise their awareness of different career options in Bahrain's financial industry, through the exchange of knowledge and expertise with assigned mentors.

CHARITABLE AND COMMUNITY-BASED ACTIVITIES

Over the years, UGB has provided financial assistance for numerous charitable, cultural, social, medical, educational and child welfare organisations that work with orphans, needy families, and the underprivileged sections of society. In 2016, contributions were also made to entities that are committed to protecting the environment and raising awareness about women's cancer.

Independent Auditors' Report To The Shareholders of United Gulf Bank B.S.C.

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Opinion
We have audited the consolidated financial statements of United Gulf Bank B.S.C. ("the Bank") and its subsidiaries (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2016, and the consolidated statements of income, comprehensive income, changes in equity and cash flows and for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2016 and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (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.

Key audit matters
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements for the year ended 31 December 2016. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

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

1. *Impairment of loans and advances*

   Key audit matter

   The management exercise significant judgement using subjective assumptions over both the timing of recognition of impairment, and estimation of the amount of the impairment provision for loans and advances. Because loans and advances form a major portion of the Group's assets, and due to the significance of judgment used in estimating both the specific and collective provisions for loans and advances, this audit area is considered a key audit risk.

   As at 31 December 2016, the gross loans and advances amounted to USD 1,228 million and related loan loss impairment provision amounted to USD 29 million and collective impairment provision of USD 15 million. The impairment provision policy is presented in the accounting policies in note 2 to the consolidated financial statements.

   How the key audit matter was addressed in the audit

   "Our audit procedures included the assessment of controls over the authorization, granting and booking of loans and advances to confirm the operating effectiveness of the key controls in place for the credit processes.

   We tested a sample of loan facilities, and assessed the criteria for determining whether an impairment event had occurred, focusing on new real estate lending, which present different risks than those ordinarily faced by the Group with trade finance or factoring business. Additionally, we selected samples of performing loans and assessed whether the borrowers exhibit any possible default risk that may affect the repayment abilities. The assessment included review of the facilities maturity dates to identify any past due exposures, discussions with the clients, review of the applicable external credit ratings and review of available external information.

   For selected non-performing loans, we assessed management's forecast of recoverable cash flows, quality of collateral held, performance of the borrower and receipts after the financial reporting date.

   For the collective impairment provision, we obtained an understanding of the methodology used by the Group to determine the collective impairment provisions, assessed the reasonableness of the underlying assumptions and the sufficiency of the data used by the management.

   We also assessed whether the consolidated financial statements disclosures appropriately reflect the Group's exposure to credit risk.

   Refer to the critical accounting estimates and judgements and disclosures of loans and advances in Note 2 and 7 to the consolidated financial statements."

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

2. *Goodwill impairment*

   Key audit matter

   Goodwill impairment testing of cash generating units ('CGUs') relies on estimates of value-in use based on estimated future cash flows. Due to the uncertainty of forecasting and discounting future cash flows and the significance of the Group's recognised goodwill of USD 52 million as at 31 December 2016, this audit area is considered a key audit risk.

   The basis of the goodwill impairment policy is presented in the accounting policies in Note 2 to the consolidated financial statements.

   How the key audit matter was addressed in the audit

   Our audit procedures included the assessment of reasonableness of cash flow projections and comparison of key inputs, such as the discount rates and growth rates, to externally available industry, economic and financial data and the Group's own historical data and performance. With the assistance of our own specialists, we assessed the assumptions and methodologies used to forecast value-in-use for those CGUs.

   Additionally, we considered whether the Group's disclosures of the application of judgement in estimating CGU cash flows and the sensitivity of the results of those estimates adequately reflect the risks associated with goodwill impairment.

   Refer to the critical accounting estimates and judgements and disclosures of goodwill in Note 2 and 11 to the consolidated financial statements.

3. *Impairment testing of investments in associates*

   Key audit matter

   The determination of recoverable amounts of the Group's investments in associates relies on management's estimates of future cash flows and their judgment with respect to the associates' performance. Due to the uncertainty of forecasting and discounting future cash flows, the level of management's judgement involved and the significance of the Group's investment in associates of USD 709 million as at 31 December 2016, this audit area is considered a key audit risk.

   The basis of impairment of investment in associates is presented in the accounting policies in Note 2 to the consolidated financial statements.

   How the key audit matter was addressed in the audit

   Our audit procedures included the assessment of forecasts of future cash flows prepared by the management, evaluating the assumptions and comparing the estimates to externally available industry, economic and financial data. With the assistance of our own specialists, we assessed the assumptions and methodologies used by the management to determine the recoverable amount of the investment in associates.

   Additionally, our audit procedures included comparison of the carrying values of the Group's investment in associates for which audited financial statements were available with their respective net asset values and discussions with management of the associates' performance and their outlook.

   Refer to the critical accounting estimates and judgements and discloures of investment in associates in Note 2 and 9 to the consolidated financial statements.

Other information included in the Group's 2016 annual report
Other information consists of the information included in the Group's 2016 Annual Report, other than the consolidated financial statements and our auditor's report thereon. The Board of Directors is responsible for the other information. Prior to the date of this 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.

Independent Auditors' Report To The Shareholders of United Gulf Bank B.S.C.

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.

- 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.

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

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

Independent Auditors' Report To The Shareholders of United Gulf Bank B.S.C.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

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

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

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, regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2016 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position; and

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

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

Ernst & Young

Partner's registration no. 121
28 February 2017
Manama, Kingdom of Bahrain

Consolidated Statement of Financial Position

At 31 December 2016

	Note	2016 US$ 000	2015 US$ 000
ASSETS			
Demand and call deposits with banks		176,880	176,793
Placements with banks		187,350	57,026
Investments carried at fair value through statement of income	5	45,178	50,661
Non-trading investments	6	404,436	285,003
Loans and receivables	7	1,184,804	1,032,098
Other assets	8	112,735	119,686
Investments in associates	9	709,043	853,984
Investment properties	10	101,326	46,222
Property and equipment		32,117	41,694
Goodwill	11	51,868	52,321
Assets of disposal group classified as held for sale		-	1,028
TOTAL ASSETS		3,005,737	2,716,516
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks and other financial institutions		726,222	838,160
Deposits from customers		985,210	462,086
Loans payable	13	652,125	714,568
Subordinated debt	14	50,000	143,270
Other liabilities	15	62,724	54,999
Liabilities of disposal group classified as held for sale		-	166
TOTAL LIABILITIES		2,476,281	2,213,249
EQUITY			
Share capital	16	208,651	208,651
Treasury shares	16	(18,131)	(18,131)
Share premium	16	11,459	11,459
Statutory reserve	16	100,514	99,888
General reserve	16	80,999	80,373
Treasury shares reserve	16	14,248	14,248
Fair value reserve	17	(49,966)	(48,159)
Foreign currency translation reserve	16	(37,476)	(34,890)
Retained earnings		83,711	80,497
CAPITAL AND RESERVES ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT		394,009	393,936
Perpetual Tier 1 capital	18	33,000	-
Non-controlling interests in equity		102,447	109,331
TOTAL EQUITY		529,456	503,267
TOTAL LIABILITIES AND EQUITY		3,005,737	2,716,516

Masaud Hayat
Chairman

Faisal Al Ayyar
Vice Chairman

Hussain Lalani
Acting Chief Executive Officer

The attached notes 1 to 33 form part of these consolidated financial statements

Consolidated Statement of Income

For the year ended 31 December 2016

	Note	2016 US$ 000	2015 US$ 000
Continuing operations			
Interest income	19	48,503	56,348
Investment income - net	20	19,709	7,662
		68,212	64,010
Fees and commissions - net	21	34,484	31,713
Foreign currency (losses) gains - net		(5,751)	3,257
Share of results of associates - net	22	41,080	45,850
Total income		138,025	144,830
Interest expense	23	(52,932)	(51,574)
Operating income before expenses and provisions		85,093	93,256
Salaries and benefits		(48,540)	(49,540)
General and administrative expenses		(24,989)	(31,829)
Operating income before provisions and tax		11,564	11,887
Impairment loss on investments	6,9	(2,933)	(3,153)
Provision for doubtful loans and advances - net	7	(8,255)	(9,617)
Taxation - net	12	577	6,637
Net profit for the year from continuing operations		953	5,754
Discontinued operations			
Net loss from discontinued operations		(80)	(2,554)
Net profit for the year		873	3,200
Net loss attributable to non-controlling interests		(5,386)	(8,019)
NET PROFIT ATTRIBUTABLE TO SHAREHOLDERS OF THE PARENT		6,259	11,219
Net (loss) profit attributable to:			
Non-controlling interests			
- from continuing operations		(5,355)	(7,028)
- from discontinued operations		(31)	(991)
		(5,386)	(8,019)
Shareholders of the parent			
- from continuing operations		6,308	12,782
- from discontinued operations		(49)	(1,563)
		6,259	11,219
Earnings per share			
Basic and diluted earnings per share attributable to shareholders of the parent (US cents)	24	0.77	1.38
Basic and diluted earnings per share from continuing operations attributable to shareholders of the parent (US cents)	24	0.77	1.57

Masaud Hayat
Chairman

Faisal Al Ayyar
Vice Chairman

Hussain Lalani
Acting Chief Executive Officer

The attached explanatory notes 1 to 33 form part of these consolidated financial statements

Consolidated Statement of Comprehensive Income

For the year ended 31 December 2016

	2016 US$ 000	2015 US$ 000
NET PROFIT FOR THE YEAR	873	3,200
Other comprehensive (loss) income to be reclassified to profit or loss in subsequent years:		
Foreign currency translation reserve	(2,806)	(25,374)
Fair value reserve	6,062	(4,046)
Transfer to consolidated statement of income upon disposal	2,681	(19,628)
Share of other comprehensive loss of associates - net	(11,690)	(32,497)
Cash flow hedges	655	279
Other comprehensive loss to be reclassified to profit or loss in subsequent years	(5,098)	(81,266)
TOTAL COMPREHENSIVE LOSS	(4,225)	(78,066)
Total comprehensive income (loss) attributable to:		
- shareholders of the parent	1,866	(68,966)
- non-controlling interests	(6,091)	(9,100)
	(4,225)	(78,066)

The attached notes 1 to 33 form part of these consolidated financial statements

Consolidated Statement of Cash Flows

For the year ended 31 December 2016

	Note	2016 US$ 000	2015 US$ 000
OPERATING ACTIVITIES			
Net profit for the year		873	3,200
Adjustments for non-cash items:			
Depreciation		5,309	3,996
Share of results of associates - net	22	(41,080)	(45,850)
Gain on sale of an associate and subsidiaries	20	(2,824)	(2,631)
Impairment loss on investments	6,9	2,933	3,153
Provisions for doubtful loans - net	7	8,255	9,617
Interest income	19	(48,503)	(56,348)
Interest expense	23	52,932	51,574
Dividend income	20	(7,230)	(5,104)
Other non-cash items	11	453	2,188
Gain on bargain purchase	20	-	(2,040)
Loss on investments carried at fair value through statement of income	20	229	4,963
Operating loss before changes in operating assets and liabilities		(28,653)	(33,282)
Changes in operating assets and liabilities:			
Placements with banks with original maturities of more than ninety days		5,699	(4,607)
Investments carried at fair value through statement of income		5,254	1,439
Non-trading investments		(17,056)	(90,075)
Loans and receivables		(161,130)	(51,551)
Other assets		10,138	2,656
Due to banks and other financial institutions		(111,938)	125,545
Deposits from customers		523,124	(86,331)
Other liabilities		5,107	(17,231)
Net assets of disposal group classified as held for sale		862	6,782
Interest received		46,140	55,370
Interest paid		(49,894)	(50,362)
Dividends received	20	7,230	5,104
Donations		(200)	(200)
Directors' remuneration		(220)	(220)
Net cash from (used in) operating activities		234,463	(136,963)
INVESTING ACTIVITIES			
Investment in subsidiaries - net of cash acquired		-	(10,661)
Investments in associates - net		25,073	23,838
Investment properties - net		896	(14,948)
Property and equipment - net		4,268	(5,764)
Net cash from (used in) investing activities		30,237	(7,535)
FINANCING ACTIVITIES			
Repayment of loans		(62,443)	(78,339)
Issue of perpetual Tier 1 capital		33,000	-
Interest payment on Tier 1 capital securities		(1,793)	-
Subordinated debt		(93,270)	50,000
Net cash used in financing activities		(124,506)	(28,339)
Foreign currency translation adjustments		(2,586)	(24,487)
Movement in non-controlling interests		(1,498)	(135)
NET CHANGE IN CASH AND CASH EQUIVALENTS		136,110	(197,459)
Cash and cash equivalents at 1 January		220,957	418,416
CASH AND CASH EQUIVALENTS AT 31 DECEMBER	25	357,067	220,957

The attached notes 1 to 33 form part of these consolidated financial statements

Consolidated Statement of Changes In Equity

For the year ended 31 December 2016

	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 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
Balance at 1 January 2015	208,651	(18,131)	11,459	98,766	79,251	14,248	7,539	(10,403)	71,522	462,902	-	117,485	580,387
Profit (loss) for the year	-	-	-	-	-	-	-	-	11,219	11,219	-	(8,019)	3,200
Other comprehensive loss	-	-	-	-	-	-	(55,698)	(24,487)	-	(80,185)	-	(1,081)	(81,266)
Total comprehensive (loss) income for the year	-	-	-	-	-	-	(55,698)	(24,487)	11,219	(68,966)	-	(9,100)	(78,066)
Transfers during the year	-	-	-	1,122	1,122	-	-	-	(2,244)	-	-	-	-
Other movements in non-controlling interests	-	-	-	-	-	-	-	-	-	-	-	946	946
BALANCE AT 31 DECEMBER 2015	208,651	(18,131)	11,459	99,888	80,373	14,248	(48,159)	(34,890)	80,497	393,936	-	109,331	503,267

The attached notes 1 to 33 form part of these consolidated financial statements

Notes to the Consolidated Financial Statements

At 31 December 2016

1 INCORPORATION AND PRINCIPAL ACTIVITIES

Incorporation

United Gulf Bank B.S.C. (the "Bank") is a joint stock company incorporated in the Kingdom of Bahrain in 1980, under Commercial Registration number 10550 and listed on the Bahrain Bourse. 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 investment banking and commercial banking. Investment banking includes 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 and ultimate holding company is Kuwait Projects Company (Holding) K.S.C. (closed) ("KIPCO"), a company incorporated in the State of Kuwait and listed on the Kuwait Stock Exchange. As at 31 December 2016 KIPCO owned 97.77% of the Bank's outstanding shares (2015: 97.77%).

These consolidated financial statements were authorised for issue by the Board of Directors on 28 February 2017.

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), relevant CBB directives and regulations and associated resolutions, rules and procedures of the Bahrain Bourse.

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.

New and amended standards and interpretations

The accounting policies adopted are consistent with those of the previous financial year, except for the following new and amended IFRSs effective as of 1 January 2016:

Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation
The amendments clarify the principle in IAS 16 Property, Plant and Equipment and IAS 38 Intangible Assets that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is a part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets. The amendments are applied prospectively and do not have any impact on the Group, given that it has not used a revenue-based method to depreciate its non-current assets.

Annual Improvements 2012-2014 Cycle

These improvements include:

IFRS 5 Non-current Assets Held for Sale and Discontinued Operations
Assets (or disposal groups) are generally disposed of either through sale or distribution to the owners. The amendment clarifies that changing from one of these disposal methods to the other would not be considered a new plan of disposal, rather it is a continuation of the original plan. There is, therefore, no interruption of the application of the requirements in IFRS 5. This amendment is applied prospectively. This did not have any impact on the consolidated financial statements of the Group.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Annual Improvements 2012-2014 Cycle (continued)

IFRS 7 Financial Instruments: Disclosures
The amendment clarifies that a servicing contract that includes a fee can constitute continuing involvement in a financial asset. An entity must assess the nature of the fee and the arrangement against the guidance for continuing involvement in IFRS 7 in order to assess whether the disclosures are required. The assessment of which servicing contracts constitute continuing involvement must be done retrospectively. However, the required disclosures need not be provided for any period beginning before the annual period in which the entity first applies the amendments. This did not have any impact on the consolidated financial statements of the Group.

IAS 19 Employee Benefits
The amendment clarifies that market depth of high quality corporate bonds is assessed based on the currency in which the obligation is denominated, rather than the country where the obligation is located. When there is no deep market for high quality corporate bonds in that currency, government bond rates must be used. This amendment is applied prospectively. This did not have any impact on the consolidated financial statements of the Group.

Amendments to IAS 1 Disclosure Initiative
The amendments to IAS 1 clarify, rather than significantly change, existing IAS 1 requirements. The amendments clarify:

- The materiality requirements in IAS 1;
- That specific line items in the statement(s) of profit or loss and OCI and the statement of financial position may be disaggregated;
- That entities have flexibility as to the order in which they present the notes to financial statements; and
- That the share of OCI of associates and joint ventures accounted for using the equity method must be presented in aggregate as a single line item, and classified between those items that will or will not be subsequently reclassified to profit or loss.

Furthermore, the amendments clarify the requirements that apply when additional subtotals are presented in the statement of financial position and the statement(s) of profit or loss and OCI. These amendments do not have any impact on the Group.

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 2016. The reporting dates of the subsidiaries and the Bank are identical and the subsidiaries' accounting policies conform to those used by the Bank for like transactions and events in similar circumstances.

Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Specifically, the Group controls an investee if and only if the Group has:

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

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

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

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation (continued)

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation (continued)

The principal subsidiaries of the Bank are as follows:

Name of the subsidiary	Country of incorporation	Ownership at 31 December 2016	2015	Year of incorporation
Held directly				
FIMBank Group [FIMBank]	Malta	61%	61%	1994
KAMCO Investment Company K.S.C.P. [KAMCO]	Kuwait	86%	86%	1998
Hatoon Real Estate Company	Kuwait	98%	98%	2008
Syria Gulf Investment Company	Syria	99%	99%	2007
Takaud Saving & Pensions Company [Takaud]	Bahrain	-	50%	2011
United Gulf Financial Services Company-North Africa	Tunisia	85%	85%	2008
United Gulf Realty International, Ltd	British Virgin Islands	100%	100%	2012
Held through KAMCO				
Al Dhiyafa United Real Estate Company W.L.L.	Kuwait	100%	100%	2007
Al Jazi Money Market Fund	Kuwait	48%	-	2007
Al Zad Real Estate W.L.L.	Kuwait	99%	99%	2007
KAMCO Investment Company (DIFC) Limited	U.A.E.	100%	-	2016
Kamco GCC Opportunistic Fund	Kuwait	100%	87%	2013
Kuwait Private Equity Opportunity Fund	Kuwait	71%	71%	2004
North Africa Real Estate Co.	Kuwait	100%	100%	2014
Orange Real Estate Co. W.L.L.	Kuwait	100%	100%	2005
KAMCO Mena Plus Fixed Income Fund	Kuwait	51%	44%	2016
Held through FIMBank				
India Factoring and Finance Solutions Private Limited	India	86%	79%	2010
CIS Factors Holdings B.V.	Russia	100%	100%	2009
FIM Holdings (Chile) S.p.a.	Chile	100%	100%	2014
First Factors S.A.	Chile	51%	51%	2014
London Forfaiting Company Limited	U.K.	100%	100%	2009
London Forfaiting International Limited	U.K.	100%	100%	2009
London Forfaiting Americas Inc.	U.S.A.	100%	100%	2009
London Forfaiting do Brasil Ltd.	Brazil	100%	100%	2009
FIM Factors B.V.	Netherlands	100%	100%	2009
Menafactors Limited	U.A.E.	100%	100%	2009
FIM Business Solutions Limited	Malta	100%	100%	2009
FIM Property Investment Limited	Malta	100%	100%	2010
The Egyptian Company for Factoring	Egypt	100%	50%	2006

Notes to the Consolidated Financial Statements
At 31 December 2016

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Principles of consolidation (continued)

During the year, the Group's management decided not to participate in a proposed capital increase of Takaud, a 50% owned subsidiary of the Group, and gave up control of Takaud over to KIPCO, the other 50% owner of Takaud. Accordingly, Takaud has not been consolidated in these consolidated financial statements with effect from 1 October 2016. As control was lost before additional share capital was issued, no consideration was transferred and no gain or loss resulted from the loss of control.

During the year, the Bank acquired additional 50% equity interest in The Egyptian Company for Factoring S.A.E. ("Egypt Factors"), following which Egypt Factors has become a subsidiary of the Group. As of 31 December 2016, the Bank indirectly owns 100% (2015: 50%) of Egypt Factors through its subsidiary FIMBank.

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.

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 statement of profit or loss.

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 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 the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

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

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

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurement (continued)

For the purpose of fair value disclosures, the Group has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy as explained above.

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

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

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

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

- brokers' quotes
- recent arm's length market transactions
- the expected cash flows discounted at current rates applicable for items with similar terms and risk characteristics
- option pricing models
- other valuation methods (Note 31)

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Non-trading investments

These are classified as follows:

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

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 statement of comprehensive income until the investment is derecognised or determined to be impaired at which time the cumulative gains or losses previously reported in the consolidated statement of comprehensive income 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.

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 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 2016 and 2015 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 statement of comprehensive income. 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 other comprehensive income 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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Investment properties (continued)

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 statement of financial position and any gain or loss resulting from disposal is included in the consolidated statement of income.

Lease assets

Leases in terms of which the Group does not assume substantially all the risks and rewards of ownership are classified as operating leases.

Leased assets held under operating lease are not recognised in the Group's statement of financial position.

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease.

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.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

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.

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 statement of income – is removed from other comprehensive income 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 other comprehensive income.

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

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of financial assets (continued)

Investments available-for-sale (continued)
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.

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 other comprehensive income.

On disposal of a foreign operation, the component of other comprehensive income 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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Contingent liabilities and contingent assets

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

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

Financial guarantee contracts

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.

Segment information

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker is the person or group that allocates resources to and assesses the performance of the operating segments of an entity. The Group has determined the Acting Chief Executive Officer of the Bank as its chief operating decision-maker.

All transactions between business segments are conducted on an arm´s length basis, with intra-segment revenue and expenses being eliminated at Group level. Income and expenses directly associated with each segment are included in determining business segment performance.

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.

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (continued)

Significant assumptions, accounting judgements and estimates (continued)

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.

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.

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;

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 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 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.

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.

Notes to the Consolidated Financial Statements
At 31 December 2016

3 PROSPECTIVE CHANGES IN ACCOUNTING POLICIES (continued)

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

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.

Amendments to IAS 12 Income Taxes

In January 2016, through issuing amendments to IAS 12, the IASB clarified the accounting treatment of deferred tax assets of debt instruments measured at fair value for accounting, but measured at cost for tax purposes. The amendment is effective from 1 January 2017. The Group is currently evaluating the impact, but does not anticipate that adopting the amendments would have a material impact on its consolidated financial statements.

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.

4 FINANCIAL ASSETS AND LIABILITIES

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

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	3,363	845	-	104,462	108,670
TOTAL FINANCIAL ASSETS	29,413	19,973	404,436	1,653,496	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	-	-	-	62,724	62,724
TOTAL FINANCIAL LIABILITIES	-	-	-	2,476,281	2,476,281

31 December 2015	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	-	-	-	176,793	176,793
Placements with banks	-	-	-	57,026	57,026
Investments carried at fair value through statement of income	21,112	29,549	-	-	50,661
Non-trading investments	-	-	285,003	-	285,003
Loans and receivables	-	-	-	1,032,098	1,032,098
Other assets	-	205	-	115,302	115,507
Assets of disposal group classified as held for sale	-	-	-	1,028	1,028
TOTAL FINANCIAL ASSETS	21,112	29,754	285,003	1,382,247	1,718,116
Due to banks and other financial institutions	-	-	-	838,160	838,160
Deposits from customers	-	-	-	462,086	462,086
Loans payable	-	-	-	714,568	714,568
Subordinated debt	-	-	-	143,270	143,270
Other liabilities	65	15	-	54,919	54,999
Liabilities of disposal group classified as held for sale	-	-	-	166	166
TOTAL FINANCIAL LIABILITIES	65	15	-	2,213,169	2,213,249

5 INVESTMENTS CARRIED AT FAIR VALUE THROUGH STATEMENT OF INCOME

	2016 US$ 000	2015 US$ 000
Investments held for trading		
Quoted equities	15,485	21,112
Quoted debt securities	10,565	-
Investments designated at fair value through statement of income		
Credit linked notes	17,800	17,741
Managed funds	1,328	11,808
	45,178	50,661

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:

	2016 US$ 000	2015 US$ 000
Quoted		
Debt securities	161,842	134,720
Equities	57,825	12,547
Total quoted	219,667	147,267
Unquoted		
Equities	121,281	63,992
Other managed funds	51,514	52,837
Real estate managed funds	11,974	16,621
Debt securities	-	4,286
Total unquoted	184,769	137,736
Total non-trading investments	404,436	285,003

Included under non-trading investments are unquoted available-for-sale investments, primarily representing nominal equity stakes up to 13.9% (2015:13.9%) in various geographically and sectorally dispersed companies, amounting to US$ 43,789 thousand (2015: US$ 42,782 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.

6 NON-TRADING INVESTMENTS (continued)

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

	2016 US$ 000	2015 US$ 000
At 1 January	21,502	27,558
Charge for the year	1,300	-
Reversed upon disposal	(335)	(6,056)
Net movement during the year	965	(6,056)
At 31 December	22,467	21,502
Gross amount of individually impaired investments	39,887	38,461

7 LOANS AND RECEIVABLES

	2016 US$ 000	2015 US$ 000
Forfaiting assets	538,226	355,064
Factoring assets	220,597	340,842
Loans to customers	168,612	164,794
Loans to banks	173,766	114,359
Syndication loans	124,024	98,091
Staff loans	3,115	3,108
	1,228,340	1,076,258
Less: Provision for impairment	(43,536)	(44,160)
	1,184,804	1,032,098

The movement in the provision for impairment is as follows:

	2016		
	Specific US$ 000	Collective US$ 000	Total US$ 000
At 1 January	34,078	10,082	44,160
Provided 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

	2015		
	Specific US$ 000	Collective US$ 000	Total US$ 000
At 1 January	68,918	9,754	78,672
Provided (written-back) during the year - net	10,285	(668)	9,617
Written-off during the year	(41,587)	-	(41,587)
Other adjustments	(3,538)	996	(2,542)
Balance at 31 December	34,078	10,082	44,160

Notes to the Consolidated Financial Statements
At 31 December 2016

7 LOANS AND RECEIVABLES (continued)

	2016 US$ 000	2015 US$ 000
Gross amount of loans, individually determined to be impaired	70,527	80,869

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

31 December 2016	Neither past due nor impaired US$ 000	Past due but not impaired US$ 000	Past due and impaired US$ 000	Total US$ 000
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

31 December 2015	Neither past due nor impaired US$ 000	Past due but not impaired US$ 000	Past due and impaired US$ 000	Total US$ 000
Forfaiting assets	354,670	394	-	355,064
Factoring assets	311,881	-	28,961	340,842
Loans to customers	141,422	-	23,372	164,794
Loans to banks	105,680	-	8,679	114,359
Syndication loans	78,234	-	19,857	98,091
Staff loans	3,108	-	-	3,108
Total	994,995	394	80,869	1,076,258

All of the Group's loans and receivables which were past due but not impaired as of 31 December 2016 or 31 December 2015 were overdue for less than 30 days.

8 OTHER ASSETS

	2016 US$ 000	2015 US$ 000
Due from customers	29,497	22,414
Deferred tax asset (Note 12)	41,884	40,568
Accounts receivable	28,047	49,647
Prepayments	4,065	4,179
Interest receivable	5,034	2,673
Derivative assets (Note 29)	4,208	205
	112,735	119,686

8 OTHER ASSETS (continued)

Due from customers and accounts receivable are stated net of provision of US$ 157 thousand (2015: US$ 157 thousand). There were no additional provisions or write-backs during the year ended 31 December 2016 (2015: same).

9 INVESTMENTS IN ASSOCIATES

		Activity	Carrying value 2016 US$ 000	Ownership 2016 %	Carrying value 2015 US$ 000	Ownership 2015 %
a)	Burgan Bank S.A.K.	Commercial banking	484,095	15	537,150	17
b)	United Real Estate Company	Real estate	67,084	10	154,779	21
c)	North Africa Holding Company	Investments	49,027	44	53,951	44
d)	Assoufid B.V.	Holding, finance and project-development company	33,677	40	28,292	40
e)	Kuwait Education Fund	Fund	19,552	34	19,345	34
f)	United Capital Transport Co K.S.C.C.	Transport	16,530	40	15,433	40
g)	Manafae Investment Company	Islamic investment	12,855	31	11,268	31
h)	N.S. 88 (formerly Savannah SPV)	Real estate	12,292	20	5,976	20
i)	Al Sharq Financial Brokerage Co.	Brokerage and investment business	7,501	19	9,544	19
j)	Syria Gulf Bank	Commercial banking	4,033	31	4,034	31
k)	Brasilfactors	Factoring and Forfaiting	1,161	50	1,301	40
l)	Meena Homes Real Estate Company	Real estate	806	20	790	20
m)	Arab Leadership Academy	Training institute	408	15	412	15
n)	United Real Estate Company - Syria	Real estate	22	20	21	20
o)	Royal Capital Company P.S.C.	Asset management and financial services	-	-	2,671	26
p)	KAMCO Real Estate Yield Fund	Real estate	-	17	9,002	22
q)	The Egyptian Company for Factoring S.A.E.	Factoring and Forfaiting	-	-	15	50
r)	Takaud Saving & Pensions Company	Pension funds	-	50	-	-
			709,043		853,984	

The Group has no share of any contingent liabilities or capital commitments, as at 31 December 2016 and 2015 on behalf of its associates.

a) Burgan Bank S.A.K. is a listed commercial bank incorporated in the State of Kuwait. The Bank directly owns 15% (2015: 17%) equity interest in Burgan Bank. The Group has the ability to exercise significant influence on Burgan Bank through representation on the board of directors of Burgan Bank. During the year the Bank sold 2% of its holding in Burgan to KIPCO.

b) United Real Estate Company (URC), is a company listed on the Kuwait Stock Exchange. At 31 December 2016, the Bank directly owns 10% (2015: 21%) of URC. The Group has the ability to exercise significant influence on URC through representation on the board of directors of URC. During the year the Bank sold 11% of its holding in URC to KIPCO.

c) The Bank directly owns 33% (2015: 33%) of North Africa Holding Company (NAHC), a closed company incorporated in the State of Kuwait in 2006, and indirectly owns 11% (2015: 11%) through its subsidiary KAMCO.

d) The Bank directly owns 40% (2015: 40%) of Assoufid B.V., a closed company incorporated in the Netherlands.

e) Kuwait Education Fund is fund incorporated in the State of Kuwait in 2007. As of 31 December 2016, the Bank owns 34% through its subsidiary KAMCO (2015: 34%).

9 INVESTMENTS IN ASSOCIATES (continued)

f) United Capital Transport Company K.S.C.C. (UniCap) was incorporated in State of Kuwait in 2011. The Bank owns a 40% (2015: 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.

g) The Bank indirectly owns 31% (2015: 31%) of Manafae Investment Company through its subsidiary KAMCO.

h) The Bank indirectly owns 20% (2015: 20%) of N.S. 88 through its subsidiary KAMCO, formerly known as Savannah SPV.

i) Al Sharq Financial Brokerage Company (Al Sharq) is a closed company incorporated in the State of Kuwait during 2005. At 31 December 2016, the Bank indirectly owns a 19% interest in the associate through its subsidiary KAMCO (2015: 19%). The Group has the ability to exercise significant influence on Al Sharq through representation on the board of directors of Al Sharq. During the year, the Group has assessed the recoverable amount of its investment in Al Sharq and determined it to be impaired by US$ 1,633 thousand (2015: US$ 1,648 thousand).

j) Syria Gulf Bank (SGB) is a commercial bank incorporated in the Syrian Arab Republic. SGB commenced commercial operations in 2007. The Bank directly owns a 31% (2015: 31%) equity stake in SGB.

k) The Bank indirectly owns 50% (2015: 40%) of Brasilfactors through its subsidiary FIMBank.

l) The Bank indirectly owns 20% (2015: 20%) of Meena Homes Real Estate Company through its subsidiary KAMCO.

m) Arab Leadership Academy is training institute incorporated in the State of Kuwait in 2007. As of 31 December 2016, the Bank owns 15% (2015: 15%) through its subsidiary KAMCO. The Group has significant influence by appointment of directors on the Board of Directors of Arab Leadership Academy.

n) United Real Estate Company - Syria is a closed company incorporated in the Syrian Arab Republic. At 31 December 2016, the Bank directly owns 20% (2015: 20%) of its equity stake.

o) Royal Capital is a closed company incorporated in the United Arab Emirates in 2007. During the year, the Bank has sold its ownership in Royal Capital.

p) The Bank indirectly owns 17% (2015: 22%) of KAMCO Real Estate Yield Fund ("KREYF") through its subsidiary KAMCO. During the year, the investment was reclassified from "Investments in associates" to "Non-trading investments" as the Group could no longer exercise significant influence over KREYF.

q) During the year, the Group acquired additional 50% equity interest in The Egyptian Company for Factoring S.A.E. ("Egypt Factors"), following which Egypt Factors has become a subsidiary of the Group. As of 31 December 2016, the Bank indirectly owns 100% (2015: 50%) of Egypt Factors through its subsidiary FIMBank. As of 31 December 2015, the Group's investment in Egypt Factors was determined to be impaired by US$ 1,505 thousand.

r) The Bank directly owns 50% of Takaud. During the year, the Bank lost control over the Takaud following the management's decision not to participate in Takaud's proposed capital increase (Note 2). Accordingly, the investment in Takaud has been classified as an investment in an associate.

Investments in associates include quoted associates with a carrying value of US$ 555,212 thousand (2015: US$ 695,963 thousand) with a total quoted market price of US$ 343,713 thousand at 31 December 2016 (2015: US$ 519,003 thousand). 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 2016 (2015: same).

9 INVESTMENTS IN ASSOCIATES (continued)

Investments in material associates

The tables below illustrate the Group's investment in associates that are considered as individually material:

	Burgan Bank US$ 000	United Real Estate Company US$ 000
Summarised statement of financial position as of 31 December 2016:		
Current assets	14,921,993	347,905
Non-current assets	8,824,744	1,519,456
Current liabilities	(17,601,885)	(336,095)
Non-current liabilities	(3,382,499)	(747,598)
Equity	2,762,353	783,668
Equity attributable to the shareholders of the Parent	2,123,839	633,449
Proportion of the Group's ownership	15%	10%
Group's ownership in equity	323,036	62,711
Other adjustments	161,059	4,373
Carrying amount of investments	484,095	67,084
Fair value of investment in associate based on quoted market price	306,357	32,655
Summarised statement of financial position as of 31 December 2015:		
Current assets	1,710,895	191,626
Non-current assets	20,795,897	1,633,707
Current liabilities	(1,248,382)	(243,844)
Non-current liabilities	(18,487,289)	(754,222)
Equity	2,771,121	827,267
Equity attributable to the shareholders of the Parent	2,113,172	678,467
Proportion of the Group's ownership	17%	21%
Group's ownership in equity	364,311	145,599
Other adjustments	172,839	9,180
Carrying amount of investments	537,150	154,779
Fair value of investment in associate based on quoted market price	442,105	72,173
Summarised statement of income for the year ended 31 December 2016:		
Operating income	81,189	105,720
Interest income	1,019,977	1,073
Interest expense	(511,186)	(38,021)
Administrative expenses	(371,931)	(34,918)
Profit for the year	218,049	33,854
Other comprehensive loss for the year	(32,555)	(50,772)
Total comprehensive income (loss) for the year	185,494	(16,918)
Group's share of profit for the year (Note 22)	35,546	3,280
Cash dividend received from the associate during the year	18,359	1,763

9 INVESTMENTS IN ASSOCIATES (continued)

Investments in material associates (continued)

	Burgan Bank US$ 000	United Real Estate Company US$ 000
Summarised statement of income for the year ended 31 December 2015:		
Operating income	168,956	93,863
Interest income	868,745	1,404
Interest expense	(352,633)	(36,532)
Administrative expenses	(380,283)	(24,962)
Profit for the year	304,785	33,773
Other comprehensive (loss) income for the year	(162,365)	15,007
Total comprehensive income for the year	142,420	48,780
Group's share of profit for the year (Note 22)	44,042	6,003
Cash dividend received from the associate during the year	16,405	3,799

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:

	2016 US$ 000	2015 US$ 000
Summarised statement of financial position as of 31 December:		
Total assets	519,826	698,607
Total liabilities	(210,429)	(267,097)
Equity	309,397	431,510
Carrying amount of investments	157,864	162,055
Summarised statement of income for the year ended 31 December:		
Revenue	103,970	30,946
Gain (loss) for the year	9,383	(6,306)
Other comprehensive loss for the year	(34,489)	(24,462)
Total comprehensive loss for the year	(25,106)	(30,768)
Group's share of profit (loss) for the year	2,254	(4,195)

10 INVESTMENT PROPERTIES

	2016 US$ 000	2015 US$ 000
At 1 January	46,222	4,774
Acquisition*	56,000	19,708
Acquisition of a subsidiary	-	26,500
Other movements / disposals	(896)	(4,760)
At 31 December	101,326	46,222

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.

10 INVESTMENT PROPERTIES (continued)

* Acquisition during the year includes buildings of US$ 56 million which are located in Kuwait City, State of Kuwait.

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 2 and 3 of the fair value hierarchy as at 31 December 2016 and 2015.

11 GOODWILL

	2016 US$ 000	2015 US$ 000
At 1 January	52,321	54,509
Foreign currency translation adjustments	(453)	(2,188)
At 31 December	51,868	52,321

The goodwill remaining as of 31 December mainly 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% (2015: 3%) and discount factor of 10.7% (2015: 10%). There was no goodwill impairment identified in 2016 or 2015 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	
Key assumptions	+10 % US$ 000	-10 % US$ 000
Growth rate	5,362	(5,080)
Discount factor	(15,239)	20,036

12 TAXATION

The Group's subsidiaries in Malta, the United Kingdom, India, Chile and the United States of America are subject to income tax.

a) Deferred tax assets

Deferred tax assets relate to the following:

	2016 US$ 000	2015 US$ 000
Excess of capital allowances over depreciation	(294)	(416)
Allowances for uncollectibility	18,069	23,610
Changes in fair value of financial instruments	3,578	163
Investment tax credits	239	328
Unabsorbed capital allowances	542	275
Unabsorbed tax losses	19,750	16,608
	41,884	40,568

Reconciliation of deferred tax assets is as follows:

2016	Opening balance US$ 000	Recongnised in other e income US$ 000	Recognised in statement of income US$ 000	Effects of movement in exchange rates US$ 000	Closing balance US$ 000
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

2015	Arising on acquisition US$ 000	Recognised in other comprehensive income US$ 000	Recognised in statement of income US$ 000	Effects of movement in exchange rates US$ 000	Closing balance US$ 000
Excess of capital allowances over depreciation	(472)	-	56	-	(416)
Allowances for uncollectibility	26,285	-	(2,213)	(462)	23,610
Changes in fair value of financial instruments	25	(205)	343	-	163
Investment tax credits	328	-	-	-	328
Unabsorbed capital allowances	-	-	275	-	275
Unabsorbed tax losses	7,747	-	9,060	(199)	16,608
	33,913	(205)	7,521	(661)	40,568

As at 31 December 2016, the Group has tax losses arising out of subsidiaries in Malta and the United Kingdom of US$ 72,854 thousand (31 December 2015: US$ 95,889 thousand) that are available for offsetting against future taxable profits.

12 TAXATION (continued)

b) Deferred tax liabilities

Deferred tax liabilities relate to the following:

	2016 US$ 000	2015 US$ 000
Excess of capital allowances over depreciation	403	403
Changes in fair value of financial instruments	1,799	1,805
	2,202	2,208

Reconciliation of deferred tax liabilities is as follows:

2016	Opening balance	Arising on acquisition	Recognised in statement of income	Closing balance
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
2015				
Excess of capital allowances over depreciation	-	115	288	403
Changes in fair value of financial instruments	-	1,259	546	1,805
	-	1,374	834	2,208

c) Income tax credit

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

	2016 US$ 000	2015 US$ 000
Consolidated statement of income		
Current income tax charge	(114)	(50)
Movement in deferred tax assets recognised in statement of income	697	7,521
Movement in deferred tax liabilities recognised in statement of income	(6)	(834)
Income tax credit reported in the statement of income - net	577	6,637

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.

Notes to the Consolidated Financial Statements
At 31 December 2016

13 LOANS PAYABLE

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 years	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

31 December 2015	Currency*	Bank US$ 000	Subsidiaries US$ 000	Total US$ 000
Maturing within one year				
1 month or less	KWD	-	21,421	21,421
	US$	-	20,000	20,000
	EUR	-	6,121	6,121
	Various	-	5,771	5,771
3 months or less but over 1 month	US$	-	25,500	25,500
	KWD	-	24,717	24,717
	EUR	-	2,185	2,185
1 year or less but over 3 months	US$	70,000	65,000	135,000
	KWD	-	26,364	26,364
	INR	-	20,477	20,477
	EUR	-	3,278	3,278
		70,000	220,834	290,834
Maturing after one year				
More than 1 year & less than 2 years	US$	346,330	-	346,330
	KWD	-	16,478	16,478
More than 2 years	US$	49,433	-	49,433
	KWD	-	11,405	11,405
	Various	-	88	88
		395,763	27,971	423,734
		465,763	248,805	714,568

* KWD represents Kuwaiti Dinar.

* INR represents Indian Rupee.

14 SUBORDINATED DEBT

During the current year, the Bank's 10-year floating rate notes amounting to US$ 100 million matured and were repaid. As of 31 December 2016, the Group's sub-ordinated debt comprises of a 5-year loan amounting to US$ 50 million issued in 2015 by FIMBank, a subsidiary of the Group. The instrument carries a floating rate of interest and ranks after the Group's unsubordinated, secured and unsecured creditors. The Group's subordinated debt qualifies as Tier 2 capital under the provisions of capital adequacy guidelines issued by the CBB.

15 OTHER LIABILITIES

	2016 US$ 000	2015 US$ 000
Staff related payables	16,955	16,607
Accrued expenses	17,717	17,620
Interest payable	11,047	7,306
Dividends payable	2,508	2,500
Deferred tax (Note 12)	2,202	2,208
Derivative financial liabilities (Note 29)	8,841	80
Other payables	3,454	8,678
	62,724	54,999

16 EQUITY

Share capital

The Bank's authorised share capital as of 31 December 2016 comprised 1 billion shares of US$ 0.25 each (2015: 1 billion shares of US$ 0.25 each).

The issued and fully paid up share capital as of 31 December 2016 comprised 834,602,295 shares of US$ 0.25 each (2015: 834,602,295 shares of US$ 0.25 each).

Treasury shares and treasury shares reserve

At 31 December 2016, the Bank held 19,454,135 treasury shares (2015: 19,454,135 shares). These treasury shares do not carry any voting rights and are not entitled to dividends. The net gain or loss on reissuance of treasury shares is taken to treasury share reserve in the consolidated statement of changes in equity and is not available for distribution. The value of treasury shares based on the last bid price of US$ 0.93 (equivalent to BD 0.350) per share as of 31 December 2016 was US$ 18,061 thousand [2015: US$ 20,125 thousand at US$ 1.03 (equivalent to BD 0.390) per share].

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.

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.

General reserve

The Directors have approved a transfer of 10% (2015:10%) of the profit of the Group for the year to general reserve in accordance with the Bank's Articles of Association. The transfer is subject to shareholders' approval at the forthcoming Annual General Meeting. The general reserve is distributable subject to the approval of the Central Bank of Bahrain.

Dividend paid

No dividend was announced or paid during the years ended 31 December 2016 or 2015.

16 EQUITY (continued)

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.

17 FAIR VALUE RESERVE

	2016 US$ 000	2015 US$ 000
Non-trading investments		
Balance at 1 January	(48,349)	7,628
Transferred to consolidated statement of income upon:		
- sale of non-trading investments	2,681	(19,628)
Net movement in unrealised fair value during the year	(5,143)	(36,349)
Balance at 31 December	(50,811)	(48,349)
Cash flow hedges		
Balance at 1 January	190	(89)
Net movement in the fair values during the year	655	279
Balance at 31 December	845	190
	(49,966)	(48,159)

18 PERPETUAL TIER 1 CAPITAL

On 28th 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 as 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

	2016 US$ 000	2015 US$ 000
Loans and receivables	43,079	53,879
Non-trading investments	4,033	42
Placements with banks	1,176	2,342
Demand and call deposits with banks	215	85
	48,503	56,348

20 INVESTMENT INCOME - NET

	2016 US$ 000	2015 US$ 000
Dividend income	7,230	5,104
Gain on sale of an associates and subsidiaries	2,824	2,631
Gain on bargain purchase	-	2,040
Rental income from investment properties	3,294	1,430
Gain (loss) on sale of non-trading investments	852	(105)
Loss on investments carried at fair value through statement of income	(229)	(4,963)
Others	5,738	1,525
	19,709	7,662

21 FEES AND COMMISSIONS - NET

	2016 US$ 000	2015 US$ 000
Credit related fees, commissions and other income - net	13,517	14,486
Management fees from fiduciary activities	13,541	13,891
Advisory fees	7,426	3,336
	34,484	31,713

22 SHARE OF RESULTS OF ASSOCIATES - NET

	2016 US$ 000	2015 US$ 000
Burgan Bank	35,546	44,042
United Real Estate Company	3,280	6,003
United Capital Transport Company	1,295	1,279
Manafae Investment Company	1,242	(390)
N.S. 88	722	-
Assoufid B.V.	586	(1,396)
KAMCO Real Estate Yield Fund	349	376
Kuwait Education Fund	299	186
Meena Homes Real Estate Company	23	23
Brasilfactors	-	(237)
The Egyptian Company for Factoring S.A.E.	(15)	(568)
Royal Capital Company P.S.C.	(35)	-
Al Sharq Financial Brokerage Co.	(54)	(10)
CIS Factors Holding B.V.	(395)	-
Takaud Saving & Pensions Company	(849)	-
North Africa Holding Company	(914)	(3,458)
	41,080	45,850

Notes to the Consolidated Financial Statements
At 31 December 2016

23 INTEREST EXPENSE

	2016 US$ 000	2015 US$ 000
Loans payable	30,413	29,847
Due to banks and other financial institutions	9,821	8,534
Subordinated debt	2,859	3,629
Deposits from customers	9,839	9,564
	52,932	51,574

24 EARNINGS PER SHARE

Basic and diluted

Basic and diluted earnings per share is calculated by dividing the profit attributable to the equity shareholders of the Bank by the weighted average number of shares outstanding during the year as follows:

	2016 US$ 000	2015 US$ 000
Profit (loss) attributable to equity shareholders of the Bank from:		
- continuing operations	6,308	12,782
- discontinued operations	(49)	(1,563)
	6,259	11,219
Weighted average number of shares outstanding during the year (in thousands)	815,254	815,254
Basic and diluted earnings per share (US cents)	0.77	1.38
Basic and diluted earnings per share from continuing operations (US cents)	0.77	1.57

25 CASH AND CASH EQUIVALENTS

	2016 US$ 000	2015 US$ 000
Demand and call deposits with banks excluding mandatory reserves	169,717	168,743
Placements with original maturities of ninety days or less	187,350	52,214
	357,067	220,957

26 SEGMENTAL INFORMATION

Following the management approach of IFRS 8, operating segments are reported in accordance with the internal reporting provided to the Acting Chief Executive Officer, who is responsible for allocating resources to the reportable segments and assessing their performance. All operating segments reported by the Group meet the definition of a reportable segment under IFRS 8.

For management purposes, the Group is organised into business units based on the nature of their operations and services. The Group has two reportable operating segments being 'asset management and investment banking' and 'commercial banking'.

Asset management and investment banking	Undertaking asset portfolio management, corporate finance, advisory, investments in quoted and private equity/funds, real estate, capital markets, international banking and treasury activities.
Commercial banking	Loans and other credit facilities, deposit and current accounts from corporate and institutional customers.

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Transactions between segments are generally recorded at estimated market rates.

26 SEGMENTAL INFORMATION (continued)

Segmental information relating to the Group's operations for the year ended 31 December 2016 was as follows:

Statement of income	Asset management and investment banking US$ 000	Commercial banking US$ 000	Total US$ 000
Income from external customers	30,860	66,085	96,945
Share of results of associates - net	6,794	34,286	41,080
Total income	37,654	100,371	138,025
Operating income before provisions and tax	8,343	3,221	11,564
Impairment loss on investments	(2,933)	-	(2,933)
Write-back of (provisions for) doubtful loans and other assets - net	894	(9,149)	(8,255)
Taxation - net	(20)	597	577
Profit (loss) for the year from continuing operations	6,284	(5,331)	953
Discontinued operations			
Net loss from discontinued operations	-	(80)	(80)
NET PROFIT (LOSS) FOR THE YEAR	6,284	(5,411)	873
Profit attributable to equity shareholders of the parent			6,259
Loss attributable to non-controlling interests			(5,386)
			873
Statement of financial position			
Investments in associates	219,754	489,289	709,043
Segment assets	901,062	2,104,675	3,005,737
Segment liabilities	936,244	1,540,037	2,476,281

26 SEGMENTAL INFORMATION (continued)

Segmental information for the year ended 31 December 2015 was as follows:

Statement of income	Asset management and investment banking US$ 000	Commercial banking US$ 000	Total US$ 000
Income from external customers	30,804	68,176	98,980
Share of results of associates and joint ventures	2,613	43,237	45,850
Total income	33,417	111,413	144,830
Operating income (loss) before provisions and tax	12,629	(742)	11,887
Impairment loss on investments	(1,648)	(1,505)	(3,153)
Provisions for doubtful loans and other assets - net	-	(9,617)	(9,617)
Taxation	-	6,637	6,637
Profit (loss) for the year	10,981	(5,227)	5,754
Discontinued operations			
Net loss from discontinued operations	-	(2,554)	(2,554)
NET PROFIT (LOSS) FOR THE YEAR	10,981	(7,781)	3,200
Profit attributable to equity shareholders of the parent			11,219
Loss attributable to non-controlling interests			(8,019)
			3,200
Statement of financial position			
Investments in associates	311,483	542,501	853,984
Segment assets	860,721	1,855,795	2,716,516
Segment liabilities	985,306	1,227,943	2,213,249

Geographical segments

The Group operates in four geographic markets: Domestic region (G.C.C.*), Middle East and North Africa (MENA) (excluding G.C.C.), Europe, North America and others. The following table shows the distribution of the Group's total income and non-current assets by geographical segment, allocated based on the location of the customers and assets for the years ended 31 December 2016 and 2015:

	G.C.C. US$ 000	MENA US$ 000	Europe US$ 000	North America US$ 000	Others US$ 000	Total US$ 000
31 December 2016						
Total income	59,287	8,465	22,864	4,091	43,318	138,025
Non-current assets	1,112,713	9,815	61,454	7,512	-	1,191,494
31 December 2015						
Total income	81,630	11,737	10,769	10,609	30,085	144,830
Non-current assets	1,181,341	5,810	64,102	7,152	-	1,258,405

* The Gulf Co-operation Council (G.C.C.) countries are Kingdom of Bahrain, State of Kuwait, Kingdom of Saudi Arabia, State of Qatar, the United Arab Emirates and the Sultanate of Oman.

27 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:

	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

	2015			
	Parent US$ 000	Associates and joint ventures US$ 000	Other related parties US$ 000	Total US$ 000
Loss on sale of non-trading investments	-	(614)	-	(614)
Gain on sale of investments in associates and subsidiaries	-	-	359	359
Fees and commissions - net	3,054	1,328	5,314	9,696
Dividend income	22	40	207	269
Interest income	1	996	341	1,338
Interest expense	(999)	(13,905)	(3,520)	(18,424)
Others	743	8,994	(904)	8,833
Purchase transactions	-			
Investments in associates	-	30,055	2,651	32,706
Investment in subsidiary	-	12,161	-	12,161
Investment properties	-	19,708	-	19,708
Sale transactions				
Non-trading investments	-	22,220	-	22,220
Investments in Subsidiaries	-	-	2,945	2,945
Investment properties	-	4,001	-	4,001

27 RELATED PARTY TRANSACTIONS (CONTINUED)

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

	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

	2015			
	Parent US$ 000	Associates US$ 000	Other related parties US$ 000	Total US$ 000
Demand and call deposits with banks	-	750	530	1,280
Placements with banks	-	10,500	20,356	30,856
Investments, carried at fair value through statement of income	724	1,104	1,931	3,759
Investments, carried at fair value through statement of income in funds managed by related party	-	-	9,962	9,962
Non-trading investments	-	4,900	23,443	28,343
Loans and receivables	-	28,014	8,825	36,839
Other assets	409	42,305	11,168	53,882
Due to banks and other financial institutions	-	(51,729)	(133,405)	(185,134)
Deposits from customers	(94)	(2,846)	(14,739)	(17,679)
Loans payable	-	(492,865)	-	(492,865)
Other liabilities	(181)	(2,561)	(2,895)	(5,637)
Subordinated debt	-	(50,000)	-	(50,000)
Off statement of financial position items:				
Letters of guarantee	-	-	-	-

* The Group has sold investments in associates 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. All related party exposures are performing and are free of any provision for possible credit losses.

27 RELATED PARTY TRANSACTIONS (CONTINUED)

Compensation of key management personnel was as follows:

	2016 US$ 000	2015 US$ 000
Short term employee benefits	8,716	7,780

28 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:

	2016 US$ 000	2015 US$ 000
Credit related		
Letters of credit	52,044	88,159
Letters of guarantee	7,161	11,082
	59,205	99,241
Investment related *	140,044	65,819
	199,249	165,060

* 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.

29 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 2016	Positive fair value US$ 000	Negative fair value US$ 000	Notional amount Total US$ 000	Within 3 months US$ 000	3 - 12 months US$ 000	1 - 5 years US$ 000
Derivatives held for trading *						
Forward foreign exchange contracts	1,506	(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 swaps	845	-	175,000	-	80,000	95,000
31 December 2015						
Derivatives held for trading *						
Forward foreign exchange contracts	54	(481)	235,538	226,308	9,230	-
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	575	(213)	699,479	699,479	-	-
Derivatives used as cash flow hedges						
Interest rate swap	205	(15)	200,000	-	50,000	150,000

* 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$ 711 million (KWD 218 million) [2015: US$ 699 million (KWD 212 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.

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:

29 DERIVATIVES (continued)

	2016		2015	
	Within 1 year US$ 000	1-5 years US$ 000	Within 1 year US$ 000	1-5 years US$ 000
Net cash outflows (liabilities)	1,347	873	882	930
Statement of comprehensive income	152	693	(15)	205

30 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 him 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.

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.

30 RISK MANAGEMENT (continued)

a) Introduction (continued)

Risk and Compliance Committee
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.

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

30 RISK MANAGEMENT (continued)

a) Introduction (continued)

Concentration risk (continued)

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 full Board.

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 master netting and collateral arrangements, but after any provision for impairment.

	2016 US$ 000	2015 US$ 000
Demand and call deposits with banks	176,880	176,793
Placements with banks	187,350	57,026
Non-trading investments	161,842	139,006
Loans and receivables	1,184,804	1,032,098
Other assets	104,462	115,302
Letters of credit	52,044	88,159
Letters of guarantee	7,161	11,082
Derivative financial assets	4,208	205
	1,878,751	1,619,671

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 2016 was US$ 120 million (2015 US$ 104 million) before taking account of collateral or other credit enhancements.

30 RISK MANAGEMENT (continued)

b) Credit risk (continued)

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

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	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	4,208	-	-	-	-	-	4,208
31 December 2016	295,204	97,739	800,967	258,420	117,559	308,862	1,878,751
Demand and call deposits with banks	21,546	5,588	75,165	74,127	336	31	176,793
Placements with banks	24,004	30,356	2,666	-	-	-	57,026
Non-trading investments	4,286	-	57,053	77,667	-	-	139,006
Loans and receivables	144,991	264,553	419,997	111,730	72,984	17,843	1,032,098
Other assets	53,711	10,964	31,310	3,106	16,211	-	115,302
Letters of credit	1,302	69,651	6,738	1,846	8,622	-	88,159
Letters of guarantee	2,734	6,679	1,133	536	-	-	11,082
Derivative financial assets	205	-	-	-	-	-	205
31 December 2015	252,779	387,791	594,062	269,012	98,153	17,874	1,619,671

30 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 2016	Trading & Manufac-turing US$ 000	Banks and other financial institutions US$ 000	Constrution 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	-	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	-	4,208	-	-	-	-	4,208
	312,167	1,203,767	58,469	2,132	97,674	204,542	1,878,751
At 31 December 2015							
Demand and call deposits with banks	-	176,793	-	-	-	-	176,793
Placements with banks	-	57,026	-	-	-	-	57,026
Non-trading investments	-	4,286	-	-	134,720	-	139,006
Loans and receivables	261,485	561,821	53,272	2,387	53,239	99,894	1,032,098
Other assets	72	54,924	1,925	258	263	57,860	115,302
Letters of credit	1,044	86,953	-	-	-	162	88,159
Letters of guarantee	1,432	7,319	-	251	-	2,080	11,082
Derivative financial assets	-	205	-	-	-	-	205
	264,033	949,327	55,197	2,896	188,222	159,996	1,619,671

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.

30 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 2016 US$ 000	Net maximum exposure 2016 US$ 000	Gross maximum exposure 2015 US$ 000	Net maximum exposure 2015 US$ 000
Loans to banks	173,766	52,123	114,359	73,645
Loans to customers	168,612	140,515	164,794	101,857
Factoring assets	220,597	170,589	340,842	156,117
Forfaiting assets	538,226	538,226	355,064	355,064
Syndication loans	124,024	124,024	98,091	87,147
Others	3,115	3,115	3,108	391
	1,228,340	1,028,592	1,076,258	774,221

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 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	4,208	-	-	4,208
	554,133	259,873	1,064,745	1,878,751
At 31 December 2015				
Demand and call deposits with banks	166,207	5,318	5,268	176,793
Placements with banks	36,671	-	20,355	57,026
Non-trading investments	134,720	-	4,286	139,006
Loans and receivables	115,007	143,346	773,745	1,032,098
Other assets	49,119	949	65,234	115,302
Letters of credit	13,872	23,818	50,469	88,159
Letters of guarantee	659	-	10,423	11,082
Derivative financial assets	205	-	-	205
	516,460	173,431	929,780	1,619,671

30 RISK MANAGEMENT (continued)

b) Credit risk (continued)

Credit risk exposure for each credit rating (continued)

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.

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 had US$ 17,258 thousand of restructured loans as of 31 December 2016 (31 December 2015: US$ 20,347 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 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	-	-
31 December 2015		
Gross amounts of recognised financial asset (liability)	155,000	(155,023)
Gross amounts offset in the consolidated statement of financial position	(155,000)	155,000
Net amount of financial liability presented in the consolidated statement of financial position	-	(23)

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.

30 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 2016	Sensitivity of net interest income 2016 US$ 000	Increase in basis points 2015	Sensitivity of net interest income 2015 US$ 000
Kuwaiti Dinar	+ 25	(439)	+ 25	(511)
United States Dollar	+ 25	(404)	+ 25	(1,040)
Euro	+ 25	(1,093)	+ 25	(109)
Pound Sterling	+ 25	6	+ 25	6
Others	+ 25	76	+ 25	143

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 2016, 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 % 2016	Effect on profit before tax 2016 US$ 000	Effect on equity 2016 US$ 000	Change in currency rate in % 2015	Effect on profit before tax 2015 US$ 000	Effect on equity 2015 US$ 000
Kuwaiti Dinar	+2	443	1,668	+2	(21,653)	1,643
	-2	(443)	(1,668)	-2	21,653	(1,643)
Euro	+2	8,001	-	+2	(1,518)	-
	-2	(8,001)	-	-2	1,518	-
Pound Sterling	+2	65	-	+2	23	-
	-2	(65)	-	-2	(23)	-

30 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 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
Credit linked notes	-	17,800	-	-	17,800
	14,434	19,098	67	1,014	34,613
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	45,911	19,139	1,014	277,207

At 31 December 2015	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	15,583	706	4,053	770	21,112
Managed funds	11,341	401	66	-	11,808
Credit linked notes	-	17,741	-	-	17,741
	26,924	18,848	4,119	770	50,661
Non-trading investments					
Quoted equities	2,497	-	10,050	-	12,547
Unquoted equities	41,131	16,406	6,455	-	63,992
Managed funds	63,072	5,689	697	-	69,458
	106,700	22,095	17,202	-	145,997
Total	133,624	40,943	21,321	770	196,658

At the reporting date, the exposure to listed equity securities at fair value was US$ 73,310 thousand (2015: US$ 33,659 thousand). A decrease of 10% on the market indices of MENA stock exchanges could have an impact of approximately US$ 7,331 thousand (2015: US$ 3,365 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.

Notes to the Consolidated Financial Statements
At 31 December 2016

30 RISK MANAGEMENT (continued)

c) Market risk (continued)

Geographical distribution (continued)

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.

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 2016 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 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
Liabilities of disposal group classified as held for sale	-	-	-	-	-	-
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.

30 RISK MANAGEMENT (continued)

d) Liquidity risk (continued)

At 31 December 2015	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	112,907	417,342	159,205	158,895	-	848,349
Deposits from customers	38,826	348,633	25,957	54,144	-	467,560
Loans payable	21,450	135,083	138,080	433,370	14,854	742,837
Subordinated debt	-	-	95,485	59,390	-	154,875
Other liabilities	-	-	-	54,999	-	54,999
Liabilities of disposal group classified as held for sale	-	-	166	-	-	166
Total non-derivative undiscounted financial liabilities	173,183	901,058	418,893	760,798	14,854	2,268,786
Derivatives						
Net cash outflows on interest rate swaps		483	399	930	-	1,812
Gross settled foreign currency derivatives		925,787	9,230	-	-	935,017
Off statement of financial position items						
Letters of credit		55,317	12,421	20,421	-	88,159
Letters of guarantee		11,082	-	-	-	11,082
Investment related commitments		-	-	65,819	-	65,819

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

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.

30 RISK MANAGEMENT (continued)

d) Liquidity risk (continued)

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 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	-	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

30 RISK MANAGEMENT (continued)

d) Liquidity risk (continued)

At 31 December 2015	Less than 12 months US$ 000	Over 12 months US$ 000	Total US$ 000
Demand and call deposits with banks	168,743	8,050	176,793
Placements with banks	52,214	4,812	57,026
Investments carried at fair value through statement of income	50,661	-	50,661
Non-trading investments	147,268	137,735	285,003
Loans and receivables	918,511	113,587	1,032,098
Other assets	119,686	-	119,686
Investments in associates and joint venture	-	853,984	853,984
Investment properties	-	46,222	46,222
Property and equipment	-	41,694	41,694
Goodwill	-	52,321	52,321
Assets of disposal group classified as held for sale	1,028	-	1,028
Total assets	1,458,111	1,258,405	2,716,516
Due to banks and other financial institutions	685,567	152,593	838,160
Deposits from customers	410,524	51,562	462,086
Loans payable	290,834	423,734	714,568
Subordinated debt	93,270	50,000	143,270
Other liabilities	-	54,999	54,999
Liabilities of disposal group classified as held for sale	166	-	166
Total liabilities	1,480,361	732,888	2,213,249
Net	(22,250)	525,517	503,267

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.

31 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 2016:

	Fair value measurement using			
	Level 1 US$ 000	Level 2 US$ 000	Level 3 US$ 000	Total US$ 000
Assets measured at fair value				
Investments carried at fair value through 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
Debt securities - unquoted	-	-	-	-
Derivatives				
Forward foreign exchange contracts	-	3,363	-	3,363
Interest rate swaps	-	845	-	845
Investment properties	-	19,722	81,604	101,326
	263,517	150,183	97,659	511,359
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	-	(8,841)	-	(8,841)
	-	(8,841)	-	(8,841)

31 FAIR VALUE MEASUREMENT (continued)

Quantitative disclosures fair value measurement hierarchy for assets as at 31 December 2015:

	Fair value measurement using			
	Level 1 US$ 000	Level 2 US$ 000	Level 3 US$ 000	Total US$ 000
Assets measured at fair value				
Investments carried at fair value through statement of income				
Quoted equities	21,112	-	-	21,112
Credit linked notes	17,741	-	-	17,741
Managed funds	9,961	1,847	-	11,808
Non-trading investments				
Equities - quoted	12,547	-	-	12,547
Debt Securities - quoted	134,720	-	-	134,720
Equities - unquoted	-	22,370	478	22,848
Real estate managed funds - unquoted	-	16,301	-	16,301
Other managed funds	-	40,238	12,599	52,837
Debt securities - unquoted	-	-	2,968	2,968
Derivatives				
Forward foreign exchange contracts	-	629	-	629
Interest rate swaps	-	205	-	205
Investment properties	-	19,722	26,500	46,222
	196,081	101,312	42,545	339,938
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	-	(694)	-	(694)
Interest rate swaps	-	(15)	-	(15)
	-	(709)	-	(709)

Transfers between Level 1, Level 2 and Level 3

During the year ended 31 December 2016 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.

31 FAIR VALUE MEASUREMENT (continued)

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

	Equities US$ 000	Other managed funds US$ 000	Debt securities US$ 000	Investment properties US$ 000	Total US$ 000
As at 1 January 2015	531	14,674	1,368	-	16,573
Recognised in statement of income	44	(19)	-	-	25
Net purchases, sales and transfers and settlements	(97)	(1,079)	1,600	26,500	26,924
Remeasurement recognised in OCI	-	(977)	-	-	(977)
As at 1 January 2016	478	12,599	2,968	26,500	42,545
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 31 December 2016	474	15,581	-	81,604	97,659

32 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.

32 CAPITAL ADEQUACY (continued)

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:

	2016 US$ 000	2015 US$ 000
Capital base:		
Tier 1	264,123	316,345
Tier 2	73,751	88,292
Total capital base (a)	337,874	404,637
Credit risk weighted exposure	2,227,194	2,576,211
Market risk weighted exposure	122,725	66,898
Operational risk weighted exposure	84,638	52,750
Total risk weighted exposure (b)	2,434,557	2,695,859
Capital adequacy (a/b * 100)	13.88%	15.01%
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.

33 MATERIAL PARTLY OWNED SUBSIDIARIES

KAMCO and FIMBank are the subsidiaries that the Group has material non-controlling interests in, and are listed on the Kuwait Stock Exchange and Malta Stock Exchange respectively. Presented below are the aggregated financial information of these subsidiaries as disclosure of the financial information for each subsidiary is not allowed by the stock exchange by-laws until the respective financial results of these subsidiaries are published.

	2016 US$ 000	2015 US$ 000
Accumulated balances of material non-controlling interest	33,786	103,793
Loss allocated to material non-controlling interest	(303)	(3,180)

The summarised financial information of these subsidiaries is provided below. This information is based on amounts before inter-company eliminations.

	2016 US$ 000	2015 US$ 000
Summarised statement of income for the year ended 31 December:		
Total income	95,135	91,014
Total expenses	(83,016)	(92,335)
Taxation	597	7,471
Losses on impairment - net	(11,118)	(12,770)
Profit (loss) for the year	1,598	(6,620)
Total comprehensive loss for the year	(12,125)	(11,944)
Total comprehensive loss attributable to non-controlling interests	(960)	(4,244)
Summarised statement of financial position as of 31 December:		
Total assets	1,957,060	1,665,804
Total liabilities	(1,666,653)	(1,371,309)
Total equity	290,407	294,495
Attributable to equity holders of the parent	256,621	190,702
Non-controlling interest	33,786	103,793
Summarised cash flow information for the year ended 31 December:		
Operating activities	260,467	(66,671)
Investing activities	(27,891)	(236,360)
Financing activities	(43,765)	85,287
Foreign currency translation adjustments	657	288
Net decrease in cash and cash equivalents	189,468	(217,456)

Group Directory

UGB is the merchant banking subsidiary of the KIPCO Group. Its proprietary investments include assets in commercial banking, real estate, private equity, and quoted securities. As of 31 December 2016, assets under management totaled US$ 10.0 billion.

UGB's core subsidiaries, associates and joint venture include: Burgan Bank, FIMBank, KAMCO Investment Company (KAMCO), North Africa Holding Company, United Gulf Financial Services - North Africa, Takaud Savings & Pension Company, United Capital Transport Company and United Real Estate Company.

UGB and its subsidiary KAMCO have a proven track record of successfully completing more than 60 investment banking transactions for clients since 2001 with an aggregate value of over US$ 10 billion including corporate finance, advisory, new issue placement and underwriting, corporate restructuring, bond issuance, and mergers and acquisitions.

United Gulf Bank B.S.C.

P O Box 5964, Diplomatic Area UGB Tower, Manama, Kingdom of Bahrain
Tel: +973 17 533233
Fax: +973 17 533137
Email: info@ugbbah.com
Website: www.ugbbh.com

Parent Company

Kuwait Projects Company (Holding) (K.S.C.)

KIPCO Tower, Khalid Bin Al Waleed Street, Sharq, Kuwait City
P.O. Box 23982, Safat 13100, Kuwait
Tel: +965 1805 885
Fax: +965 2243 5790
Email: kipco@kipco.com
Website: www.kipco.com

Asset Management & Investment Banking

KAMCO Investment Company (KAMCO) K.S.C.(Public)

Al-Shaheed Tower Khalid Bin Waleed Street Sharq, Kuwait
P O Box 28873, Safat 13149, Kuwait
Tel: +965 1852626
Fax: +965 2244 5918
Email: info@kamconline.com
Website: www.kamconline.com

North Africa Holding Company K.S.C.(c)

Sharq, Al Shaheed Tower, 5th Floor Khaled Bin Al Waleed Street,
P O Box 1246, Dasman 15463, Kuwait
Tel: +965 2291 3733
Fax: +965 22450371
Email: info@northafricaholding.com
Website: www.northafricaholding.com

United Gulf Financial Services - North Africa

Rue du Lac Biwa ImmFraj 2 ème Etage, 1053 Les Berges du Lac, Tunis, Tunisia
Tel: + 216 71 167 500
Fax: +216 71 965 181
Email: contact@ugfsnorthafrica.com.tn
Website: www.ugfsnorthafrica.com.tn

Savings & Pensions

TAKAUD Savings & Pensions B.S.C.(c)

P O Box 65167, UGB Tower, 7th Floor Diplomatic Area, Manama, Kingdom of Bahrain
Tel: +973 1751 1611
Fax: +973 1751 1600
Email: info@takaud.com
Website: www.takaud.com

Brokerage

Al Sharq Financial Brokerage Company K.S.C.(c)

P O Box 187, Kuwait Souk Al Dakhelely 15252, Kuwait
Tel: +965 2224 8444
Fax: +965 22424378
Email: webmaster@sharqetrade.com
Website: www.sharqetrade.com

Commercial Banking

FIMBank p.l.c

Mercury Tower, The Exchange Financial & Business Centre
Elia Zammit Street, St. Julian's STJ 3155, Malta
Tel: +356 21322100
Fax: +356 21322122
Email: info@fimbank.com
Website: www.fimbank.com

Burgan Bank K.P.S.C.

Burgan Tower, Al Sharq, Abdullah Al Ahmed St.
P O Box 5389, Safat 12170, Kuwait
Tel: +965 2298 8000
Fax: +965 22417926
Email: info@burgan.com
Website: www.burgan.com

Major Non-Financial Operating Companies

United Real Estate Company

P O Box 2232, Safat 13023, Kuwait
Tel: +965 22953500
Fax: +965 2244 1003
Email: info@urc.com.kw
Website: www.urc.com.kw

Major Subsidiaries and Affiliates

P.O. Box 5964, Diplomatic Area
UGB Tower, Manama, Kingdom of Bahrain
Tel: +973 17 533 233, Fax: +973 17 533 137
info@ugbbah.com
www.ugbbh.com

Licensed as a conventional wholesale bank by the Central Bank of Bahrain