**BANK ALKHAIR B.S.C. (c)**

**CONSOLIDATED FINANCIAL STATEMENTS**

**31 December 2016**

| | |
|---|---|
| Commercial registration: | 53462 (registered with Central Bank of Bahrain as a wholesale Islamic bank). |
| Registered Office: | 26th Floor, West Tower, Bahrain Financial Harbour<br>Building No. 1459, Road 4626, Manama, Sea Front 346<br>PO Box 31700, Manama, Kingdom of Bahrain |
| Directors: | Yousef Abdullah AlShelash, *Chairman*<br>Majed Abdulrahman Al Qasem, Vice Chairman<br>Abdulrazaq Mohamed Al Wohaib<br>Abdulaziz Naif Al Orayer<br>Abdullatif Abdullah AlShalash<br>Ahmed Saleh Dehailan<br>Khaled Shaheen Saqer Shaheen<br>Abdullah Ali Al Dubaikhi<br>Meshari Al Mulla |
| Group Chief Executive Officer: | Ayman Sejiny |
| Auditors: | KPMG Fakhro |

## Chairman's Message

**In the name of Allah, the Beneficent, the Merciful, Prayers and Peace upon the Last Apostle and Messenger, Our Prophet Mohammed, His Companions and Relatives.**

On behalf of the Board of Directors, it is my privilege to present the annual report and consolidated financial statements of Bank Alkhair for the year ended 31st December 2016 being our twelfth year of operation.

I am gratified to report a positive and productive year for Bank Alkhair across our offices in Bahrain, KSA, UAE, Turkey and Malaysia, due in no small measure to the sound business and banking practices that were primarily achieved through optimising financial efficiencies, minimising exposure to risk and reducing costs by a substantial 16%.

While the financial climate remained challenging for financial institutions with low oil prices and liquidity remaining under pressure, Bank Alkhair's investments performed encouragingly. Last year's focus providing Islamic capital market advisory services continued to prove a wise path with debt capital markets being the trend in the region.

For the Bank's investments, it was an active year for Bahrain Financing Company as it approaches its 100-year anniversary in 2017. In the UK, BFC Bank was granted its banking licence by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). Successfully obtained after a rigorous 3-year process, this licence enables BFC Bank to operate as a low-cost operator for corporate banking products for SMEs and focus on becoming the bank of choice for payment service providers who wish to make payments through UK payment gateways. BFC also expanded closer to home with its 46th branch opening at Harbour Gate within Bahrain Financial Harbour.

During 2016, Bank Alkhair achieved approval from the Central Bank of Pakistan to successfully exit Burj Bank after many years of investment; this was in order to align with the Bank's strategic direction moving forward. Our investment in Open-Silicon, a semiconductor solutions company and a market leader in chip design and outsourced manufacturing services continued with positive progress through building solid partnerships with industry leaders and was voted one of the 20 most promising semiconductor companies in 2016.

Over the year we realised value in our investments across a number of areas. Our focus was to enhance our investee companies and I am delighted to report that this was achieved through several business lines.

Given we are a 2006-2008 vintage private equity house, our aim remains focused on realising value through growing and exiting investments at the most opportune time, while realising optimum returns for shareholders. Beyond PE, value was also realised through the successful sale of land owned by the Bank in the Seef district.

The Group continued its efforts to curtail the cost and succeeded to reduce total cost by 16% for the year 2016. The major contributor to the cost savings was Bahrain office for which total expenses witnessed a sharp decline of USD 7 million for the year i.e., 38% as compared to previous year. Despite our successful efforts on the cost side, the Group declared a net loss of USD 33 million for the year mainly due to some impairments and reclassification of reserves from equity to income statement on disposal of an equity-accounted investee.

Throughout the year we have protected our investors' interests and ensured a stable company. We have achieved this through enhancing corporate governance, implementing prudent risk management functions and corporate culture and advocating regular board training globally to ensure responsibilities are effectively performed. These actions are driven by our values of integrity, professionalism and innovation and such proactive internal actions have delivered meaningful value for our investors externally.

To qualify the reasons for our progress throughout 2016, our resilience and steadfast growth has been achieved through taking a judicious course in not being overexposed in single markets, adopting a conservative approach, conducting internal restructuring, always meeting our financial commitments on time, exploring strategically aligned partnerships and having a strong shareholder base that provides loyal support and from which we grow organically.

Structurally, we reduced the number of directors on our board from 15 to 9 and on our Shari'ah board from 6 to 3. We offer our sincere appreciation to all of the outgoing members for their guidance and invaluable contributions in helping make the bank stronger throughout their tenures. We would also like to welcome Mr Meshari Abdullah Al Mulla who joined the board in 2016 and who already has established a distinguished career in finance. Furthermore, our relocation to Bahrain Financial Harbour, Bahrain's most prestigious business address, helped enhance our business and brand's reputation.

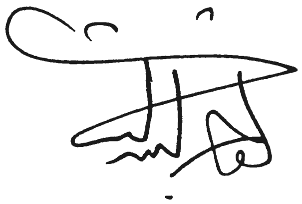
Looking forward, it seems the near future for the region is in a state of flux. On the macro-finance front, I envision 2017 to remain challenging while oil prices are low, though modest growth may occur and I also expect some consolidation in the marketplace. For us, the focus will be on strengthening our balance sheet and our liquidity position to enable us to become the premier Islamic investment Bank. For the Kingdom, I am heartened given Islamic Finance seems in good health with Bahrain placed second for global indicator value in the ICD Thomson Reuters Islamic Finance Development Indicator, which is designed to represent the overall health and development of the Islamic finance industry worldwide. Indeed, the Bank's own contributions to Islamic Finance were upheld during the year through our Group CEO's notable contributions as a panellist at the AAOIFI and World Islamic Banking conferences in KSA and Bahrain.

I would like to draw our valued shareholders' attention to the disclosures made in the FS (note 21) with regard to the details of the related party transactions for year 2016 and previous years balances and results, which includes the Board of Directors and Shari'ah Supervisory Board attendance fees/and remunerations expenses for year 2016.

Bank Alkhair wishes to extend its appreciation to the governments of the countries in which our associates and subsidiaries operate for the privilege of conducting our business. We also proffer our appreciation to the Government of Bahrain for its resolute support of the financial services industry and in particular the evolution of Islamic finance, and to the Central Bank of Bahrain for its prudent regulation, innovative approach and valuable progression of the industry.

To conclude, in a year of challenges I am satisfied that our actions enabled the Bank to head into 2017 with genuine impetus. On behalf of the Bank's Board of Directors and Executive Management Team, I would like to offer our sincere appreciation to our family of valued Shareholders for their invaluable support and confidence, our exceptional Shari'ah Supervisory Board for its foresight and valuable assistance in our investment decisions. And lastly, I pay a very warm tribute to the dedication, commitment and positive attitude of our management and employees globally for their considerable contribution to the forward momentum gained by Bank Alkhair in helping transform a year of challenges into a year of progress.

May Allah guide us on the proper path, and lead us to the fulfillment of our goals for the future success of the Bank.



**Yousef Abdullah Al-Shelash**
Chairman of the Board

23 March 2017

# SHARI'AH SUPERVISORY BOARD REPORT TO THE SHAREHOLDERS OF BANK ALKHAIR B.S.C. (c)

**Asslamo A'laikom WA Rahmatu Allah WA Barakatuh**

In compliance with the terms of our letter of appointment, we are required to report as follows:

The Shari'ah Board, through the Shari'ah department, and under its direct supervision, reviewed the principles and the contracts relating to the transactions conducted by Bank Alkhair B.S.C. (c) ("the Bank") and its subsidiaries (together "the Group") during the year ended 31 December 2016. The review was conducted in order to form an opinion as to whether the Group has complied with rules and principles of Islamic Shari'ah and also with the specific fatwa's, rulings and guidelines issued by us.

Based on the Articles of Association of the Bank, the Group's management is responsible for ensuring that the Group conducts its business in accordance with the rules and principles of Shari'ah while the Shari'ah Board's responsibility is to form an independent opinion, based on our review of the operations of the Group, and to report this to you.

We conducted our review through the Shari'ah department and under our supervision which included examining, on a test basis, each type of transaction and the relevant documentation and procedures adopted by the Group. We performed our review so as to obtain all the information and explanations that we considered necessary in order to provide us with sufficient evidence to give assurance that the Group has not violated any rules and principles of Shari'ah.

In our opinion:

a) The contracts, transactions and dealings entered into by the Group during the year ended 31 December 2016 are in compliance with the rules and principles of Shari'ah.
b) The Shari'ah Board emphasis that non-Shari'ah compliance issues related to the investment in Taj Mall project, Open Silicon and Logistics Warehousing which were not submitted to the Shari'ah Board for approval before its execution, and appear later to be having explicitly non-Shari'ah Compliance issues and not being corrected yet although a various Shari'ah Board resolution issued requesting solving the same.
c) The Shari'ah Board resolved that all earnings that have been realized from sources or by means prohibited by rules and principles of Shari'ah shall be disposed off and given to charity under the supervision of the Shari'ah Board. The Shari'ah Board noticed the accumulation of US$ 564,786 non-Shari'ah Compliance income only US$ 24,668 being donated, the management is request to distribute the same in annual basis under Shari'ah Board supervision.
d) The allocation of profit and charging of losses relating to investment accounts conform to the basis that had been approved by us in accordance with Shari'ah rules and principles.

e) The calculation of Zakah is in compliance with the rules and principles of Islamic Shari'ah.

We supplicate to Allah the Almighty to grant us success and a straight path.
Wa Asslamo A'laikom Wa Rahmatu Allah Wa Barakatuh.

Dr. Ali M. Al Qaradaghi

Sh. Dr. Nizam M. Yacoubi

Dr. Mohamed Daud Bakar

*1 Jamadah II 1438 H - 28 February 2017*

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CR No. 6220

**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS**

Bank Alkhair BSC (c)
Manama, Kingdom of Bahrain

**Report on the consolidated financial statements**

We have audited the accompanying consolidated financial statements of Bank Al Khair BSC (c) (the "Bank") and its subsidiaries (together the "Group") which comprise the consolidated statement of financial position as at 31 December 2016, the consolidated statements of income, changes in equity and cash flows 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.

*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 2016, and of its consolidated results of operations, its consolidated cash flows and its consolidated changes in equity for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions.

*Emphasis of matter*

Without qualifying our opinion, we draw our attention to note 2 ( b) to the consolidated financial statements which discusses certain matters relating to the Group's accumulated losses, liquidity position and regulatory capital adequacy ratio, implications of these matters for the basis of preparation of these consolidated financial statements and management's action plans to deal with these matters.

**Report on other regulatory requirements**

As required by the Bahrain 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) as disclosed in note 33, the Bank's capital adequacy ratio as of 31 December 2016 was below the minimum requirement. Except for this, we are not aware of any violations during the year of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6 and CBB directives) 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;
d) except for the matters discussed in the Shari'a Supervisory Board report dated 28 February 2017, we are not aware of any other breaches of the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank; and
e) satisfactory explanations and information have been provided to us by management in response to all our requests.

KPMG

KPMG Fakhro
Partner Registration No. 137
26 March 2017

**BANK ALKHAIR B.S.C ( C )**
**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**
**as at 31 December 2016** US$ 000's

| | note | **31 December 2016** | 31 December 2015 (Restated- note 34) |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with banks | 4 | 15,479 | 17,021 |
| Placements with financial institutions | | 8,402 | 9,648 |
| Financing receivables | 5 | 16,075 | 66,713 |
| Investment securities | 6 | 61,603 | 64,930 |
| Equity-accounted investees | 7 | 124,994 | 136,753 |
| Investment property | 8 | 224,448 | 241,466 |
| Other assets | 9 | 29,226 | 32,313 |
| Equipment | | 9,466 | 13,274 |
| **TOTAL ASSETS** | | **489,693** | 582,118 |
| | | | |
| **LIABILITIES AND EQUITY** | | | |
| | | | |
| **LIABILITIES** | | | |
| Due to financial institutions | 10 | 87,566 | 123,252 |
| Due to customers | 11 | 151,034 | 208,250 |
| Other liabilities | 12 | 53,017 | 28,727 |
| **TOTAL LIABILITIES** | | **291,617** | 360,229 |
| | | | |
| **EQUITY** | | | |
| Share capital | 13 | 207,962 | 207,962 |
| Statutory reserve | | 664 | 664 |
| Investments fair value reserve | | 151 | (249) |
| Foreign currency translation reserve | | (6,469) | (15,290) |
| Accumulated losses | | (98,478) | (61,383) |
| **Equity attributable to shareholders of the Bank** | | **103,830** | 131,704 |
| | | | |
| Non-controlling interests | | 94,246 | 90,185 |
| **TOTAL EQUITY** (page 4) | | **198,076** | 221,889 |
| **TOTAL LIABILITIES AND EQUITY** | | **489,693** | 582,118 |

The Board of Directors approved the consolidated financial statements consisting of pages 5 to 44 on 23 March 2017 and signed on it's behalf by:

Yousef Abdullah Al-Shelash
*Chairman*

Majid Al Qasem
*Vice Chairman*

The notes 1 to 34 form an integral part of these consolidated financial statements.

**BANK ALKHAIR B.S.C ( C )**
**CONSOLIDATED INCOME STATEMENT**
**for the year ended 31 December 2016**

US$ 000's

| | note | 2016 | 2015 |
|---|---|---|---|
| Finance income | | 2,194 | 4,321 |
| Income from investment securities, net | 14 | (6,065) | (3,371) |
| Fees and commission | 15 | 9,323 | 5,383 |
| Share of (loss)/profit of equity-accounted investees, net | 7 | (328) | 5,253 |
| Income from non-banking operations | 16 | 31,020 | 32,389 |
| Rental income | | 2,422 | 3,361 |
| (Loss)/gain on sale of investment property | 8 | (2,239) | 721 |
| Net loss on disposal of an equity-accounted investee | 7 | (7,088) | - |
| Foreign exchange loss, net | | (904) | (148) |
| Other income | | 1,917 | 2,088 |
| **Total income** | | **30,252** | 49,997 |
| Staff cost | | 13,533 | 14,112 |
| Finance expense | | 11,552 | 10,967 |
| Legal and professional expenses | | 2,163 | 7,150 |
| Premises cost | | 1,044 | 1,205 |
| Business development expenses | | 406 | 510 |
| Depreciation | | 1,841 | 2,919 |
| Expenses of non-banking operations | 16 | 21,926 | 23,823 |
| Other operating expense | | 4,392 | 4,285 |
| **Total expenses** | | **56,857** | 64,971 |
| **Loss for the year before impairment allowance** | | **(26,605)** | (14,974) |
| Impairment allowances | 17 | (6,429) | 12,474 |
| **Loss for the year** | | **(33,034)** | (2,500) |
| Attributable to: | | | |
| Shareholders of the Bank | | (37,095) | (5,999) |
| Non-controlling interests | | 4,061 | 3,499 |
| | | **(33,034)** | (2,500) |

The notes 1 to 34 form an integral part of these consolidated financial statements.

**BANK ALKHAIR B.S.C ( C )**
**CONSOLIDATED STATEMENT OF CHANGES IN EQUITY**
**for the year ended 31 December 2016**

US$ 000's

| 2016 | Attributable to shareholders of the Bank | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Share capital** | **Statutory reserve** | **Investments fair value reserve** | **Foreign currency translation reserve** | **Accumulated losses** | **Total** | **Non-controlling interests** | **Total equity** |
| As at 1 January 2016 | 207,962 | 664 | (249) | (15,290) | (61,383) | 131,704 | 90,185 | 221,889 |
| (Loss) / profit for the year (page 3) | - | - | - | - | (37,095) | (37,095) | 4,061 | (33,034) |
| Foreign currency translation differences | - | - | - | (231) | - | (231) | - | (231) |
| Share of changes in reserves of equity-accounted investees | - | - | 278 | (214) | - | 64 | - | 64 |
| Derecognition/transfer to income statement on disposal of equity-accounted investee | | | 122 | 9,266 | - | 9,388 | - | 9,388 |
| **Total recognised income and expense for the year** | **-** | **-** | **400** | **8,821** | **(37,095)** | **(27,874)** | **4,061** | **(23,813)** |
| **As at 31 December 2016** | **207,962** | **664** | **151** | **(6,469)** | **(98,478)** | **103,830** | **94,246** | **198,076** |

| 2015 (Restated) | Attributable to shareholders of the Bank | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Share capital | Statutory reserve | Investments fair value reserve | Foreign currency translation reserve | Accumulated losses | Total | Non-controlling interests | Total equity |
| As at 1 January 2015 (Previously reported) | 207,962 | 664 | (185) | (13,333) | (52,479) | 142,629 | 86,744 | 229,373 |
| Prior year adjustments (note 34) | - | - | - | - | (2,905) | (2,905) | - | (2,905) |
| As at 1 January 2015 (restated) | 207,962 | 664 | (185) | (13,333) | (55,384) | 139,724 | 86,744 | 226,468 |
| (Loss) / profit for the year (page 3) | - | - | - | - | (5,999) | (5,999) | 3,499 | (2,500) |
| Foreign currency translation differences | - | - | | (333) | - | (333) | (58) | (391) |
| Share of changes in reserves of equity-accounted investees | - | - | (64) | (1,624) | - | (1,688) | - | (1,688) |
| Total recognised income and expense for the year | - | - | (64) | (1,957) | (5,999) | (8,020) | 3,441 | (4,579) |
| As at 31 December 2015 | 207,962 | 664 | (249) | (15,290) | (61,383) | 131,704 | 90,185 | 221,889 |

The notes 1 to 34 form an integral part of these consolidated financial statements.

**BANK ALKHAIR B.S.C ( C )**
**CONSOLIDATED STATEMENT OF CASH FLOWS**
**for the year ended 31 December 2016**

US$ 000's

| | 2016 | 2015 |
|---|---|---|
| Loss for the year | (33,034) | (2,500) |
| Adjustments for: | | |
| Loss/(gain) on sale of investment securities | 47 | (1,510) |
| Fair value changes in investment securities | 6,071 | 5,220 |
| Share of (profit)/loss of equity-accounted investees | 328 | (5,253) |
| Loss/(gain) on disposal of investment property | 2,239 | (721) |
| Loss on sale of equity-accounted investee | 7,088 | - |
| Depreciation and amortisation | 1,841 | 2,919 |
| Sukuk amortisation | (28) | 141 |
| Impairment allowance | 6,429 | (12,474) |
| | **(9,019)** | (14,178) |
| Changes in: | | |
| Financing receivables | 47,215 | (61,361) |
| Other assets | 2,684 | (18,100) |
| Due to financial institutions | (28,111) | 24,617 |
| Due to customers | (57,215) | 10,696 |
| Other liabilities | 24,290 | (4,170) |
| **Net cash used in operating activities** | **(20,156)** | (62,496) |
| **INVESTING ACTIVITIES** | | |
| Purchase of equipment, net | (344) | (157) |
| Proceeds from sale of investment securities | 44,871 | 86,342 |
| Purchase of investment securities | (47,927) | (69,794) |
| Proceeds from sale of investment property | 14,782 | 14,523 |
| Dividends received from equity-accounted investees | 2,168 | 2,168 |
| Proceeds from sale of equity-accounted investee | 11,811 | |
| **Net cash generated from investing activities** | **25,361** | 33,082 |
| **FINANCING ACTIVITIES** | | |
| Repayment of financing liabilities | (7,760) | (8,351) |
| **Net cash used in financing activities** | **(7,760)** | (8,351) |
| **Net decrease in cash and cash equivalents during the year** | **(2,555)** | (37,765) |
| Effect of exchange rate changes on cash and cash equivalents | (233) | (714) |
| Cash and cash equivalents at the beginning of the year | 26,669 | 65,148 |
| **CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR** | **23,881** | 26,669 |

| | 2016 | 2015 |
|---|---|---|
| Cash and cash equivalents comprise: | | |
| Cash and balances with banks | 15,479 | 17,021 |
| Placements with financial institutions (with maturities of 3 months or less) | 8,402 | 9,648 |
| | **23,881** | 26,669 |

US$ 000's

## 1 REPORTING ENTITY

Bank Alkhair B.S.C. (c) ("the Bank") was incorporated in the Kingdom of Bahrain and registered with the Ministry of Industry and Commerce under Commercial Registration No. 53462 on 29 April 2004 and operates under a wholesale Islamic banking license granted by the Central Bank of Bahrain (CBB). The Bank's registered office is at the 26th floor, West Tower Bahrain Financial Harbour, Building No. 1459, Road No. 4626, Manama Sea Front 346, Kingdom of Bahrain.

The Bank aim to provide a full range of investment banking products and services that are compliant with Shari'ah principles. The principal products and services offered by the Group are:

- financial advisory services;
- private equity, equity structuring, private placements and initial public offerings;
- facility structuring, restructuring and placement including project finance, securitisation and Sukuk;
- structuring and marketing of both open and closed end mutual funds as well as client portfolio management and brokerage services that aim to meet investor driven return and asset criteria;
- advisory and investment services for takaful (Islamic insurance) and retakaful (Islamic reinsurance) providers; and
- mergers and acquisitions, including deal sourcing, structuring, valuations and advisory.

*Consolidated financial statements*

The consolidated financial statements comprise the results of the Bank and its subsidiaries (the "Group").

The following are the principal subsidiaries of the Bank that are consolidated:

| Subsidiary | Ownership | | Year of incorporation/ Acquisition | Country of incorporation | Principal activity |
|---|---|---|---|---|---|
| | 2016 | 2015 | | | |
| Alkhair International Islamic Bank Malaysia Berhad | 100% | 100% | 2004 | Malaysia | Alkhair International Islamic Bank Malaysia Berhad was established in 2004 to source investment opportunities in the Far East and monitor the performance of the acquired companies on behalf of the Bank and investors and to establish distribution channels for the Group. In 2007, Alkhair International Islamic Bank Malaysia Berhad was granted an investment banking license by Bank Negara Malaysia to carry out investment banking activity in currencies other than the Malaysian Ringgit. |
| Alkhair Capital Menkul Degerler A.S. | 95.8% | 95.8% | 2007 | Turkey | The main activities of Alkhair Capital Menkul Degerler A.S. are to provide investment consultancy and asset management. |
| Alkhair Portföy Yönetimi A.Ş. | 98.9% | 98.6% | 2007 | Turkey | The main activities of Alkhair Portföy Yönetimi A.Ş. are to provide investment consultancy and asset management. |
| Al-Tajamouat for Touristic Projects Co Plc | 50.6% | 50.6% | 2013 | Jordan | Al-Tajamouat for Touristic Projects Co was incorporated in January 2004. Its principal activities are real estate property investment & development and ownership and operation of a shopping mall in Amman. |
| Tintoria International Limited | 52.1% | 52.1% | 2014 | UAE | General trading and investing in UAE and foreign companies. |
| Alkhair Capital Saudi Arabia | 53.3% | 53.3% | 2009 | Kingdom of Saudi Arabia | Alkhair Capital Saudi Arabia is registered with Capital Markets Authority. Its principal activities are Asset Management, Corporate Finance & Investment banking and Brokerage. |

The Bank has other special purpose entities (SPE's) holding companies and subsidiaries which are set up to supplement the activities of the Bank and its principal subsidiaries.

## 2 BASIS OF PREPARATION

### (a) Statement of compliance

The consolidated 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 and the CBB Rule Book, for matters that are not covered by FAS, the Group uses guidance from the relevant International Financial Reporting Standards ('IFRS').

### (b) Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention except for certain investment securities and investment property which are carried at fair value. The consolidated financial statements are presented in United States Dollars (US$), being the functional currency of the Group's operations. All financial information presented in US$ has been rounded to the nearest thousands, except when otherwise indicated.

*Going concern*

As at 31 December 2016, the current contractual liabilities of the Group exceeded its liquid assets. As a result, the ability of the Group to meet its obligations when due, depends on its ability to roll over short term liabilities and timely disposal of assets. Further, the Bank's capital adequacy ratio as of 31 December 2016 was below the minimum regulatory capital requirements. These factors indicate the existence of material uncertainties, which may cast doubt about the Group's ability to continue as a going concern. To address these, the management has taken a number of initiatives including discussions with creditors who have shown willingness in the past to roll over short term placements, putting together a robust assets sales plan and support from major shareholders who have also in the past provided support when it was needed. The Board of Directors has reviewed these initiatives and is satisfied with the appropriateness of the going concern assumption for preparation of the consolidated financial statements".

### (c) Basis of consolidation

#### (i) Subsidiaries

Subsidiaries are those enterprises (including special purpose entities) controlled by the Bank. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an entity 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.

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 all investees and exposure to variability of returns determines whether it acts as a principal or as an agent to determine whether there is linkage between power and return. When the decision maker is an agent, the link between power and return 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 also manages and administers assets held in trust and other investment vehicles on behalf of investors. The financial statements of these entities 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 20.

*Loss of control*

Upon the loss of control, the Group derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in the consolidated income statement. If the Group retains any interest in the previous subsidiary, then such interest is measured at fair value at the date that control is lost. Subsequently it is accounted for as an equity-accounted investee or in accordance with the Group's accounting policy for financial instruments depending on the level of influence retained.

*Non-controlling interests*

Interests in the equity of subsidiaries not attributable to the parent are reported in consolidated statement of financial position as non-controlling interests. Profits or losses attributable to non-controlling interests are reported in the consolidated income statement as income attributable to non-controlling interests. Losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance.

2 *BASIS OF PREPARATION (continued)*
*(c) Basis of consolidation (continued)*
*(i) Subsidiaries (continued)*

The Group treats transactions with non-controlling interests as transactions with equity owners of the Group. For purchases from non-controlling interests, the difference between any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

When the Group ceases to have control or significant influence, any retained interest in the entity is remeasured to its fair value, with the change in carrying amount recognised in the consolidated income statement. The fair value is the initial carrying amount for the purposes of subsequently accounting for the retained interest as an associate, joint venture or financial asset. In addition, any amounts previously recognised in equity in respect of that entity are accounted for as if the Group had directly disposed of the related assets or liabilities. This may mean that amounts previously recognised in other equity are reclassified to the consolidated income statement.

**(ii) Equity-accounted investees**

Associates are those entities in which the Group has significant influence, but not control or joint control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20% and 50% of the voting power of another entity.

On initial recognition of an associate, the Group makes an accounting policy choice as to whether the associate shall be equity accounted or designated as at fair value through income statement. The Group makes use of the exemption in FAS 24 – *Investment in Associates* for venture capital organisation and designates certain of its investment in associates, as 'investments carried at fair value through income statement'. These investments are managed, evaluated and reported on internally on a fair value basis (refer note 3 (b)).

If the equity accounting method is chosen for an associate, these are initially recognised at cost and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investees 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 investees arising from changes in the investee's equity.

When the Group's share of losses exceeds its interest in an equity-accounted investee, the Group's carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the equity-accounted investees.

Any excess of the cost of acquisition over the Group's share of the net fair value of the identifiable assets, liabilities and contingent liabilities of an equity-accounted investee at the date of acquisition is recognised as goodwill, and included within the carrying amount of the investment. When the excess is negative, a bargain purchase gain is recognised immediately in the consolidated income statement.

If the ownership interest in an equity-accounted investee is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in equity is reclassified to the consolidated income statement where appropriate.

**(iii) Transactions eliminated on consolidation and equity accounting**

Intra-group balances and transactions, and any unrealised gains or losses 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 investees 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.

The reporting period of the Group's subsidiaries and equity-accounted investees are identical and their accounting policies conform to those used by the Bank for like transactions and events in similar circumstances. The accounting policies of the subsidiaries and equity-accounted investees have been changed where necessary to ensure consistency with the policies adopted by the Group.

2 *BASIS OF PREPARATION (continued)*
*(c) Basis of consolidation (continued)*

**(d) Business combination**

Business combinations are accounted for using the acquisition method as at the acquisition date i.e. when control is transferred to the Group. The consideration transferred in the acquisition is generally measured at fair value, as are the identifiable net assets acquired. Any goodwill that arises is tested annually for impairment. Any gain on a bargain purchase is recognised in the consolidated income statement immediately. Transaction costs are expensed as incurred, except if they are related to the issue of debt or equity securities.

The consideration transferred does not include amounts related to the settlement of pre-existing relationships. Such amounts are generally recognised in consolidated income statement. Any contingent consideration payable is measured at fair value at the acquisition date. If the contingent consideration is classified as equity, then it is not remeasured and settlement is accounted for within equity. Otherwise, subsequent changes in the fair value of the contingent consideration are recognised in profit or loss.

If share-based payment awards (replacement awards) are required to be exchanged for awards held by the acquiree's employees (acquiree's awards) and relate to past services, then all or a portion of the amount of the acquirer's replacement awards is included in measuring the consideration transferred in the business combination. This determination is based on the market-based value of the replacement awards compared with the market-based value of the acquiree's awards and the extent to which the replacement awards relate to pre-combination service

## 3 SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently by Group entities to all periods presented in these consolidated financial statements except for change in subsequent measurement of investment property. The Group previously used to measure the investment property at cost. During the year 2015, the Group voluntarily changed the accounting policy for remeasurement of investment property to fair value from previous measure of cost basis. This has been carried out to represent a more relevant presentation of the financial position.

***New standards, amendments and interpretations effective from 1 January 2016***

The following new standards, amendments to standards and interpretations are effective for annual periods beginning on or after 1 January 2016 and are expected to be relevant to the Group.

FAS 27 - Investment Accounts

FAS 27 Investment accounts was issued in December 2014, replacing FAS 5 "Disclosures of Bases for Profit Allocation between Owner's Equity and Investment Account Holders" and FAS 6 "Equity of Investment Account Holders and their Equivalent". The adoption of this standard expanded the disclosures related to equity of Investment Account Holders. The standard has no significant impact on the consolidated financial statements of the Bank.

***New standards, amendments and interpretations issued but not yet effective for adoption***

There are no new standards, amendments to standards and interpretations that are effective for annual periods beginning on or after 1 January 2017.

**a) 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'). The consolidated financial statements are presented in US$, which is the Bank's functional and presentation 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 consolidated 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.

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*
*a) Foreign currency transactions (continued)*

Other group companies
As at the reporting date, the assets and liabilities of subsidiaries, equity-accounted investees and joint venture are translated into the Bank's functional currency at the rate of exchange prevailing at the reporting date, and their statements of income are translated at the average exchange rates for the year. Exchange differences arising on translation are taken directly to a separate reserve in equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the consolidated income statement.

**b) Investment securities**

Investment securities comprise debt and equity instruments, but exclude investment in subsidiaries and equity-accounted investees (refer note 2 (c ii)).

**(i) *Classification***
The Group segregates its investment securities into debt-type instruments and equity-type instruments.

**Debt-type instruments**
Debt-type instruments are investments that provide fixed or determinable payments of profits and capital. Investments in debt-type instruments are classified in the following categories:

At fair value through income statement (FVTIS)
These investments are either not managed on contractual yield basis or designated on initial recognition at FVTIS to avoid any accounting mismatch that would arise on measuring the assets or liabilities or recognising the gains or losses on them on different bases. Currently, the Group does not have any investment under this category.

At amortised cost
This classification is for debt-type instruments which are not designated as FVTIS and are managed on contractual yield basis. These include investments in medium to long-term sukuk.

**Equity-type instruments**
Equity-type instruments are investments that do not exhibit features of debt-type instruments and include instruments that evidence a residual interest in the assets of an entity after deducting all its liabilities. Investments in equity type instruments are classified in the following categories:

At fair value through income statement (FVTIS)
Equity-type instruments classified and measured at FVTIS include investments held-for-trading and those designated on initial recognition at FVTIS.

Investments are classified as held-for-trading if acquired or originated principally for the purpose of generating a profit from short-term fluctuations in price or dealers margin or that form part of a portfolio where there is an actual pattern of short-term profit taking. The Group currently does not have any of its investments classified as investments held-for-trading purposes.

On initial recognition, an equity-type instrument is designated as FVTIS only if the investment is managed and its performance is evaluated and reported on internally by the management on a fair value basis. This category currently includes investment in private equity, funds and investment in associates (refer note 2 (c) (ii)).

At fair value through equity (FVTE)
Equity-type instruments other than those designated at FVTIS are classified as at fair value through equity. This category includes investment in unquoted equity securities.

***(ii) Recognition and de-recognition***
Investment securities are recognised at the trade date i.e. the date that the Group contracts to purchase 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.

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*
*b) Investment securities (continued)*

***(iii) Measurement***

Investment securities are measured initially at fair value, which is the value of the consideration given. For investments carried at FVTIS, transaction costs are expensed in the consolidated 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 consolidated 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.

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 consolidated income statement.

Investments carried at FVTE where the entity is unable to determine a reliable measure of fair value on a continuing basis, such as investments that do not have a quoted market price or where there are no other appropriate methods from which to derive reliable fair values, are stated at cost less impairment allowances.

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

***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 for impairment. The calculation of the effective profit rate includes all fees and profits paid or received that are an integral part of the effective profit rate.

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

The Group measures the fair value of quoted investments using the market bid-prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If a market for a financial instrument is not active or the instrument is not quoted, the Group establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), discounted cash flow analysis and other valuation models with accepted economic methodologies for pricing financial instruments.

**c) Financing receivables**

Financing receivables comprise Shari'ah compliant financing contracts with fixed or determinable payments. These include financing provided through Murabaha contracts. Financing assets are recognised on the date they are originated and are carried at their amortised cost.

**d) Placements with financial institutions**

These comprise inter-bank placements mainly made using Shari'ah compliant contracts. Placements are usually for short-term and are stated at their amortised cost.

**e) Due to financial institutions**

These comprise funds from financial institutions received on Shari'ah compliant contracts. Due to financial institutions are stated at their amortised cost.

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*

**f) Bank financing**

Bank financing represents facilities from financial institutions that are initially measured at fair value plus transaction costs, and subsequently measured at their amortised cost using the effective profit rate method. Financing costs, dividends and losses relating to bank financing are recognised in the consolidated income statement as finance expense. The Group derecognises a financing liability when its contractual obligations are discharged, cancelled or expire.

**g) Due to customers**

These comprise funds payable to corporate customers received using Shari'ah compliant contracts. Due to customers are stated at their amortised cost.

**h) Impairment of assets**

The Group assesses at each reporting date whether there is objective evidence that a specific financial asset or a group of financial assets may be impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (an incurred "loss event") and that the loss event(s) have an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

*Financial assets carried at amortised cost*

For financial assets carried at amortised cost impairment is measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the assets' original effective profit rate. Losses are recognised in consolidated income statement and reflected in an allowance account. When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the consolidated income statement. The Group considers evidence of impairment for financial assets carried at amortised cost at both a specific asset and collective level. All individually significant financial assets are assessed for specific impairment. All individually significant financial assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Financial assets that are not individually significant are collectively assessed for impairment by grouping together assets with similar risk characteristics.

Investments carried at fair value through equity (FVTE)

In the case of investments in equity securities classified as FVTE, a significant or prolonged decline in the fair value of the security below its cost is an objective evidence of impairment. If any such evidence exists for FVTE investments, the unrealised re-measurement loss shall be transferred from equity to the consolidated income statement.

The cumulative loss measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the consolidated statement of changes in equity is removed from equity and recognised in the consolidated income statement. Impairment losses recognised in the consolidated income statement on equity instruments are subsequently reversed through equity.

For FVTE investments carried at cost less impairment due to the absence of reliable 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 assessed to be below the cost of the investment. Currently, the Group does not have any investments under this category.

Non-financial assets

The carrying amount of the Group's assets or its cash generating unit, other than financial assets carried at amortised cost and investments carried at FVTE, are reviewed at each reporting date to determine whether there is any indication of impairment. A cash generating unit is the smallest identifiable asset group that generates cash flows that largely are independent from other asset and groups. If any such indication exists, the asset's recoverable amount is estimated. The recoverable amount of an asset or a cash generating unit is the greater of its value in use or fair value less costs to sell.

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*
*h) Impairment of assets (continued)*

In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of expected return 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 consolidated 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.

**i) Investment property**

Investment property comprises of land and building. Investment property is an investment that earns rental income and/or is expected to benefit from capital appreciation or land held for undetermined future use. Investment property is measured initially at cost, including directly attributable expenditures. Subsequently, investment property is carried at fair value.

Any unrealized gains arising from a change in the fair value of investment property is recognized directly in equity under "Investment Property Fair Value Reserve" for the period in which it arises. Any unrealized losses resulting from re-measurement at fair value of investment property is adjusted in equity against the investment property fair value reserve to the extent of the available credit balance of this reserve. In case such losses exceed the available balance, the unrealised losses are recognised in the consolidated income statement. In case there are unrealised losses relating to investment property that have been recognised in the consolidated income statement in a previous financial period, the unrealised gains relating to the current financial period are recognised to the extent of crediting back such previous losses in the consolidated income statement.

Investment property is derecognised when it has been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. The realised profits or losses resulting from the sale of investment property are measured as the difference between the carrying value and the net cash or cash equivalent proceeds from the sale of each investment separately. The resulting profit or loss together with the available balance on the investment property fair value reserve account is recognised in the consolidated income statement for the current financial period.

**j) Equipment**

Equipment includes computers, office equipment, fixtures and fittings. Equipment is recorded at cost less accumulated depreciation. Depreciation is computed using the straight-line method to write-off the cost of the assets over their estimated useful lives ranging from 1 to 8 years. The assets residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

**k) Revenue recognition**

Revenue is recognised when it is probable that future economic benefits will flow to the Group and the amount of the revenue can be reliably measured. Revenue earned by the Group and gain / loss on assets are recognised on the following basis:

**Dividend income**

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

**Gain / (loss) on sale of investment securities (realised gain / (loss)**

Gain / (loss) on sale of investment securities (realised gain / (loss)) is recognised on trade date at the time of derecognition of the investment securities. The gain or loss is the difference between the carrying value on the trade date and the consideration received or receivable.

**Fair value gain / (loss) on investment securities (unrealised gain or loss**

Fair value gain / (loss) on investment securities (unrealised gain or loss) is recognised on each measurement date in accordance with the accounting policy for equity-type instruments carried at fair value through income statement (refer note 3 b).

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*
*k) Revenue recognition (continued)*

**Sukuk Income**
Sukuk Income comprises the coupon profit on Sukuk and realised gain or loss on the sale of Sukuk. The coupon profit is recognised through the effective profit rate in accordance with the accounting policy for debt-type instrument carried at amortised costs (refer to 3 b). Realised gain or loss on sale of Sukuk is recognised on trade date at the time of de-recognition of the Sukuk. The gain or loss is the difference between the carrying value on the trade date and the fair value of consideration received or receivable.

**Fees and Commission income**
Fees and Commission income represents advisory fees, arrangement fees, management fees and brokerage fees. Fees and Commission income is recognised at the fair value of consideration received or receivable and when the service is provided and income is earned. This is usually when the Group has performed all significant acts in relation to a transaction and it is highly probable that the economic benefits from the transaction will flow to the Group. Significant acts in relation to a transaction are determined based on the terms for each transaction.

**Finance income and expense**
Finance income and expense is recognised using effective profit rate.

**Income from non-banking operations**
This consists of income from Al-Tajamouat for Touristic Projects Company PLC (lease income) and Tintoria International Limited (income from contracts for laundry operations).

**Lease income**
Lease income is recognised on straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease.

**Revenue from a contract to provide services**
Revenue from a contract to provide services is recognised by reference to the stage of completion of the contract, when the outcome of the transaction and related revenue and cost can be measured reliably, and that economic benefit flows to the Group.

**l) 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 and recognised as staff cost in the consolidated income statement. 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 local 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 staff cost in the consolidated income statement when they are due. Termination benefits are recognised as an expense when the Group is committed demonstrably, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy.

Certain employees on fixed contracts are also entitled to leaving indemnities payable, 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 as staff cost in the consolidated income statement.

**m) Earnings prohibited by Shari'ah**
The Bank 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 Bank uses these funds for charitable purposes.

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*

**n) Zakah**

The Bank is not obliged to pay Zakah on behalf of its shareholders. However, the Bank is required to calculate and notify individual shareholders of their pro-rata share of the Zakah payable amount.

**o) Provision for taxation**

There is no tax on corporate income in the Kingdom of Bahrain. Taxation on foreign operations is provided in accordance with the fiscal regulations of the respective countries in which the subsidiaries operate.

**p) Offsetting of financial instruments**

Financial instruments comprise of financial assets and financial liabilities. Financial assets include cash and balances with banks, placements with financial institutions, financing receivables, investment securities and other assets. Financial liabilities include due to financial institutions, due to customers, other liabilities and financial guarantees.

Financial assets and financial liabilities are only offset and the net amounts reported in the consolidated statement of financial position when there is a legally enforceable right to set off the recognised amounts and the Group intends to either settle these on a net basis, or intends to realise the asset and settle the liability simultaneously.

**q) Statutory reserve**

The Bahrain Commercial Companies Law 2001 requires that 10 percent 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 percent of the paid up share capital.

**r) Provisions**

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. A provision for restructuring is recognised when the Group has approved a detailed and formal restructuring plan, and the restructuring either has commenced or has been announced publicly. Future operating losses are not provided for.

**s) Contingent liabilities and contingent assets**

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

**t) 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. Loan commitments are firm commitments to provide credit under pre-specified terms and commitments. Financial guarantee liabilities are recognised initially at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The financial guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment when a payment under the guarantee has become probable.

**u) Leases**

Payments under operating lease are recognised in the consolidated income statement on a straight line basis over the term of the lease. Lease incentives are recognised as an integral part of the total lease expense, over the term of the lease.

**v) Onerous contracts**

A provision for onerous contracts is recognised when the expected benefits to be derived by the Group from the contract are lower than the unavoidable cost of meeting its obligations under the contract. The provision is measured at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing with the contract.

**w) Trade date accounting**

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

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*

**x) Cash and cash equivalents**

For the purpose of consolidated statement of cash flows, cash and cash equivalents comprise cash in hand, bank balances and placements with financial institutions with maturities of three months or less from the acquisition date that are subject to insignificant risk of changes in fair value and are used by the Group in the management of its short-term commitments.

**y) Critical accounting estimates and judgements**

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.

**Judgements**

**(i) *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 investments at fair value through income statement or investments carried at fair value through equity or investments carried at amortised cost. The classification of each investment reflects the management's judgement in relation to its strategy for each investment and is subject to different accounting treatments based on such classification (refer note 3 (b)).

**(ii) *Special purpose entities***

The Group sponsors the formation of special purpose entities (SPE's) primarily for the purpose of allowing clients to hold investments. The Group provides corporate administration, investment management and advisory services to these SPE's, which involve the Group making decisions on behalf of such entities. The Group administers and manages these entities on behalf of its clients, who are by and large third parties and are the economic beneficiaries of the underlying investments. The Group does not consolidate SPE's that it does not have the power to control.

In determining whether the Group has the power to control an SPE, judgements are made about the objectives of the SPE's activities, its exposure to the risks and rewards, as well as about the Group intention and ability to make operational decisions for the SPE and whether the Group derives benefits from such decisions.

**Estimations**

**(i) *Fair value of financial instruments***

Where the fair values of financial assets and financial liabilities cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility for discount rates.

Fair value is determined for each investment individually in accordance with the valuation policies set out below:

- For investment that is traded in an active market, fair value is determined by reference to the quoted bid market price prevailing on the reporting date;
- For investment in unquoted equity securities, the Bank establishes fair value by using valuation techniques. Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available, reference to the current fair value of another instrument that is substantially the same and discounted cash flow analysis; and
- Investments in funds or similar investment entities are carried at the latest net asset valuation provided by the fund administrator.

The impact on fair value of financial instruments measured at fair value for changes in key assumptions is given in note 19.

3 *SIGNIFICANT ACCOUNTING POLICIES (continued)*
*y) Critical accounting estimates and judgements (continued)*

**(ii) *Impairment of financing receivables***

Each counterparty exposure is evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counterparty's financial situation and the net realisable value of any underlying assets/ collaterals. Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently evaluated by the Risk Management Department. All individually significant financing receivables are tested for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified.

Financing receivables that are not individually significant are collectively assessed for impairment by grouping together assets with similar risk characteristics.

In assessing collective impairment, the Group uses historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or lesser than suggested by historical trends.

An impairment loss in respect of a financing receivables measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective profit rate. Losses are recognised in profit or loss and reflected in an allowance account against financing receivable.

Profit on the impaired asset does not continue to be recognised. When an event occurring after the impairment was recognised causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through consolidated income statement.

***(iii) Impairment of cash generating units***

Cash generating units include the Group's investments in certain subsidiaries and equity-accounted investees and investment property that generate cash flows that are largely independent from other assets and activities of the Group. The basis of impairment assessment for such cash generating units is described in accounting policy 3 (g). For equity-accounted investees with indicators of impairment, the recoverable amounts have been determined based on higher of fair value less costs to sell or value in use.

Value in use for the equity-accounted investees was determined by discounting the future cash flows expected to be generated from continuing operations, comparison to similar instruments for which market observable prices exist and other valuation models.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length. Fair value less costs to sell of certain cash generating units is based on indicative offer prices received by the Group.

Key assumptions used in the calculation of value in use were the following: cash flows were projected based on 3-5 year business plans, after ensuring consistency with historical operating results and forecasted economic growth rates for mature companies. Terminal value was calculated by dicounting (to arrive at present value) the book vlaue at terminal year using the price to book value multiple.

Discount rates were based on a CAPM formula, with the risk-free rate obtained from the yield on 10-year bonds issued by the government in the relevant market and in the same currency as the cash flows, adjusted for a risk premium to reflect both the increased risk of investing in equities generally, as well as liquidity and control factors. The key assumptions described above may change as economic and market conditions change.

for the year ended 31 December 2016 US$ 000's

## 4 CASH AND BALANCES WITH BANKS

| | **31 December 2016** | 31 December 2015 |
|---|---|---|
| Cash on hand | 7 | 5 |
| Balances with banks | 15,472 | 17,016 |
| | **15,479** | 17,021 |

## 5 FINANCING RECEIVABLES

| | **31 December 2016** | 31 December 2015 |
|---|---|---|
| Gross murabaha receivables | 29,733 | 77,338 |
| Less: Deferred profits | (165) | (556) |
| **Net murabaha receivables** | **29,568** | 76,782 |
| Less: Specific impairment allowances | (12,679) | (9,269) |
| Less: Collective impairment allowances | (814) | (800) |
| | **16,075** | 66,713 |

Financing receivables comprise due from customers under murabaha financing contracts. The average profit on these balances during the year was 7.8% per annum (2015: 5.9% per annum).

## 6 INVESTMENT SECURITIES

| | **31 December 2016** | 31 December 2015 |
|---|---|---|
| **Equity type instruments** | | |
| At fair value through income statement: | | |
| - Quoted equity securities | - | 673 |
| - Unquoted equity securities | 15,840 | 21,593 |
| - Quoted funds | 14,105 | 7,855 |
| - Unquoted funds | 28,822 | 29,490 |
| **Total equity type instruments** | **58,767** | 59,611 |
| **Debt type instruments** | | |
| At amortised cost : | | |
| - Sukuk | 2,836 | 5,319 |
| | **61,603** | 64,930 |

The fair value of the sukuk at 31 December 2016 is US$ 2,809 thousands (2015: US$ 5,267 thousands).

**Movement on equity type investments carried at fair value through income statement as follows:**

| | At 01-Jan-16 | Additions during the year | Disposal during the year | Fair value changes/ exchange diff | **At 31-Dec-16** |
|---|---|---|---|---|---|
| Quoted equity securities | 673 | 14,239 | (14,912) | - | - |
| Unquoted equity securities | 21,593 | - | - | (5,754) | 15,839 |
| Quoted funds | 7,855 | 17,173 | (10,980) | 57 | 14,105 |
| Unquoted funds | 29,490 | - | - | (667) | 28,823 |
| | **59,611** | **31,412** | **(25,892)** | **(6,364)** | **58,767** |

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## 7 EQUITY-ACCOUNTED INVESTEES

| | 31 December 2016 | 31 December 2015 (Restated) |
|---|---|---|
| BFC Group Holdings Ltd. | 115,606 | 116,255 |
| Burj Bank Limited | - | 11,215 |
| t'azur Company B.S.C. (c) | 9,388 | 9,283 |
| | **124,994** | 136,753 |

(i) The Group has 43.36% stake (2015: 43.36%) in BFC Group Holdings Ltd. ("BFC"), a company incorporated in the United Arab Emirates. BFC is a holding company of a group of money changers in different jurisdictions. BFC is engaged in buying and selling foreign currencies and traveller's cheques, handling of remittance business and provision of other exchange house services in both local and foreign currencies.
A prior year adjustment was made in the books of BF during the year and the Bank has accounted for it's share amounting to USD 2.9 million and restated the comparative numbers accordingly.

During the period, Group received the regulatory approval for sale of it's stake in Burj Bank Limited for a consideration of US$ 11.8 million. Compared with the carrying value of US$ 9.5 million resulted in a profit of US$ 2.3 million. Howerver, the Group had foreign currency translation and investment fair value loss in reserves of US$ 9.3 million and US$ 0.1 million respectively relating to Burj Bank which were transferred to income statement on disposal. This resulted in a net loss from disposal of US$ 7.1 million presented in the consolidated income statement under "loss from sale of equity-accounted investee".

(iii) The Group has 25.86% stake (2015: 25.86%) in T'azur B.S.C. (c), an unlisted regional takaful company incorporated in the Kingdom of Bahrain. T'azur Company B.S.C (c) has a commitment to provide a Qard Hassan to the extent of the accumulated deficit in the participants' fund of US$ 35 million at 31 December 2016 (31 December 2015: US$ 33.3 million). The Group's share of the commitment is US$ 8.5 million (31 December 2015: US$ 8.6 million) (note 18).

The movement on equity-accounted investees is as follows:

| | 2016 | 2015 (Restated) |
|---|---|---|
| At 1 January | 136,753 | 119,069 |
| Net share of profits of equity-accounted investees | (328) | 5,253 |
| Share of reserves of equity-accounted investees | 248 | (1,501) |
| Disposal during the year | (9,511) | - |
| Reversal of impairment allowance/(charge) | - | 16,100 |
| Dividends received | (2,168) | (2,168) |
| **At 31 December** | **124,994** | 136,753 |

Summarised financial information of associates that have been equity accounted not adjusted for the percentage ownership held by the Group (based on most recent audited financial statements / most recent management accounts):

| | 2016 | 2015 |
|---|---|---|
| Assets | 453,197 | 700,904 |
| Liabilities | 193,904 | 397,223 |
| Revenue | 62,256 | 90,975 |
| Profit for the year | 2,856 | 11,458 |

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## 8 INVESTMENT PROPERTY

| | At 1 January 2016 | Acquisition/ (Disposal) | Additions | Fair value changes | **At 31 December 2016** |
|---|---|---|---|---|---|
| Land and building - Jordan | 185,239 | - | 688 | - | **185,927** |
| Land and building - Kingdom of Saudi Arabia | 38,521 | - | - | - | **38,521** |
| Land - Kingdom of Bahrain * | 17,706 | (17,706) | - | - | **-** |
| | **241,466** | **(17,706)** | **688** | **-** | **224,448** |

| | At 1 January 2015 | Addition/ (Disposal) | Additions | Fair value changes | At 31 December 2015 |
|---|---|---|---|---|---|
| Land and building - Jordan | 184,137 | - | 1,102 | - | 185,239 |
| Land and building - Kingdom of Saudi Arabia | 54,728 | (16,207) | - | - | 38,521 |
| Land - Kingdom of Bahrain | 17,706 | - | - | - | 17,706 |
| | 256,571 | (16,207) | 1,102 | - | 241,466 |

* During the second quarter, land was sold at a loss of US$ 2,239 thousand.

## 9 OTHER ASSETS

| | **31 December 2016** | 31 December 2015 |
|---|---|---|
| Prepayments and advances | 6,265 | 6,721 |
| Rental income receivable | 6,769 | 2,548 |
| Fees and expenses recoverable | 3,240 | 2,980 |
| Intangible assets | 11 | 19 |
| Others | 15,210 | 21,947 |
| | **31,495** | 34,215 |
| Less: Provision for impairment | (2,269) | (1,902) |
| | **29,226** | 32,313 |

## 10 DUE TO FINANCIAL INSTITUTIONS

| | **31 December 2016** | 31 December 2015 |
|---|---|---|
| Placements from financial institutions | 31,304 | 59,229 |
| Bank financing | 56,262 | 64,023 |
| | **87,566** | 123,252 |

The average profit rate on placements from financial institutions was 3.5% per annum (2015: 2.7% per annum).

Bank financing represents a syndicated loan through the Housing Bank for Trade and Finance in Jordan secured by mortgage over the Group's investment property. The profit rate of the syndicated loan equals the prime lending rate of the Jordanian Dinar, plus an annual margin of 1.0%. The bank financing is repayable in annual installment of US$ 7.76 million with the final payments of US$1.94 million in 2024.

## 11 DUE TO CUSTOMERS

This includes deposits from corporate customers on Wakala basis with maturities ranging from 1 month to 1 year (2015: 1 month to 1 year) and carries an average profit rate of 5% per annum (2015: 4.7% per annum).

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## 12 OTHER LIABILITIES

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Accounts payables | 10,552 | 11,120 |
| Unearned rental income | 9,310 | 5,240 |
| Accruals and other provisions | 4,828 | 4,382 |
| Advance received for partial sale of a subsidiary * | 20,143 | - |
| Deal-related payables | 4,725 | 4,725 |
| Staff-related payables | 2,840 | 2,641 |
| Provision for legal and professional expenses | 200 | 200 |
| Restructuring provision | 419 | 419 |
| | **53,017** | 28,727 |

* This represents advance received for sale of 33% of a subsidiary in which Group owns 53%. The sale is pending regulatory approvals.

## 13 SHARE CAPITAL

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Authorised: | | |
| 750,000,000 (2015: 750,000,000) ordinary shares of US$1 each | 750,000 | 750,000 |
| Issued and fully paid up: | | |
| 186,170,234 (2015: 186,170,234) ordinary shares of US$1 each, issued against cash | 186,170 | 186,170 |
| 20,371,807 (2015: 20,371,807) ordinary shares of US$1 each, issued in kind | 20,372 | 20,372 |
| 1,419,873 (2015:1,419,873) ordinary shares of US$1 each,granted to employees | 1,420 | 1,420 |
| | **207,962** | 207,962 |

## 14 INCOME FROM INVESTMENT SECURITIES, NET

| | 2016 | 2015 |
|---|---|---|
| Net fair value loss on equity type investment securities | (6,071) | (5,220) |
| Gain on sale of equity type investment securities, net | 12 | 876 |
| Sukuk income: | | |
| - Sukuk profit | 48 | 315 |
| - (Loss)/gain on sale of sukuk | (59) | 634 |
| Dividend income | 5 | 24 |
| | **(6,065)** | (3,371) |

## 15 FEES AND COMMISSION INCOME

| | 2016 | 2015 |
|---|---|---|
| Arrangement fees | 1,251 | 794 |
| Management fees | 7,701 | 3,857 |
| Brokerage fees | 371 | 732 |
| | **9,323** | 5,383 |

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## 16 NET INCOME FROM NON-BANKING OPERATIONS

| | 2016 | 2015 |
|---|---|---|
| Revenue from Al-Tajamouat for Touristic Projects Co Plc | 22,784 | 24,383 |
| Revenue from Tintoria International | 8,236 | 8,006 |
| Total Revenue | **31,020** | 32,389 |
| Expenses of Al-Tajamouat for Touristic Projects Co Plc | (13,749) | (15,864) |
| Expenses of Tintoria International | (8,177) | (7,959) |
| Total Expenses | **(21,926)** | (23,823) |
| **Net income from non-banking operations** | **9,094** | 8,566 |

## 17 IMPAIRMENT ALLOWANCE

| | 2016 | 2015 |
|---|---|---|
| Impairment allowance on: | | |
| Financing receivables | (3,759) | (3,626) |
| Impairment on equipment | (2,670) | - |
| Reversal of impairment allowance on: | | |
| Equity-accounted investee | - | 16,100 |
| | **(6,429)** | 12,474 |

## 18 COMMITMENTS AND CONTINGENCIES

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Commitment to invest | 10,030 | 10,030 |
| Guarantees | 5,131 | 5,311 |
| Lease commitments | 404 | 727 |
| | **15,565** | 16,068 |

Litigations and claims

Group has filed a number of legal cases against the former Chief Executive Officer before the Civil and Criminal Courts of the Kingdom of Bahrain and the UK. The former CEO has also filed a counter claim in the Bahraini courts for wrongful dismissal. The Bahraini Courts have ruled in favour of the Bank in a number of the civil and criminal cases. The case in the UK was filed by the Group to remedy the damages resulting from defamation and unlawful conspiracy. The case is currently in progress and the ultimate outcome of the matter cannot presently be determined and, accordingly, no provision for any effects on the Group that may result has been made in the financial statements. In 2015, the Group paid US$ 8.1 million to the UK court, of which US$ 4 million was utilised to pay legal expenses of the counterparties and the balance is included under "prepayment and advances" pending outcome of the case.

A number of employment claims have been filed against the Bank by former employees. The Bank's external legal counsel has confirmed that the Bank has strong grounds to successfully defend itself against these claims. No disclosure regarding contingent liabilities arising from the employment claims has been made as the directors of the Bank believe that such disclosures may be prejudicial to the Bank's legal position.

The Group's share of commitments arising from its equity-accounted investees is given in note 8.

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## 19 FAIR VALUE

Fair value is the amount for which an asset could be exchanged or an obligation settled between well informed, willing parties (seller and buyer) in an arm's length transaction. Underlying the definition of fair value is the presumption that the Group is a going concern without any intention or requirement to curtail materially the scale of its operation or to undertake a transaction on adverse terms. Generally accepted methods of determining fair value include reference to quoted prices and the use of valuation techniques such as discounted cash flow analysis.

**Valuation techniques**

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

The fair value of unquoted funds are based on net asset values which are determined by the fund manager using the quoted market prices of the underlying assets, if available, or other acceptable methods such as a recent price paid by another investor, the market value of a comparable company or other proprietary valuation models.

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

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

**Level 1**

Inputs that are quoted (unadjusted) prices in active markets for identical assets or liabilities;

**Level 2**

Other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly. The category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instuments in markets that are considered less than active; or other valuation techniques in which all significant inputs or directly or indirectly are observable; and

**Level 3**

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

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

| **31 December 2016** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Investments carried at fair value through income statement | 14,105 | 40,172 | 4,490 | 58,767 |
| | **14,105** | **40,172** | **4,490** | **58,767** |

| 31 December 2015 | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Investments carried at fair value through income statement | 8,528 | 46,584 | 4,499 | 59,611 |
| | 8,528 | 46,584 | 4,499 | 59,611 |

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19 FAIR VALUE (continued)

Movements in level 3 financial instruments

The following table shows the reconciliation of the opening and closing amount of Level 3 financial assets which are recorded at fair value:

| | **At 01 Januray 2016** | **Total losses recorded in consolidated income statement** | **Additions** | **Sales/ transfers** | **At 31 December 2016** |
|---|---|---|---|---|---|
| **Investments carried at fair value through income statement** | 4,499 | (9) | - | - | 4,490 |
| | **4,499** | **(9)** | **-** | **-** | 4,490 |

| | At 01 Januray 2015 | Total losses recorded in consolidated income statement | Additions | Sales/ transfers | At 31 December 2015 |
|---|---|---|---|---|---|
| Investments carried at fair value through income statement | 5,618 | (2,089) | 970 | - | 4,499 |
| | 5,618 | (2,089) | 970 | - | 4,499 |

Transfers between level 1, level 2 and level 3

There were no transfers between the levels during the year ended 31 December 2016.

The following table shows the impact on fair value of level 3 financial instruments using reasonably possible alternative assumptions.

For investment securities the Bank adjusted the discount rate ± 1% and carrying values ± 5% where appropriate, which is considered by the Bank to be within a range of reasonably possible alternatives.

| | **Carrying amount** | **Effects of reasonably possible alternative assumptions on carrying amount** |
|---|---|---|
| **31 December 2016** | | |
| Investments carried at fair value through income statement | **4,490** | 225 |
| 31 December 2015 | | |
| Investments carried at fair value through income statement | 4,499 | 225 |

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## 20 ASSETS UNDER MANAGEMENT

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Proprietary | 44,616 | 47,532 |
| Clients | 139,347 | 155,811 |
| | **183,963** | 203,343 |

Proprietary assets are included in the consolidated statement of financial position under "investment securities". Client assets, which represent client investments, are managed in a fiduciary capacity without recourse to the Group and are not included in the consolidated statement of financial position.

## 21 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 significant shareholders and entities over which the Bank and shareholders exercise significant influence, directors, members of Shari'ah Supervisory Board and executive management 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:

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Short term employee benefits | 9,199 | 10,230 |
| Post-employment benefits | 765 | 748 |
| | **9,964** | 10,978 |

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21 *RELATED PARTY TRANSACTIONS (continued)*

The significant related party transactions and balances included in this consolidated financial statements are as follows:

| | **31 December 2016** | | | | 31 December 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Associates** | **Significant shareholders/ entities in which directors have interest** | **Key management** | **Assets under management and other entities** | Associates | Significant shareholders/ entities in which directors have interest | Key management | Assets under management and other entities |
| **Assets** | | | | | | | | |
| Cash and balances with banks | - | - | - | - | 22 | - | - | - |
| Financing receivables | - | - | - | 986 | - | - | - | 15,070 |
| Investment securities | 40,171 | - | - | 18,880 | 46,584 | - | - | 6,910 |
| Equity-accounted investees | 124,994 | - | - | - | 136,753 | - | - | - |
| Other assets | 1,580 | - | 639 | 1,179 | 1,849 | - | 497 | 366 |
| **Liabilities** | | | | | | | | |
| Due to financial institutions | 14,708 | - | - | - | 14,570 | - | - | - |
| Due to customers | 918 | 131,690 | - | - | 918 | 30,461 | - | - |
| Other liabilities | - | 599 | 2,109 | 28 | 222 | 417 | 1,304 | 516 |

| | **Year ended 31 December 2016** | | | | Year ended 31 December 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| | **Associates** | **Significant shareholders/ entities in which directors have interest** | **Key management** | **Assets under management and other entities** | Associates | Significant shareholders/ entities in which directors have interest | Key management | Assets under management and other entities |
| **Income / (expenses)** | | | | | | | | |
| Income from investment securities | (6,412) | - | - | 460 | (4,467) | - | - | 1,841 |
| Fees and commission | 2,601 | - | - | 103 | 2,320 | - | - | 195 |
| Net finance income / (expense) | (528) | (5,706) | - | 71 | (524) | (1,641) | - | 614 |
| Share of (loss)/profit of equity-accounted investees | (328) | - | - | - | 5,253 | - | - | - |
| Directors' and Shari'ah board remuneration and expenses | - | (389) | - | (87) | - | (412) | - | 81 |

## 22 RISK MANAGEMENT

Risk is an inherent part of the Group's business activities. The Group's risk management and governance framework is intended to provide progressive controls and continuous management of the major risks involved in the Group's activities. Risks are managed by a process of identification, measurement and monitoring, and are subject to risk limits and other controls. The process of risk management is critical to the Group's operations and each business unit within the Group is accountable for the risk exposures relating to their responsibilities. The Group's main risk exposure categories are Investment and Credit risk, Market risk, Liquidity risk and Operational

– Risk identification: The Group's exposure to risk through its business activities, including investment in Private Equity, Brokerage, and Capital Markets, is identified through the Group's risk management infrastructure, which includes prior review of all new activities by Risk management.

– Risk measurement: The Group measures risk using risk management position methodologies which reflect the Group's investment risks, foreign exchange and profit rate exposure risks. The Bank relies on both quantitative and qualitative approaches in quantifying risks.

– Risk monitoring: The Group's risk management policies and procedures incorporate respective limits and the Group's activities. The Bank conducts periodic reporting for ongoing monitoring of its position at both Management and Board level.

– Risk reporting: The Group undertakes reporting of all core risks relevant to its businesses on a consolidated basis. In line with the Board-approved risk framework. The Bank has risk governance arrangements to oversee risk management and transaction approval and key governance committees include; the Group Asset and Liability Committee ("ALCO") which oversees liquidity, cash flow planning and general asset liability management, the Group Risk Executive Committee ("REXCO") which oversees risk management across the group including review and approval of risk limits, credit facilities and key risk processes and the Investment and Post Investment Management Committee ("IPIMC") which is responsible for review and approval of new investments, funding requirements, divestments and general investment processes.

Group Risk Framework and Governance

The Board of Directors is ultimately accountable for the risk management of the Group. The Board has advocated a wholly integrated risk management process within the Group, in which all business activities are aligned to the risk framework. The Group Risk Framework establishes Group risk management standards, risk processes, structures, and defines the Bank's risk philosophy.

Board of Directors

The Board of Directors is responsible for defining the Group's risk appetite within which it manages its risk exposures and reviews the Group's compliance with delegated risk authorities.

Audit Committee

The Audit Committee is appointed by the Board of Directors and consists of four non-executive Board members. The Audit Committee assists the Board in carrying out its responsibilities with respect to assessing the quality and integrity of financial reporting and oversight of the Internal Audit function.

Shari'ah Supervisory Board

The Group's Shari'ah Supervisory Board is vested with the responsibility of ensuring that the Group complies with the Shari'ah rules and principles in its transactions, activities and general philosophy.

**Group Risk Executive Committee**

Group Risk Executive Committee REXCO has the overall responsibility for ensuring that the Group develops appropriate risk policies and strategies for the relevant business activities, and makes preparations for forthcoming regulatory arrangements in line with Basel Committee recommendations. It oversees the risk management activities of the Group, reviews and approves risk management principles, frameworks, policies, limits, processes and procedures. It is responsible for assessing fundamental risk issues within the general development strategy of the Group.

22 RISK MANAGEMENT (continued)

Internal Audit and Independent Review

All key operational, financial and risk management processes are audited by Internal Audit according to risk based auditing standards. Internal Audit examines the adequacy of the relevant policies and procedures and the Group's compliance with internal policies and regulatory guidelines. Internal Audit discusses the result of all assessments with management and reports its findings and recommendations to the Audit Committee. The Internal Audit recommendations are tracked for resolution via the Committee.

Group Asset and Liability Committee (ALCO)

The Group Asset and Liability Committee establishes the funding, liquidity and market risk policies for the Group. It is composed of the CEO, CFO, Treasury and control areas. ALCO's objectives are to manage the assets and liabilities of the Group, determine the statement of financial position mix and appropriate risk and return profile. It oversees all treasury and capital markets activities and all areas affected by liquidity and market risk. Cash flow management is a major focus of ALCO and ALCO regularly reviews the business line investment plans to ensure that sufficient funding is in place. ALCO ensures that the appropriate mix of short and long term funding strategies are developed in conjunction with the Group's treasury and capital markets functions.

Risk Management

The Risk Management function is responsible for designing and implementing the Group's risk framework, including policies, processes and systems. The Chief Risk Officer reports functionally to the Board Risk Committee and administratively to the Chief Executive Officer. Risk Management conducts risk assessments of individual transactions (including their respective credit, investment, counterparty and operational risks), products and services. Risk Management is responsible for ensuring that the Group's processes capture all sources of transaction risk and that appropriate limit methodologies are developed for use in the management of business risk. In addition to the above the Risk Function also supports investment processes throughout the investment cycle by monitor the investment risk.

Treasury Activities

Treasury is responsible for managing the Group's day to day funding, liquidity management, foreign exchange and profit rate exposures, under the review of Risk Management and the supervision of ALCO.

Investment Monitoring and Reporting

Proprietary investment risks are identified and assessed via extensive due diligence activities conducted by the respective departments. This is supported by Risk Management which undertakes an independent risk assessment of every investment transaction. Post-acquisition investment management is rigorously exercised, mainly via board representation within the investee company, during the life of the investment transaction.

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

- credit risk
- liquidity risk
- market risk
- operational risk

The information about the Group's exposure to each of the above risks, its objectives, policies and processes for measuring and managing risk, and the Bank's management of capital is explained in notes 23 to 26 and 33.

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## 23 CREDIT RISK

Credit Risk Policy Framework

The Bank has a Group Credit Risk Policy framework establishing Group credit risk appetite, credit risk origination, underwriting and administration standards. The credit policy articulates key credit markets, minimum criteria for the granting of credit, minimum requirements on collateral and defines roles and responsibilities for credit risk management. The policy provides a guideline to business units when originating credit business.

Credit Risk Management

Credit risk is the risk that the Group will incur a loss of principal or profit earned because its customers, clients or counterparties fail to discharge their contractual obligations and arises principally from the Group's balances with banks, placements with financial institutions, financing receivables, investment securities – sukuk and other receivables. Institutional Banking proposes limits for its interbank placement activities and other client groups for review and approval by REXCO. Further, Risk Management independently analyses the applications and rates for the respective counterparties. Based on this an independent recommendation is forwarded to the REXCO for approval. REXCO periodically reviews these limits for appropriateness in prevailing market conditions.

The table below shows the maximum exposure to credit risk for the components of the consolidated statement of financial position. There is no significant use of master netting and collateral agreements.

| | **Maximum exposure 2016** | Maximum exposure 2015 |
|---|---|---|
| On balance sheet | | |
| Balances with banks | 15,472 | 17,016 |
| Placements with financial institutions | 8,402 | 9,648 |
| Financing receivables | 16,075 | 66,713 |
| Investment securities – Sukuk | 2,836 | 5,319 |
| Other assets | 26,394 | 25,206 |
| Off balance sheet | | |
| Guarantees | 5,131 | 5,311 |
| | **74,310** | 129,213 |

### *Risk Exposure Concentration*

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

In order to avoid excessive concentrations of risk, the Group's policies and procedures include guidelines to focus on maintaining a diversified portfolio. In line with regulatory requirements, the Bank has a group level Large Exposure Policy which details the Bank's approach in managing concentration risk to sectors, asset classes, single obligors and countries including defining specific limits.

Concentration of risks is managed by counterparty, by geographical region and by industry sector. The maximum credit exposure to any client, or counterparty, or group of closely related counterparties as of 31 December 2016 was US$ 9.1 million, relating to "cash and balances with banks" (2015: US$ 10.2 million).

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23 *CREDIT RISK (continued)*

Geographical Exposure Distribution

The analysis by geographical region of the Group's financial assets having credit risk exposure is as follows:

| | 31 December 2016 | | | | | |
|---|---|---|---|---|---|---|
| **Type of Assets/Region** | **Bahrain** | **Other Middle East** | **North America** | **Asia** | **Europe** | **Grand Total** |
| Balances with banks | 2,651 | 9,603 | - | 3,218 | - | 15,472 |
| Placement with financial institutions | 6,004 | - | - | 2,000 | 398 | 8,402 |
| Financing receivables | - | - | - | 15,089 | 986 | 16,075 |
| Investment securities - Sukuk | - | 330 | - | 2,506 | - | 2,836 |
| Other assets | 2,105 | 20,081 | 20 | 313 | 3,875 | 26,394 |
| Off Balance sheet | - | - | 5,000 | - | 131 | 5,131 |
| **Grand Total** | **10,760** | **30,014** | **5,020** | **23,126** | **5,390** | **74,310** |

| | 31 December 2015 | | | | | |
|---|---|---|---|---|---|---|
| Type of Assets/Region | Bahrain | Other Middle East | North America | Asia | Europe | Grand Total |
| Balances with banks | 821 | 5,947 | - | 10,248 | - | 17,016 |
| Placement with financial institutions | 3,040 | - | - | 6,010 | 598 | 9,648 |
| Financing Receivables | 1,927 | - | - | 64,786 | - | 66,713 |
| Investment securities - Sukuk | - | 857 | - | 4,462 | - | 5,319 |
| Other Assets | 2,389 | 22,376 | 13 | 164 | 264 | 25,206 |
| Off Balance sheet | - | - | 5,000 | - | 311 | 5,311 |
| Grand Total | 8,177 | 29,180 | 5,013 | 85,670 | 1,173 | 129,213 |

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23 *CREDIT RISK (continued)*

*Industry Sector Exposure*

*The distribution of assets and off-statement of financial position items by industry sector is as follows:*

| Type of Assets/Industry | 31 December 2016 Banking and Finance | Industrial | Real Estate and Const-ruction | Tech-nology | Funds | Trade | Total |
|---|---|---|---|---|---|---|---|
| **Funded:** | | | | | | | |
| Balances with banks | 15,472 | - | - | - | - | - | 15,472 |
| Placement with financial institutions | 8,402 | - | - | - | - | - | 8,402 |
| Financing Receivables | - | 4,730 | 986 | 5,476 | - | 4,883 | 16,075 |
| Investment securities - Sukuk | 2,506 | - | 330 | - | - | - | 2,836 |
| Other Assets | 5,659 | 54 | 17,436 | 18 | 1,393 | 1,834 | 26,394 |
| **UnFunded:** | | | | | | | - |
| Guarantees | 131 | - | - | 5,000 | - | - | 5,131 |
| **Grand Total** | **32,170** | **4,784** | **18,752** | **10,494** | **1,393** | **6,717** | **74,310** |

| Type of Assets/Industry | 31 December 2015 Banking and Finance | Industrial | Real Estate and Construction | Technology | Funds | Trade | Total |
|---|---|---|---|---|---|---|---|
| **Funded:** | | | | | | | |
| Balances with banks | 17,016 | - | - | - | - | - | 17,016 |
| Placement with financial institutions | 9,648 | - | - | - | - | - | 9,648 |
| Financing Receivables | 5,781 | 4,612 | 8,488 | 8,525 | - | 39,307 | 66,713 |
| Investment securities - Sukuk | 4,463 | - | 856 | - | - | - | 5,319 |
| Other Assets | 1,159 | 54 | 20,219 | 11 | 1,629 | 2,134 | 25,206 |
| **UnFunded:** | | | | | | | - |
| Guarantees | 311 | - | - | 5,000 | - | - | 5,311 |
| Grand Total | 38,378 | 4,666 | 29,563 | 13,536 | 1,629 | 41,441 | 129,213 |

***Collateral and other credit enhancements***

The Group utilizes collateral and other credit enhancements mostly on its credit facilities, in line with Shari'ah requirements. Before taking any form of collateral the Bank pre-assesses impediments that may restrict accessibility to collateral should the need arise as well as acceptability from a Shari'ah perspective. In this respect the Bank will formally agree with the customer at the time of signing the offer letter on the usage, redemption and utilization of collateral when the customer/counterparty defaults. In the past year, the Bank has obtained collateral including shareholders' personal guarantees, cash, real estate, unlisted equity shares and debentures. The Bank's credit policy discourages taking collateral value where there is positive correlation between collateral value and obligor's ability to pay.

Credit quality per class of financial assets

The Group did not apply a standard credit rating to its investment business, as the Group assessed credit quality according to the policies of the respective business areas. Management considers the credit quality of the Group's financial assets to be of standard quality as of 31 December 2016. Following is an analysis of credit quality by class of financial assets:

| | 2016 Neither past due nor impaired | Past due but not impaired | Individually impaired | Impairment/ provision | Total |
|---|---|---|---|---|---|
| Balances with banks | 15,472 | | | | 15,472 |
| Placements with financial institutions | 8,402 | | | | 8,402 |
| Financing receivables | 14,771 | | 14,797 | (13,493) | 16,075 |
| Investment securities – Sukuk | 2,836 | | | | 2,836 |
| Other assets | 25,835 | 559 | 2,269 | (2,269) | 26,394 |
| Guarantees | 5,131 | | | | 5,131 |
| Total | **72,447** | **559** | **17,066** | **(15,762)** | **74,310** |

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23 CREDIT RISK (continued)

Exposures that are past due but not impaired are either past due for less than 90 days and the financial condition of the customer is sound, or has adequate unimpaired collateral coverage. Provisioning is driven by the performance of the customer against laid down terms and conditions of the facility, internal credit grading and classification system calculated on net exposure after deducting the discounted value of recoverable collateral and any disposal costs.

| | 2015 | | | | |
|---|---|---|---|---|---|
| | Neither past due nor impaired | Past due but not impaired | Individually impaired | Impairment/ provision | Total |
| Balances with banks | 17,016 | - | - | - | 17,016 |
| Placements with financial institutions | 9,679 | - | - | (31) | 9,648 |
| Financing receivables | 67,513 | - | 9,269 | (10,069) | 66,713 |
| Investment securities – Sukuk | 5,319 | - | - | - | 5,319 |
| Other assets | 24,653 | 553 | 1,902 | (1,902) | 25,206 |
| Guarantees | 5,311 | - | - | - | 5,311 |
| Total | 129,491 | 553 | 11,171 | (12,002) | 129,213 |

Ageing analysis of past due but not impaired by class of financial assets:

| | 2016 | | | |
|---|---|---|---|---|
| | Less than 120 days | Less than 365 days | More than 365 days | Total |
| Other assets | 144 | 179 | 236 | 559 |

| | 2015 | | | |
|---|---|---|---|---|
| | Less than 120 days | Less than 365 days | More than 365 days | Total |
| Other assets | 317 | 108 | 128 | 553 |

## 24 LIQUIDITY RISK MANAGEMENT

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.

The key features of the Group's liquidity methodology are:

– The Group Asset and Liability Committee ("ALCO") is responsible for liquidity monitoring, cash flow planning and general asset liability management.

– In accordance with the Basel recommendations on liquidity management, the Group measures liquidity according to two criteria: "normal business", reflecting day-to-day expectations regarding the funding of the Group; and "crisis scenario", reflecting simulated extreme business circumstances in which the Group's survival may be threatened.

– The Group's liquidity policy is to hold sufficient liquid assets to cover its committed statement of financial position requirements, plus its budgeted expenses for the liquidity horizon and its forecast investment commitments over the liquidity horizon.

Analysis of financial liabilities

The table below summarises the maturity profile of the Group's financial liabilities based on contractual undiscounted repayment obligations.

| | **Gross undiscounted cash flows** | | | | **Carrying value** |
|---|---|---|---|---|---|
| | **Less than 3 months** | **3 to 12 months** | **Over 1 year** | **Total** | |
| **At 31 December 2016** | | | | | |
| Due to financial Institutions | 25,547 | 17,993 | 60,829 | 104,369 | 87,566 |
| Due to customers | 94,634 | 59,143 | - | 153,777 | 151,034 |
| Other liabilities | 45,521 | 4,725 | 2,771 | 53,017 | 53,017 |
| **Total financial liabilities** | **165,702** | **81,861** | **63,600** | **311,163** | **291,617** |

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24 *LIQUIDITY RISK MANAGEMENT (continued)*

| | Gross undiscounted cash flows | | | | Carrying value |
|---|---|---|---|---|---|
| | Less than 3 months | 3 to 12 months | Over 1 year | Total | |
| At 31 December 2015 | | | | | |
| Due to financial Institutions | 49,736 | 22,442 | 72,762 | 144,940 | 123,252 |
| Due to customers | 128,795 | 81,192 | - | 209,987 | 208,250 |
| Other liabilities | 24,002 | - | 4,725 | 28,727 | 28,727 |
| Total financial liabilities | 202,533 | 103,634 | 77,487 | 383,654 | 360,229 |

*The table below shows the contractual expiry by maturity of the Group's commitments.*

| | On demand | 3 to 12 months | Over 1 year |
|---|---|---|---|
| **31 December 2016** | | | |
| Investment-related Commitments | 10,030 | - | - |
| Lease Commitments | - | 323 | 81 |
| Guarantees | 5,131 | - | - |
| Total | **15,161** | **323** | **81** |

| | On demand | 3 to 12 months | Over 1 year |
|---|---|---|---|
| 31 December 2015 | | | |
| Investment-related Commitments | 10,030 | - | - |
| Lease Commitments | - | 323 | 404 |
| Guarantees | 5,311 | - | - |
| Total | 15,341 | 323 | 404 |

25 **MARKET RISK MANAGEMENT**

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to adverse changes in market variables such as profit rates, foreign exchange rates, equity prices and commodities. The Group classifies exposures to market risk into either trading or non-trading portfolios. The Group does not currently engage in significant trading activity. Non-trading positions are managed and monitored using sensitivity analysis.

**Market Risk: Non-trading**

*Profit rate risk*

Profit rate risk arises from the possibility that changes in profit rates will affect future cash flows or the fair values of the financial instruments. The Group currently has limited exposure to profit rate risk. The Group's assets and liabilities that are exposed to profit rate risk include: placements with financial institutions, financing receivables, investments in sukuk and due to financial and non-financial institutions.

The following table demonstrates the sensitivity to a reasonable possible change in profit rates by 200 bps, with all other variables held constant. The effect of decreases in profit rate is expected to be equal and opposite to the effect of the increases shown.

| | **2016** | | | 2015 | | |
|---|---|---|---|---|---|---|
| | Balance | Change in profit rate bps (+/-) | Effect on net profit (+/-) | Balance | Change in profit rate bps (+/-) | Effect on net profit (+/-) |
| **Assets** | | | | | | |
| Placements with financial institutions | 8,402 | 200 | 4 | 9,648 | 200 | 105 |
| Financing receivables | 16,075 | 200 | 27 | 66,713 | 200 | 204 |
| Investment securities – Sukuk | 2,836 | 200 | 13 | 5,319 | 200 | 33 |
| **Liabilities** | | | | | | |
| Due to financial institutions | (87,566) | 200 | (1,337) | (123,252) | 200 | (1,759) |
| Due to customers | (151,034) | 200 | (258) | (208,250) | 200 | (682) |
| **Total** | | | **(1,551)** | | | (2,099) |

US$ 000's

25 *MARKET RISK MANAGEMENT (continued)*

*Currency risk*

Currency risk is the risk that the value of a financial instrument will fluctuate due to adverse changes in foreign exchange rates.

The table below indicates the currencies to which the Group has significant exposure. The analysis shows the impact of a 20% movement in the currency rate against the United States Dollar, with all other variables held constant on the consolidated statement of income and equity. The effect of decreases in the currency rates is expected to be equal and opposite to the effect of the increases shown.

| | 2016 | | | 2015 | | |
|---|---|---|---|---|---|---|
| **Currency** | Exposure (USD equivalent) | Effect on net profit (+/-) | Effect on equity (+/-) | Exposure (US$ equivalent) | Effect on net profit (+/-) | Effect on equity (+/-) |
| Kuwaiti Dinar | (9,951) | (1,990) | - | (10,024) | (2,005) | - |
| Turkish Lira | 984 | 92 | 104 | 1,136 | 106 | 121 |
| Malaysian Ringgit | - | - | - | 26 | 5 | - |
| Euro | 23 | 5 | - | 23 | 5 | - |
| Jordanian Dinar * | 53,291 | 10,658 | - | 50,424 | 10,085 | - |
| Sterling Pounds | 3,367 | 673 | - | 4,065 | 813 | - |

* Jordanian Dinar is officially pegged to International Monetary Fund (IMP) special drawing rights (SDR's). In practice this is fixed at 1US$=0.706 JOD most of the times.

*Equity price risk*

Equity price risk is the risk that the fair value of equities decreases as the result of adverse changes in the levels of equity prices and the value of individual stocks. Equity price risk arises from the Group's investment portfolio. The Group conducts significant investment activity in private equity, mainly in unquoted entities. The Group manages this risk through diversification of its investments in terms of geographical distribution and industry concentration by arranging representation on the Board of Directors within the investee company, wherever possible. Investments are managed within maximum concentration risk limits, approved by the Board of Directors of the Bank.

*Sensitivity analysis*

Unquoted securities - Investment securities carried at fair value through income statement:

The effect on profit as a result of a change in the fair value of equity instruments at 31 December 2016 due to a reasonable possible change (i.e. +/-15%) in the value of individual investments, with all other variables held constant, is US$ 6.7 million (2015: US$ 7.8 million). The effect of decrease in the value of individual investments is expected to be equal and opposite to the effect of an increase.

*Prepayment risk*

Prepayment risk is the risk that the Group will incur a financial loss because its customers and counterparties prepay or request repayment earlier than expected. The Group is not exposed to any significant prepayment risk.

26 **OPERATIONAL RISK**

Operational risk is the risk of unexpected losses resulting from inadequate or failed internal controls or procedures, systems failures, fraud, business interruption, compliance breaches, human error, management failure or inadequate staffing. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications or lead to financial loss.

While operational risks cannot be entirely eliminated, they are managed and mitigated by ensuring that appropriate infrastructure, controls, systems, procedures and trained and competent people are in place throughout the Group.

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## 27 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled.

| | 2016 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | Total up to 1 year | Over 1 year | Undated | Total |
| **ASSETS** | | | | | | | | |
| Cash and balances with banks | 15,479 | | | | 15,479 | | | 15,479 |
| Placements with financial institutions | 8,402 | | | | 8,402 | | | 8,402 |
| Financing receivables | 5,606 | 8,888 | 1,581 | - | 16,075 | - | - | 16,075 |
| Investment securities | - | 12,827 | 40,217 | 8,559 | 61,603 | | | 61,603 |
| Equity-accounted investees | | | | | - | | 124,994 | 124,994 |
| Investment properties | | | | | - | | 224,448 | 224,448 |
| Other assets | 717 | 25,065 | 3,444 | | 29,226 | | | 29,226 |
| Equipment | | | | | - | | 9,466 | 9,466 |
| **Total assets** | **30,204** | **46,780** | **45,242** | **8,559** | **130,785** | **-** | **358,908** | **489,693** |
| **LIABILITIES** | | | | | | | | |
| Due to financial institutions | 14,096 | 10,285 | 6,061 | 8,622 | 39,064 | 48,502 | | 87,566 |
| Due to customers | 7,558 | 86,033 | 56,975 | 468 | 151,034 | | | 151,034 |
| Other liabilities | - | 45,521 | 4,725 | - | 50,246 | 2,771 | - | 53,017 |
| **Total liabilities** | **21,654** | **141,839** | **67,761** | **9,090** | **240,344** | **51,273** | **-** | **291,617** |
| **Commitments** | | 81 | 81 | 161 | 323 | 81 | 15,161 | 15,565 |
| **Net liquidity gap** | 8,550 | (95,140) | (22,600) | (692) | (109,882) | (51,354) | 343,747 | 182,511 |
| **Net cumulative gap** | **8,550** | **(86,590)** | **(109,190)** | **(109,882)** | **(109,882)** | **(161,236)** | **182,511** | |

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27 *MATURITY ANALYSIS OF ASSETS AND LIABILITIES (continued)*

| | 2015 | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **Up to 1 month** | **1 to 3 months** | **3 to 6 months** | **6 to 12 months** | **Total up to 1 year** | **Over 1 year** | **Undated** | **Total** |
| ASSETS | | | | | | | | |
| Cash and balances with banks | 17,021 | - | - | - | 17,021 | - | - | 17,021 |
| Placements with financial institutions | 9,614 | 34 | - | - | 9,648 | - | - | 9,648 |
| Financing receivables | 6,152 | 54,079 | 6,482 | - | 66,713 | - | - | 66,713 |
| Investment securities | 4,465 | 55 | 1,988 | - | 6,508 | 58,422 | - | 64,930 |
| Equity-accounted investees | | | | | - | | 136,753 | 136,753 |
| Investment properties | | | | | - | | 241,466 | 241,466 |
| Other assets | - | 32,313 | - | - | 32,313 | - | - | 32,313 |
| Equipment | - | - | - | - | - | - | 13,274 | 13,274 |
| **Total assets** | **37,252** | **86,481** | **8,470** | **-** | **132,203** | **58,422** | **391,493** | **582,118** |
| LIABILITIES | | | | | | | | |
| Due to financial institutions | 30,057 | 18,363 | 6,090 | 12,478 | 66,988 | 56,264 | - | 123,252 |
| Due to customers | 15,548 | 116,039 | 15,997 | 60,666 | 208,250 | - | - | 208,250 |
| Other liabilities | - | 26,153 | - | - | 26,153 | 2,574 | - | 28,727 |
| **Total liabilities** | **45,605** | **160,555** | **22,087** | **73,144** | **301,391** | **58,838** | **-** | **360,229** |
| **Commitments** | - | 81 | 81 | 161 | 15,664 | 404 | 15,341 | 16,068 |
| **Net liquidity gap** | (8,353) | (74,155) | (13,698) | (73,305) | (184,852) | (820) | 394,398 | 208,726 |
| **Net cumulative gap** | **(8,353)** | **(82,508)** | **(96,206)** | **(169,511)** | **(184,852)** | **(185,672)** | **208,726** | |

US$ 000's

## 28 SEGMENT INFORMATION

Operating segments are reported in accordance with internal reporting provided to Executive Management (the chief operating decision-maker), which is responsible for allocating resources to the reportable segments and assesses its performance. All operating segments used by the Group meet the definition of a reportable segment under FAS 22.

During the year, the Group has changed its reportable segments as a result of the recent restructuring of its business and in-line with the current internal reporting to the Chief Operating decision-maker for segment measurement and monitoring. Currently, the Group is organised into business units based on their nature of operations and services and has three reportable operating segments which are as follows:

| | |
|---|---|
| **Investment Banking & Alkhair Capital Menkul Degerler A.S** | The Group's Investment banking business is engaged in transaction origination and structuring, investment, placement to third-party investors, restructuring and managing portfolio companies. This segment focuses on stable companies, historically revenue-generating with positive profitability, requiring growth capital or partial exits. The segment focuses on specific sectors and geographies, whilst avoiding start-ups, venture capital, and greenfield investments. The segment targets businesses in the oil & gas services; industrial services; building materials; logistics; and agri-business; specifically in the MENA region including Turkey.<br><br>The business manages Al-Tajamouat for Touristic Projects Co. "Taj" which own and operate a shopping mall in Amman. At 31 December 2015, the total assets of Taj are US$ 219 million and the total equity is US$ 143 million. In 2015, Taj reported a net profit of US$ 8.5 million.<br><br>Alkhair Capital Menkul Degerler A.S originates Shari'ah compliant PE transactions, especially proprietary deals from direct contacts with a wide range of local sources. The Turkey office also provides a post-investment management services (post management until successful exit, advisory for an IPO or trade sale) to co-investors.<br><br>The business manages the Bank's Global Private Equity Fund. It also sources and manages investments on behalf of the Bank's Strategic Acquisition Fund. |
| **Alkhair International Islamic Bank Malaysia Berhad** | Alkhair International Islamic Bank Malaysia Berhad was established in 2004 to source investment opportunities in the Far East and monitor the performance of the acquired companies on behalf of the Bank and investors and to establish distribution channels for the Group. |
| **Alkhair Capital Saudi Arabia** | Alkhair Capital Saudi Arabia was incorporated in March 2009 and registered with Capital Markets Authority. Its principal activities are Asset Management, Corporate Finance & Investment banking and Brokerage. |

Information regarding the results of each reportable segment is included below. Inter-segment pricing is determined on an arm's length basis. Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment.

for the year ended 31 December 2016 US$ 000's

28 *SEGMENT INFORMATION (continued)*

| | for the year ended 31 December 2016 | | | | |
|---|---|---|---|---|---|
| | Investment Banking & Alkhair Capital Menkul Degerler A.S | Alkhair International Islamic Bank Malaysia Berhad | Alkhair Capital Saudi Arabia | Inter-company | Total |
| Net finance (expense) / income | (10,310) | 952 | - | - | (9,358) |
| Income from investment securities | (6,348) | 20 | 263 | - | (6,065) |
| Fees and commission | 2,734 | 232 | 6,357 | - | 9,323 |
| Share of loss of equity-accounted investees | (328) | - | - | - | (328) |
| Income from non-banking operations | 31,020 | - | - | - | 31,020 |
| Rental income | - | - | 2,422 | - | 2,422 |
| Loss from sale of investment property | (2,239) | - | - | - | (2,239) |
| Foreign exchange (loss)/gain, net | (926) | 22 | - | - | (904) |
| Other income | 1,917 | - | - | - | 1,917 |
| Inter-segment income | (275) | 275 | - | - | - |
| **Total income** | **15,245** | **1,501** | **9,042** | **-** | **25,788** |
| Total operating expenses | (35,469) | (2,171) | (7,665) | - | (45,305) |
| Impairment allowance | (3,986) | (2,443) | - | - | (6,429) |
| Net loss on disposal of an associate | (7,088) | - | - | - | (7,088) |
| **(Loss)/profit for the year** | **(31,298)** | **(3,113)** | **1,377** | **-** | **(33,034)** |
| Equity-accounted investees | 124,994 | - | - | - | 124,994 |
| Segment assets | 392,738 | 47,489 | 70,146 | (20,680) | 489,693 |
| Segment liabilities | 278,601 | 27,151 | 6,545 | (20,680) | 291,617 |

**for the year ended 31 December 2016** US$ 000's

28 SEGMENT INFORMATION (continued)

| | for the year ended 31 December 2015 | | | | |
|---|---|---|---|---|---|
| | Investment Banking & Alkhair Capital Menkul Degerler A.S | Alkhair International Islamic Bank Malaysia Berhad | Alkhair Capital Saudi Arabia | Inter-company | Total |
| Net finance (expense) / income | (8,945) | 2,299 | - | - | (6,646) |
| Income from investment securities | (4,016) | 350 | 295 | - | (3,371) |
| Fees and commission | 2,497 | 528 | 2,358 | - | 5,383 |
| Share of profit of equity-accounted investees | 5,253 | - | - | - | 5,253 |
| Income from non-banking operations | 32,389 | - | - | - | 32,389 |
| Rental income | - | - | 3,361 | - | 3,361 |
| Gain on sale of investment property | - | - | 721 | - | 721 |
| Foreign exchange (loss)/gain, net | (148) | - | - | - | (148) |
| Other income | 2,088 | - | - | - | 2,088 |
| Inter-segment income | - | - | - | - | - |
| Total income | 29,118 | 3,177 | 6,735 | - | 39,030 |
| Total operating expenses | (44,742) | (2,367) | (6,895) | - | (54,004) |
| Impairment allowance | 16,049 | (3,575) | - | - | -<br>12,474 |
| Profit/(loss) for the year | 425 | (2,765) | (160) | - | (2,500) |
| As at 31 December 2015 | | | | | |
| Equity-accounted investees | 136,753 | - | - | - | 136,753 |
| Segment assets | 430,548 | 104,293 | 68,038 | (20,761) | 582,118 |
| Segment liabilities | 294,327 | 80,842 | 5,821 | (20,761) | 360,229 |

**Geographic segment information:**

The Group operates in four geographic markets: Bahrain, Other Middle East, Asia Pacific and Europe. The following tables show the distribution of the Group's total income and non-current assets by geographical segments:

| **31 December 2016** | **Bahrain** | **Other Middle East** | **Asia Pacific** | **Europe** | **Total** |
|---|---|---|---|---|---|
| Total income | (22,923) | 40,030 | 1,500 | 93 | **18,700** |
| Net (loss) / profit for the year | (35,745) | 6,820 | (3,114) | (995) | **(33,034)** |
| Non-current assets * | 126 | 233,563 | 180 | 45 | **233,914** |

| | Bahrain | Other Middle East | Asia Pacific | Europe | Total |
|---|---|---|---|---|---|
| Total income | (3,336) | 38,997 | 3,176 | 193 | 39,030 |
| Net (loss) / profit for the year | (5,900) | 7,383 | (2,767) | (1,216) | (2,500) |
| Non-current assets * | 18,128 | 236,312 | 207 | 93 | 254,740 |

** includes equipment and investment property*

## 29 SHARI'AH SUPERVISORY BOARD

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

## 30 EARNINGS AND EXPENSES PROHIBITED BY SHARI'AH

The Group did not receive any significant income or incur significant expenses that were prohibited by the Shari'ah.

## 31 SOCIAL RESPONSIBILITIES

The Group discharges its social responsibilities through donations to good faith charity funds.

## 32 ZAKAH

The Bank is not obliged to pay Zakah. Payment of Zakah is the responsibility of the shareholders of the Bank. Zakah payable by shareholders on their holdings in the Bank is calculated on the basis of a method prescribed by the Bank's Shari'ah Supervisory Board. Zakah payable by the shareholders in respect of the year ended 31 December 2016 was US$ 0.00541 per share (2015: US$ 0.00655 per share).

## 33 CAPITAL MANAGEMENT

The Group is regulated by the Central Bank of Bahrain (CBB) which sets and monitors capital requirements for the Group as a whole. CBB required the Group to maintain a prescribed ratio of total capital (net of prudential deductions) to total risk-weighted assets (determined according to specified requirements to reflect the varying levels of risk attached to assets and off-balance sheet exposures).

The primary objectives of the Group's capital management policies are to ensure that the Group complies with externally imposed capital requirements and that the Group maintaining capital ratios in order to support its business and to maximise shareholders' value. The Group does not have any significant restrictions on its ability to access or use its assets and settle its liabilities other than any restrictions that may result from the supervisory frameworks within which the banking subsidiaries operate.

The Bank's capital adequacy ratio, is calculated in accordance with the capital adequacy rules set by the regulator. The Group's regulatory capital is analysed into two tiers:

- Tier 1 capital

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 of instruments that meet the criteria for inclusion in AT1, 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.

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33 *CAPITAL MANAGEMNT (continued)*

- Tier 2 capital

It 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 regulatory adjustments applied in the calculation of Tier 2 capital.

The regulatory adjustments are subject to limits prescribed by the CBB requirements. These deductions would be effective in a phased manner through transitional arrangements from 2015 to 2018. The regulations prescribe higher risk weights for certain exposures that exceed 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 Bank 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.

The Bank's regulatory capital position at 31 December is as follows:

| | **2016** | 2015 |
|---|---|---|
| **Total risk-weighted exposures** | 1,598,468 | 1,332,357 |
| CET1 capital | 40,372 | 68,541 |
| Tier 1 capital | 814 | 831 |
| Total Capital | 41,186 | 69,372 |
| **% of Total Risk Weighted Exposures (CAR)** | | |
| CET1 capital adequacy ratio | 2.53% | 5.14% |
| Tier1 capital adequacy ratio | 2.53% | 5.14% |
| Total capital adequacy ratio | 2.58% | 5.21% |

The capital adequacy ratio as at 31 December 2016 was below the minimum regulatory capital requirement of 12.5%. Based on the planned asset sales program and operating cash flow projections, the Group expects to improve its risk weighted assets profile and capital adequacy ratio.

## 34 COMPARATIVES

An equity-accounted investee made a prior year adjustment (note 7) and the Bank has accounted for it's share of the adjustment. Loss of USD 2.9 million was adjusted in the opening accumulated losses and the carrying value of the investment was decreased by the same amount.
Certain prior year amounts have been regrouped to agree with current year presentations. Such regrouping does not affect the previously reported loss or total equity, except for the effect of adjustments mentioned above.