

**BAHRAIN ISLAMIC BANK B.S.C.**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**31 DECEMBER 2018**

Commercial registration	: 9900 (registered with Central Bank of Bahrain as a retail Islamic bank)
Board of directors	: Dr. Esam Abdulla Fakhro, <i>Chairman</i> Brig. Ebrahim Abdulla Al Mahmood, <i>Vice Chariman</i> Talal Ali Al Zain Khalil Ebrahim Nooruddin Mohammed Ahmed Abdulla (Up to 2 December 2018) Khalid Yousif Abdulrahman Ebrahim Husain Ebrahim Aljassmi Othman Ebrahim Naser Al Askar Muhammad Zarrug Rajab
Office	: Salam Tower, Diplomatic Area PO Box 5240 Manama, Kingdom of Bahrain Telephone 17 546-111, Telefax 17 535-808
Auditors	: KPMG Fakhro

**CONSOLIDATED FINANCIAL STATEMENTS**  
**For the year ended 31 December 2018**

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<b>CONTENTS</b>	<b>Page</b>
Board of Directors report	1 - 2
Sharia'a supervisory board report	3 - 4
Independent auditors' report to the shareholders	5
<b>Consolidated financial statements</b>	
Consolidated statement of financial position	6
Consolidated statement of income	7
Consolidated statement of cash flows	8
Consolidated statement of changes in owners' equity	9
Consolidated statement of sources and uses of good faith qard fund	10
Consolidated statement of sources and uses of zakah and charity fund	11
Notes to the consolidated financial statements	12 - 58

## Board of Directors Report

In the name of Allah, the Most Beneficent. Prayers and Peace be upon the last Apostle and Messenger, His Comrades and Relatives.

On behalf of the Board of Directors, I am privileged to present the annual report and consolidated financial statements of Bahrain Islamic Bank for 2018. As the Bank's Back to Basics strategy finishes its last year, BisB continues to make significant strides in nearly every aspect of the Bank.

The turbulent events throughout the region I spoke about in 2017 have carried forward deep into 2018. Despite that, the Bank has achieved another year of solid performance with a 12% growth in net profits over 2017. Earnings stood at BD 11.4 million, which translates to earnings per share of 10.83 fils compared to 9.65 fils in 2017.

With strict adherence to a prudent risk appetite, financing assets stood at BD 765.8 million compared to BD 740.7 million in 2017.

Technology was the dominant theme in 2018 and is expected to continue well into the future. BisB continues to invest in technology platforms and to strengthen technical capabilities within the Bank. Our most recent investment was in a much-needed business planning management architecture (BPM), which will enable the Bank to adapt to fast-changing technological trends.

Another critical pillar is our people. Our commitment to invest in Bahraini talent continues unabated as we hone the Bank's succession line in preparation of our future leaders.

We expect 2019 to carry similar challenges. However, I remain optimistic about BisB's future and our ability to adapt to fast regulatory and technological changes. We have come a long way in improving nearly every aspect of the bank's operations but there is always much more to be accomplished.

On behalf of the shareholders, the Directors record their grateful thanks and sincere appreciation to His Majesty King Hamad bin Isa Al Khalifa – the King of Bahrain; to His Royal Highness Shaikh Khalifa bin Salman Al Khalifa - the Prime Minister; to His Royal Highness Shaikh Salman bin Hamad Al Khalifa – the Crown Prince, Deputy Supreme Commander and First Deputy Prime Minister. The Directors also express thanks to all Government ministries and authorities – in particular to the Central Bank of Bahrain and the Ministry of Industry, Commerce & Tourism for their invaluable guidance, kind consideration and constant support.

The Directors are grateful for the guidance and counsel of the Bank's Sharia'a Supervisory Board. The committed dedication of BisB's management and staff is also acknowledged, as well as our loyal customers and business partners, for their trust and confidence in Bahrain Islamic Bank.



Dr. Esam Abdulla Fakhro  
Chairman of the Board



## Sharia'a Supervisory Board report

For the year ended on 31/12/2018

In The Name of Allah, most Gracious,  
Most Merciful Peace and Blessings Be Upon His Messenger.

To the shareholders of Bahrain Islamic Bank B.S.C.

Assalam Alaykum Wa Rahmatu Allah Wa Barakatoh.

The Sharia'a Board hereby present the following report on its activities in supervising the Bank's finances and investments from a Sharia perspective for the financial year ending on 31<sup>st</sup> December 2018, in fulfillment to the mandate conferred upon it by BisB's Articles of Association:

- In coordination with the Sharia Coordination and implementation, the Sharia Supervisory Board has monitored the implementation on the Bank's products and its applicable fees and the relevant policies and procedures, in addition to advising and providing fatwas in regards to the finance agreements up to 31st December 2018 to ensure the Bank's adherence to the provisions and principles of Islamic Sharia'a.
- The Sharia'a Supervisory Board believes that ensuring the conformity of Bank's activities and investments with the provisions of Islamic Sharia'a is the sole responsibility of the Management while the Sharia'a Supervisory Board is only responsible for expressing an independent opinion and preparing a report to you.
- We planned with the Sharia'a Internal Audit department to carry out monitoring functions by obtaining all the information and clarifications that were deemed necessary to confirm that the Bank did not violate the principles and provisions of Islamic Sharia'a and Fatwas and decisions of the Sharia'a Board.
- Our supervision constituted of inspection, documenting of policies followed by the Bank on the basis of examining each kind of operation either directly or indirectly by the internal Sharia'a Department in conformity with the Plan and methodology approved by the Sharia'a Board.
- The Sharia'a Internal Audit department performed its mission of auditing the transactions executed by the Bank and submitted its periodic reports to the Sharia'a Supervisory Board, which confirmed the Bank's adherence in its dealings and investments with the Sharia'a Board's fatwas and decisions.
- The 12 reports submitted by Internal Sharia Audit Department to the Sharia'a Supervisory Board included results of auditing the files, contracts, executed deals

Shaikh Dr. A.Latif Mahmood Al Mahmood  
Chairman

Shaikh Mohammed Jaffar Al Juffairi  
Vice Chairman

Shaikh Adnan Abdullah Al Qattan  
Member

Shaikh Dr. Nedham M. Saleh Yacoubi  
Member

Shaikh Dr. Essam Khalaf Al Onazi  
Member

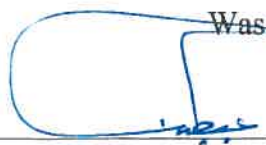


in fulfillment to the Sharia'a Board annual approved audit plan. The Sharia'a Board obtained the requested information and explanations from the departments it deemed necessary to confirm that the Bank did not violate the Sharia principles and Fatwas and decisions of the Sharia'a Board.

- The Sharia Board and its Committees held (16) meetings during the year and issued (98) decisions and fatwas, and approved (80) contracts.
- The Sharia Supervisory Board confirms that it has, along with the Sharia Coordination and implementation Department and Internal sharia Audit Department, fulfilled all the CBB's Sharia Supervisory Governance requirements.
- The Sharia Board has reviewed the financial Statements for the year ended on 31st December 2018, the income statement, the attached notes and the Zakat calculation methods. The Sharia'a Supervisory Board believes that:
  1. All the Financial Statements inspected by the Sharia'a Board conform to what has been approved by the Board, and to the standards issued by the Accounting & Auditing Organization for Islamic Financial Institutions AAOIFI.
  2. Contracts, and transactions conducted by the Bank throughout were in accordance with the standard contracts pre-approved by the Sharia'a Supervisory Board.
  3. The distribution of profit and allocation of losses on investment accounts was in line with the basis and principles approved by the Sharia'a Supervisory Board and in accordance to Islamic Sharia.
  4. Any gains resulted from sources or means prohibited by the provisions and principles of Islamic Sharia'a, have been directed to the Charity and Donations Fund.
  5. Zakah was calculated according to the provisions and principles of Islamic Sharia'a, by the net invested assets method. And the shareholders should pay their portion of Zakah on their shares as stated in the financial report.
  6. The Bank was committed to the Sharia'a standards issued by the Accounting & Auditing Organization for Islamic Financial Institutions (AAOIFI).


We pray that Allah may grant all of us further success and prosperity.

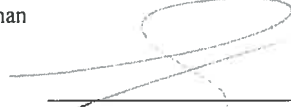
Wassalam Alaykum Wa Rahmatu Allah Wa Barakatoh

  
Shaikh Dr. A.Latif Mahmood Al Mahmood  
Chairman

  
Shaikh Mohammed Jaffar Al Juffairi  
Vice Chairman

  
Shaikh Adnan Abdullah Al Qattan  
Member

  
Shaikh Dr. Nedham M. Saleh Yacoubi  
Member

  
Shaikh Dr. Essam Khalaf Al Onazi  
Member



KPMG Fakhro  
Audit  
12<sup>th</sup> Floor, Fakhro Tower  
PO Box 710, Manama  
Kingdom of Bahrain

Telephone +973 17 224807  
Fax +973 17 227443  
Website: [www.kpmg.com/bh](http://www.kpmg.com/bh)  
CR No. 6220

## INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS

Bahrain Islamic Bank B.S.C.  
Manama, Kingdom of Bahrain

### Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Bahrain Islamic Bank B.S.C. (the "Bank") and its subsidiary (together the "Group") which comprise the consolidated statement of financial position as at 31 December 2018, the consolidated statements of income, cash flows, changes in owners' equity, sources and uses of good faith qard fund and sources and uses of zakah and charity fund for the year then ended, and a summary of significant accounting policies and other explanatory notes.

#### *Respective responsibilities of board of directors and auditors*

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

#### *Basis of opinion*

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

#### *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 2018, and of its consolidated results of operations, its consolidated cash flows, its consolidated changes in owners' equity, its consolidated sources and uses of good faith qard fund, and its consolidated sources and uses of zakah and charity fund for the year then ended in accordance with Financial Accounting Standards issued by the Accounting and Auditing Organisation for Islamic Financial Institutions and the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

### Report on other regulatory requirements

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

- the Bank has maintained proper accounting records and the consolidated financial statements are in agreement therewith;
- the financial information contained in the chairman's report is consistent with the consolidated financial statements;
- we are not aware of any violations during the year of the Commercial Companies Law, the CBB and Financial Institutions Law No. 64 of 2016 (as amended), the CBB Rule Book (Volume 2, applicable provisions of Volume 6 and CBB directives), the CBB Capital Markets Regulations and associated resolutions, the Bahrain Bourse rules and procedures or the terms of the Bank's memorandum and articles of association that would have had a material adverse effect on the business of the Bank or on its financial position; and
- satisfactory explanations and information have been provided to us by management in response to all our requests.

KPMG Fakhro  
Partner Registration No. 100  
24 February 2019




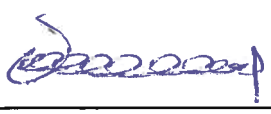

# Bahrain Islamic Bank B.S.C.

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2018

	Note	2018 BD'000	2017 BD'000
<b>ASSETS</b>			
Cash and balances with banks and Central Bank	3	65,437	69,666
Placements with financial institutions	4	137,450	80,845
Financing assets	5	578,953	561,822
Investment securities	6	240,053	258,399
Ijarah Muntahia Bittamleek	8	165,730	164,397
Ijarah rental receivables	8	21,141	14,483
Investment in associates	7	21,643	23,739
Investment in real estate	10	24,284	29,831
Property and equipment	9	13,641	14,270
Other assets	11	11,062	11,195
<b>TOTAL ASSETS</b>		<b>1,279,394</b>	<b>1,228,647</b>
<b>LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS AND OWNERS' EQUITY</b>			
<b>Liabilities</b>			
Placements from financial institutions		114,744	67,872
Placements from non-financial institutions and individuals		7,255	-
Borrowings from financial institutions	12	96,386	101,576
Customers' current accounts		133,244	131,666
Other liabilities	13	24,025	11,507
<b>Total Liabilities</b>		<b>375,654</b>	<b>312,621</b>
<b>Equity of Investment Accountholders</b>	14	<b>785,991</b>	<b>793,756</b>
<b>Owners' Equity</b>			
Share capital	15	106,406	101,339
Treasury shares	15	(892)	(864)
Shares under employee share incentive scheme		(391)	(498)
Share premium		120	98
Reserves		12,506	22,195
<b>Total Owners' Equity</b>		<b>117,749</b>	<b>122,270</b>
<b>TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS AND OWNERS' EQUITY</b>		<b>1,279,394</b>	<b>1,228,647</b>

The consolidated financial statements were approved by the Board of Directors on 24 February 2019 and signed on its behalf by:

		
Dr. Esam Abdulla Fakhro Chairman	Brig. Ebrahim Abdulla Al Mahmood Vice Chairman	Hassan Amin Jarrar Chief Executive Officer





# Bahrain Islamic Bank B.S.C.

## CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2018

	Note	2018 BD'000	2017 BD'000
<b>INCOME</b>			
Income from financing	18	43,110	40,507
Income from investment in Sukuk		10,829	6,808
<b>Total income from jointly financed assets</b>		<b>53,939</b>	<b>47,315</b>
Return on equity of investment accountholders		(41,162)	(36,010)
Group's share as Mudarib		27,223	24,646
Net return on equity of investment accountholders	14.5	(13,939)	(11,364)
<b>Group's share of income from jointly financed assets (both as mudarib and investor)</b>		<b>40,000</b>	<b>35,951</b>
Expense on placements from financial institutions		(2,043)	(1,018)
Expense on placements from non-financial institutions and individuals		(57)	-
Expense on borrowings from financial institutions		(4,034)	(2,032)
Fee and commission income		7,547	7,642
Income from investment securities	19	216	513
Income from investment in real estate	20	(556)	213
Share of results of associates, net	7	86	(1,103)
Other income	21	4,372	2,740
<b>Total income</b>		<b>45,531</b>	<b>42,906</b>
<b>EXPENSES</b>			
Staff costs		12,588	12,611
Depreciation	9	1,473	1,570
Other expenses	22	11,194	12,387
<b>Total expenses</b>		<b>25,255</b>	<b>26,568</b>
<b>Profit before impairment allowances</b>		<b>20,276</b>	<b>16,338</b>
Impairment allowance, net	23	(8,895)	(6,197)
<b>PROFIT FOR THE YEAR</b>		<b>11,381</b>	<b>10,141</b>
<b>BASIC AND DILUTED EARNINGS PER SHARE (fls)</b>	25	<b>10.83</b>	<b>9.65</b>

  
 Dr. Esam Abdulla Fakhro  
 Chairman

  
 Brig. Ebrahim Abdulla Al Mahmood  
 Vice Chairman

  
 Hassan Amin Jarrar  
 Chief Executive Officer

# Bahrain Islamic Bank B.S.C.

## CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2018

		2018 BD'000	2017 BD'000
	Note		
<b>OPERATING ACTIVITIES</b>			
Profit for the year		11,381	10,141
Adjustments for non-cash items:			
Depreciation	9	1,473	1,570
Impairment allowance, net	23	8,895	6,197
Loss on sale of investment in associates		-	83
Impairment on investment in real estate	20	204	119
Loss on sale of investment in real estate	20	531	39
Gain on sale of investment securities		-	(3)
Gain on foreign exchange revaluation		29	-
Recoveries from written off accounts		(3,472)	-
Share of results of associates, net	7	(86)	1,103
<b>Operating profit before changes in operating assets and liabilities</b>		<b>18,955</b>	<b>19,249</b>
Working capital adjustments:			
Mandatory reserve with Central Bank of Bahrain		100	(1,440)
Financing assets		(34,485)	(57,605)
Ijarah Muntahia Bittamleek		(8,359)	(18,808)
Other assets		(693)	739
Customers' current accounts		1,578	(800)
Other liabilities		11,729	(3,596)
Placements from financial institutions		44,719	(24,582)
Placements from non-financial institutions and individuals		7,255	-
Equity of investment accountholders		(7,765)	139,440
<b>Net cash from operating activities</b>		<b>33,034</b>	<b>52,597</b>
<b>INVESTING ACTIVITIES</b>			
Capitalized expenditure of investment in real estate		-	(28)
Disposal of investment in real estate		3,480	314
Disposal of investment in associates		-	1,348
Purchase of investment securities		(75,590)	(119,546)
Purchase of property and equipment		(845)	(1,193)
Disposal of property and equipment		1	-
Proceeds from disposal of investment securities		95,504	3,538
<b>Net cash from / (used in) investing activities</b>		<b>22,550</b>	<b>(115,567)</b>
<b>FINANCING ACTIVITIES</b>			
Purchase of treasury shares		-	(301)
(Repayment) / drawdown of borrowings from financial institutions		(5,190)	90,156
Dividends paid		(72)	(4,827)
<b>Net cash (used in) / from financing activities</b>		<b>(5,262)</b>	<b>85,028</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>		<b>50,322</b>	<b>22,058</b>
Cash and cash equivalents at 1 January		112,794	90,736
<b>CASH AND CASH EQUIVALENTS AT 31 DECEMBER</b>		<b>163,116</b>	<b>112,794</b>
Cash and cash equivalents comprise of:			
Cash on hand	3	15,318	13,042
Balances with CBB, excluding mandatory reserve deposits	3	242	3,654
Balances with banks and other financial institutions excluding restricted balances	3	10,106	15,253
Placements with financial institutions with original maturities less than 90 days	4	137,450	80,845
		<b>163,116</b>	<b>112,794</b>

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

# Bahrain Islamic Bank B.S.C.

## CONSOLIDATED STATEMENT OF CHANGES IN OWNERS' EQUITY

For the year ended 31 December 2018

	Shares under employee share			Reserves						Total owners' equity BD'000
	Share capital BD'000	Treasury shares BD'000	incentive scheme BD'000	Share premium BD'000	Statutory reserve BD'000	Real estate		Investment securities		
						fair value reserve BD'000	fair value reserve BD'000	fair value reserve BD'000	Retained earnings BD'000	
Balance at 1 January 2018	101,339	(864)	(498)	98	2,977	6,145	745	12,328	22,195	122,270
Impact of adopting FAS 30 (note 3a)	-	-	-	-	-	-	-	(13,943)	(13,943)	(13,943)
Impact of adopting FAS 30 by associate (note 3a)	-	-	-	-	-	-	-	(350)	(350)	(350)
Balance at 1 January 2018 (Restated)	101,339	(864)	(498)	98	2,977	6,145	745	(1,965)	7,902	107,977
Profit for the year	-	-	-	-	-	-	-	11,381	11,381	11,381
Bonus shares declared for 2017	5,067	(28)	(34)	(35)	-	-	-	(4,970)	(4,970)	-
Transfer to zakah fund	-	-	-	-	-	-	-	(265)	(265)	(265)
Transfer to charity fund	-	-	-	-	-	-	-	(200)	(200)	(200)
Shares allocated during the year	-	-	141	57	-	-	-	-	-	198
Net movement in investment securities fair value reserve	-	-	-	-	-	-	(27)	-	(27)	(27)
Net movement in real estate fair value reserve	-	-	-	-	-	(1,315)	-	-	(1,315)	(1,315)
Transfer to statutory reserve	-	-	-	-	1,138	-	-	(1,138)	-	-
Balance at 31 December 2018	106,406	(892)	(391)	120	4,115	4,830	718	2,843	12,506	117,749
Balance at 1 January 2017	101,339	(563)	(604)	56	1,963	5,361	531	8,389	16,244	116,472
Profit for the year	-	-	-	-	-	-	-	10,141	10,141	10,141
Dividends declared for 2016	-	-	-	-	-	-	-	(5,051)	(5,051)	(5,051)
Transfer to zakah fund	-	-	-	-	-	-	-	(137)	(137)	(137)
Purchase of treasury shares	-	(301)	-	-	-	-	-	-	-	(301)
Shares allocated during the year	-	-	106	42	-	-	-	-	-	148
Net movement in investment securities fair value reserve	-	-	-	-	-	-	214	-	214	214
Net movement in real estate fair value reserve	-	-	-	-	-	784	-	-	784	784
Transfer to statutory reserve	-	-	-	-	1,014	-	-	(1,014)	-	-
Balance at 31 December 2017	101,339	(864)	(498)	98	2,977	6,145	745	12,328	22,195	122,270

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

**Bahrain Islamic Bank B.S.C.**

**CONSOLIDATED STATEMENT OF SOURCES AND USES OF GOOD FAITH  
QARD FUND**

For the year ended 31 December 2018

	<i><b>Qard Hasan receivables BD'000</b></i>	<i><b>Funds available for Qard Hasan BD'000</b></i>	<i><b>Total BD'000</b></i>
<b>Balance at 1 January 2018</b>	<b>71</b>	<b>57</b>	<b>128</b>
Uses of Qard fund			
Marriage	<b>10</b>	<b>(10)</b>	-
Others (Waqf)	<b>26</b>	<b>(26)</b>	-
<b>Total uses during the year</b>	<b>36</b>	<b>(36)</b>	-
Repayments	<b>(36)</b>	<b>36</b>	-
<b>Balance at 31 December 2018</b>	<b>71</b>	<b>57</b>	<b>128</b>
Balance at 1 January 2017	65	63	128
Uses of Qard fund			
Marriage	13	(13)	-
Others (Waqf)	24	(24)	-
Total uses during the year	37	(37)	-
Repayments	(31)	31	-
Balance at 31 December 2017	71	57	128
	<b>2018 BD'000</b>	<b>2017 BD'000</b>	
<b>Sources of Qard fund</b>			
Contribution by the Bank	<b>125</b>	125	
Donation	<b>3</b>	3	
	<b>128</b>	128	

**Bahrain Islamic Bank B.S.C.****CONSOLIDATED STATEMENT OF SOURCES AND USES OF ZAKAH AND CHARITY FUND**

For the year ended 31 December 2018

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
<b>Sources of zakah and charity funds</b>		
Undistributed zakah and charity funds at the beginning of the year	<b>259</b>	222
Non-Islamic income / late payment fee	<b>374</b>	510
Contributions by the Bank for zakah	<b>265</b>	137
Contributions by the Bank for donations	<b>200</b>	-
<b>Total sources of zakah and charity funds during the year</b>	<b>1,098</b>	869
<b>Uses of zakah and charity funds</b>		
Philanthropic societies	<b>366</b>	253
Aid to needy families	<b>381</b>	357
Islamic events	<b>37</b>	-
<b>Total uses of funds during the year</b>	<b>784</b>	610
<b>Undistributed zakah and charity funds at the end of the year</b>	<b>314</b>	259

**1 REPORTING ENTITY**

Bahrain Islamic Bank B.S.C. (the "Bank") was incorporated in the Kingdom of Bahrain in 1979 by Amiri Decree No.2 of 1979 and registered with the Ministry of Industry and Commerce ("MOIC") under Commercial Registration (CR) number 9900, to carry out banking and other financial trading activities in accordance with the teachings of Islam (Shari'a). The Bank operates under an Islamic retail banking license issued by the Central Bank of Bahrain ("CBB"). The Bank's Shari'a Supervisory Board is entrusted to ensure the Bank's adherence to Shari'a rules and principles in its transactions and activities. The Bank is listed on the Bahrain Bourse.

The Bank's registered office is at Building 722, Road 1708, Block 317, Manama, Kingdom of Bahrain.

The Bank has nine branches (2017: eight), all operating in the Kingdom of Bahrain.

The consolidated financial statements include the results of the Bank and its wholly owned subsidiary (together the "Group"). The Bank holds 100% of the share capital of Abaad Real Estate Company B.S.C. (c).

Abaad Real Estate Company B.S.C. (c) ("Abaad")

Abaad was incorporated in the Kingdom of Bahrain on 8 April 2003 with an authorised and fully paid-up share capital of BD 25 million. Abaad started operations in 2007. The main activity of Abaad is investment in real estate (in accordance with the Islamic Shari'a rules and principles).

The consolidated financial statements were authorised for issue in accordance with a resolution of the Board of Directors issued on 24 February 2019.

**a. Basis of preparation**

The consolidated financial statements have been prepared on a historical cost basis, except for "investment in real estate" and "equity type instruments carried at fair value through equity" that have been measured at fair value.

The preparation of consolidated financial statements requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. Estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected. Management believes that the underlying assumptions are appropriate and the Group's consolidated financial statements therefore present the financial position and results fairly. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in note 2.bb.

The consolidated financial statements have been presented in Bahraini Dinars ("BD"), which is also the functional currency of the Group's operations. All the values are rounded to the nearest BD thousand except when otherwise indicated.

**b. Statement of Compliance**

The consolidated financial statements are prepared in accordance with the Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"), and the Bahrain Commercial Companies Law. In accordance with the requirements of AAOIFI, for matters for which no AAOIFI standard exists, the Group uses guidance from the relevant International Financial Reporting Standards ("IFRS") issued by International Accounting Standards Board.

**2 SIGNIFICANT ACCOUNTING POLICIES**

The significant accounting policies applied in the preparation of these consolidated financial statements are set out below. These accounting policies have been consistently applied by the Group and are consistent with those used in the previous years except for changes arising from adoption of FAS 30 as set out below.

**a. New standards, amendments, and interpretations**

*New standards, amendments, and interpretations issued and effective:*

There are no AAOIFI accounting standards or interpretations that are effective for the first time for the financial year beginning on or after 1 January 2018 that would be expected to have a material impact on the Group.

## 2 SIGNIFICANT ACCOUNTING POLICIES (continued)

### a. New standards, amendments, and interpretations (continued)

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

*Early adoption of FAS 30*

*FAS 30 – Impairment, credit losses and onerous commitments*

AAOIFI has issued FAS 30 Impairment, credit losses and onerous commitments with effective date of 1 January 2020 with early adoption permitted. FAS 30 replaces FAS 11 Provisions and reserves and parts of FAS 25 Investment in Sukuk, shares and similar instruments that deals with impairment. The Group early adopted the standard as of 1 January 2018 as mandated by CBB. The objective of this standard is to establish the principles of accounting and financial reporting for the impairment and credit losses on various Islamic financing, investment and certain other assets of Islamic financial institutions (the institutions), and provisions against onerous commitments enabling in particular the users of financial statements to fairly assess the amounts, timing and uncertainties with regard to the future cash flows associated with such assets and transactions.

FAS 30 classifies assets and exposures into three categories based on the nature of risks involved (i.e. credit risk and other risks) and prescribes three approaches for assessing losses for each of these categories of assets 1) Credit losses approach, 2) Net Realizable Value approach ("NRV") and 3) Impairment approach.

For the purpose of the standard, the assets and exposures shall be categorized, as under:

i. Assets and exposures subject to credit risk (subject to credit losses approach):

- Receivables; and

- Off-balance sheet exposures;

ii. Inventories (subject to net realizable value approach); and

iii. Other financing and investment assets and exposures subject to risks other than credit risk (subject to impairment approach) , excluding inventories.

Credit losses approach for receivables and off balance sheet exposures uses a dual measurement approach, under which the loss allowance is measured as either a 12-month expected credit loss or a lifetime expected credit loss.

**Expected Credit Losses (ECL)**

FAS 30 introduces the credit losses approach with a forward-looking 'expected credit loss' model. The new impairment model will apply to exposures which are subject to credit risk. A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining criteria for Significant Increase in Credit Risk (SICR);
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Identifying groups of similar financial instruments for the purpose of measuring ECL.

### *Changes in Accounting Policies*

The key changes to the Group's accounting policies resulting from the adoption of FAS 30 are summarised in note 2a (i). As permitted by the transitional provisions of FAS 30, the Group elected not to restate comparative figures. Any adjustments to the carrying amounts of exposures subject to credit risk as at the date of transition were recognized in the opening balance of retained earnings at 1 January 2018. Since the comparative financial information has not been restated, the accounting policies in respect of these items for comparative periods are based on respective standards as disclosed in the audited financial statements as of and for the year ended 31 December 2017.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)****a. New standards, amendments, and interpretations (continued)***(i) Impact of adopting FAS 30*

Disclosures of FAS 30 transition impact is set out below:

The following table reconciles the carrying amounts of exposures subject to credit risk under FAS 11 to the carrying amounts under FAS 30 as at 1 January 2018:

	<i>Original carrying amount under FAS 11</i>	<i>Re- measure ment*</i>	<i>New carrying amount under FAS 30</i>
	BD'000		
Cash and balances with banks and Central Bank	69,666	-	69,666
Placements with financial institutions	80,845	(3)	80,842
Financing Assets - net	561,822	(12,031)	549,791
Investment in sukuk	227,906	(96)	227,810
Ijarah Muntahia Bittamleek & Ijarah rental receivables	178,880	(1,142)	177,738
Other receivables	1,991	(60)	1,931
Commitments	148,540	(611)	147,929
	<b>1,269,650</b>	<b>(13,943)</b>	<b>1,255,707</b>

\*Re-measurement is due to increase in impairment allowance due to change from incurred to expected credit loss (ECL).

The following table shows the carrying amounts of exposures subject to credit risk as of 1 January 2018 by stage:

	<i>Stage 1</i>	<i>Stage 2</i>	<i>Stage 3</i>	<i>Total</i>
	BD'000			
Cash and balances with banks and Central Bank	69,666	-	-	69,666
Placements with financial institutions	80,842	-	-	80,842
Financing Assets - net	441,746	96,007	12,038	549,791
Investment in sukuk	226,741	-	1,069	227,810
Ijarah Muntahia Bittamleek & Ijarah rental receivables	154,108	9,914	13,716	177,738
Other receivables	-	1,931	-	1,931
Commitments	143,416	4,506	7	147,929
	<b>1,116,519</b>	<b>112,358</b>	<b>26,830</b>	<b>1,255,707</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)****a. New standards, amendments, and interpretations (continued)***(i) Impact of adopting FAS 30 (continued)*

The following table reconciles the impairment allowance recorded under FAS 11 to that of FAS 30 as at 1 January 2018:

	31 December 2017 (FAS 11)	Re- measur- ment	1 January 2018 (FAS 30)
	BD'000		
Placements with financial institutions	-	3	3
Financing assets	15,167	12,031	27,198
Investment in sukuk	11,481	96	11,577
Ijarah Muntahia Bittamleek & Ijarah rental receivables	13,175	1,142	14,317
Investment in associates	2,830	-	2,830
Investment in equity and funds	8,638	-	8,638
Other receivables	-	60	60
Commitments*	-	611	611
	<b>51,291</b>	<b>13,943</b>	<b>65,234</b>

\* Disclosed as part of other liabilities.

*(ii) Impact on owners equity*

	<b>Owners equity</b>
	<b>BD'000</b>
Balance as at 31 December 2017 (as previously reported)	122,270
Recognition of expected credit losses under FAS 30	(13,943)
Impact of adopting FAS 30 by associate	(350)
<b>Opening balance as at 1 January 2018 (restated)</b>	<b>107,977</b>

**b. Basis of consolidation**

Subsidiaries are all entities (including special purpose entities) controlled by the Group. Control exists when the Group has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. Subsidiaries are consolidated from the date on which control is transferred to the Group to the date that control ceases.

The financial statements of the subsidiaries are prepared for the same reporting year as the Group, using consistent accounting policies.

All intra-group balances, income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full.

**c. Cash and cash equivalents**

For the purpose of the consolidated cash flows statement, "cash and cash equivalents" consist of cash on hand, balances with the Central Bank of Bahrain excluding mandatory reserve deposits, balances with banks and other financial institutions and placements with financial institutions with original maturities of 90 days or less when acquired.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**d. Placements with and borrowings from financial institutions**

*Placements with financial institutions*

Placements with financial institutions comprise commodity Murabaha receivables and Wakala receivables. Commodity Murabaha receivables are stated at amortised cost net of deferred profits and provision for impairment, if any. Wakala receivables are stated at amortised cost less provision for impairment, if any.

*Borrowings from financial institutions*

Borrowings from financial institutions comprise borrowings obtained through murabaha contract recognized on the origination date and carried at amortized cost.

**e. Financing assets**

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

**f. Murabaha financing**

Murabaha financing consist mainly of deferred sales transactions which are stated net of deferred profits and provisions for impairment, if any.

Murabaha financing are sales on deferred terms. The Group arranges a Murabaha transaction by buying a commodity (which represents the object of the Murabaha) and then resells this commodity to a Murabeh (beneficiary) after computing a margin of profit over cost. The sale price (cost plus profit margin) is repaid in instalments by the Murabeh over the agreed period.

**g. Musharaka financing**

Musharaka financing are stated at the fair value of consideration given less impairment, if any.

Musharaka financing are a form of capital partnership. Musharaka financing capital provided by the Group at inception in kind (if other than cash) is measured at the fair value of the assets. If the valuation of the assets results in a difference between fair value and book value, such difference is recognised as profit or loss to the Group.

**h. Investment securities**

Investment securities comprise debt type instruments carried at amortised cost and equity type instruments carried at fair value through equity.

All investments securities, are initially recognised at fair value, being the value of the consideration given including transaction costs directly attributable to the acquisition.

*Debt type instruments carried at amortised cost*

These are investments which have fixed or determinable payments of profit and capital. Subsequent to initial recognition, these are measured at amortised cost using the effective profit rate method less impairment, if any. Any gain or loss on such instruments is recognised in the consolidated income statement when the instruments are de-recognised or impaired.

*Equity type instruments carried at fair value through equity*

Equity-type instruments are investments that do not exhibit features of debt-type instruments and include instruments that evidence residual interest in the assets of entity after reducing all its liabilities. On initial recognition, equity-type instruments that are not designated to fair value through income statement are classified as investments at fair value through equity.

Subsequent to acquisition, these are remeasured at fair value, with unrealised gains and losses recognised in a separate component of equity until the investment is derecognised or the investment is considered as impaired. On derecognition or impairment, the cumulative gain or loss previously recorded in equity is recognised in the consolidated income statement for the year.

Impairment losses on equity type instruments carried at fair value through equity are not reversed through the consolidated income statement and increases in their fair value after impairment are recognised directly in owners' equity.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**i. Measurement principles**

*Fair value measurement*

For investments traded in organised financial markets, fair value is determined by reference to quoted market bid prices at the close of business on the reporting date.

For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another instrument, which is substantially the same or is based on the assessment of future cash flows. The cash equivalent values are determined by the Group at current profit rates for contracts with similar terms and risk characteristics.

Investments classified at fair value through equity where there is no quoted price or the Group is unable to determine a reliable measure of fair value on a continuing basis are stated at cost less impairment allowances.

*Amortised cost*

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

**j. Investment in associates**

Associates are all entities in which the Group holds, between 20% and 50% of the voting rights and exercises significant influence, but not control or joint control, over the financial and operating policies of the entities. Investment in associates are accounted for using the equity method of accounting.

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

The Group determines at each reporting date whether there is any objective evidence that the investments in associates are impaired. If this is the case the Group calculates the amount of impairment as being the difference between the recoverable amount of the associates and the carrying value and recognises this amount in the consolidated income statement.

Accounting policies of the associates are consistent with the policies adopted by the Group.

**k. Ijarah Muntahia Bittamleek**

Ijarah Muntahia Bittamleek are stated at cost less accumulated depreciation and any impairment in value. Under the terms of lease, the legal title of the asset passes to the lessee at the end of the lease term, provided that all lease installments are settled. Depreciation is calculated on a straight line basis at rates that systematically reduce the cost of the leased assets over the period of the lease. The Group assesses at each reporting date whether there is objective evidence that the assets acquired for leasing are impaired. Impairment losses are measured as the difference between the carrying amount of the asset (including lease rental receivables) and the estimated recoverable amount. Impairment losses, if any, are recognised in the income statement.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)****l. Investment in real estate**

Properties held for rental, or for capital appreciation purposes, or both, are classified as investment in real estate. Investments in real estate are initially recorded at cost, being the fair value of the consideration given and acquisition charges associated with the property. Subsequent to initial recognition, investments in real estate are re-measured to fair value and changes in fair value (only gains) are recognised in a property fair value reserve in the consolidated statement of changes in owners' equity.

Losses arising from changes in the fair values of investment in real estate are firstly adjusted against the property fair value reserve to the extent of the available balance and then the remaining losses are recognised in the consolidated income statement. If there are unrealised losses that have been recognised in the consolidated income statement in previous financial periods, the current period unrealised gain shall be recognised in the consolidated income statement to the extent of crediting back such previous losses in the consolidated income statement. When the property is disposed of, the cumulative gain previously transferred to the property fair value reserve, is transferred to the consolidated income statement.

**m. Property and equipment**

Property and equipment is recognised at cost. The cost of additions and major improvements are capitalised; maintenance and repairs are charged to the consolidated income statement as incurred. Depreciation is provided on the straight-line basis over the estimated useful lives of the assets as follows;

Buildings	25 to 35 years
Fixtures and fittings	5 years
Equipment	5 years
Furniture	5 years

**n. Equity of investment accountholders**

Equity of investment account holders are funds held by the Group in unrestricted investment accounts, which it can invest at its own discretion. The investment account holder authorises the Group to invest the account holders' funds in a manner which the Group deems appropriate without laying down any restrictions as to where, how and for what purpose the funds should be invested. The Group charges management fee (Mudarib fees) to investment account holders. Of the total income from investment accounts, the income attributable to customers is allocated to investment accounts after setting aside provisions, reserves (profit equalisation reserve and investment risk reserve) and deducting the Group's share of income as a Mudarib. The allocation of income is determined by the management of the Group within the allowed profit sharing limits as per the terms and conditions of the investment accounts. Administrative expenses incurred in connection with the management of the funds are borne directly by the Group and are not charged separately to investment accounts. Only profits earned on pool of assets funded from IAH are allocated between the owners' equity and IAH.

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

**o. Investment risk reserve**

Investment risk reserves are amounts appropriated out of the income of equity of investment accountholders, after allocating the Mudarib share, in order to cater for future losses for equity of investment accountholders.

**p. Profit equalisation reserve**

The Group appropriates a certain amount in excess of the profit to be distributed to equity of investment accountholders after taking into consideration the Mudarib share of income. This is used to maintain a certain level of return on investment for equity of investment accountholders.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**q. Zakah**

Zakah is calculated on the Zakah base of the Group in accordance with FAS 9 issued by AAOIFI using the net invested funds method. Zakah is paid by the Group based on the consolidated figures of statutory reserve, general reserve and retained earning balances at the beginning of the year. The remaining Zakah is payable by individual shareholders. Payment of Zakah on equity of investment accountholders and other accounts is the responsibility of investment accountholders.

**r. Provisions**

Provisions are recognised when the Group has a present obligation (legal or constructive) arising from 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 obligation.

**s. Dividends and board remuneration**

Dividends are recognised as liabilities in the year in which they are declared / approved by the shareholders.

**t. Derecognition of financial assets and liabilities**

*Financial assets*

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- the right to receive cash flows from the asset has expired;
- the Group has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the assets, but has transferred control of the asset; or
- the Group retains the right to receive cash flows from the asset, but has assumed an obligation to pay them in full without material delay to a third party under a 'pass through' arrangement.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the Group's continuing involvement in the asset.

*Financial liabilities*

A financial liability is derecognised when the obligation specified in the contract is discharged, cancelled or expired.

**u. Treasury shares**

These are own equity instruments of the Group which are reacquired through its own broker. Treasury shares are deducted from equity and accounted for at weighted average cost. Consideration paid or received on the purchase or sale of the Group's own equity instruments is recognised directly in equity. No gain or loss is recognised in consolidated income statement on the purchase, sale, issue or cancellation of own equity instruments.

**v. Earnings prohibited by Shari'a**

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

**w. Offsetting**

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

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**x. Income recognition**

*Murabaha and Wakala*

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

*Musharaka*

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

*Sukuk*

Income from Sukuk is recognised using the effective profit rate over the term of the instrument.

*Placements with financial institutions*

Income on placements from financial institutions is recognised proportionately over the period of the contract based on the principal amounts outstanding and the profit agreed with clients.

*Ijarah Muntahia Bittamleek*

Income from Ijarah Muntahia Bittamleek is recognised proportionately over the lease term.

*Dividend income*

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

*Fee and commission income*

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

**y. Foreign currencies**

Transactions in foreign currencies are recorded at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated into Bahraini Dinars at the rate of exchange ruling at the consolidated statement of financial position date. All differences are taken to the consolidated income statement.

Translation gains or losses on non-monetary items carried at fair value are included in owners' equity as part of the fair value adjustment.

**z. Impairment of exposures subject to credit risk**

**(a) Policy applicable from 1 January 2018**

The Group recognizes loss allowances based ECL on the following:

- (i) Bank balances and placements with banks;
- (ii) Financing assets;
- (iii) Ijarah muntahia bittamleek & rental receivables;
- (iv) Investment in Sukuk - debt type securities at amortised cost;
- (v) Financial guarantee contracts issued; and
- (vi) Commitments to finance.



**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**z. Impairment of exposures subject to credit risk (continued)**

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

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

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

The Group assumes that the credit risk on an exposure subject to credit risk has increased significantly if it is more than 30 days past due.

The Group considers an exposures subject to credit risk to be in default when:

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

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

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

**Stage 1: 12-months ECL**

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

**Stage 2: Lifetime ECL - not credit impaired**

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

**Stage 3: Lifetime ECL - credit impaired**

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

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

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2. Impairment of exposures subject to credit risk (continued)**

*ii) Measurement of ECL*

ECL is a probability-weighted estimate of credit losses. It is measured as follows:

- (i) Exposures subject to credit risk that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive);
- (ii) Exposures subject to credit risk that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- (iii) Undrawn commitments to finance: as the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and
- (iv) Financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group expects to recover.

*iii) Restructured exposures*

If the terms of an exposures subject to credit risk are renegotiated or modified or an existing exposures subject to credit risk is replaced with a new one due to financial difficulties of the borrower, the exposures subject to credit risk should be derecognized and ECL is calculated using the cash shortfalls from the existing exposures subject to credit risk that are discounted from the expected date of derecognition to the reporting date using the original effective profit rate of the existing exposures subject to credit risk.

*iv) Credit-impaired exposures*

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

Evidence that an exposure subject to credit risk is credit-impaired includes the following observable data:

- (i) significant financial difficulty of the borrower or issuer;
- (ii) a breach of contract such as a default;
- (iii) the restructuring of a financing facility by the Group on terms that the Group would not consider
- (iv) it is becoming probable that the borrower will enter bankruptcy or other financial reorganization.

*v) Presentation of allowance for ECL in the statement of financial position*

Loss allowances for ECL are presented in the statement of financial position as a deduction from gross carrying amount of exposures subject to credit risk.

*vi) Write-off*

Exposures subject to credit risk are written off either partially or in their entirety only when the Group has stopped pursuing the recovery. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to other income.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**z. Impairment of exposures subject to credit risk (continued)**

**(b) Policy applicable before 1 January 2018**

*Impairment of financial assets at amortized cost*

An assessment is made at each consolidated financial position date to determine whether there is objective evidence that a specific financial asset or a group of financial assets may be impaired. Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of financing facility or advance by the Group on the terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrower or issuers in the group or economic conditions that correlate with the defaults in the group. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the assessment by the Group of the estimated cash equivalent value, is recognised in the consolidated income statement. Specific provisions are created to reduce all impaired financial contracts to their realisable cash equivalent value. Financial assets are written off only in circumstances where effectively all possible means of recovery have been exhausted.

**aa. Equity investments classified at Fair Value Through Equity (FVTE) - Applicable to 2017 and 2018**

For equity-type securities carried at fair value through equity, a significant or prolonged decline in fair value below its cost is an objective evidence of impairment. If such evidence exists, impairment is measured as the difference between acquisition cost and current fair value, less any impairment loss previously recognised in the consolidated income statement.

For equity type instruments carried at fair value through equity, impairment losses recognised in the consolidated income statement are subsequently reversed through equity.

For investments classified at fair value through equity but 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 carried value of the investment.

**bb. Use of estimates and judgements in preparation of the consolidated financial statements**

In the process of applying the Group's accounting policies, management has made estimates and judgements in determining the amounts recognised in the consolidated financial statements. The most significant use of judgements and estimates are as follows:

**(i) Applicable from 1 January 2018:**

*Impairment of exposures subject to credit risk*

- Establishing the criteria for determining whether credit risk on exposures subject to credit risk has increased significantly since initial recognition, determining methodology for incorporating forward looking information into measurement of ECL and selection and approval of models used to measure ECL is set out in Note 2(z) and Note 28.
- Impairment on Ijara rental receivables: key assumptions used in estimating recoverable cash flows is set out in Note 2 (z).
- Determining inputs into ECL measurement model including incorporation of forward looking information is set out in Note 2 (z) and Note 28.

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**bb. Use of estimates and judgements in preparation of the consolidated financial statements (continued)**

**(ii) Applicable before 1 January 2018:**

*Impairment of financing assets*

Financing assets are evaluated for impairment on a basis described in accounting policy, [refer to note 2.z]. 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.

For the purposes of a collective evaluation of impairment, financing assets are grouped on the basis of similar credit risk characteristics (that is, on the basis of the Group's grading process that considers asset type, collateral type, past-due status and other relevant factors). The methodology and assumptions used for the grading process and estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

**(iii) Applicable for 2017 and 2018:**

*Going concern*

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

*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 debt type instruments carried at fair value through equity or amortised cost, or equity-type instruments carried at fair value through equity or fair value through income statement. The classification of each investment reflects the management's intention in relation to each investment and is subject to different accounting treatments based on such classification [refer note 2.h].

*Impairment of equity investments*

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

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

For unquoted equity investments carried at cost, 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. In making this judgment, the Group evaluates among other factors, evidence of a deterioration in the financial health of the investee, and operational and financing cash flows. It is reasonably possible, based on existing knowledge, that the current assessment of impairment could require a material adjustment to the carrying amount of the investments within the next financial year due to significant changes in the assumptions underlying such assessments.

**cc. 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.

**dd. Customers' current accounts**

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

**2 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**ee. Employees' benefits**

*i. Short-term benefits*

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus as 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*

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

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

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

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

*iii. Share based employee incentive scheme*

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

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

**ff. Financial guarantees**

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

**gg. Repossessed assets**

In certain circumstances, property is repossessed following the foreclosure on financing facilities that are in default. Repossessed properties are measured at the lower of carrying amount and fair value less costs to sell and reported within 'other assets'.

**hh. Statutory reserve**

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

**ii. URIA protection scheme**

Investment accounts held within the Group's Bahrain operations are covered by the regulation protecting URIA issued by the Central Bank of Bahrain in accordance with Resolution No (34) of 2010. The scheme applies to all eligible accounts held with Bahrain offices of the Bank subject to specific exclusions, maximum total amount entitled and other regulations governing the establishment of a URIA Protection Scheme and a URIA Protection Board.

**3 CASH AND BALANCES WITH BANKS AND CENTRAL BANK**

	<b>2018</b>	<b>2017</b>
	<b>BD'000</b>	<b>BD'000</b>
Cash on hand	<b>15,318</b>	13,042
Balances with CBB, excluding mandatory reserve deposits	<b>242</b>	3,654
Balances with banks and other financial institutions	<b>14,772</b>	17,765
	<b>30,332</b>	34,461
Mandatory reserve with CBB	<b>35,105</b>	35,205
	<b>65,437</b>	69,666

The mandatory reserve with CBB is not available for use in the day-to-day operations.

Balances with banks and other financial institutions include an amount of BD 4,666 thousand (2017: BD 2,512 thousand) which is not available for use in the day-to-day operations.

**4 PLACEMENTS WITH FINANCIAL INSTITUTIONS**

	<b>2018</b>	<b>2017</b>
	<b>BD'000</b>	<b>BD'000</b>
Commodity Murabaha	<b>54,975</b>	53,519
Deferred profits	<b>(6)</b>	(5)
	<b>54,969</b>	53,514
Wakala	<b>82,486</b>	27,331
	<b>137,455</b>	80,845
Impairment allowance	<b>(5)</b>	-
	<b>137,450</b>	80,845

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**5 FINANCING ASSETS**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Murabaha (note 5.1)	<b>481,612</b>	455,501
Musharaka (note 5.2)	<b>97,341</b>	106,321
	<b>578,953</b>	<b>561,822</b>

**5.1 Murabaha**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Tasheel	<b>217,622</b>	206,855
Tawarooq	<b>214,778</b>	195,474
Altamweel Almaren	<b>82,128</b>	64,912
Letters of credit refinance	<b>32,819</b>	27,229
Motor vehicles Murabaha	<b>7,858</b>	9,625
Credit cards	<b>18,596</b>	17,992
Others	<b>46</b>	58
	<b>573,847</b>	522,145
Qard fund	<b>71</b>	71
<b>Gross receivables</b>	<b>573,918</b>	522,216
Deferred profits	<b>(65,253)</b>	(52,695)
Impairment allowance	<b>(27,053)</b>	(14,020)
	<b>481,612</b>	455,501

Non-performing Murabaha financing outstanding as of 31 December 2018 amounted to BD 71,265 thousand (2017: BD 34,436 thousand).

The Group considers the promise made in the Murabaha to the purchase orderer as obligatory.

The composition of the Murabaha financing portfolio net of deferred profit and before provision for impairment by sector is as follows:

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Commercial	<b>120,762</b>	95,128
Financial institutions	<b>26,310</b>	32,693
Others including retail	<b>361,593</b>	341,700
	<b>508,665</b>	469,521

The Group exposures of Murabaha financing portfolio is concentrated in the Middle East.

**5.2 Musharaka**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Musharaka in real estate	<b>100,127</b>	107,468
Provision for impairment	<b>(2,786)</b>	(1,147)
	<b>97,341</b>	106,321

Non-performing Musharaka financing outstanding as of 31 December 2018 amounted to BD 4,920 thousand (2017: BD 3,678 thousand).



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**5 FINANCING ASSETS (continued)****5.3 The movement on impairment allowances is as follows:**

<b>2018</b>	<b>Stage 1</b>	<b>Stage 2</b>	<b>Stage 3</b>	<b>Total</b>
At 1 January 2018	2,367	9,486	15,345	27,198
Net movement between stages	1,302	(4,304)	3,002	-
Net charge for the year	(1,512)	(2,036)	10,079	6,531
Write-backs	-	-	(784)	(784)
Write-off	-	-	(3,106)	(3,106)
<b>At 31 December 2018</b>	<b>2,157</b>	<b>3,146</b>	<b>24,536</b>	<b>29,839</b>

<b>2017</b>	<b>Specific</b>	<b>Collective</b>	<b>Total</b>
At 1 January 2017	16,560	10,141	26,701
Net movement between stages	-	-	-
Net charge for the year	6,254	(1,092)	5,162
Write-backs	(3,489)	-	(3,489)
Write-off	(13,207)	-	(13,207)
<b>At 31 December 2017</b>	<b>6,118</b>	<b>9,049</b>	<b>15,167</b>

**6 INVESTMENT SECURITIES**

	<b>2018</b>	<b>2017</b>
	<b>BD'000</b>	<b>BD'000</b>
<b>a. Debt type instruments*</b>		
<i>Quoted Sukuk - carried at amortised cost</i>		
Gross balance at beginning of the year	176,806	89,706
Acquisitions	41,891	89,474
Disposals and redemptions	(57,970)	(2,374)
<b>Gross balance at the end of the year</b>	<b>160,727</b>	<b>176,806</b>
Impairment allowance	(23)	-
<b>Net balance at the end of the year</b>	<b>160,704</b>	<b>176,806</b>
<i>Unquoted Sukuk - carried at amortised cost</i>		
Gross balance at beginning of the year	62,581	32,683
Acquisitions	33,699	30,072
Disposals and redemptions	(37,534)	(223)
Foreign currency translation changes	(21)	49
<b>Gross balance at the end of the year</b>	<b>58,725</b>	<b>62,581</b>
Impairment allowance	(12,196)	(11,481)
<b>Net balance at the end of the year</b>	<b>46,529</b>	<b>51,100</b>
<b>b. Equity type instruments</b>		
<i>Quoted shares - at fair value through equity</i>		
Gross balance	-	2,392
Impairment allowance	-	(1,704)
Disposals	-	(688)
<b>Net balance at the end of the year</b>	<b>-</b>	<b>-</b>
<i>Unquoted shares - at cost less impairment</i>		
Gross balance	28,436	24,963
Impairment allowance	(9,784)	(8,638)
<b>Net balance at the end of the year</b>	<b>18,652</b>	<b>16,325</b>
<i>Unquoted managed funds - at cost less impairment</i>		
Gross balance	14,168	14,168
Impairment allowance	-	-
<b>Net balance at the end of the year</b>	<b>14,168</b>	<b>14,168</b>
<b>Total net investment securities</b>	<b>240,053</b>	<b>258,399</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**6 INVESTMENT SECURITIES (continued)**

\* As of 31 December 2018, debt type instruments includes sukuk of BD 134,895 thousand (2017: BD 25,057 thousand) pledged against borrowings from financial institutions of BD 96,386 thousand (2017: BD 63,488 thousand). (note 12)

The movement on impairment allowances on debt type instruments (Sukuk) is as follows:

<b>2018</b>	<b>Stage 1</b>	<b>Stage 2</b>	<b>Stage 3</b>	<b>Total</b>
At 1 January 2018	96	-	11,481	11,577
Net movement between stages	-	-	-	-
Net charge for the year	(44)	-	707	663
Recoveries / write-backs	-	-	-	-
Write-off	-	-	-	-
Foreign exchange movement	-	-	(21)	(21)
<b>At 31 December 2018</b>	<b>52</b>	<b>-</b>	<b>12,167</b>	<b>12,219</b>

<b>2017</b>	<b>Specific</b>	<b>Collective</b>	<b>Total</b>
At 1 January 2017	9,105	-	9,105
Net movement between stages	-	-	-
Net charge for the year	2,327	-	2,327
Recoveries	-	-	-
Write-off	-	-	-
Foreign exchange movement	49	-	49
<b>At 31 December 2017</b>	<b>11,481</b>	<b>-</b>	<b>11,481</b>

During the year impairment of BD 1,147 thousand (2017: BD 1,013 thousand) was provided on equity investments.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 7 INVESTMENT IN ASSOCIATES

	2018 BD'000	2017 BD'000
At 1 January	23,739	26,487
Share of results of associates, net	86	(1,103)
Share of changes in investee's equity	(27)	17
Disposals	-	(1,431)
Impact of adopting FAS 30	(350)	-
Foreign currency translation changes	(29)	89
Impairment allowance	(1,776)	(320)
<b>At 31 December</b>	<b>21,643</b>	<b>23,739</b>

Summarised financial information of associates that have been equity accounted in these consolidated financial statements, not adjusted for percentage of ownership held by the Group:

	2018 BD'000	2017 BD'000
Total assets	196,652	200,373
Total liabilities	77,726	80,925
Total revenues	4,508	5,086
Total net loss	(1,373)	(810)

Investment in associates comprise of:

Name of associate	Ownership %	Country of incorporation	Nature of business
Liquidity Management Centre B.S.C. (c)	25.00%	Bahrain	Liquidity Management Centre B.S.C. (c) was incorporated in 2002 as a bank, licensed and regulated by the Central Bank of Bahrain to facilitate the creation of an Islamic inter-bank market that allow Islamic financial services institutions to effectively manage their assets and liabilities.
Arabian C Real Estate Company	19.00%	Kuwait	Arabian C Real Estate Company is a Kuwaiti Shareholding Company incorporated in accordance with the Kuwaiti Commercial Companies law. The company's activity focuses on real estate development and the overall management of a variety of strategic investments in the real estate and infrastructure sectors in GCC/MENA region.
Al Dur Energy Investment Company	29.41%	Bahrain	Al Dur Energy Investment Company is an exempt company with limited liability incorporated in the Cayman Islands on 10 June 2009 and operates under registration number 227032. The company operates in the Kingdom of Bahrain with the sole purpose of holding a 15% indirect interest in a power and water plant project company, Al Dur Power and Water Company B.S.C.(c), in the Kingdom of Bahrain.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 8 IJARAH MUNTAHIA BITTAMLEEK

	2018				2017			
	<i>Properties</i>	<i>Aviation related assets</i>	<i>Others</i>	<i>Total</i>	<i>Properties</i>	<i>Aviation related assets</i>	<i>Others</i>	<i>Total</i>
	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>
<b>Cost:</b>								
At 1 January	204,063	7,540	-	211,603	178,374	7,540	2,503	188,417
Additions	41,541	-	-	41,541	36,238	-	-	36,238
Settlements / adjustments	(28,192)	-	-	(28,192)	(10,549)	-	(2,503)	(13,052)
<b>At 31 December</b>	<b>217,412</b>	<b>7,540</b>	<b>-</b>	<b>224,952</b>	<b>204,063</b>	<b>7,540</b>	<b>-</b>	<b>211,603</b>
<b>Accumulated depreciation:</b>								
At 1 January	46,093	1,113	-	47,206	33,936	226	2,503	36,665
Charge for the year	20,931	887	-	21,818	17,014	887	-	17,901
Settlements / adjustments	(9,802)	-	-	(9,802)	(4,857)	-	(2,503)	(7,360)
<b>At 31 December</b>	<b>57,222</b>	<b>2,000</b>	<b>-</b>	<b>59,222</b>	<b>46,093</b>	<b>1,113</b>	<b>-</b>	<b>47,206</b>
<b>Net Book Value</b>	<b>160,190</b>	<b>5,540</b>	<b>-</b>	<b>165,730</b>	<b>157,970</b>	<b>6,427</b>	<b>-</b>	<b>164,397</b>

Ijarah Muntahia Bittamleek and Ijarah rental receivable of BD 200,414 thousand (2017: BD 192,055 thousand) is net of impairment allowance of BD 13,543 thousand (2017: BD 13,175 thousand) refer note 27 (a). During the year an impairment release of BD 774 thousand (2017: charge of BD 299 thousand) refer note 23.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 9 PROPERTY AND EQUIPMENT

9

PROPERTY AND EQUIPMENT

		2018						
		<i>Lands BD'000</i>	<i>Buildings BD'000</i>	<i>Fixture and fitting BD'000</i>	<i>Equipment BD'000</i>	<i>Furniture BD'000</i>	<i>Work in progress BD'000</i>	<i>Total BD'000</i>
<b>Cost:</b>								
At 1 January		5,521	7,651	3,837	11,519	890	569	29,987
Additions / Transfers		-	-	401	817	10	(383)	845
Disposals		-	-	(74)	(24)	(6)	-	(104)
<b>At 31 December</b>		<b>5,521</b>	<b>7,651</b>	<b>4,164</b>	<b>12,312</b>	<b>894</b>	<b>186</b>	<b>30,728</b>
<b>Depreciation:</b>								
At 1 January		-	2,223	3,404	9,287	803	-	15,717
Charge for the year		-	260	217	946	50	-	1,473
Relating to disposed assets		-	-	(74)	(23)	(6)	-	(103)
<b>At 31 December</b>		<b>-</b>	<b>2,483</b>	<b>3,547</b>	<b>10,210</b>	<b>847</b>	<b>-</b>	<b>17,087</b>
<b>Net Book Value</b>		<b>5,521</b>	<b>5,168</b>	<b>617</b>	<b>2,102</b>	<b>47</b>	<b>186</b>	<b>13,641</b>
		2017						
		<i>Lands BD'000</i>	<i>Buildings BD'000</i>	<i>Fixture and fitting BD'000</i>	<i>Equipment BD'000</i>	<i>Furniture BD'000</i>	<i>Work in progress BD'000</i>	<i>Total BD'000</i>
<b>Cost:</b>								
At 1 January		5,521	7,651	3,814	10,367	883	558	28,794
Additions		-	-	23	1,152	7	11	1,193
At 31 December		5,521	7,651	3,837	11,519	890	569	29,987
<b>Depreciation:</b>								
At 1 January		-	1,962	3,144	8,298	743	-	14,147
Charge for the year		-	261	260	989	60	-	1,570
At 31 December		-	2,223	3,404	9,287	803	-	15,717
<b>Net Book Value</b>		<b>5,521</b>	<b>5,428</b>	<b>433</b>	<b>2,232</b>	<b>87</b>	<b>569</b>	<b>14,270</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**10 INVESTMENT IN REAL ESTATE**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Land	23,966	27,796
Buildings	318	2,035
	<b>24,284</b>	<b>29,831</b>
	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Movement in investment in real estate:		
At 1 January	29,831	29,510
Capitalized expenditure	-	28
Disposal	(4,028)	(372)
Fair value changes	(1,519)	665
<b>At 31 December</b>	<b>24,284</b>	<b>29,831</b>

Investment in real estate comprises of properties located in the Kingdom of Bahrain and the United Arab Emirates.

Investment in real estate is stated at fair value, which has been determined based on valuations performed by independent third party property valuers who have the qualification and experience of valuing similar properties in the same location. Fair value of Investments in real estate is classified as category 2 of fair value hierarchy.

**11 OTHER ASSETS**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Reposessed assets*	5,103	5,689
Receivables**	3,224	2,475
Staff advances	1,717	1,608
Prepaid expenses	803	1,138
Other	215	285
	<b>11,062</b>	<b>11,195</b>

\*Reposessed assets are net of impairment allowance of BD 585 thousand (2017: Nil thousand).

\*\*Impairment on receivables includes Stage 1 BD 5 thousand, Stage 2 BD 127 thousand (2017: collective provision of BD Nil thousand) and Stage 3 BD 101 thousand (2017: specific provision of BD Nil thousand). During the year impairment charge of BD 173 thousand was provided (2017: Nil) representing BD 5 thousand (stage 1), BD 67 thousand (stage 2) and BD 101 thousand (stage 3).

**12 BORROWINGS FROM FINANCIAL INSTITUTIONS**

Represents term murabaha facilities of BD 96,386 thousand (2017: BD 101,576 thousand) secured by pledge over sukuk of BD 134,895 thousand (2017: BD 25,057 thousand) maturing within 9 months from year end. The average rate of borrowings is 3.49%. (note 6)

**13 OTHER LIABILITIES**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Managers' cheques	3,560	1,833
Payable to vendors	3,874	708
Accrued expenses	3,551	3,618
Life insurance (Takaful) fees payable	845	999
Dividends payable	928	1,000
Zakah and charity fund	314	259
Other	10,953	3,090
	<b>24,025</b>	<b>11,507</b>

**14 EQUITY OF INVESTMENT ACCOUNTHOLDERS**

The Group combines the Investment Account Holders' (IAH) funds with the owners' equity. In line with its policy, the Group utilizes the funds from IAH to finance assets.

**14.1 Equity of investment accountholders balances**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
<b>Type of Equity of Investment Accountholders</b>		
Customer investment accounts		
Balances on demand	<b>296,140</b>	303,345
Contractual basis	<b>489,851</b>	490,411
	<b>785,991</b>	793,756

**14.2 Assets in which IAH funds were invested**

Assets in which IAH funds were invested as at 31 December are as follows:

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
<b>Asset</b>		
Cash and balances with banks and Central Bank	<b>44,993</b>	30,334
Financing assets, net	<b>440,882</b>	429,390
Ijarah Muntahia Bittamleek and rental receivables, net	<b>142,304</b>	131,545
Investment securities, net	<b>157,812</b>	189,478
Investment in real estate	-	5,329
Other assets	-	7,680
	<b>785,991</b>	793,756

The Bank temporarily allocates non-performing assets (past due greater than 90 days) from IAH to the equity shareholders and charges the specific impairment provisions to the owners' equity. Amounts recovered from these impaired assets is not subject to allocation between the IAH and owners' equity. The Bank takes remedial action on these non-performing assets and once these assets become performing, the assets and related income are allocated between the IAH and owners' equity.

The Bank charges IAH with their share of collective impairment provisions on financing facilities not past due and past due less than 90 days. During the year the Bank allocated BD 42,351 thousand of ECL (2017: Collective provision of BD 3,778 thousand) to the IAH.

During the year, the Bank did not charge any administration expenses to investment accounts.



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**14 EQUITY OF INVESTMENT ACCOUNTHOLDERS (continued)****14.3 Profit distribution by account type**

Following is the average percentage of profit allocation between the owner's accounts applied during the year for each type of IAH account as agreed contractually with the customers:

Account type	2018			2017		
	Utilization	Mudarib Share	Profit to IAH	Utilization	Mudarib Share	Profit to IAH
Tejoori	90%	97.49%	2.51%	90%	97.39%	2.61%
Savings	90%	97.47%	2.53%	90%	97.39%	2.61%
Vevo	90%	97.41%	2.59%	90%	97.39%	2.61%
IQRA	100%	72.99%	27.01%	100%	71.75%	28.25%
Time deposits	100%	45.50%	54.50%	100%	43.56%	56.44%

During the year, the Group did not increase its percentage of profits as mudarib. Further, the Group did not receive any incentive from profits of investment account holders.

The Group does not share profits with IAH resulting from investing current accounts and other funds received on the basis other than mudaraba contract.

Funds from IAH are invested in assets on a priority basis.

**14.4 Equity of Investment Accountholders Reserves**

	2018 BD'000	Movement BD'000	2017 BD'000
Profit equalisation reserve	1,245	-	1,245
Investment risk reserve	1,177	-	1,177

**14.5 Return on equity of investment accountholders**

	2018 BD'000	2017 BD'000
Gross return to equity of investment accountholders	41,162	36,430
Group's share as a Mudarib	(27,223)	(24,646)
Allocation to profit equalization reserve	-	-
Allocation to investment risk reserve	-	(420)
Net return on equity of investment accountholders	13,939	11,364

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 15 OWNERS' EQUITY

		2018 BD'000	2017 BD'000
a.	Share capital		
i.	Authorised		
	2,000,000,000 shares (2017: 2,000,000,000 shares) of BD 0.100 each	200,000	200,000
ii.	Issued and fully paid up		
	1,064,058,587 shares (2017: 1,013,389,130 shares) of BD 0.100 each	106,406	101,339
b.	Treasury Shares		
		2018 Number of Shares	2017 BD'000
	At 31 December	5,855,358	864

	2018 BD'000
Cost of treasury shares	892
Market value of treasury shares	761

The treasury shares as a percentage of total shares in issue is 0.55%

Owners' equity instruments which are reacquired are deducted from equity. No gain or loss is recognised in the consolidated income statement on the purchase, sale, issue or cancellation of the Group's own equity instruments.

## c. Reserves

*Statutory reserve*

During the year the Bank has appropriated BD 1,138 thousand (2017: 1,014 thousand) to the statutory reserve representing 10% of the profit for the year BD 11,381 thousand (2017: 10,141 thousand). The reserve is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of CBB.

*General reserve*

The general reserve is established in accordance with the articles of association of the Bank and is distributable following a resolution of shareholders at a general meeting and the approval of CBB. The Group may transfer any amount to the general reserve, as approved by the shareholders at a general meeting, out of the net income for the year after appropriating statutory reserve.

*Real estate fair value reserve*

This represents cumulative unrealised revaluation gains on investment in real estate. This reserve is transferred to the consolidated income statement upon sale of the investment in real estate.

*Investment fair value reserve*

This represents the net unrealised gains or losses on equity investments relating to self financed investments.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**15 OWNERS' EQUITY (continued)**

d. Additional information on shareholding pattern

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

Names	Nationality	2018		2017	
		Number of shares	% holding	Number of shares	% holding
National Bank of Bahrain	Bahraini	309,206,266	29.06%	294,482,159	29.06%
Social Insurance Organisation	Bahraini	154,604,585	14.53%	147,242,463	14.53%
Social Insurance Organisation - Military Pension Fund	Bahraini	154,604,587	14.53%	147,242,464	14.53%
Islamic Development Bank	Saudi	153,423,081	14.42%	146,117,221	14.42%
General Council of Kuwaiti Awqaf	Kuwaiti	76,366,321	7.18%	72,729,830	7.18%

ii. The Group has only one class of shares and the holders of these shares have equal voting rights.

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

	2018			2017		
	Number of shares	Number of shareholders	% of total outstanding shares	Number of shares	Number of shareholders	% of total outstanding shares
Less than 1%	137,353,127	3,244	12.91%	145,805,613	3,232	14.38%
1% and less than 5%	78,854,583	4	7.41%	59,769,380	3	5.90%
5% and less than 10%	76,273,875	1	7.17%	72,729,830	1	7.18%
10% and less than 50%	771,577,002	4	72.51%	735,084,307	4	72.54%
	<b>1,064,058,587</b>	<b>3,253</b>	<b>100.00%</b>	<b>1,013,389,130</b>	<b>3,240</b>	<b>100.00%</b>

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

**Categories:**

	2018		2017	
	No. of shares	No. of directors	No. of shares	No. of directors
Less than 1%	487,535	4	464,320	4

The following is the number of shares, and percentage of shareholding of Directors, Shari'a supervisory members and senior management (Assistant General Managers and above):

	2018		2017	
	No. of shares	Percentage of Shareholding	No. of shares	Percentage of Shareholding
Directors	487,535	0.046%	464,320	0.046%
Shari'a supervisory members	190,817	0.018%	181,731	0.018%
Senior management	1,202,534	0.113%	777,167	0.077%
	<b>1,880,886</b>	<b>0.177%</b>	<b>1,423,218</b>	<b>0.141%</b>

e. Proposed appropriations

The Board of Directors propose the appropriation for zakah of BD 179 thousand in 2018 (2017: BD 265 thousand), charitable donations of BD 250 thousand in 2018 (2017: BD 200 thousand) and dividends amounting to BD Nil thousand (2017: bonus shares as dividends amounting to BD 5,066 thousand) which are subject to regulatory and shareholders' approval in the ensuing Annual General Meeting.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**16 COMMITMENTS AND CONTINGENT LIABILITIES*****Credit related commitments***

These include commitments to enter into financing contracts which are designed to meet the requirements of the Group's customers.

Letters of credit and guarantees commit the Group to make payments on behalf of customers.

The Group has the following credit related commitments and contingent liabilities on behalf of customers:

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Letters of credit and acceptances	<b>6,166</b>	5,470
Guarantees	<b>66,316</b>	74,159
Credit cards	<b>34,048</b>	30,508
Altamweel Almaren	<b>15,405</b>	19,033
Operating lease commitments *	<b>327</b>	223
Commitments to finance	<b>35,422</b>	19,147
	<b>157,684</b>	148,540

\* The Group has entered into commercial leases for certain branches. The remaining average period of these leases ranges between 1 month and 3 years with renewal terms included in the contracts. Renewals are at the option of the Bank. There are no restrictions placed upon the lessee by entering into these leases.

Future minimum rentals payable under non-cancellable operating leases as at 31 December are as follows:

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Within one year	<b>182</b>	170
After one year but not more than five years	<b>145</b>	53
	<b>327</b>	223

**17 CAPITAL ADEQUACY**

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue Sukuk etc. No changes were made in the objectives, policies and processes from the previous years.

The Group's capital structure primarily consists of its paid-up capital, including share premium and reserves. From a regulatory perspective, a significant amount of the Group's capital is classified as Tier 1 as defined by the CBB, i.e. most of the capital is of a permanent nature.

The Group's capital adequacy policy is to maintain a strong capital base to support the development and growth of the business. Current and future capital requirements are determined on the basis of financing facilities growth expectations for each business group, expected growth in off-balance sheet facilities and future sources and uses of funds.

**17 CAPITAL ADEQUACY (continued)**

The Central Bank of Bahrain issued the final regulation to give effect to the Basel III framework which came into effect on 1 January 2015. The Basel III framework significantly revises the definition of regulatory capital. The framework emphasises on common equity as the predominant component of tier 1 capital by adding a minimum Common Equity Tier 1 (CET 1) capital ratio. The Basel III rules also require institutions to hold capital buffers. For the purpose of calculating CET 1 capital, the regulatory adjustments (deductions) including amounts above the aggregate limit for significant investments in financial institutions, mortgage servicing rights, and deferred tax assets from temporary differences, will be deducted from CET1 over a phased manner to be fully deducted by 1 January 2019. The Bank's current capital position is sufficient to meet the new regulatory capital requirements.

The classification of the Group's capital in accordance with the regulatory requirements is as follows:

	<b>2018</b>	<b>2017</b>
	<b>BD'000</b>	<b>BD'000</b>
CET 1 Capital before regulatory adjustments	<b>112,919</b>	116,125
Less: regulatory adjustments	-	-
<b>CET 1 Capital after regulatory adjustments</b>	<b>112,919</b>	116,125
T 2 Capital adjustments	<b>12,559</b>	13,283
<b>Regulatory Capital</b>	<b>125,478</b>	129,408

To assess its capital adequacy requirements in accordance with the CBB requirements, the Group adopts the Standardised Approach for its Credit Risk, Basic Indicator Approach for its Operational Risk and Standardised Approach for its Market Risk. The capital requirements for these risks are as follows:

	<b>2018</b>	<b>2017</b>
	<b>BD'000</b>	<b>BD'000</b>
<b>Risk weighted exposure:</b>		
Total Credit Risk Weighted Assets	<b>618,293</b>	571,069
Total Market Risk Weighted Assets	<b>11,891</b>	10,702
Total Operational Risk Weighted Assets	<b>103,812</b>	86,085
<b>Total Regulatory Risk Weighted Assets</b>	<b>733,996</b>	667,856
Investment risk reserve (30% only)	<b>353</b>	353
Profit equalization reserve (30% only)	<b>374</b>	374
<b>Total Adjusted Risk Weighted Exposures</b>	<b>733,269</b>	667,129
<b>Capital Adequacy Ratio</b>	<b>17.11%</b>	19.40%
<b>Tier 1 Capital Adequacy Ratio</b>	<b>15.40%</b>	17.41%
Minimum requirement	<b>12.5%</b>	12.5%

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**18 INCOME FROM FINANCING**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Income from Murabaha financing	<b>25,755</b>	23,483
Income from placements with financial institutions	<b>1,903</b>	1,093
Income from Musharaka financing	<b>5,923</b>	6,580
Income from Ijarah Muntahia Bittamleek	<b>9,529</b>	9,351
	<b>43,110</b>	40,507

**19 INCOME FROM INVESTMENT SECURITIES**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Dividend income	<b>216</b>	513
	<b>216</b>	513

**20 INCOME FROM INVESTMENT IN REAL ESTATE**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Loss on sale	<b>(531)</b>	(39)
Rental income	<b>179</b>	371
Impairment charge	<b>(204)</b>	(119)
	<b>(556)</b>	213

**21 OTHER INCOME**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Recoveries from previously written off financing	<b>4,491</b>	1,883
Foreign exchange (loss) / gain	<b>(123)</b>	489
Others	<b>4</b>	368
	<b>4,372</b>	2,740

**22 OTHER OPERATING EXPENSES**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Marketing and advertisement expenses	<b>2,123</b>	2,811
Information technology related expenses	<b>1,558</b>	1,602
Card Centre expenses	<b>2,181</b>	1,951
Premises and equipment expenses	<b>918</b>	1,150
Communication expenses	<b>662</b>	920
Professional services	<b>916</b>	1,254
Board remunerations	<b>266</b>	500
Board of directors sitting fees	<b>153</b>	141
Shari'a committee fees & expenses	<b>65</b>	111
Others	<b>2,352</b>	1,947
	<b>11,194</b>	12,387

**23 IMPAIRMENT ALLOWANCE, NET**

	<b>2018</b> <b>BD'000</b>	<b>2017</b> <b>BD'000</b>
Financing assets (note 5.3)	<b>5,747</b>	2,238
Ijarah rental receivables (note 8)	<b>(774)</b>	299
Investments in Sukuk (note 6)	<b>663</b>	2,327
Investments at fair value through equity (note 6)	<b>1,147</b>	1,013
Investment in associate (note 7)	<b>1,776</b>	320
Placements with financial institutions	<b>3</b>	-
Other assets	<b>758</b>	-
Commitments	<b>(425)</b>	-
	<b>8,895</b>	6,197

**24 ZAKAH**

The total Zakah payable as of 31 December 2018 amounted to BD 1,961 thousand (2017: BD 1,875 thousand) of which the Bank has BD 179 thousand Zakah payable (2017: BD 265 thousand ) based on the statutory reserve, general reserve and retained earning as at 1 January 2018. The Zakah balance amounting to BD 1,782 thousand or 1.7 fils per share (2017: BD BD 1,610 thousand or 1.6 fils per share) is due and payable by the shareholders.

**25 EARNINGS PER SHARE**

Basic and diluted earnings per share is calculated by dividing the net profit or loss for the year by the weighted average number of shares during the year as follows:

	<b>2018</b>	<b>2017</b>
Profit for the year in BD'000	<b>11,381</b>	10,141
Weighted average number of shares	<b>1,051,093</b>	1,050,452
Basic and diluted earnings per share (fils)	<b>10.83</b>	9.65

Basic and diluted earnings per share are the same since the Group has not issued any instruments that would have a dilutive effect.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**26 RELATED PARTY TRANSACTIONS**

Related parties comprise of major shareholders, directors of the Bank, senior management, close members of their families, entities owned or controlled by them and companies affiliated by virtue of common ownership or directors with that of the Bank. The transactions with these parties were made on commercial

The significant balances and transactions with related parties at 31 December were as follows:

	2018				
	Shareholders BD'000	Associates and joint ventures BD'000	Directors and related entities BD'000	Senior management BD'000	Total BD'000
<b>Assets</b>					
Financing assets	-	-	1,615	-	1,615
Investment in associates	-	21,643	-	-	21,643
Other assets	-	-	-	285	285
<b>Liabilities and Equity of investment accountholders</b>					
Borrowings from financial institutions	-	-	-	-	-
Customers' current accounts	-	177	425	77	679
Other liabilities	-	-	500	-	500
Equity of investment accountholders	48,972	-	695	980	50,647
	2018				
	Shareholders BD'000	Associates and joint ventures BD'000	Directors and related entities BD'000	Senior management BD'000	Total BD'000
<b>Income</b>					
Income from financing	-	-	105	-	105
Share of results of associates, net	-	86	-	-	86
<b>Return on equity of investment accountholders</b>	(1,512)	-	(33)	(35)	(1,580)
<b>Expense on borrowings from financial institutions</b>	(532)	-	-	-	(532)
<b>Expenses</b>					
Other expenses	-	-	(484)	-	(484)
Staff costs	-	-	-	(1,405)	(1,405)



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 26 RELATED PARTY TRANSACTIONS (continued)

	2017				
	Shareholders BD'000	Associates and joint ventures BD'000	Directors and related entities BD'000	Senior management BD'000	Total BD'000
<b>Assets</b>					
Financing assets	-	-	1,580	-	1,580
Investment in associates	-	23,739	-	-	23,739
Other assets	-	-	-	268	268
<b>Liabilities and Equity of investment accountholders</b>					
Borrowings from financial institutions	38,991	-	-	-	38,991
Customers' current accounts	-	122	453	109	684
Other liabilities	-	-	517	-	517
Equity of investment accountholders	47,092	-	1,923	1,206	50,221
	2017				
	Shareholders BD'000	Associates and joint ventures BD'000	Directors and related entities BD'000	Senior management BD'000	Total BD'000
<b>Income</b>					
Income from financing	-	-	98	-	98
Share of results of associates, net	-	(1,103)	-	-	(1,103)
Return on equity of investment accountholders	(1,469)	-	(28)	(39)	(1,536)
Expense on borrowings	(750)	-	-	-	(750)
<b>Expenses</b>					
Other expenses	-	-	(753)	-	(753)
Staff costs	-	-	-	(1,439)	(1,439)

Compensation of the key management personnel is as follows:

	2018 BD'000	2017 BD'000
Short term employee benefits	1,143	1,178
Other long term benefits	262	261
	<b>1,405</b>	<b>1,439</b>

Key management personnel includes staff at the grade of assistant general manager or above.

**27 RISK MANAGEMENT**

**Introduction**

Risk is inherent in the Group's activities but it is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his or her responsibilities. The risks and the processes to mitigate these risks have not significantly changed from the previous year.

The Bank is primarily exposed to credit risk, liquidity risk, market risk (including profit rate risk, equity price risk, and foreign exchange risks), operational risk, reputational risk and Sharia'a-compliance risk.

**Risk management objectives**

The risk management philosophy of the Group is to identify, monitor and manage the various dimensions of risk with the objective of protecting asset values and income streams such that the interest of the Group's shareholders (and others to whom the Group owes a liability) are safeguarded, while maximising the returns intended to optimise the Group's shareholder return while maintaining its risk exposure within self-imposed parameters.

The Bank's risk appetite is embodied through its risk strategy; BisB reviews and aligns its risk appetite in line with its evolving business plan, and changing economic and market scenarios, in addition to evolving regulatory requirements. The Bank also assesses its tolerance for specific risk categories and its strategy to manage these risks. To monitor and report exposures to these identified risks, the Bank adopted a comprehensive enterprise-wide Risk Management Framework that encompasses the risk limit, monitoring, and reporting structures.

**Structure and Organization of the Risk Management Function**

Risk management structure includes all levels of authorities, organizational structure, people and systems required for the effective functioning of risk management processes in the Group. The responsibilities associated with each level of the risk management structure and authorities include the following:

The Board retains ultimate responsibility and authority for all risk matters, including:

- i. Establishing overall policies and procedures; and
- ii. Delegating authority to the Executive Committee, Credit and Investment Committee, Chief Executive Officer and further delegation to the management to approve and review.

Executive Committee (EC) comprises of four designated members of the Board of Directors. The Executive Committee has delegated authority by the Board to manage the ongoing activities of the Group. Decisions are taken by the Executive Committee either at periodic meetings or if the need arises, by circulation.

Credit and Investment Committee (CIC): The CIC determines the Credit & Investment Policy of the bank, identifies possible risk assumed by the bank for different transactions. The CIC has the authority to make final decision on approval or rejection of proposed transactions within its delegated authority as well as to monitor the performance and quality of the bank's credit and investment portfolio. The purpose of CIC is to assist management in fulfilling its oversight responsibilities relating to the credit & investment objectives, policies, controls, procedures and related activities, including but not limited to the review of the bank's investment and credit exposures, credit, investment, per party, concentration and group limits.

The Credit & Risk Management (C&RM) division – headed by the Chief Risk Officer - has day-to-day responsibility for managing the risks involved across all areas of the Bank. C&RM provides independent identification, measurement, monitoring and control of all risk parameters, while liaising with the business divisions that ultimately own the risks. C&RM comprises a number of specialist units, including Risk Management, Credit Review & Analysis, and Credit Administration.

**Risk Measurement and Reporting Systems**

Based on the risk appetite, the Group has put in place various limits. These limits have been approved by the Board. Any limit breach is reported by the Credit & Risk Management Department (C&RM) to the relevant management/Board-level committee. The limits are reviewed and revised periodically, as required by the relevant policy and regulatory requirements.

**27 RISK MANAGEMENT (continued)****a. Credit Risk**

Credit risk is considered to be the most significant and pervasive risk for the Group. The Group takes on exposure to credit risk, which is the risk that the counter-party to a financial transaction will fail to discharge an obligation causing the Group to incur a financial loss. Credit risk arises principally from financing (credit facilities provided to customers), investment in Sukuk and from cash and deposits held with other banks. Further, there is credit risk in certain off-balance sheet financial instruments, including guarantees relating to purchase and sale of foreign currencies, letters of credit, acceptances and commitments to extend credit. Credit risk monitoring and control is performed by the Credit and Risk Management Department which sets parameters and thresholds for the Group's financing activities.

*(i) ECL – Significant increase in credit risk (SICR)*

To determine whether credit risk has significantly increased since initial recognition, the Group will compare the risk of default at the assessment date with the risk of default at initial recognition. This assessment is to be carried out at each assessment date.

For the Corporate portfolio, The Group assess for significant increase in credit risk (SICR) at a counterparty level as internal rating is currently carried out at a counterparty level and rating is not assigned at facility level. The Group maintains a facility level rating being the counterparty's internal rating at date of facility origination and date of assessment.

For the Retail portfolio, Group currently manages its retail portfolio at a facility level. However, assessment for SICR on the retail portfolio is done on a counterparty level. Days past due (DPD) of individual facilities will reflect on the counterparty SICR assessment.

*(ii) Generating the term structure of PD*

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

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

This analysis includes the identification and calibration of relationships between changes in default rates and macro-economic factors as well as in-depth analysis of the impact of certain other factors (e.g. forbearance experience) on the risk of default. The macro economic factors used in this analysis are shortlisted from the list given below:

1. Gross domestic product, constant prices;
2. Total investments;
3. Gross national savings;
4. Inflation, average consumer prices;
5. Volume of imports of goods and services;
6. Volume of exports of goods and services (including oil);
7. Population;
8. General government revenue;
9. General government total expenditure;
10. General government net lending / borrowing; and
11. General government net debt.

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

For Corporate portfolio, through the yearly review of the corporate portfolio, the Group observes yearly performances to compute a count based PD over the one year horizon for the past 5 years. These PDs are grouped as per internal risk ratings (i.e. from 1 to 7). An average default rate of the 5 yearly observed default provides the through the cycle PDs. Where a counterparty is not rated, PD assigned for rating 6 is used.

In relation to the retail portfolio, the portfolio is segmented by product, as demonstrated below:

- (i) Auto finance;
- (ii) Mortgage finance;
- (iii) Tasheel Finance and Others; and
- (iv) Credit cards.

PDs for each segment are measured using Observed Default Estimation and thus PD is calculated based on DPD bucket level for each segment separately. Under this analysis, the delinquency status of accounts is tracked at an interval of one year with a moving month cycle. A minimum of 5 year DPD data is considered.

**27 RISK MANAGEMENT (continued)****a. Credit Risk (Continued)***(iii) Determining whether credit risk has increased significantly*

In determining whether credit risk has increased significantly since initial recognition, the Group uses its internal credit risk grading system, external risk ratings, delinquency status of accounts, restructuring, expert credit judgement and, where possible, relevant historical experience.

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

As a backstop, the Group considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

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

The Group classifies its financial instruments into stage 1, stage 2 and stage 3, based on the applied impairment methodology, as described below:-

**Stage 1 (12 months ECL):** for exposures subject to credit risk where there has not been a significant increase in credit risk since initial recognition and that are not credit-impaired on origination, the Group recognises an allowance based on the 12-month ECL. All accounts at origination would be classified as Stage 1 only exceptions are Purchased or Originated Credit Impaired (POCI) assets.

**Stage 2 (lifetime ECL not credit impaired):** for exposures subject to credit risk where there has been a significant increase in credit risk since initial recognition but they are not credit-impaired, the Group recognises an allowance for the lifetime ECL for all financings categorized in this stage based on the actual / expected maturity profile including restructuring or rescheduling of facilities.

**Stage 3 (lifetime ECL credit impaired):** for credit-impaired exposures subject to credit risk, the Group recognises the lifetime ECL. Default identification process i.e. DPD of 90 more is used as stage 3.

*(iv) Definition of 'Default'*

The Group definition of default is aligned with regulatory guidelines and internal credit risk management practices. Defaulted assets will fall under the Stage 3. In general, a counterparty is considered in default and hence relevant exposure or a group of exposures is impaired if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the exposure or group of exposures that can be reliably estimated. It may not be possible to identify a single, discrete event that caused the impairment; rather the combined effect of several events may have caused the impairment losses expected as a result of future events, no matter how likely, are not recognised. Objective evidence that an exposure or group of exposures is impaired includes observable data that comes to the attention of the holder of the exposure.

In general, counterparties with facilities exceeding 90 days past dues are considered in default.

*(v) Incorporation of forward looking information*

The Group incorporates forward-looking information into both its assessment of whether the credit risk of an exposure has increased significantly since its initial recognition and its measurement of ECL. The Group annually source macro-economic forecast data for eleven variables from the International Monetary Fund (IMF) database for Bahrain.

Macro-economic variables checked for correlation with the probability of default for the past five years and only those variables for which the movement can be explained are used. Management judgement is exercised when assessing the macroeconomic variables.

**27 RISK MANAGEMENT (continued)****a. Credit Risk (Continued)***(vi) Measurement of ECL*

The Group measures an ECL at an individual instrument level taking into account the projected cash flows, PD, LGD, CCF and discount rate. For portfolios wherein instrument level information is not available, the Group carries out ECL estimation on a collective basis.

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

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

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

Corporate PD estimates are calculated based on statistical rating models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally compiled data comprising both quantitative and qualitative factors. If a counterparty or exposure migrates between ratings classes, then this will lead to a change in the estimate of the associated PD.

Retail PD estimates are measured using Observed Default Estimation at the segment level and thus PD will be calculated based at DPD bucket level for each segment separately. Under this analysis, the delinquency status of accounts will be tracked at an interval of one year with a moving month cycle.

Debt type instruments Portfolio, Nostro and Interbank Placements portfolio is assessed for SICR using external ratings, the Group shall obtain PD estimates from Moody's / Standard & Poor's (S&P) / Fitch or any other external ratings.

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset.

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

The period of exposure limits the period over which possible defaults are considered and thus affects the determination of PDs and measurement of ECLs (especially for Stage 2 accounts with lifetime ECL).

Subject to using a maximum of a 12-month PD for exposures subject to credit risk for which credit risk has not significantly increased, the Group measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for risk management purposes, the Group considers a longer period. The maximum contractual period extends to the date at which the Group has the right to require repayment of an advance or terminate a financing commitment or guarantee.

*(vii) Modified exposures subject to credit risk*

The contractual terms of exposures subject to credit risk may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer.

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

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

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

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

**27 RISK MANAGEMENT (continued)****a. Credit Risk (Continued)****(vii) Modified exposures subject to credit risk (Continued)**

For exposures modified as part of the Group's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Group's ability to collect profit and principal and the Group's previous experience of similar forbearance action. As part of this process, the Group evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired / in default. A customer needs to demonstrate consistently good payment behaviour over a period of time (12 months) before the exposure is no longer considered to be credit-impaired/ in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to 12-month ECL.

**Credit Risk Mitigation**

Credit risk mitigation refers to the use of a number of techniques, such as obtaining collateral and guarantees to mitigate the credit risks that the Group is exposed to. Credit risk mitigants reduce the credit risk by allowing the Group to protect against counterparty non-performance of credit contracts through collaterals, netting agreements and guarantees.

Generally, the Group extends credit facilities only where supported by adequate tangible collateral security and/or audited financial statements. Facilities may be considered without adequate tangible collateral security when audited financial statements reveal satisfactory financial position/repayment ability and the facilities are properly structured and supported by assignments, guarantees, etc. as appropriate.

In general, personal guarantees of the partners/promoters/directors of the borrowing entity are obtained in support of credit facilities. In all cases, a statement of net worth of the guarantor is to be compiled by the Account Officer, so that adequate information is available at a future date in case the guarantees need to be enforced.

Notwithstanding the above, when facilities are extended to family owned limited liability entities, the following is normally obtained;

- i. Collateral security, fully covering the exposure; or
- ii. Joint and several guarantees of shareholders directly involved in managing the entity as well as of shareholders owing at least 80% of the shares of the entity.

Third party guarantees in support of credit facilities are accepted only after review and approval of appropriate guarantor lines.

Collateral coverage by type of credit exposure:

<b>2018</b>	<b>Properties BD'000</b>	<b>Others BD'000</b>	<b>Total BD'000</b>
Financing assets	<b>650,819</b>	<b>52,924</b>	<b>703,743</b>
Ijarah muntahia bittamleek & rental receivables	<b>221,745</b>	<b>27,647</b>	<b>249,392</b>
	<b>872,564</b>	<b>80,571</b>	<b>953,135</b>
<b>2017</b>	<b>Properties BD'000</b>	<b>Others BD'000</b>	<b>Total BD'000</b>
Financing assets	678,305	55,207	733,512
Ijarah muntahia bittamleek & rental receivables	226,133	27,709	253,842
	904,438	82,916	987,354

The fair value of collateral that the Group holds relating to non performing facilities at 31 December 2018 amounts to BD 192,505 thousand (31 December 2017: 180,740 thousand). The collateral consists of cash, securities and properties. The utilisation of the above collaterals will be on a customer by customer basis and will be limited to the customer's total exposure.

**27 RISK MANAGEMENT (continued)****a. Credit Risk (Continued)****Gross maximum exposure to credit risk**

The market value of tangible collateral security is properly evaluated by the Group approved surveyors (for properties) or based on publicly available quotations. Only the amount of such security equivalent to the exposure is taken into account while considering credit facilities.

The CIC periodically reviews and approves the value of securities. It has also approved a list of acceptable securities.

The table below shows the gross maximum exposure to credit risk for the components of the consolidated statement of financial position, including credit related commitments. The figures represent gross exposure, without taking account of any collateral held or other credit enhancements.

	<b>2018</b>	<b>2017</b>
	<b>BD'000</b>	<b>BD'000</b>
Balances with banks and Central Bank	<b>50,119</b>	56,624
Placements with financial institutions	<b>137,450</b>	80,845
Financing assets	<b>578,953</b>	561,822
Ijarah Muntahia Bittamleek and Ijarah rental receivables	<b>186,871</b>	178,880
Investment debt securities	<b>207,233</b>	227,906
	<b>1,160,626</b>	1,106,077
Letters of credit, guarantees and acceptances	<b>72,482</b>	79,629

**Risk concentrations of the maximum exposure to credit risk**

Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location. The Group seeks to manage its credit risk exposure through diversification of financing activities to avoid undue concentrations of risks with individuals or groups of customers in specific locations or businesses.

The distribution of the Group's assets, liabilities, equity of investment accountholders, commitments and contingent liabilities by geographic region and industry sector is as follows:

	<i>Assets</i>		<i>Liabilities and equity of investment accountholders</i>		<i>Commitments and contingent liabilities</i>	
	<i>31 December</i>	<i>31 December</i>	<i>31 December</i>	<i>31 December</i>	<i>31 December</i>	<i>31 December</i>
	<i>2018</i>	<i>2017</i>	<i>2018</i>	<i>2017</i>	<i>2018</i>	<i>2017</i>
	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>	<i>BD'000</i>
<b>Geographical region</b>						
Middle East	<b>1,260,338</b>	1,194,057	<b>1,153,369</b>	1,091,639	<b>157,684</b>	148,540
North America	<b>5,751</b>	10,473	<b>258</b>	229	-	-
Europe	<b>13,285</b>	24,107	<b>7,265</b>	13,628	-	-
Other	<b>20</b>	10	<b>753</b>	881	-	-
	<b>1,279,394</b>	1,228,647	<b>1,161,645</b>	1,106,377	<b>157,684</b>	148,540
<b>Industry sector</b>						
Trading and manufacturing	<b>126,379</b>	105,018	<b>46,076</b>	19,022	<b>39,725</b>	25,211
Aviation	<b>17,128</b>	-	<b>11,925</b>	53,029	-	-
Real Estate	<b>171,828</b>	211,603	<b>79,832</b>	43,352	<b>40,790</b>	47,843
Banks and financial institutions	<b>206,593</b>	171,187	<b>249,184</b>	216,833	<b>1,403</b>	4,379
Personal / Consumer	<b>430,374</b>	391,662	<b>526,956</b>	472,366	<b>34,935</b>	33,590
Government Organization	<b>240,817</b>	251,777	<b>146,193</b>	165,358	<b>20,159</b>	21,081
Others	<b>86,275</b>	97,400	<b>101,479</b>	136,417	<b>20,672</b>	16,436
	<b>1,279,394</b>	1,228,647	<b>1,161,645</b>	1,106,377	<b>157,684</b>	148,540

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**27 RISK MANAGEMENT (Continued)***a) Credit Risk (continued)*

- a. The following table sets out information about the credit quality of exposures subject to credit risk, unless specifically indicated:

	31 December 2018			
	Stage 1	Stage 2	Stage 3*	Total
<b>Financing Assets (Funded exposure)</b>				
Low risks	357,627	22,913	-	380,540
Acceptable risks	113,067	31,572	-	144,639
Watch list	344	7,084	-	7,428
Non performing	-	-	76,185	76,185
<b>Gross exposure</b>	<b>471,038</b>	<b>61,569</b>	<b>76,185</b>	<b>608,792</b>
Less: ECL	(2,157)	(3,146)	(24,536)	(29,839)
<b>Financing Assets carrying amount</b>	<b>468,881</b>	<b>58,423</b>	<b>51,649</b>	<b>578,953</b>
<b>ljarah muntahia bittamleek &amp; ljarah rental receivables</b>				
Low risks	157,789	1,469	-	159,258
Acceptable risks	11,723	927	-	12,650
Watch list	-	9,653	-	9,653
Non performing	-	-	18,853	18,853
<b>Gross exposure</b>	<b>169,512</b>	<b>12,049</b>	<b>18,853</b>	<b>200,414</b>
Less: ECL	(399)	(2,320)	(10,824)	(13,543)
<b>ljarah muntahia bittamleek &amp; ljarah rental receivables carrying amount</b>	<b>169,113</b>	<b>9,729</b>	<b>8,029</b>	<b>186,871</b>
<b>Investment in Sukuk</b>				
Low risks	199,326	-	-	199,326
Acceptable risks	7,583	-	-	7,583
Watch list	-	-	-	-
Non performing	-	-	12,543	12,543
<b>Gross exposure</b>	<b>206,909</b>	<b>-</b>	<b>12,543</b>	<b>219,452</b>
Less: ECL	(52)	-	(12,167)	(12,219)
<b>Investment in Sukuk carrying amount</b>	<b>206,857</b>	<b>-</b>	<b>376</b>	<b>207,233</b>
<b>Placements with financial institutions</b>				
Low risks	137,455	-	-	137,455
Acceptable risks	-	-	-	-
Watch list	-	-	-	-
Non performing	-	-	-	-
<b>Gross exposure</b>	<b>137,455</b>	<b>-</b>	<b>-</b>	<b>137,455</b>
Less: ECL	(5)	-	-	(5)
<b>Placements with financial institutions carrying amount</b>	<b>137,450</b>	<b>-</b>	<b>-</b>	<b>137,450</b>



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**27 RISK MANAGEMENT (Continued)***a) Credit Risk (continued)*

	31 December 2018			
	Stage 1	Stage 2	Stage 3*	Total
<b>Balances with Banks</b>				
Low risks	15,014	-	-	15,014
Acceptable risks	-	-	-	-
Watch list	-	-	-	-
Non performing	-	-	-	-
<b>Gross exposure</b>	<b>15,014</b>	<b>-</b>	<b>-</b>	<b>15,014</b>
Less: ECL	-	-	-	-
<b>Balances with Banks carrying amount</b>	<b>15,014</b>	<b>-</b>	<b>-</b>	<b>15,014</b>
<b>Other Receivables</b>				
Low risks	-	-	-	-
Acceptable risks	1,423	1,802	-	3,225
Watch list	-	-	-	-
Non performing	-	-	101	101
<b>Gross exposure</b>	<b>1,423</b>	<b>1,802</b>	<b>101</b>	<b>3,326</b>
Less: ECL	(5)	(127)	(101)	(233)
<b>Other Receivables carrying amount</b>	<b>1,418</b>	<b>1,675</b>	<b>-</b>	<b>3,093</b>
<b>Total funded exposures subject to credit risk carrying amount</b>	<b>998,733</b>	<b>69,827</b>	<b>60,054</b>	<b>1,128,614</b>

\*This includes BD 37,829 thousand of exposures in the cooling off period.

**Commitments**

Gross exposure	40,820	405	159	41,384
ECL	(171)	(3)	(11)	(185)
<b>Commitments carrying amount</b>	<b>40,649</b>	<b>402</b>	<b>148</b>	<b>41,199</b>

b. The following table shows the movement in ECL in various stages:

	31 December 2018			
	Stage 1	Stage 2	Stage 3	Total
At 1 January 2018	3,012	11,184	39,570	53,766
Transfer to Stage 1	2,471	(1,323)	(1,148)	-
Transfer to Stage 2	(111)	2,708	(2,597)	-
Transfer to Stage 3	(27)	(4,837)	4,864	-
Net movement between stages	2,333	(3,452)	1,119	-
Charge for the year (net)	(2,556)	(2,136)	10,077	5,385
Write-off	-	-	(3,106)	(3,106)
Foreign exchange movement	-	-	(21)	(21)
<b>At 31 December 2018</b>	<b>2,789</b>	<b>5,596</b>	<b>47,639</b>	<b>56,024</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**27 RISK MANAGEMENT (continued)****a) Credit Risk (continued)**

	31 December 2017					
	Balances with banks and Central Bank BD'000	Placements with financial institutions BD'000	Financing assets BD'000	Ijarah Muntahia Bittamleek and rental receivables BD'000	Investment securities (Sukuk) BD'000	Total BD'000
Past due and impaired	-	-	38,112	16,814	12,550	67,476
Specific impairment	-	-	(6,118)	(11,277)	(11,481)	(28,876)
Carrying value	-	-	31,994	5,537	1,069	38,600
Past due but not impaired:						
up to 30 days	-	-	62,977	13,181	-	76,158
31 to 60 Days	-	-	8,585	1,050	-	9,635
61 to 90 days	-	-	7,468	711	-	8,179
Carrying value	-	-	79,030	14,942	-	93,972
Neither past due nor impaired	17,765	77,145	452,238	135,120	27,001	709,269
Carrying value	17,765	77,145	452,238	135,120	27,001	709,269
Sovereign	38,859	3,700	7,609	25,179	199,836	275,183
Carrying value	38,859	3,700	7,609	25,179	199,836	275,183
Collective impairment	-	-	(9,049)	(1,898)	-	(10,947)
	56,624	80,845	561,822	178,880	227,906	1,106,077

Restructured facilities during the year amounted to BD 11,267 thousand (2017: BD 24,586 thousand).

**b. Liquidity Risk**

Liquidity risk is the risk that the Group will be unable to meet its liabilities when they fall due. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to cease immediately. To guard against this risk, the Group has a large customer base and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents, commodity Murabaha, Wakala receivables, credit lines and quoted investments. The Group has leveraged part of its sukuk portfolio by obtaining medium term financing maturing in one year.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

## 27 RISK MANAGEMENT (continued)

## b. Liquidity Risk (continued)

**Maturity profile of Group's assets and liabilities**

The table below summarises the maturity profile of the Group's assets and liabilities. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period from the consolidated statement of financial position date to the contractual maturity date and do not take account of the effective maturities as indicated by the Group's retention history of its equity of investment accountholders.

The maturity profile of assets, liabilities and equity of investment accountholders at 31 December 2018 was as follows:

	Up to 1 month	1 to 3 months	3 to 6 months	6 months to 1 year	1 to 3 years	Over 3 years	No fixed maturity	Total
	BD '000	BD '000	BD '000	BD '000	BD '000	BD '000	BD '000	BD '000
<b>ASSETS</b>								
Cash and balances with the banks and Central Bank	30,332	-	-	-	-	-	35,105	65,437
Placements with financial institutions	129,809	-	-	7,641	-	-	-	137,450
Financing assets	38,539	33,252	37,585	52,871	190,771	225,935	-	578,953
Ijarah Muntahia Bittamleek and Rental Receivables	661	14,592	2,015	3,505	21,351	144,747	-	186,871
Investment securities	-	5,774	20,069	1,611	50,017	129,763	32,819	240,053
Investment in associates	-	-	-	-	-	-	21,643	21,643
Investment in real estate	-	-	-	-	-	-	24,284	24,284
Property and equipment	-	-	-	-	-	-	13,641	13,641
Other assets	2	771	520	595	642	1,765	6,767	11,062
<b>Total assets</b>	<b>199,343</b>	<b>54,389</b>	<b>60,189</b>	<b>66,223</b>	<b>262,781</b>	<b>502,210</b>	<b>134,259</b>	<b>1,279,394</b>
<b>LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS</b>								
Placements from financial institutions	84,681	11,643	-	9,184	9,236	-	-	114,744
Placements from non-financial institutions and individual:	-	-	-	7,255	-	-	-	7,255
Borrowings from financial institutions	36,799	14,343	-	45,244	-	-	-	96,386
Customers' current accounts	26,648	-	-	-	-	106,596	-	133,244
Other liabilities	24,025	-	-	-	-	-	-	24,025
Equity of investment accountholders	184,394	125,390	87,384	119,493	29,991	239,339	-	785,991
<b>Total liabilities and equity of investment accountholders</b>	<b>356,547</b>	<b>151,376</b>	<b>87,384</b>	<b>181,176</b>	<b>39,227</b>	<b>345,935</b>	<b>-</b>	<b>1,161,645</b>
<b>Liquidity gap</b>	<b>(157,204)</b>	<b>(96,987)</b>	<b>(27,195)</b>	<b>(114,953)</b>	<b>223,554</b>	<b>156,275</b>	<b>134,259</b>	<b>117,749</b>
<b>Cumulative liquidity gap</b>	<b>(157,204)</b>	<b>(254,191)</b>	<b>(281,386)</b>	<b>(396,339)</b>	<b>(172,785)</b>	<b>(16,510)</b>	<b>117,749</b>	<b>-</b>

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**27 RISK MANAGEMENT (continued)****b. Liquidity risk (continued)**

The maturity profile of assets, liabilities and equity of investment accountholders at 31 December 2017 was as follows:

ASSETS	Up to	1 to 3	3 to 6	6 months	1 to 3	Over	No fixed	Total
	1 month	months	months	to 1 year	years	3 years	maturity	
	BD '000	BD '000	BD '000	BD '000	BD '000	BD '000	BD '000	BD '000
Cash and balances with the banks and Central Bank	34,461	-	-	-	-	-	35,205	69,666
Placements with financial institutions	80,845	-	-	-	-	-	-	80,845
Financing assets	23,595	28,150	29,159	63,784	65,411	351,723	-	561,822
Ijarah Muntahia Bittamleek and Rental Receivables	10,193	8,309	162	56	4,222	155,938	-	178,880
Investments securities	11,295	40,179	27,603	10,167	34,766	103,896	30,493	258,399
Investment in associates	-	-	-	-	-	-	23,739	23,739
Investment in real estate	-	-	-	-	-	-	29,831	29,831
Property and equipment	-	-	-	-	-	-	14,270	14,270
Other assets	5	310	397	357	1,527	8,599	-	11,195
Total assets	160,394	76,948	57,321	74,364	105,926	620,156	133,538	1,228,647
<b>LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS</b>								
Placements from financial institutions	61,086	6,786	-	-	-	-	-	67,872
Borrowings from financial institutions	-	63,488	-	38,088	-	-	-	101,576
Customers' current accounts	26,333	-	-	-	-	105,333	-	131,666
Other liabilities	11,507	-	-	-	-	-	-	11,507
Equity investment accountholders	206,961	102,475	146,113	72,960	9,334	255,913	-	793,756
Total liabilities and equity of investment accountholders	305,887	172,749	146,113	111,048	9,334	361,246	-	1,106,377
Liquidity gap	(145,493)	(95,801)	(88,792)	(36,684)	96,592	258,910	133,538	122,270
Cumulative liquidity gap	(145,493)	(241,294)	(330,086)	(366,770)	(270,178)	(11,268)	122,270	-

**27 RISK MANAGEMENT (continued)**

**c. Market Risk**

The Group has accepted the definition of market risk as defined by CBB as “the risk of losses in on and off balance sheet positions arising from movements in market prices.

**i. Profit rate risk**

Profit rate risk is the sensitivity of financial products to changes in the profit rates. Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Group's management believe that the Group is not exposed to material profit rate risk as a result of mismatches of profit rate repricing of assets, liabilities, and equity of investment accountholders as the repricing of assets, liabilities and equity of investment accountholders occur at similar intervals. The profit distribution to equity of investment accountholders is based on profit sharing agreements. Therefore, the Group is not subject to any significant profit rate risk.

However, the profit sharing agreements will result in displaced commercial risk when the Group's results do not allow the Group to distribute profits inline with the market rates.

**ii. Equity price risk**

Equity price risk is the sensitivity of financial products to the changes in equity prices. Equity risk arises from holding open positions in equities or equity based instruments, thereby creating exposure to a change in the market price of the equity. In addition to Group performance expectations, equity prices are also susceptible to general economic data and sector performance expectations.

In order to measure the risk of equity on its financial positions, the Group adopts a sensitivity analysis on its quoted equity portfolio for a 10% increase of the portfolio value with all other variables remaining constant. The effect of a similar decrease in equity prices is expected to be equal and opposite to the effect of the increase shown.

As at the consolidated statement of financial position date, the Group has unquoted (equities and sukuk) of BD 122 million (31 December 2017: BD 115 million). The impact of changes in the value of these unquoted equities and sukuk and the related impact on equity will only be reflected when the financial instrument is sold or deemed to be impaired.

**27 RISK MANAGEMENT (continued)****c. Market Risk (continued)****iii. Foreign exchange risk**

Foreign exchange risk is the sensitivity of financial products to changes in spot foreign exchange rates. The value of the Group's portfolio which is denominated in a number of currencies may be exposed to these risks when converted back to the Group's base currency.

The Group had the following significant net exposures denominated in foreign currencies as of 31 December:

	<i><b>Equivalent Long (short)</b></i>	<i><b>Equivalent Long (short)</b></i>
	<i><b>2018</b></i>	<i><b>2017</b></i>
	<i><b>BD '000</b></i>	<i><b>BD '000</b></i>
<b>Currency</b>		
Pound Sterling	<b>(1,075)</b>	(1,020)
Euro	<b>(1,084)</b>	(985)
CAD	<b>(50)</b>	(4)
JPY	<b>(15)</b>	(6)
Kuwaiti Dinars	<b>(9,619)</b>	(8,659)

As the Bahraini Dinar is pegged to the US Dollar, positions in US Dollars are not considered to represent significant foreign exchange risk.

Moreover, as the Group does not have significant exposures in other currencies, movement of the currency exchange rates against the Bahraini Dinar with other variables held constant will have an immaterial impact on the consolidated income statement and owners' equity.

**iv. Commodity risk**

Commodity risk is defined as inherent risk in financial products arising from their sensitivity to changes in commodity prices. Since prices in commodity markets are determined by fundamental factors (i.e. supply and demand of the underlying commodity) these markets may be strongly correlated within particular sector and less correlated across sectors.

**d. Operational Risk**

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Group cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Group is able to manage the risks. Controls include effective segregation of duties, access, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the year ended 31 December 2018

**28 SEGMENTAL INFORMATION**

For management purposes, the Group is organized into three major business segments;

Corporate	Principally handling equity of corporate investment accountholders', corporate current accounts, and providing Islamic financing facilities to corporate customers.
Retail	Principally handling equity of individual retail customers' investment accountholders', retail current accounts, and providing Islamic financing facilities to individual customers.
Investment	Principally handling equity of banks' and financial institutions' investment accountholders, providing money market, trading and treasury services as well as the management of the Group's investment activities. Investment activities involve handling investments in local and international markets and investment in properties.

These segments are the basis on which the Group reports its primary segment information. Transactions between segments are conducted at estimated market rates on an arm's length basis. Transfer charges are based on a pool rate which approximates the cost of funds.

Segment information is disclosed as follows:

	<b>31 December 2018</b>			
	<b>Corporate BD'000</b>	<b>Retail BD'000</b>	<b>Investment BD'000</b>	<b>Total BD'000</b>
Total net income	10,139	23,611	11,781	45,531
Total expenses	(5,157)	(17,914)	(2,184)	(25,255)
Provision for impairment	(3,808)	(740)	(4,347)	(8,895)
<b>Profit for the year</b>	<b>1,174</b>	<b>4,957</b>	<b>5,250</b>	<b>11,381</b>
<b>Other information</b>				
Segment assets	365,325	465,835	448,234	1,279,394
Segment liabilities, and equity	410,663	544,700	324,031	1,279,394
	<b>31 December 2017</b>			
	<b>Corporate BD'000</b>	<b>Retail BD'000</b>	<b>Investment BD'000</b>	<b>Total BD'000</b>
Total income	10,732	27,170	5,004	42,906
Total expenses	(5,043)	(18,154)	(3,371)	(26,568)
Provision for impairment	(7,399)	529	673	(6,197)
<b>Profit / (loss) for the year</b>	<b>(1,710)</b>	<b>9,545</b>	<b>2,306</b>	<b>10,141</b>
<b>Other information</b>				
Segment assets	330,624	455,535	442,488	1,228,647
Segment liabilities, and equity	450,926	517,873	259,848	1,228,647

The Group operates solely in the Kingdom of Bahrain and, as such, no geographical segment information is presented.

## 29 FINANCIAL INSTRUMENTS

### *Fair value hierarchy*

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

Fair values of quoted securities / Sukuk are derived from quoted market prices in active markets, if available. In case of financing assets and Ijarah Muntahia Bittamleek, the average profit rate of the portfolio is in line with current market rates for similar facilities and hence after consideration of adjustment for prepayment risk and impairment charges, it is expected that the current value would not be materially different to fair value of these assets. None of the Group's financial instruments are at fair value.

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

**Level 1:** 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; 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.

## 30 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

The Group is committed to avoid recognising any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a Qard fund account where the Group uses these funds for various charitable purposes. The movements in these funds is shown in statement of sources and uses of good faith Qard fund. The non-Islamic income includes the penalties charged on late repayments for Islamic facilities.

## 31 SHARI'A SUPERVISORY BOARD

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

## 32 SOCIAL RESPONSIBILITY

The Group discharges its social responsibilities through Zakah and charity fund's expenditures and donations to good faith Qard fund for marriage, refurbishment, medical treatments, etc.

## 33 COMPARATIVE FIGURES

Certain of the prior year's figures have been reclassified to conform to the presentation adopted in the current year. Such reclassification did not affect previously reported profit for the year or total owners' equity.