

KHALEEJI COMMERCIAL BANK BSC

CONSOLIDATED FINANCIAL STATEMENTS

31 DECEMBER 2020

Commercial registration	:	55133 (registered with Central Bank of Bahrain as a retail Islamic bank).
Office	:	Bahrain Financial Harbour East Tower PO Box 60002, Manama, Kingdom of Bahrain
Directors	:	Jassim Mohamed Alseddiqi – Chairman Sh. Ahmed Bin Isa Khalifa Al Khalifa – Vice Chairman Hisham Ahmed Al Rayes Reyadh Eid Al Yaqoob Abdulla Abdulkarim Showaiter (Resigned on 26 MAR 2020) Dr. Khalid Mohammed Al Khazraji (Resigned on 26 MAR 2020) Mosaboh Saif Al Mutaury (Appointed on 23 SEP 2020) Mustafa Ghazi Kheriba (Resigned on 25 JAN 2021) Fawad Tariq Khan (Resigned on 22 NOV 2020) Yousef Ibrahim Al Ghanim (His term ended in SEP 2020) Mohammad Abdulmohsen Al Rashed (His term ended in SEP 2020) Isa Abdulla Zainal (Appointed on 23 SEP 2020) Mazen Ibrahim Abdulkarim (Appointed on 23 SEP 2020) Salah Abdulla Sharif (Appointed on 19 NOV 2020) Hussain Sayed Ali Al Hussaini (Appointed on 10 DEC 2020)
Chief Executive Officer	:	Sattam Sulaiman Algosaibi
Company secretary	:	Mohammed Abdulla Saleh
Auditors	:	KPMG Fakhroo, Bahrain

CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

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**Chairman's Report
For the Year Ended 31 December 2020
Khaleeji Commercial Bank BSC**

*In the name of Allah, the beneficent, the merciful,
Prayers and peace upon the last apostle and messenger, our prophet Muhammad.*

Dear Shareholders,

On behalf of the Board of Directors, it is my pleasure to present the annual financial statements of Khaleeji Commercial Bank (the "Bank") for the year ended 31 December 2020.

In all areas, it has been a challenging year with the Coronavirus (COVID-19) pandemic bringing significant human repercussions and important economic variations around the world. The impact of COVID-19 on all fronts is rapidly developing. The Bank is continuously looking at different scenarios and revisiting its strategy to ensure continuous growth and support to its community.

As a result of an ambitious business strategy approved by the board, the Bank has recorded a remarkable performance despite the uncertainty the global market scene is witnessing. The Bank is equipped to face these challenges where it successfully achieved growth and progress during the year. Strong foundations were laid for this strategy by issuing Sukuk worth BD 60 million as Additional Tier 1 "AT1" Capital and reached an agreement to exchange Financial and Investment Assets worth BD 46.4 million both of which were signed with GFH Financial Group. These agreements were an integral part of the Bank's strategy in paving the path towards success and the unwavering steps towards achieving a strong foundation and success. This business model ensures that the Bank keeps pace with current developments and take advantage of new opportunities.

Over the year, the Bank was able to achieve positive results in spite of extraordinary circumstances witnessed by the world due to the spread of COVID-19, confirming the Bank's strong foundation and infrastructure that is based on stable financial performance and client confidence. Achieving these results reflects the efficiency and intactness of the plans that the Management and Board of Directors has put together to strengthen the capital base and develop the business. The Sukuk issuance had a great impact on strengthening our financial position which allowed us to engage in new strategic partnerships and promising projects, creating the basis for the bank's growth and profitability.

Moreover, the Kingdom's economic climate played an important role in protecting all sectors, including the Banking and Finance Sectors from the negative impacts of the pandemic. This was done thanks to the almighty God first, then to the preventive decisions and measures taken by the Government's Executive Committee and The National Task Force for Combating the Corona Virus that contributed to the continuation of economic activity and enabled companies and institutions to continue growing and generate profits.

**Chairman's Report
For the Year Ended 31 December 2020
Khaleeji Commercial Bank BSC**

Overall Performance

The Bank, during 2020, was able to achieve the strategic goals set by the Board. This was achieved by providing innovative financial solutions and quickly adapting to the ever-changing market and understanding customer needs and requirements.

A positive indicator of the Bank's performance this year is the net profit attributable to the shareholders of the parent which amounted to BD 7.99 million an increase of 152.6% from a loss of BD 14.94 million in 2019. Despite the challenges faced, the bank managed to achieve a growth of total assets from BD 939.75 million in 2019 to BD 1,015.59 million in 2020, a growth of 8.1%.

Furthermore, the Bank was able to achieve growth in liquid assets which currently comprises of 24.41% of Total Assets while the Capital Adequacy Ratio ("CAR") reached 20.31%. In addition to this, the Bank is maintaining healthy Liquidity Coverage Ratio ("LCR") of 198.28% and Net Stable Funding Ratio ("NSFR") of 103.65% as of 31 December 2020. The Bank's return on average equity reached 7.02% while the Return on Average Assets reached 0.81%.

This has in turn allowed the Bank to invest the liquidity in prominent Sukuk investments that are characterized with high yield and low risk. Such investments resulted in a considerable increase in the Sukuk portfolio reaching BD 261.13 million in 2020 compared to BD 195.05 million in 2019, a growth of 33.9%. Moreover, the Bank's total equity reached BD 141.81 million compared to BD 85.71 million, an increase of 65.5%.

The Bank's cost rationalization measures were fruitful as the bank succeeded to obtain a 45.92% Cost to Income Ratio. The cost rationalization measures will continue to control expenses and further measures are taken to ensure improvement in the efficiency of the Bank in the future.

Looking Ahead

We trust that the Bank will continue its growth by applying its flexible strategy that is capable of adapting to various regional and international variables imposed by COVID-19 Pandemic, and the accompanying financial and economic repercussions. The Board of Directors shall spare no effort in providing the necessary support to the Executive Management in achieving sustainability, reinforcing profitability, and attaining remunerative returns for the shareholders.

The Bank will continue to invest its improved financial position towards new strategic partnerships, enhancing the financing portfolio, investing in Sukuk, and continuing the work on implementing the Bank's strategic plan towards digital transformation at an accelerated pace with confidence to implement the latest technology introduced to banking services, and to develop an integrated set of innovative technological banking solutions. KHCB is also striving to enhance its customer service quality, and to

**Chairman's Report
For the Year Ended 31 December 2020
Khaleeji Commercial Bank BSC**

introduce banking solutions and services that meet the diverse aspirations of our clients, individuals and corporates alike.

KHCB is a leading Islamic bank that strives to achieve clients' aspirations through an Islamic banking model that offers a comprehensive range of high quality Shari'a-complaint banking services and investment opportunities to individuals and companies.

Appreciation

On behalf of myself, the Board members, the Executive management, and all employees of KHCB, I would like to take this opportunity to express my utmost thanks and gratitude to His Majesty King Hamad bin Isa Al Khalifa may God protect him, and His Royal Highness Prince Salman bin Hamad Al Khalifa, the Crown Prince and Prime Minister may God protect him, for the proactive decisions they have taken to preserve the financial and business market and all other sectors from the negative impacts of the COVID-19 Pandemic. This made the Kingdom one of the top advanced countries facing this pandemic. Also, I would like to thank the Central Bank of Bahrain for its directives and support of the banking sector, which has contributed to its stability under current circumstances. I also extend my thanks to all government ministries, and Bahrain Bourse for their continued guidance and support.

Special appreciation is due to the Bank's shareholders, clients and business partners for their on-going confidence and loyalty; and to the Bank's management and staff for their hard work and dedication.

Allah the almighty is the purveyor of all success.



Jassim Mohamed Alseddiqi
Chairman

03 February 2021
21 Jamadah II 1442 AH

**SHARI'A SUPERVISORY BOARD REPORT TO THE SHAREHOLDERS
On the Activities of Khaleeji Commercial Bank B.S.C.
For the financial year ending 31 December 2020**

Prayers and Peace upon the Last Apostle and Messenger, Our prophet Mohammed, His Family and companions.

In compliance with our terms of appointment, the Shari'a Supervisory Board ("SSB") hereby presents the following report to the Shareholders on the activities of Khaleeji Commercial Bank ("KHC") and its subsidiaries for the financial year ending 31st December 2020.

Respective responsibility of the Board of Directors and the SSB

The SSB confirms that as a general principle and practice, KHC's management is responsible for ensuring that it conducts its business in accordance with Islamic Shari'a rules and principles. The SSB's responsibility is to form an independent Shari'a opinion based on our review of the Bank's operations and to prepare this report.

Basis of opinion


In compliance with the Shari'a Governance and based on SSB's Fatwas, decisions and the AAOIFI standards, the SSB through its periodic meetings and its executive member have reviewed the internal Shari'a audit plan and Shari'a audit reports and examined the documents and transactions by conducting a sample-test method to ensure its compliance with the Shari'a rules and principles. In addition, the SSB has reviewed the IESCA report for 2020. The SSB in collaboration with Shari'a coordination and implementation department has reviewed contracts, agreements, financings and investment structures, products, related policies, consolidated Financial Statements and attached notes for the year ended 31st December 2020.

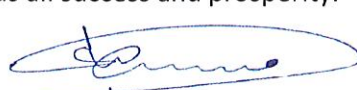
Opinion

Based on our review, The SSB is satisfied that:

1. The contracts, agreements and transactions entered into by the Bank that have been reviewed by the SSB are in compliance with the Shari'a rules and principles.
2. The allocation of profits and charging of losses 'if any' on investment accounts conform to the basis that had been approved by the SSB and in accordance with Shari'a rules and principles.
3. Any earnings resulted by means prohibited by the Shari'a rules and principles have been channeled to charity account.
4. Zakah was calculated in accordance with Shari'a rules and principles based on net assets method according to AAOIFI standards. Each shareholder is responsible to pay their relevant zakah portion related to their respected shares as per zakah guide.
5. The Bank is in compliance with Shari'a rules and principles, SSB's Fatwas and decisions, Shari'a related policies and procedures, AAOIFI's Shari'a standards, relevant rulings of the CSSB and the regulations, resolutions and directives issued by the CBB.

We pray to Allah the almighty to grant us all success and prosperity.


Shaikh Dr. Fareed Al-Muftah
Chairman


Shaikh Dr. Fareed Hadi
Vice-Chairman & Executive Member


Shaikh Dr. Nizam Yaqoobi
Board Member



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CR No. 6220

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INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS

Khaleeji Commercial Bank B.S.C.
PO Box 106
Manama
Kingdom of Bahrain

Report on the audit of the consolidated financial statements

Opinion

We have audited the accompanying consolidated financial statements of Khaleeji Commercial Bank B.S.C. (the "Bank"), and its subsidiaries (together the "Group") which comprise the consolidated statement of financial position as at 31 December 2020, the consolidated statements of income, changes in owner's equity, cash flows, changes in restricted investment accounts and sources and uses of Zakah and charity fund for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

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 2020, and consolidated results of its operations, changes in owners' equity, its cash flows, changes in restricted investment accounts and its sources and uses of Zakah and charity fund for the year then ended in accordance with the Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI") as modified by the Central Bank of Bahrain (the "CBB").

In our opinion, the Group has also complied with the Islamic Shariah Principles and Rules as determined by the Group's Shariah Supervisory Board during the year ended 31 December 2020.

Basis for opinion

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions ("ASIFIs") issued by AAOIFI. Our responsibilities under those standards are further described in the *Auditors' responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with AAOIFI's Code of Ethics for Accountants and Auditors of Islamic Financial Institutions, together with the ethical requirements that are relevant to our audit of the consolidated financial statements in the Kingdom of Bahrain, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters

Impairment allowance on financing assets and assets acquired for leasing

(refer to accounting policy in Note 5j(i), use of estimates and judgments in Note 25 and management of credit risk in Note 35).

Description	How the matter was addressed in our audit
<p>We focused on this area because:</p> <ul style="list-style-type: none"> of the significance of financing assets and assets acquired for leasing representing 44 % of total assets. 	<p>Our procedures included:</p> <p>Control testing</p> <p>We performed walk throughs to identify the key systems, applications and controls used in the ECL processes.</p> <p>Key aspects of our controls testing involved the following:</p> <ul style="list-style-type: none"> testing the design and operating effectiveness of the key controls over the completion and accuracy of the key inputs and assumptions into the ECL Model;

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS (continued)

Khaleeji Commercial Bank B.S.C.

Description	How the matter was addressed in our audit
<ul style="list-style-type: none"> Th estimation of expected credit losses ("ECL") on financing assets and assets acquired for leasing involve significant judgment and estimates. The key areas where we identified greater level of management judgment and estimates are: <ul style="list-style-type: none"> ➤ <i>Use of complex models</i> Use of inherently judgmental complex models to estimate ECL which involves determining Probabilities of default ("PD"), Loss Given Default ("LGD") and Exposure At default ("EAD"). The PD models are considered the drivers of the ECLs. ➤ <i>Economic scenarios</i> The need to measure ECLs on an unbiased forward-looking basis incorporating a range of economic conditions. Significant management judgment is applied in determining the economic scenarios used and the probability weightings applied to them. ➤ <i>Management overlays</i> Adjustments to the ECL model results are made by management to address known impairment model limitations or emerging trends or risks, including the potential impacts of COVID-19. Such adjustments are inherently uncertain and significant management judgment is involved in estimating these amounts especially in the current COVID-19 environment. 	<ul style="list-style-type: none"> evaluating the design and operating effectiveness of the key controls over the application of staging criteria; Evaluating controls over validation, implementation and model monitoring; evaluating controls over authorization and calculation of post model adjustments and management overlays; and testing key controls relating to selection and implementation of material macro-economic variables and the controls over the scenario selection and probabilities. <p>Tests of details</p> <ul style="list-style-type: none"> Sample testing over key inputs and assumptions impacting ECL calculations to assess the reasonableness of economic forecast, weights, and PD assumptions applied; and Selecting a sample of post model adjustments to assess the reasonableness of the adjustments by challenging key assumptions, inspecting the calculation methodology and tracing a sample of the data used back to the source data. <p>Use of specialists</p> <ul style="list-style-type: none"> We involved our information technology specialists in testing the relevant general IT and applications controls over the key systems used in the ECL process; We involved our credit risk specialists to assist us in: <ul style="list-style-type: none"> ➤ evaluating the appropriateness of the Groups' ECL methodologies (including the staging criteria used); ➤ on a test basis, re-performing the calculation of certain components of the ECL model (including the staging criteria); ➤ evaluating the appropriateness of the Group's methodology for determining the economic scenarios used and the probability weighing applied to them; and ➤ evaluating the overall reasonableness of the management economic forecast by comparing it to external market data. <p>Disclosures</p> <ul style="list-style-type: none"> evaluating the adequacy of the Group's disclosures related to ECL on financing assets and assets acquired for leasing by reference to the relevant accounting standards.

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS (continued)

Khaleeji Commercial Bank B.S.C.

Valuation of unquoted equity investments

(refer to accounting policy in Note 5j (ii) and fair value in Note 34)

Description	How the matter was addressed in our audit
<p>We considered this as a key audit area we focused on because the valuation of unquoted equity securities held at fair value requires the application of valuation techniques which often involve the exercise of significant judgment by the Group and the use of significant unobservable inputs and assumptions.</p>	<p>Our procedures included:</p> <ul style="list-style-type: none"> we involved our own valuation specialists to assist us in: <ul style="list-style-type: none"> evaluating the appropriateness of the valuation methodologies used by comparing with observed industry practice; evaluating the reasonableness of key input and assumptions used by using our knowledge of the industries in which the investees operate and industry norms. comparing the key underlying financial data inputs used in the valuation to external sources, investee company financial and management information, as applicable; evaluating the adequacy of the Group's disclosures related to valuation of unquoted equity instruments by reference to the relevant accounting standards.

Impairment of investment in real estate

(Refer to accounting policies in Note 5 (h) and impairment of non-financial assets in Note 5 (k))

Description	How the scope of our audit addressed the matter
<p>We considered this as a key audit area we focused on because of:</p> <ul style="list-style-type: none"> the uncertainty prevalent in the property market; and application of valuation techniques which often involve the exercise of judgment and the use of assumptions and estimates. 	<p>Our procedures included:</p> <ul style="list-style-type: none"> we involved our own real estate valuation specialists, who used their knowledge of the industry and available historical data to assist us in: <ul style="list-style-type: none"> evaluating the appropriateness of the valuation methodology used by the external, independent property valuers appointed by the Group; and evaluating the reasonableness of key inputs and assumptions used in the valuation. Assessing the qualification and experience of the independent property valuers and reviewing the terms of their engagement letter to determine whether there were any matters that might have affected their objectivity or limited their scope of work; and evaluating the adequacy of the Group's disclosures related to valuation of investment in real estate by reference to the relevant accounting standards.

*INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS (continued)**Khaleeji Commercial Bank B.S.C.**Other information*

The board of directors is responsible for the other information. The other information comprises the annual report but does not include the consolidated financial statements and our auditors' report thereon. Prior to the date of this auditors' report, we obtained the board of directors' report and other sections which forms part of the annual report.

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

In connection with our audit of the financial statements, our responsibility is to read the other information identified above 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 that we have obtained prior to the date of this auditors' 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 financial statements

The board of directors is responsible for the Group's undertaking to operate in accordance with Islamic Sharia Rules and Principles as determined by the Group's Shariah Supervisory Board.

The board of directors is also responsible for the preparation and fair presentation of the consolidated financial statements in accordance with FAS as modified by CBB, 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.

Auditors' 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 auditors' 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 ASIFIs 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.

*INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS (continued)**Khaleeji Commercial Bank B.S.C.*

As part of an audit in accordance with ASIFs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the board of directors.
- Conclude on the appropriateness of the board of directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank 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 board of directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the board of directors with a statement that we have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

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

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS (continued)

Khaleeji Commercial Bank B.S.C.

Report on other regulatory requirements

As required by the Commercial Companies Law and Volume 2 of the Rulebook issued by the CBB, 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 chairman's report is consistent with the consolidated financial statements;
- c) we are not aware of any violations during the year of the Commercial Companies Law, the CBB and Financial Institutions Law No. 64 of 2006 (as amended), the CBB Rule Book (Volume 2, applicable provisions of Volume 6 and CBB directives), the CBB Capital Markets Regulations and associated resolutions, the Bahrain Bourse rules and procedures or the terms of the Bank's memorandum and articles of association that would have had a material adverse effect on the business of the Bank or on its financial position; and
- d) satisfactory explanations and information have been provided to us by management in response to all our requests.

The engagement partner on the audit resulting in this independent auditors' report is Jalil Al'Aali.




KPMG Fakhroo
Partner Registration No. 100
10 February 2021

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
as at 31 December 2020

BD 000's

	Note	31 December 2020	31 December 2019
ASSETS			
Cash and bank balances	6	83,017	104,376
Placements with financial institutions	7	17,720	65,508
Financing assets	8	307,717	324,355
Investment in sukuk	9	261,132	195,050
Assets acquired for leasing	10	126,934	129,097
Lease rentals receivables		12,820	17,102
Investment securities	11	55,892	43,989
Investment in real estate	12	83,303	24,032
Equity accounted investees	13	31,963	4,524
Other assets	14	27,646	23,969
Property and equipment	15	7,450	7,750
Total assets		1,015,594	939,752
LIABILITIES			
Placements from financial institutions		79,545	117,098
Placements from non-financial institutions and individuals	16	214,243	134,654
Term borrowings	17	75,477	-
Customers' current accounts		55,676	58,105
Other liabilities	18	13,269	19,798
Total liabilities		438,210	329,655
Equity of investment account holders			
From financial institutions		26,154	22,367
From non-financial institutions and individuals		399,195	499,823
Total equity of investment account holders	19	425,349	522,190
OWNERS' EQUITY			
Share capital	20	89,212	105,000
Subordinated Mudaraba (AT1)	35	47,222	-
Statutory reserve		9,024	8,225
Treasury shares		(11,859)	(11,730)
Employee share incentive scheme		-	-
Investment fair value reserve		348	-
Retained earnings / (accumulated losses)		7,863	(15,788)
Total owners' equity		141,810	85,707
Non-controlling interest		10,225	2,200
Total liabilities, equity of investment account holders, owners' equity and non-controlling interest		1,015,594	939,752

The consolidated financial statements were approved by the Board of directors on 10 February 2021 and signed on its behalf by:


Jassim Mohamed Alseddigi
 Chairman


Sh. Ahmed Bin Isa Al Khalifa
 Vice Chairman


Sattam Sulaiman Algosaihi
 Chief Executive Officer

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT
for the year ended 31 December 2020

BD 000's

	Note	2020	2019
Income from financing assets and assets acquired for leasing		29,921	31,334
Income from placements with financial institutions		551	2,183
Income from sukuk		15,242	10,031
Income from investment securities		366	(1,687)
Fees and other income		2,117	5,726
Total income before return to investment account holders		48,197	47,587
Less: Return to investment account holders before Bank's share as Mudarib	19	(21,575)	(27,059)
Bank's share as a Mudarib	19	9,289	8,457
Return to investment account holders		(12,286)	(18,602)
Finance expense on placements from financial institutions, non-financial institutions and individuals		(12,472)	(8,188)
Finance expense on term borrowings		(796)	(1,241)
Total income		22,643	19,556
Staff cost	21	5,874	8,158
Other operating expenses	22	4,523	6,036
Total expenses		10,397	14,194
Profit before impairment allowances		12,246	5,362
Net impairment charge	23	(4,341)	(20,389)
PROFIT / (LOSS) FOR THE YEAR		7,905	(15,027)
Attributable to:			
Shareholders of the Parent		7,986	(14,937)
Non-controlling interest		(81)	(90)
		7,905	(15,027)
Earnings per share			
Basic and diluted earnings per share (fils)	28	9.94	(18.56)


Jassim Mohamed Alseddiqi
Chairman


Sh. Ahmed Bin Isa Al Khalifa
Vice Chairman


Sattam Sulaiman Algosaibi
Chief Executive Officer

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
for the year ended 31 December 2020

BD 000's

2020	Equity attributable to shareholders of the parent								Non-Controlling interest	Total Equity
	Share Capital	Statutory reserve	Treasury shares	Employee share incentive scheme	Investment fair value reserve	Subordinated mudaraba (AT1)	Retained earnings / (accumulated losses)	Total		
Balance at 1 January 2020	105,000	8,225	(11,730)	-	-	-	(15,788)	85,707	2,200	87,907
Profit for the year	-	-	-	-	-	-	7,986	7,986	(81)	7,905
Total recognised income and expense for the year	-	-	-	-	-	-	7,986	7,986	(81)	7,905
Issuance of AT1 (Note 35)	-	-	-	-	-	60,000	12,000	72,000	-	72,000
Issuance costs of AT1 (Note 35)	-	-	-	-	-	(12,778)	-	(12,778)	-	(12,778)
Modification loss (Note 2a)	-	-	-	-	-	-	(9,452)	(9,452)	-	(9,452)
Government grant (Note 2b)	-	-	-	-	-	-	1,069	1,069	-	1,069
Capital reduction (Note 20)	(15,788)	-	-	-	-	-	15,788	-	-	-
Purchase of Treasury shares	-	-	(129)	-	-	-	-	(129)	-	(129)
Issue of shares under staff incentive scheme	-	-	-	-	-	-	111	111	-	111
Fair value movement	-	-	-	-	348	-	-	348	-	348
Profit distribution on AT 1 Capital	-	-	-	-	-	-	(2,834)	(2,834)	-	(2,834)
Acquisition of a subsidiary (Note 27)	-	-	-	-	-	-	-	-	8,106	8,106
Transfer to statutory reserve	-	799	-	-	-	-	(799)	-	-	-
Transfer to Zakah fund	-	-	-	-	-	-	(218)	(218)	-	(218)
Balance at 31 December 2020	89,212	9,024	(11,859)	-	348	47,222	7,863	141,810	10,225	152,035

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
for the year ended 31 December 2020 *(continued)*

BD 000's

2019

	Equity attributable to shareholders of the parent						Non-Controlling interest	Total Equity
	Share Capital	Statutory reserve	Treasury shares	Employee share incentive scheme	(Accumulated losses)	Total		
Balance at 1 January 2019	105,000	8,225	(11,295)	(29)	(729)	101,172	2,290	103,462
Loss for the year	-	-	-	-	(14,937)	(14,937)	(90)	(15,027)
Total recognised income and expense for the year	-	-	-	-	(14,937)	(14,937)	(90)	(15,027)
Transfer to statutory reserve	-	-	-	-	-	-	-	-
Net treasury shares purchased	-	-	(435)	-	-	(435)	-	(435)
Issue of shares under incentive scheme	-	-	-	29	65	94	-	94
Transfer to Zakah fund	-	-	-	-	(187)	(187)	-	(187)
Balance at 31 December 2019	105,000	8,225	(11,730)	-	(15,788)	85,707	2,200	87,907

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CASH FLOWS
for the year ended 31 December 2020

BD 000's

	Note	2020	2019
OPERATING ACTIVITIES			
Receipts from financing assets, net		3,828	9,621
Receipts / (Payments) towards asset acquired for leasing, net		11,509	(17,786)
Receipt of profit on short-term placements		551	2,183
Returns paid to investment account holders		(15,615)	(10,454)
(Withdrawals) / Receipts from investment account holders, net		(97,296)	165,461
Payment of profit on placements		(12,472)	(11,703)
Payment for expenses		(13,137)	(19,441)
Other receipts		2,048	3,964
Payment for charity		(276)	(235)
Withdrawals from customers' current accounts, net		(2,430)	(12,311)
Payment towards placements from financial institutions, net		(37,552)	(29,839)
Receipts from placements from non-financial institutions and individuals, net		79,589	14,184
Net receipt / (Payment) to CBB reserve account		10,016	(4,610)
Income from sukuk received		15,187	10,006
Net cash (used) / generated from operating activities		(56,050)	99,040
INVESTING ACTIVITIES			
Purchase of sukuk		(102,254)	(37,407)
Proceeds from redemption / sale of sukuk		29,967	3,269
Purchase of equity securities		(15,080)	-
Proceeds from disposal / redemption of equity securities		-	1,438
Proceeds from investment in real estate, net		728	-
Receipt of dividends / income from equity securities		316	343
Purchase of property and equipment, net		(249)	(452)
Net cash used in investing activities		(86,572)	(32,809)
FINANCING ACTIVITIES			
Purchase of treasury shares		(129)	(350)
Proceeds from ATI Capital		11,447	-
Profit distribution on AT 1 Capital		(2,834)	-
Drawdown / (Repayment) of term borrowings, net		75,524	(41,357)
Finance expense on term borrowings		(517)	(1,241)
Net cash from / (used) in financing activities		83,491	(42,948)
Net (decrease) / increase in cash and cash equivalents		(59,131)	23,283
Cash and cash equivalents at 1 January		144,454	121,171
Cash and cash equivalents at 31 December		85,323	144,454
Cash and cash equivalent comprise:			
Cash and bank balances (excluding CBB reserve)	6	67,603	78,946
Placements with financial institutions with original maturities of 90 days or less	7	17,720	65,508
		85,323	144,454

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS
for the year ended 31 December 2020

BD 000's

2020

	Balance at 1 January 2020			Movements during the year						Balance at 31 December 2020		
	No of units (000's)	Average value per share BD	Total BD 000's	Investment (withdrawals) BD 000's	Revalua- tion BD 000's	Gross income/ (loss) BD 000's	Dividends paid BD 000's	Bank's fees as an agent BD 000's	Administra- tion expenses BD 000's	No of units (000's)	Average value per share BD	Total BD 000's
Safana Investment WLL (RIA 1) and NS12	6,254	1.00	6,254	-	-	-	-	-	-	6,254	1.00	6,254
Shaden Real Estate Investment WLL (RIA 5)	3,434	1.00	3,434	-	-	-	-	-	-	3,434	1.00	3,434
Locata Corporation Pty Ltd (RIA 6)	2,633	0.38	993	-	-	-	-	-	-	2,633	0.38	993
			10,681	-	-	-	-	-	-			10,681

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN RESTRICTED INVESTMENT ACCOUNTS**for the year ended 31 December 2020** *(continued)*

BD 000's

2019

	Balance at 1 January 2019			Movements during the year						Balance at 31 December 2019		
	No of units (000's)	Average value per share BD	Total BD 000's	Investment (withdrawals) BD 000's	Revalua- tion BD 000's	Gross income/ (loss) BD 000's	Dividends paid BD 000's	Bank's fees as an agent BD 000's	Administra- tion expenses BD 000's	No of units (000's)	Average value per share BD	Total BD 000's
Safana Investment WLL (RIA 1) and NS12	6,254	1.00	6,254	-	-	-	-	-	-	6,254	1.00	6,254
Shaden Real Estate Investment WLL (RIA 5)	3,434	1.00	3,434	-	-	-	-	-	-	3,434	1.00	3,434
Locata Corporation Pty Ltd (RIA 6)	2,633	0.38	993	-	-	-	-	-	-	2,633	0.38	993
			10,681	-	-	-	-	-	-			10,681

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENT OF SOURCES AND USES OF ZAKAH AND CHARITY FUND
for the year ended 31 December 2020

BD 000's

	2020	2019
Sources of zakah and charity fund		
At 1 January	714	708
Contributions by the Bank	218	187
Non-Islamic income	40	54
Total sources	972	949
Uses of zakah and charity fund		
Contributions to charitable organisations	(276)	(235)
Total uses	(276)	(235)
Undistributed zakah and charity fund at 31 December	696	714

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2020

BD 000's

1. REPORTING ENTITY

Khaleeji Commercial Bank BSC ("the Bank"), a public shareholding company listed on Bahrain Bourse, was incorporated on 24 November 2004 in the Kingdom of Bahrain under Commercial Registration No. 55133. The Bank operates under an Islamic retail banking license granted by the Central Bank of Bahrain ("CBB") on 20 October 2003. The Bank's Additional Tier 1 securities were listed on London Stock Exchange (International Securities Market) in 2020.

The Bank's activities are regulated by the CBB and supervised by a Shari'a Supervisory Board to ensure adherence to Shari'a rules and principles in its activities.

The principal activities of the Bank include retail and corporate banking, consumer finance, wealth management, structured investment products and project financing facilities which comply with Islamic Shari'a rules and principles as determined by the Bank's Shari'a Supervisory Board.

The consolidated financial statements include the results of the Bank and its subsidiaries (together "the Group"). The significant subsidiaries are as follows:

Name	Country of incorporation	% holding 2020	% holding 2019	Nature of business
Harbour West 2 Real Estate SPC	Bahrain	100%	100%	To hold property.
Harbour West 4 Real Estate SPC	Bahrain	100%	100%	To hold property .
Surooh Limited	Cayman Islands	19.08%	19.08%	To construct and sell properties at "Oryx Hills".
H.H. Hospitality SPC (Note 27)	Bahrain	86%	-	Hospitality business
KHCB Tier 1 Sukuk Limited	Cayman Islands	100%	-	To issue sukuk

2. STATEMENT OF COMPLIANCE

The consolidated financial statements of the Group have been prepared in accordance with applicable rules and regulations issued by the CBB. These rules and regulations require the adoption of all Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation of Islamic Financial Institutions ("AAOIFI"), except for:

- a) recognition of modification losses on financial assets arising from 6 months payment holidays provided to customers impacted by COVID-19 without profit, in equity instead of the profit or loss as required by FAS. Any other modification gain or loss on financial assets are recognised in accordance with the requirements of applicable FAS.

The modification loss has been calculated as the difference between the net present value of the modified cash flows calculated using the original effective profit rate and the current carrying value of the financial assets on the date of modification; and

- b) recognition of financial assistance received from the government and/ or regulators as part of to its COVID-19 support measures that meets the government grant requirement, in equity, instead of the profit or loss as required by the statement on "Accounting implications of the impact of COVID-19 pandemic" issued by AAOIFI to the extent of any modification loss recognised in equity as a result of (a) above. In case this exceeds the modification loss amount, the balance amount is recognized in the profit or loss. Any other financial assistance is recognised in accordance with the requirements of FAS.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**for the year ended 31 December 2020**

BD 000's

2. STATEMENT OF COMPLIANCE (CONTINUED)

The above framework for basis of preparation of the consolidated financial statements is hereinafter referred to as 'Financial Accounting Standards as modified by CBB'.

The modification to accounting policies have been applied retrospectively and did not result in any change to the comparatives.

In line with the requirements of AAOIFI and the CBB rule book, for matters not covered by AAOIFI standards, the group takes guidance from the relevant International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB").

3. BASIS OF MEASUREMENT

The consolidated financial statements have been prepared on the historical cost basis except for equity securities that are measured at fair value through equity and structured notes that are measured at fair value through income statement.

4. USE OF SIGNIFICANT JUDGEMENTS AND ESTIMATES

The preparation of consolidated financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. Management believes that the underlying assumptions are appropriate and the Group's consolidated financial statements therefore present the financial position and results fairly. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 25

5. SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies applied in the preparation of these consolidated financial statements are set out below. These accounting policies have been consistently applied by the Group and are consistent with those used in the previous year except as described in Note 2 above "statement of compliance" and those arising from the adoption of the following standards and amendments to Standards early adopted by the Group.

i) Standards issued not yet effective but early adopted**a) FAS 31 – Investment Agency (Al-Wakala Bi Al-Istithmar)**

The Group has early adopted FAS 31 as issued by AAOIFI in 2019 effective 1 January 2021. The objective of this standard is to establish the principles of accounting and financial reporting for investment agency (Al- Wakala Bi Al- Istithmar) instruments and the related assets and obligations from both the principal (investor) and the agent perspectives.

The Group uses Wakala structure to raises funds from interbank market and from customers, and these were reported as liabilities under placements from financial institutions and placements from non-financial institutions and individuals, respectively as of 31 December 2019. All funds raised using Wakala structure, together called "Wakala pool" are comingled with the Bank's jointly financed pool of funds based on an underlying equivalent Mudaraba arrangement.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

i) Standards issued not yet effective but early adopted (continued)

a) FAS 31 – Investment Agency (Al-Wakala Bi Al-Istithmar) (continued)

This comingled pool of funds is invested in a common pool of assets of in the manner which the Group deems appropriate without any restrictions as to where, how and for what purpose the funds should be invested. After adopting FAS 31 on 1 January 2020, the Wakala pool is now classified as part of the Mudaraba pool of funding under equity of investment account holders and the profit paid on these contracts is reported as part of determination of return on investment of equity of investment account holders.

As per the transitional provisions of FAS 31, the entity may choose not to apply this standard on existing transactions executed before 1 January 2020 and have an original contractual maturity before 31 December 2020. However, the Bank decided to apply the standard retrospectively, thereby reclassifying all transactions outstanding as of the year end and the corresponding previous year end. The adoption of this standard has resulted in a change in classification of all Wakala based funding contracts as part of equity of investment account holders and additional associated disclosures (refer note 19).

b) FAS 33 - Investment in Sukuk, shares and similar instruments

The Group has early adopted FAS 33 as issued by AAOIFI effective 1 January 2021. The objective of this standard is to set out the principles for the classification, recognition, measurement and presentation and disclosure of investment in Sukuk, shares and other similar instruments made by Islamic financial institutions. This standard shall apply to an institution's investments whether in the form of debt or equity securities. This standard replaces FAS 25 Investment in Sukuk, shares and similar instruments.

The standard classifies investments into equity type, debt-type and other investment instruments. Investment can be classified and measured at amortized cost, fair value through equity or fair value through the income statement. Classification categories are now driven by business model tests and reclassification will be permitted only on change of a business model and will be applied prospectively.

Investments in equity instruments must be at fair value and those classified as fair value through equity will be subject to impairment provisions as per FAS 30 "Impairment, Credit Losses and Onerous Commitments". In limited circumstances, where the institution is not able to determine a reliable measure of fair value of equity investments, cost may be deemed to be best approximation of fair value.

The standard is effective from 1 January 2021 with an option to early adopt and is applicable on a retrospective basis. However, the cumulative effect, if any, attributable to owners' equity, equity of investment account holders relating to previous periods, shall be adjusted with investments fair value pertaining to assets funded by the relevant class of stakeholders.

The adoption of FAS 33 has resulted in changes in accounting policies for recognition, classification and measurement of investment in sukuks, shares and other similar instruments, however, the adoption of FAS 33 had no significant impact on any amounts previously reported in the consolidated financial statements for the year ended 31 December 2020 and the consolidated financial statement of the Group for the year ended 31 December 2019. Set out below are the details of the specific FAS 33 accounting policies applied in the current year.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

i) *Standards issued not yet effective but early adopted (continued)*

b) *FAS 33 - Investment in Sukuk, shares and similar instruments (continued)*

Changes in accounting policies

Categorization and classification

FAS 33 sets out classification and measurement approach for investments in sukuk, shares and similar instruments that reflects the business model in which such investments are managed and the underlying cash flow characteristics. Under the standard, each investment is to be categorized as either investment in:

- i) equity-type instruments;
- ii) debt-type instruments, including:
 - monetary debt-type instruments; and
 - non-monetary debt-type instruments; and
- iii) other investment instruments

Unless irrevocable initial recognition choices as per the standard are exercised, an institution shall classify investments as subsequently measured at either of (i) amortised cost, (ii) fair value through equity or (iii) fair value through income statement, on the basis of both:

- the Bank's business model for managing the investments; and
- the expected cash flow characteristics of the investment in line with the nature of the underlying Islamic finance contracts.

Reclassification of assets and liabilities

The adoption of FAS 33 has resulted in the following change in the classification of investments based on the reassessment of business model classification of the assets at 1 January 2020:

	Original classification under FAS 25	New classification under FAS 33	Original carrying amount under FAS 25	New carrying amount under FAS 33
Investment in sukuk	Amortised cost	Amortised cost	195,050	195,050
Investment securities	FVTPL	FVTE	11,174	11,174
Investment securities	FVTE	FVTE	32,815	32,815

ii) *New Standards, amendments to Standards issued but not yet effective and not early adopted.*

FAS 32 - Ijarah

This standard issued in 2020 supersedes the existing FAS 8 "Ijarah and Ijarah Muntahia Bittamleek", and effective for the financial periods beginning on or after 1 January 2021 with early adoption permitted.

The objective of this standard is to set out principles for the classification, recognition, measurement, presentation and disclosure for Ijarah (asset Ijarah, including different forms of Ijarah Muntahia Bittamleek) transactions entered into by the Islamic Financial Institutions as a lessor and lessee. This new standard aims to address the issues faced by the Islamic finance industry in relation to accounting and financial reporting as well as to improve the existing treatments in line with the global practices.

The Group is currently evaluating the impact of adopting this standard.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**for the year ended 31 December 2020**

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ii) *New Standards, amendments to Standards issued but not yet effective and not early adopted (continued).*

FAS 38 Wa'ad, Khiyar and Tahawwut

FAS 38 Wa'ad, Khiyar and Tahawwut was issued in 2020 and is effective for the financial reporting periods beginning on or after 1 January 2022.

The objective of this standard is to prescribe the accounting and reporting principles for recognition, measurement and disclosures in relation to shariah compliant Wa'ad (promise), Khiyar (option) and Tahawwut (hedging) arrangements for Islamic financial institutions.

This standard classifies Wa'ad and Khiyar arrangements into two categories as follows:

- a) "ancillary Wa'ad or Khiyar" which is related to a structure of transaction carried out using other products i.e. Murabaha, Ijarah Muntahia Bittamleek, etc.; and
- b) "product Wa'ad and Khiyar" which is used as a stand-alone Shariah compliant arrangement.

Further, the standard prescribes accounting for constructive obligations and constructive rights arising from the stand-alone Wa'ad and Khiyar products.

The Group is currently evaluating the impact of adopting this standard.

(a) Basis of consolidation**(i) Business combination**

The Group accounts for business combinations using the acquisition method when the acquired set of activities and assets meet the definition of a business and control is transferred to the Group.

The consideration transferred in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain on a bargain purchase is recognised in profit or loss immediately. Transaction costs are expensed as incurred, except if related to the issue of debt or equity securities.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of financial instrument is classified as equity, then it is not re-measured and settlement is accounted for within equity. Otherwise, other contingent consideration is re-measured at fair value at each reporting date and subsequent changes in the fair value of the contingent consideration are recognized in profit or loss.

(ii) Subsidiaries

Subsidiaries are those enterprises (including special purpose entities) controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group and de-consolidated from the date that control ceases. Control is presumed to exist, when the Group owns more than 50% of voting rights on an entity.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020**

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)*(a) Basis of consolidation (continued)**(ii) Subsidiaries (continued)*

Special purpose entities (SPEs) are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets, or the execution of a specific borrowing or investment transaction and usually voting rights are relevant for the operating of such entities. An investor that has decision-making power over an investee and exposure to variability of returns determines whether it acts as a principal or as an agent to determine whether there is a linkage between power and returns. When the decision maker is an agent, the link between power and returns is absent and the decision maker's delegated power does not lead to a control conclusion. Where the Group's voluntary actions, such as lending amounts in excess of existing liquidity facilities or extending terms beyond those established originally, change the relationship between the Group and an SPE, the Group performs a reassessment of control over the SPE.

The Group in its fiduciary capacity manages and administers assets held in trust and other investment vehicles on behalf of investors.

The financial statements of SPE are not included in these consolidated financial statements except when the Group controls the entity. Information about the Group's fiduciary assets under management is set out in note 26.

(iii) Equity accounted investees

The Group's interests in equity accounted investees comprise interests in associates and a joint venture.

Associates are those entities over which the Group holds exercises significant influence, but not control or joint control, over the financial and operating policies. A Joint venture is an arrangement in which the Group has joint control whereby the Group has rights to the net assets of the arrangement, rather than rights to its assets and obligations for its liabilities. These are accounted for using the equity method.

Investments in associates and joint ventures are initially recognised at cost including transactions cost and the carrying amount is adjusted to recognise the Group's share of the post-acquisition profits or losses of the investee after the date of acquisition. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in the investor's proportionate interest in the investee arising from changes in the investee's equity. When the Group's share of losses exceeds its interest in the investee, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued, except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the investee.

The carrying amount of the equity accounted investee is tested for impairment in accordance with the policy described in note 5 (k).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**for the year ended 31 December 2020**

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)*(a) Basis of consolidation (continued)***(iv) Transactions eliminated on consolidation**

Intra-group balances and transactions, and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Intra-group gains on transactions between the Group and its equity accounted associates are eliminated to the extent of the Group's interest in the investees. Unrealised losses are also eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. Accounting policies of the subsidiaries and associates have been changed where necessary to ensure consistency with the policies adopted by the Group.

(b) Foreign currency transactions

Items included in the consolidated financial statements of the Group are measured using the currency of the primary economic environment in which the entity operates ('the functional currency').

Foreign currency transactions are translated using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement. Translation differences on non-monetary items carried at their fair value, such as certain equity securities measured at fair value through equity, are included in investments fair value reserve.

The other Group companies functional currencies are either denominated in Bahraini dinars or US dollars which is effectively pegged to the Bahraini dinar. Hence, the translation of financial statements of the group entities that have a functional currency different from the presentation currency do not result in an exchange difference.

(c) Investment securities

Investment securities comprise investments in equity securities and investments in debt-type securities, sukuk. Investment securities exclude investments in subsidiaries and equity accounted investees (refer note 5(a)).

(i) Classification

The Group segregates its investment securities into debt-type and equity-type instruments. Debt-type instruments are investments that have terms that provide fixed or determinable payments of instruments and include instruments that evidence a residual interest in the assets of an entity after deducting all its liabilities profits and capital. Equity-type instruments are investments that do not exhibit features of debt-type.

Debt-type Instruments:

A debt-type investment is classified and measured at amortised cost only if the instrument is managed on a contractual yield basis or the instrument is not held for trading and has not been designated at FVTIS. Debt-type investments at amortised cost include investment in sukuk.

Equity-type investments:

Investments in equity type instruments are classified in the following categories: 1) at fair value through income statement ('FVTIS') or 2) at fair value through equity ('FVTE'), consistent with its investment strategy.

The Group has one investment in structured notes that is designated at FVTIS. The rest are classified as investments at fair value through equity.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Investment securities (continued)

(ii) Recognition and de-recognition

Investment securities are recognised at the trade date i.e. the date that the Group contracts to purchase or sell the asset, at which date the Group becomes party to the contractual provisions of the instrument.

Investment securities are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risk and rewards of ownership.

(iii) Measurement

Investment securities are measured initially at fair value, which is the value of the consideration given. For FVTIS investments, transaction costs are expensed in the income statement. For other investment securities, transaction costs are included as a part of the initial recognition.

Subsequent to initial recognition, investments carried at FVTIS and FVTE are re-measured to fair value. Gains and losses arising from a change in the fair value of investments carried at FVTIS are recognised in the income statement in the period in which they arise. Gains and losses arising from a change in the fair value of investments carried at FVTE are recognised in the consolidated statement of changes in equity and presented in a separate fair value reserve within equity. The fair value gains/losses are recognised taking into consideration the split between portions related to owners' equity and equity of investment account holders. When the investments carried at FVTE are sold, impaired, collected or otherwise disposed of, the cumulative gain or loss previously recognised in the statement of changes in equity is transferred to the income statement.

Subsequent to initial recognition, debt-type securities, other than those carried at FVTIS, are measured at amortised cost using the effective profit method less any impairment allowances.

(iv) Measurement principles

Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus capital repayments, plus or minus the cumulative amortisation using the effective profit method of any difference between the initial amount recognised and the maturity amount, minus any reduction (directly or through use of an allowance account) for impairment or uncollectability. The calculation of the effective profit rate includes all fees and points paid or received that are an integral part of the effective profit rate.

Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

The best evidence of the fair value of a financial instrument on initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received.

When one is available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as 'active' if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**for the year ended 31 December 2020**

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)*(c) Investment securities (continued)**(iv) Measurement principles (continued)*

If a market for a financial instrument is not active or there is no market, the Group establishes fair value using well-recognised valuation techniques that may include recent arm's length transactions between knowledgeable, willing parties (if available), discounted cash flows or market multiples for similar instruments.

Some or all of the inputs into these models may not be market observable, but are estimated based on assumptions. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument.

Fair value estimates involve uncertainties and matters of significant judgement and therefore, cannot be determined with precision. There is no certainty about future events (such as continued operating profits and financial strengths). It is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions could require a material adjustment to the carrying amount of the investments.

In determining fair valuation, the Group in many instances relies on the financial data of investees and on estimates by the management of the investee companies as to the effect of future developments.

The fair value of a financial liability with a demand feature (e.g. a demand deposit) is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Group recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

(d) Financing assets

Financing assets comprise Shari'a compliant financing contracts with fixed or determinable payments. These include financing provided through Murabaha, Musharaka, Mudharaba, Istisna and Wakala contracts. Financing assets are recognised on the date they are originated and are carried at their amortised cost less impairment allowances, if any.

(e) Placements with and from financial institutions, non-financial institutions and individuals

These comprise inter-bank and over the counter customer placements made/received using Shari'a compliant contracts. Placements are usually for short-term and are stated at their amortised cost.

(f) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents comprise cash and bank balances (excluding CBB reserve account), and placement with financial institutions with original maturities of three months or less when acquired which are subject to insignificant risk of changes in fair value and are used by the Group in the management of its short-term commitments.

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020**

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(g) Assets acquired for leasing**

Assets acquired for leasing (Ijarah Muntahia Bittamleek) are stated at cost less accumulated depreciation and any impairment. Under the terms of lease, the legal title of the asset passes to the lessee at the end of the lease term, provided that all lease instalments are settled. Depreciation is calculated on a straight line basis at rates that systematically reduce the cost of the leased assets over the period of the lease. The Group assesses at each reporting date whether there is objective evidence that the assets acquired for leasing are impaired. Impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount. Impairment losses, if any, are recognised in the income statement. The estimates of future cash flows, when dependent on a single customer, takes into consideration the credit evaluation of the respective customer in addition to other factors.

(h) Investment in real estate*Investment property*

Real estate properties held for rental, or for capital appreciation purposes, or both, are classified as investment property. Investment property are carried at cost less depreciation and impairment allowances. Cost includes expenditure that is directly attributable to the acquisition of the investment property. Investment property includes plots of land held for undetermined use and property leased to third parties. Land is not depreciated.

Development property

Development property is measured at lower of cost or net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less costs to complete development and selling expenses.

Development property comprise a property being developed as a hotel in the Kingdom of Bahrain.

Trading properties

Trading properties are measured at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business less costs to complete development and selling expenses.

Trading properties include properties for the sale in the ordinary course of business.

(i) Property and equipment

Property and equipment is stated at cost, net of accumulated depreciation and impairment allowances, if any. Property includes land which is not depreciated. Other equipment is depreciated using the straight-line method to write-off the cost of the assets over their estimated useful lives ranging from 3 to 5 years. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(j) Impairment of financial instruments

i) Exposures subject to credit risk

The Group recognises loss allowances for ECLs on:

- Cash and bank balances;
- Placements with financial institutions;
- Financing assets;
- Assets acquired for leasing (including lease rental receivable);
- Investments in Sukuk - debt-type securities at amortised cost; and
- Undrawn financing commitments and financial guarantee contracts issued.

The Group measures loss allowances at an amount equal to lifetime ECLs, except for the following, which are measured at 12-month ECLs:

- Debt-type securities that are determined to have low credit risk at the reporting date; and
- other debt-type securities and bank balances for which credit risk (i.e. the risk of default occurring over the expected life of the financial instrument) has not increased significantly since initial recognition.

When determining whether the credit risk of an exposure subject to credit risk has increased significantly since initial recognition when estimating ECLs, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and informed credit assessment including forward-looking information.

The Group assumes that the credit risk on a financial asset has increased significantly if it is more than 30 days past due.

The Group considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security, if any is held; or
- the financial asset is more than 90 days past due

The Group considers a debt security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of 'investment grade'. The Group considers this to be BBB- or higher per S&P.

The Group applies a three-stage approach to measuring ECL on exposures subject to credit risk. Assets migrate through the following three stages based on the change in credit quality since initial recognition.

Stage 1: 12-months ECL

Stage 1 includes exposures subject to credit risk on initial recognition and that do not have a significant increase in risk since initial recognition or that have low credit risk. 12-month ECL is the expected credit losses that from default events that are possible within 12 months after the reporting date. It is not the expected cash shortfalls over the 12-month period but the entire credit loss on an asset weighted by the probability that the loss will occur in the next 12-months.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(j) Impairment of financial instruments (continued)

i) Exposures subject to credit risk (continued)

Stage 2: Lifetime ECL - not credit impaired

Stage 2 includes exposures subject to credit risk that have had a significant increase in credit risk since initial recognition but that do not have objective evidence of impairment. For these assets, lifetime ECL are recognised. Lifetime ECL are the expected credit losses that result from all possible default events over the expected life of the financial instrument. Expected credit losses are the weighted average credit losses with the life-time probability of default ('PD').

Stage 3: Lifetime ECL - credit impaired

Stage 3 includes exposures subject to credit risk that have objective evidence of impairment at the reporting date in accordance with the indicators specified in the CBB's rule book. For these assets, lifetime ECL is recognised.

The maximum period considered when estimating ECLs is the maximum contractual period over which the Group is exposed to credit risk.

Measurement of ECLs

ECLs are a probability-weighted estimate of credit losses. They are measured as follows:

- Financing assets and assets acquired for leasing that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive).
- Financing assets and assets acquired for leasing that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- Undrawn financing commitment: as the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn and the cash flows that the Group expects to receive;
- Financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group expects to recover; and
- Purchased or originated credit-impaired financial assets are those assets that are credit-impaired on initial recognition. Their ECL is measured on a lifetime basis (stage 3).

ECLs are discounted at the effective profit rate of the financial instrument.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(j) Impairment of financial instruments (continued)

i) Exposures subject to credit risk (continued)

Credit-impaired exposures

At each reporting date, the Group assesses whether exposures subject to credit risk are credit-impaired. An exposure is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the exposure have occurred. Evidence that an exposure is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or being more than 90 days past due;
- the restructuring of a financing facility or advance by the Group on terms that the Group would not consider otherwise;
- it is probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for financial assets measured at amortised cost and assets acquired for leasing are deducted from the gross carrying amount of the assets. Loss on undrawn commitments and financial guarantees are disclosed in other liabilities.

ii) Impairment of equity investments classified at fair value through equity (FVTE)

In the case of investments in equity securities classified as FVTE, a significant or prolonged decline in the fair value of the security below its cost is an objective evidence of impairment. The group considers a decline of 30% to be significant and a period of nine months to be prolonged. If any such evidence exists, 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 income statement – is removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are subsequently reversed through equity.

(k) Impairment of non-financial assets

The carrying amount of the Group's non-financial assets (other than for financial assets covered above), are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of an asset is the greater of its value in use or fair value less costs to sell. An impairment loss is recognised whenever the carrying amount of an asset exceeds its estimated recoverable amount. Impairment losses are recognised in the income statement. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(k) Impairment of non-financial assets (continued)

In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash generating unit. An impairment loss is recognised whenever the carrying amount of an asset or its cash generating unit exceeds its estimated recoverable amount. Impairment losses are reversed only if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount.

(l) Customers' current accounts

Balances in current (non-investment) accounts are recognised when received by the Group. The transaction are measured at the cash equivalent amount received by the Group at the time of contracting. At the end of the accounting period, the accounts are measured at their book value.

(m) Equity of investment account holders

Equity of investment account holders are funds held by the Group in unrestricted investment accounts, which it can invest at its own discretion. The investment account holder authorises the Group to invest the account holders' funds in a manner which the Group deems appropriate without laying down any restrictions as to where, how and for what purpose the funds should be invested.

The Group charges management fee (Mudarib fees) to investment account holders. Of the total income from investment accounts, the income attributable to customers is allocated to investment accounts after setting aside provisions, reserves (Profit equalisation reserve and Investment risk reserve) and deducting the Group's share of income as a Mudarib. The allocation of income is determined by the management of the Group within the allowed profit sharing limits as per the terms and conditions of the investment accounts. Only the income earned on pool of assets funded from IAH are allocated between the owners' equity and investment account holders. Administrative expenses incurred in connection with the management of the funds are borne directly by the Group and are not charged separately to investment accounts.

The Group charges specific provision and collective provision to owners' equity. Amounts recovered from these impaired assets is not subject to allocation between the IAH and owners' equity.

Investment accounts are carried at their book values and include amounts retained towards profit equalisation, investment risk reserves, if any. Profit equalisation reserve is the amount appropriated by the Group out of the Mudaraba income, before allocating the Mudarib share, in order to maintain a certain level of return to the deposit holders on the investments. Investment risk reserve is the amount appropriated by the Group out of the income of investment account holders, after allocating the Mudarib share, in order to cater against future losses for investment account holders. Creation of any of these reserves results in an increase in the liability towards the pool of unrestricted investment accounts.

(n) Restricted investment accounts

Restricted investment accounts represent assets acquired by funds provided by holders of restricted investment accounts and their equivalent and managed by the Group as an investment manager based on either a Mudharaba contract or agency contract. The restricted investment accounts are exclusively restricted for investment in specified projects as directed by the investments account holders. Assets that are held in such capacity are not included as assets of the Group in the consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(o) Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. A financial guarantee contract is recognised from the date of its issue. The liability arising from a financial guarantee contract is recognised at the present value of any expected payment, when a payment under the guarantee has become probable.

(p) Treasury shares

The amount of consideration paid including all directly attributable costs incurred in connection with the acquisition of the treasury shares are recognised in equity. Consideration received on sale of treasury shares is presented in the financial statements as a change in equity. No gain or loss is recognised in the income statement on sale of treasury shares.

(q) Statutory reserve

The Bahrain Commercial Companies Law 2001 requires that 10 per cent of the annual net profit be appropriated to a statutory reserve which is normally distributable only on dissolution. Appropriations may cease when the reserve reaches 50 per cent of the paid up share capital.

(r) Revenue recognition

Income from Murabaha and Wakala contracts are recognised on a time-apportioned basis over the period of the contract using the effective profit method.

Profit or losses in respect of the Group's share in **Musharaka and Mudharaba financing** transaction that commence and end during a single financial period are recognised in the income statement at the time of liquidation (closure of the contract). Where the Musharaka and Mudharaba financing continues for more than one financial period, profit is recognised to the extent that such profits are being distributed during that period in accordance with profit sharing ratio as stipulated in the agreements.

Istisna'a revenue and the associated profit margin is recognised using the percentage of completion method.

Income from assets acquired for leasing (Ijarah Muntahia Bittamleek) are recognised proportionately over the lease term.

Income from sukuk and income/expenses on placements is recognised at its effective profit rate over the term of the instrument.

Dividend income is recognised when the right to receive is established.

Rental income is recognised on a straight line basis over the term of the contract.

Fees and commission income that are integral to the effective profit rate on a financial asset carried at amortised cost are included in the measurement of the effective profit rate of the financial asset. Other fees and commission income, including account servicing fees, sales commission, management fees, placement and arrangement fees and syndication fees, are recognised as the related services are performed.

(s) Earnings prohibited by Shari'a

The Group is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity account where the Group uses these funds for charitable purposes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2020

BD 000's

5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(t) Zakah

Zakah is calculated on the Zakah base of the Group in accordance with FAS 9 Zakah using the net assets method. Zakah is paid by the Group based on the eligible reserve and retained earnings balances at the end of the year and the remaining Zakah is payable by individual shareholders. The Group calculates and notifies the shareholders of their pro-rata share of the Zakah payable annually. The Group also pays Zakah on the balance of treasury shares held at the year-end based on the pro-rata share of Zakah. The calculations of Zakah is approved by the Shari'a Supervisory Board. Payment of Zakah on the unrestricted investment and other accounts is the responsibility of the investment account holders.

(u) Employee benefits***(i) Short-term benefits***

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

(ii) Post-employment benefits

Pensions and other social benefits for Bahraini employees are covered by the Social Insurance Organisation scheme, which is a "defined contribution scheme" in nature, and to which employees and employers contribute monthly on a fixed-percentage-of-salaries basis. Contributions by the Group are recognised as an expense in income statement when they are due.

Expatriate employees on fixed contracts are entitled to leaving indemnities payable under the Bahraini Labour Law, based on length of service and final remuneration. Provision for this unfunded commitment has been made by calculating the notional liability had all employees left at the reporting date.

These benefits are in the nature of "defined benefit scheme" and any increase or decrease in the benefit obligation is recognised in the income statement.

The Group also operates a voluntary employees saving scheme under which the Group and the employee contribute monthly on a fixed percentage of salaries basis. The scheme is managed and administered by a board of trustees who are employees of the Group. The scheme is in the nature of a defined contribution scheme and contributions by the Group are recognised as an expense in the income statement when they are due.

(iii) Share-based employee incentive scheme

The grant-date fair value of equity-settled share-based payment arrangements granted to employees is generally recognised as an expense, with a corresponding increase in equity, over the vesting period of the awards. The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market performance conditions are expected to be met, such that the amount ultimately recognised is based on the number of awards that meet the related service and non-market performance conditions at the vesting date.

For share-based payment awards with non-vesting conditions, the grant-date fair value of the share-based payment is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**for the year ended 31 December 2020**

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(v) Dividends and board remuneration**

Dividends to shareholders and board remuneration are recognised as liabilities in the period in which they are declared.

(w) Trade date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. the date that the Group commits to purchase or sell the asset.

(x) Offsetting

Financial assets and liabilities are offset only when there is a legal or Shari'a based 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.

(y) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

(z) URIA Protection Scheme

Funds held with the Group in investment accounts and current accounts are covered by the Deposit and URIA Protection Scheme ('the Scheme') established by the Central Bank of Bahrain regulation in accordance with Resolution No (34) of 2010.

The Scheme applies to all eligible accounts held with the Group subject to certain specific exclusions, maximum total amount entitled and other regulations governing the establishment of a Deposit and URIA Protection Scheme and a Deposit Protection Board.

(aa) Repossessed assets

In certain circumstance, properties are repossessed following the foreclosure on financing facilities that are in default. Repossessed properties are measured at the lower of carrying value and fair value less cost to sell in accordance with IFRS 5 "Non-current assets held for sale and discontinued operation".

(bb) Term Borrowings

Term borrowings represents borrowing obtained through murabaha contract recognized on the origination date and carried at amortized cost.

6. CASH AND BANK BALANCES

	31 December 2020	31 December 2019
Cash	5,031	5,299
Balances with banks	33,280	42,601
Balances with the Central Bank:		
- Current account	29,292	31,047
- Reserve account	15,414	25,430
Less: Impairment allowance	-	(1)
	83,017	104,376

The reserve account with the Central Bank of Bahrain is not available for day-to-day operational purposes.

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7. PLACEMENTS WITH FINANCIAL INSTITUTIONS

	31 December 2020	31 December 2019
Gross Murabaha and Wakala receivable	17,720	65,524
Less: Deferred profits	-	(15)
Less: Impairment allowance	-	(1)
	17,720	65,508

The average profit rate on placement with financial institutions for 2020 was 1.55% per annum (31 December 2019: 3.07% per annum).

8. FINANCING ASSETS

	31 December 2020	31 December 2019
Murabaha	322,220	354,510
Musharaka	104	104
Wakala	90	5,007
Mudharaba	1,014	1,047
Istisna	1,344	1,733
	324,772	362,401
Less: Impairment allowances	(17,055)	(38,046)
	307,717	324,355

Murabaha financing receivables are net of deferred profits of BD 18,862 thousand (2019: BD 25,724 thousand).

The movement on impairment allowances is as follows:

2020	Stage 1	Stage 2	Stage 3	Total
At 1 January 2020	4,581	2,730	30,735	38,046
Net movement between stages	85	(1,701)	1,616	-
Charge for the year	2,672	905	1,180	4,757
Write back for the year	-	-	(2,046)	(2,046)
Write-off	-	-	(11,010)	(11,010)
Disposal	(108)	-	(12,584)	(12,692)
At 31 December 2020	7,230	1,934	7,891	17,055

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8. FINANCING ASSETS (CONTINUED)

2019	Stage 1	Stage 2	Stage 3	Total
At 1 January 2019	4,762	3,695	13,566	22,023
Net movement between stages	(20)	(1,221)	1,241	-
Net charge for the year	(161)	256	15,928	16,023
Write-off	-	-	-	-
At 31 December 2019	4,581	2,730	30,735	38,046

9. INVESTMENT IN SUKUK

Debt type instruments – at amortized cost

- Quoted sukuk *

- Unquoted sukuk

Less: Impairment allowances

31 December 2020	31 December 2019
261,539	195,061
1,317	1,317
(1,724)	(1,328)
261,132	195,050

* Quoted Sukuk of BD 113,952 thousand are pledged against term borrowings of BD 75,477 (refer note 17).

10. ASSETS ACQUIRED FOR LEASING

Cost

At 1 January

Additions during the year

Settlements/adjustments during the year

At 31 December

Accumulated depreciation

At 1 January

Charge for year

Settlements during the year

At 31 December

Net book value at 31 December

2020	2019
168,309	138,952
34,618	53,688
(33,521)	(24,331)
169,406	168,309
39,212	30,274
17,494	16,714
(14,234)	(7,776)
42,472	39,212
126,934	129,097

At 31 December 2020, accrued lease rental receivable amounted to BD 12,820 thousand (2019: BD 17,102 thousand). Lease rental receivable is net of stage 1 and 2 ECL of BD 969 thousands (2019: BD 516 thousand) and Stage 3 ECL of BD 3,014 thousand (2019: BD 2,705 thousand). During the year, an impairment allowance of BD 762 thousand (2019: BD 765 thousand) was provided on the lease rental receivables (note 23).

Of the total net book value of assets acquired for leasing, consumer financing amounted to BD 83,394 thousand (2019: BD 84,958 thousand).

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for the year ended 31 December 2020

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11. INVESTMENT SECURITIES

	31 December 2020	31 December 2019
<i>At fair value through income statement</i>		
- Structured notes	15,080	-
<i>At fair value through equity</i>		
- unquoted equity securities*	40,812	43,989
	55,892	43,989

* additional impairment charge for the year of BD 500 thousand was made (2019: BD 2,667 thousand).

12. INVESTMENT IN REAL ESTATE

	2020	2019
Investment property	15,081	15,081
Development property	65,522	6,251
Trading properties	3,000	3,000
Impairment allowance	(300)	(300)
	83,303	24,032

- (i) *Investment property*
Investment property comprise plots of land in the Kingdom of Bahrain and United Arab Emirates, net of impairment allowance of BD 300 thousand (2019: BD 300 thousand).

The fair value of investment property as of 31 December 2020 was BD 15,259 thousand, determined by an external independent real estate valuer based on sales comparison approach and accordingly has been categorised as level 2 in the fair value hierarchy.

- (ii) *Development property*
Development property comprise mainly a property under construction in Bahrain Financial Harbour in the Kingdom of Bahrain acquired during the year from the Parent part of a swap transaction (refer note 27).

- (iii) *Trading properties*
Trading properties comprise villas for sale in the ordinary course of business.

The net realisable value of development property and trading properties were determined by external, independent property valuers, having appropriate recognised professional qualification and recent experience in the location and category of the property being valued.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

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13. EQUITY ACCOUNTED INVESTEEES

	2020	2019
At 1 January	4,524	4,575
Additions during the year	27,759	-
Share of loss for the year	(320)	(51)
At 31 December	31,963	4,524

Name	Country of incorporation	% holding		Nature of business
		2020	2019	
Amlak II	Kingdom of Bahrain	23.51%	23.51%	Investment in real estate
Capital Real Estate Projects Company	Kingdom of Bahrain	30.00%	30.00%	Real estate development
NS 12	Kingdom of Bahrain	28.41%	28.41%	Investment in real estate
Lagoon Real Estate Development	Kingdom of Bahrain	22.97%	-	Investment in real estate
Al Areen Hotels W.L.L.	Kingdom of Bahrain	50.00%	-	Hospitality business

During the year, the Group acquired 50% stake in Al Areen Hotels W.L.L., a Bahraini incorporated company operating in the hospitality business from the parent as part of the Parent's subscription to a subordinated Modaraba (additional Tier One Capital securities) issued by the Bank (refer to Note 35). The investment is accounted for as joint venture based on shareholders' agreement.

14. OTHER ASSETS

	31 December 2020	31 December 2019
Reposessed assets	15,708	13,513
Profit accrued on Sukuk	3,836	3,250
Due from investments	1,044	985
Prepaid expenses	608	776
Other receivables*	6,450	5,445
	27,646	23,969

*This is net of impairment allowance of BD 1,742 thousand (2019: BD 1,742 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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15. PROPERTY AND EQUIPMENT

	Land	Furniture and fixtures	Computers	Motor vehicle and Other equipment	Work-in-progress	2020 Total	2019 Total
Cost							
At 1 January	6,714	4,471	5,254	576	175	17,190	16,843
Additions	-	7	152	1	111	271	452
Disposals	-	(103)	-	-	(11)	(114)	(105)
Transfer	-	-	81	-	(81)	-	-
At 31 December	6,714	4,375	5,487	577	194	17,347	17,190
Accumulated Depreciation							
At 1 January	-	4,350	4,583	507	-	9,440	8,978
Charge for year (note 22)	-	47	466	36	-	549	567
Disposals	-	(92)	-	-	-	(92)	(105)
At 31 December	-	4,305	5,049	543	-	9,897	9,440
Net book value							
At 31 December 2020	6,714	70	438	34	194	7,450	7,750
At 31 December 2019	6,714	121	671	69	175	7,750	

16. PLACEMENTS FROM NON-FINANCIAL INSTITUTIONS AND INDIVIDUALS

	31 December 2020	31 December 2019
Non-financial institutions	96,635	51,660
Individuals	117,608	82,994
	214,243	134,654

These represent placements in the form of Murabaha and Wakala contracts, net of deferred profit of BD 5,622 thousand (2019: BD 5,218 thousand).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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17. TERM BORROWINGS

As of 31 December 2020, the Bank had five term Murabaha facilities of BD 75,477 thousand secured by pledge over sukuk of BD 113,952 thousand.

18. OTHER LIABILITIES

	31 December 2020	31 December 2019
Mudaraba profit accrual	5,581	8,911
Advance received from customers	443	3,274
Employee related accruals	269	1,251
Zakah and charity payable	696	714
Payable for Istisna'a contracts	27	27
Other payables and accrued expenses	6,253	5,621
	13,269	19,798

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2020

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19. EQUITY OF INVESTMENT ACCOUNT HOLDERS

	31 December 2020	31 December 2019
Placements and borrowings from financial institutions – Wakala	-	10,355
Mudaraba	425,349	511,835
	425,349	522,190

The funds received from investment account holders have been commingled and jointly invested with the Group in the following asset classes:

	31 December 2020	31 December 2019
Balances with banks	33,280	42,601
CBB reserve account	15,414	25,430
Placements with financial institutions	17,720	65,508
Debt type instruments – sukuk	261,132	195,050
Financing assets	97,803	193,601
	425,349	522,190

As at 31 December 2020, the balance of profit equalisation reserve and investment risk reserve was Nil (2019: Nil).

The Group does not allocate non-performing assets to IAH pool. All the impairment allowances are allocated to owners' equity. Recoveries from non-performing financial assets are also not allocated to IAH accountholders.

Only profits earned on pool of assets funded from IAH are allocated between the owners' equity and IAH. The Group did not charge any administration expenses to investment accounts.

Following is the average percentage for profit allocation between owner's equity and investment accountholders.

	2020		2019	
	Mudarib share	IAH shares	Mudarib share	IAH shares
1 month Mudharaba *	87.96%	12.04%	80.61%	19.39%
3 months Mudharaba	75.35%	24.65%	65.38%	34.62%
6 months Mudharaba	71.57%	28.43%	60.00%	40.00%
12 months Mudharaba	62.50%	37.50%	42.96%	57.04%
18 months Mudharaba	60.09%	39.91%	38.65%	61.35%
24 months Mudharaba	67.35%	32.65%	43.11%	56.89%
36 months Mudharaba	55.72%	44.28%	32.37%	67.63%

* Includes savings, Al Waffer and Call Mudaraba accounts.

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19. EQUITY OF INVESTMENT ACCOUNT HOLDERS(CONTINUED)

During the year, average mudarib share as a percentage of total income allocated to IAH was 60.72% (2019: 46.56%) as against the average mudarib share contractually agreed with IAH. Hence the Group sacrificed average mudarib fees of 3.17% (2019: 12.83%).

The Group does not share profits resulting from the assets funded through current accounts and other funds received on the basis other than mudarba contract.

The funds raised from IAH are deployed in the assets on a priority basis after setting aside certain amount in cash and placement with Banks for liquidity management purposes

20. SHARE CAPITAL

	31 December 2020	31 December 2019
Authorised:		
3,000,000,000 ordinary shares of BD 0.100 each	300,000	300,000
Issued and fully paid up:		
892,119,480 ordinary shares (2019: 1,050,000,000) of BD 0.100 each	89,212	105,000

In their Extra -ordinary meeting on 25 March 2020, the shareholders resolved to write-off losses of BD 15,788 thousand against paid up capital by reducing the number of shares. The Group has only one class of equity shares and the holders of these shares have equal voting rights. At 31 December 2020, the Group holds 92,048,004 as treasury shares (2019: 105,573,476 shares).

Distribution schedule of equity shares, setting out the number of holders and percentage in the following categories:

31 December 2020

Categories*	Number of Shares	Number of Shareholders	% of total outstanding shares
Less than 1%	117,417,814	541	13.16
1% up to less than 5%	104,880,910	5	11.76
5% up to less than 10% **	175,490,264	2	19.67
10% up to less than 20%	-	-	-
20% and less than 50%	-	-	-
50% and above	494,330,492	1	55.41
	892,119,480	549	100.00

* Expressed as a percentage of total outstanding shares of the Bank.

** Includes treasury shares.

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20. *SHARE CAPITAL (continued)*

31 December 2019

Categories*	Number of Shares	Number of Shareholders	% of total outstanding shares
Less than 1%	137,765,476	604	13.12
1% up to less than 5%	122,049,555	5	11.62
5% up to less than 10% **	296,694,051	3	28.26
10% up to less than 20%	-	-	-
20% and less than 50%	493,490,918	1	47.00
50% and above	-	-	-
	1,050,000,000	613	100.00

* Expressed as a percentage of total outstanding shares of the Bank.

** Includes treasury shares.

Names and nationalities of the major shareholders and the number of equity shares held in which they have an interest of 5% or more of outstanding shares:

31 December 2020

	Nationality	Number of shares	% of total outstanding shares
GFH Financial Group*	Bahrain	494,330,492	55.41
Khaleeji Commercial Bank B.S.C	Bahrain	88,411,540	9.91
Goldilocks Investment Company Limited	UAE	87,078,724	9.76

*These shares are held by KHCB Asset Company on behalf of GFH Financial Group, the Parent.

31 December 2019

	Nationality	Number of shares	% of total outstanding shares
GFH Financial Group*	Bahrain	493,490,918	47.00
Goldilocks Investment Company Limited	UAE	104,779,110	9.98
Khaleeji Commercial Bank B.S.C	Bahrain	103,592,516	9.87
Emirates Islamic Bank PJSC	UAE	88,322,425	8.41

*These shares are held by KHCB Asset Company on behalf of GFH Financial Group, the Parent.

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21. STAFF COST

	2020	2019
Salaries and short-term benefits	4,974	7,073
Social insurance expenses	835	964
Other staff expenses	65	121
	5,874	8,158

22. OTHER OPERATING EXPENSES

	2020	2019
Premises cost	773	1,059
Advertisement and marketing expenses	157	660
Professional fees	743	1,194
Information technology expenses	549	536
Board expenses	216	244
Communication expenses	135	286
Distribution channel expenses	663	589
Depreciation expense	549	567
Other operating expenses	738	901
	4,523	6,036

23. NET IMPAIRMENT CHARGE

	2020	2019
Balances and placements with banks and financial institutions	(2)	(50)
Financing assets (note 8)	2,711	16,023
Investments in sukuk (note 9)	401	8
Assets acquired for leasing - including lease rentals receivables (note 10)	762	765
Investment securities (note 11)	500	2,667
Investment in real estate (note 12)	-	300
Other assets	-	788
Commitments and financial guarantees	(31)	(112)
	4,341	20,389

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24. SHARE-BASED EMPLOYEE INCENTIVE SCHEME

The shareholders, in their annual general meeting held on 30 March 2015, approved the employee share based incentive scheme (the "scheme") in line with the CBB's Sound Remuneration Practices. Under the share incentive scheme, certain covered employees are granted the Group's shares as compensation for their performance.

In 2018 the Group had incorporated a Trust, Khaleeji Commercial Bank Employee Benefit Trust ("Trust"), to hold the beneficial interest of the shares under the scheme.

As per the scheme, the share awards from each performance year will vest immediately but will be released over three years period from the date of grant. The share awards are subject to an additional retention period of six months from the date of completion of deferred period, after which the employee is unconditionally allowed to sell the shares in the market. The scheme allows the Bank's Nomination, Remuneration and Governance Committee ("BNRGC") to determine that, if appropriate, un-awarded shares can be forfeited or clawed back in certain situations.

As at 31 December 2020, 3,636,464 shares were held by the Trust (2019: 1,980,960 shares). During the year, 2,827,275 shares (2019: 1,182,516 shares) shares were awarded to the employees as awards under the terms of the scheme subject to a three-year deferment period.

During the year, the Group transferred 896,634 shares (2019: 1,465,997 shares) to the employees.

During the year, the shareholders resolved to write-off accumulated losses of BD 15,788 thousand against paid up capital by reducing the number of shares (refer Note 20). Accordingly, the number of shares held by the trust was reduced by 297,862 shares.

25. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group makes judgments, estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectation of future events that are believed to be reasonable under the circumstances. However, the process of making the required estimates and assumptions involved further challenges due to the prevailing uncertainties arising from Covid-19.

I. Judgements

- a) Establishing the criteria for determining whether credit risk on an exposure subject to credit risk has increased significantly since initial recognition, determining methodology for incorporating forward looking information into measurement of ECL and selection and approval of models used to measure ECL is set out in Note 5j(i) and Note 35.

Covid 19 impact

Covid 19 was declared a worldwide pandemic by the World Health Organisation in March 2020. Covid 19 and related measures taken by governments worldwide to slow the spread of the virus, have since had a significant impact on the local and global economy, supply chains and financial markets.

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25. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (CONTINUED)*I. Judgements (continued)**Covid 19 impact (continued)*

The Group has considered the impact of COVID-19 and related market volatility in preparing these consolidated financial statements. While the methodologies and assumptions applied in the measurement of various items within the financial statements remain unchanged from those applied in the 2020 consolidated financial statements, the impact of COVID-19 has resulted in the application of further judgement and the incorporation of estimates and assumptions specific to the impact of COVID-19.

Principally this has resulted in updates to the Group's economic assumptions used in determining expected credit losses (ECL) and the impairment assessment for other non-financial assets.

The Group's risk and capital management framework continues to be applied and the Group continues to monitor the impact of COVID-19 on the Group's risk and capital profile. Non-financial risks reemerging from local and global movement restrictions, and remote working by staff, counterparties, clients and suppliers, are being identified, assessed, managed and governed through timely application of the Group's Risk Management Framework.

Financing portfolio

In accordance with the CBB relief measures, the Group has introduced a number of support measures for customers impacted by COVID-19, including the deferral of payments without profit for retail and small business customers for an initial period of six months without profit which was later extended by another 4 months with profit.

Impairment allowance on financing portfolio at amortised cost

In determining the appropriate level of expected credit losses (ECLs) the Group considered the macro-economic outlook, customer credit quality, the type of collateral held, exposure at default, and the effect of payment deferral options as at the reporting date.

The ECL methodology, significant increase in credit risk (SICR) thresholds, and definition of default remain consistent with those used as at 31 December 2020.

The model inputs, including forward-looking information, scenarios and associated weightings, were revised to reflect the current outlook. Noting the wide range of possible scenarios and macroeconomic outcomes, and the relative uncertainty of how the social and economic consequences of COVID-19 will materialize, these scenarios represent reasonable and supportable forward-looking views as at the reporting date.

The Group's models are calibrated to consider past performance and macrocosmic forward-looking variables as inputs. The global regulators have issued guidance, to consider the exceptional circumstances of the Covid 19 pandemic. This includes consideration of significant government support and the high degree of uncertainty around historic long-term trends used in determining reasonable and supportable forward-looking information as well as the assessment of underlying credit deterioration and migration of balances to progressive stages.

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25. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (CONTINUED)*I. Judgements (continued)**Impairment allowance on financing portfolio at amortised cost (continued)*

The Group considers both qualitative and quantitative information in the assessment of significant increase in credit risk. The utilisation of a payment deferral program was not considered an immediate trigger for a significant increase in credit risk ("SICR") or a staging migration for the purposes of calculating ECL, given the purpose of these programs is to provide temporary cash flow relief to the Group's customers affected by the COVID-19.

The Group continues to assess borrowers for other indicators of unlikeliness to pay, taking into consideration the underlying cause of any financial difficulty and whether it is likely to be temporary as a result of COVID-19 or longer term.

b. Classification of investments

In the process of applying the Group's accounting policies, management decides on acquisition of an investment whether it should be classified as 1) debt type instruments carried at fair value through equity or at amortised cost, or 2) equity-type instruments carried at fair value through equity or at fair value through income statement. The classification of each investment reflects the management's intention in relation to each investment and is subject to different accounting treatments based on such classification (refer note 5 (c) (i)).

*c. Impairment of equity investments at fair value through equity – (refer to Note 5 (j) (ii))***II. Estimations***a) Impairment of financing assets at amortised cost*

- Determining inputs into ECL measurement model including incorporation of forward-looking information is set out in Note 5(j) and Note 35; and
- Ky assumptions used in estimating recoverable cash flows

*b) Measurement of fair value of unquoted equity investments (level 3) -refer to Note 5c (iv) and Note 34**c) Assessment of impairment of investment in real estate (Note 5(h, 5(k)) and Note 12).***26. ASSETS UNDER MANAGEMENT**

The Group provides corporate administration, investment management and advisory services to its investment entities, which involves making decisions on behalf of such entities. Assets that are held in such capacity are not included in these consolidated financial statements. At the reporting date, the Group had assets under management of BD 267.98 million (31 December 2019: BD 262.25 million). During the year, the Group has not charged any management fees (2019: BD Nil) for the management of these assets.

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27. RELATED PARTY TRANSACTIONS

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties include the parent company, other significant shareholders and entities over which the Group and the shareholders exercises significant influence, directors, sharia board members and executive management of the Group. The transactions with these parties were made on agreed commercial terms.

During the year, the Group entered into a swap transaction with its Parent at agreed terms by transferring assets of BD 46.4 million comprising financing assets of BD 27.7 million, Sukuk of BD 7.5 million and equity investment of BD 11.2 million in exchange for a 86% stake in HH Hospitality SPC, a Bahraini company incorporated solely to own a hotel under construction in the Kingdom of Bahrain. The transaction was assessed as an asset acquisition and did not result in any gain or loss for the Bank. The property under development was recognised at the fair value on the date of transfer.

31 December 2020

	Associates	Significant shareholders / entities in which directors are interested	Total
Transactions with related parties			
Underwriting fee on Subordinated Mudaraba	-	12,100	12,100
Sub-ordinated Mudaraba	-	60,000	60,000
Cash injection of AT1 Capital	-	23,600	23,600
Investment in associates	24,500	-	24,500
Acquisition of development property	-	60,000	60,000
Sale of financial assets	-	46,376	46,376
Transfer of financial assets	-	18,433	18,433
Profit distribution on AT 1 Capital	-	2,834	2,834

Details of Directors' interests in the Bank's ordinary shares as at the end of the year were nil (2019: 1,050,763 shares representing less than 1% of total outstanding shares of the Bank were held by one director).

Compensation of key management personnel

Key management personnel of the Group comprise of the Board of Directors and key members of management having authority and responsibility for planning, directing and controlling the activities of the Group.

The key management personnel compensation during the year is as follows:

	2020	2019
Board member fees and allowances	236	254
Salaries and other short-term benefits	1,452	1,150

The key management personnel balances as of the end the year is as follows:

	2020	2019
Balances due to key management as compensation	228	426

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27. RELATED PARTY TRANSACTIONS (CONTINUED)

The related party balances and transactions (except for compensation of key managerial personnel) included in these consolidated financial statements are as follows:

31 December 2020

	Associates	Directors / Key management personnel and shari'a board members	Parent company / other significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Assets					
Financing assets	-	3,576	6,671	-	10,247
Investment securities	-	-	2,284	18,537	20,821
Equity accounted investees	31,963	-	-	-	31,963
Other assets	117	-	-	825	942
Liabilities					
Placement from financial institutions, Non-FIs and individuals	-	2,105	42,438	-	44,543
Customers' current accounts	135	85	6,784	1,211	8,215
Equity of investment account holders	413	241	79,846	327	80,827
Other liabilities	-	-	1,030	-	1,030

31 December 2019

	Associates	Directors / Key management personnel and shari'a board members	Parent company / other significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Assets					
Financing assets	-	2,017	5,710	-	7,727
Investment securities	-	-	2,284	18,051	20,335
Equity accounted investees	4,524	-	-	-	4,524
Other assets	121	-	-	865	986
Liabilities					
Placement from financial institutions, Non-FIs and individuals	-	1,784	-	-	1,784
Customers' current accounts	194	61	5,634	1,207	7,096
Equity of investment account holders	404	598	122,880	380	124,262

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27. RELATED PARTY TRANSACTIONS (CONTINUED)

2020	Associates	Directors / Key management personnel and shari'a board members	Parent company / other significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Income					
Income from financing assets and assets acquired for leasing	-	100	987	-	1,087
Fees and other income	(320)	-	2	-	(318)
Expenses					
Finance expense on placements from financial institutions, non-financial institutions and individuals	-	100	1,937	-	2,037
Return to investment account holders	14	2	1,820	9	1,845
Staff cost	-	1,452	-	-	1,452
Other expenses	-	-	-	25	25

2019	Associates	Directors / Key management personnel and shari'a board members	Parent company / other significant shareholders / entities in which directors are interested	Assets under management (including special purpose entities)	Total
Income					
Income from financing assets and assets acquired for leasing	-	128	373	-	501
Fees and other income	(42)	-	-	-	(42)
Expenses					
Finance expense on placements from financial institutions, non-financial institutions and individuals	-	-	2,931	-	2,931
Return to investment account holders	15	18	4,153	11	4,197
Staff cost	-	1,150	-	-	1,150
Other expenses	-	-	-	32	32

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28. EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the profit for the year by the weighted average number of equity shares outstanding during the year adjusted for impact arising from shares issued under the employee share incentive scheme.

Basic EPS	2020	2019
Profit attributable to parent for the year (BD 000's)	7,986	(14,937)
Weighted average number of equity shares (Nos. in 000's)	803,874	804,820
Basic earnings per share (in fils)	9.94	(18.56)

The Group did not have any dilutive instruments as of 31 December 2020 and December 2019.

29. SHARI'A SUPERVISORY BOARD

The Group's Shari'a Supervisory Board consists of three Islamic scholars who review the Group's compliance with general Shari'a principles and specific fatwas, rulings and guidelines issued. Their review includes examination of evidence relating to the documentation and procedures adopted by the Group to ensure that its activities are conducted in accordance with Islamic Shari'a principles.

30. ZAKAH

Zakah is directly borne by the shareholders on distributed profits and investment account holders. The Group currently does not collect or pay Zakah on behalf of its shareholders and investors in restricted investment accounts. Zakah payable by the shareholders is computed by the Group on the basis of the method prescribed by the Group's Shari'a Supervisory Board and notified to shareholders annually. During the year, the Shari'a Supervisory Board has computed Zakah payable of BD 246 thousand (2019: BD 222 thousand) of which BD 230 thousand (2019: 218 thousand) represents the Zakah computed on the statutory reserve and cumulative retained earnings as at 31 December 2020, payable by the Group. The remaining Zakah balance amounting to BD 16 thousand or 0.018 fils per share (2019: BD 4 thousand or 0.003 fils per share) is due and payable by the shareholders. The Group will pay Zakah of BD 1.6 thousand (2019: BD 0.4 thousand) on the treasury shares held as of 31 December 2020 based on 0.018 fils per share.

31. SEGMENT REPORTING

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, whose operating results are regularly reviewed by the Group's chief operating decision maker (Board of Directors) to make decisions about resource allocation to each segment and assess its performance and for which discrete financial information is available. An operating segment is divided into business segment and geographic segments. For management purposes, the Group is organised into two major business segments:

Corporate and retail banking

Providing customer services such as accepting Mudaraba deposits, savings account and current account facilities, fund transfer facilities, bill payment facilities. It also provides financing facilities (in the form of Commodity Murabaha, Musharaka, Istisna'a and Ijarah facilities) to corporate clients and High-Networth-Individuals and consumer finance products. This segment includes money market and treasury services in the form of short term Commodity Murabaha and Wakala to banks, financial institutions and investments in sukuk to manage funding of the Group.

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31. SEGMENT REPORTING (CONTINUED)*Investment banking*

Primarily relates to conceptualising of investment deals and performing roles of an arranger, lead manager, and administrator of the funds (involves structuring of deals, raising of funds through private placement and fund administration). Also offers products like Restricted Investment Accounts (RIA) and management of funds raised through the RIA structures. Also involves carrying out strategic investments in the form of equity contribution (either in the funds created and managed by the Group or other institutions).

Segment performance is measured based on results for each department as mentioned in the internal management reports that are reviewed by the Board of directors on a quarterly basis. Segment results is used to measure performance as management believes that such information is the most relevant in evaluating the results of certain segments relative to other entities that operate in these industries.

The Group reports directly attributable revenue and cost relating to transactions originating from respective segments as segment revenue and segment cost respectively. Indirect costs and corporate overheads are treated as unallocated. The internal management reports are designed to reflect revenue and cost for respective segments which are measured against the budgeted figures.

The Group primarily operates from Bahrain and does not have any overseas branches/divisions. The geographic concentration of assets and liabilities is disclosed in note 33 (b) to the consolidated financial statements.

The Group is winding down in investment banking business.

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31. SEGMENT REPORTING (CONTINUED)

These segments are the basis on which the Group reports its primary segment information. Transactions between segments (if any) are conducted on an arm's length basis

31 December 2020

	Investment Banking	Corporate and Retail Banking	Unallocated	Total
Cash and bank balances	2	83,015	-	83,017
Placements with financial institutions	902	16,818	-	17,720
Financing assets	-	307,717	-	307,717
Investment in sukuk	-	261,132	-	261,132
Assets acquired for leasing (including lease rentals receivables)	-	139,754	-	139,754
Investment securities	55,892	-	-	55,892
Investment in real estate	83,303	-	-	83,303
Equity accounted investees	31,963	-	-	31,963
Other assets	16,069	4,894	6,683	27,646
Property and equipment	-	-	7,450	7,450
Total segment assets	188,131	813,330	14,133	1,015,594
Placements from financial institutions	-	79,545	-	79,545
Placements from non-financial institutions and individuals	-	214,243	-	214,243
Term borrowings	-	75,477	-	75,477
Customers' current accounts	902	54,774	-	55,676
Other liabilities	1,591	8,364	3,314	13,269
Total segment liabilities	2,493	432,403	3,314	438,210
Equity of investment account holders	-	425,349	-	425,349
Restricted investment accounts	10,681	-	-	10,681

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31. SEGMENT REPORTING (CONTINUED)

2020

	Investment Banking	Corporate and Retail Banking	Unallocated	Total
Income from financing assets and assets acquired for leasing	(175)	30,096	-	29,921
Income from placements with financial institutions	28	523	-	551
Income from sukuk	-	15,242	-	15,242
Income from investment securities	366	-	-	366
Fees and other income	(308)	2,425	-	2,117
Total income before return to investment account holders	(89)	48,286	-	48,197
Less: Return to investment account holders before Bank's share as Mudarib	-	(21,575)	-	(21,575)
Bank's share as a Mudarib	-	9,289	-	9,289
Return to investment account holders	-	(12,286)	-	(12,286)
Less:				
Expense on placements from financial institutions, non- financial institutions and individuals	-	(12,472)	-	(12,472)
Finance expense on term borrowings	-	(796)	-	(796)
Total segment income	(89)	22,732	-	22,643
Staff cost	587	2,350	2,937	5,874
Other expenses	93	825	3,605	4,523
Total segment expenses	680	3,175	6,542	10,397
Segment results before impairment allowances	(769)	19,557	(6,542)	12,246
Net impairment charge	(500)	(3,841)	-	(4,341)
Segment results	(1,269)	15,716	(6,542)	7,905

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31. SEGMENT REPORTING (CONTINUED)

31 December 2019	Investment Banking	Corporate and Retail Banking	Unallocated	Total
Cash and bank balances	1	104,375	-	104,376
Placements with financial institutions	1,184	64,324	-	65,508
Financing assets	-	324,355	-	324,355
Investment in sukuk	-	195,050	-	195,050
Assets acquired for leasing (including lease rentals receivables)	-	146,199	-	146,199
Investment securities	43,989	-	-	43,989
Investment in real estate	24,032	-	-	24,032
Equity accounted investees	4,524	-	-	4,524
Other assets	13,906	4,182	5,881	23,969
Property and equipment	-	-	7,750	7,750
Total segment assets	87,636	838,485	13,631	939,752
Placements from financial institutions	-	117,098	-	117,098
Placements from non- financial institutions and individuals	-	134,654	-	134,654
Term borrowings	-	-	-	-
Customers' current accounts	1,184	56,921	-	58,105
Other liabilities	1,847	13,647	4,304	19,798
Total segment liabilities	3,031	322,320	4,304	329,655
Equity of investment account holders	-	522,190	-	522,190
Restricted investment accounts	10,681	-	-	10,681

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31. SEGMENT REPORTING (CONTINUED)

2019	Investment Banking	Corporate and Retail Banking	Unallocated	Total
Income from financing assets and assets acquired for leasing	102	31,232	-	31,334
Income from placements with financial institutions	39	2,144	-	2,183
Income from sukuk	-	10,031	-	10,031
Income from investment securities	(1,687)	-	-	(1,687)
Fees and other income	(51)	5,777	-	5,726
Total income before return to investment account holders	(1,597)	49,184	-	47,587
Less: Return to investment account holders before Bank's share as Mudarib	-	(27,059)	-	(27,059)
Bank's share as a Mudarib	-	8,457	-	8,457
Return to investment account holders	-	(18,602)	-	(18,602)
Less:				
Expense on placements from financial institutions, non- financial institutions and individuals	-	(8,188)	-	(8,188)
Finance expense on term borrowings	-	(1,241)	-	(1,241)
Total segment income	(1,597)	21,153	-	19,556
Staff cost	816	3,263	4,079	8,158
Other expenses	101	1,262	4,673	6,036
Total segment expenses	917	4,525	8,752	14,194
Segment results before impairment allowances	(2,514)	16,628	(8,752)	5,362
Net impairment charge	(2,968)	(17,421)	-	(20,389)
Segment results	(5,482)	(793)	(8,752)	(15,027)

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32. MATURITY PROFILE

The maturity profile of placements with and from financial institutions, financing assets, assets acquired for leasing, (including lease rental receivable), and equity of investment account holders has been presented using their contractual maturity period. For other balances, maturity profile is based on expected cash flows/ settlement profile of the respective assets and liabilities.

31 December 2020	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total
Assets						
Cash and bank balances	75,238	1,875	3,918	1,986	-	83,017
Placements with financial institutions	17,720	-	-	-	-	17,720
Financing assets	43,397	18,839	37,549	123,057	84,875	307,717
Investment in sukuk	249,716	11,416	-	-	-	261,132
Assets acquired for leasing (including lease rentals receivables)	5,266	3,724	7,457	32,884	90,423	139,754
Investment securities	-	-	22,622	15,549	17,721	55,892
Investment in real estate	-	-	-	-	83,303	83,303
Equity accounted investees	-	923	1,981	-	29,059	31,963
Other assets	953	206	61	26,426	-	27,646
Property and equipment	-	-	-	-	7,450	7,450
Total assets	392,290	36,983	73,588	199,902	312,831	1,015,594
Liabilities						
Placements from financial institutions	32,906	34,948	8,077	3,614	-	79,545
Placements from non-financial institutions and individuals	86,708	62,708	45,795	14,369	4,663	214,243
Term borrowings	67,915	7,562	-	-	-	75,477
Customers' current account	17,117	5,419	5,884	6,724	20,532	55,676
Other liabilities	4,918	1,651	1,589	5,111	-	13,269
Total liabilities	209,564	112,288	61,345	29,818	25,195	438,210
Equity of investment account holders	95,829	73,308	107,892	73,093	75,227	425,349
Restricted investment accounts	-	-	-	10,681	-	10,681
Commitments and financial guarantees	6,896	4,796	5,495	17,459	6,923	41,569

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32. MATURITY PROFILE (CONTINUED)

31 December 2019	Up to 3 months	3 to 6 months	6 months-1 year	1 to 3 years	Over 3 years	Total
Assets						
Cash and bank balances	90,605	4,727	5,485	3,559	-	104,376
Placements with financial institutions	65,508	-	-	-	-	65,508
Financing assets	75,634	24,168	38,425	121,509	64,619	324,355
Investment in sukuk	195,050	-	-	-	-	195,050
Assets acquired for leasing (including lease rentals receivables)	6,106	11,191	8,358	38,729	81,815	146,199
Investment securities	-	-	7,056	15,549	21,384	43,989
Investment in real estate	-	-	-	-	24,032	24,032
Equity accounted investees	-	923	1,981	-	1,620	4,524
Other assets	844	138	12	22,975	-	23,969
Property and equipment	-	-	-	-	7,750	7,750
Total assets	433,747	41,147	61,317	202,321	201,220	939,752
Liabilities						
Placements from financial institutions	-	-	15,637	101,461	-	117,098
Placements from non-financial institutions and individuals	37,914	39,623	41,594	12,232	3,291	134,654
Term borrowings	-	-	-	-	-	-
Customers' current account	17,864	5,655	6,141	7,018	21,427	58,105
Other liabilities	6,731	2,164	3,305	7,598	-	19,798
Total liabilities	62,509	47,442	66,677	128,309	24,718	329,655
Equity of investment account holders	124,172	86,311	126,115	92,855	92,737	522,190
Restricted investment accounts	-	-	-	10,681	-	10,681
Commitments and financial guarantees	32,422	7,579	5,203	35,406	102	80,712

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33. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS

(a) Industry sector

31 December 2020

	Banks and financial institutions	Real estate	Others	Total
Assets				
Cash and bank balances	83,017	-	-	83,017
Placements with financial institutions	17,720	-	-	17,720
Financing assets	4,420	89,532	213,765	307,717
Investment in sukuk	1,137	21,177	238,818	261,132
Assets acquired for leasing (including lease rentals receivables)	-	127,333	12,421	139,754
Investment securities	22,785	28,952	4,155	55,892
Investment in real estate	-	83,303	-	83,303
Equity accounted investees	-	31,963	-	31,963
Other assets	1,400	16,982	9,264	27,646
Property and equipment	-	6,739	711	7,450
Total assets	130,479	405,981	479,134	1,015,594
Liabilities				
Placements from financial institutions	79,545	-	-	79,545
Placements from non-financial institutions and individuals	1,209	42,798	170,236	214,243
Term borrowings	75,477	-	-	75,477
Customers' current accounts	848	8,524	46,304	55,676
Other liabilities	-	398	12,871	13,269
Total liabilities	157,079	51,720	229,411	438,210
Equity of investment account holders	20,343	59,171	345,835	425,349
Restricted investment accounts	-	9,688	993	10,681
Commitments and financial guarantees	-	15,015	26,554	41,569

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**33. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS
AND RESTRICTED INVESTMENT ACCOUNTS (CONTINUED)**

(a) Industry sector (continued)

31 December 2019

	Banks and financial institutions	Real estate	Others	Total
Assets				
Cash and bank balances	104,376	-	-	104,376
Placements with financial institutions	65,508	-	-	65,508
Financing assets	7,857	72,043	244,455	324,355
Investment in sukuk	11,737	7,539	175,774	195,050
Assets acquired for leasing (including lease rentals receivables)	-	133,657	12,542	146,199
Investment securities	11,174	29,147	3,668	43,989
Investment in real estate	-	24,032	-	24,032
Equity accounted investees	-	4,524	-	4,524
Other assets	954	14,871	8,144	23,969
Property and equipment	-	6,739	1,011	7,750
Total assets	201,606	292,552	445,594	939,752
Liabilities				
Placements from financial institutions	117,098	-	-	117,098
Placements from non-financial institutions and individuals	-	-	134,654	134,654
Term borrowings	-	-	-	-
Customers' current accounts	4,661	7,422	46,022	58,105
Other liabilities	17	588	19,193	19,798
Total liabilities	121,776	8,010	199,869	329,655
Equity of investment account holders	18,792	119,463	383,935	522,190
Restricted investment accounts	-	9,688	993	10,681
Commitments and financial guarantees	-	51,779	28,933	80,712

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33. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS (CONTINUED)**(b) Geographic sector****31 December 2020**

	GCC countries	Europe	America	Asia	Australia	Total
Assets						
Cash and bank balances	74,873	2,693	5,442	9	-	83,017
Placements with financial institutions	17,720	-	-	-	-	17,720
Financing assets	305,606	-	-	2,111	-	307,717
Investment in sukuk	261,132	-	-	-	-	261,132
Assets acquired for leasing (including lease rentals receivables)	139,626	-	-	128	-	139,754
Investment securities	22,275	15,080	-	14,383	4,154	55,892
Investment in real estate	83,303	-	-	-	-	83,303
Equity accounted investees	31,963	-	-	-	-	31,963
Other assets	26,706	131	-	808	1	27,646
Property and equipment	7,450	-	-	-	-	7,450
Total assets	970,654	17,904	5,442	17,439	4,155	1,015,594
Liabilities						
Placements from financial institutions	79,545	-	-	-	-	79,545
Placements from non-financial institutions and individuals	214,158	10	-	75	-	214,243
Term borrowings	48,945	26,532	-	-	-	75,477
Customers' current accounts	54,945	260	-	471	-	55,676
Other liabilities	13,269	-	-	-	-	13,269
Total liabilities	410,862	26,802	-	546	-	438,210
Equity of investment account holders	417,914	42	-	7,393	-	425,349
Restricted investment accounts	9,688	-	-	-	993	10,681
Commitments and financial guarantee	41,569	-	-	-	-	41,569

Concentration by location for financing assets is measured based on the location of the counterparty, which has a high correlation with the location of the collateral for the exposure.

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33. CONCENTRATION OF ASSETS, LIABILITIES, EQUITY OF INVESTMENT ACCOUNT HOLDERS AND RESTRICTED INVESTMENT ACCOUNTS (CONTINUED)*(b) Geographic sector (continued)*

31 December 2019	GCC countries	Europe	America	Asia	Australia	Total
Assets						
Cash and bank balances	91,971	1,593	10,786	26	-	104,376
Placements with financial institutions	65,508	-	-	-	-	65,508
Financing assets	320,083	4,258	-	14	-	324,355
Investment in sukuk	195,050	-	-	-	-	195,050
Assets acquired for leasing (including lease rentals receivables)	146,160	-	-	39	-	146,199
Investment securities	25,938	-	-	14,383	3,668	43,989
Investment in real estate	24,032	-	-	-	-	24,032
Equity accounted investees	4,524	-	-	-	-	4,524
Other assets	23,203	15	-	750	1	23,969
Property and equipment	7,750	-	-	-	-	7,750
Total assets	904,219	5,866	10,786	15,212	3,669	939,752
Liabilities						
Placements from financial institutions	117,098	-	-	-	-	117,098
Placements from non-financial institutions and individuals	134,654	-	-	-	-	134,654
Term borrowings	-	-	-	-	-	-
Customers' current accounts	57,230	257	-	618	-	58,105
Other liabilities	19,798	-	-	-	-	19,798
Total liabilities	328,780	257	-	618	-	329,655
Equity of investment account holders	519,655	694	-	1,841	-	522,190
Restricted investment accounts	9,688	-	-	-	993	10,681
Commitments and financial guarantee	80,712	-	-	-	-	80,712

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34. FAIR VALUE

a) Fair value

Fair value is an amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The fair value of quoted Sukuk carried at amortised cost of BD 261,539 thousand (31 December 2019: BD 195,061 thousand) is BD 275,366 thousand as at 31 December 2020 (31 December 2019: BD 204,198 thousand).

In case of financing assets and lease receivables, the average profit rate of the portfolio is in line with current market rates for similar facilities and hence after consideration of adjustment for prepayment risk and impairment charges it is expected that the current value would not be materially different to fair value of these assets. The estimated fair values of the Group's other financial instruments are not significantly different from their carrying values due to their short-term nature.

b) Fair value hierarchy

The table below analyses the financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets and liabilities.
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

31 December 2020

Structured notes at fair value through income statement
 Unquoted equity type securities carried at fair value through equity

Level 1	Level 2	Level 3	Total
-	15,080	-	15,080
-	-	40,812	40,812
-	15,080	40,812	55,892

31 December 2019

Unquoted equity type securities carried at fair value through income statement

Level 1	Level 2	Level 3	Total
-	-	11,174	11,174
-	-	11,174	11,174

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34. FAIR VALUE (CONTINUED)**b) Fair value hierarchy (continued)**

The table below shows the reconciliation of movements in value of investments measured using Level 3 inputs:

	2020	2019
At 1 January	11,174	13,148
Reclassification due to FAS 33 implementation	32,815	-
Fair value loss in income statement	(556)	(1,974)
Movement in foreign exchange reserve	348	-
Purchases	8,205	-
Settlements	(11,174)	-
At 31 December	40,812	11,174

The potential effect of using reasonable possible alternative assumptions for fair valuing equity investments classified as level 3 are summarised below:

31 December 2020

Valuation technique used	Key unobservable inputs	Fair value at 31 December 2020	Reasonable possible shift +/- (in average input)	Increase / (decrease) in valuation
Market multiples approach	Enterprise value to EBITDA	2,817	+/- 5%	103 / (103)
Market multiples approach	Price to book value	11,664	+/- 5%	702 / (702)
Market multiples approach	Price to total assets	1,142	+/- 5%	32 / (32)
Discounted cash flow	Cost of equity and terminal growth rate	792	+/- 5%	27 / (27)
		16,415		

31 December 2019

Valuation technique used	Key unobservable inputs	Fair value at 31 December 2019	Reasonable possible shift +/- (in average input)	Increase / (decrease) in valuation
Market multiples approach	Price to book value	11,174	+/- 5%	559 / (559)
		11,174		

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35. FINANCIAL RISK MANAGEMENT**Introduction and overview**

The Group has exposure to the following risks from its use of financial instruments:

- credit risk
- liquidity risk
- market risk

This note presents information about the Group's exposure to each of the above risks, its objectives, policies and processes for measuring and managing risk, and the Group's management of capital.

Risk management framework

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Board has established various committees with responsibilities for managing the overall risks associated with the Group. The committees also continuously monitors consistent implementation of the Board approved policies in the Group and reports deviations, if any, to the Board. The committees consists of heads of business and other functional units in the Group. The committees comprise the following: Management Committee (operational risks), Executive Credit and Investment Committee (credit and investment risks), and Assets and Liabilities Committee (market and capital risks). In addition to the Committees, the Board has established an independent Risk Management Department with an overall responsibility to identify, measure, control risks and recommend policies and corrective actions. Risk Management Department reports directly to the Board Audit and Risk Management Committee.

The Group's risk management policies are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Group, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment, in which all employees understand their roles and obligations.

The Group's Audit and Risk Management Committee is responsible for monitoring compliance with the risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Group. The Audit and Risk Management Committee is assisted in these functions by Internal Audit. Internal Audit undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit and Risk Management Committee.

CREDIT RISK

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's exposures to placements with financial institutions, financing assets, assets acquired for leasing (including lease rental receivable), investment in sukuk and other receivables. For risk management reporting purposes, the Group considers and consolidates all elements of credit risk exposure (such as individual and group exposure risk, country and sector concentration risk, related party exposure, etc.).

The uncertainties due to COVID-19 and resultant economic volatility has impacted the Group's financing operations and is expected to affect most of the customers and sectors to some degree. Although it is difficult to assess at this stage the degree of impact faced by each sector, the main industries impacted are hospitality, tourism, leisure, airlines/transportation and retailers. In addition, some other industries are expected to be indirectly impacted such as contracting, real estate and

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35. *FINANCIAL RISK MANAGEMENT (CONTINUED)*

CREDIT RISK (CONTINUED)

wholesale trading. Also, the volatility in oil prices during the early part of 2020, will have a regional impact due to its contribution to regional economies.

Considering this evolving situation, the Group has taken pre-emptive measures to mitigate credit risk by adopting more cautious approach for credit approvals thereby tightening the criteria for extending credit to impacted sectors.

Payment holidays have been extended to customers, including private and SME sector, in line with the instructions of CBB. These measures may lead to lower disbursement of financing facilities, resulting in lower net financing income and decrease in of other revenue.

In September 2020, the CBB issued another regulatory directive to extend the concessionary measures, i.e. payment holiday to customers till end of December 2020. However, customers will be charged profits during this payment holiday extension period, and hence the Group does not expect significant modification loss as a result of the extension. This payment holiday is expected to further delay expected contractual cash inflows of the Group for four months. However, the management will take appropriate steps to mitigate its impact on the liquidity position.

The Group has updated its inputs and assumptions for computation of ECL (refer note 25).

The Group manages its credit risks through its various business units, an independent Risk Management Department, Board Audit & Risk Management Committee ("BARMC"), and the Executive Credit & Investment Committee ("ECICOM"). The Credit risk management framework comprises the following:

- Formulating credit risk strategies policies and risk appetite which are developed after careful assessment of the market, capital requirement, regulatory rules, and the Board's risk appetite. The risk strategies and risk appetites are coded into policies approved by the Board. The Group's credit policy framework includes, inter alia, the following: in consultation with business units, credit risk management framework, credit risk mitigations, credit risk rating, credit risk pricing, expected credit loss, cross boarder business policy, personal finance product programs, approval authorities' matrix, and many others.
- Credit granting process. All credit exposures are assumed after careful assessment of the risks. Business proposals are initiated by the business units through formal credit applications. Such credit application provide adequate information about the proposed exposure including description of possible risks and mitigating factors. All credit applications are independently reviewed by Credit Review Unit to assess the adequacy of the due diligence conducted, independent assessment of the risks and mitigants, ensure compliance with limits and policies. Credit Review Unit issue formal opinion in respect of the proposals which may include recommendations for enhancing the Group's position. Proposals are then presented to approving authorities for their considerations (see proceeding point below). Where applicable and necessary, credit applications are also independently reviewed by the Sharia Compliance Officer to ensure adherence to Islamic principles.
- Establishing the authorisation structure for the approval and renewal of credit facilities. Approval authorities are documented in the Credit Authorities Policy of the Group which describes the various approval authorities, conditions, and limits for approving business transactions arising from investment and credit activities within the Group. There are 5 main levels of credit and investment authorities within the Group: Board of Directors, Board Investment & Credit Committee, Executive Credit & Investment Committee, Chief Executive Officer, and Heads of Business Units. Approval authorities are decided based on the magnitude of the risk and transactions size while at the same time allowing for smooth business operations.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)*CREDIT RISK (CONTINUED)*

- **Managing concentrations.** The Group places significant emphasis on diversifying its portfolio through applying a portfolio strategy in which the Group spreads its assets and liabilities' businesses so that results from volatility or fluctuations in such businesses become subdued, controlled, and assist in the consistent long-term growth of the shareholders' interests. An important element of such portfolio strategy is to establish limits within which the Management may conduct business. In principle, the Group shall adhere to all maximum limits established by regulatory authorities. At the same time, the Group has defined its own internal limits to control the following: Credit risk concentration, Counterparty limits, Industry limits, Country limits, Collateral concentration limits, Product mix, Maturity limits, amongst others. These internal limits are reviewed on periodic basis taking into considerations the following factors: The Group's risk appetite, Business and budget plans, Counterparty's risk rating, Risk rating of the Counterparty's country, The Group's financial positions including liquidity and Capital adequacy, General market condition; and other factors as determined by the Board of Directors or the Board Audit & Risk Management Committee. In general, the Group adopts a negative correlation between risks and limits in that lower limits are defined for higher risks.
- **Credit Measurement Methodologies.** The Group quantifies its credit risk using two main metrics: expected loss (EL) and economic capital (EC). The expected loss reflects the average value of the estimated losses (i.e. the cost of the business) and is associated with the Group's policy on provisions, while economic capital is the amount of capital necessary to cover unexpected losses (i.e. if actual losses are higher than expected losses). As part of its measurement techniques, the Group conducts adequate stress testing on its portfolio.
- **Credit risk rating.** An important tool in monitoring the quality of individual credits, as well as the total portfolio, is the use of Credit Risk Rating systems. The Group adopts a well-structured internal CRR system as a mean of differentiating the degree of credit risk in the different credit exposures of the Group to allow more accurate determination of the overall characteristics of the asset portfolio, concentrations, limits management, problem assets, pricing, and the adequacy of loss reserves (provisions). As well as identifying the risks associated with a counterparty and a credit facility, CRRs provide a key input for the capital charges and risk weights. The Group's approach to credit risk rating is documented in the Credit Risk Rating Policy which aims at achieving the following: (a) create a benchmark for assessing relative creditworthiness of the graded entity and measure credit risk in relation to the market, (b) arrive at a system of risk-based pricing for credit facilities granted by the Group, (c) monitor the overall credit risk inherent in the Group's Credit portfolio, (d) create a benchmark for recognition of accrued income on credit assets, (e) link asset review frequency and approval authority levels to Credit risk and emphasize focus on effective management of weak assets, and (f) provide a means to link Internal Capital Adequacy to the portfolio credit risk.
- **Classifications and identification of non-performing exposures.** The Group has adopted FAS 30 / IFRS 9 standards for classifying exposures into three stages. Accounts are moved into higher staging depending on occurrence of Significant Increase in Credit Risks. Exposures with past due exceeding 90 days are classified as non-performing.
Remedial management. All credit exposures assumed by the Group are considered after thorough risk and reward analysis adequate for the size and nature of business being considered. However, despite all due diligence exercised to minimize the risks involved, it is inevitable that certain exposures may experience setbacks due to various reasons such as: fundamental changes in the market conditions, changes in regulations and laws, changes in the status of counterparties (such as death, loss of job, sanctions, seizure of business, or bankruptcy), delays in deliverables (such as delays in completion of projects), or Unintentional errors in the initial assumptions. From business impact point of view, such exposures would have high costs due to suspension of profits, provisioning, liquidity, reputational, or opportunity costs. To prevent such adverse business impact, the Group has developed a prudent remedial strategy appropriate for the size, nature, and delinquency period. Such strategy is documented in the Remedial Management Policy. The Group, through its Remedial and Collection department pursue various recovery techniques including: dunning, rescheduling, restructuring, collateral foreclosure, legal actions, and cash settlement amongst others.

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

Exposures subject to credit risk

31 December 2020

Financing facilities

Grade 8 -10 Impaired

Past due but not impaired

Grade 1-6 Low-Fair Risk

Grade 7 Watch list

Past due comprises:

Up to 30 days

30-60 days

60-90 days

Neither past due nor impaired

Grade 1-6 Low-Fair Risk

Grade 7 Watch list

Gross carrying amount

Less: expected credit losses

Net carrying amount

Assets acquired for leasing (including lease rentals receivables)

Grade 8 -10 Impaired

Past due but not impaired

Grade 1-6 Low-Fair Risk

Grade 7 Watch list

Past due comprises:

Up to 30 days

30-60 days

60-90 days

Neither past due nor impaired

Grade 1-6 Low-Fair Risk

Grade 7 Watch list

Gross carrying amount

Less: expected credit losses

Net carrying amount

	Stage 1	Stage 2	Stage 3*	Total
Grade 8 -10 Impaired	-	-	39,977**	39,977
Past due but not impaired				
<i>Grade 1-6 Low-Fair Risk</i>	9,248	995	-	10,243
<i>Grade 7 Watch list</i>	25	16,540	-	16,565
<u>Past due comprises:</u>				
Up to 30 days	8,596	15,826	-	24,422
30-60 days	82	1,257	-	1,339
60-90 days	595	452	-	1,047
Neither past due nor impaired				
<i>Grade 1-6 Low-Fair Risk</i>	241,978	10,461	-	252,439
<i>Grade 7 Watch list</i>	209	5,339	-	5,548
Gross carrying amount	251,460	33,335	39,977	324,772
Less: expected credit losses	7,230	1,934	7,891	17,055
Net carrying amount	244,230	31,401	32,086	307,717
Assets acquired for leasing (including lease rentals receivables)				
Grade 8 -10 Impaired	-	-	15,208	15,208
Past due but not impaired				
<i>Grade 1-6 Low-Fair Risk</i>	10,783	10,773	-	21,556
<i>Grade 7 Watch list</i>	1,258	320	-	1,578
<u>Past due comprises:</u>				
Up to 30 days	2,781	360	-	3,141
30-60 days	2,016	110	-	2,126
60-90 days	7,244	10,623	-	17,867
Neither past due nor impaired				
<i>Grade 1-6 Low-Fair Risk</i>	83,624	10,579	-	94,203
<i>Grade 7 Watch list</i>	9,894	1,298	-	11,192
Gross carrying amount	105,559	22,970	15,208	143,737
Less: expected credit losses	545	424	3,014	3,983
Net carrying amount	105,014	22,546	12,194	139,754

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

Exposures subject to credit risk (continued)

31 December 2020

Investment in Sukuk

Grade 8 -10 Impaired

Stage 1	Stage 2	Stage 3	Total
-	-	1,317	1,317
261,539	-	-	261,539
261,539	-	1,317	262,856
407	-	1,317	1,724
261,132	-	-	261,132
95,706	-	-	95,706
95,706	-	-	95,706
-	-	-	-
95,706	-	-	95,706
-	-	727	727
38,108	2,627	-	40,735
-	107	-	107
38,108	2,734	727	41,569
155	6	76	237
37,953	2,728	651	41,332
744,035	56,675	44,931	845,641

Grade 1-6 Low-Fair Risk

Gross carrying amount

Less: expected credit losses

Net carrying amount

Balances with banks and placements

Grade 1-6 Low-Fair Risk

Gross carrying amount

Less: expected credit losses

Net carrying amount

Commitments and financial guarantees

Grade 8 -10 Impaired

Grade 1-6 Low-Fair Risk

Grade 7 Watch list

Gross carrying amount

Less: expected credit losses

Net carrying amount

Total net carrying amount

* Includes facilities under cooling off period of BD 24,405 thousand.

** includes BD 6,621 thousand of purchased or originated credit impaired assets (POCI).

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

Exposures subject to credit risk (continued)

31 December 2019	Stage 1	Stage 2	Stage 3*	Total
Financing facilities				
Grade 8 -10 Impaired	-	-	71,289	71,289
Past due but not impaired				
Grade 1-6 Low-Fair Risk	33,624	6,790	56	40,470
Grade 7 Watch list	9	6,867	6	6,882
<u>Past due comprises:</u>				
Up to 30 days	30,049	4,047	18	34,114
30-60 days	18	1,858	41	1,917
60-90 days	3,566	7,752	3	11,321
Neither past due nor impaired				
Grade 1-6 Low-Fair Risk	229,041	12,117	734	241,892
Grade 7 Watch list	87	1,780	1	1,868
Gross carrying amount	262,761	27,554	72,086	362,401
Less expected credit losses	4,581	2,730	30,735	38,046
Net carrying amount	258,180	24,824	41,351	324,355
Assets acquired for leasing (including lease rentals receivables)				
Grade 8 -10 Impaired	-	-	35,137	35,137
Past due but not impaired				
Grade 1-6 Low-Fair Risk	12,648	7,501	769	20,918
Grade 7 Watch list	-	3,272	-	3,272
<u>Past due comprises:</u>				
Up to 30 days	11,220	7,462	105	18,787
30-60 days	1,428	2,609	664	4,701
60-90 days	-	702	-	702
Neither past due nor impaired				
Grade 1-6 Low-Fair Risk	86,315	2,249	108	88,672
Grade 7 Watch list	-	1,421	-	1,421
Gross carrying amount	98,963	14,443	36,014	149,420
Less expected credit losses	140	376	2,705	3,221
Net carrying amount	98,823	14,067	33,309	146,199

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

31 December 2019	Stage 1	Stage 2	Stage 3	Total
Investment in Sukuk				
Grade 8 -10 Impaired	-	-	1,317	1,317
Grade 1-6 Low-Fair Risk	195,061	-	-	195,061
Gross carrying amount	195,061	-	1,317	196,378
Less: expected credit losses	11	-	1,317	1,328
Net carrying amount	195,050	-	-	195,050
Balances with banks and placements				
Grade 1-6 Low-Fair Risk	164,587	-	-	164,587
Gross carrying amount	164,587	-	-	164,587
Less: expected credit losses	2	-	-	2
Net carrying amount	164,585	-	-	164,585
Commitments and financial guarantees				
Grade 8 -10 Impaired	-	-	1,415	1,415
Grade 1-6 Low-Fair Risk	77,309	1,950	13	79,272
Grade 7 Watch list	-	25	-	25
Gross carrying amount	77,309	1,975	1,428	80,712
Less: expected credit losses	175	17	76	268
Net carrying amount	77,134	1,958	1,352	80,444
Total net carrying amount	793,772	40,849	76,012	910,633

* Includes facilities under cooling off period of BD 46,900 thousand.

Significant increase in credit risk

When determining whether the risk of default on a financial instrument and assets acquired for leasing has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and expert credit assessment and including forward-looking information.

In determining whether credit risk has increased significantly since initial recognition, the following criteria are considered:

- 1 Downgrade in risk rating according to the approved ECL policy;
- 2 Facilities restructured during previous twelve months;
- 3 Qualitative indicators; and
- 4 Facilities overdue by 30 days as at the reporting date subject to rebuttal in deserving circumstances

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)**CREDIT RISK (CONTINUED)****Credit risk grades**

The Group allocates each exposure to credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades (continued)

Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 2 and 3.

Each exposure is allocated to a credit risk grade at initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. Exposers are rated 1 to 10 with 1 to being good and 7 being watch list and 8, 9 and 10 default grades. The monitoring typically involves use of the following data.

Corporate exposures

- Information obtained during periodic review of customer files- e.g. audited financial statements, management accounts, budgets and projections. Examples of areas of particular focus are: gross profit margins, financial leverage ratios, debt service coverage, compliance with covenants, quality of management, senior management changes
- Data from credit reference agencies, press articles, changes in external credit ratings
- Quoted bond and credit default swap (CDS) prices for the borrower where available
- Actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities

Retail exposures

- Internally collected data on customer behaviour -e.g. utilisation of credit card facilities
- Affordability metrics
- External data from credit reference agencies including industry-standard credit scores

All exposures

- Payment record this includes overdue status as well as a range of variables about payment ratios
- Utilisation of the granted limit
- Requests for and granting of forbearance
- Existing and forecast changes in business, financial and economic conditions

Generating the term structure of PD

Credit risk grades are a primary input into the determination of the term structure of PD for exposures. The Group collects performance and default information about its credit risk exposures analyzed by jurisdiction or region and by type of product, borrower and credit risk grading.

The Group employs statistical models to analyze the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change as a result of the passage of time.

This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors as well as in-depth analysis of the impact of certain other factors (e.g. forbearance experience) on the risk of default. For most exposures, key macro-economic indicators include: GDP growth, benchmark profit rates and oil price. For exposures to specific industries and/or regions, the analysis may extend to relevant commodity and/or real estate prices.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)***CREDIT RISK (CONTINUED)******Generating the term structure of PD (continued)***

Based on advice from the Risk Management Department and economic experts and consideration of a variety of external actual and forecast information, the Group formulates a 'base case' view of the future direction of relevant economic variables as well as a representative range of other possible forecast scenarios (see discussion below on incorporation of forward-looking information). The Group then uses these forecasts to adjust its estimates of PDs.

Determining whether credit risk has increased significantly

The criteria for determining whether credit risk has increased significantly vary by portfolio and include quantitative changes in PDs and qualitative factors, including a backstop based on delinquency.

Using its expert credit judgement and, where possible, relevant historical experience, the Group may determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

Qualitative indicators, including different criteria used for different portfolios credit cards and commercial real estate.

As a backstop, the Group considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower. For the purpose of calculating ECL for the year ended 31 December 2020, the Bank has applied the backstop of 74 days as against 30 days, in line with the CBB concessionary measures.

The Group monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- the criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- the criteria do not align with the point in time when an asset becomes 30 days past due; and
- there is no unwarranted volatility in loss allowance from transfers between 12-month PD (stage 1) and lifetime PD (stage 2).

Definition of default

The Group considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held); or
- the borrower is more than 90 days past due on any material obligation to the Group.
- It is becoming probable that the borrower will restructure the asset as a result of bankruptcy due to the borrower's inability to pay its credit obligation.

In assessing whether the borrower is in default, the Group considers qualitative and quantitative indicators. The definition of default aligns with that applied by the Group for regulatory capital purposes.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)**CREDIT RISK (CONTINUED)*****Incorporation of forward-looking information***

The Group incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. Based on advice from the Assets and Liabilities Committee ("ALCO") and economic experts and consideration of a variety of external actual and forecast information, the Group formulates a 'base case' view of the future direction of relevant economic variables as well as a representative range of other possible forecast scenarios. This process involves developing two or more additional economic scenarios and considering the relative probabilities of each outcome.

External information includes economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Group operates, supranational organisations such as the OECD and the International Monetary Fund, and selected private-sector and academic forecasters.

The base case represents a most-likely outcome and is aligned with information used by the Group for other purposes such as strategic planning and budgeting. The other scenarios represent more optimistic and more pessimistic outcomes. Periodically, the Group carries out stress testing of more extreme shocks to calibrate its determination of these other representative scenarios.

The Group has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses. The economic scenarios used as at 31 December 2020 included the key indicators for the selected countries such as the unemployment rates, profit rates and the GDP growth.

Modified financial assets and assets acquired for leasing

The contractual terms of a financing asset and assets acquired for leasing may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer.

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- Its remaining lifetime PD at the reporting date based on the modified terms; with
- The remaining lifetime PD estimated based on data at initial recognition and the original contractual terms.

The Group renegotiates financing to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Group's forbearance policy, forbearance of financing assets is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of profit payments and amending the terms of loan covenants. Both retail and corporate financings are subject to the forbearance policy.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)**CREDIT RISK (CONTINUED)***Modified financial assets and assets acquired for leasing (continued)*

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired / in default (refer Note 5). A customer needs to demonstrate consistently good payment behaviour over a period of time (12 months) before the exposure is no longer considered to be credit-impaired/ in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to 12-month ECL. For the purpose of calculating ECL for the year ended 31 December 2020, the Bank has applied the 3 months as against 12 months, in order to assess consistent good payment behaviour of customer this is in line with the CBB concessionary measures.

Measurement of ECLs

ECLs are a probability-weighted estimate of credit losses. Credit losses are measured as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive). ECLs are discounted at the effective profit rate of the financial asset.

The key inputs into the measurement of ECL are the term structure of the following variables:

- probability of default (PD);
- loss given default (LGD); and
- exposure at default (EAD).

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

PD estimates are estimates at a certain date, which are calculated based on statistical rating models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally compiled data comprising both quantitative and qualitative factors. Where it is available, market data may also be used to derive the PD for large corporate counterparties. If a counterparty or exposure migrates between rating classes, then this will lead to a change in the estimate of the associated PD.

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset. For financing assets secured by retail property, LTV ratios are a key parameter in determining LGD. They are calculated on a discounted cash flow basis using the effective profit rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Group derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortisation. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount drawn, as well as potential future amounts that may be drawn under the contract, which are estimated based on historical observations.

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

The following tables show reconciliations from the opening to the closing balance of the loss allowance: 12-month ECL, lifetime ECL and credit-impaired.

	12 month ECL (Stage 1)	Lifetime ECL not credit impaired (Stage 2)	Lifetime ECL credit impaired (Stage 3)	Total
<i>Balance at 1 January 2020</i>	4,909	3,123	34,833	42,865
<i>Transfer to 12-month ECL</i>	1,430	(979)	(451)	-
<i>Transfer to lifetime ECL non-credit-impaired</i>	(122)	360	(238)	-
<i>Transfer to lifetime ECL credit-impaired</i>	(991)	(1,169)	2,160	-
<i>Net transfers</i>	317	(1,788)	1,471	-
<i>Net re-measurement of loss allowance</i>	3,224	1,029	2,292	6,545
<i>Recoveries / write backs</i>	-	-	(2,704)	(2,704)
<i>Write-offs</i>	-	-	(11,010)	(11,010)
<i>Disposals</i>	(113)	-	(12,584)	(12,697)
<i>Balance at 31 December 2020</i>	8,337	2,364	12,298	22,999

Break down of ECL by category of assets in the statement of financial position and off-balance sheet commitments:

	12 month ECL (Stage 1)	Lifetime ECL not credit impaired (Stage 2)	Lifetime ECL credit impaired (Stage 3)	Total 2020
<i>Cash and balances with banks (note 6)</i>	-	-	-	-
<i>Placements with financial institutions (note 7)</i>	-	-	-	-
<i>Financing assets (note 8)</i>	7,230	1,934	7,891	17,055
<i>Assets acquired for leasing – Including lease rentals receivables (note 10)</i>	545	424	3,014	3,983
<i>Investment in sukuk (note 9)</i>	407	-	1,317	1,724
<i>Commitments and financial Guarantees</i>	155	6	76	237
	8,337	2,364	12,298	22,999

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

	12 month ECL (Stage 1)	Lifetime ECL not credit impaired (Stage 2)	Lifetime ECL credit impaired (Stage 3)	Total
<i>Balance at 1 January 2019</i>	5,099	3,918	17,214	26,231
<i>Transfer to 12-month ECL</i>	1,338	(1,118)	(220)	-
<i>Transfer to lifetime ECL non-credit-impaired</i>	(500)	604	(104)	-
<i>Transfer to lifetime ECL credit-impaired</i>	(863)	(856)	1,719	-
<i>Net transfers</i>	(25)	(1,370)	1,395	-
<i>Net re-measurement of loss allowance</i>	(165)	575	16,304	16,714
<i>Recoveries / write backs</i>	-	-	(80)	(80)
<i>Write-offs</i>	-	-	-	-
<i>Balance at 31 December 2019</i>	4,909	3,123	34,833	42,865

Break down of ECL by category of assets in the statement of financial position and off-balance sheet commitments:

	12 month ECL (Stage 1)	Lifetime ECL not credit impaired (Stage 2)	Lifetime ECL credit impaired (Stage 3)	Total 2019
<i>Cash and balances with banks (note 6)</i>	1	-	-	1
<i>Placements with financial institutions (note 7)</i>	1	-	-	1
<i>Financing assets (note 8)</i>	4,581	2,730	30,735	38,046
<i>Assets acquired for leasing – Including lease rentals receivables (note 10)</i>	140	376	2,705	3,221
<i>Investment in sukuk (note 9)</i>	11	-	1,317	1,328
<i>Commitments and financial Guarantees</i>	175	17	76	268
	4,909	3,123	34,833	42,865

Impaired financial assets

Impaired financial assets are those for which the Group determines that it is probable that it will be unable to collect all or part of the principal and profit due according to the contractual terms of the exposure and these fall under risk grades 8, 9 and 10. For other financial assets impairment is assessed on an individual basis for each exposure by considering various factors.

Past due but not impaired exposures

The exposure pertains to financing assets where contractual profit or principal payments are past due but the Group believes that impairment is not appropriate on the basis of subsequent collections, the level of security / collateral available and / or the stage of collection of amounts owed to the Group.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)**CREDIT RISK (CONTINUED)****Renegotiated facilities**

During the year, facilities of BD 19,676 thousands (2019: BD 37,917 thousand) were renegotiated, out of which BD 6,056 thousand (2019: BD 1,096 thousand) are classified as neither past due nor impaired as of 31 December 2020. The renegotiated terms usually require settlement of profits accrued till date on the facility and/or part payment of the principal and/or obtaining of additional collateral coverage. The renegotiated facilities are subject to revised credit assessments and independent review by the RMD. Of the total past due facilities of BD 83,612 thousand (2019: BD 166,033 thousand) only instalments of BD 42,555 thousand (2019: BD 36,625 thousand) are past due as at 31 December 2020.

Allowances for impairment

The Group makes provisions for impairment on individual assets classified under grades 8,9 and 10. This is done on the basis of the present value of projected future cash flows from the assets themselves and consideration of the value of the collateral securities available. On a collective basis, the Group has provided for impairment losses based on management's judgment of the extent of losses incurred but not identified based on the current economic and credit conditions.

Non-accrual basis

Group classifies financing facility/Sukuk as non-accrual status, if the facility/Sukuk is past due greater than 90 days or there is reasonable doubt about the collectability of the receivable amount. The profits on such facilities are not recognized in the income statement until there are repayments from the borrower or the exposure is upgraded to regular status.

Write-off policy

The gross carrying amount of a financial asset is written off when the Group has no reasonable expectations of recovering a financial asset in its entirety or a portion thereof. The Group expects no significant recovery from the amount written off. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due. During the year, the Group has written off financing facilities amounting to BD 11,010 thousand (2019: BD Nil thousand) which were fully impaired. The Group has recovered BD 628 thousand from a financing facility written off in previous years (2019: 964 thousand).

Collaterals

The Group holds collateral against financing assets and receivables from assets acquired for leasing in the form of mortgage/ pledge over property, listed securities, other assets and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing. Valuation of collateral is updated when the loan is put on a watch list and the loan is monitored more closely. Collateral generally is not held against exposure to other banks and financial institutions. An estimate of the fair value of collateral and other security enhancements held against financial assets is shown below. This includes the value of financial guarantees from banks, but not corporate and personal guarantees as the values thereof are not readily quantifiable. The collateral values considered for disclosure are restricted to the extent of the outstanding exposures.

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CREDIT RISK (CONTINUED)

Collaterals (continued)

	As at 31 December 2020			As at 31 December 2019		
	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total
<u>Against impaired</u>						
Property	17,018	11,838	28,856	20,181	32,464	52,645
Other	1,162	-	1,162	1,888	-	1,888
<u>Against past due but not impaired</u>						
Property	23,369	22,957	46,326	35,420	23,949	59,369
Other	628	-	628	1,157	-	1,157
<u>Against neither past due nor impaired</u>						
Property	140,863	105,173	246,036	96,730	89,681	186,411
Other	17,337	-	17,337	9,280	-	9,280
Total	200,337	139,968	340,345	164,656	146,094	310,750

The average collateral coverage ratio on secured facilities is 149.71% at 31 December 2020 (31 December 2019: 130.5%).

For analysis of concentration of total assets and liabilities refer note 33.

Further, for financing assets and assets acquired for leasing including lease rentals receivable, the Group monitors concentrations of credit risk by sector and by geographic location.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)**CREDIT RISK (CONTINUED)**

An analysis of concentrations of credit risk at the reporting date is shown below:

Concentration by Sector	As at 31 December 2020			As at 31 December 2019		
	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total	Financing assets	Assets acquired for leasing (including lease rentals receivable)	Total
Banking and finance	4,420	-	4,420	7,857	-	7,857
Real estate	89,532	127,333	216,865	72,043	133,657	205,700
Construction	56,623	-	56,623	51,038	-	51,038
Trading	48,951	-	48,951	57,224	-	57,224
Manufacturing	14,617	-	14,617	13,955	-	13,955
Others	93,574	12,421	105,995	122,238	12,542	134,780
Total carrying amount	307,717	139,754	447,471	324,355	146,199	470,554

Settlement risk

The Group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a company to honour its obligations to deliver cash, securities or other assets as contractually agreed.

Settlement limits form part of the credit approval / limit monitoring process described earlier. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals from RMD.

LIQUIDITY RISK

Liquidity risk is the risk that the Group will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial assets.

Management of liquidity risk

The effect of COVID-19 on the liquidity and funding risk profile of the banking system is evolving and is subject to ongoing monitoring and evaluation.

The Group's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Group's reputation.

Payment holidays have been extended to customers, including private and SME sector, in line with the instructions of CBB from March 2020 to 30 June 2021. This payment holiday is expected to delay expected contractual cash inflows of the Group. However, the management will take appropriate steps to mitigate its impact on the liquidity position.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)

LIQUIDITY RISK (CONTINUED)

The CBB has announced various measures to combat the effects of COVID-19 and to ease liquidity in the banking sector including, concessionary repos at zero percent, reduction of cash reserve ratio from 5% to 3%; and reduction in LCR and NSFR ratio from 100% to 80%;

In response to COVID-19 outbreak, the Group continues to monitor and respond to all liquidity and funding requirements that are presented. The Group continues to calibrate stress testing scenarios to current market conditions in order to assess the impact on the Group in current extreme stress.

As at the reporting date, the liquidity and funding position of the Group remains strong and is well placed to absorb and manage the impacts of this disruption. Further information on the regulatory liquidity and capital ratios as at 31 December 2020 have been disclosed below.

Financial Control Department (FCD) collates data from treasury and other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. FCD communicates the information to the treasury who manages the Group's portfolio of short-term liquid assets, largely made up of short-term placements with other banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Group as a whole.

The daily liquidity position is monitored by FCD. The Group has in place a Liquidity Contingency Plan, the elements of which are periodically tested. Tools for implementation of regular stress testing under various scenarios are in place. All liquidity policies and procedures are subject to review by ALCO and approval by appropriate authorities. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO members.

Exposure to liquidity risk

The key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For computation of this, net liquid assets are considered as including cash and bank balances and placements with financial Institutions and investments in sukuk net of sukuk pledged against term borrowings less placements from financial institution, and deposits comprise current accounts, placements from non-financial institutions and individuals, and equity of investment account holders.

Details of the reported Group ratio of net liquid assets to deposits and customers current accounts at the reporting date and during the reporting period were as follows:

	2020 %	2019 %
At 31 December	35.7%	33.70
Average for the period	36.4%	29.11
Maximum for the period	39.9%	33.70
Minimum for the period	33.6%	22.32

For maturity profile of assets and liabilities refer note 32.

The Central Bank of Bahrain introduced Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) during 2019.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)*LIQUIDITY RISK (CONTINUED)*

LCR has been developed to promote short-term resilience of a bank's liquidity risk profile. The LCR requirements aim to ensure that a bank has an adequate stock of unencumbered high quality liquidity assets (HQLA) that consists of assets that can be converted into cash immediately to meet its liquidity needs for a 30 calendar day stressed liquidity period. The stock of unencumbered HQLA should enable the Bank to survive until day 30 of the stress scenario, by which time appropriate corrective actions would have been taken by management to find the necessary solutions to the liquidity crisis.

LCR is computed as a ratio of Stock of HQLA over the Net cash outflows over the next 30 calendar days. Until 31 December 2021, the Bank is required to maintain LCR greater than 80%. As of 31 December 2020, the Bank had LCR ratio of 198.28%.

NSFR is to promote the resilience of banks' liquidity risk profiles and to incentivise a more resilient banking sector over a longer time horizon. The NSFR will require banks to maintain a stable funding profile in relation to the composition of their assets and off-balance sheet activities. A sustainable funding structure is intended to reduce the likelihood that disruptions to a bank's regular sources of funding will erode its liquidity position in a way that would increase the risk of its failure and potentially lead to broader systemic stress. The NSFR limits overreliance on short-term wholesale funding, encourages better assessment of funding risk across all on-balance sheet and off-balance sheet items, and promotes funding stability.

NSFR as a percentage is calculated as "Available stable funding" divided by "Required stable funding". Until 31 December 2021, the Bank is required to maintain NSFR ratio greater than 80%. As of 31 December 2020, the Bank had NSFR ratio of 103.65%.

MARKET RISK

Market risk is the risk that changes in market prices, such as profit rate, equity prices, foreign exchange rates and credit spreads will affect the Group's income, future cash flows or the value of its holdings of financial instruments. Market risk comprises three types of risk: currency risk, profit rate risk and other price risk. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

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35. *FINANCIAL RISK MANAGEMENT (CONTINUED)*

MARKET RISK (CONTINUED)

Exposure to profit rate risk—non—trading portfolios

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market profit rates. Profit rate risk is managed principally through monitoring profit rate gaps and by having pre-approved limits for re-pricing bands. The ALCO is the monitoring body for compliance with these limits and is assisted by the Group's Risk Management Department in its day-to-day monitoring activities.

A summary of the Group's profit rate gap position at 31 December 2020 is as follows:

31 December 2020	Up to 3 months	3 - 6 months	6 months - 1 year	1 - 3 years	More than 3 years	Total
Assets						
Placements with financial institutions	17,720	-	-	-	-	17,720
Financing assets	49,758	13,386	16,998	48,964	178,611	307,717
Assets acquired for leasing (including lease rentals receivables)	31	36	15	2,576	137,096	139,754
Investment in sukuk	2,147	536	16,556	6,800	235,093	261,132
Total profit rate sensitive assets	69,656	13,958	33,569	58,340	550,800	726,323
Liabilities and investment accounts						
Placements from financial institutions	32,906	34,948	8,077	3,614	-	79,545
Placements from non-financial institutions and individuals	74,188	32,705	59,918	47,432	-	214,243
Term borrowings	67,915	7,562	-	-	-	75,477
Customers' current accounts	1,188	-	-	-	-	1,188
Equity of investments account holders	144,256	41,472	51,894	185,652	2,075	425,349
Total profit rate sensitive liabilities and investment accounts	320,453	116,687	119,889	236,698	2,075	795,802
Profit rate gap	(250,797)	(102,729)	(86,320)	(178,358)	548,725	(69,479)

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

MARKET RISK (CONTINUED)

Exposure to profit rate risk—non—trading portfolios (continued)

31 December 2019	Up to 3 months	3 - 6 months	6 months - 1 year	1 - 3 years	More than 3 years	Total
Assets						
Placements with financial institutions	65,508	-	-	-	-	65,508
Financing assets	62,733	15,395	25,046	58,075	163,106	324,355
Assets acquired for leasing (including lease rentals receivables)	1	6,597	133	2,030	137,438	146,199
Investment in sukuk	1,951	-	-	18,096	175,003	195,050
Total profit rate sensitive assets	130,193	21,992	25,179	78,201	475,547	731,112
Liabilities and investment accounts						
Placements from financial institutions	-	-	15,637	101,461	-	117,098
Term borrowings	-	-	-	-	-	-
Placements from non-financial institutions and individuals	29,382	21,056	38,307	45,909	-	134,654
Customers' current accounts	1,193	-	-	-	-	1,193
Equity of investments account holders	266,735	104,746	99,735	50,974	-	522,190
Total profit rate sensitive liabilities and investment accounts	297,310	125,802	153,679	198,344	-	775,135
Profit rate gap	(167,117)	(103,810)	(128,500)	(120,143)	475,547	(44,023)

The management of profit rate risk against profit rate gap limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various standard and non-standard profit rate scenarios. Standard scenarios that are considered on a monthly basis include a 100 basis point (bp) parallel fall or rise across all yield curves and a 50 bp rise or fall of all yield curves.

An analysis of the Group's sensitivity to an increase or decrease in market profit rates (assuming no asymmetrical movement in yield curves and a constant statement of financial position position) is as follows:

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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

MARKET RISK (CONTINUED)

Exposure to profit rate risk—non—trading portfolios (continued)

	100bp parallel increase/ decrease	50bp increase/ decrease
At 31 December 2020	± 690	± 345
At 31 December 2019	± 433	± 216

Overall non-trading profit rate risk positions are managed by Treasury department, which uses short term investment securities, placement with banks and placement from banks to manage the overall position arising from the Group's non-trading activities.

A fundamental review and reform of major profit rate benchmarks is being undertaken globally. There is uncertainty as to the timing and the methods of transition for replacing existing benchmark interbank offered rates (IBORs) with alternative rates.

As a result of these uncertainties, there could be an impact on the values of financial contracts entered by the Bank. While the IBOR continues to be used as a reference rate in financial markets and is used in the valuation of instruments with maturities that exceed the expected end date for IBOR. The Bank will have to assess the impact. As at 31 December 2020, the Bank is in the process of assessing the impact on its financial instruments which are maturing after the expected end date for IBOR.

Exposure to foreign exchange risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group had the following significant net exposures denominated in foreign currency as of 31 December.

	2020 BHD Equivalent	2019 BHD Equivalent
US Dollars*	103,734	145,868
Other GCC Currencies *	(39,435)	(63,732)
Euros	(1,079)	(280)
Australian Dollars	5,100	4,608
Kuwaiti Dinars	3,158	3,322
Sterling Pounds	(433)	1,443
Indian Rupee	13	30

(*) The exposure in US dollars and other GCC currencies does not create any foreign exchange risk for the Group since Bahrain Dinars and other GCC currencies except for Kuwaiti Dinars are effectively pegged to the US Dollars.

The management of foreign exchange risk against net exposure limits is supplemented by monitoring the sensitivity of the Group's financial assets and liabilities to various foreign exchange scenarios. Standard scenarios that are considered on a monthly basis include a 5% plus/minus increase in exchange rates, for currencies other than US Dollars, other GCC currencies.

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35. FINANCIAL RISK MANAGEMENT (CONTINUED)**MARKET RISK (CONTINUED)***Exposure to foreign exchange risk (continued)*

An analysis of the Group's sensitivity to an increase or decrease in foreign exchange rates (assuming all other variables, primarily profit rates, remain constant) is as follows:

	2020 BHD Equivalent	2019 BHD Equivalent
Euros	±54	±14
Australian Dollars	±255	±230
Kuwaiti Dinars	±158	±166
Sterling Pounds	±22	±72
Indian Rupees	±1	±2

Exposure to other price risks–non–trading portfolios

Credit spread risk on debt securities is subject to regular monitoring by RMD, but is not currently significant in relation to the overall financial position of the Group.

The Group's unquoted equity securities carried at cost are exposed to risk of changes in equity values. Refer to note 25 for significant estimates and judgments in relation to impairment assessment of unquoted equity investments carried at cost. The Group manages exposure to other price risks by actively monitoring the performance of the equity securities. The performance assessment is performed on a quarterly basis and is reported to the Board Investment and Credit Committee

OPERATIONAL RISK

Operational risk is the risk of loss arising from systems and control failures, fraud and human errors, which can result in financial and reputation loss, and legal and regulatory consequences. The Group manages operational risk through appropriate controls, instituting segregation of duties and internal checks and balances, including internal audit and compliance. The Risk Management Department is in charge of identifying, monitoring and managing operational risk in the Group. The Group already has an approved policy for doing this and all required organisational and physical infrastructure are in place.

The Group has completed conducting one cycle of Risk Control Self-Assessment (RCSA) of Operational risk for majority of the departments of the Group to identify the important Key Risk Areas, Key Risk Indicators and Key Risk Triggers. Furthermore, for the remaining departments Key Risk Areas have been identified and the next process will be the identification of Key Risk Indicators and Key Risk Triggers. The RCSA process is a continuous process and will be conducted at regular frequencies across the Group. It will be an annual process to review all the KRI's. A software for monitoring these triggers and recording actual and near miss losses is already in place. The medium-term objective of the Group is to generate statistically reliable data to upgrade to more sophisticated modes of Operational Risk Control both to manage the risk better and to reduce capital commitment.

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35. *FINANCIAL RISK MANAGEMENT (CONTINUED)*

OPERATIONAL RISK (CONTINUED)

In response to COVID-19 outbreak, there were various changes in the working model, interaction with customers, digital modes of payment and settlement, customer acquisition and executing contracts and carrying out transactions with and on behalf of the customers. The management of the Group has enhanced its monitoring to identify risk events arising out of the current situation and the changes in the way business is conducted. The operational risk department has carried out a review of the existing control environment and has considered whether to update the risk registers by identifying potential loss events based on their review of the business processes in the current environment.

During 2020, the Group did not have any significant issues relating to operational risks.

CAPITAL MANAGEMENT

The Central Bank of Bahrain (CBB) sets and monitors capital requirements for the Group as a whole. In implementing current capital requirements CBB requires the Group to maintain a prescribed ratio of total capital to total risk-weighted assets. The capital adequacy regulations of CBB is based on the principles of Basel III of the IFSB guidelines.

The Group's regulatory capital is analysed into two tiers:

▪ *Tier 1 capital: includes CET1 and AT1.*

CET1 comprise of ordinary share capital that meet the classification as common shares for regulatory purposes, disclosed reserves including share premium, general reserves, legal / statutory reserve, common shares issued by consolidated banking subsidiaries of the Bank and held by third parties, retained earnings after regulatory adjustments relating to goodwill and items that are included in equity which are treated differently for capital adequacy purposes.

AT1 comprise instruments issued by consolidated banking subsidiaries of the Bank which meet the criteria of AT1, and regulatory adjustments applied in calculation of AT1.

Subordinated Mudaraba

In order to meet minimum regulatory requirements relating to total equity of BD 100 million, during the year, the Bank issued a Subordinated Mudaraba (Basel III compliant Additional Tier 1 capital securities) of US\$ 159 million (BD 60 million) at a premium of BD 12 million. The issue was fully subscribed for by the Parent through a combination of cash of BD 23.6 million and in-kind of BD 48.4 million comprising of a stake in a joint venture of BD 24.5 million (Note 13), properties of BD 5.5 million, and financing assets of BD 18.4 million. The in-kind contribution was recognised at the fair value of the consideration received on the date of transfer. The premium received has been added to retained earnings and recognized as part of the total equity attributable to AT1.

Issuance costs of BD 12.7 million representing BD 12.1 million underwriting fee to the Parent and BD 0.6 million other transaction costs have been adjusted against the AT1 issued capital.

Profits on these securities shall be distributed on a semi-annual basis subject to and in accordance with terms and conditions on the outstanding nominal value of the securities at an expected rate of 10% p.a. The Subordinated Mudaraba is recognised in owners' equity and the profits paid to rab al-maal (security holder) are accounted for as appropriation of profits. Security holder will not have a right to claim the profits and such event will not be considered as event of default.

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35. *FINANCIAL RISK MANAGEMENT (CONTINUED)*

CAPITAL MANAGEMENT (CONTINUED)

Subordinated Mudaraba (continued)

▪ *Tier 2 capital*

This includes instruments issued by the Bank that meet the criteria for inclusion in Tier 2 capital, stock surplus resulting from issue of Tier 2 capital, instruments issued by consolidated banking subsidiaries of the Bank held by third parties that meet the criteria for inclusion in Tier 2, general provisions held against unidentified losses on financing and qualify for inclusion within Tier 2, asset revaluation reserve from revaluation of fixed assets and instruments purposes and regulatory adjustments applied in the calculation of Tier 2 capital.

The regulations prescribe higher risk weights for certain exposures that exceeds materiality thresholds. These regulatory adjustments required for certain items such as goodwill on mortgage service right, deferred tax assets, cash flow hedge reserve, gain on sale of related securitization transactions, defined benefit pension fund assets and liabilities, investment in own shares and reciprocal cross holdings in the capital of Banking and financial entities, investment in the capital of Banking and financial entities that are outside the scope of regulatory consolidation and where the Group does not own more than 10% of issued common shares capital of the entity and significant investments in the capital of banking and financial entities that are outside the scope of regulatory consolidation.

As at 31 December 2020, the Group has made regulatory adjustments of BD 11,859 thousand (2019: BD 14,356 thousand) in line with the CBB requirements.

Banking operations are categorised as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures.

To combined the effect of Covid 19, the CBB has allowed the Aggregate of modification loss and incremental ECL provision for stage 1 and stage 2 for the period from March to December 2020 to be added back to Tier 1 capital for the two years ending 31 December 2020 and 31 December 2021. And to deduct this amount proportionately from Tier 1 capital on an annual basis for three years ending 31 December 2022, 31 December 2023 and 31 December 2024.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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35. **FINANCIAL RISK MANAGEMENT (CONTINUED)**

CAPITAL MANAGEMENT (CONTINUED)

The Group's regulatory capital position at 31 December was as follows:

	31 December 2020	31 December 2019
Total risk weighted exposure	791,271	532,793
Tier 1 capital:		
- CET 1 capital prior to regulatory adjustments	116,422	97,215
- Less: regulatory adjustments	(11,859)	(14,356)
CET 1 after regulatory adjustments	104,932	82,859
AT 1	47,222	-
Tier 2 capital:	8,940	5,726
Total regulatory capital	160,725	88,585
Total regulatory capital expressed as a percentage of total risk weighted assets	20.31%	16.63%
Liquidity coverage ratio	198.28%	733.93%
Net stable funding ratio	103.65%	108.5%
Leverage ratio	20.84%	13.72%

The Group has complied with all externally imposed capital requirements throughout the year.

Capital allocation

The allocation of capital between specific operations and activities is primarily driven by regulatory requirements. The Group's capital management policy seeks to maximise return on risk adjusted while satisfying all the regulatory requirements. The Group's policy on capital allocation is subject to regular review by the Board.

36. COMMITMENTS AND CONTINGENCIES

The commitments contracted in the normal course of business of the Group:

	2020	2019
Undrawn commitments to extend finance *	31,389	68,876
Financial guarantees	10,180	11,836
Legal contingencies	19,000	-
	60,569	80,712

* The Group has a right to revoke the undrawn commitment to extend finance prior to expiry of its tenor.

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36. COMMITMENTS AND CONTINGENCIES (CONTINUED)*Performance obligations*

During the ordinary course of business, the Group may enter into performance obligations in respect of certain of its infrastructure development projects. It is the usual practice of the Group to pass these performance obligations, wherever possible, on to the companies that own the projects. In the opinion of the management, no liabilities are expected to materialise on the Group at 31 December 2020 due to the performance of any of its projects.

Litigations and claims

An investor in one of the Group's projects has filed a claim against the Group. Based on the advice of the Bank's external legal counsel, the Board of directors is of the opinion that the Group has strong grounds to successfully defend itself against this claim. No further disclosures regarding contingent liabilities arising from any such claims are being made by the Bank as the directors believe that such disclosures may be prejudicial to the Group's legal position.

37. SOCIAL RESPONSIBILITY

The Group discharges its social responsibilities through donations to charitable causes and organisations from its zakah and charity fund.

38. COMPARITIVES

Certain prior year amounts have been regrouped to conform the current year's presentation. Such regrouping did not affect previously reported profit for the year or owner's equity.

SUPPLEMENTARY DISCLOSURE

(The attached information does not form part of the consolidated financial statements)

SUPPLEMENTARY DISCLOSURE

UNAUDITED SUPPLEMENTARY DISCLOSURE TO THE CONSOLIDATED FINANCIAL STATEMENTS

On 11 March 2020, the Coronavirus (COVID-19) outbreak was declared, a pandemic by the World Health Organization (WHO) and has rapidly evolved globally. This has resulted in a global slowdown with uncertainties in the economic environment. This included disruption to capital markets, deteriorating credit markets and liquidity concerns. Authorities have taken various measures to contain the spread including implementation of travel restrictions and quarantine measures. The pandemic as well as the resulting measures and policies have had some impact on the Group. The Group is actively monitoring the COVID-19 situation, and in response to this outbreak, has activated its business continuity plan and various other risk management practices to manage the potential business disruption on its operations and financial performance.

The Central Bank of Bahrain (CBB) announced various measures to combat the effect of COVID-19 to ease liquidity conditions in the economy as well as to assist banks in complying with regulatory requirements. These measures include the following:

- Payments holiday for 6 months to eligible customers starting from and including 1 March 2020;
- Concessionary repo to eligible banks at zero percent;
- Reduction of cash reserve ratio from 5% to 3%;
- Reductions of liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) from 100% to 80%;
- Aggregate of modification loss and incremental expected credit losses (ECL) provisions for stage 1 and stage 2 from March to December 2020 to be added to Tier 1 capital for two years ending 31 December 2020 and 31 December 2021. And to deduct this amount proportionally from Tier 1 capital on an annual basis for three years ending December 2022, 31 December 2023 and 31 December 2024.
- The CBB subsequently announced second and third deferrals of instalments of financing effective September 2020 for a period of four months, and January 2021 for a period of six months. These deferrals allowed the Banks to charge profit, and as such, did not result any additional modification losses to the Group;

The aforementioned measures have resulted in the following effects to the Group:

- The CBB mandated 6-month payment holiday requires impacted banks to recognize a one-off modification loss directly in equity. The modification loss has been calculated as the difference between the net present value of the modified cash flows calculated using the original effective profit rate and the carrying value of the financial assets on the date of modification.
- The Government of Kingdom of Bahrain has announced various economic stimulus programmes ("Packages") to support businesses in these challenging times. The Group received regulatory directive financial assistance representing specified reimbursement of a portion of staff costs, waive of fees, levies and utility charges and zero cost funding received from the Government and/or regulators, in response to its COVID-19 support measures. This has been recognized directly in the Group's equity.
- The mandated 6 months payments holiday included the requirement to suspend minimum payments and service fees and outstanding credit card balances, this resulted in a significant decline in the Group's fees income.

SUPPLEMENTARY DISCLOSURE

- The Group continues to meet the regulatory requirement of CAR, LCR and NSFR.
- The strain caused by COVID-19 on the local economy resulted in a slow-down in the booking of new financing assets by the Group. During year ended 31 December 2020, financing assets bookings were 30.80% lower than the same period of the previous year.
- Decreased consumer spending caused by the economic slow-down in the booking of new financing assets by the Bank, whereas, deposit balances decreased compared to the same period of the previous year. These effects partly alleviated the liquidity stress faced by the Group due to the mandated 6 months payments holiday.
- The stressed economic situation resulted in the Bank recognizing incremental ECL on its exposure.

A summary of the financial impact of the impact of the above effects is as follows:

	Net Impact on the Group's consolidated income statement BD '000	Net Impact on the Group's consolidated financial position BD '000	Net Impact on the Group's consolidated owners' equity BD '000
Average reduction of cash reserve	-	9,482	-
Concessionary repo at 0%	(278)	48,888	278
Modification loss	-	(9,452)	(9,452)
Modification loss amortization	9,452	9,452	-
Government grants	-	-	791
Credit card income	(313)	-	-
ECL attributable to COVID-19	(1,700)	(1,700)	-
	<u>7,161</u>	<u>56,670</u>	<u>(8,383)</u>

The above supplementary information is provided to comply with CBB circular number OG/259/2020 (reporting of Financial Impact of COVID-19), dated 14 July 2020. This information should not be considered as indication of the results of the entire year or relied upon for any other purposes. Since the situation of COVID-19 is uncertain and is still evolving, the above impact is as of date of preparation of this information. Circumstances may change which may result in this information to be out-of-date. In addition, this information does not represent a full comprehensive assessment of COVID-19 impact on the Group. This information has not been audited by the external auditors.