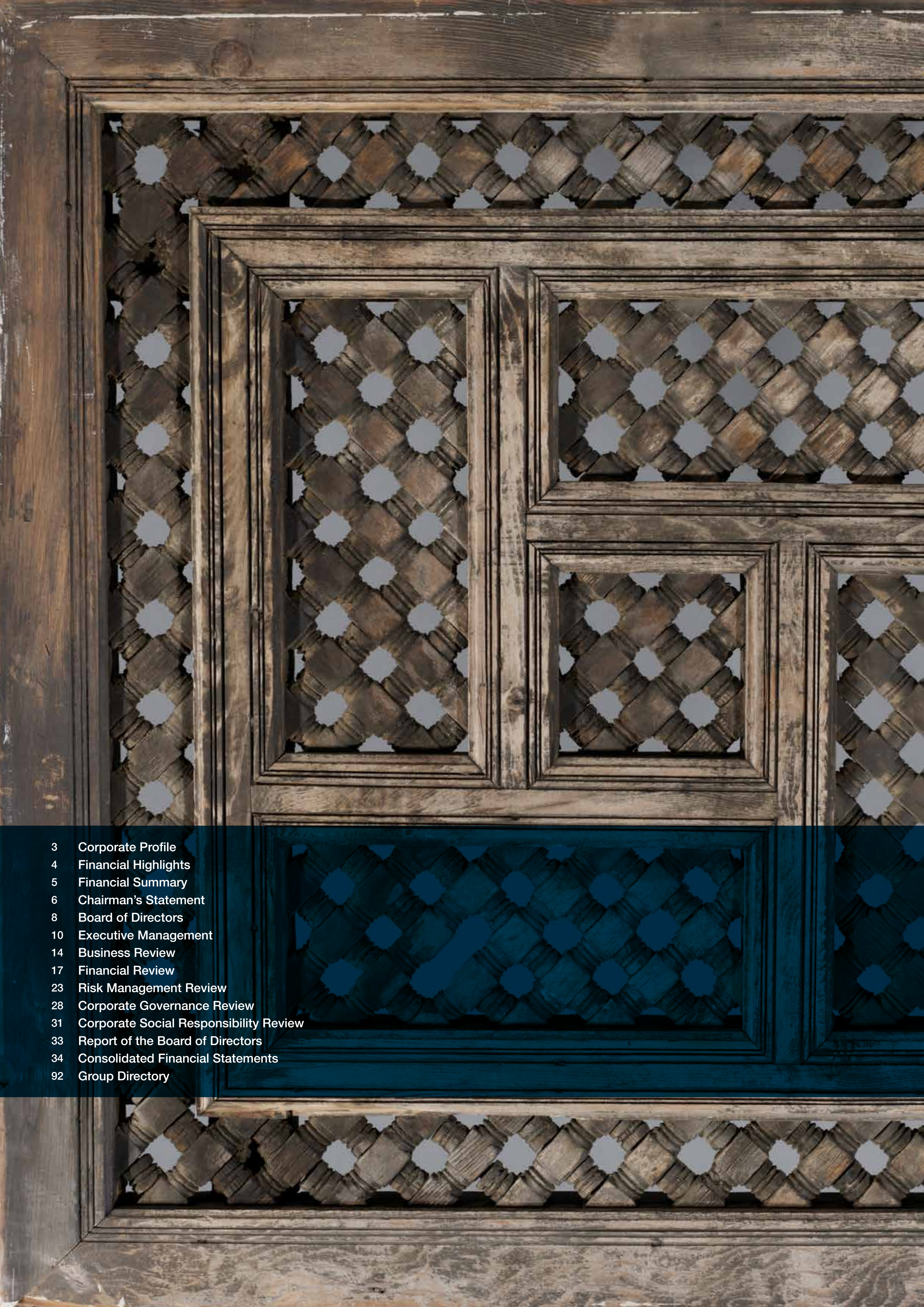
ANNUAL REPORT **2017**

بنك الخليج المتحد ش.م.ب.

United Gulf Bank B.S.C.

A member of the KIPCO Group



Dar al-Athar al-Islamiyyah, one of Kuwait'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 wooden artifact 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 featured here (LNS 51 W) is a wooden screen that was probably made in Morocco during the 14th -15th century CE. The central panel features a parallel-set square 'pinwheel' motif, in between which are units of 'mashrabiya' work. 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.E. SHEIKH SABAH AL AHMAD AL JABER AL-SABAH

Amir of the State of Kuwait

CORPORATE PROFILE

United Gulf Bank

Established in 1980 and operating under a conventional wholesale banking licence from the Central Bank of Bahrain, UGB is the merchant banking arm of the KIPCO Group. A leading asset management and investment banking group headquartered in the Kingdom of Bahrain, its operations span the MENA region. UGB's proprietary investments include assets in real estate, private equity, and quoted securities. As of 31 December 2017, assets under management totalled US$ 10.8 billion (31 December 2016: US$ 10.0 billion).

UGB's core subsidiaries and associates are KAMCO Investment Company (KAMCO), United Gulf Financial Services - North Africa, and United Gulf Realty International, Ltd.

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.

The KIPCO Group

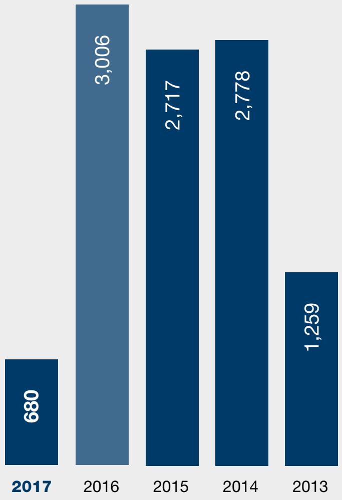
The KIPCO Group is one of the biggest holding companies in the Middle East and North Africa, with consolidated assets of US$ 34.5 billion as at 31 December 2017. The Group has significant ownership interests in over 60 companies operating across 24 countries. The Group's main business sectors are financial 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

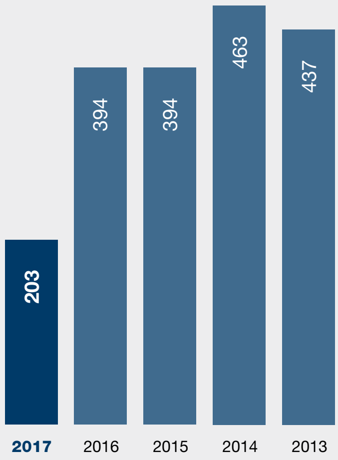
United Gulf Bank B.S.C.
PO Box 5964, Diplomatic Area
UGB Tower, Manama, Kingdom of Bahrain
Tel: (+973) 17 533 233 Fax: (+973) 17 533 137
Email: info@ugbbh.com
www.ugbbh.com
Licensed as a Conventional Wholesale Bank by the Central Bank of Bahrain

FINANCIAL HIGHLIGHTS

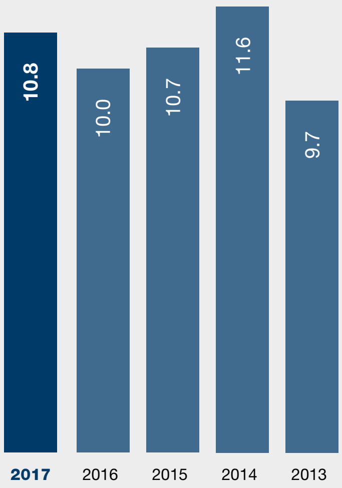
Total Assets
US$ million



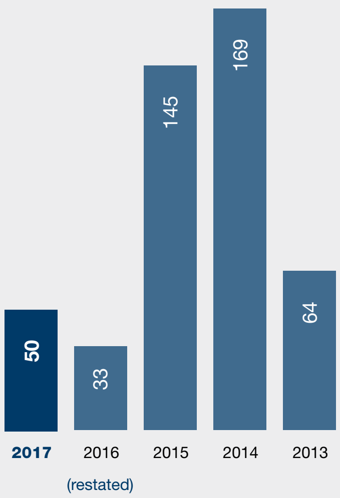
Shareholders' Equity
US$ million



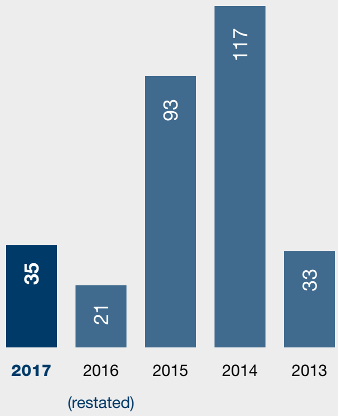
Assets Under Management
US$ billion



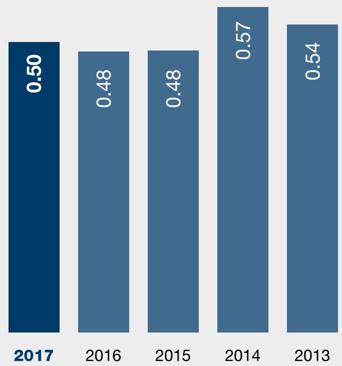
Total Income
US$ million



Operating Income
US$ million



Book Value per Share
US$ cents



US$
680 million

Total Assets

21.5 %

Capital Adequacy Ratio

US$
10.8 billion

Assets Under Management

Income statement amounts for 2016 have been reclassified to conform to the presentation adopted for 2017. Corresponding amounts for 2015, 2014 and 2013 are unchanged (Also refer to Note 2 of the financial statements).

FINANCIAL SUMMARY

US$ million	2017	2016 (Restated)	2015	2014	2013
Total Income	50.3	32.8	144.8	169.1	64.3
Investment income	23.8	9.8	7.7	44.2	20.0
Operating income	35.1	21.1	93.3	117.4	33.0
Shareholders' Equity Attributable to Shareholders of the Parent	203.0	394.0	394.0	462.9	436.3
Total Assets	680.1	3,005.7	2,716.5	2,777.8	1,258.6
Net Income Attributable to Shareholders of the Parent before reclassification adjustment on restructuring	7.9	6.3	11.2	18.8	2.6
%					
Return on Average Equity before reclassification adjustment on restructuring	2.65%	1.59%	2.62%	4.19%	0.58%
Return on Average Assets	0.43%	0.22%	0.41%	0.93%	0.21%
Operating Expense / Operating Income	73%	97.5%	87.3%	58.6%	72.4%
Average Equity to Average Assets	16.2%	13.8%	15.6%	22.3%	35.9%
US$					
Book Value per share	0.5017	0.48	0.48	0.56	0.53

COMPARATIVES AVERAGES BALANCES (based on quarterly averages)

US$ million	2017	2016	2015	2014	2013
Assets	2,508.9	2,990.9	2,645.7	2,617.8	1,258.1
Liabilities	2,031.1	2,455.0	2,122.5	2,056.4	784.6
Minority Interest	86.4	107.0	113.5	99.0	22.8
Shareholders' Equity	391.4	428.9	409.7	462.5	450.7
	2,508.9	2,990.9	2,645.7	2,617.8	1,258.1
Guarantees and commercial LC	49.3	65.3	78.0	145.3	39.4
Commitments	183.2	100.5	62.4	133.9	8.1
Assets Under Management (US$ billion)	10.8	10.0	10.7	11.8	9.3

Income statement amounts for 2016 have been reclassified to conform to the presentation adopted for 2017. Corresponding amounts for 2015, 2014 and 2013 are unchanged (Also refer to Note 2 of the financial statements).

CHAIRMAN'S STATEMENT

During 2017, we substantially completed implementation of UGB's corporate reorganisation and strategic realignment, which aims to optimise capital efficiency and further strengthen the balance sheet. This will help ensure that the Bank maintains adequate capital to meet its growth plans, while keeping pace with a changing regulatory landscape.

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 2017. This proved to be a pivotal year for the Bank, during which we substantially completed implementation of our corporate reorganisation and strategic realignment plan.

Economic Environment

The year 2017 witnessed a general strengthening of the global outlook, with many major economies reporting an improvement in their underlying economic indicators. The tax cuts in the USA are expected to give a further impetus to an economy that has already benefited from the era of quantitative easing. In the Eurozone, the recovery continued to appear robust. While inflation remained under control for most of the year in the advanced economies, concerns of it rising could propel an increasing interest rate regime in 2018.

Oil prices which remained subdued in the beginning of the year, benefited from the OPEC led agreement to reduce production. This concerted move was taken by members and non-members to boost global oil prices and rebalance markets that have been under pressure over the past few years due to lacklustre demand. However, oil analysts feel that 2018 could see some downward pressure on prices from more modest global oil demand growth as well as increasing supplies from the resurgent USA based shale oil producers. In a bid to reduce dependency on the hydrocarbon sector, there is an emphasis by the GCC countries to increase investments in infrastructure and non-oil related industries.

The introduction of VAT (value added tax) in the United Arab Emirates and the Kingdom of Saudi Arabia was yet another move introduced by governments to augment their sources of revenue. This is part of the regime of regulatory change, which has been implemented by regional authorities since commencement of the global crisis in 2008. Introduction of new regulations, both on compliance and capital management, have profound implications on the banking business model. It is consequently becoming increasingly important to understand and adapt to the new regulations.

Corporate Reorganisation

At an extraordinary general assembly meeting held on 25 September 2017, shareholders of UGB approved the corporate reorganisation plan of the Bank, aimed at optimising capital efficiency and further strengthening the balance sheet. Under this plan, the KIPCO Group incorporated a wholly-owned subsidiary – United Gulf Holding Company (UGH) – in Bahrain, which acquired 100 per cent shareholding in UGB in consideration of one UGH share for every two UGB shares.

Following the extraordinary general assembly meeting, UGH was listed on the Bahrain Bourse on 28 September 2017, with UGB being simultaneously delisted. The Bank is in the process of being converted into a closed Bahraini shareholding company. UGB will continue to operate as a conventional wholesale bank licensed by the Central Bank of Bahrain, focused on asset management and investment banking across the MENA region.

Financial Results

In line with our tradition and track record, UGB recorded a good performance in the year ended 2017 despite the challenging circumstances that characterised the year. The Bank reported total income before interest and other expenses of US$ 50.3 million for 2017 compared with US$ 32.8 million for the previous year. Total expenses were US$ 25.6 million versus US$ 20.6 million in 2016. As a result, net profit before reclassification adjustments rose more than ten-fold to US$ 8.4 million from US$ 873 thousand a year earlier. Total assets under management (AUM) as at 31 December 2017 amounted to US$ 10.8 billion, compared with total AUM of US$ 10.0 billion at the end of the previous year.

At the end of 2017, total assets stood at US$ 680.1 million compared with US$ 3.0 billion at the end of 2016. Total equity was US$ 262.9 million against US$ 529.5 million at the end of the previous year. UGB's consolidated capital adequacy ratio improved considerably to 21.5 per cent from 13.9 per cent in 2016, comfortably exceeding the Central Bank of Bahrain's minimum requirement of 12.5 per cent. Liquidity remained healthy, with total liquid assets of US$ 227.6 million representing 33.5 per cent of the balance sheet at the end of the year.

Track Record

Significantly, our financial results for 2017 mark the Bank's 27th consecutive year of operating profitability and the 34th year of positive performance, since its establishment in 1980. This further reinforces UGB's successful track record as a leading asset management and investment banking group in the MENA region.

In June 2017, the international rating agency Capital Intelligence affirmed the long-term and short-term foreign currency ratings (FCRs) of UGB at 'BBB' and 'A3' respectively, with a 'Negative' outlook. The agency cited 'the Bank's strong ownership combined with the demonstrated financial and liquidity support from its parent KIPCO; its ability to repay and refinance maturing debt; and its effective access to term finance.' We regard the affirmation of UGB's ratings as an independent validation of the actions we are taking to realign the Bank's strategic direction, strengthen the balance sheet, and optimise its strong underlying fundamentals.

Subsidiaries and Associates

The main contributors to the share of results from the Bank's subsidiaries and associates for most of 2017 were Burgan Bank, KAMCO Investment Company (KAMCO) and FIMBank. Burgan Bank recorded growth in its operating income, and improved operating efficiency by reducing its operating expenses. The high quality earnings combined with across-the-board efficiencies, enabled the Bank to grow its operating profit by 8 per cent. Asset quality registered significant improvement with the non-performing loans (NPL) ratio declining to reach 2.7 per cent, with a corresponding coverage ratio of 144 per cent. KAMCO posted improved financial results due to a continued focus on strengthening its competitive advantage, and also enhancing its ability to capture profitable and risk-adjusted opportunities. Having achieved considerably improved financial results over the previous year, FIMBank continues to evolve into a stronger banking institution based on sound business discipline, centrally-aligned operations, and effective management of enterprise risks.

Sound Governance

UGB continues to place the highest importance on sound corporate governance and risk management. During 2017, we maintained our compliance with the latest regulatory requirements of the Central Bank of Bahrain while further enhancing our risk management framework to ensure that UGB remains robust and resilient in the face of challenging market conditions.

We also continued to implement the Bank's enduring 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 support for charitable and community-based activities.

Future Outlook

Looking ahead, we expect next year to be yet another highly challenging period for the region, with many of the concerns and issues witnessed in 2017 continuing to affect corporate and investor sentiment. However, the recovery of oil prices during the second half of this year, together with the economic transformation plans being implemented across the region, provide cautious optimism for the immediate future.

Reinforcing this outlook, the World Bank forecasts GDP growth in MENA to improve to 3.0 per cent in 2018 from 1.7 per cent the previous year, based on assumptions of a modest rise in oil prices and a lessening of geopolitical tensions. GCC economies are anticipated to lead stronger growth in the region, supported by easing fiscal adjustment, infrastructure investment and reforms to promote non-oil sector activity.

As a result of our corporate reorganisation, I would like to stress that UGB is in a stronger financial position to withstand the ongoing headwinds of economic and market volatility. The Board has full confidence in the ability of the Management team to adapt to changing market dynamics and seize promising new business opportunities. As such, we remain cautiously optimistic about the Bank's prospects in 2018.

Acknowledgements

On behalf of the Board of Directors, it is with deep gratitude that I acknowledge the immense support and encouragement that we continue to receive from the Government of the Kingdom of Bahrain, the Central Bank of Bahrain, Bahrain Bourse, the Ministry of Industry, Commerce & Tourism, and the various regulatory and supervisory authorities of the different jurisdictions in which UGB operates.

In particular, I would like to thank the team at the Central Bank of Bahrain for the invaluable cooperation and guidance it provided for the corporate restructuring of UGB during the year.

I also gratefully acknowledge the financial support and confidence of our shareholders; the trust and loyalty of our clients; and the collaboration of our business partners. Finally, I pay special 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

BOARD OF DIRECTORS

Masaud M. J. Hayat

Chairman

Chairman of the Executive Committee

Chief Executive Officer, Banking Sector, Kuwait Projects Company (Holding) - Kuwait

Chairman, United Gulf Holding Company - Bahrain

Chairman and Chairman of the Executive Committee, Tunis International Bank - Tunisia

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 plc - Malta

Board Member, Burgan Bank - Kuwait

Board Member, Jordan Kuwait Bank - Jordan

Board Member, KAMCO Investment Company KSC (Public) - Kuwait

Board Member, North Africa Holding Company - Kuwait

Board Member, Mashare'a Al Khair Est. - Kuwait

Over 41 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
Member of the Board Audit Committee

Vice Chairman (Executive), Kuwait Projects Company (Holding) - Kuwait

Chairman, Panther Media Group - Dubai, UAE

Vice Chairman, United Gulf Holding Company - Bahrain

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 2005

Over 31 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 B.S.C. (c) - Bahrain

Chairman, United Gulf Management, Inc. - USA

Board Member, Burgan Bank - Kuwait

Board Member, United Real Estate Company - Kuwait

Director, United Gulf Management Ltd. - UK

Board Member, United Gulf Investments Ltd. - Cayman Islands

Trustee, American University of Kuwait - Kuwait

Member, Corporation Development Committee and 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 41 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 KSC (Public) - Kuwait

Vice-Chairman, Al Daiya United Real Estate Company - Kuwait

Over 21 years of experience in the financial sector

Graduate of the Royal Military Academy, Sandhurst, UK

BSc, Business Administration, New York Institute of Technology, USA

BOARD OF DIRECTORS

Mubarak Mohammed Al-Maskati

Independent Director

Chairman of the Nominating & Remuneration Committee
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 31 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 - Tunisia

Independent Director Assoufid BV - Morocco

Board Member, Manar Interholdings SL - Spain

Founder of Mada Alsharqia Real Estate Development Company, Khobar - Saudi Arabia

Over 31 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
Member of the Nominating & Remuneration Committee

Former Advisor to the Board of Directors, United Gulf Bank BSC - Bahrain

Former Acting Chief Executive and Deputy Chief Executive Officer, United Gulf Bank BSC - Bahrain

Previously served National Bank of Pakistan in Bahrain and in Pakistan, and Investment Corporation of Pakistan, in various management positions

Over 48 years of experience in the financial industry

BSc (Hons), Peshawar University, Pakistan

Diploma in Banking

EXECUTIVE MANAGEMENT

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 21 years, and 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 BSC (c), Bahrain; Global Banking Corporation, Bahrain; United Gulf Financial Services - North Africa, Tunisia; FIMBank plc. - Malta and Assoufid BV, Morocco. 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.

Mohammed Alqumaish CIA CISA MBA

Assistant General Manager, Chief Audit Executive and Corporate Secretary

Mr. Alqumaish joined UGB in September 2001. He has more than 21 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 Director, Board Audit Committee member and Nominating & Remuneration Committee member of Tunis International Bank, Tunisia; Director, Board Audit Committee member and Nominating & Remuneration Committee member of Syria Gulf Bank, Syria; and a Director of Al Ameen Real Estate Investment Company, Iraq. He also serves as an external Board Committee member of Gulf Bank Algeria, Algeria; and Bank of Baghdad, Iraq. A Certified Internal Auditor (CIA) and Certified Information Systems Auditor (CISA), Mr. Alqumaish holds an MBA from the University of Strathclyde Business School, UK.

EXECUTIVE MANAGEMENT

Deepa Chandrasekhar APRM CAMS (FCI) FICA CFE Chartered MCSI

Senior Vice President, Chief Compliance Officer & MLRO

Mrs. Chandrasekhar joined UGB in 2008. She has over 29 years' experience in the areas of risk management, treasury, operations, internal audit and compliance. She holds an MBA degree from the University of Alberta, Canada; as well as several professional certifications. Mrs. Chandrasekhar 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 in the field of compliance and corporate governance, for the Finance Accreditation Agency, Malaysia. Mrs. Chandrasekhar is a frequent speaker at professional forums, and has published several financial articles.

Syed Rehan Ashraf FCA MBA

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 20 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, Pakistan; Faysal Bank, Pakistan; and PriceWaterhouse Coopers, Pakistan. A Chartered Accountant (ACA) from the Institute of Chartered Accountants of Pakistan, Mr. Ashraf holds an MBA from DePaul University of Chicago, USA.

EXECUTIVE MANAGEMENT

Adel Al Arab CRA

Senior Vice President, Head of Operations

Mr. Al Arab joined UGB in 1994. He has over 21 years of experience in the field of operations, credit and risk management. Mr. Al Arab holds a Bachelor of Science 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.

Nirmal Parik CFA MBA

Vice President, Head of Asset Management & Investment Banking

Mr. Parik joined UGB in 2007. He was appointed Head of Asset Management & Investment Banking in October 2015. He has more than 15 years of experience in the financial services industry in investment banking, asset management and corporate banking. Prior to joining UGB, Mr. Parik worked in various capacities with multinational firms including ING Investment Management (I) Pvt. Ltd., the asset management arm of ING Group NV, Netherlands; 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.

EXECUTIVE MANAGEMENT

Abbas Al Tooq APRM MBA

Assistant Vice President, Head of Credit & Risk Management

Mr. Al Tooq joined UGB in 1999. He assumed the role of Head of the Credit and Risk Management in October 2015. He has more than 21 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; and is an Associate Professional Risk Manager (APRM) from the Professional Risk Managers International Association.

Hamid Al Hashimi

Vice President, Head of Treasury

Mr. Al Hashimi joined UGB in March 2017. He has over 15 years of experience within Treasury, across all asset classes including structuring, sales and trading; as well as a syndication team leader 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. He holds a Bachelor’s Degree with Honours 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 Treasury.

BUSINESS REVIEW

STRATEGY AND BUSINESS OVERVIEW

The strategic objective of United Gulf Bank is to create the MENA region's premier asset management, merchant banking and investment banking group. UGB seeks to be the preferred gateway to the region for its clients and global partners through the delivery of both conventional and Sharia'h-compliant 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 and associate companies, UGB engages primarily in asset and fund management, investment banking, private equity and corporate banking. Other business activities include proprietary investments, 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 merger 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.

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

Brokerage

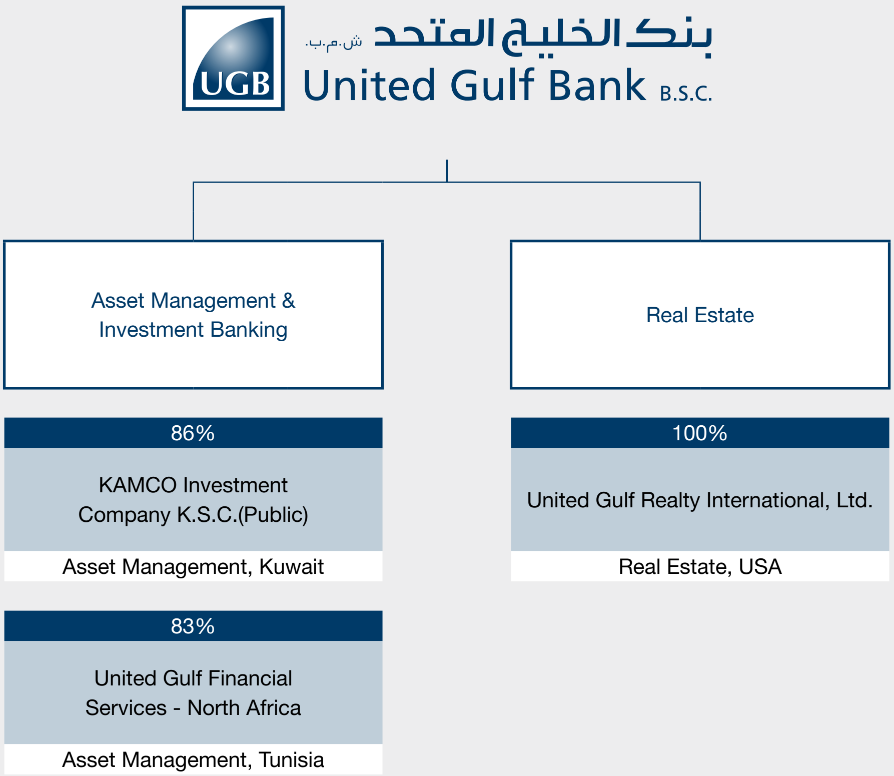
UGB provides financial brokerage services for overseas clients who wish to trade on shares listed on the Bahrain Bourse. The Bank also provides clients with access to the Kuwait Stock Exchange through its affliate, Al Sharq Financial Brokerage Company.

KEY BUSINESS DEVELOPMENTS AND INITIATIVES IN 2017

- UGB completed its restructuring whereby regulated banking activities were segregated from core business.
- UGB's assets under management stood at US$ 10.8 billion at the end of 2017 compared with US$ 10.0 billion at the end of the previous year.
- The main contributors to the share of results from the Bank's subsidiaries and associates for most of 2017 were Burgan Bank, KAMCO Investment Company (KAMCO) and FIMBank plc.
- The Bank increased the capital of United Gulf Realty International, Ltd. USA – a fully leased prime income generating commercial property – and continued to be actively involved in its day-to-day management, with the aim of continuing to enhance the overall value of the investment.
- UGB made an additional investment in Tunis International Bank and participated in the capital increase of Hannibal Lease, a car leasing company in Tunisia.

BUSINESS REVIEW

UGB SUBSIDIARIES AND ASSOCIATES



UGB consolidated holdings, as at 31 December 2017

SUBSIDIARIES & ASSOCIATES

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

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. The Company won the 'Best Investment Research Company - Kuwait' award for 2017 from World Finance. Other key developments in 2017 include acting as the acquisition advisor to Qurain Petrochemical Industries Company KSCP in its successful acquisition of 20.5 per cent of National Petroleum Services Company KSCP; and acting as the Joint Lead Manager and Book Runner for the Tier 1 Basel III compliant USD 250 million sukuk issuance by Warba Bank KSCP. At the end of 2017, the Company had total client AUM of over US$ 11 billion (KWD 3.37 billion). UGB owns 86 per cent of KAMCO, which is listed on the Kuwait Stock Exchange.

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

Consolidated Subsidiary based in Tunisia

Commencing operations in 2009, UGFS-NA is an asset management company regulated by the Tunisian Capital Market Authority – Conseil du Marché Financier. 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 83 per cent in UGFS-NA, whose shares are unlisted.

United Gulf Realty International, Ltd.

Consolidated Subsidiary based in USA

UGRIL was incorporated in the British Virgin Islands in March 2012. The Company's wholly owned subsidiary, Federal Street 176 Holdings, Inc., was incorporated in April 2012. In June 2012, UGRIL (through its subsidiary) acquired 100% ownership in a commercial real estate property located in the financial district submarket in Boston, USA. It was originally constructed in 1901 and underwent a significant renovation in 1986. UGB has a total consolidated interest of 100% per cent in UGRIL, whose shares are unlisted.

BUSINESS REVIEW

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 continued to build upon its successful track record and benefit from KIPCO Group synergies, increasing the number of counterparty relationships with both conventional and Sharia'h-compliant institutions. Treasury adopted a more proactive approach, with a focus on reviving dormant relationships and also introduced new hedging instruments. Deposits from customers totalled US$ 31 million in 2017, reflecting UGB's strong reputation in the market. The Bank retained a robust balance sheet with an improved consolidated capital adequacy ratio (CAR) of 21.54 per cent, comfortably higher than the Central Bank of Bahrain's minimum requirement of 12.5 per cent. Liquidity remained healthy, with total liquid assets of US$ 227.6 million representing 33.5 per cent of the balance sheet at the end of the year. During 2017, UGB repaid financing facilities with regional banks totalling US$ 265 million, raised additional financing of US$ 375 million, and extended the maturity profile of its liabilities by up to three years.

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. Key developments in 2017 included collaborating with Information Technology in migrating the SWIFT system to a new internet based platform in line with SWIFT security and control regulations of the Central Bank of Bahrain (CBB). Operations also worked closely with Compliance in the preparation of new FATCA and CRS related reports requested by the CBB.

Human Resources

UGB places the highest importance on the professional development of its people. During 2017, focus was placed on building leadership skills and investing in future leaders, as well as supporting the professional and personal development of all employees. This entailed 29 per cent of staff completing 198 hours of mandatory continuous professional development (CPD) and 31 per cent attending courses at the Bahrain Institute of Banking & Finance (BIBF). The Bank also continued to encourage and support staff to obtain appropriate professional qualifications and certification. Mandatory regulatory-related training, such as Anti-Money Laundering and Code of Conduct was conducted in-house for all staff; together with an occupational health and safety workshop. The Bank's merit-based Mashare'a Al Khair Scholarship Programme continued to assist dependants of Bank staff to obtain degrees from accredited colleges, universities or other academic institutions during the year. UGB also continued to support women's empowerment. At the end of the year, female employees accounted for 35 per cent of the total workforce and 20 per cent occupied managerial positions.

Information Technology

During 2017, UGB continued to invest in further strengthening and enhancing its information and communications technology framework. In light of increasing cyber attacks, external consultants completed an assessment of 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 2017 in line with regulatory requirements of the 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 addition, a vendor was appointed for the implementation of a new core banking system in 2018.

FINANCIAL REVIEW

This review provides a detailed description of the financial performance of United Gulf Bank ("UGB" or "the Bank") for the year ended 31 December 2017.

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.

RESTRUCTURING

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

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

As at 31 December 2017, UGH is the Bank's parent company and holds 100% shares of UGB, with KIPCO being the ultimate parent company owning 98% of UGH's outstanding shares on a consolidated basis.

Accordingly, certain 2016 figures have been reclassified to conform to the presentation adopted in 2017. Such reclassification did not affect the previously reported net profit or the total equity of the Bank.

REVENUES

UGB's total revenues were US$ 50.3 million in 2017 compared with US$ 32.8 million in 2016 as indicated below:

Total Revenues US$ million	2017	2016 (restated)
Financial Services	(1.9)	1.1
Real Estate	7.5	4.3
Other Associates	(1.0)	1.6
Fees and commissions	2.3	(0.8)
Management fees from fiduciary activities	16.0	13.2
Advisory fees	7.2	7.4
Interest Income	4.4	3.3
Realised gain on non - trading investments	4.4	0.9
Trading gain / (loss)	3.9	(3.6)
Dividend	1.9	1.8
Gain on sale of associates and subsidiaries	2.7	2.8
Gain on sale due to reclassification of investment	3.0	-
Foreign currency translation (losses) - net	(0.4)	(3.9)
Other income	0.3	4.7
Total	50.3	32.8

During 2017, the increase in total revenues was mainly attributed to trading gains from recovering regional stock markets, lower foreign currency losses, realised gain on the sale of associates and available for sale investments and higher fee and commissions income. The impact was partially offset by lower income from financial services, share of results from associates, and other investment related income.

FINANCIAL REVIEW

Financial Services

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

Results from financial associates recorded a loss of US$ 1.9 million compared with an income of US$ 1.1 million in 2016. The decrease was mainly due to a loss incurred by the KAMCO Investment Fund, which was classified as an associate in 2017.

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

Revenue - Financial Associates US$ million	2017	2016 (restated)
Al Sharq Financial Brokerage Co.	0.1	(0.1)
KAMCO Investment Fund	(1.8)	-
Manafae Investment Company	(0.2)	1.2
Total	(1.9)	1.1

Real Estate

UGB's real estate revenues were derived mainly from rental income from real estate properties in Bahrain, Kuwait and the USA. The increase was mainly due to a US$ 2.7 million unrealised gain on investment properties in the USA.

Revenues - Real Estate US$ million	2017	2016 (restated)
KAMCO Real Estate Yield Fund	-	0.3
N.S. 88	-	0.7
Rental income	4.8	3.3
Unrealised gain on investment properties	2.7	-
Total	7.5	4.3

Other Associates

Profits from other associates of UGB decreased from a profit of US$ 1.6 million in 2016 to a loss of US$ 1.0 million in 2017.

Revenues: Non-financial Associates US$ million	2017	2016 (restated)
United Capital Transport Company	(2.1)	1.3
Kuwait Education Fund	1.1	0.3
Total	(1.0)	1.6

Fees and Commission Income

Credit related fees and commission income increased to US$ 2.3 million in 2017 from a net expense of US$ 0.8 million in 2016, mainly due to mandates at the UGB level with its Group companies.

Management Fees from Fiduciary Activities

Management fees increased from US$ 13.2 million in 2016 to US$ 16.0 million in 2017, after regional stock markets stabilised during the year resulting in performance and management fees on fiduciary assets. The increase was mainly from mandates at the KAMCO level.

Advisory Fees

Advisory fee income decreased moderately to US$ 7.2 million in 2017 from US$ 7.4 million in 2016.

Interest Income

The main source of interest income for UGB was derived from interbank placements. Interest income increased from US$ 3.3 million in 2016 to US$ 4.4 million in 2017, mainly due to the increase in LIBOR and higher interbank placements at UGB during Q4 2017.

Trading gains / losses

Trading positions recorded a profit of US$ 3.9 million in 2017 compared with a loss of US$ 3.6 million for 2016. Trading gains were recorded mainly due to the recovery of regional stock markets during the year.

Dividend Income

Dividend income increased marginally to US$ 1.9 million in 2017 compared with US$ 1.8 million in 2016.

Foreign Currency Translation Losses

Foreign currency translation losses of US$ 0.4 million were recorded in 2017 compared with losses of US$ 3.9 million in 2016. This was attributed mainly to the appreciation of the Kuwaiti Dinar and Euro during the year.

EXPENSES

Interest Expense

Interest expense increased from US$ 11.7 million in 2016 to US$ 15.2 million in 2017, mainly due to the increase in LIBOR by 75 bps during the year and new deposits from KIPCO, UGH and FIMBank plc.

Operating Expenses

Operating expenses increased by 24% to US$ 25.6 million in 2017 compared with US$ 20.6 million in 2016. Salaries and benefits increased to US$ 15.9 million (2016: US$ 12.6 million) largely due to higher salary expenses at KAMCO level following the opening of a new office at the Dubai International Financial Centre (DIFC). A slight increase of US$ 0.3 million in UGB's salary expenses was due to indemnity accruals for staff completing 10 years of service and normal increments.

General and administration expenses increased to US$ 9.7 million (2016: US$ 8.0 million). This originated mainly from KAMCO due to an increase in depreciation on office refurbishments during the year, an increase in consultancy fees, and additional administrative expenses at the office in the DIFC.

FINANCIAL REVIEW

Operating expenses US$ million	2017	2016 (restated)
Salaries and benefits	15.9	12.6
General and administrative expenses	9.7	8.0
Total	25.6	20.6

Taxation

A net income tax expense of US$ 1.0 million was recorded in 2017 compared with US$ 0.02 million in 2016. The Income tax expenses for 2017 related mainly to tax expense booked at United Gulf Realty International, Ltd.

Provisions

UGB made total provisions of US$ 3.4 million in 2017 compared with US$ 2.0 million in 2016. Provisions for 2017 mainly resulted at UGB due to collective impairment provisions on loans and advances, and certain available for sale investments.

Provisions for impairment US$ million	2017	2016 (restated)
Impairment loss on investments	0.5	2.9
Provision for doubtful loans and other assets - net	2.9	(0.9)
Total	3.4	2.0

Net income from discontinued operations

As part of UGB's restructuring plan, beneficial interest in some of the Bank's core assets such as Burgan Bank, FIMBank and URC, were transferred to UGH during the beginning of the fourth quarter of 2017.

Accordingly, income earned by UGB from these assets during the years ended 31 December 2016 and 31 December 2017 have been reclassified under Income from Discontinued Operations. Moreover, interest expenses on medium-term facilities held by UGB until 3Q17 and transferred to UGH in 4Q17, have also been reclassified to Discontinued Operations. Income and expenses for 4Q17 from the above assets and medium-term facilities are accounted for normally in UGH's financial statements.

Net Income Attributable to Parent before reclassification adjustments

Net income attributable to parent before reclassification adjustments in 2017 increased to US$ 8.4 million from US$ 0.9 million in 2016.

Reclassification adjustment

As part of the Group's restructuring, foreign currency losses of US$ 27.9 million and fair value losses of US$ 59.8 million were transferred to the consolidated statement of income.

CONSOLIDATED BALANCE SHEET

Consolidated Assets

UGB's consolidated assets stood at US$ 680.1 million at the end of 2017 compared with US$ 3,005.7 million at the end of 2016. A comparison of the two years is provided below:

Assets US$ million	2017	2016
Demand and call deposits with banks	98.0	176.9
Placements with banks	68.6	187.4
Investments carried at fair value through statement of income	19.3	45.2
Non-trading investments	221.6	404.4
Loans and receivables	4.2	1,184.8
Other assets	31.7	112.7
Investments in associates	77.5	709.0
Investment properties	105.1	101.3
Property and equipment	1.7	32.1
Goodwill	52.4	51.9
Total	680.1	3,005.7

Demand, Call and Placements with Banks

Demand, call and placements with banks were US$ 166.6 million in 2017 compared with US$ 364.3 million in 2016, as liquid funds at FIMBank were consolidated in UGH as of 31 December 2017. Total liquid assets – comprising cash, deposits, liquid securities and other assets, represented 33.5% of the balance sheet as at year end 2017 (2016: 20.7%).

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

Investments carried at fair value through the statement of income were US$ 19.3 million in 2017 compared with US$ 45.2 million in 2016. This portfolio mainly comprises quoted equity and debt 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 were US$ 221.6 million in 2017 compared with US$ 404.4 million in 2016. The total portfolio mainly comprises listed equities of US$ 42.1 million (2016: US$ 57.8 million), unlisted equities of US$ 143.1 million (2016: US$ 121.3 million), other managed funds of US$ 36.1 million (2016: US$ 51.5 million), real estate managed funds of US$ 0.3 million (2016: US$ 12.0 million) and quoted debt securities of US$ nil million (2016: US$ 161.8 million).

The major investments classified under the non-trading investments portfolio as at 31 December 2017 were:

FINANCIAL REVIEW

Advanced Technologies Company (ATC): UGB acquired a 9.8% stake in ATC during 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. During the year, 4.6% stake in ATC was transferred to UGH as part of the restructuring.

Assoufid B.V.: 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.

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 2017, UGB owned an equity stake of 1.2% (2016: 1.2%) in Kuwait Energy plc.

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 Kuwait Stock Exchange. 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% (2016: 8.9%).

Al Sharq Financial Brokerage Company: During the year, the Group's effective interest in Al Sharq Financial Brokerage Company K.S.C. (Closed) ("Al Sharq") through its subsidiary KAMCO was diluted to 7.33% as a result of subscription of rights issue by the other shareholders. Accordingly, upon loss of significant influence, the Group has reclassified its investment in Al Sharq to financial assets available for sale.

Loans and Advances

Loans and advances in 2017 amounted to US$ 4.2 million (2016: US$ 1,184.8 million).

Details of the loan book are as follows:

Loans and Advances US$ million	2017	2016
Forfaiting assets	-	538.2
Factoring assets	-	220.6
Loans to customers	4.1	168.6
Loans to banks	-	173.8
Syndication loans	-	124.0
Staff loans	2.6	3.1
Gross loans and advances	6.7	1,228.3
Less: Provision for impairment	(2.5)	(43.5)
Total	4.2	1,184.8

Past due and impaired loans amounted to US$ nil million (2016: US$ 70.5 million) against which provisions of US$ 2.5 million (2016: US$ 43.5 million) were recorded. This was reduced due to transfer of FIMBank plc to UGH.

Investments in Associated Companies

Investments in UGB's associated companies decreased to US$ 77.5 million in 2017 compared with US$ 709 million in 2016, mainly due to the sale of the Bank's core investments to UGH. UGB's associated companies contributed a total loss of US$ 2.9 million in 2017 (2016: profit of US$ 3.8 million), with key contributors being United Capital Transport Company (US$ 2 million loss), KAMCO Investment Fund (US$ 1.8 million loss) and Kuwait Education Fund (income of US$ 1.1 million).

Investment Properties

UGB's investment properties mainly comprise real estate properties in Kuwait, United States of America and the Kingdom of Bahrain. Rental income on these investments amounted to US$ 4.8 million (2016: US$ 3.3 million).

FINANCIAL REVIEW

Consolidated Liabilities

UGB's consolidated liabilities decreased to US$ 417.2 million in 2017 from US$ 2,476.3 million in 2016 as all medium-term facilities were transferred to UGH as part of the restructuring exercise, as well as FIMBank's liabilities being consolidated in UGH.

Liabilities US$ million	2017	2016
Due to banks and other financial institutions	250.2	726.2
Deposits from customers	31.0	985.2
Loans payable	98.7	652.2
Subordinated debt	-	50.0
Other liabilities	37.3	62.7
Total	417.2	2,476.3

Total Equity

During the year, as part of the overall Group restructuring, the Bank reduced its share capital by 410,622,078 shares (US$ 107,519 thousand). The issued and fully paid up share capital as of 31 December 2017 comprised 404,526,082 shares of US$ 0.25 each (2016: 834,602,295 shares of US$ 0.25 each). As at 31 December 2017, UGB's equity stood at US$ 262.9 million (2016: US$ 529.5 million).

Equity US$ million	2017	2016
Share capital	101.1	208.7
Treasury shares	-	(18.1)
Share premium	5.7	11.5
Statutory reserve	49.9	100.5
General reserve	29.6	81.0
Treasury share reserve	-	14.2
Fair value reserve	12.9	(50.0)
Foreign currency translation reserve	(3.9)	(37.5)
Retained earnings	7.7	83.7
Capital and reserves attributable to the shareholders of the parent	203.0	394.0
Perpetual Tier 1 capital	33.0	33.0
Non-controlling interests in equity	26.9	102.5
Total Equity	262.9	529.5

The major movements in equity from 31 December 2016 to 31 December 2017 were:

- Net profit before reclassification adjustments of US$ 7.9 million
- Positive fair value reserve movement of US$ 3.0 million
- Positive FX revaluation reserve movement of US$ 5.7 million mainly due to appreciation of the Kuwaiti Dinar
- Capital reduction by US$ 211.6 million
- Interest payment of US$ 3.5 million on the Bank's Additional Perpetual Tier 1 Capital

The minority interest decreased by US$ 76.7 million mainly due to the transfer of FIMBank to UGH.

Assets and Liabilities transferred to UGH

The major classes of assets and liabilities transferred to UGH during 2017 were as follows:

Assets US$ million	2017
Demand and call deposits with banks	229
Placements with banks	38
Non-trading investments	125
Loans and receivables	1,041
Other assets	74
Investments in associates	606
Property and equipment	30
Assets transferred	2,145
Liabilities	
Due to banks and other financial institutions	322
Deposits from customers	811
Loans payable	617
Subordinated debt	50
Other liabilities	25
Liabilities transferred	1,825
Net assets transferred	320

FINANCIAL REVIEW

OFF-BALANCE SHEET COMMITMENTS

UGB's off-balance sheet commitments comprise guarantees, undrawn investment commitments; 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$ 4.8 million as at 31 December 2017 (2016: US$ 199.2 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 26 to the Consolidated Financial Statements for the year ended 31 December 2017.

CAPITAL ADEQUACY

UGB's consolidated capital adequacy ratio of 21.5% at 31 December 2017 (2016: 13.9%) under the Basel III regulations as mandated by the Central Bank of Bahrain, was above the minimum requirement of 12.5%.

US$ million	2017	2016
Capital base:		
Tier 1 capital	188.66	264.12
Tier 2 capital	3.43	73.75
Total capital base (a)	192.09	337.87
Credit risk weighted exposure	750.07	2,227.19
Market risk weighted exposure	54.40	122.73
Operational risk weighted exposure	87.46	84.64
Total risk weighted exposure (b)	891.94	2,434.56
Capital adequacy (a/b * 100)	21.5%	13.9%
Minimum requirement	12.5%	12.5%

RISK MANAGEMENT REVIEW

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 2017

- Meetings were held with the Central Bank of Bahrain (CBB) regarding UGB's capital optimisation strategy and corporate reorganisation plan. These were subsequently approved by the CBB and UGB shareholders at an extraordinary general assembly held on 25 September 2017.
- UGB maintained its focus on operational consolidation and strengthening liquidity in order to achieve financial efficiency across Bank-wide operations.
- The Bank continued to monitor the recent implementation of a new custom-designed Enterprise Risk Management (ERM) system, which enhances 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.
- 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 2017, 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.

RISK MANAGEMENT REVIEW

Risk Type	Risk Management Philosophy
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 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 nil as at 31 December 2017 (2016: US$ 70.5 million) against which a provision of US$ 2.5 million exists as at 31 December 2017 (2016: US$ 43.5 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

RISK MANAGEMENT REVIEW

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 the 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 28(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 28(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 28 (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.

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

RISK MANAGEMENT REVIEW

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'h 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 2017, UGB's solo liquidity ratio was 36% (2016: 35%).The Bank monitors this on a daily basis to ensure that the regulatory level 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 2017 is detailed in Note 28(d) of the Consolidated Financial Statements. As of this date, 38% of total assets and 89% of total liabilities were contracted to mature within one year (2016: 60% and 86% respectively). A significant portion of assets with longer term maturities comprise readily realisable securities or listed assets with active markets. A significant portion of liabilities with short term contractual maturities comprise of term deposits from KIPCO Group entities that are expected to roll-over.

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.

RISK MANAGEMENT REVIEW

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 and, for special assignments documentation, the Bank involves local and international law firms. 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 2017, several meetings were held with the CBB in which UGB submitted its capital optimisation strategy and corporate reorganisation plan, which were subsequently approved by shareholders at an extraordinary general assembly meeting.

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 the proposed corrective action.

Internal Capital Adequacy Assessment Process

The Internal Capital Adequacy Assessment Process (ICAAP) is a requirement of 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 subordinated long-term debt.

Capital Management

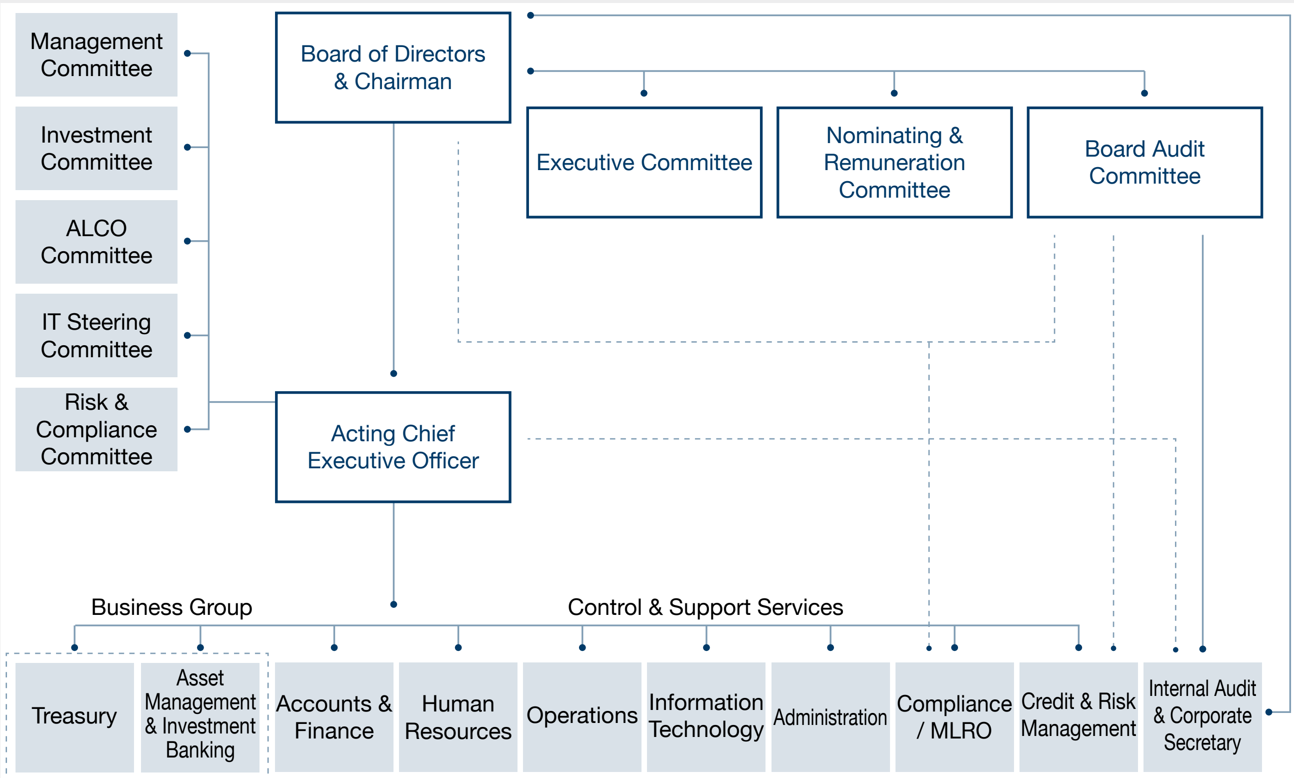
The Board of Directors of the Bank is responsible for ensuring that adequate levels of capital are maintained at all times. The Board also approves and oversees the processes adopted for capital management by the Bank.

CORPORATE GOVERNANCE REVIEW

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 Management 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 2017

Throughout the year, UGB continued to take steps to ensure compliance with 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 2017 comprised:

- Preparation of the required regulatory documentation for the corporate restructuring plan, covering the change in ownership to United Gulf Holding (UGH); share swap with UGH; conversion of UGB to a closed Bahraini shareholding company and reduction in the Bank's capital; the delisting of UGB from the Bahrain Bourse; and the regulatory aspects pertaining to the transfer of certain core assets managed by UGB to UGH.
- UGB signed a service level agreement (SLA) with UGH to provide shared services covering Financial Control, Treasury, Operations, Human Resources and Information Technology; and control functions comprising Compliance, Credit & Risk Management and Internal Audit.
- Compliance and Internal Audit collaborated in the development of a new automated system to act as a repository of all corporate governance-related Board and Management Committee agendas, minutes, supporting documentation, and Members' profiles and attendance records. The system is currently work in progress.
- To ensure compliance with the new Common Reporting Standards (CRS) introduced by the CBB, the Bank realigned its Know-Your-Customer (KYC) procedures, and also expanded its FATCA forms to capture the necessary information.

CORPORATE GOVERNANCE REVIEW

- A new Customer Database was developed in-house to act as a repository of all customer data, with a special emphasis on capturing beneficial ownership of entities (including Treasury counterparties) in accordance with new AML requirements of the CBB. The new system will facilitate provision of timely information and regular risk assessments. It is currently in the testing phase and is envisaged to be fully functional by year-end 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 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. 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. The RiskNucleus Compliance system is used proactively by all departments who receive automated e-mail alerts on forthcoming deadlines and activities.

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 Regulatory Sandbox; Financing-based and Equity-based Crowdfunding Directives; Secured Transactions Law; Internal Audit; and proposed methodology for calculating Financial Penalties.

ANTI-MONEY LAUNDERING

UGB has a designated Money Laundering Reporting Officer (MLRO) and a Deputy MLRO (DMLRO) who are Controlled Persons approved by 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 annually 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 Reuter's 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 audited annually by the independent external auditors for UGB and its main subsidiaries. Their separate assurance report is 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

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 II have also been uploaded under 'Investor Relations'. The Bank's Corporate Governance Report, as well as incorporation documents, are also available on UGB's website.

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 REVIEW

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 2017, 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:

- **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 20 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, who has supported this competition for the past 16 years by sponsoring one of the participating schools, became a Gold Sponsor in 2017. The UGB-supported school team won second place in the 2017-2018 competition. The Bank's Chief Compliance Officer is actively involved in working with the students, and guiding them through the elements of investing and risk management.

- **Mashare'a Al Khair Scholarship Programme**

  This 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 continuous 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 supported 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 2017, contributions were also made to entities that are committed to protecting the environment and raising awareness about women's cancer.

REPORT OF THE BOARD OF DIRECTORS

The Board of Directors is pleased to submit its report and the audited consolidated financial statements of United Gulf Bank ("the Bank" or "UGB") for the year ended 31 December 2017.

Principal activities and review of business developments

The principal activities of the Bank and its subsidiaries (together the "Group") comprise investment and commercial banking. Investment banking including 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.

Restructuring

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

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

Results for the year

For the year ended 31 December 2017, the Bank earned a net profit before reclassification adjustments of US$ 8.4 million and total operating income of US$ 50.3 million. Reclassification adjustments include foreign currency losses of US$ 27.9 million and fair value losses of US$ 59.8 million that were reclassified to the consolidated statement of income as part of the Group's restructuring.

As of 31 December 2017, total assets of the Group were US$ 680.1 million with total equity of shareholders at US$ 203.0 million.

Appropriations for the year

As the Bank suffered a net loss after reclassification adjustments, no transfer were made to the Bank's Statutory Reserves for the year ended 31 December 2017.

Auditors

Ernst & Young have expressed their willingness to continue in office and a resolution for their appointment as auditors of the Bank for the year ending 31 December 2018 has been put for approval by the Shareholders.

Signed on behalf of the Board of Directors

Masaud Hayat
Chairman

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

REPORT ON THE AUDIT OF THE CONSOLIDATED FINANCIAL STATEMENTS

Opinion

We have audited the accompanying consolidated financial statements of United Gulf Bank B.S.C. (c) ("the Bank") and its subsidiaries (together "the Group"), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statements of income and other comprehensive income, cash flows and changes in equity for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017 and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other information included in the Group's 2017 annual report

Other information consists of the information included in the Group's 2017 Annual Report, other than the consolidated financial statements and our auditor's report thereon. The Board of Directors is responsible for the other information. Prior to the date of this auditors' report, we obtained the Directors' report which forms part of the annual report, and the remaining sections of the annual report are expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information obtained prior to the date of the auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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.

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

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

- 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.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

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

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

b) the financial information contained in the Report of the Board of Directors is consistent with the consolidated financial statements;

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

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

Ernst & Young

Partner's registration no. 121

27 February 2018

Manama, Kingdom of Bahrain

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

At 31 December 2017

	Note	2017 US$ 000	2016 US$ 000
ASSETS			
Demand and call deposits with banks		97,993	176,880
Placements with banks		68,577	187,350
Investments carried at fair value through statement of income	5	19,268	45,178
Non-trading investments	6	221,566	404,436
Loans and receivables	7	4,216	1,184,804
Other assets	8	31,820	112,735
Investments in associates	9	77,512	709,043
Investment properties	10	105,093	101,326
Property and equipment		1,679	32,117
Goodwill	11	52,390	51,868
TOTAL ASSETS		680,114	3,005,737
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks and other financial institutions		250,211	726,222
Deposits from customers		31,018	985,210
Loans payable	13	98,658	652,125
Subordinated debt	14	-	50,000
Other liabilities	15	37,358	62,724
TOTAL LIABILITIES		417,245	2,476,281
EQUITY			
Share capital	16	101,132	208,651
Treasury shares	16	-	(18,131)
Share premium	16	5,687	11,459
Statutory reserve	16	49,881	100,514
General reserve	16	29,612	80,999
Treasury shares reserve	16	-	14,248
Fair value reserve	17	12,867	(49,966)
Foreign currency translation reserve	16	(3,871)	(37,476)
Retained earnings		7,659	83,711
CAPITAL AND RESERVES ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT		202,967	394,009
Perpetual Tier 1 capital	18	33,000	33,000
Non-controlling interests in equity		26,902	102,447
TOTAL EQUITY		262,869	529,456
TOTAL LIABILITIES AND EQUITY		680,114	3,005,737

Masaud Hayat
Chairman

Faisal Al Ayyar
Vice Chairman

Hussain Lalani
Acting Chief Executive Officer

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

CONSOLIDATED STATEMENT OF INCOME AND OTHER COMPREHENSIVE INCOME

For the year ended 31 December 2017

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

Masaud Hayat
Chairman

Faisal Al Ayyar
Vice Chairman

Hussain Lalani
Acting Chief Executive Officer

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

CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2017

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

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

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2017

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

1 INCORPORATION AND PRINCIPAL ACTIVITIES

Incorporation

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

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

Activities

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

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

Restructuring

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

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

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

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

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

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

Basis of preparation

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

Presentation and functional currency

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

Certain of the prior year figures have been reclassified to conform to the presentation adopted in the current year. Such reclassification did not affect the previously reported net loss or the total equity of the Company. For more details, please refer to the paragraph on Restructuring in note 1 above.

New and amended standards and interpretations

The accounting policies used in the preparation of these consolidated financial statements are consistent with those used in previous year, except for the adoption of the following amendments to IFRS, applicable to the Group, and which are effective from 1 January 2017:

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2.1 Standards effective for the year

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

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

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

Annual Improvements 2012-2016 Cycle
These improvements include:

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

Significant accounting policies are set out below:

Principles of consolidation

The consolidated financial statements include the financial statements of the Bank and its subsidiaries as at 31 December 2017. The reporting dates of the subsidiaries and the Bank are identical and the subsidiaries' accounting policies conform to those used by the Bank for like transactions and events in similar circumstances.

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

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Principles of consolidation (continued)

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

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 2017	Ownership at 31 December 2016	Year of incorporation
Held directly				
KAMCO Investment Company K.S.C.P. [KAMCO]	Kuwait	86%	86%	1998
United Gulf Financial Services Company-North Africa	Tunisia	83%	85%	2008
United Gulf Realty International, Ltd [UGRIL]	British Virgin Islands	100%	100%	2012
FIMBank Group [FIMBank]	Malta	0%	61%	1994
Hatoon Real Estate Company	Kuwait	0%	98%	2008
Syria Gulf Investment Company	Syria	0%	99%	2007
Held through KAMCO				
Al Dhiyafa United Real Estate Company W.L.L.	Kuwait	100%	100%	2007
Al Jazi Money Market Fund	Kuwait	51%	48%	2007
Al Tadamon United Holding Co	Kuwait	96%	0%	2017
Al Zad Real Estate W.L.L.	Kuwait	99%	99%	2007
Bukeye Power Project Advisory Co	U.S.A.	50%	0%	2017
Bukeye Power Project Manager Ltd	Jersey	100%	0%	2017
Flint Advisor Company Llc	Jersey	46%	0%	2017
Flint Manager Ltd	U.S.A.	100%	0%	2017
Kamco GCC Opportunistic Fund	Kuwait	100%	100%	2013
KAMCO Investment Company (DIFC) Limited	U.A.E.	100%	100%	2016
KAMCO Mena Plus Fixed Income Fund	Kuwait	71%	51%	2016
Kuwait Private Equity Opportunity Fund	Kuwait	73%	71%	2004
Nawasi United Holding Co	Kuwait	96%	0%	2017
North Africa Real Estate Co.	Kuwait	100%	100%	2014
Orange Real Estate Co. W.L.L.	Kuwait	0%	100%	2005
Held through FIMBank				
India Factoring and Finance Solutions Private Limited	India	0%	86%	2010
CIS Factors Holdings B.V.	Russia	0%	100%	2009
FIM Holdings (Chile) S.p.a.	Chile	0%	100%	2014
Latam Factors S.A.	Chile	0%	51%	2014
London Forfaiting Company Limited	U.K.	0%	100%	2009
London Forfaiting International Limited	U.K.	0%	100%	2009
London Forfaiting Americas Inc.	U.S.A	0%	100%	2009
London Forfaiting do Brasil Ltd.	Brazil	0%	100%	2009
FIM Factors B.V.	Netherlands	0%	100%	2009
Menafactors Limited	U.A.E.	0%	100%	2009
FIM Business Solutions Limited	Malta	0%	100%	2009
FIM Property Investment Limited	Malta	0%	100%	2010
The Egyptian Company for Factoring S.A.E.	Egypt	0%	100%	2016

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 consolidated statement of income.

Goodwill

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

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

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

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

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

Investments in associates

An associate is an entity over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

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

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

Under the equity method, the investment in an associate is initially recognised at cost. The carrying amount of the investment is adjusted to recognise changes in the Group's share of net assets of the associate since the acquisition date. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investments in associates (continued)

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

The financial statements of associates are prepared for the same reporting period as that of the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

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

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

Fair value measurement

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

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible to by the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

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

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

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

Level 2: valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable; and

Level 3: valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

For assets and liabilities that are recognised in the consolidated financial statements on a recurring basis, the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Fair value measurement (continued)

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

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

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

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

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

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

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

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

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

Investments carried at fair value through statement of income

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

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

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

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

Non-trading investments

These are classified as follows:

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Non-trading investments (continued)

Held to maturity

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

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

Investments available-for-sale

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

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

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

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

Loans and receivables

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

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

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

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

Derivatives and hedge accounting

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Derivatives and hedge accounting (continued)

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

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

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

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

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

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

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

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

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

Investment properties

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Investment properties (continued)

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

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

Property and equipment

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

Financial liabilities

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

Treasury shares and treasury share reserve

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

Cash and cash equivalents

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

Fiduciary assets

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

Dividends on ordinary shares

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

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

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

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

Taxes

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

Deferred Tax

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Taxes (continued)

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.

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 consolidated statement of income – is removed from consolidated OCI and recognised in the consolidated statement of income. Impairment losses on equity investments are not reversed through the consolidated statement of income. Increases in their fair value after impairment are recognised directly in consolidated OCI.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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 consolidated OCI.

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

Recognition of income and expenses

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

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

Commission income and other fees are recognised when earned.

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

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

Contingent liabilities and contingent assets

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial guarantee contracts

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

Significant assumptions, accounting judgements and estimates

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

Going concern

The Group's management has made an assessment of the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Group's ability to continue as a going concern. Therefore, the consolidated financial statements continue to be prepared on the going concern basis.

Classification of investments

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

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

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

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

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

Impairment of investments

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

Impairment of goodwill

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

Impairment losses on loans and receivables

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

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

2 BASIS OF PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Significant assumptions, accounting judgements and estimates (continued)

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;
- 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

3 PROSPECTIVE CHANGES IN ACCOUNTING POLICIES (CONTINUED)

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

IFRS 9 Financial Instruments (continued)

Impairment of financial assets

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

The Group is currently working on establishing a policy to perform an assessment at the end of each reporting period of whether credit risk has increased significantly since initial recognition by considering the change in the risk of default occurring over the remaining life of the financial instrument.

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

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

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

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

IFRS 15 Revenue from Contracts with Customers

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

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

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

IFRS 16 Leases

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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4 FINANCIAL ASSETS AND LIABILITIES

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

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

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

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5 INVESTMENTS CARRIED AT FAIR VALUE THROUGH STATEMENT OF INCOME

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

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

6 NON-TRADING INVESTMENTS

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

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

7 LOANS AND RECEIVABLES

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

The movement in the provision for impairment is as follows:

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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7 LOANS AND RECEIVABLES (CONTINUED)

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

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

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

8 OTHER ASSETS

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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9 INVESTMENTS IN ASSOCIATES

		Activity	Carrying value 2017 US$ 000	Ownership 2017 %	Carrying value 2016 US$ 000	Ownership 2016 %
a)	Kamco Investment Fund	Fund	22,750	23	-	-
b)	Kuwait Education Fund	Fund	14,139	34	19,552	34
c)	United Capital Transport Co K.S.C.C.	Transport	15,038	40	16,530	40
d)	Manafae Investment Company	Islamic investment	12,870	31	12,855	31
e)	N.S. 88	Real estate	12,280	20	12,292	20
f)	Arab Leadership Academy	Training institute	414	15	408	15
g)	United Real Estate Company - Syria	Real estate	21	20	22	20
h)	Al Sharq Financial Brokerage Co.	Brokerage and investment business	-	-	7,501	19
i)	Meena Homes Real Estate Company	Real estate	-	-	806	20
j)	Burgan Bank S.A.K.	Commercial banking	-	-	484,095	15
k)	United Real Estate Company	Real estate	-	-	67,084	10
l)	North Africa Holding Company	Investments	-	-	49,027	44
m)	Assoufid B.V.	Holding, finance and project-development	-	-	33,677	40
n)	Syria Gulf Bank	Commercial banking	-	-	4,033	31
o)	Brasilfactors	Factoring and Forfaiting	-	-	1,161	50
p)	Takaud Savings & Pensions Company	Pension funds	-	-	-	50
			77,512		709,043	

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

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

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

9 INVESTMENTS IN ASSOCIATES (CONTINUED)

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

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

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

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

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

In accordance with IAS 36, 'Impairment of Assets', the Group's recoverable amount of these associates (i.e. value in use) was in excess of their carrying values and accordingly no impairment was recognised against these investments during the year ended 31 December 2017 (2016: same).

Investments in associates that are individually not significant

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

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

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10 INVESTMENT PROPERTIES

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

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

Valuations of investment properties were conducted by independent appraisers with a recognised and relevant professional qualification and recent experience of the location and category of investment property being valued. The discounted future cash flow method or property market value method have been used as deemed appropriate considering the nature and usage of the property. The Group's investment properties are categorised in level 3 of the fair value hierarchy as at 31 December 2017 and 2016.

11 GOODWILL

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

The goodwill remaining as of 31 December relates to KAMCO (a subsidiary) and is allocated to the asset management and investment banking operating segment, a cash generating unit (a CGU). The recoverable amount of the CGU is determined based on a value in use calculation using cash flow projections from financial budgets approved by the Group's senior management covering a five year period. The key assumptions used in the value in use calculation include a perpetuity growth rate of 3% (2016: 3%) and discount factor of 9.5% (2016: 10.7%). There was no goodwill impairment identified in 2017 or 2016 as the recoverable amount of the CGU was higher than its net book value.

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

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

	Impact of change	
Key assumptions	+10%	-10%
Growth rate	12,169	(11,101)
Discount factor	(40,750)	54,811

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12 TAXATION

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

a) Deferred tax assets

Deferred tax assets relate to the following:

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

Reconciliation of deferred tax assets is as follows:

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

12 TAXATION (CONTINUED)

b) Deferred tax liabilities

Deferred tax liabilities relate to the following:

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

Reconciliation of deferred tax liabilities is as follows:

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

c) Income tax credit

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

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

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

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13 LOANS PAYABLE

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

31 December 2016	Currency*	Bank US$ 000	Subsidiaries US$ 000	Total US$ 000
Maturing within one year				
1 month or less	Various	-	58,740	58,740
3 months or less but over 1 month	US$	-	40,000	40,000
1 year or less but over 3 months	US$	350,522	-	350,522
	KWD	-	60,438	60,438
		350,522	159,178	509,700
Maturing after one year				
More than 1 year & less than 2 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

* KWD represents Kuwaiti Dinar.

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14 SUBORDINATED DEBT

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

15 OTHER LIABILITIES

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

16 EQUITY

a) Share capital

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

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

b) Treasury shares and treasury shares reserve

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

c) Share premium

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

d) Statutory reserve

In accordance with the Bahrain Commercial Companies Law and the Bank's articles of association, 10% of the profit for the year is transferred to a statutory reserve until such time as the reserve reaches 50% of the Bank's paid-up share capital. The reserve is not available for distribution, except in circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the Central Bank of Bahrain.

e) General reserve

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

f) Dividend paid

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

g) Foreign currency translation reserve

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

16 EQUITY (CONTINUED)

h) Reclassification adjustment

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

17 FAIR VALUE RESERVE

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

18 PERPETUAL TIER 1 CAPITAL

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

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

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

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

19 INTEREST INCOME

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

20 INVESTMENT INCOME - NET

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

21 FEES AND COMMISSIONS - NET

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

22 SHARE OF RESULTS OF ASSOCIATES - NET

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

23 INTEREST EXPENSE

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

24 CASH AND CASH EQUIVALENTS

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

25 RELATED PARTY TRANSACTIONS

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

25 RELATED PARTY TRANSACTIONS (CONTINUED)

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

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

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

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

25 RELATED PARTY TRANSACTIONS (CONTINUED)

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.

Compensation of key management personnel was as follows:

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

26 COMMITMENTS AND CONTINGENCIES

Credit-related commitments

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

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

The Group has the following credit and investment related commitments:

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

27 DERIVATIVES

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

			Notional amounts by term to maturity			
31 December 2017	Positive fair value US$ 000	Negative fair value US$ 000	Notional amount Total US$ 000	Within 3 months US$ 000	3 - 12 months US$ 000	1 - 5 years US$ 000
Derivatives held for trading *						
Forward foreign exchange contracts	774	(889)	427,968	274,505	153,463	-
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	-	-	245,114	245,114	-	-
Derivatives used as cash flow hedges						
Interest rate swaps	1,100	-	145,000	-	70,000	75,000
31 December 2016						
Derivatives held for trading *						
Forward foreign exchange contracts	1,506	(8,827)	432,242	311,519	120,723	-
Derivatives used as hedge of net investments in foreign operations						
Forward foreign exchange contracts	1,857	(14)	711,424	562,877	148,547	-
Derivatives used as cash flow hedges						
Interest rate swap	845	-	175,000	-	80,000	95,000

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

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

Swaps are contractual agreements between two parties to exchange interest or foreign currency differentials based on a specific notional amount. For interest rate swaps, counterparties generally exchange fixed and floating rate interest payments based on a notional value in a single currency.

Hedge of net investments in foreign operations

The Bank has designated certain forward foreign exchange contracts to hedge against changes in the value of its investments in foreign operations for an amount of US$ 245 million (KWD 74 million) [2016: US$ 711 million (KWD 218 million)]. Gains or losses on the retranslation of these forward foreign exchange contracts are transferred to equity through other comprehensive income to offset any gains or losses on the translation of the net investments in foreign operations.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

27 DERIVATIVES (CONTINUED)

Cash flow hedges

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

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

28 RISK MANAGEMENT

a) Introduction

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

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

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

Risk management structure

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

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

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

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

Executive Committee

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

a) Introduction (continued)

Risk management structure (continued)

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

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

Risk and Compliance 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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

a) Introduction (continued)

Risk mitigation

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

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

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

Concentration risk

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

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

b) Credit risk

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

Credit risk is mitigated through:

(i) Establishing an appropriate credit risk environment;

(ii) Operating under a sound credit and investment approval process;

(iii) Maintaining appropriate credit administration, measurement and monitoring processes; and

(iv) Ensuring adequate controls over the credit risk management process.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Risk concentrations of the maximum exposure to credit risk

Concentration of risk is managed by client/counterparty, by geographical region and by industry sector. The maximum credit exposure to any single client or counterparty as of 31 December 2017 was US$ 72.1 million (2016: US$ 120 million) before taking account of collateral or other credit enhancements.

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

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

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

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

Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. Guidelines are implemented regarding the acceptability of types of collateral and valuation parameters.

The main types of collateral obtained for commercial lending include charges over real estate properties, inventory, trade receivables, trading securities and bank guarantees.

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

b) Credit risk (continued)

Collateral and other credit enhancements (continued)

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

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

Credit risk exposure for each credit rating

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

28 RISK MANAGEMENT (CONTINUED)

b) Credit risk (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 has not restructured any loans as of 31 December 2017 (31 December 2016: US$ 17,258 thousand).

Offsetting financial assets and financial liabilities

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

	Loans and receivables US$ 000	Customer deposits US$ 000
31 December 2017		
Gross amounts of recognised financial asset (liability)	305,700	305,700
Gross amounts offset in the consolidated statement of financial position	(305,700)	(305,700)
Net amount of financial liability presented in the consolidated statement of financial position	-	-
31 December 2016		
Gross amounts of recognised financial asset (liability)	133,450	(133,450)
Gross amounts offset in the consolidated statement of financial position	(133,450)	133,450
Net amount of financial liability presented in the consolidated statement of financial position	-	-

c) Market risk

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

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

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

The Group has entered into interest rate swaps and forward foreign exchange contracts for hedging purposes and does not actively trade in derivatives.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

c) Market risk (continued)

Interest rate risk

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

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

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

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

The sensitivity of the consolidated statement of income is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate financial assets and financial liabilities held at 31 December 2017, including the effect of hedging instruments.

Currency risk

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

c) Market risk (continued)

Equity price risk

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

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

Geographical distribution

At 31 December 2017	Middle East/ North Africa US$ 000	Europe US$ 000	North America US$ 000	Others US$ 000	Total US$ 000
Investments carried at fair value through statement of income					
Quoted equities	6,303	-	1	1	6,305
Managed funds	956	263	66	-	1,285
	7,259	263	67	1	7,590
Non-trading investments					
Quoted equities	31,514	-	10,567	-	42,081
Unquoted equities	111,629	25,609	5,879	-	143,117
Managed funds	34,129	-	2,239	-	36,368
	177,272	25,609	18,685	-	221,566
Total	184,531	25,872	18,752	1	229,156

At 31 December 2016	Middle East/ North Africa US$ 000	Europe US$ 000	North America US$ 000	Others US$ 000	Total US$ 000
Investments carried at fair value through statement of income					
Quoted equities	13,413	1,057	1	1,014	15,485
Managed funds	1,021	241	66	-	1,328
	14,434	1,298	67	1,014	16,813
Non-trading investments					
Quoted equities	46,265	-	11,560	-	57,825
Unquoted equities	92,900	21,237	7,144	-	121,281
Managed funds	57,544	5,576	368	-	63,488
	196,709	26,813	19,072	-	242,594
Total	211,143	28,111	19,139	1,014	259,407

At the reporting date, the exposure to listed equity securities at fair value was US$ 48,386 thousand (2016: US$ 73,310 thousand). A decrease of 10% on the market indices of MENA stock exchanges could have an impact of approximately US$ 4,839 thousand (2016: US$ 7,331 thousand) on the income or equity attributable to the Group, depending on whether the decline is significant or prolonged. The majority of the equities in the MENA region are quoted on the Kuwait Stock Exchange.

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

d) Liquidity risk

Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2017 based on contractual undiscounted repayment obligations. Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

At 31 December 2017	On demand US$ 000	1 - 6 months US$ 000	6 - 12 months US$ 000	1 - 5 years US$ 000	Over 5 years US$ 000	Total US$ 000
Financial liabilities						
Due to banks and other financial institutions	133,661	16,757	101,423	-	-	251,841
Deposits from customers	62,395	6,323	-	-	-	68,718
Loans payable	663	40,270	14,746	49,224	-	104,903
Other liabilities	37,358	-	-	-	-	37,358
Total non-derivative undiscounted financial liabilities	234,077	63,350	116,169	49,224	-	462,820
Derivatives						
Net cash outflows on interest rate swaps	-	780	583	1,985	-	3,348
Gross settled foreign currency derivatives	-	673,082	-	-	-	673,082
Off-statement of financial position items						
Letters of guarantee	-	-	812	-	-	812
Investment related commitments	-	-	-	4,017	-	4,017

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

At 31 December 2016	On demand US$ 000	1 - 6 months US$ 000	6 - 12 months US$ 000	1 - 5 years US$ 000	Over 5 years US$ 000	Total US$ 000
Financial liabilities						
Due to banks and other financial institutions	342,730	177,494	207,333	3,726	-	731,283
Deposits from customers	469,249	255,233	202,473	89,846	-	1,016,801
Loans payable	79,601	181,065	259,378	156,159	-	676,203
Subordinated debt	182	1,590	2,141	56,072	-	59,985
Other liabilities	-	-	62,724	-	-	62,724
Total non-derivative undiscounted financial liabilities	891,762	615,382	734,049	305,803	-	2,546,996
Derivatives						
Net cash outflows on interest rate swaps	-	773	574	873	-	2,220
Gross settled foreign currency derivatives	-	874,396	269,270	-	-	1,143,666
Off statement of financial position items						
Letters of credit	-	11,837	32,801	2,548	4,858	52,044
Letters of guarantee	-	2,139	479	4,543	-	7,161
Investment related commitments	-	-	-	140,044	-	140,044

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

d) Liquidity risk (continued)

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

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

At 31 December 2017	Less than 12 months US$ 000	Over 12 months US$ 000	Total US$ 000
Demand and call deposits with banks	97,675	318	97,993
Placements with banks	68,577	-	68,577
Investments carried at fair value through statement of income	19,268	-	19,268
Non-trading investments	42,081	179,485	221,566
Loans and receivables	1,564	2,652	4,216
Other assets	31,820	-	31,820
Investments in associates	-	77,512	77,512
Investment properties	-	105,093	105,093
Property and equipment	-	1,679	1,679
Goodwill	-	52,390	52,390
Total assets	260,985	419,129	680,114
Due to banks and other financial institutions	250,211	-	250,211
Deposits from customers	31,018	-	31,018
Loans payable	54,517	44,141	98,658
Other liabilities	37,358	-	37,358
Total liabilities	373,104	44,141	417,245
Net	(112,119)	374,988	262,869

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

28 RISK MANAGEMENT (CONTINUED)

d) Liquidity risk (continued)

At 31 December 2016	Less than 12 months US$ 000	Over 12 months US$ 000	Total US$ 000
Demand and call deposits with banks	169,717	7,163	176,880
Placements with banks	187,350	-	187,350
Investments carried at fair value through statement of income	45,178	-	45,178
Non-trading investments	219,666	184,770	404,436
Loans and receivables	1,079,597	105,207	1,184,804
Other assets	112,735	-	112,735
Investments in associates and joint venture	-	709,043	709,043
Investment properties	-	101,326	101,326
Property and equipment	-	32,117	32,117
Goodwill	-	51,868	51,868
Total assets	1,814,243	1,191,494	3,005,737
Due to banks and other financial institutions	723,069	3,153	726,222
Deposits from customers	899,192	86,018	985,210
Loans payable	509,700	142,425	652,125
Subordinated debt	-	50,000	50,000
Other liabilities	-	62,724	62,724
Total liabilities	2,131,961	344,320	2,476,281
Net	(317,718)	847,174	529,456

e) Operational risk

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

29 FAIR VALUE MEASUREMENT

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

Management has assessed that financial assets comprising of demand and call deposits with banks, placements with banks, and loans and receivables maturing within one year, and financial liabilities comprising of on-demand customer deposits, amounts due to banks and loans payable falling due within one year approximate their carrying values largely due to the short term maturities of these instruments. Non-trading investments carried at cost are disclosed in Note 6.

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

Quantitative disclosures fair value measurement hierarchy for assets as at 31 December 2017:

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

29 FAIR VALUE MEASUREMENT (CONTINUED)

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
Derivatives				
Interest rate swaps	-	845	-	845
Investment properties	-	-	101,326	101,326
	263,517	127,098	117,381	507,996
Liabilities measured at fair value				
Derivatives				
Forward foreign exchange contracts	-	(5,478)	-	(5,478)
	-	(5,478)	-	(5,478)

Transfers between Level 1, Level 2 and Level 3

During the year ended 31 December 2017 there were no transfers between Level 1 and Level 2 fair value measurements and no transfers into or out of Level 3 fair value measurement.

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

30 CAPITAL ADEQUACY

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

Capital management

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

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

	2017 US$ 000	2016 US$ 000
Capital base:		
Tier 1	188,657	264,123
Tier 2	3,428	73,751
Total capital base (a)	192,085	337,874
Credit risk weighted exposure	750,074	2,227,194
Market risk weighted exposure	54,400	122,725
Operational risk weighted exposure	87,463	84,638
Total risk weighted exposure (b)	891,937	2,434,557
Capital adequacy (a/b * 100)	21.54%	13.88%
Minimum requirement	12.5%	12.5%

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

31 IFRS 9 TRANSITION DISCLOSURES

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

IFRS 9 Financial Instruments

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

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

(a) Classification and measurement

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

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

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

(b) Impairment

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

(c) Hedge accounting

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

(d) Other adjustments

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

32 DISCONTINUED OPERATIONS

Restructuring

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

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

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

At 31 December 2017

32 DISCONTINUED OPERATIONS (CONTINUED)

Restructuring (continued)

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

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

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

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

GROUP DIRECTORY

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@ugbbh.com
Website: www.ugbbh.com

Parent Company

United Gulf Holding B.S.C

PO Box 5565, Diplomatic Area
UGB Tower, Manama, Kingdom of Bahrain
Tel: (+973) 17 533233
Fax: (+973) 17 533137
Email: info@ughbh.com
Website: www.ughbh.com

Ultimate Parent Company

Kuwait Projects Company (Holding) (KSC)

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) KSC (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

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

Major Subsidiaries

KAMCO كامكو

UGFS North Africa

الخليج المتحد للخدمات المالية شمال افريقيا
United Gulf Financial Services North Africa

United Gulf Bank B.S.C.
PO Box 5964, Diplomatic Area
UGB Tower, Manama, Kingdom of Bahrain
Tel: (+973) 17 533 233 Fax: (+973) 17 533 137
Email: info@ugbbh.com
www.ugbbh.com

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