

KHALEEJI COMMERCIAL BANK BSC
CONSOLIDATED FINANCIAL STATEMENTS
31 DECEMBER 2019

| | | |
|-------------------------|---|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 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 Dr. Khalid Mohammed Al Khazraji Mustafa Ghazi Kheriba Fawad Tariq Khan Yousef Ibrahim Al Ghanim Mohammad Abdulmohsen Al Rashed |
| Chief Executive Officer | : | Sattam Sulaiman Algosaibi |
| Company secretary | : | Mohammed Abdulla Saleh |
| Auditors | : | KPMG Fakhroo, Bahrain |

CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

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Chairman's Report
For the Year Ended 31 December 2019
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 2019.

We are pleased to share certain strategic decisions taken by the Bank in 2019 aimed at significantly transforming the Bank's operations and market approach. The management focused on increasing the asset quality by booking high quality assets and strategically adopted a conservative stance against legacy assets by taking further provisions. In addition, key decisions include the cost rationalization initiative and strategically reevaluating distribution channels while still maintaining operational effectiveness, efficiency and profound customer experience.

On all fronts, it has been a year full of challenges and opportunities. The Bank have accepted these challenges and was able to implement a new strategic approach and was able to provide various innovative financial solutions that added value to all stakeholders. This is evident by Bank's initiative to support the growth in the local market by financing and providing financial solutions to key local landmark projects. Moreover, the Bank is also extending support to the local consumer finance sector by participation in the Mazaya housing program. The Bank will continue to pursue its expansion strategy through adopting several initiatives and progressive strategies that are directed towards enhancement of the Bank's positioning, market reach and competitive advantage.

We are pleased to report that the bank continues to progress with plans to become a leading Islamic retail bank. Despite a challenging environment, these plans are fast taking shape and, already started showing tangible results and the management are continuously working to achieve the full benefits of the bank's strategic initiatives, cost synergies and rationalization.

Meanwhile, new products and enhanced services are the key drivers of our business growth and increase in assets, therefore, the bank continues to invest heavily in developing its products and services. The Bank continues to grow closer to its customers, listening closely to their needs and providing tailored financial solutions.

**Chairman's Report
For the Year Ended 31 December 2019
Khaleeji Commercial Bank BSC**

Overall Performance

The Bank, during 2019, 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 growth of total assets from BD 850.9 million in 2018 to BD 939.8 million in 2019, a growth of 10.4%. Customer Deposits grew to BD 704.6 million in 2019 compared to BD 537.3 million in 2018, a growth of 31.1%. Corporate financing assets reached BD 342.6 million in 2019 compared to BD 299.7 million in 2018, a growth of 14.3%.

Furthermore, the Bank was able to achieve growth in liquid assets which currently comprises of 38.8% of Total Assets while the Capital Adequacy Ratio ("CAR") reached 16.63%. In addition to this, the Bank is maintaining healthy Liquidity Coverage Ratio ("LCR") of 733.93% and Net Stable Funding Ratio ("NSFR") of 108.5% as of 31 December 2019. 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 195.1 million in 2019 compared to BD 161.3 million in 2018, a growth of 20.9%.

The Bank reported a net loss attributable to the shareholders of the parent BD 14.9 million. As the Board decided to take an amount of BD 22.4 million as provisions and fair value losses for the year ended 31 December 2019, such conservative approach has been taken in order to enhance the Bank's financial positioning and to further support its growth in 2020.

The new 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.

**Chairman's Report
For the Year Ended 31 December 2019
Khaleeji Commercial Bank BSC**

Looking Ahead

The Bank's inclination towards digital banking would be key in increasing customer acquisition through digital channels which would reduce acquisition cost and time. Digital banking will empower customers to perform transactions at any moment thereby enhancing their experience.

Technology, risk management and controls are the backbone that support business growth and ensure competitiveness in the market place. The Bank continues to invest in further enhancing them by implementing new solutions for risk, compliance, core banking and others. The Bank continues to align risk management with business to contribute in the creation, optimization and protection of enterprise value by managing business risks while creating value in the marketplace and continuous asset management of investment portfolio by establishing strategic investment exits.

The Bank is driven towards adopting important expansionary initiatives that it aims to achieve in 2020 and the years to follow which include the Bank's plans to continue improving the financing portfolio at both the Corporate and Retail level, with special consideration to the sovereign exposures, while maintaining appropriate liquidity buffers and financial ratios.

Further, the Bank is rationalizing the number of branches with potential to reevaluate the branches network in the following years while increasing customer acquisition through digital channels and reduce acquisition cost, time and widen its customer base. The Bank is focusing on continuously working on reengineering and automation of controls to ensure higher efficiency and effectiveness.

Appreciation

On behalf of the Board, I would like to express my gratitude to his Majesty King Hamad Bin Isa Al Khalifa; His Royal Highness Prince Khalifa Bin Salman Al Khalifa, the Prime Minister; and His Royal Highness Prince Salman Bin Hamad Al Khalifa, the Crown Prince and Deputy Supreme Commander of Bahrain Defence Force and First Deputy Prime Minister for their encouragement of the growth of the private sector and the development of the banking and finance industry in Bahrain. I also extend my thanks to all government ministries, the Central Bank of Bahrain, 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 2020
09 Jamadah II 1441 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 2019

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 ("KHCB") and its subsidiaries for the financial year ending 31st December 2019.

Respective responsibility of the Board of Directors and the SSB

The SSB confirms that as a general principle and practice, KHCB'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 2019. 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 2019.

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.

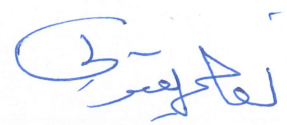
We pray to Allah the almighty to grant us all success and prosperity.



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 BSC
Manama, Kingdom of Bahrain

Report on the consolidated financial statements

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 2019, the consolidated statements of income, the changes in equity, cash flows, changes in restricted investment accounts and sources and uses of zakah and charity fund for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Respective responsibilities of board of directors and auditors

These consolidated financial statements and the Group's undertaking to operate in accordance with Islamic Shari'a rules and principles are the responsibility of the board of directors of the Bank. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

Basis of opinion

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by Accounting and Auditing Organisation for Islamic Financial Institutions. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Emphasis of Matter

We draw attention to Note 1 of the consolidated financial statements, which describes that as at 31 December 2019 the Bank's shareholders' equity is below the minimum requirement of BD 100 million as prescribed by the Central Bank of Bahrain and the Board's action plan to address this. Our opinion is not modified in respect of this matter.

Opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2019 and of its consolidated results of operations, its consolidated cash flows, its consolidated changes in equity, its consolidated changes in restricted investment accounts and its consolidated sources and uses of zakah and charity fund for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

Report on other regulatory requirements

As required by the Commercial Companies Law and Volume 2 of the Central Bank of Bahrain (CBB) Rule Book, we report that:

- a) the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;
- b) the financial information contained in the chairman's report is consistent with the consolidated financial statements;
- c) Except for the matter referred to in the Emphasis of Matter paragraph above, we are not aware of any other instances of 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.

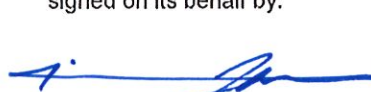
KPMG Fakhro
Partner Registration No. 100
9 February 2020


CONSOLIDATED STATEMENT OF FINANCIAL POSITION
as at 31 December 2019

BD 000's

| | Note | 31 December 2019 | 31 December 2018 |
|-------------------------------------------------------------------------------------------------------------|------|---------------------|---------------------|
| ASSETS | | | |
| Cash and bank balances | 6 | 104,376 | 99,401 |
| Placements with financial institutions | 7 | 65,508 | 43,637 |
| Financing assets | 8 | 324,355 | 327,640 |
| Investment in sukuk | 9 | 195,050 | 161,324 |
| Assets acquired for leasing | 10 | 129,097 | 108,678 |
| Lease rentals receivables | | 17,102 | 11,525 |
| Investment in equity securities | 11 | 43,989 | 50,039 |
| Investment in real estate | 12 | 17,781 | 18,081 |
| Development property | | 6,251 | 6,251 |
| Other assets | 13 | 28,493 | 16,498 |
| Property and equipment | 14 | 7,750 | 7,865 |
| Total assets | | 939,752 | 850,939 |
| LIABILITIES | | | |
| Placements from financial institutions | | 127,453 | 158,349 |
| Placements from non-financial institutions and individuals | 15 | 134,654 | 120,470 |
| Medium-term borrowing | 16 | - | 41,357 |
| Customers' current accounts | | 58,105 | 70,416 |
| Other liabilities | 17 | 19,798 | 10,512 |
| Total liabilities | | 340,010 | 401,104 |
| Equity of investment account holders | 18 | 511,835 | 346,373 |
| OWNERS' EQUITY | | | |
| Share capital | 19 | 105,000 | 105,000 |
| Statutory reserve | | 8,225 | 8,225 |
| Treasury shares | | (11,730) | (11,295) |
| Employee share incentive scheme | | - | (29) |
| Accumulated losses | | (15,788) | (729) |
| Total owners' equity | | 85,707 | 101,172 |
| Non-controlling interest | | 2,200 | 2,290 |
| Total liabilities, equity of investment account holders, owners' equity and non-controlling interest | | 939,752 | 850,939 |

The consolidated financial statements were approved by the Board of directors on 09 February 2020 and signed on its behalf by:


Jassim Mohamed Alseddlqi
Chairman


Sh. Ahmed Bin Isa Al Khalifa
Vice Chairman



Sattam Sulaiman Algosaibi
Chief Executive Officer

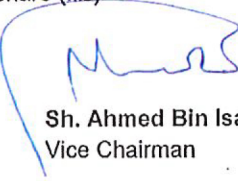
The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

CONSOLIDATED INCOME STATEMENT
for the year ended 31 December 2019

BD 000's

| | Note | 2019 | 2018 |
|-------------------------------------------------------------------------------------------------------|------|-----------------|----------------|
| Income from financing assets and assets acquired for leasing | | 31,334 | 26,565 |
| Income from placements with financial institutions | | 2,183 | 955 |
| Income from sukuk | 20 | 10,031 | 6,377 |
| Income from equity securities | | (1,687) | 1,422 |
| Fees and other income | | 5,726 | 2,842 |
| Total income before return to investment account holders | | 47,587 | 38,161 |
| Less: Return to investment account holders before Bank's share as Mudarib | 18 | (23,544) | (14,221) |
| Bank's share as a Mudarib | 18 | 8,457 | 5,619 |
| Return to investment account holders | | (15,087) | (8,602) |
| Finance expense on placements from financial institutions, non-financial institutions and individuals | | (11,703) | (8,190) |
| Finance expense on medium-term borrowing | | (1,241) | (2,054) |
| Total income | | 19,556 | 19,315 |
| Staff cost | 21 | 8,158 | 7,175 |
| Other operating expenses | 22 | 6,036 | 5,252 |
| Total expenses | | 14,194 | 12,427 |
| Profit before impairment allowances | | 5,362 | 6,888 |
| Net impairment charge | 23 | (20,389) | (6,288) |
| (LOSS)/PROFIT FOR THE YEAR | | (15,027) | 600 |
| Attributable to: | | | |
| Shareholders of the parent | | (14,937) | 659 |
| Non-controlling interest | | (90) | (59) |
| | | (15,027) | 600 |
| Earnings per share | | | |
| Basic and diluted earnings per share (fils) | 28 | (15.86) | 0.69 |


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 2019

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) |
| 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 CHANGES IN EQUITY
for the year ended 31 December 2019 (continued)

BD 000's

2018

| | Equity attributable to shareholders of the parent | | | | | Non-Controlling interest | Total Equity |
|----------------------------------------------------|---------------------------------------------------|-------------------|-----------------|---------------------------------|------------------------------------------|--------------------------|--------------|
| | Share Capital | Statutory reserve | Treasury shares | Employee share incentive scheme | (Accumulated losses) / retained earnings | | |
| Balance at 1 January 2018 (as previously reported) | 105,000 | 8,159 | (10,212) | (70) | 10,162 | 2,645 | 115,684 |
| Impact of adopting FAS 30 | - | - | - | - | (11,069) | - | (11,069) |
| Restated balance at 1 January 2018 | 105,000 | 8,159 | (10,212) | (70) | (907) | 2,645 | 104,615 |
| Profit for the year | - | - | - | - | 659 | (59) | 600 |
| Transfer to statutory reserve | - | 66 | - | - | (66) | - | - |
| Net treasury shares purchased | - | - | (1,083) | - | - | - | (1,083) |
| Issue of shares under incentive scheme | - | - | - | 41 | 42 | - | 83 |
| Loss of Control | - | - | - | - | (16) | (296) | (312) |
| Transfer to Zakah fund | - | - | - | - | (441) | - | (441) |
| Balance at 31 December 2018 | 105,000 | 8,225 | (11,295) | (29) | (729) | 2,290 | 103,462 |

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 2019

BD 000's

| | Note | 2019 | 2018 |
|------------------------------------------------------------------------------------|------|-----------------|-----------------|
| OPERATING ACTIVITIES | | | |
| Receipts from financing assets, net | | 9,621 | 40,392 |
| Payment for asset acquired for leasing, net | | (17,786) | (15,145) |
| Receipt of profit on short-term placements | | 2,183 | 955 |
| Returns paid to investment account holders | | (10,454) | (7,184) |
| Receipts / (Withdrawals) from investment account holders, net | | 165,461 | (13,444) |
| Payment of profit on placements | | (11,703) | (8,190) |
| Payment for expenses | | (19,441) | (10,642) |
| Other receipts | | 3,964 | 2,878 |
| Payment for charity | | (235) | (422) |
| Withdrawals from customers' current accounts, net | | (12,311) | (4,341) |
| (Payments) toward / Receipts from placements from financial institutions, net | | (29,839) | 34,084 |
| Receipts from placements from non-financial institutions and individuals, net | | 14,184 | 59,111 |
| Net payment to CBB reserve account | | (4,610) | (3,360) |
| Income from sukuk received | | 10,006 | 5,937 |
| Net cash generated from operating activities | | 99,040 | 80,629 |
| INVESTING ACTIVITIES | | | |
| Purchase of sukuk | | (37,407) | (63,205) |
| Proceeds from redemption / sale of sukuk | | 3,269 | 15,135 |
| Disposal / (Purchase) of equity securities | | 1,438 | (97) |
| Purchase of Investment in real estate, net | | - | (105) |
| Receipt of dividends / income from equity securities | | 343 | 1,478 |
| Purchase of property and equipment, net | | (452) | (674) |
| Net cash used in investing activities | | (32,809) | (47,468) |
| FINANCING ACTIVITIES | | | |
| Purchase of treasury shares, net | | (350) | (1,234) |
| (Repayment) / drawdown of medium-term borrowing, net | | (41,357) | 50 |
| Finance expense paid on medium-term borrowing | | (1,241) | (2,054) |
| Net cash used in financing activities | | (42,948) | (3,238) |
| Net increase in cash and cash equivalents | | 23,283 | 29,923 |
| Cash and cash equivalents at 1 January | | 121,171 | 91,248 |
| Cash and cash equivalents at 31 December | | 144,454 | 121,171 |
| Cash and cash equivalent comprise: | | | |
| Cash and bank balances (excluding CBB reserve) | 6 | 78,946 | 78,581 |
| Placements with financial institutions with original maturities of 90 days or less | 7 | 65,508 | 42,590 |
| | | 144,454 | 121,171 |

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 2019

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 CHANGES IN RESTRICTED INVESTMENT ACCOUNTS
for the year ended 31 December 2019 (continued)

BD 000's

2018

| | Balance at 1 January 2018 | | | Movements during the year | | | | | | Balance at 31 December 2018 | | |
|----------------------------------------------|------------------------------|-------------------------------------|----------------------|-----------------------------------------|------------------------------|----------------------------------------|-------------------------------|-------------------------------------------|--------------------------------------------|--------------------------------|-------------------------------------|-------------------|
| | 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 | Adminstra- 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) | 3,529 | 1.00 | 3,529 | (95) | - | 117 | (117) | - | - | 3,434 | 1.00 | 3,434 |
| Locata Corporation Pty Ltd (RIA 6) | 2,633 | 0.38 | 993 | - | - | - | - | - | - | 2,633 | 0.38 | 993 |
| | | | 10,776 | (95) | - | 117 | (117) | - | - | | | 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 2019**

BD 000's

| | 2019 | 2018 |
|------------------------------------------------------------|--------------|--------------|
| Sources of zakah and charity fund | | |
| At 1 January | 708 | 674 |
| Contributions by the Bank | 187 | 441 |
| Non-Islamic income | 54 | 15 |
| Total sources | 949 | 1,130 |
| Uses of zakah and charity fund | | |
| Contributions to charitable organisations | (235) | (422) |
| Total uses | (235) | (422) |
| Undistributed zakah and charity fund at 31 December | 714 | 708 |

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 2019

BD 000's

1. REPORTING ENTITY

Khaleeji Commercial Bank BSC ("the Bank"), a public shareholding company, 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 shares are listed on the Bahrain Bourse and Dubai Financial Markets.

The Bank's activities are regulated by the Central Bank of Bahrain (CBB) and supervised by a Religious Supervisory Board to ensure adherence to Shari'a rules and principles in its transactions and activities.

The principal activities of the Bank include providing banking and investment products and services to retail customers, high net worth individuals, corporate entities, and financial institutions. These 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 financial statements of the Bank and its subsidiaries (together "the Group"). The significant subsidiaries are as follows:

| Name | Country of incorporation | % holding 2019 | % holding 2018 | Nature of business |
|--------------------------------|--------------------------|----------------|----------------|-----------------------------------------------------------|
| Harbour West 2 Real Estate SPC | Bahrain | 100% | 100% | To hold property for the beneficial interest of the Bank. |
| Harbour West 4 Real Estate SPC | Bahrain | 100% | 100% | To hold property for the beneficial interest of the Bank. |
| Surooh Limited | Cayman Islands | 19.08% | 19.08% | To construct and sell properties at "Oryx Hills". |

Going concern:

As of 31 December 2019, the total equity of the Bank was below the minimum BD 100 million required under LR module of volume 2 of the rule book issued by CBB. The Board of directors has mandated an international bank to assist it with issuing additional tier 1 capital (AT1) of BD 37.7 million to help strengthen its equity and meet the regulatory requirements.

The Bank is in the process of obtaining regulatory approval for this issue. Notwithstanding this, the Bank's regulatory capital adequacy ratio as of 31 December 2019 was 16.25%, well above the minimum ratio required by the CBB. Accordingly, the financial statements have been prepared on going concern basis.

2. STATEMENT OF COMPLIANCE

The financial statements have been prepared in accordance with Financial Accounting Standards ('FAS') issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ('AAOIFI'). In line with the requirement of AAOIFI, for matters that are not covered by AAOIFI standards, the Group uses guidance from the relevant International Financial Reporting Standards.

3. BASIS OF PREPARATION

The consolidated financial statements are presented in Bahraini Dinars, which is also the principal currency of the Bank's operations. They have been prepared on the historical cost basis except for the measurement at fair value of certain investments carried at fair value.

The Group classifies its expenses in the income statement by the nature of expense method.

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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.

i) Standards issued and effective from 1 January 2019

There are no new AAOIFI standards and interpretations effective for financial year beginning on or after 1 January 2019 that would be expected to have a material impact on the Group.

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

The objective of this standard is to establish the principles of accounting and financial reporting for the investment agency (Al-Wakala Bi Al-Istithmar) instruments and the related assets and obligations, as applicable, for the Islamic financial institutions from both perspectives i.e. the principal (investor) and the agent.

Principal (Investor)

The standard requires the principal either to follow the Pass through approach (as a preferred option) or the Wakala venture approach.

Pass through approach

A pass-through investment is an investment in which the involvement of the agent, as well as, the options for transferability of the instrument are limited and the investor principally takes a direct exposure on the underlying assets. There is a rebuttable assumption that in all investment agency arrangements, the investor takes direct exposure on the underlying assets (including a business) at the back end. As a result, the investor shall account for the assets (including the business) in its books directly, according to appropriate accounting policies applicable on such assets (or business) in line with respective FAS or the generally accepted accounting principles in absence of a specific FAS on the subject.

Wakala venture approach

Wakala venture approach can be adopted when the, if the investment agency contracts meets the conditions of the instrument being transferable and the investment is subject to frequent changes at the discretion of the agent. In case of this approach, the principal accounts for the investment in Wakala venture by applying the equity method of accounting.

Agent

The standard requires the agent either to follow the off- balance sheet approach or the on- balance sheet approach (only on exceptions by virtue of additional considerations attached to the investment agency contract).

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ii) Standards issued but not yet effective (continued)

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

Off-balance sheet approach

At inception of the transaction the agent shall recognize an agency arrangement under off-balance sheet approach whereby, since the agent does not control the related assets / business and hence does not record the assets and related income and expenditure in its books of account. The agent shall not recognize the assets and / or liabilities owned by the investor(s) (principal(s)) in its books of account.

If the agent previously owned such assets directly or through on-balance sheet equity of investment accountholders or similar instruments, the agent shall de-recognize the assets (and liabilities) from its books of account.

On-balance sheet approach

An agent may maintain multi-level investment arrangements based on independent permissible transactions with the agent itself. Notwithstanding the requirements of this standard with regard to investment agency arrangements, such secondary transactions shall be accounted for in line with the requirements of respective FAS in the books of the agent.

The agent shall consider the investment agency arrangement as a quasi-equity instrument for accounting purposes, if the investment agency instrument, by virtue of additional considerations attached to the instrument, is subordinated to all liabilities of the agent.

This standard is not expected to have a significant impact on the bank. This standard shall be effective for the financial periods beginning on or after 1 January 2020. Early adoption is permitted.

Transitional provisions

An entity may opt not to apply this standard only on such transactions:

- a. which were already executed before the adoption date of this standard for the entity; and
- b. their original maturity falls no later than 12 months after the adoption date of this standard for the entity.

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

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 institutions investments whether in the form of debt or equity securities. This standard replaces FAS 25 Investment in Sukuk, shares and similar instruments and produces revised guidance for classification and measurement of investments to align with international practices.

The standard classifies investments into equity type, debt type and other investment instruments. Investments in equity instruments must be at fair value and will not 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.

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.

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ii) Standards issued but not yet effective (continued)

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

Transitional provisions

The standard shall be applicable on a retrospective basis. However, the cumulative effect, if any, attributable to profit and loss taking stakeholders, including investment accountholders related to previous periods, shall be adjusted with the investments fair value reserve pertaining to such class of stakeholders.

The Bank is still in the process of estimating the impact of adoption of this standard on the consolidated financial statements. This standard shall be effective from the financial periods beginning on or after 1 January 2020. Early adoption is permitted.

c) FAS 34 - Financial Reporting for Sukuk-holders

The objective of this standard is to establish the principles of accounting and financial reporting for assets and business underlying the Sukuk to ensure transparent and fair reporting to all relevant stakeholders particularly Sukuk-holders.

This standard shall apply to Sukuk in accordance with Shari'ah principles and rules issued by an IFI or other institution (called "originator"), directly or through the use of a Special Purpose Vehicle (SPV) or similar mechanism. In respect of Sukuk which are kept on-balance sheet by the originator in line with requirements of FAS 29 "Sukuk in the books of the originator", the originator may opt not to apply this standard.

The standard classifies Sukuk as Business Sukuk and Non-business sukuk and lays down accounting treatment for Business and Non- business Sukuk.

This standard is not expected to have an impact on the bank. This standard shall be effective from the financial periods beginning on or after 1 January 2020. Early adoption is permitted.

Transitional provisions

An entity may opt not to apply this standard only on following transactions:

- a. which were already executed before the adoption date of this standard for the entity; and
- b. their original maturity falls no later than 12 months after the adoption date of this standard for the entity.

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(a) Basis of consolidation

(i) 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.

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.

(ii) Associates

Associates are those entities over which the Group holds exercises significant influence, but not control or joint control, over the financial and operating policies. These are accounted for under the equity method.

Investments in associates are initially recognised at 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 an associate, 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 associate.

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

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(a) Basis of consolidation (continued)

(iii) 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 equity securities that is designated at FVTIS. The rest are classified as investments at fair value through equity.

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for the year ended 31 December 2019

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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.

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(c) Investment securities (continued)

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. When available, the Group measure the fair value of an instruments using the quoted price in an active market for that instrument.

For unquoted investments at fair value, the Group uses recognised valuation techniques for fair valuation. 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.

Valuation adjustments are recorded to allow for bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state the values of these investments.

When there is no quoted price or other appropriate methods from which to derive a reliable fair value, equity investments are carried at cost less impairment.

(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.

(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 customers, takes into consideration the credit evaluation of the respective customer in addition to other factors.

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5. *SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)***(h) Investment in real estate**

Real estate properties held for rental, or for capital appreciation purposes, or both, are classified as investment in real estate. Investments in real estate are carried at cost less depreciation and impairment allowances, if any. Cost includes expenditure that is directly attributable to the acquisition of the investment property. Investment in real estate includes plots of land held for capital appreciation purposes, villas and buildings held for earning rentals. Land is not depreciated. Buildings are depreciated over 25 years.

(i) Development properties

Development property consists of villas being developed for sale in the ordinary course of business and costs incurred in bringing such property to its saleable condition.

Development property is stated 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.

(j) 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.

(k) 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.

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

*(k) Impairment of financial instruments (continued)**i) Exposures subject to credit risk (continued)*

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.

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').

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(k) Impairment of financial instruments (continued)

i) Exposures subject to credit risk (continued)

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; and
- Financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group expects to recover.

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

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.

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5. *SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**(k) Impairment of financial instruments (continued)***ii) Equity investments classified at fair value through equity (FVTE)**

In the case of investments in equity securities classified as FVTE and measured at fair value, 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.

For FVTE investments carried at cost less impairment due to the absence of reliable measure of fair value, the Group makes an assessment of whether there is an objective evidence of impairment for each investment by assessment of financial and other operating and economic indicators. Impairment is recognised if the estimated recoverable amount is below the carrying value of the investment.

(l) 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.

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 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. Separately recognised goodwill is not amortised and is tested annually for impairment and carried at cost less accumulated impairment losses. Impairment losses on separately recognised goodwill are not reversed. As at December 2019, the Group did not have any goodwill recognised.

(m) 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.

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5. *SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)***(n) 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.

(o) Restricted investment accounts

Restricted investment accounts represents 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.

(p) 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.

(q) 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.

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(r) 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.

(s) 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.

(t) 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.

(u) 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.

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5. *SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)*

(v) 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.

(w) Dividends and board remuneration

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

(x) 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.

(y) 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.

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5. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(z) 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.

(aa) 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.

(bb) 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.

(cc) Medium term Borrowing

Medium-term borrowing represents borrowing obtained through murabaha contract recognized on the origination date and carried at amortized cost.

6. CASH AND BANK BALANCES

| | 31 December 2019 | 31 December 2018 |
|---------------------------------|-----------------------------|-----------------------------|
| Cash | 5,299 | 8,130 |
| Balances with banks | 42,601 | 55,551 |
| Balances with the Central Bank: | | |
| - Current account | 31,047 | 14,950 |
| - Reserve account | 25,430 | 20,820 |
| Less: Impairment allowance | (1) | (50) |
| | 104,376 | 99,401 |

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

7. PLACEMENTS WITH FINANCIAL INSTITUTIONS

| | 31 December 2019 | 31 December 2018 |
|--------------------------------------|-----------------------------|-----------------------------|
| Gross Murabaha and Wakala receivable | 65,524 | 43,689 |
| Less: Deferred profits | (15) | (50) |
| Less: Impairment allowance | (1) | (2) |
| | 65,508 | 43,637 |

The average profit rate on placement with financial institutions for 2019 was 3.07% per annum (31 December 2018: 2.92% per annum). Placements with financial institutions with original maturities of 90 days or less is nil (31 December 2018: BD 42,590).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

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8. FINANCING ASSETS

| | 31 December 2019 | 31 December 2018 |
|-----------------------------|-----------------------------|-----------------------------|
| Murabaha | 354,510 | 338,012 |
| Musharaka | 104 | 3,541 |
| Wakala | 5,007 | 5,007 |
| Mudharaba | 1,047 | 1,049 |
| Istisna | 1,733 | 2,054 |
| | 362,401 | 349,663 |
| Less: Impairment allowances | (38,046) | (22,023) |
| | 324,355 | 327,640 |

Murabaha financing receivables are net of deferred profits of BD 25,724 thousand (2018: BD 25,088 thousand).

The movement on impairment allowances is as follows:

| 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 |

| 2018 | Stage 1 | Stage 2 | Stage 3 | Total |
|-----------------------------|----------------|----------------|----------------|---------------|
| At 1 January 2018 | 2,647 | 9,621 | 7,778 | 20,046 |
| Net movement between stages | 2,545 | (4,792) | 2,247 | - |
| Net charge for the year | (430) | (1,134) | 5,107 | 3,543 |
| Write-off | - | - | (1,566) | (1,566) |
| At 31 December 2018 | 4,762 | 3,695 | 13,566 | 22,023 |

9. INVESTMENT IN SUKUK

| | 31 December 2019 | 31 December 2018 |
|--------------------------------------------------|-----------------------------|-----------------------------|
| Debt type instruments – at amortized cost | | |
| - Quoted sukuk * | 195,061 | 161,327 |
| - Unquoted sukuk | 1,317 | 1,317 |
| Less: Impairment allowances | (1,328) | (1,320) |
| | 195,050 | 161,324 |

* Sukuk of BD 48,888 thousand were pledged against medium-term borrowings of BD 41,357 thousand which was repaid during the year (refer note 16).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

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10. ASSETS ACQUIRED FOR LEASING

| | 2019 | 2018 |
|-----------------------------------------|----------------|-------------|
| Cost | | |
| At 1 January | 138,952 | 119,995 |
| Additions during the year | 53,688 | 31,446 |
| Settlements/adjustments during the year | (24,331) | (12,489) |
| At 31 December | 168,309 | 138,952 |
| Accumulated depreciation | | |
| At 1 January | 30,274 | 22,802 |
| Charge for year | 16,714 | 11,400 |
| Settlements during the year | (7,776) | (3,928) |
| At 31 December | 39,212 | 30,274 |
| Net book value at 31 December | 129,097 | 108,678 |

At 31 December 2019, accrued lease rental receivable amounted to BD 17,102 thousand (2018: BD 11,525 thousand). Lease rental receivable is net of stage 1 and 2 ECL of BD 516 thousand (2018: BD 245 thousand) and Stage 3 ECL of BD 2,705 thousand (2018: 2,211 thousand). During the year, an impairment allowance of BD 765 thousand (2018: BD 725 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 84,958 thousand (2018: BD 85,644 thousand).

11. INVESTMENT IN EQUITY SECURITIES

| | 31 December 2019 | 31 December 2018 |
|---------------------------------------------------------------------------------------|-------------------------|-------------------------|
| <i>At fair value through income statement</i> | | |
| - Unquoted equity securities | 11,174 | 13,148 |
| <i>At fair value through equity</i> | | |
| - Gross Unquoted equity securities carrying amount (carried at cost less impairment)* | 50,563 | 51,972 |
| Less: Impairment allowances | (17,748) | (15,081) |
| | 43,989 | 50,039 |

* Unquoted equity securities at fair value through equity comprise investments in closed companies. These investments are carried at cost less impairment in the absence of a market price or a reliable measure of fair value. The Group intends to exit these investments principally by means of private placements, strategic buy outs or sale of underlying assets.

During the year, impairment charge of BD 2,667 thousand (31 December 2018: BD 2,205 thousand) was recognised on equity securities carried at cost (note 23).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

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12. INVESTMENT IN REAL ESTATE

| | Land | Building | 2019 Total | 2018 Total |
|--------------------------------------|---------------|----------|---------------|---------------|
| Cost | | | | |
| At 1 January | 18,081 | - | 18,081 | 20,992 |
| Additions | - | - | - | 105 |
| Disposals | - | - | - | (3,016) |
| Impairment (note 23) | (300) | - | (300) | - |
| At 31 December | 17,781 | - | 17,781 | 18,081 |
| Accumulated Depreciation | | | | |
| At 1 January | - | - | - | 1,371 |
| Charge for year | - | - | - | - |
| Disposals | - | - | - | (1,371) |
| At 31 December | - | - | - | - |
| Net book value at 31 December | 17,781 | - | 17,781 | 18,081 |

13. OTHER ASSETS

| | 31 December 2019 | 31 December 2018 |
|--------------------------|---------------------|---------------------|
| Reposessed assets | 13,513 | 853 |
| Investment in associates | 4,524 | 4,575 |
| Profit accrued on Sukuk | 3,250 | 2,820 |
| Due from investments | 985 | 1,070 |
| Prepaid expenses | 776 | 765 |
| Other receivables | 5,445 | 6,415 |
| | 28,493 | 16,498 |

Other receivables is net of impairment allowance of BD 1,742 thousand (2018: BD 954 thousands).

14. PROPERTY AND EQUIPMENT

| | Land | Furniture and fixtures | Computers | Motor vehicle and Other equipment | Work-in- progress | 2019 Total | 2018 Total |
|---------------------------------|--------------|------------------------------|--------------|--------------------------------------------|----------------------|---------------|---------------|
| Cost | | | | | | | |
| At 1 January | 6,714 | 4,472 | 5,085 | 572 | - | 16,843 | 16,169 |
| Additions | - | 6 | 267 | 4 | 175 | 452 | 674 |
| Disposals | - | (7) | (98) | - | - | (105) | - |
| At 31 December | 6,714 | 4,471 | 5,254 | 576 | 175 | 17,190 | 16,843 |
| Accumulated Depreciation | | | | | | | |
| At 1 January | - | 4,285 | 4,234 | 459 | - | 8,978 | 8,414 |
| Charge for year (note 22) | - | 72 | 447 | 48 | - | 567 | 564 |
| Disposals | - | (7) | (98) | - | - | (105) | - |
| At 31 December | - | 4,350 | 4,583 | 507 | - | 9,440 | 8,978 |
| Net book value | | | | | | | |
| At 31 December 2019 | 6,714 | 121 | 671 | 69 | 175 | 7,750 | 7,865 |
| At 31 December 2018 | 6,714 | 187 | 851 | 113 | - | 7,865 | |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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15. PLACEMENTS FROM NON-FINANCIAL INSTITUTIONS AND INDIVIDUALS

| | 31 December 2019 | 31 December 2018 |
|----------------------------|-----------------------------|---------------------|
| Non-financial institutions | 51,660 | 48,325 |
| Individuals | 82,994 | 72,145 |
| | 134,654 | 120,470 |

These represent placements in the form of Murabaha and Wakala contracts. These are net of deferred profit of BD 5,218 thousand (2018: BD 4,188 thousand).

16. MEDIUM-TERM BORROWING

During 2018, the Bank had two medium-term Murabaha facilities of BD 41,357 thousand secured by pledge over sukuk of BD 48,888 thousand. These borrowings were repaid during the year.

17. OTHER LIABILITIES

| | 31 December 2019 | 31 December 2018 |
|-------------------------------------|-----------------------------|---------------------|
| Mudaraba profit accrual | 8,911 | 4,278 |
| Advance received from customers | 3,274 | 361 |
| Employee related accruals* | 1,251 | 245 |
| Zakah and charity payable | 714 | 708 |
| Payable for Istisna'a contracts | 27 | 27 |
| Other payables and accrued expenses | 5,621 | 4,893 |
| | 19,798 | 10,512 |

* During the fourth quarter, the Bank has offered a voluntary retirement scheme to its employees. As of 31 December 2019, the total retrenchment cost amounted to BD 825 thousand.
Other payables and accrued expenses is net of impairment allowance of BD 268 thousand (2018: BD 380 thousand).

18. EQUITY OF INVESTMENT ACCOUNT HOLDERS

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

| | 31 December 2019 | 31 December 2018 |
|----------------------------------------|-----------------------------|---------------------|
| Balances with banks | 42,601 | 55,550 |
| CBB reserve account | 25,430 | 20,820 |
| Placements with financial institutions | 65,508 | 43,637 |
| Debt type instruments – sukuk | 195,050 | 161,327 |
| Financing assets | 183,246 | 65,039 |
| | 511,835 | 346,373 |

As at 31 December 2019, the balance of profit equalisation reserve and investment risk reserve was Nil (2018: Nil).

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18. EQUITY OF INVESTMENT ACCOUNT HOLDERS (CONTINUED)

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 the 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.

| | 2019 | | 2018 | |
|---------------------|---------------|------------|---------------|------------|
| | Mudarib share | IAH shares | Mudarib share | IAH shares |
| 1 month Mudharaba * | 80.61% | 19.39% | 78.66% | 21.34% |
| 3 months Mudharaba | 65.38% | 34.62% | 54.41% | 45.59% |
| 6 months Mudharaba | 60.00% | 40.00% | 49.31% | 50.69% |
| 12 months Mudharaba | 42.96% | 57.04% | 29.50% | 70.50% |
| 18 months Mudharaba | 38.65% | 61.35% | 23.28% | 76.72% |
| 24 months Mudharaba | 43.11% | 56.89% | 21.15% | 78.85% |
| 36 months Mudharaba | 32.37% | 67.63% | 14.70% | 85.30% |

* Includes savings, Al Waffer and Call Mudaraba accounts.

During the year, average mudarib share as a percentage of total income allocated to IAH was 46.56% (2018: 41.82%) as against the average mudarib share contractually agreed with IAH. Hence the Group sacrificed average mudarib fees of 12.83% (2018: 20.38%).

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.

19. SHARE CAPITAL

| | 31 December 2019 | 31 December 2018 |
|----------------------------------------------------------------------|---------------------|---------------------|
| Authorised: | | |
| 3,000,000,000 ordinary shares of BD 0.100 each | 300,000 | 300,000 |
| Issued and fully paid up: | | |
| 1,050,000,000 ordinary shares (2018: 1,050,000,000) of BD 0.100 each | 105,000 | 105,000 |

The Group has only one class of equity shares and the holders of these shares have equal voting rights. At 31 December 2019, the Group holds 105,573,476 as treasury shares (2018: 101,081,714 shares).

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19. SHARE CAPITAL (CONTINUED)

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

| 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 |
| | 1,050,000,000 | 613 | 100 |

* 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:

| | 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 |

*As at 31 December 2019, these shares representing 47% (2018: 47%) were held by KHCB Asset Company on behalf of GFH Financial Group, which is considered as the parent of the Bank for financial reporting purposes.

20. INCOME FROM SUKUK

| | 2019 | 2018 |
|------------------------|---------------|--------------|
| Profit earned on Sukuk | 10,068 | 6,489 |
| Loss on sale of Sukuk | (37) | (112) |
| | 10,031 | 6,377 |

21. STAFF COST

| | 2019 | 2018 |
|----------------------------------|--------------|--------------|
| Salaries and short-term benefits | 7,073 | 6,075 |
| Social insurance expenses | 964 | 929 |
| Other staff expenses | 121 | 171 |
| | 8,158 | 7,175 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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22. OTHER OPERATING EXPENSES

| | 2019 | 2018 |
|--------------------------------------|--------------|--------------|
| Premises cost | 1,059 | 1,037 |
| Advertisement and marketing expenses | 660 | 437 |
| Professional fees | 1,194 | 825 |
| Information technology expenses | 536 | 483 |
| Board expenses | 244 | 441 |
| Communication expenses | 286 | 300 |
| Distribution channel expenses | 589 | 495 |
| Depreciation expenses (note 14) | 567 | 564 |
| Other administrative expenses | 901 | 670 |
| | 6,036 | 5,252 |

23. NET IMPAIRMENT CHARGE

| | 2019 | 2018 |
|-------------------------------------------------------------------------------|---------------|--------------|
| Balances and placements with banks and financial institutions (notes 6 and 7) | (50) | 50 |
| Financing assets (note 8) | 16,023 | 3,543 |
| Investments in sukuk (note 9) | 8 | (100) |
| Assets acquired for leasing - including lease rentals receivables (note 10) | 765 | 725 |
| Equity investments at fair value through equity (note 11) | 2,667 | 2,205 |
| Investment in real estate (note 12) | 300 | - |
| Other assets (note 13) | 788 | - |
| Commitments and financial guarantees | (112) | (135) |
| | 20,389 | 6,288 |

24. SHARE-BASED EMPLOYEE INCENTIVE SCHEME

During 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. Prior to this the shares were held in Hawafiz Khaleeji Management Company BSC (c).

The shareholders, in their annual general meeting held on 30 March 2015, approved the employee share based incentive scheme (the "scheme") which is 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.

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 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 2019, 1,980,960 shares were held by the Trust (2018: 2,746,957 shares were held by Hawafiz). During the year 1,182,516 shares (2018: 917,628 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 1,465,997 shares (2018: 1,896,808 shares) to the employees.

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25. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The Group makes 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.

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 5(k) and Note 35.

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) Going concern

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

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(k) and Note 35.

b) Impairment of equity investments at fair value through equity

The Group determines that equity securities carried at fair value are impaired when there is an objective evidence of impairment and there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment.

In case of quoted equity securities, the Group considers a decline of more than 30% in the fair value below cost to be significant and considers a decline below cost which persists for more than 9 months as prolonged.

For unquoted equity investments carried at cost less impairment, the Group makes an assessment of whether there is an objective evidence of impairment for each investment by assessment of financial and other operating and economic indicators. Impairment is recognised if the estimated recoverable amount is assessed to be below the cost of the investment. It is reasonably possible, based on existing knowledge, that the current assessment of impairment could require a material adjustment to the carrying amount of the investments within the next financial year due to significant changes in the assumptions underlying such assessments.

Determining fair value of unquoted equity securities

The Group determines the fair value of unquoted investments by using valuation techniques. This includes using recent arm's length transactions between knowledgeable, willing parties (if available), discounted cash flow analysis or market multiples for similar instruments. Fair value estimates are made at a specific point in time, based on market conditions and information about the investee companies.

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25. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES
(continued)

These 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.

Significant judgment is required to be made by the Group and the Board of Directors in the selection of an approach that would reflect the best measure of fair value of the investments. The choice of the models used for valuation on each reporting period may have a significant impact on the fair value of investments and the amounts reported in the consolidated financial statements. During the year, Group has adopted the adjusted net book value approach for valuation of its unquoted equity security as compared to the market multiple approach used in prior year.

The potential effect of using reasonable possible alternative assumptions for valuing the investments resulting in 5% decrease/increase in the relevant variable used would increase/decrease the fair value by BD 558 thousand (31 December 2018: BD 657 thousand). The corresponding impact would be on the profit or loss reported by the Group.

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 262.25 million (31 December 2018: BD 230.72 million). During the year, the Group has not charged any management fees (2018: BD Nil) for the management of these assets.

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.

Details of Directors' interests in the Bank's ordinary shares as at the end of the year were:

| Categories* | Number of Shares | Number of Directors |
|--------------|------------------|---------------------|
| Less than 1% | 1,050,763 | 1 |

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

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:

| | 2019 | 2018 |
|----------------------------------------|-------|-------|
| Board member fees and allowances | 254 | 433 |
| Salaries and other short-term benefits | 1,150 | 1,402 |

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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 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 in equity securities | - | - | 2,284 | 18,051 | 20,335 |
| Other assets | 4,645 | - | - | 865 | 5,510 |
| Liabilities | | | | | |
| Placement from financial institutions and others | - | 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 |

31 December 2018

| | 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 | - | 2,268 | 5,710 | - | 7,978 |
| Investment in equity securities | - | - | 2,284 | 20,719 | 23,003 |
| Other assets | 117 | - | - | 853 | 970 |
| Liabilities | | | | | |
| Placement from financial institutions and others | - | - | 93,917 | - | 93,917 |
| Customers' current accounts | 67 | 798 | 695 | 1,205 | 2,765 |
| Equity of investment account holders | 480 | 1,370 | 10,779 | 468 | 13,097 |

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27. **RELATED PARTY TRANSACTIONS** (continued)

2019

| | Associates | Directors / Key management personnel | 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 |
| Income from equity securities | - | - | - | - | - |
| 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 |

2018

| | Associates | Directors / Key management personnel | 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 | - | 133 | 373 | - | 506 |
| Income from equity securities | - | - | - | 143 | 143 |
| Fees and other income | - | - | - | - | - |
| Expenses | | | | | |
| Finance expense on placements from financial institutions, non-financial institutions and individuals | - | - | 2,278 | - | 2,278 |
| Return to investment account holders | 12 | 31 | 350 | 11 | 404 |
| Staff cost | - | 1,402 | - | - | 1,402 |
| Other expenses | - | - | - | 59 | 59 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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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

| | 2019 | 2018 |
|----------------------------------------------------------|-------------|-------------|
| Profit attributable to parent for the year (BD 000's) | (14,937) | 659 |
| Weighted average number of equity shares (Nos. in 000's) | 941,703 | 956,400 |
| Basic earnings per share (in fils) | (15.86) | 0.69 |

The Group did not have any dilutive instruments as of 31 December 2019 and December 2018.

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 222 thousand (2018: BD 191 thousand) of which BD 218 thousand (2018: 187 thousand) represents the Zakah computed on the statutory reserve and cumulative retained earnings as at 31 December 2019, payable by the Group. The remaining Zakah balance amounting to BD 4 thousand or 0.003 fils per share (2018: BD 4 thousand or 0.004 fils per share) is due and payable by the shareholders. The Group will pay Zakah of BD 0.4 thousand (2018: BD 0.4 thousand) on the treasury shares held as of 31 December 2019 based on 0.003 fils per share.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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BD 000's

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

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.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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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 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 in equity securities | 43,989 | - | - | 43,989 |
| Investment in real estate | 17,781 | - | - | 17,781 |
| Development property | 6,251 | - | - | 6,251 |
| Other assets | 18,430 | 4,182 | 5,881 | 28,493 |
| Property and equipment | - | - | 7,750 | 7,750 |
| Total segment assets | 87,636 | 838,485 | 13,631 | 939,752 |
| Placements from financial institutions | - | 127,453 | - | 127,453 |
| Placements from non- financial institutions and individuals | - | 134,654 | - | 134,654 |
| Medium-term borrowing | - | - | - | - |
| Customers' current accounts | 1,184 | 56,921 | - | 58,105 |
| Other liabilities | 1,847 | 13,647 | 4,304 | 19,798 |
| Total segment liabilities | 3,031 | 332,675 | 4,304 | 340,010 |
| Equity of investment account holders | - | 511,835 | - | 511,835 |
| Restricted investment accounts | 10,681 | - | - | 10,681 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

BD 000's

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 equity 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 | - | (23,544) | - | (23,544) |
| Bank's share as a Mudarib | - | 8,457 | - | 8,457 |
| Return to investment account holders | - | (15,087) | - | (15,087) |
| Less: | | | | |
| Expense on placements from financial institutions, non-financial institutions and individuals | - | (11,703) | - | (11,703) |
| Finance expense on medium-term borrowing | - | (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 allowances | (2,968) | (17,421) | - | (20,389) |
| Segment results | (5,482) | (793) | (8,752) | (15,027) |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

BD 000's

31. *SEGMENT REPORTING (continued)*

| 31 December 2018 | Investment Banking | Corporate and Retail Banking | Unallocated | Total |
|-------------------------------------------------------------------------|-----------------------|---------------------------------|-------------|---------|
| Cash and bank balances | 1 | 99,400 | - | 99,401 |
| Placements with financial institutions | 1,175 | 42,462 | - | 43,637 |
| Financing assets | - | 327,640 | - | 327,640 |
| Investment in sukuk | - | 161,324 | - | 161,324 |
| Assets acquired for leasing (including lease rentals receivables) | - | 120,203 | - | 120,203 |
| Investment in equity securities | 50,039 | - | - | 50,039 |
| Investment in real estate | 18,081 | - | - | 18,081 |
| Development property | 6,251 | - | - | 6,251 |
| Other assets | 11,320 | 3,958 | 1,220 | 16,498 |
| Property and equipment | - | - | 7,865 | 7,865 |
| Total segment assets | 86,867 | 754,987 | 9,085 | 850,939 |
| Placements from financial institutions | - | 158,349 | - | 158,349 |
| Placements from non- financial institutions and individuals | - | 120,470 | - | 120,470 |
| Medium-term borrowing | - | 41,357 | - | 41,357 |
| Customers' current accounts | 1,175 | 69,241 | - | 70,416 |
| Other liabilities | 2,171 | 6,220 | 2,121 | 10,512 |
| Total segment liabilities | 3,346 | 395,637 | 2,121 | 401,104 |
| Equity of investment account holders | - | 346,373 | - | 346,373 |
| Restricted investment accounts | 10,681 | - | - | 10,681 |

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

BD 000's

31. **SEGMENT REPORTING** (continued)

| 2018 | Investment Banking | Corporate and Retail Banking | Unallocated | Total |
|---------------------------------------------------------------------------------------------------------|-----------------------|---------------------------------|-------------|----------|
| Income from financing assets and assets acquired for leasing | - | 26,565 | - | 26,565 |
| Income from placements with financial institutions | 25 | 930 | - | 955 |
| Income from sukuk | - | 6,377 | - | 6,377 |
| Income from equity securities | 1,422 | - | - | 1,422 |
| Fees and other income | (35) | 2,877 | - | 2,842 |
| Total income before return to investment account holders | 1,412 | 36,749 | - | 38,161 |
| Less: Return to investment account holders before Bank's share as Mudarib | - | (14,221) | - | (14,221) |
| Bank's share as a Mudarib | - | 5,619 | - | 5,619 |
| Return to investment account holders | - | (8,602) | - | (8,602) |
| Less: | | | | |
| Expense on placements from financial institutions, non- financial institutions and individuals | - | (8,190) | - | (8,190) |
| Finance expense on medium- term borrowing | - | (2,054) | - | (2,054) |
| Total segment income | 1,412 | 17,903 | - | 19,315 |
| Staff cost | 718 | 2,870 | 3,587 | 7,175 |
| Other expenses | 92 | 951 | 4,209 | 5,252 |
| Total segment expenses | 810 | 3,821 | 7,796 | 12,427 |
| Segment results before impairment allowances | 602 | 14,082 | (7,796) | 6,888 |
| Net impairment allowances | (2,205) | (4,083) | - | (6,288) |
| Segment results | (1,603) | 9,999 | (7,796) | 600 |

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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 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 in equity securities | - | - | 7,056 | 15,549 | 21,384 | 43,989 |
| Investment in real estate | - | - | - | - | 17,781 | 17,781 |
| Development property | - | - | - | - | 6,251 | 6,251 |
| Other assets | 844 | 1,061 | 1,993 | 22,975 | 1,620 | 28,493 |
| 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 | 3,774 | - | 15,637 | 108,042 | - | 127,453 |
| Placements from non-financial institutions and individuals | 37,914 | 39,623 | 41,594 | 12,232 | 3,291 | 134,654 |
| Medium-term borrowing | - | - | - | - | - | - |
| 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 | 66,283 | 47,442 | 66,677 | 134,890 | 24,718 | 340,010 |
| Equity of investment account holders | 120,398 | 86,311 | 126,115 | 86,274 | 92,737 | 511,835 |
| 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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32. **MATURITY PROFILE** (continued)

| 31 December 2018 | 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 | 87,253 | 3,591 | 6,065 | 2,492 | - | 99,401 |
| Placements with financial institutions | 42,590 | - | 1,047 | - | - | 43,637 |
| Financing assets | 73,057 | 26,731 | 69,848 | 119,405 | 38,599 | 327,640 |
| Investment in sukuk | 112,436 | - | 48,888 | - | - | 161,324 |
| Assets acquired for leasing (including lease rentals receivables) | 4,805 | 3,549 | 7,069 | 34,572 | 70,208 | 120,203 |
| Investment in equity securities | - | - | - | 25,273 | 24,766 | 50,039 |
| Investment in real estate | - | - | - | - | 18,081 | 18,081 |
| Development property | - | - | - | - | 6,251 | 6,251 |
| Other assets | 1,939 | - | 9 | 12,028 | 2,522 | 16,498 |
| Property and equipment | - | - | - | - | 7,865 | 7,865 |
| Total assets | 322,080 | 33,871 | 132,926 | 193,770 | 168,292 | 850,939 |
| Liabilities | | | | | | |
| Placements from financial institutions | 31,312 | 17,664 | 109,373 | - | - | 158,349 |
| Placements from non-financial institutions and individuals | 35,172 | 38,057 | 34,314 | 10,108 | 2,819 | 120,470 |
| Medium-term borrowing | - | - | 41,357 | - | - | 41,357 |
| Customers' current account | 21,649 | 6,853 | 7,442 | 8,505 | 25,967 | 70,416 |
| Other liabilities | 3,233 | 1,304 | 1,131 | 4,844 | - | 10,512 |
| Total liabilities | 91,366 | 63,878 | 193,617 | 23,457 | 28,786 | 401,104 |
| Equity of investment account holders | 69,089 | 43,815 | 98,703 | 55,512 | 79,254 | 346,373 |
| Restricted investment accounts | - | - | - | 10,681 | - | 10,681 |
| Commitments and financial guarantees | 20,284 | 3,986 | 16,204 | 5,577 | 6 | 46,057 |

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

(a) Industry sector

31 December 2019

Assets

| | Banks and financial institutions | Real estate | Others | Total |
|-------------------------------------------------------------------|-----------------------------------------|--------------------|---------------|----------------|
| 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 in equity securities | 11,174 | 29,147 | 3,668 | 43,989 |
| Investment in real estate | - | 17,781 | - | 17,781 |
| Development property | - | 6,251 | - | 6,251 |
| Other assets | 954 | 19,395 | 8,144 | 28,493 |
| Property and equipment | - | 6,739 | 1,011 | 7,750 |

Total assets

| | | | |
|----------------|----------------|----------------|----------------|
| 201,606 | 292,552 | 445,594 | 939,752 |
|----------------|----------------|----------------|----------------|

Liabilities

| | | | | |
|------------------------------------------------------------|---------|-------|---------|----------------|
| Placements from financial institutions | 127,453 | - | - | 127,453 |
| Placements from non-financial institutions and individuals | - | - | 134,654 | 134,654 |
| Medium-term borrowing | - | - | - | - |
| Customers' current accounts | 4,661 | 7,422 | 46,022 | 58,105 |
| Other liabilities | 17 | 588 | 19,193 | 19,798 |

Total liabilities

| | | | |
|----------------|--------------|----------------|----------------|
| 132,131 | 8,010 | 199,869 | 340,010 |
|----------------|--------------|----------------|----------------|

Equity of investment account holders

| | | | |
|--------------|----------------|----------------|----------------|
| 8,437 | 119,463 | 383,935 | 511,835 |
|--------------|----------------|----------------|----------------|

Restricted investment accounts

| | | | |
|----------|--------------|------------|---------------|
| - | 9,688 | 993 | 10,681 |
|----------|--------------|------------|---------------|

Commitments and financial guarantees

| | | | |
|----------|---------------|---------------|---------------|
| - | 51,779 | 28,933 | 80,712 |
|----------|---------------|---------------|---------------|

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BD 000's

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

(a) Industry sector (continued)

31 December 2018

| | Banks and financial institutions | Real estate | Others | Total |
|-------------------------------------------------------------------|----------------------------------|----------------|----------------|----------------|
| Assets | | | | |
| Cash and bank balances | 99,401 | - | - | 99,401 |
| Placements with financial institutions | 43,637 | - | - | 43,637 |
| Financing assets | 10,358 | 51,630 | 265,652 | 327,640 |
| Investment in sukuk | 11,795 | 7,540 | 141,989 | 161,324 |
| Assets acquired for leasing (including lease rentals receivables) | - | 118,615 | 1,588 | 120,203 |
| Investment in equity securities | 13,148 | 33,223 | 3,668 | 50,039 |
| Investment in real estate | - | 18,081 | - | 18,081 |
| Development property | - | 6,251 | - | 6,251 |
| Other assets | 1,040 | 6,822 | 8,636 | 16,498 |
| Property and equipment | - | 6,739 | 1,126 | 7,865 |
| Total assets | 179,379 | 248,901 | 422,659 | 850,939 |
| Liabilities | | | | |
| Placements from financial institutions | 158,349 | - | - | 158,349 |
| Placements from non-financial institutions and individuals | 101 | - | 120,369 | 120,470 |
| Medium-term borrowing | 41,357 | - | - | 41,357 |
| Customers' current accounts | 4,920 | 7,832 | 57,664 | 70,416 |
| Other liabilities | - | 27 | 10,485 | 10,512 |
| Total liabilities | 204,727 | 7,859 | 188,518 | 401,104 |
| Equity of investment account holders | 14,543 | 12,894 | 318,936 | 346,373 |
| Restricted investment accounts | - | 9,688 | 993 | 10,681 |
| Commitments and financial guarantees | 513 | 12,913 | 32,631 | 46,057 |

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

(b) Geographic sector

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 in equity securities | 25,938 | - | - | 14,383 | 3,668 | 43,989 |
| Investment in real estate | 17,781 | - | - | - | - | 17,781 |
| Development property | 6,251 | - | - | - | - | 6,251 |
| Other assets | 27,727 | 15 | - | 750 | 1 | 28,493 |
| 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 | 127,453 | - | - | - | - | 127,453 |
| Placements from non-financial institutions and individuals | 134,654 | - | - | - | - | 134,654 |
| Medium-term borrowing | - | - | - | - | - | - |
| Customers' current accounts | 57,230 | 257 | - | 618 | - | 58,105 |
| Other liabilities | 19,798 | - | - | - | - | 19,798 |
| Total liabilities | 339,135 | 257 | - | 618 | - | 340,010 |
| Equity of investment account holders | 509,300 | 694 | - | 1,841 | - | 511,835 |
| Restricted investment accounts | 9,688 | - | - | - | 993 | 10,681 |
| Commitments and financial guarantee | 80,712 | - | - | - | - | 80,712 |

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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BD 000's

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

(b) Geographic sector (continued)

| 31 December 2018 | GCC countries | Europe | America | Asia | Australia | Total |
|-------------------------------------------------------------------|---------------|--------|---------|--------|-----------|---------|
| Assets | | | | | | |
| Cash and bank balances | 73,827 | 7,230 | 18,306 | 38 | - | 99,401 |
| Placements with financial institutions | 43,637 | - | - | - | - | 43,637 |
| Financing assets | 313,642 | 13,960 | - | 38 | - | 327,640 |
| Investment in sukuk | 161,324 | | | | | 161,324 |
| Assets acquired for leasing (including lease rentals receivables) | 120,162 | - | - | 41 | - | 120,203 |
| Investment in equity securities | 29,320 | - | - | 17,051 | 3,668 | 50,039 |
| Investment in real estate | 18,081 | - | - | - | - | 18,081 |
| Development property | 6,251 | - | - | - | - | 6,251 |
| Other assets | 15,794 | 15 | - | 689 | - | 16,498 |
| Property and equipment | 7,865 | - | - | - | - | 7,865 |
| Total assets | 789,903 | 21,205 | 18,306 | 17,857 | 3,668 | 850,939 |
| Liabilities | | | | | | |
| Placements from financial institutions | 158,349 | - | - | - | - | 158,349 |
| Placements from non-financial institutions and individuals | 120,470 | - | - | - | - | 120,470 |
| Medium-term borrowing | 41,357 | - | - | - | - | 41,357 |
| Customers' current accounts | 69,916 | 274 | - | 226 | - | 70,416 |
| Other liabilities | 10,512 | - | - | - | - | 10,512 |
| Total liabilities | 400,604 | 274 | - | 226 | - | 401,104 |
| Equity of investment account holders | 343,589 | 545 | - | 2,231 | 8 | 346,373 |
| Restricted investment accounts | 9,688 | - | - | 993 | - | 10,681 |
| Commitments and financial guarantee | 45,801 | 256 | - | - | - | 46,057 |

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BD 000's

34. FAIR VALUE*a) Fair value of financial instruments*

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 195,061 thousand (31 December 2018: BD 161,327 thousand) is BD 204,198 thousand as at 31 December 2018 (31 December 2018: BD 161,644 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. Other than equity investments carried at cost of BD 32,815 thousand (2018: BD 36,891 thousand), 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 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 |

31 December 2018

Unquoted equity type securities carried
at fair value through income statement

| Level 1 | Level 2 | Level 3 | Total |
|---------|---------|---------------|---------------|
| - | - | 13,148 | 13,148 |
| - | - | 13,148 | 13,148 |

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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:

| | 2019 | 2018 |
|-------------------------------------|---------------|---------------|
| At 1 January | 13,148 | 13,148 |
| Fair value loss in income statement | (1,974) | - |
| At 31 December | 11,174 | 13,148 |

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
- operational 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.

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for the year ended 31 December 2019

BD 000's

35. *FINANCIAL RISK MANAGEMENT (continued)*

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 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.
- 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.

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BD 000's

35. *FINANCIAL RISK MANAGEMENT (continued)*

CREDIT RISK (continued)

- **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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for the year ended 31 December 2019

BD 000's

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

CREDIT RISK (continued)

Exposures subject to credit risk

31 December 2019

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 |
|--------------------------------------------------------------------------|----------------|---------------|---------------|----------------|
| 31 December 2019 | | | | |
| Financing facilities | | | | |
| Grade 8 -10 Impaired | - | - | 71,289 | 71,289 |
| Past due but not impaired | | | | |
| <i>Grade 1-6 Low-Fair Risk</i> | 33,624 | 6,790 | 56 | 40,470 |
| <i>Grade 7 Watch list</i> | 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 | | | | |
| <i>Grade 1-6 Low-Fair Risk</i> | 229,041 | 12,117 | 734 | 241,892 |
| <i>Grade 7 Watch list</i> | 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 | | | | |
| <i>Grade 1-6 Low-Fair Risk</i> | 12,648 | 7,501 | 769 | 20,918 |
| <i>Grade 7 Watch list</i> | - | 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 | | | | |
| <i>Grade 1-6 Low-Fair Risk</i> | 86,315 | 2,249 | 108 | 88,672 |
| <i>Grade 7 Watch list</i> | - | 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 |

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

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

for the year ended 31 December 2019

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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 |
|---------------------------------------------|----------------|---------------|---------------|----------------|
| 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 |

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

Exposure to credit risk (continued)

| 31 December 2018 | Stage 1 | Stage 2 | Stage 3* | Total |
|-------------------------------------------------------------------|---------|---------|----------|----------|
| Financing facilities | | | | |
| Grade 8 -10 Impaired | 1,071 | 70 | 71,628 | 72,769 |
| Past due but not impaired | | | | |
| Grade 1-6 Low-Fair Risk | 28,158 | 10,732 | 3,349 | 42,239 |
| Grade 7 Watch list | 14 | 15,403 | - | 15,417 |
| <u>Past due comprises:</u> | | | | |
| Up to 30 days | 27,287 | 15,866 | - | 43,153 |
| 30-60 days | 885 | 1,743 | - | 2,628 |
| 60-90 days | - | 8,526 | 3,349 | 11,875 |
| Neither past due nor impaired | | | | |
| Grade 1-6 Low-Fair Risk | 196,925 | 18,829 | - | 215,754 |
| Grade 7 Watch list | 139 | 3,345 | - | 3,484 |
| Gross carrying amount | 226,307 | 48,379 | 74,977 | 349,663 |
| Less expected credit losses | (4,762) | (3,695) | (13,566) | (22,023) |
| Net carrying amount | 221,545 | 44,684 | 61,411 | 327,640 |
| Assets acquired for leasing (including lease rentals receivables) | | | | |
| Grade 8 -10 Impaired | - | 316 | 18,613 | 18,929 |
| Past due but not impaired | | | | |
| Grade 1-6 Low-Fair Risk | 12,990 | 2,388 | - | 15,378 |
| Grade 7 Watch list | - | 3,846 | - | 3,846 |
| <u>Past due comprises:</u> | | | | |
| Up to 30 days | 12,212 | 1,926 | - | 14,138 |
| 30-60 days | 778 | 3,227 | - | 4,005 |
| 60-90 days | - | 1,080 | - | 1,080 |
| Neither past due nor impaired | | | | |
| Grade 1-6 Low-Fair Risk | 82,417 | 2,041 | - | 84,458 |
| Grade 7 Watch list | - | 48 | - | 48 |
| Gross carrying amount | 95,407 | 8,639 | 18,613 | 122,659 |
| Less expected credit losses | (106) | (139) | (2,211) | (2,456) |
| Net carrying amount | 95,301 | 8,500 | 16,402 | 120,203 |

* Includes facilities under cooling off period of BD 31,133 thousand.

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35. FINANCIAL RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Exposures subject to credit risk (continued)

| 31 December 2018 | Stage 1 | Stage 2 | Stage 3 | Total |
|--------------------------------------|---------|---------|---------|---------|
| Investment in Sukuk | | | | |
| Grade 8 -10 Impaired | - | - | 1,317 | 1,317 |
| Grade 1-6 Low-Fair Risk | 161,327 | - | - | 161,327 |
| Gross carrying amount | 161,327 | - | 1,317 | 162,644 |
| Less: expected credit losses | (3) | - | (1,317) | (1,320) |
| Net carrying amount | 161,324 | - | - | 161,324 |
| Balances with banks and placements | | | | |
| Grade 1-6 Low-Fair Risk | 134,960 | - | - | 134,960 |
| Gross carrying amount | 134,960 | - | - | 134,960 |
| Less: expected credit losses | (52) | - | - | (52) |
| Net carrying amount | 134,908 | - | - | 134,908 |
| Commitments and financial guarantees | | | | |
| Grade 8 -10 Impaired | - | - | 1,670 | 1,670 |
| Grade 1-6 Low-Fair Risk | 41,733 | 2,639 | - | 44,372 |
| Grade 7 Watch list | - | 15 | - | 15 |
| Gross carrying amount | 41,733 | 2,654 | 1,670 | 46,057 |
| Less: expected credit losses | (176) | (84) | (120) | (380) |
| Net carrying amount | 41,557 | 2,570 | 1,550 | 45,677 |
| Total net carrying amount | 654,635 | 55,754 | 79,363 | 789,752 |

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BD 000's

35. *FINANCIAL RISK MANAGEMENT (continued)*

CREDIT RISK (continued)

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

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 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

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35. FINANCIAL RISK MANAGEMENT (continued)

*CREDIT RISK (continued)**Credit risk grades (continued)**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 and borrower as well as by 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.

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.

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35. *FINANCIAL RISK MANAGEMENT (continued)*

CREDIT RISK (continued)

Determining whether credit risk has increased significantly (continued)

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.

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.

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.

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BD 000's

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

CREDIT RISK (continued)

Incorporation of forward looking information (continued)

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 2019 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.

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.

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BD 000's

35. *FINANCIAL RISK MANAGEMENT (continued)**CREDIT RISK (continued)***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);
- 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 |
|-------------------------------------------------|---------------------------------------|-------------------------------------------------------------------|---------------------------------------------------------------|---------------|
| Balance at 1 January 2019 | 5,099 | 3,918 | 17,214 | 26,231 |
| Transfer to 12-month ECL | 1,338 | (1,118) | (220) | - |
| Transfer to lifetime ECL non-credit-impaired | (500) | 604 | (104) | - |
| Transfer to lifetime ECL credit-impaired | (863) | (856) | 1,719 | - |
| Net transfers | (25) | (1,370) | 1,395 | - |
| Net re-measurement of loss allowance | (165) | 575 | 16,304 | 16,714 |
| Recoveries / write backs | - | - | (80) | (80) |
| Write-offs | - | - | - | - |
| Balance at 31 December 2019 | 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 |
|--------------------------------------------------------------------------------|---------------------------------------|-------------------------------------------------------------------|---------------------------------------------------------------|-----------------------|
| Cash and balances with banks (note 6) | 1 | - | - | 1 |
| Placements with financial institutions (note 7) | 1 | - | - | 1 |
| Financing assets (note 8) | 4,581 | 2,730 | 30,735 | 38,046 |
| Assets acquired for leasing – Including lease rentals receivables (note 10) | 140 | 376 | 2,705 | 3,221 |
| Investment in sukuk (note 9) | 11 | - | 1,317 | 1,328 |
| Commitments and financial Guarantees | 175 | 17 | 76 | 268 |
| | 4,909 | 3,123 | 34,833 | 42,865 |

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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 2018 |
|-------------------------------------------------|------------------------------|-----------------------------------------------------|----------------------------------------------|---------------|
| Balance at 1 January 2018 | 2,860 | 10,537 | 10,317 | 23,714 |
| Transfer to 12-month ECL | 3,188 | (3,086) | (102) | - |
| Transfer to lifetime ECL non-credit-impaired | (316) | 398 | (82) | - |
| Transfer to lifetime ECL credit-impaired | (229) | (2,463) | 2,692 | - |
| Net transfers | 2,643 | (5,151) | 2,508 | - |
| Net re-measurement of loss allowance | (404) | (1,468) | 7,668 | 5,796 |
| Recoveries / write backs | - | - | (1,713) | (1,713) |
| Write-offs | - | - | (1,566) | (1,566) |
| Balance at 31 December 2018 | 5,099 | 3,918 | 17,214 | 26,231 |

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 2018 |
|----------------------------------------------------------------------|------------------------------|--------------------------------------------------|----------------------------------------------|---------------|
| Cash and balances with banks | 50 | - | - | 50 |
| Placements with financial institutions | 2 | - | - | 2 |
| Financing assets | 4,762 | 3,695 | 13,566 | 22,023 |
| Assets acquired for leasing (including lease rentals receivables) | 106 | 139 | 2,211 | 2,456 |
| Investment in sukuk | 3 | - | 1,317 | 1,320 |
| Commitments and financial Guarantees | 176 | 84 | 120 | 380 |
| | 5,099 | 3,918 | 17,214 | 26,231 |

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 37,917 thousands (2018: BD 16,896 thousand) were renegotiated, out of which BD 1,096 thousand (2018: BD 8,806 thousand) are classified as neither past due nor impaired as of 31 December 2019. 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 166,033 thousand (2018: BD 142,895 thousand) only instalments of BD 36,625 thousand (2018: BD 39,269 thousand) are past due as at 31 December 2019.

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 Nil (2018: BD 1,566 thousand) which were fully impaired. The Group has recovered BD 964 thousand from a financing facility written off in previous years (2018: 99 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 2019 | | | As at 31 December 2018 | | |
|----------------------------------------------|------------------------|------------------------------------------------------------------|----------------|------------------------|------------------------------------------------------------------|----------------|
| | 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 | 20,181 | 32,464 | 52,645 | 40,471 | 16,587 | 57,058 |
| Other | 1,888 | - | 1,888 | 2,193 | - | 2,193 |
| <u>Against past due but not impaired</u> | | | | | | |
| Property | 35,420 | 23,949 | 59,369 | 21,397 | 19,232 | 40,629 |
| Other | 1,157 | - | 1,157 | 2,929 | - | 2,929 |
| <u>Against neither past due nor impaired</u> | | | | | | |
| Property | 96,730 | 89,681 | 186,411 | 87,637 | 82,680 | 170,317 |
| Other | 9,280 | - | 9,280 | 12,416 | - | 12,416 |
| Total | 164,656 | 146,094 | 310,750 | 167,043 | 118,499 | 285,542 |

The average collateral coverage ratio on secured facilities is 130.5% at 31 December 2019 (31 December 2018: 136.05%).

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 2019 | | | As at 31 December 2018 | | |
|------------------------------|------------------------|------------------------------------------------------------------|----------------|------------------------|------------------------------------------------------------------|----------------|
| | 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 | 7,857 | - | 7,857 | 10,358 | - | 10,358 |
| Real estate | 72,043 | 133,657 | 205,700 | 51,630 | 118,615 | 170,245 |
| Construction | 51,038 | - | 51,038 | 54,803 | - | 54,803 |
| Trading | 57,224 | - | 57,224 | 78,009 | - | 78,009 |
| Manufacturing | 13,955 | - | 13,955 | 13,880 | - | 13,880 |
| Others | 122,238 | 12,542 | 134,780 | 118,960 | 1,588 | 120,548 |
| Total carrying amount | 324,355 | 146,199 | 470,554 | 327,640 | 120,203 | 447,843 |

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 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.

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.

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35. *FINANCIAL RISK MANAGEMENT (continued)*

LIQUIDITY RISK (continued)

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 medium-term borrowing 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:

| | 2019 % | 2018 % |
|------------------------|------------------|-----------|
| At 31 December | 33.70 | 16.79 |
| Average for the period | 29.11 | 13.09 |
| Maximum for the period | 33.70 | 19.55 |
| Minimum for the period | 22.32 | 6.60 |

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.

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. Effective from 30 June 2019, the Bank is required to maintain LCR greater than 100%. As of 31 December 2019 the Bank had LCR ratio of 733.93%.

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". Effective from 31 December 2019, the Bank is required to maintain NSFR ratio greater than 100%. As of 31 December 2019 the Bank had NSFR ratio of 108.5%.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
for the year ended 31 December 2019

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

Management of market risks

The Group separates its exposure to market risk between trading and non-trading portfolios. The Group has no trading positions in equity or commodities and the main source of market risk for the Group is its foreign exchange exposure and profit rate gap.

The Group does not do any trading in foreign exchange. The Group does not engage in proprietary trading of foreign exchange derivatives. All foreign exchange income/ losses arising out of customer transactions and revaluation of statement of financial position assets and liabilities are booked by the treasury operations. The responsibility for monitoring and managing the related risks also rests with the Treasury department.

Overall authority for market risk management is vested with ALCO. The RMD is responsible for the development of detailed risk management policies (subject to review and approval by appropriate approval authorities) and the Financial Control Department is responsible for the day-to-day review of their implementation.

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.

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

MARKET RISK (continued)

A summary of the Group's profit rate gap position at 31 December 2019 is as follows:

| 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 |
| Investments securities (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 | 3,774 | - | 15,637 | 108,042 | - | 127,453 |
| Medium-term borrowing | - | - | - | - | - | - |
| 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 | 262,961 | 104,746 | 99,735 | 44,393 | - | 511,835 |
| 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) |

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35. *FINANCIAL RISK MANAGEMENT (continued)*

MARKET RISK (continued)

| 31 December 2018 | Up to 3 months | 3 - 6 months | 6 months - 1 year | 1 - 3 years | More than 3 years | Total |
|-------------------------------------------------------------------|----------------|--------------|-------------------|-------------|-------------------|----------|
| Assets | | | | | | |
| Placements with financial institutions | 42,590 | - | 1,047 | - | - | 43,637 |
| Financing assets | 40,881 | 9,345 | 36,588 | 66,003 | 174,823 | 327,640 |
| Assets acquired for leasing (including lease rentals receivables) | 15 | 7 | 230 | 7,528 | 112,423 | 120,203 |
| Investments securities (sukuk) | - | - | - | 16,227 | 145,097 | 161,324 |
| Total profit rate sensitive assets | 83,486 | 9,352 | 37,865 | 89,758 | 432,343 | 652,804 |
| Liabilities and investment accounts | | | | | | |
| Placements from financial institutions | 31,312 | 17,664 | 109,373 | - | - | 158,349 |
| Medium-term borrowing | - | - | 41,357 | - | - | 41,357 |
| Placements from non-financial institutions and individuals | 37,180 | 21,163 | 27,722 | 34,405 | - | 120,470 |
| Customers' current accounts | 1,199 | - | - | - | - | 1,199 |
| Equity of investments account holders | 154,133 | 73,102 | 98,830 | 20,308 | - | 346,373 |
| Total profit rate sensitive liabilities and investment accounts | 223,824 | 111,929 | 277,282 | 54,713 | - | 667,748 |
| Profit rate gap | (140,338) | (102,577) | (239,417) | 35,045 | 432,343 | (14,944) |

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:

At 31 December 2019

At 31 December 2018

| 100bp parallel increase/decrease | 50bp increase/decrease |
|----------------------------------|------------------------|
| ± 433 | ± 216 |
| ± 149 | ± 67 |

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.

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35. *FINANCIAL RISK MANAGEMENT (continued)*

MARKET RISK (continued)

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 2019, 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.

| | 2019 BHD Equivalent | 2018 BHD Equivalent |
|------------------------|------------------------------------|------------------------------------|
| US Dollars* | 145,868 | 28,905 |
| Other GCC Currencies * | (63,732) | 20,226 |
| Euros | (280) | (402) |
| Australian Dollars | 4,608 | 4,627 |
| Kuwaiti Dinars | 3,322 | 3,379 |
| Sterling Pounds | 1,443 | (579) |
| Indian Rupee | 30 | 38 |

(*) 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.

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:

| | 2019 BHD Equivalent | 2018 BHD Equivalent |
|--------------------|------------------------------------|------------------------------------|
| Euros | ±14 | ±20 |
| Australian Dollars | ±230 | ±231 |
| Kuwaiti Dinars | ±166 | ±169 |
| Sterling Pounds | ±72 | ±29 |
| Indian Rupees | ±2 | ±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.

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35. *FINANCIAL RISK MANAGEMENT (continued)*

MARKET RISK (continued)

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.

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 held by third parties which meet the criteria of AT1, and regulatory adjustments applied in calculation of AT1.

- *Tier 2 capital, 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.*

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35. *FINANCIAL RISK MANAGEMENT (continued)*

CAPITAL MANAGEMENT (continued)

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 2019, the Group has made regulatory adjustments of BD 14,356 thousand (2018: 13,725 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.

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

| | 31 December 2019 | 31 December 2018 |
|-----------------------------------------------------------------------------------------|-----------------------------|---------------------|
| Total risk weighted exposure | 532,793 | 653,067 |
| Tier 1 capital: | | |
| - CET 1 capital prior to regulatory adjustments | 97,215 | 112,401 |
| - Less: regulatory adjustments | (14,356) | (13,725) |
| CET 1 after regulatory adjustments | 82,859 | 98,676 |
| AT 1 | - | - |
| Tier 2 capital: | 5,726 | 7,286 |
| Total regulatory capital | 88,585 | 105,962 |
| Total regulatory capital expressed as a percentage of total risk weighted assets | 16.63% | 16.23% |
| Liquidity coverage ratio | 733.93% | 395.03% |
| Net stable funding ratio | 108.5% | 88.31% |
| Leverage ratio | 5.40 | 4.77 |

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

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35. RISK MANAGEMENT (continued)

CAPITAL MANAGEMENT (continued)

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

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

| | 2019 | 2018 |
|-----------------------------------------|---------------|---------------|
| Undrawn commitments to extend finance * | 68,876 | 33,193 |
| Financial guarantees | 11,836 | 12,864 |
| | 80,712 | 46,057 |

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

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 2019 due to the performance of any of its projects.

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.