# Al Salam Bank-Bahrain B.S.C.

## CONSOLIDATED FINANCIAL STATEMENTS

### 31 DECEMBER 2015

EY
Building a better working world

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# INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF AL SALAM BANK-BAHRAIN B.S.C.

## Report on the consolidated financial statements

We have audited the accompanying consolidated statement of financial position of Al Salam Bank-Bahrain B.S.C. ["the Bank"] and its subsidiaries [together "the Group"] as of 31 December 2015, and the related consolidated statements of income, cash flows and changes in equity for the year then ended. 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 Bank's Board of Directors. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ["AAOIFI"]. 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 the Bank's Board of Directors, as well as evaluating the overall consolidated financial statements presentation. We believe that our audit provides a reasonable basis for our opinion.

## Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as of 31 December 2015, the results of its operations, its cash flows and changes in equity for the year then ended in accordance with the Financial Accounting Standards issued by AAOIFI.

## Other matters

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

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

b) the financial information contained in the report of the Board of Directors is consistent with the consolidated financial statements.

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**INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF AL SALAM BANK-BAHRAIN B.S.C. (continued)**

**Other matters (continued)**

We are not aware of any violations of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 2 and applicable provisions of Volume 6) and CBB directives, regulations and associated resolutions, rules and procedures of the Bahrain Bourse or the terms of the Bank's memorandum and articles of association during the year ended 31 December 2015 that might have had a material adverse effect on the business of the Bank or on its consolidated financial position. Satisfactory explanations and information have been provided to us by management in response to all our requests. The Bank has also complied with the Islamic Shari'a Rules and Principles as determined by the Shari'a Supervisory Board of the Bank.

Ernst + Young

Partner's Registration No. 115
9 February 2016
Manama, Kingdom of Bahrain

# CONSOLIDATED STATEMENT OF FINANCIAL POSITION

31 December 2015

| | Note | 2015<br>BD '000 | 2014<br>BD '000 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with banks and Central Bank | 5 | **152,572** | 277,751 |
| Sovereign Sukuk | | **313,109** | 145,789 |
| Murabaha and Wakala receivables from banks | 6 | **103,345** | 182,110 |
| Corporate Sukuk | 7 | **64,157** | 88,193 |
| Murabaha financing | 8 | **268,848** | 270,428 |
| Mudaraba financing | 8 | **239,031** | 189,601 |
| Ijarah Muntahia Bittamleek | 10 | **155,217** | 141,052 |
| Musharaka | | **7,154** | 10,851 |
| Assets under conversion | 11 | **32,032** | 308,659 |
| Non-trading investments | 12 | **123,514** | 147,096 |
| Investments in real estate | 13 | **68,786** | 65,149 |
| Development properties | 14 | **49,021** | 59,262 |
| Investment in associates | 15 | **9,994** | 10,492 |
| Other assets | 16 | **43,892** | 32,893 |
| Goodwill | 3 | **25,971** | 25,971 |
| **TOTAL ASSETS** | | **1,656,643** | 1,955,297 |
| **LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS AND OWNERS' EQUITY** | | | |
| **LIABILITIES** | | | |
| Murabaha and Wakala payables to banks | | **120,795** | 121,266 |
| Murabaha and Wakala payables to non-banks | | **842,570** | 1,034,052 |
| Current accounts | | **224,366** | 226,648 |
| Liabilities under conversion | 11 | **2,327** | 149,621 |
| Term financing | 17 | **35,986** | 21,337 |
| Other liabilities | 18 | **48,246** | 45,418 |
| **TOTAL LIABILITIES** | | **1,274,290** | 1,598,342 |
| **EQUITY OF INVESTMENT ACCOUNTHOLDERS** | 19 | **62,351** | 28,152 |
| **OWNERS' EQUITY** | | | |
| Share capital | 20 | **214,093** | 214,093 |
| Reserves and retained earnings | | **94,140** | 93,777 |
| Proposed appropriations | 20 | **10,705** | 10,705 |
| Total equity attributable to shareholders of the Bank | | **318,938** | 318,575 |
| Non-controlling interest | | **1,064** | 10,228 |
| **TOTAL OWNERS' EQUITY** | | **320,002** | 328,803 |
| **TOTAL LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS AND OWNERS' EQUITY** | | **1,656,643** | 1,955,297 |

Sh. Hessa Bint Khalifa Al Khalifa
Chairperson of the Board

Yousif A. Taqi
Director & Chief Executive Officer

The attached notes 1 to 42 form part of these consolidated financial statements.

# CONSOLIDATED INCOME STATEMENT

Year ended 31 December 2015

| | Note | 2015 BD '000 | 2014 BD '000 |
|---|---|---|---|
| **OPERATING INCOME** | | | |
| Income from financing contracts | 22 | 48,230 | 51,494 |
| Income from Sukuk | | 13,109 | 7,120 |
| Gains on sale of investments and Sukuk | 23 | 8,334 | 12,282 |
| Income from investments | 24 | 3,249 | 2,863 |
| Fair value changes on investments | | 399 | (6,413) |
| Dividend income | | 820 | 758 |
| Foreign exchange gains | | 870 | 1,578 |
| Fees, commission and other income - net | 25 | 9,184 | 6,650 |
| | | 84,195 | 76,332 |
| Profit on Murabaha and Wakala payables to banks | | (931) | (1,035) |
| Profit on Wakala payables to non-banks | | (23,805) | (28,040) |
| Profit on term financing | | (839) | (974) |
| Return on equity of investment accountholders before Group's share as a Mudarib | 19 | (1,471) | (391) |
| Group's share as a Mudarib | 19 | 662 | 176 |
| | | (809) | (215) |
| Total operating income | | 57,811 | 46,068 |
| **OPERATING EXPENSES** | | | |
| Staff cost | | 12,474 | 13,991 |
| Premises and equipment cost | | 2,752 | 2,415 |
| Depreciation | | 1,821 | 1,507 |
| Other operating expenses | | 8,220 | 8,505 |
| Total operating expenses | | 25,267 | 26,418 |
| **PROFIT BEFORE PROVISIONS AND RESULTS OF ASSOCIATES** | | 32,544 | 19,650 |
| Provision for impairment - net | 9 | (22,851) | (4,198) |
| Share of profit from associates | 15 | 855 | 369 |
| Net profit for the year | | 10,548 | 15,821 |
| **ATTRIBUTABLE TO:** | | | |
| **- SHAREHOLDERS OF THE BANK** | | 12,346 | 15,550 |
| - Non-controlling interest | | (1,798) | 271 |
| | | 10,548 | 15,821 |
| **Weighted average number of shares (in '000)** | | 2,140,931 | 1,982,531 |
| **Basic and diluted earnings per share (fils)** | | 5.8 | 8.0 |

Sh. Hessa Bint Khalifa Al Khalifa
Chairperson of the Board

Yousif A. Taqi
Director & Chief Executive Officer

The attached notes 1 to 42 form part of these consolidated financial statements.

# CONSOLIDATED STATEMENT OF CASH FLOWS

Year ended 31 December 2015

| | Note | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|---|
| **OPERATING ACTIVITIES** | | | |
| Net profit for the year | | **10,548** | 15,821 |
| Adjustments: | | | |
| Depreciation | | **1,821** | 1,507 |
| Amortisation of premium on Sukuk | | **1,945** | 3,509 |
| Fair value changes on investments | | **(399)** | 6,413 |
| Provision for impairment - net | | **22,851** | 4,198 |
| Share of profit from associates | | **(855)** | (369) |
| Operating income before changes in operating assets and liabilities | | **35,911** | 31,079 |
| **Changes in operating assets and liabilities:** | | | |
| Mandatory reserve with Central Bank | | **10,109** | (22,400) |
| Sovereign Sukuk | | **(168,112)** | 79,767 |
| Murabaha and Wakala receivables from banks with original maturities of 90 days or more | | **8,976** | 4,358 |
| Corporate Sukuk | | **22,883** | (41,342) |
| Murabaha financing | | **52,916** | (102,733) |
| Mudaraba financing | | **(4,886)** | (59,890) |
| Ijarah Muntahia Bittamleek | | **11,033** | (2,319) |
| Musharaka financing | | **4,272** | 8,294 |
| Assets under conversion | | **140,870** | 130,707 |
| Other assets | | **(20,187)** | (2,901) |
| Murabaha and Wakala payables to banks | | **(471)** | (38,874) |
| Wakala from non-banks | | **(245,716)** | 91,894 |
| Current accounts | | **(2,282)** | 105,438 |
| Liabilities under conversion | | **(64,855)** | (59,800) |
| Other liabilities | | **2,729** | 3,216 |
| Net cash (used in) from operating activities | | **(216,810)** | 124,494 |
| **INVESTING ACTIVITIES** | | | |
| Investments and investment in associates, net | | **21,464** | (13,604) |
| Investments in real estate and development properties, net | | **8,153** | 9,238 |
| Cash flow arising on acquisition of a subsidiary | 3 | **-** | 127,670 |
| Sale of treasury stock | | **-** | 1,754 |
| Purchase of premises and equipment | | **(237)** | (1,015) |
| Net cash from investing activities | | **29,380** | 124,043 |
| **FINANCING ACTIVITIES** | | | |
| Term financing | | **14,649** | (2,300) |
| Equity of investment accountholders | | **5,994** | (84) |
| Share issue expenses | | **-** | (125) |
| Dividends paid | | **(10,705)** | (7,446) |
| Dividends paid to non-controlling interest | | **(566)** | (345) |
| Net movements in non-controlling interest | | **(6,800)** | (742) |
| Net cash from (used in) financing activities | | **2,572** | (11,042) |
| **NET CHANGE IN CASH AND CASH EQUIVALENTS** | | **(184,858)** | 237,495 |
| Cash and cash equivalents at 1 January | | **408,535** | 171,040 |
| **CASH AND CASH EQUIVALENTS AT 31 DECEMBER** | | **223,677** | 408,535 |
| **Cash and cash equivalents comprise of:** | | | |
| Cash and other balances with Central Bank of Bahrain | 5 | **81,448** | 187,313 |
| Balances with other banks | 5 | **38,884** | 48,088 |
| Murabaha and Wakala receivables from banks with original maturities of less than 90 days | | **103,345** | 173,134 |
| | | **223,677** | 408,535 |

The attached notes 1 to 42 form part of these consolidated financial statements.

Al Salam Bank-Bahrain B.S.C.

# CONSOLIDATED STATEMENT OF CHANGES IN OWNERS' EQUITY

Year ended 31 December 2015

*Amounts in BD '000s*

| | *Attributable to shareholders of the Bank* | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | *Share capital* | *Treasury stock* | *Statutory reserve* | *Retained earnings* | *Changes in fair value* | *Real estate fair value reserve* | *Foreign exchange translation reserve* | *Share premium reserve* | *Total reserves* | *Proposed appropriations* | *Total* | *Non-controlling interest* | *Total owners' equity* |
| **Balance as of 1 January 2015** | **214,093** | **-** | **12,481** | **46,497** | **1,287** | **22,704** | **(1,401)** | **12,209** | **93,777** | **10,705** | **318,575** | **10,228** | **328,803** |
| Net profit for the year | - | - | - | 12,346 | - | - | - | - | 12,346 | - | 12,346 | (1,798) | 10,548 |
| Net changes in fair value | - | - | - | - | (1,435) | 1,549 | - | - | 114 | - | 114 | - | 114 |
| Foreign currency re-translation | - | - | - | - | - | - | (1,292) | - | (1,292) | - | (1,292) | (180) | (1,472) |
| Dividend paid | - | - | - | - | - | - | - | - | - | (10,705) | (10,705) | - | (10,705) |
| Proposed dividend for 2015 | - | - | - | (10,705) | - | - | - | - | (10,705) | 10,705 | - | - | - |
| Dividend relating to subsidiaries | - | - | - | - | - | - | - | - | - | - | - | (566) | (566) |
| Net movements in non-controlling interest | - | - | - | - | - | - | - | - | - | - | - | (6,620) | (6,620) |
| Transfer to statutory reserve | - | - | 1,235 | (1,235) | - | - | - | - | - | - | - | - | - |
| Charitable donations | - | - | - | (100) | - | - | - | - | (100) | - | (100) | - | (100) |
| **Balance at 31 December 2015** | **214,093** | **-** | **13,716** | **46,803** | **(148)** | **24,253** | **(2,693)** | **12,209** | **94,140** | **10,705** | **318,938** | **1,064** | **320,002** |
| Balance as of 1 January 2014 | 149,706 | (492) | 10,926 | 43,272 | 651 | 21,659 | (501) | 2,573 | 78,580 | 7,485 | 235,279 | 10,818 | 246,097 |
| Net profit for the year | - | - | - | 15,550 | - | - | - | - | 15,550 | - | 15,550 | 271 | 15,821 |
| Net changes in fair value | - | - | - | - | 636 | 1,045 | - | - | 1,681 | - | 1,681 | - | 1,681 |
| Foreign currency re-translation | - | - | - | - | - | - | (900) | - | (900) | - | (900) | 81 | (819) |
| Dividend paid | - | - | - | - | - | - | - | - | - | (7,446) | (7,446) | - | (7,446) |
| Proposed dividend for 2014 | - | - | - | (10,705) | - | - | - | - | (10,705) | 10,705 | - | - | - |
| Dividend relating to subsidiaries | - | - | - | - | - | - | - | - | - | - | - | (345) | (345) |
| Shares issued on acquisition | 64,387 | - | - | - | - | - | - | 8,499 | 8,499 | - | 72,886 | - | 72,886 |
| Share issue expenses | - | - | - | - | - | - | - | (125) | (125) | - | (125) | - | (125) |
| Net movements in non-controlling interest | - | - | - | (4) | - | - | - | - | (4) | - | (4) | (597) | (601) |
| Sale of treasury stock | - | 492 | - | - | - | - | - | 1,262 | 1,262 | - | 1,754 | - | 1,754 |
| Transfer to statutory reserve | - | - | 1,555 | (1,555) | - | - | - | - | - | - | - | - | - |
| Transfer | - | - | - | 39 | - | - | - | - | 39 | (39) | - | - | - |
| Charitable donations | - | - | - | (100) | - | - | - | - | (100) | - | (100) | - | (100) |
| Balance at 31 December 2014 | 214,093 | - | 12,481 | 46,497 | 1,287 | 22,704 | (1,401) | 12,209 | 93,777 | 10,705 | 318,575 | 10,228 | 328,803 |

The attached notes 1 to 42 form part of these consolidated financial statements.

## 1 INCORPORATION AND PRINCIPAL ACTIVITIES

Al Salam Bank-Bahrain B.S.C. ("the Bank") was incorporated in the Kingdom of Bahrain under the Bahrain Commercial Companies Law No. 21/2001 and is registered with Ministry of Industry and Commerce ("MOIC") under Commercial Registration Number 59308 on 19 January 2006. The Bank is regulated and supervised by the Central Bank of Bahrain ("the CBB") and has an Islamic retail banking license and is operating under Islamic principles, and in accordance with all the relevant regulatory guidelines for Islamic banks issued by the CBB. The Bank's registered office is P.O. Box 18282, Bahrain World Trade Centre East Tower, King Faisal Highway, Manama 316, Kingdom of Bahrain.

On 30 March 2014, the Bank acquired 100% stake in BMI Bank B.S.C.(c) ("BMI"), a closed shareholding company in the Kingdom of Bahrain, through exchange of shares. The current year numbers include the effect of consolidation of BMI and the comparatives include the results of BMI for the period from 1 April 2014 to 30 September 2014 as the acquisition was completed on 30 March 2014. BMI operates under a retail conventional banking license issued by the CBB. BMI's Shari'a Supervisory Board approved BMI to be an Islamic Bank effective 1 January 2015 and approved all conventional income of BMI to be recognised in the consolidated income statement for the year ended 31 December 2015.

The Bank and its subsidiary BMI operate through eleven branches in the Kingdom of Bahrain and offers a full range of Shari'a-compliant banking services and products. The activities of the Bank include managing profit sharing investment accounts, offering Islamic financing contracts, dealing in Shari'a-compliant financial instruments as principal/agent, managing Shari'a-compliant financial instruments and other activities permitted for under the CBB's Regulated Islamic Banking Services as defined in the licensing framework. The Bank's ordinary shares are listed in the Bahrain Bourse and Dubai Financial Market.

In addition to BMI, the principal subsidiaries are as follows:

| *Name of entity* | *Nature of entity* | *% holding 2015* | *2014* |
|---|---|---|---|
| Al Salam Leasing Two Ltd ("ASL II") | Aircraft under lease (note 16) | 76% | 76% |
| Auslog Holding Trust | Investment in real estates | 90% | 90% |
| Al Salam Asia REIT Fund | Open-ended mutual fund | - | 44% |

The Bank together with its subsidiaries is referred to as "the Group".

These consolidated financial statements have been authorised for issue in accordance with a resolution of the Board of Directors dated 9 February 2016.

## 2 ACCOUNTING POLICIES

### 2.1 BASIS OF PREPARATION

The consolidated financial statements are prepared on a historical cost basis, except for investments held at fair value through profit or loss, available-for-sale equity investments and investments in real estates which are held at fair value. These consolidated financial statements incorporate all assets, liabilities and off balance sheet financial instruments held by the Group.

These consolidated financial statements are presented in Bahraini Dinars, being the functional and presentation currency of the Group, rounded to the nearest thousand [BD '000], except where otherwise indicated.

#### 2.1.a Statement of compliance

The consolidated financial statements of the Group are prepared in accordance with the Financial Accounting Standards (FAS) issued by the Accounting and Auditing Organisation for Islamic Financial Institutions ("AAOIFI"), the Islamic Sharia' rules and principles as determined by the Sharia' Supervisory Board of the Group and in conformity with the Bahrain Commercial Companies Law and the CBB and Financial Institutions Law. Matters for which no AAOIFI standards exist, the Group uses the relevant International Financial Reporting Standard.

The Group presents its consolidated statement of financial position broadly in order of liquidity. An analysis regarding recovery or settlement within 12 months after the consolidated statement of financial position date (current) and more than 12 months after the consolidated statement of financial position date (non-current) is presented in Note 32.

## 2 ACCOUNTING POLICIES (continued)

### 2.1 BASIS OF PREPARATION (continued)

#### 2.1.b Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiaries as at 31 December 2015. The financial statements of the subsidiaries are prepared for the same reporting year as the Bank, using consistent accounting policies. All intra-group balances, transactions, income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full.

Subsidiaries are fully consolidated from the date on which control is transferred to the Group and continue to be consolidated until the date when such control ceases. Control is achieved where the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The results of subsidiaries acquired or disposed of during the year, if any, are included in the consolidated statement of income from the date of acquisition or up to the date of disposal, as appropriate. A change in the Group's ownership of a subsidiary, without a loss of control, is accounted for as an equity transaction.

Share of minority stakeholder' interest (non-controlling interest) represents the portion of profit or loss and net assets not held by the Group and are presented separately in the consolidated statement of income and within owners' equity in the consolidated statement of financial position, separately from the equity attributable to shareholders of the parent.

### 2.2 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES

The preparation of the consolidated financial statements requires management to make judgements and estimates that affect the reported amount of financial assets and liabilities and disclosure of contingent liabilities. These judgements and estimates also affect the revenues and expenses and the resultant provisions as well as fair value changes reported in equity.

*Classification of investments*

Management decides upon acquisition of an investment whether it should be classified as fair value through profit or loss, available for sale or held-to-maturity.

**Estimation uncertainty**

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

*Impairment of goodwill*

Impairment exists when carrying value of an asset or cash generating unit (CGU) exceeds its recoverable amount, which is the higher of its fair value less costs of disposal and its value in use.

The recoverable amount of each cash-generating unit's goodwill is based on value-in-use calculations using cash flow projections from financial budgets approved by the Board of Directors, extrapolated for five year projections using nominal projected Gross Domestic Product growth rate.

The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

*Collective impairment provisions on financial contracts*

In addition to specific provisions against individually significant financial contracts, the Group also considers the need for a collective impairment provision against financial contracts which although not specifically identified as requiring a specific provision, have a greater risk of default than when originally granted. This collective provision is based on any deterioration in the status, as determined by the Group, of the financial contracts since they were granted (acquired). The amount of the provision is based on the historical loss pattern for other contracts within each grade and is adjusted to reflect current economic changes.

*Impairment losses on financial contracts*

The Group reviews its financial contracts on a regular basis to assess whether a provision for impairment should be recorded in the consolidated statement of income. In particular, considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions. During the last interim period of the year, the Group re-assessed its previous estimates and made provisions for financing facilities and other assets.

## 2 ACCOUNTING POLICIES (continued)

### 2.2 SIGNIFICANT ACCOUNTING JUDGEMENTS AND ESTIMATES (continued)

**Estimation uncertainty (continued)**

*Impairment of available-for-sale equity investments*
The Group treats available-for-sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of significant or prolonged decline and other objective evidence involves judgement. In addition, the Group evaluates other factors, including normal volatility in share price for quoted equities and the future cash flows and the present value calculation factors for unquoted equities.

*Valuation of unquoted private equity and real estate investments*
Valuation of above investments involves judgement and is normally based on one of the following:

- valuation by independent external valuers;
- recent arm's length market transactions;
- current fair value of another instrument that is substantially the same;
- present value of expected cash flows at current rates applicable for items with similar terms and risk characteristics; or
- other valuation models.

The Group calibrates the valuation techniques periodically and tests these for validity using either prices from observable current market transactions in the same instrument or other available observable market data.

**Going concern**
The Group has made an assessment of the Group's ability to continue on 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 consolidated financial statements continue to be prepared on the going concern basis.

**Control over special purpose entities**
The Group sponsors the formation of special purpose entities (SPEs) primarily for the purpose of allowing clients to hold investments. The Group does not consolidate SPEs that it does not have the power to control. In determining whether the Group has the power to control an SPE, judgements are made about the objectives of the SPEs activities, Group's exposures to the risk and rewards, as well as its ability to make operational decisions of the SPEs.

### 2.3 SIGNIFICANT ACCOUNTING POLICIES

#### 2.3.1 New standards, interpretations and amendments
These consolidated financial statements have been prepared using accounting policies, which are consistent with those used in the preparation of the annual consolidated financial statements for the year ended 31 December 2014, except for FAS 27 and amendment to FAS 23 which have been issued by AAOIFI and are effective 1 January 2016.

- ***Amendment to FAS 23 – Consolidation***

The amendment introduced to FAS 23 is to give clarification on the way an Islamic financial institution (IFI) should determine if financial statements of an investee company, or a subsidiary, should be consolidated with its own. The amendment provides clarification that, in addition to the existing stipulations in the standard, control may also exist through rights arising from other contractual arrangement, voting rights of the Islamic financial institutions that give de facto power over an entity, potential voting rights, or a combination of these factors. In terms of voting rights, the amendment also clarifies that an Islamic financial institution shall consider only substantive voting rights in its assessment of whether the institution has power over an entity. In order to be substantive, the voting rights need to be exercisable when relevant decisions are required to be made and the holder of such rights must have the practical ability to exercise those rights. Determination of voting rights shall include current substantive voting rights and currently-exercisable voting rights.

The amendments and clarifications are effective for the annual financial periods ending on or after 31 December 2015. The transition provision requires retrospective application including restatement of previous period comparatives. The amendment had no impact on the consolidated financial statements of the Group.

**2 ACCOUNTING POLICIES (continued)**

**2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.3.1 New standards, interpretations and amendments (continued)**

- ***FAS 27 – Investment Accounts***

FAS 27 will replace FAS 5 - 'Disclosures of Bases for Profit Allocation between Owner's Equity and Investment Account Holders' and FAS 6 - 'Equity of Investment Account Holders and their Equivalent'. Upon adoption of this standard certain disclosures with respect to investment account holders and bases of profit allocation will be enhanced without having any significant impact on the financial statements of the Group.

**2.3.2 Summary of significant accounting policies**

**a) Financial contracts**

Financial contracts consist of balances with banks and the Central Bank, Sovereign Sukuk, Corporate Sukuk, Murabaha financing (net of deferred profit), Mudaraba, Musharaka and Ijarah Muntahia Bittamleek. Balances relating to these contracts are stated net of provisions for impairment.

**b) Sovereign Sukuk and corporate sukuk**

These are quoted / unquoted securities and classified as investments at amortised cost in accordance with FAS 25 issued by AAOIFI.

**c) Murabaha receivables**

Murabaha is a contract whereby one party ("Seller") sells an asset to the other party ("Purchaser") at cost plus profit and on a deferred payment basis, after the Seller has purchased the asset based on the Purchaser's promise to purchase the same on such Murabaha basis. The sale price comprises the cost of the asset and an agreed profit margin. The sale price (cost plus the profit amount) is paid by the Purchaser to the Seller on installment basis over the agreed finance tenure. Under the Murabaha contract the Group may act either as a Seller or a Purchaser, as the case may be.

The Group considers the promise to purchase made by the Purchaser in a Murabaha transaction in favour of the Seller to be binding.

Murabaha receivables are stated at cost, net of deferred profits, provision for impairment, if any, and amounts settled.

**d) Mudaraba financing**

Mudaraba is a contract between two parties whereby one party is a fund provider (Rab Al Mal) who would provide a certain amount of funds (Mudaraba Capital), to the other party (Mudarib). Mudarib would then invest the Mudaraba Capital in a specific enterprise or activity deploying its experience and expertise for a specific pre-agreed share in the resultant profit. The Rab Al Mal is not involved in the management of the Mudaraba activity. The Mudarib would bear the loss in case of its default, negligence or violation of any of the terms and conditions of the Mudaraba contract; otherwise the loss would be borne by the Rab Al Mal. Under the Mudaraba contract the Group may act either as Mudarib or as Rab Al Mal, as the case may be.

Mudaraba financing are recognized at fair value of the Mudaraba assets net of provision for impairment, if any, and Mudaraba capital amounts settled. If the valuation of the Mudaraba assets results in difference between fair value and book value, such difference is recognized as profit or loss to the Group.

**e) Ijarah Muntahia Bittamleek**

Ijara (Muntahia Bittamleek) is an agreement whereby the Group (as lessor) leases an asset to the customer (as lessee) (after purchasing/acquiring the specified asset, either from a third party seller or from the customer itself, according to the customer's request and promise to lease) against certain rental payments for a specific lease term/periods, payable on fixed or variable rental basis.

The Ijara agreement specifies the leased asset, duration of the lease term, as well as, the basis for rental calculation, the timing of rental payment and responsibilities of both parties during the lease term. The customer (lessee) provides the Group (lessor) with an undertaking to renew the lease periods and pay the relevant rental payment amounts as per the agreed schedule and applicable formula throughout the lease term.

## 2 ACCOUNTING POLICIES (continued)

## 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.3.2 Summary of significant accounting policies (continued)

**e) Ijarah Muntahia Bittamleek (continued)**

The Group (lessor) retains the ownership of the assets throughout the lease term. At the end of the lease term, upon fulfillment of all the obligations by the customer (lessee) under the Ijara agreement, the Group (lessor) will sell the leased asset to the customer (lessee) for a nominal value based on sale undertaking given by the Group (lessor). Leased assets are usually residential properties, commercial real estate or aircrafts.

Depreciation is provided on a systematic basis on all Ijarah Muntahia Bittamleek assets other than land (which is deemed to have an indefinite life), at rates calculated to write off the cost of each asset over the shorter of either the lease term or economic life of the asset.

**f) Musharaka**

Musharaka is used to provide venture capital or project finance. The Group and customer contribute towards the capital of the Musharaka. Usually a special purpose company or a partnership is established as a vehicle to undertake the Musharaka. Profits are shared according to a pre-agreed profit distribution ratio but losses are borne by the partners according to the capital contributions of each partner. Capital contributions may be in cash or in kind, as valued at the time of entering into the Musharaka.

Musharaka is stated at cost, less any impairment.

**g) Assets and liabilities under conversion**

***Assets under conversion:***

*Due from Banks and financial institutions*
At amortised cost less any amounts written off and provision for impairment, if any.

*Loans and advances*
At amortised cost less any amounts written off and provision for impairment, if any.

*Non-trading investments*
These are classified as available-for-sale investments and are fair valued based on criteria set out in Note 2.3.2 h. Any changes in fair values subsequent to acquisition date are recognized in total comprehensive income (note 26).

***Liabilities under conversion:***
These are remesured at amortised cost.

**h) Non-trading investments**

These classified as available-for-sale or fair value through profit or loss.

All investments are initially recognised at cost, being the fair value of the consideration given including acquisition costs associated with the investment. Acquisition cost relating to investments designated as fair value through profit or loss is charged to consolidated income statement.

Following the initial recognition of investments, the subsequent period-end reporting values are determined as follows:

*Investments available-for-sale*
After initial recognition, equity investments which are classified as investments at fair value through equity are disclosed as "available-for-sale investments". These are normally remeasured at fair value, unless the fair value cannot be reliably determined, in which case they are measured at cost less impairment. Fair value changes are reported in equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment the cumulative gain or loss previously reported as "changes in fair value" within equity, is included in the consolidated income statement.

**2 ACCOUNTING POLICIES (continued)**

**2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.3.2 Summary of significant accounting policies (continued)**

**h) Non-trading investments (continued)**

*Investments available-for-sale (continued)*
Impairment losses on available-for-sale investments are not reversed through the consolidated statement of income and increases in their fair value after impairment are recognised directly in owners' equity.

*Investments carried at fair value through profit or loss*
Investments in this category are designated as such on initial recognition if these investments are evaluated on a fair value basis in accordance with the Group's risk management policy and its investment strategy. These include all private equity investments including those in joint ventures and associates which are not strategic in nature.

Investments at fair value through profit or loss are recorded in the consolidated statement of financial position at fair value. Changes in fair value are recorded as "Fair value changes on investments" in the consolidated income statement. Gain on sale of these investments is included in "Gain on sale of investments and sukuk" in the consolidated income statement. Income earned on these investments is included in "Income from investments" in the consolidated income statement.

**i) Investments in associates**
The Group's investments in associates, that are acquired for strategic purposes, are accounted for under the equity method of accounting. Other equity investments in associates are accounted for as fair value through profit or loss by availing the scope exemption under FAS 24, Investments in Associates. An associate is an entity over which the Group has significant influence and which is neither a subsidiary nor a joint venture. An entity is considered as an associate if the Group has more than 20% ownership of the entity or the Group has significant influence through any other mode.

Under the equity method, investment in associate is carried in the consolidated statement of financial position at cost plus post-acquisition changes in the Group's share of net assets of the associate. Losses in excess of the cost of the investment in associates are recognised when the Group has incurred obligations on its behalf. Goodwill relating to an associate is included in the carrying amount of the investment and is not amortised. The consolidated income statement reflects the Group's share of results of operations of the associate. Where there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes and discloses this, when applicable, in the consolidated statement of changes in equity.

The reporting dates of the associate and the Group are identical and the associates accounting policy conform to those used by the Group for like transactions and events in similar transactions.

After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on its investment in associates. The Group determines at each reporting date whether there is any objective evidence that the investment in associates are impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in the consolidated income statement.

Profit and losses resulting from transactions between the Group and the associates are eliminated to the extent of the interest in associates.

Foreign exchange translation gains/losses arising out of the above investment in the associate are included in the consolidated statement of changes in equity.

## 2 ACCOUNTING POLICIES (continued)

## 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.3.2 Summary of significant accounting policies (continued)

**j) Investments in real estate**

Properties held for rental, or for capital appreciation purposes, or both, are classified as investments in real estate. In accordance with FAS 26, the investments in real estate is initially recognized at cost and subsequently measured based on intention whether the investments in real estate is held-for-use or held for sale. The Group has adopted the fair value model for its investments in real estate. Under the fair value model any unrealized gains are recognized directly in owners' equity. Any unrealized losses are adjusted in equity to the extent of the available credit balance. Where unrealized losses exceed the available balance in owners' equity, these are recognized in the consolidated income statement. In case there are unrealized losses relating to investments in real estate that have been recognized in the consolidated income statement in a previous financial period, the unrealized gains relating to the current financial period is recognized to the extent of crediting back such previous losses in the consolidated income statement. Investments in real estate held-for-sale is carried at lower of its carrying value and expected fair value less costs to sell.

**k) Development properties**

Properties acquired exclusively for development are classified as development properties and are measured at the lower of cost or net realisable value.

**l) Premises and equipment**

Premises and equipment are stated at cost less accumulated depreciation and any impairment in value. Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment, other than freehold land and capital work-in-progress.

| | |
|---|---|
| - Computer equipment | 3 to 5 years |
| - Furniture and office equipment | 3 to 5 years |
| - Motor vehicle | 4 to 5 years |
| - Leasehold improvements | Over the lease period |
| - Computer software | 10 years |

**m) Subsidiaries acquired with a view to sell**

A subsidiary acquired with a view to subsequent disposal within twelve months is classified as "held-for-sale" when the sale is highly probable. Related assets and liabilities of the subsidiary are shown separately on the consolidated statement of financial position as "Assets held-for-sale" and "Liabilities relating to assets classified as held-for-sale". Assets that are classified as held-for-sale are measured at the lower of carrying amount and fair value less costs to sell. Any resulting impairment loss reduces the carrying amount of the assets. Assets that are classified as held-for-sale are not depreciated.

**n) Business combinations and goodwill**

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred measured at acquisition date fair value and the amount of any non-controlling interests in the acquiree. For each business combination, the Group elects whether to measure the non-controlling interests in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date.

In a business combination in which the Bank and the acquiree exchange only equity interests, the acquisition-date fair value of the acquiree's equity interests is used to determine the amount of goodwill.

## 2 ACCOUNTING POLICIES (continued)

## 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.3.2 Summary of significant accounting policies (continued)

**n) Business combinations and goodwill (continued)**

Investments acquired but do not meet the definition of business combination are recorded as financing assets or investment in properties as appropriate. When such investments are acquired, the Group allocates the cost of acquisition between the individual identifiable assets and liabilities based on their relative fair values at the date of acquisition. Cost of such assets is the sum of all consideration given and any non-controlling interest recognised. If the non-controlling interest has a present ownership interest and is entitled to a proportionate share of net assets upon liquidation, the Group recognises the non-controlling interest at its proportionate share of net assets.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interests, and any previous interest held, over the net identifiable assets acquired and liabilities assumed. If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the Group re-assesses whether it has correctly identified all of the assets acquired and all of the liabilities assumed and reviews the procedures used to measure the amounts to be recognised at the acquisition date. If the re-assessment still results in an excess of the fair value of net assets acquired over the aggregate consideration transferred, then the gain is recognised in consolidated income statement.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is tested for impairment at least annually. Any impairment is recognised immediately in the consolidated income statement. Goodwill is allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Impairment exists when carrying value of an asset or cash generating unit (CGU) exceeds its recoverable amount, which is the higher of its fair value less costs of disposal and its value in use.

The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Impairment of goodwill is determined by assessing the recoverable amount of the cash generating unit (or group of cash-generating units), to which the goodwill relates. Where the recoverable amount of the cash generating unit (or group of cash-generating units) is less than the carrying amount, an impairment loss is recognised immediately in the consolidated statement of income.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units or groups of units. Each unit or group of units to which the goodwill is allocated:

- represents the lowest level within the Group at which the goodwill is monitored for internal management purposes; and
- is not larger than a segment based on either the Group's primary or the Group's geographic segment reporting format.

**o) Impairment and uncollectability of financial assets**

An assessment is made at each reporting date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, any impairment loss, is recognised in the consolidated income statement.

Impairment is determined as follows:

(i) for assets carried at amortised cost, impairment is based on estimated cash flows based on the original effective profit rate;

(ii) for assets carried at fair value, impairment is the difference between cost and fair value; and

(iii) for assets carried at cost, impairment is based on present value of anticipated cash flows based on the current market rate of return for a similar financial asset.

**2 ACCOUNTING POLICIES (continued)**

**2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.3.2 Summary of significant accounting policies (continued)**

**o) Impairment and uncollectability of financial assets (continued)**
For available-for-sale equity investments reversal of impairment losses are recorded as increases in cumulative changes in fair value through equity.

**p) Offsetting**
Financial assets and financial liabilities can only be offset with the net amount being reported in the consolidated statement of financial position when there is a religious or legally enforceable right to set off the recognised amounts and the Group intends to either settle on a net basis, or intends to realise the asset and settle the liability simultaneously.

**q) Provisions**
Provisions are recognised when the Group has a present obligation (legal or constructive) arising from a past event and the costs to settle the obligation are both probable and able to be reliably measured.

**r) Employees' end of service benefits**
The Group provides end of service benefits to its expatriate employees. Entitlement to these benefits is based upon the employees' final salary and length of service, subject to completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment.

For Bahraini employees, the Group makes contributions to Social Insurance Organisation calculated as a percentage of the employees' salaries. The Group's obligations are limited to these contributions, which are expensed when due.

**s) Revenue recognition**

*Murabaha receivables*
As the income is quantifiable and contractually determined at the commencement of the contract, income is recognized on a straight-line basis over the deferred period. Recognition of income is suspended when the Group believes that the recovery of these amounts may be doubtful or normally when the payments of Murabaha installments are overdue by 90 days, whichever is earlier.

*Sukuk*
Income on Sukuk is recognized on a time-proportionate basis based on underlying rate of return of the respective type of sukuk. Recognition of income is suspended when the Group believes that the recovery of these amounts may be doubtful or normally when the payments are overdue by 90 days, whichever is earlier.

*Mudaraba*
Income on Mudaraba transactions are recognised when the right to receive payment is established or these are declared by the Mudarib, whichever is earlier. In case of losses in Mudaraba, the Group's share of loss is recognised to the extent that such losses are being deducted from its share of the Mudaraba capital.

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

*Ijarah Muntahia Bittamleek*
Ijarah Muntahia Bittamleek income is recognised on a time-proportionate basis over the lease term. Income related to non-performing Ijarah Muntahia Bittamleek is suspended. Accrual of income is suspended when the Group believes that the recovery of these amounts may be doubtful or normally when the rental payments are overdue by 90 days, whichever is earlier.

*Musharaka*
Income on Musharaka is recognized when the right to receive payment is established or on distributions. In case of losses in Musharaka, the Group's share of loss is recognized to the extent that such losses are being deducted from its share of the Musharaka capital.

**2 ACCOUNTING POLICIES (continued)**

**2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.3.2 Summary of significant accounting policies (continued)**

**s) Revenue recognition (continued)**

*Fees and commission income*
The Group earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following main categories:

Fee income on financing transactions: Fee earned on financing transactions including up-front fees and early settlement fees are recognised when earned. To the extent the fees are deemed yield enhancement they are recognised over the period of the financing contracts.

Fee income from transaction services: Fee arising from corporate finance, corporate advisory, arranging the sale of assets and wealth management are recognised when earned or on a time proportionate basis when the fee is linked to time. Other fee income is recognised when services are rendered.

**t) Fair value of financial assets**
For investments that are traded in organised financial markets, fair value is determined by reference to the prevailing market bid price on the reporting date.

For investments where there is no quoted market price, a reasonable estimate of fair value is determined by reference to valuation by independent external valuers or based on recent arm's length market transactions. Alternatively, the estimate would also be based on 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 by calculating the present value of future cash flows at current profit rates for contracts with similar terms and risk characteristics.

For investments having fixed or determinable payments, fair value is based on the net present value of estimated future cash flows determined by the Group using current profit rates for instruments with similar terms and risk characteristics.

**u) Foreign currencies**
Foreign currency transactions are recorded at rates of exchange prevailing at the dates of the transactions. Monetary assets and liabilities in foreign currencies at the consolidated statement of financial position date are retranslated at market rates of exchange prevailing at that date. Gains and losses arising on translation are recognised in the consolidated income statement. Non-monetary assets that are measured in terms of historical cost in foreign currencies are recorded at rates of exchange prevailing at the value dates of the transactions. Translation gains or losses on non-monetary items classified as "available-for-sale" and investment in associates are included in consolidated statement of changes in equity until the related assets are sold or derecognised at which time they are recognised in the consolidated income statement. Translation gains on non-monetary assets classified as "fair value through profit or loss" are directly recognised in the consolidated income statement.

**v) Translation of foreign operation**
Assets and liabilities of foreign subsidiaries whose functional currency is not Bahraini Dinars are translated into Bahraini Dinars at the rates of exchange prevailing at the reporting date. Income and expense items are translated at average exchange rates prevailing for the reporting period. Any exchange differences arising on translation are included in "foreign exchange translation reserve" forming part of other comprehensive income except to the extent that the translation difference is allocated to the non-controlling interest. On disposal of foreign operations, exchange differences relating thereto and previously recognised in other comprehensive income are recognised in the consolidated income statement.

**w) Repossessed assets**
Repossessed assets are assets acquired in settlement of dues. These assets are carried at the lower of carrying amount and fair value less costs to sell and reported within 'other assets'.

**2 ACCOUNTING POLICIES (continued)**

**2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**2.3.2 Summary of significant accounting policies (continued)**

**x) Trade and settlement date accounting**
Purchases and sales of financial assets and liabilities are recognised on the trade date, i.e. the date that the Group contracts to purchase or sell the asset or liability.

**y) Derecognition of financial assets**
Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Group has transferred substantially all risk and rewards of ownership.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Group could be required to pay.

**z) Derecognition of financial liabilities**
A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same source on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in the respective carrying amounts is recognised in the consolidated statement of income.

**aa) Fiduciary assets**
Assets held in a fiduciary capacity are not treated as assets of the Group and are accordingly not included in the consolidated statement of financial position.

**ab) Dividend on ordinary shares**
Dividend on ordinary shares is recognised as a liability and deducted from equity when it is approved by the Group's shareholders. Dividend for the year that is approved after the reporting date is included in the equity and is disclosed as an event after the balance sheet date.

**ac) Equity of investment account holders**
All equity of investment accountholders are carried at cost plus profit and related reserves less amounts settled.

Share of income for equity of investment accountholder is calculated based on the income generated by the assets funded by such investment accounts after deducting Mudarib share (as Mudarib and Rabalmal). Operating expenses are charged to shareholders' funds and are not included in the calculation.

The basis applied by the Group in arriving at the equity of investment accountholders' share of income is total investment income less shareholders' income. Portion of the income generated from equity of investment accountholders is transferred to profit equalization reserve, mudarib share and investment risk reserve and the remaining is distributed to the equity of investment accountholders.

**ad) Treasury Stock**
Own equity instruments that are reacquired, are recognised at cost and deducted from equity. No gain or loss is recognised in profit or loss on the purchase, sale, issue or cancellation of the Bank's own equity instruments. Any difference between the carrying amount and the consideration, if reissued, is recognised in share premium.

**ae) Zakah**
In accordance with the Articles of Association of the Group, the responsibility to pay Zakah is on the shareholders of the Bank.

**af) Cash and cash equivalents**
Cash and cash equivalents comprise of cash and balances with the CBB and Murabaha receivables from banks with original maturities of less than 90 days.

## 2 ACCOUNTING POLICIES (continued)

## 2.3 SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.3.2 Summary of significant accounting policies (continued)

**ag) Wakala payables**
The Group accepts funds from banks and customers under Wakala arrangement in which a return is payable to customers as agreed in the agreement. There is no restriction on the Group for the use of funds received under wakala agreement.

**ah) Jointly financed and self financed**
Investments, financing and receivables that are jointly funded by the Group and the equity of investment accountholders are classified under the caption "jointly financed" in the consolidated financial statements. Investments, financing and receivables that are funded solely by the Group are classified under "self financed".

The equity of investment accountholders is used to finance the assets of the Group as appropriate.

**ai) Investment risk reserve**
This is the amount appropriated by the Group out of the income of investment account holders, after allocating the Mudarib share, in order to compensate future losses for investment account holders.

**aj) Earnings prohibited by Shari'a**
The Group is committed to contributing to charity any income generated from non-Islamic sources. Accordingly, any earning prohibited by Shari'a is credited to charity funds to be used for social welfare purposes.

**ak) Profit on Murabaha and Wakala payables to banks non-banks**
Profit on these is accrued on a time-apportioned basis over the period of the contract based on the principal amounts outstanding.

## 3 BUSINESS COMBINATION

During 2014, the Bank made an offer to acquire 100% of the issued and paid up shares of BMI, at an exchange ratio of eleven new shares of the Bank for each share of BMI. The acquisition through share exchange was approved by the shareholders of the Bank in their Extraordinary General Assembly Meeting held on 8 October 2013. The Bank issued 643,866,927 to former shareholders of the Bank. The total proceeds amounted to BD 72,886 thousands from the new issue, including a share premium of BD 8,499 thousands. The goodwill arising out of above acquisition amounted to BD 25,971 thousands.

The management carried out an annual impairment test of goodwill by comparing the carrying amount with its recoverable amount (value-in-use) as of 31 December 2015. The detemination of value-in-use involved the use of various assumptions including estimating discounted cash flows. The discount rate applied to cash flow projections represent the cost of capital adjusted for an appropriate risk premium.

The key assumptions used in estimating recoverable amounts of cash generating units were sensitised to test the resilience of value-in-use calculations. On this basis, management believes that reasonable changes in the key assumptions used to determine the recoverable amount of the Group's cash-generating units will not result in an impairment.

## 4 CLASSIFICATION OF ASSETS, LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS

| | *31 December 2015* | | | |
|---|---|---|---|---|
| | *At fair value through profit or loss BD '000* | *Available for sale / fair value through equity BD '000* | *At amortised cost / others BD '000* | *Total BD '000* |
| **ASSETS** | | | | |
| Cash and balances with banks and Central Bank | - | - | 152,572 | 152,572 |
| Sovereign Sukuk | - | - | 313,109 | 313,109 |
| Murabaha and Wakala receivables from banks | - | - | 103,345 | 103,345 |
| Corporate Sukuk | - | - | 64,157 | 64,157 |
| Murabaha financing | - | - | 268,848 | 268,848 |
| Mudaraba financing | - | - | 239,031 | 239,031 |
| Ijarah Muntahia Bittamleek | - | - | 155,217 | 155,217 |
| Musharaka | - | - | 7,154 | 7,154 |
| Assets under conversion | - | 41 | 31,991 | 32,032 |
| Non-trading investments | 115,008 | 8,506 | - | 123,514 |
| Investments in real estate | - | 68,786 | - | 68,786 |
| Development properties | - | - | 49,021 | 49,021 |
| Investment in associates | - | - | 9,994 | 9,994 |
| Other assets | - | 2,037 | 41,855 | 43,892 |
| Goodwill | - | - | 25,971 | 25,971 |
| | 115,008 | 79,370 | 1,462,265 | 1,656,643 |

| | *At fair value through profit or loss BD '000* | *Available for sale / fair value through equity BD '000* | *At amortised cost / others BD '000* | *Total BD '000* |
|---|---|---|---|---|
| **LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS** | | | | |
| Murabaha and Wakala payables to banks | - | - | 120,795 | 120,795 |
| Murabaha and Wakala payables to non-banks | - | - | 842,570 | 842,570 |
| Current accounts | - | - | 224,366 | 224,366 |
| Liabilities under conversion | - | - | 2,327 | 2,327 |
| Term financing | - | - | 35,986 | 35,986 |
| Other liabilities | - | - | 48,246 | 48,246 |
| Equity of investment accountholders | - | - | 62,351 | 62,351 |
| | - | - | 1,336,641 | 1,336,641 |

**4 CLASSIFICATION OF ASSETS, LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS (continued)**

| | *31 December 2014* | | | |
|---|---|---|---|---|
| | *At fair value through profit or loss BD '000* | *Available for sale / fair value through equity BD '000* | *At amortised cost / others BD '000* | *Total BD '000* |
| ASSETS | | | | |
| Cash and balances with banks and Central Bank | - | - | 277,751 | 277,751 |
| Sovereign Sukuk | - | - | 145,789 | 145,789 |
| Murabaha and Wakala receivables from banks | - | - | 182,110 | 182,110 |
| Corporate Sukuk | - | - | 88,193 | 88,193 |
| Murabaha financing | - | - | 270,428 | 270,428 |
| Mudaraba financing | - | - | 189,601 | 189,601 |
| Ijarah Muntahia Bittamleek | - | - | 141,052 | 141,052 |
| Musharaka | - | - | 10,851 | 10,851 |
| Assets under conversion | - | 75,189 | 233,470 | 308,659 |
| Non-trading investments | 125,779 | 21,317 | - | 147,096 |
| Investments in real estates | - | 65,149 | - | 65,149 |
| Development properties | - | - | 59,262 | 59,262 |
| Investment in associates | - | - | 10,492 | 10,492 |
| Other assets | - | 2,412 | 30,481 | 32,893 |
| Goodwill | - | - | 25,971 | 25,971 |
| | 125,779 | 164,067 | 1,665,451 | 1,955,297 |

| | *At fair value through profit or loss BD '000* | *Available for sale / fair value through equity BD '000* | *At amortised cost / others BD '000* | *Total BD '000* |
|---|---|---|---|---|
| LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS | | | | |
| Murabaha and Wakala payables to banks | - | - | 121,266 | 121,266 |
| Murabaha and Wakala payables to non-banks | - | - | 1,034,052 | 1,034,052 |
| Current accounts | - | - | 226,648 | 226,648 |
| Liabilities under conversion | - | - | 149,621 | 149,621 |
| Term financing | - | - | 21,337 | 21,337 |
| Other liabilities | - | - | 45,418 | 45,418 |
| Equity of investment accountholders | - | - | 28,152 | 28,152 |
| | - | - | 1,626,494 | 1,626,494 |

## 5 CASH AND BALANCES WITH BANKS AND CENTRAL BANK

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Mandatory reserve with Central Bank* | **32,240** | 42,350 |
| Cash and other balances with Central Bank | **81,448** | 187,313 |
| Balances with other banks | **38,884** | 48,088 |
| | **152,572** | 277,751 |

* This balance is not available for use in the day-to-day operations of the Group.

## 6 MURABAHA AND WAKALA RECEIVABLES FROM BANKS

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| GCC | **103,345** | 176,455 |
| Europe | **-** | 5,655 |
| | **103,345** | 182,110 |

In addition to above amounts, deferred profits on Murabaha receivables from banks amounted to BD 12 thousands (2014: BD 30 thousands).

This consists of BD 62,351 thousands (2014: BD 24,281 thousands) of jointly financed assets and BD 40,994 thousands (2014: BD 157,829 thousands) of self financed assets.

## 7 CORPORATE SUKUK

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Investment grade | **45,518** | 70,011 |
| Non-investment grade | **10,330** | 9,364 |
| Un-rated Sukuk | **8,309** | 8,818 |
| | **64,157** | 88,193 |

This consists of nil (2014: BD 3,871 thousands) of jointly financed assets and BD 64,157 thousands (2014: BD 84,322 thousands) of self financed assets.

## 8 MURABAHA AND MUDARABA FINANCING

### 8.a Murabaha Financing

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Murabaha financing - gross | **273,300** | 275,166 |
| Less: Specific provision | **(4,452)** | (4,738) |
| Murabaha financing - net | **268,848** | 270,428 |

Murabaha financing is shown net of deferred profits of BD 50,310 thousands (2014: BD 53,630 thousands).

## 8 MURABAHA AND MUDARABA FINANCING (continued)

### 8.b Mudaraba Financing

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Mudaraba financing - gross | **248,354** | 189,607 |
| Less: Specific provision | **(9,323)** | (6) |
| Mudaraba financing - net | **239,031** | 189,601 |

## 9 MOVEMENTS IN PROVISIONS

| | ***2015*** | | |
|---|---|---|---|
| | ***Financing facilities & other assets*** | ***Available-for-sale investments*** | ***Total*** |
| | ***BD '000*** | ***BD '000*** | ***BD '000*** |
| **Balance at beginning of the year:** | | | |
| Specific provision | **5,073** | **4,328** | **9,401** |
| Collective provision | **4,709** | **-** | **4,709** |
| **Transfer** | | | |
| Specific provision | **160** | **-** | **160** |
| Collective provision | **(160)** | **-** | **(160)** |
| **Write offs** | | | |
| Specific provision | **(1,928)** | **-** | **(1,928)** |
| Collective provision | **-** | **-** | **-** |
| **Provision for impairment:** | | | |
| Charge for the year - specific | **21,802** | **1,143** | **22,945** |
| Charge for the year - collective | **500** | **-** | **500** |
| Recoveries during the year | **(594)** | **-** | **(594)** |
| | **21,708** | **1,143** | **22,851** |
| **Balance at end of the year:** | | | |
| Specific provision | **24,513** | **5,471** | **29,984** |
| Collective provision | **5,049** | **-** | **5,049** |

| | *2014* | | |
|---|---|---|---|
| | *Financing facilities & other assets* | *Available-for-sale investments* | *Total* |
| | *BD '000* | *BD '000* | *BD '000* |
| Balance at beginning of the year: | | | |
| Specific provision | 4,580 | 4,038 | 8,618 |
| Collective provision | 1,294 | - | 1,294 |
| Transfer | | | |
| Specific provision | 708 | - | 708 |
| Collective provision | (708) | - | (708) |
| Provision for impairment: | | | |
| Charge for the year - specific | 725 | 290 | 1,015 |
| Charge for the year - collective | 4,123 | - | 4,123 |
| Recoveries during the year | (940) | - | (940) |
| | 3,908 | 290 | 4,198 |
| Balance at end of the year: | | | |
| Specific provision | 5,073 | 4,328 | 9,401 |
| Collective provision | 4,709 | - | 4,709 |

## 10 IJARAH MUNTAHIA BITTAMLEEK

This represents net investments in assets leased for periods which either approximate or cover major parts of the estimated useful lives of such assets. The majority of the lease documentations provide that the lessor undertakes to transfer the leased assets to the lessee at the end of the lease term upon the lessee fulfilling all its obligations under the lease agreement.

| | ***2015*** | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| Movements in Ijarah Muntahia Bittamleek assets are as follows: | | |
| At 1 January | **141,052** | 110,631 |
| Ijarah assets arising on acquisition of BMI | **-** | 3,654 |
| Additions during the year - net | **48,277** | 37,887 |
| Ijarah assets depreciation | **(15,939)** | (10,101) |
| Transfer to other assets* | **(17,729)** | - |
| Specific provision | **(444)** | (1,019) |
| At 31 December | **155,217** | 141,052 |

* On termination of lease, this asset was transferred to other assets.

| | ***2015*** | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| The future minimum lease receivable in aggregate are as follows: | | |
| Due within one year | **10,494** | 41,446 |
| Due in one to five years | **62,881** | 59,141 |
| Due after five years | **81,842** | 40,465 |
| | **155,217** | 141,052 |

| | ***2015*** | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| Ijarah Muntahia Bittamleek is divided into the following asset classes: | | |
| Land and buildings | **155,217** | 119,836 |
| Aircraft | **-** | 19,334 |
| Machinery | **-** | 1,882 |
| | **155,217** | 141,052 |

The accumulated depreciation on Ijarah Muntahia Bittamleek assets amounted to BD 31,236 thousands (2014: BD 23,852 thousands).

## 11 ASSETS AND LIABILITIES UNDER CONVERSION

These represent interest bearing non-Shari'a compliant assets and liabilities of BMI. These assets and liabilities have been reported as separate line items on the face of the consolidated statement of financial position. The details of the assets and liabilities under conversion are as follows:

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| **Assets** | | |
| Due from banks and financial institutions | - | 13,949 |
| Loans and advances | 31,437 | 215,438 |
| Non-trading investments - debt | 16 | 75,165 |
| Non-trading investment - available-for-sale - equity * | 24 | 24 |
| Other assets | 555 | 4,083 |
| | 32,032 | 308,659 |
| **Liabilities** | | |
| Customers' deposits | - | 138,793 |
| Other liabilities | 2,327 | 10,828 |
| | 2,327 | 149,621 |

Note: In addition to the above, "Cash and balances with banks and Central bank of Bahrain" include an amount of BD nil (2014 : BD 54,000 thousands) of conventional balances. These represent short term placements with Central bank of Bahrain which carries a nominal income on conventional assets.

* The above available-for-sale equity investment is classified as Level 3 (2014: Level 3) in the fair value hierarchy (note 12). During the year, there were no movements in the fair value of this investment.

## 12 NON-TRADING INVESTMENTS

Non-trading investments are classified as available-for-sale or fair value through profit or loss.

**Fair value hierarchy**

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 that have a significant effect on the recorded fair value are observable, either directly or indirectly;

Level 3: techniques that use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

## 12 NON-TRADING INVESTMENTS (continued)

**Fair value hierarchy (continued)**

The following table shows an analysis of the financial instruments carried at fair value in the consolidated statement of financial position:

| **31 December 2015** | ***Level 1*** | ***Level 2*** | ***Level 3*** | ***Total*** |
|---|---|---|---|---|
| | ***BD '000*** | ***BD '000*** | ***BD '000*** | ***BD '000*** |
| Financial assets at fair value through profit or loss | **7,646** | **4,702** | **102,660** | **115,008** |
| Available-for-sale financial assets | **4,774** | **-** | **3,732** | **8,506** |
| | **12,420** | **4,702** | **106,392** | **123,514** |

| 31 December 2014 | *Level 1* | *Level 2* | *Level 3* | *Total* |
|---|---|---|---|---|
| | *BD '000* | *BD '000* | *BD '000* | *BD '000* |
| Financial assets at fair value through profit or loss | 18,476 | - | 107,303 | 125,779 |
| Available-for-sale financial assets | 6,730 | - | 14,587 | 21,317 |
| | 25,206 | - | 121,890 | 147,096 |

During the years ended 31 December 2015 and 2014, there were no transfers between Level 1, Level 2, and Level 3 fair value measurements. The movements in non-trading investments classified in level 3 of the fair value hierarchy are as follows:

| | ***Fair value measurement using significant unobservable inputs Level 3*** | |
|---|---|---|
| | ***2015*** | *2014* |
| | ***BD '000*** | *BD '000* |
| At 1 January | **121,890** | 110,404 |
| Additions during the year | **-** | 35,031 |
| Fair value changes | **(2,426)** | (6,797) |
| Repayments during the year | **(408)** | (1,303) |
| Disposals during the year | **(12,653)** | (15,020) |
| Other movements | **(11)** | (425) |
| At 31 December | **106,392** | 121,890 |

## 13 INVESTMENTS IN REAL ESTATE

| | ***2015*** | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| Buildings | **19,027** | 20,759 |
| Land | **49,759** | 44,390 |
| | **68,786** | 65,149 |

The above investments are classified under level 3 (2014: level 3) in fair value hierarchy. Movements represent fair value changes during the year.

## 14 DEVELOPMENT PROPERTIES

These represent properties acquired and held through investment vehicles exclusively for development in the Kingdom of Bahrain and the United Kingdom. The carrying amounts include land price and related construction costs.

## 15 INVESTMENT IN ASSOCIATES

The Group has a 14.4% (2014: 14.4%) stake in Al Salam Bank Algeria (ASBA), an unlisted bank incorporated in Algeria. The Bank has representation on the board of ASBA through which the Bank has a significant influence on ASBA.

The Group has a 20.9% (2014: 20.9%) stake in Gulf African Bank ("GAB"), a private Islamic bank incorporated in Kenya. This investment is denominated in Kenyan Shillings and is held through BMI.

The Group's interest in ASBA and GAB is accounted for using the equity method in the consolidated financial statements.

The following table illustrates summarised financial information of Group's investments in ASBA and GAB:

| | *2015* | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| Associates' statement of financial position: | | |
| Total assets | **234,168** | 236,788 |
| Total liabilities | **169,231** | 163,546 |
| Net assets | **64,937** | 73,242 |
| Total revenue | **20,484** | 22,844 |
| Total expenses | **16,411** | 14,837 |
| Net profit for the year | **4,073** | 8,007 |
| Group's share of associates' net profit | **855** | 369 |

## 16 OTHER ASSETS

| | *2015* | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| **Assets under conversion (a)** | | |
| Non-trading-investments - debt | **236** | 3,848 |
| Non-trading investments - available-for-sale - equity (b) | **2,036** | 2,412 |
| | **2,272** | 6,260 |
| Repossessed assets | **4,007** | 3,897 |
| Profit receivable | **7,995** | 6,878 |
| Premises and equipment | **3,910** | 5,494 |
| Prepayments | **1,066** | 1,001 |
| Rental receivable on Ijarah Muntahia Bittamleek assets | **685** | 669 |
| Other receivables and advances (c) | **15,469** | 8,694 |
| Aircraft [net of impairment of BD 7,600 thousands (d)] | **8,488** | - |
| | **43,892** | 32,893 |

## 16 OTHER ASSETS (continued)

(a) These represent non-Shari'a compliant assets resulted from the acquisition of Bahraini Saudi Bank B.S.C. ("ex-BSB").

(b) The above available-for-sale equity investments are classified as Level 3 in the fair value hierarchy (note 12). Movements in these investments are as follows:

| | ***Fair value measurement using significant unobservable inputs Level 3*** | |
|---|---|---|
| | ***2015*** | *2014* |
| | ***BD '000*** | *BD '000* |
| At 1 January | **2,412** | 2,656 |
| Fair value changes | **188** | 20 |
| Repayments during the year | **(69)** | (100) |
| Disposals during the year | **(334)** | - |
| Provision | **(161)** | (164) |
| | **2,036** | 2,412 |

(c) This includes BD 10,865 thousands (2014: 5,687 thousands) relating to receivable from sale of investments and advances to contractors.

(d) This aircraft was on lease and the lease was terminated during the year. The management is in the process of re-leasing the aircraft.

## 17 TERM FINANCING

Term financing is subject to the following key terms:

a) BD 7,531 thousands ( 2014: BD 8,446 thousands) carries a profit and is repayable on quarterly basis with final maturity on 13 December 2018. The collateral for this facility is an aircraft, with a carrying value of BD 8,488 thousands (2014: BD 17,728) thousands; and

b) BD 11,490 thousands (2014: BD 12,891) thousands carries profit and matures on 21 August 2016. The collateral for this facility is investments in real estate with a carrying value of BD 19,027 thousands (2014: BD 20,759) thousands.

c) BD 16,965 thousands (2014: nil) carries profit and matures on 28 December 2018. The collateral for this facility is investments in corporate and sovereign Sukuk with a carrying value of BD 40,710 thousands (2014: nil).

## 18 OTHER LIABILITIES

| | ***2015*** | *2014* |
|---|---|---|
| | ***BD '000*** | *BD '000* |
| Advances received from customers for sale of properties | **13,034** | 14,558 |
| Accounts payable and accruals | **19,623** | 11,704 |
| Profit payable | **5,474** | 8,119 |
| Dividends payable | **3,728** | 3,129 |
| End of service benefits and other employee related accruals | **6,387** | 7,908 |
| | **48,246** | 45,418 |

## 19 EQUITY OF INVESTMENT ACCOUNTHOLDERS

Equity of investment account holders funds is commingled with the Group's funds and used to fund / invest in Islamic modes of finance and no priority is granted to any party for the purpose of investments and distribution of profits. According to the terms of acceptance of the unrestricted investment accounts, 100% of the funds are invested taking into consideration the relevant weightage, if any. The Mudarib's share of profit ranges between 40% and 50%. Operating expenses are charged to shareholders' funds and not included in the calculation.

The balances consists of savings accounts of BD 49,093 thousands (2014: BD 17,814 thousands) and call accounts of BD 13,258 thousands (2014: BD 10,338 thousands).

The average profit rate for the holders is 0.21% (2014: 0.38%).

## 20 SHARE CAPITAL

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Authorised: | | |
| 2,500,000,000 ordinary shares (2014: 2,500,000,000 shares) of BD 0.100 each | **250,000** | 250,000 |
| Issued and fully paid: ( BD 0.100 per share ) | | |
| Balance at the beginning | **214,093** | 149,706 |
| Shares issued | **-** | 64,387 |
| | **214,093** | 214,093 |

### 20.1 Proposed appropriation

The Board of Directors in its meeting on 9 February 2016 has resolved to recommend a cash dividend of 5 fils per share or 5% (2014: 5 fils or 5%) of the paid-up capital subject to approval at the forthcoming annual general meeting.

## 21 STATUTORY RESERVE

As required by Bahrain Commercial Companies Law and the Bank's articles of association, 10% of the net profit for the year has been transferred to the statutory reserve. The Group may resolve to discontinue such annual transfers when the reserve totals 50% of the paid up share capital of the Bank. The reserve is not distributable except in such circumstances as stipulated in the Bahrain Commercial Companies Law and following the approval of the CBB.

## 22 INCOME FROM FINANCING CONTRACTS

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Murabaha financing | **15,736** | 15,192 |
| Mudaraba financing | **13,104** | 7,584 |
| Ijarah Muntahia Bittamleek* | **10,136** | 7,930 |
| Musharaka | **558** | 2,807 |
| Murabaha and Wakala receivables from banks | **896** | 725 |
| Income from assets under conversion ** | **7,800** | 17,256 |
| | **48,230** | 51,494 |

* Depreciation on Ijarah Muntahia Bitamleek amounted to BD 15,939 thousands (2014: BD 10,101thousands).

** The Bank's shareholders are advised, but not obliged, to contribute this income to charity at their discretion.

## 23 GAINS ON SALE OF INVESTMENTS AND SUKUK

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| **Gain on sale of:** | | |
| Available-for-sale investments | **3,555** | - |
| Development properties* | **2,469** | 941 |
| Sukuk | **905** | 2,970 |
| FVTPL investments | **265** | 7,352 |
| Investment properties | **-** | 698 |
| Other investments | **1,140** | 321 |
| | **8,334** | 12,282 |

* Sales: BD 17,203 thousands (2014: BD 3,934 thousands) and cost: BD 14,734 thousands (2014: 2,993 thousands).

## 24 INCOME FROM INVESTMENTS

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| (Loss) / income from FVTPL investments | **(728)** | 997 |
| Rental income from investments in real estate | **1,687** | 1,866 |
| Income from assets classified as held-for-sale | **2,290** | - |
| | **3,249** | 2,863 |

## 25 FEES, COMMISSION AND OTHER INCOME - NET

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| Financing and transaction related fees and commissions | **4,336** | 3,775 |
| Fiduciary and other fees | **387** | 268 |
| Other income | **4,461** | 2,607 |
| | **9,184** | 6,650 |

## 26 TOTAL COMPREHENSIVE INCOME

| | *2015* *BD '000* | *2014* *BD '000* |
|---|---|---|
| **Net profit for the year** | **10,548** | 15,821 |
| **Other comprehensive (loss) / income :** | | |
| *Items to be reclassified to consolidated income statement in subsequent periods:* | | |
| Unrealized gain reclassified to consolidated income statement on disposal of available-for-sale investments | **(965)** | - |
| Unrealised (loss) / gain on available-for-sale investments | **(470)** | 636 |
| Changes in fair value of investments in real estate | **1,549** | 1,045 |
| Foreign currency re-translation | **(1,472)** | (819) |
| **Other comprehensive (loss) / income for the year** | **(1,358)** | 862 |
| **Total comprehensive income for the year** | **9,190** | 16,683 |
| ***Attributable to:*** | | |
| Equity holders of the Bank | **11,168** | 16,331 |
| Non-controlling interest | **(1,978)** | 352 |
| | **9,190** | 16,683 |

## 27 RELATED PARTY TRANSACTIONS

Related parties comprise 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 approved by the Board of Directors. All the loans and advances to related parties are performing and are free of any provision for possible credit losses.

The balances with related parties at 31 December 2015 were as follows:

| | ***2015*** | | | | |
|---|---|---|---|---|---|
| | ***Associates, and joint ventures BD '000*** | ***Major shareholders BD '000*** | ***Directors and related entities BD '000*** | ***Senior management BD '000*** | ***Total BD '000*** |
| **Assets:** | | | | | |
| Cash and balances with banks and Central Bank | **-** | **-** | **-** | **-** | **-** |
| Murabaha and Wakala receivables from banks | **-** | **36** | **-** | **-** | **36** |
| Murabaha financing | **32,799** | **-** | **-** | **36** | **32,835** |
| Mudaraba financing | **1,885** | **-** | **-** | **-** | **1,885** |
| Ijarah Muntahia Bittamleek | **-** | **-** | **-** | **187** | **187** |
| Musharaka financing | **-** | **-** | **55** | **-** | **55** |
| Other assets | **1,924** | **-** | **3,660** | **4** | **5,588** |
| **Liabilities and equity of investment accountholders:** | | | | | |
| Murabaha and Wakala due to banks | **1,508** | **-** | **-** | **-** | **1,508** |
| Wakala payables to non-banks | **2,235** | **23,400** | **637** | **653** | **26,925** |
| Current accounts | **2,216** | **4,010** | **163** | **50** | **6,439** |
| Equity of investment accountholders | **-** | **-** | **153** | **64** | **217** |
| Other liabilities | **911** | **191** | **3** | **3** | **1,108** |
| Contingent liabilities and commitments | **743** | **-** | **-** | **-** | **743** |

| | *2014* | | | | |
|---|---|---|---|---|---|
| | *Associates, and joint ventures BD '000* | *Major shareholders BD '000* | *Directors and related entities BD '000* | *Senior management BD '000* | *Total BD '000* |
| Assets: | | | | | |
| Cash and balances with banks and Central Bank of Bahrain | - | 28 | - | - | 28 |
| Murabaha financing | 30,160 | - | 20 | 49 | 30,229 |
| Mudaraba financing | 14,310 | - | 56 | - | 14,366 |
| Ijarah Muntahia Bittamleek | - | - | 1,007 | 207 | 1,214 |
| Musharaka financing | 843 | - | 65 | - | 908 |
| Assets under conversion | 243 | - | 404 | 74 | 721 |
| Other assets | 885 | 6 | 3 | 6 | 900 |
| Liabilities and equity of investment accountholders: | | | | | |
| Wakala payables to non-banks | 9,057 | 90,015 | 3,355 | 946 | 103,373 |
| Current accounts | 941 | 3,905 | 1,980 | 55 | 6,881 |
| Equity of investment accountholders | - | - | 1,400 | 121 | 1,521 |
| Liabilities under conversion | 1,554 | - | 805 | - | 2,359 |
| Other liabilities | 129 | 4 | 17 | 4 | 154 |
| Contingent liabilities and commitments | 1,106 | - | - | - | 1,106 |

**27 RELATED PARTY TRANSACTIONS (continued)**

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

| | ***2015*** | | | | |
|---|---|---|---|---|---|
| | ***Associates and joint ventures BD '000*** | ***Major shareholders BD '000*** | ***Directors and related entities BD '000*** | ***Senior management BD '000*** | ***Total BD '000*** |
| **Income:** | | | | | |
| Income from financing contracts | **54** | **-** | **4** | **5** | **63** |
| Other income | **80** | **-** | **-** | **1** | **81** |
| Gain on sale of investments & Sukuk | **217** | **-** | **1,259** | **-** | **1,476** |
| **Expenses:** | | | | | |
| Profit on Murabaha and Wakala payables to banks | **3** | **-** | **-** | **-** | **3** |
| Profit paid on Wakala from non-banks | **144** | **2,720** | **13** | **16** | **2,893** |
| Share of profits on equity of investment account holders | **-** | **-** | **2** | **-** | **2** |
| Other operating expenses | **6** | **-** | **432** | **-** | **438** |
| Provision for impairment | **9,425** | **-** | **-** | **-** | **9,425** |

| | *2014* | | | | |
|---|---|---|---|---|---|
| | *Associates and joint ventures BD '000* | *Major shareholders BD '000* | *Directors and related entities BD '000* | *Senior management BD '000* | *Total BD '000* |
| Income: | | | | | |
| Income from financing contracts | 397 | - | 115 | 14 | 526 |
| Fair value changes on investments | (3,799) | - | - | - | (3,799) |
| Other income | 195 | - | - | - | 195 |
| Expenses: | | | | | |
| Profit on Wakala payables to non-banks | 291 | 1,612 | 57 | 32 | 1,992 |
| Share of profits on equity of investment account holders | - | - | 4 | 23 | 27 |

Directors' remuneration for 2015 amounted to BD 365 thousands (2014: BD 329 thousands).

Compensation of key management personnel, consisting of short-term benefits and non-cash remuneration, for the year was BD 3,142 thousands (2014: BD 3,493 thousands).

## 28 CONTINGENT LIABILITIES AND COMMITMENTS

| | 2015 BD '000 | 2014 BD '000 |
|---|---|---|
| **Contingent liabilities on behalf of customers** | | |
| Guarantees | **28,144** | 37,077 |
| Letters of credit | **9,594** | 9,704 |
| Acceptances | **2,275** | 3,464 |
| | **40,013** | 50,245 |
| **Irrevocable unutilised commitments** | | |
| Unutilised financing commitments | **79,465** | 87,337 |
| Unutilised non-funded commitments | **37,023** | 50,023 |
| Commitments towards development cost | **6,981** | 23,880 |
| | **123,469** | 161,240 |
| **Commitment relating to purchase of investment** | **4,182** | 4,182 |
| **Capital expenditure commitments** | | |
| Estimated capital expenditure contracted for at the consolidated statement of financial position date but not provided for | **29** | 45 |
| | **167,693** | 215,712 |
| **Forward foreign exchange contracts - notional amount** | **14,448** | 15,781 |

Letters of credit, guarantees (including standby letters of credit) commit the Group to make payments on behalf of customers contingent upon their failure to perform under the terms of the contract.

Commitments generally have fixed expiration dates, or other termination clauses. Since commitment may expire without being utilized, the total contract amounts do not necessarily represent future cash requirements.

**Operating lease commitment - Group as lessee**

The Group has entered into various operating lease agreements for its premises. Future minimal rentals payable under the non-cancellable leases are as follows:

| | 2015 BD '000 | 2014 BD '000 |
|---|---|---|
| Within 1 year | **1,328** | 1,789 |
| After one year but not more than five years | **2,576** | 3,517 |
| | **3,904** | 5,306 |

## 29 RISK MANAGEMENT

### 29.1 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 Group is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to early settlement risk and operational risks.

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

**29 RISK MANAGEMENT (continued)**

**29.1 Introduction (continued)**

***Risk management structure***
The Board of Directors is ultimately responsible for identifying and controlling risks; however, there are separate independent bodies responsible for managing and monitoring risks.

***Board of Directors***
The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and principles.

***Executive Committee***
The Executive Committee has the responsibility to monitor the overall risk process within the Bank.

***Shari'a Supervisory Board***
The Group's Shari'a Supervisory Board is entrusted with the responsibility to ensure the Group's adherence to Shari'a rules and principles in its transactions and activities.

***Credit/ Risk Committee***
Credit/ Risk committee recommends the risk policy and framework to the Board. Its primary role is selection and implementation of risk management systems, portfolio monitoring, stress testing, risk reporting to the Board, Board Committees, Regulators and Executive management. In addition, individual credit transaction approval and monitoring is an integral part of the responsibilities of Credit/Risk Committee.

***Asset and Liability Committee***
The Asset and Liability Committee establishes policy and objectives for the asset and liability management of the Group's financial position in terms of structure, distribution, risk and return and its impact on profitability. It also monitors the cash flow, tenor and cost/yield profiles of assets and liabilities and evaluates The Group's financial position both from profit rate sensitivity and liquidity points of view, making corrective adjustments based upon perceived trends and market conditions, monitoring liquidity, monitoring foreign exchange exposures and positions.

***Audit Committee***
The Audit Committee is appointed by the Board of Directors who are non-executive directors of the Group. The Audit Committee assists the Board in carrying out its responsibilities with respect to assessing the quality and integrity of financial reporting, the audit thereof, the soundness of the internal controls of the Group, the measurement system of risk assessment, and the methods for monitoring compliance with laws, regulations and supervisory and internal policies.

The audit committee reviews Group's accounting and financial practices, integrity of the Group's financial and internal controls and consolidated financial statements. It also reviews the Group's compliance with legal requirements, recommends the appointment, compensation and oversight of the Group's external and internal auditors.

***Internal Audit***
Risk management processes throughout the Group are audited by the internal audit function, that examines both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Board Audit Committee.

***Risk measurement and reporting systems***
The Group's risks are measured using a method which reflects both the expected loss likely to arise in normal circumstances and unexpected losses, which are an estimate of the ultimate actual loss based on statistical models. The models make use of probabilities derived from historical experience, adjusted to reflect the economic environment. The Group also runs worse case scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

**29 RISK MANAGEMENT (continued)**

**29.1 Introduction (continued)**

***Risk measurement and reporting systems (continued)***
Monitoring and controlling risks is primarily performed based on limits established by the Group. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept, with additional emphasis on selected industries. In addition, the Group monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the Board of Directors, the Credit / Risk Committee, and the head of each business division. The report includes aggregate credit exposure, credit metric forecasts, hold limit exceptions, liquidity ratios and risk profile changes. On a monthly basis detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the allowance for credit losses on a quarterly basis. The Board of Directors receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Group.

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information. A daily briefing is given to all relevant members of the Group on the utilisation of market limits, proprietary investments and liquidity, plus any other risk developments.

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

In order to avoid excessive concentrations of risk, the Group's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

**29.2 Credit risk**
Credit risk is the risk that one party to a financial contract will fail to discharge an obligation and cause the other party to incur a financial loss. The Group attempts to control credit risk by monitoring credit exposures, setting limits for transactions with counterparties, and continually assessing the creditworthiness of counterparties.

In addition to monitoring credit limits, the Group manages the credit exposures by entering into collateral arrangements with counterparties in appropriate circumstances and by limiting the duration of the exposure.

**29 RISK MANAGEMENT (continued)**

**29.2 Credit risk (continued)**

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

The table below shows the maximum exposure (excluding sovereign exposure) to credit risk for the components of the consolidated statement of financial position. The maximum exposure is shown net of provision, before the effect of mitigation through the use of master netting and collateral agreements.

| | ***Gross maximum exposure 2015 BD '000*** | *Gross maximum exposure 2014 BD '000* |
|---|---|---|
| **ASSETS** | | |
| Balances with other banks | **38,884** | 48,088 |
| Murabaha receivables from banks | **103,345** | 182,110 |
| Corporate Sukuk | **64,157** | 88,193 |
| Murabaha and Mudaraba financing | **413,308** | 376,716 |
| Ijarah Muntahia Bittamleek | **154,501** | 137,719 |
| Musharaka financing | **7,154** | 10,851 |
| Assets under conversion | **31,334** | 290,618 |
| Other assets | **23,714** | 16,753 |
| Total | **836,397** | 1,151,048 |
| Contingent liabilities and commitments | **167,693** | 215,712 |
| **Total credit risk exposure** | **1,004,090** | 1,366,760 |

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

***Type of credit risk***

Various contracts entered into by the Group comprise Murabaha financing, Mudaraba financing, Musharaka financing, Sukuk and Ijarah Muntahia Bittamleek contracts. Murabaha financing contracts cover land, buildings, commodities, motor vehicles and others. Mudaraba financing consist of financing transactions entered through other Islamic banks and financial institutions. Mudaraba is a partnership agreement in which the Islamic bank acts as the provider of funds (the Rabamal) while the recipient of the funds (the Mudarib or the manager) provides the professional, managerial and technical know-how towards carrying out the venture, trade or service with an aim of earning profit. The various financial instruments are:

*Murabaha financing*

The Group arranges Murabaha transactions by buying an asset (which represents the object of the Murabaha) and then selling this asset to customers (beneficiary) after adding a margin of profit over the cost. The sale price (cost plus profit margin) is paid in instalments over the agreed period.

**29 RISK MANAGEMENT (continued)**

**29.2 Credit risk (continued)**

*Ijarah Muntahia Bittamleek*

The legal title of the leased asset under Ijarah Muntahia Bittamleek passes to the lessee at the end of the Ijarah term, provided that all Ijarah instalments are settled.

a) The credit quality of balances with banks and Murabaha receivables from banks subject to credit risk is as follows:

| | ***31 December 2015*** | | | | |
|---|---|---|---|---|---|
| | ***Neither past due nor impaired*** | | | ***Past due or individually impaired*** | |
| | ***'A' Rated BD '000*** | ***'B' Rated BD '000*** | ***Unrated BD '000*** | ***BD '000*** | ***Total BD '000*** |
| Balances with banks | **34,999** | **2,326** | **1,559** | **-** | **38,884** |
| Murabaha and Wakala receivables from banks | **46,016** | **27,659** | **29,670** | **-** | **103,345** |
| | **81,015** | **29,985** | **31,229** | **-** | **142,229** |

| | *31 December 2014* | | | | |
|---|---|---|---|---|---|
| | *Neither past due nor impaired* | | | *Past due or individually impaired* | |
| | *'A' Rated BD '000* | *'B' Rated BD '000* | *Unrated BD '000* | *BD '000* | *Total BD '000* |
| Balances with banks | 37,365 | 5,446 | 5,277 | - | 48,088 |
| Murabaha and Wakala receivables from banks | 73,275 | 77,119 | 31,716 | - | 182,110 |
| | 110,640 | 82,565 | 36,993 | - | 230,198 |

The ratings referred to in the above tables are by one or more of the 4 international rating agencies (Standards & Poors, Moody's, Fitch and Capital Intelligence). The unrated exposures are with various high quality Middle East financial institutions, which are not rated by a credit rating agency. In the opinion of the management, these are equivalent to "A" rated banks.

b) The credit quality of Corporate sukuk, financing facilities and other assets that are subject to credit risk, based on internal credit ratings, is as follows:

| | ***31 December 2015*** | | | | | |
|---|---|---|---|---|---|---|
| | ***Neither past due nor impaired*** | | | ***Past due*** | | |
| | ***Satisfactory BD '000*** | ***Watch List BD '000*** | ***Substandard BD '000*** | ***Not impaired BD '000*** | ***Impaired BD '000*** | ***Total BD '000*** |
| Corporate Sukuk | **63,514** | **-** | **-** | **-** | **643** | **64,157** |
| Murabaha and Mudaraba financing | **306,449** | **11,254** | **-** | **56,489** | **39,117** | **413,309** |
| Ijarah Muntahia Bittamleek | **132,171** | **5,409** | **-** | **14,282** | **2,640** | **154,502** |
| Musharaka financing | **3,790** | **435** | **-** | **2,928** | **-** | **7,153** |
| Assets under conversion | **983** | **-** | **-** | **15,438** | **14,913** | **31,334** |
| Other assets | **23,714** | **-** | **-** | **-** | **-** | **23,714** |
| | **530,621** | **17,098** | **-** | **89,137** | **57,313** | **694,169** |

**29 RISK MANAGEMENT (continued)**

**29.2 Credit risk (continued)**

| | *31 December 2014* | | | | | |
|---|---|---|---|---|---|---|
| | *Neither past due nor impaired* | | | *Past due* | | |
| | *Satisfactory BD '000* | *Watch List BD '000* | *Substandard BD '000* | *Not impaired BD '000* | *Impaired BD '000* | *Total BD '000* |
| Corporate Sukuk | 87,550 | - | - | - | 643 | 88,193 |
| Murabaha and Mudaraba financing | 325,576 | 43,141 | - | 4,348 | 3,651 | 376,716 |
| Ijarah Muntahia Bittamleek | 128,547 | 1,818 | 967 | 4,850 | 1,537 | 137,719 |
| Musharaka financing | 10,274 | - | - | 525 | 52 | 10,851 |
| Assets under conversion | 214,012 | 1,167 | - | 47,736 | 27,703 | 290,618 |
| Other assets | 16,753 | - | - | - | - | 16,753 |
| | 782,712 | 46,126 | 967 | 57,459 | 33,586 | 920,850 |

In addition to the above, the financing facilities provided to the Government of Bahrain, its related entities and GCC sovereign entities amounts to BD 95,964 thousands (2014: BD 86,644 thousands).

All internal risk ratings are tailored to the various categories and are derived in accordance with the Group's rating policy. The attributable risk ratings are assessed and updated regularly.

c) Past due but not impaired financing facilities are analysed as follows:

| | ***31 December 2015*** | | | |
|---|---|---|---|---|
| | ***0-30 days BD '000*** | ***31-90 days BD '000*** | ***> 90 days BD '000*** | ***Total BD '000*** |
| Murabaha and Mudaraba financing | **19,447** | **17,836** | **19,205** | **56,488** |
| Ijarah Muntahia Bittamleek | **4,600** | **7,080** | **2,602** | **14,282** |
| Musharaka financing | **148** | **2,182** | **599** | **2,929** |
| Assets under conversion | **1,147** | **638** | **13,653** | **15,438** |
| | **25,342** | **27,736** | **36,059** | **89,137** |

| | *31 December 2014* | | | |
|---|---|---|---|---|
| | *0-30 days BD '000* | *31-90 days BD '000* | *> 90 days BD '000* | *Total BD '000* |
| Murabaha and Mudaraba financing | 2,753 | 1,420 | 175 | 4,348 |
| Ijarah Muntahia Bittamleek | 6 | 195 | 4,649 | 4,850 |
| Musharaka financing | 73 | - | 452 | 525 |
| Assets under conversion | 26,598 | 13,092 | 8,046 | 47,736 |
| | 29,430 | 14,707 | 13,322 | 57,459 |

All the past due but not impaired financing facilities are covered by collateral of BD 186,280 thousands (2014: BD 77,935 thousands). The utilisation of the collateral will be on customer by customer basis and is limited to the customers' total exposure.

The maximum credit risk, without taking into account the fair value of any collateral and Shari'a-compliant netting agreements, is limited to the amounts on the consolidated statement of financial position plus commitments to customers disclosed in Note 28 except capital commitments.

## 29 RISK MANAGEMENT (continued)

### 29.2 Credit risk (continued)

During the year BD 57,899 thousands (2014: BD 53,187 thousands) of financing facilities were renegotiated. Most of the renegotiated facilities are performing and are secured.

At 31 December 2015, the amount of credit exposure in excess of 15% of the Group's regulatory capital to individual counterparties was nil (2014: BD 3,356 thousands).

### 29.3 Legal risk and claims

Legal risk is the risk arising from the potential that unenforceable contracts, lawsuits or adverse judgements can disrupt or otherwise negatively affect the operations of the Group. The Group has developed controls and procedures to identify legal risks and believes that losses will be minimised.

As at 31 December 2015, legal suits amounting to BD 6,285 thousands (2014: BD 2,586 thousands) were pending against the Group. Based on the opinion of the Group's legal counsel, the total estimated liability arising from these cases is not considered to be material to the Group's consolidated financial position as the Group also has filed counter cases against these parties.

## 30 CONCENTRATIONS

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

The distribution of assets, liabilities and equity of investment account holders by geographic region and industry sector was as follows:

| | *Assets* | *Liabilities, equity of investment account holders and owners' equity* | *Contingent liabilities and Commitments* | *Assets* | *Liabilities, equity of investment account holders and owners' equity* | *Contingent liabilities and Commitments* |
|---|---|---|---|---|---|---|
| | *2015* | *2015* | *2015* | *2014* | *2014* | *2014* |
| | *BD '000* | *BD '000* | *BD '000* | *BD '000* | *BD '000* | *BD '000* |
| **Geographic region** | | | | | | |
| GCC | 1,470,200 | 1,266,869 | 170,087 | 1,732,319 | 1,553,152 | 215,180 |
| Arab World | 20,031 | 26,722 | 23 | 7,764 | 1,887 | - |
| Europe | 67,108 | 21,067 | 694 | 51,977 | 6,038 | 4,133 |
| Asia Pacific | 77,351 | 15,643 | 744 | 117,572 | 52,728 | 1,133 |
| North America | 10,923 | 1,302 | - | 22,179 | 7,007 | 4 |
| Others | 11,030 | 5,038 | 49 | 23,486 | 5,682 | 568 |
| | 1,656,643 | 1,336,641 | 171,597 | 1,955,297 | 1,626,494 | 221,018 |
| Owners' equity | - | 320,002 | - | - | 328,803 | - |
| | 1,656,643 | 1,656,643 | 171,597 | 1,955,297 | 1,955,297 | 221,018 |

## 30 CONCENTRATIONS (continued)

| | Assets | Liabilities, equity of investment account holders and owners' equity | Contingent liabilities and Commitments | Assets | Liabilities, equity of investment account holders and owners' equity | Contingent liabilities and Commitments |
|---|---|---|---|---|---|---|
| | 2015 | 2015 | 2015 | 2014 | 2014 | 2014 |
| | BD '000 | BD '000 | BD '000 | BD '000 | BD '000 | BD '000 |
| **Industry sector** | | | | | | |
| Government and public sector | 537,925 | 107,008 | 28,168 | 467,622 | 119,408 | 30,642 |
| Banks and financial institutions | 303,063 | 273,763 | 4,911 | 554,429 | 426,788 | 5,366 |
| Real estate | 407,449 | 210,969 | 48,089 | 410,678 | 205,966 | 83,405 |
| Trading and manufacturing | 122,415 | 103,745 | 48,678 | 193,638 | 104,447 | 55,553 |
| Aviation | 11,171 | 37,704 | - | 21,822 | 47,412 | - |
| Individuals | 179,001 | 499,008 | 1,456 | 185,828 | 547,402 | 4,186 |
| Others | 95,619 | 104,444 | 40,295 | 121,280 | 175,071 | 41,866 |
| | 1,656,643 | 1,336,641 | 171,597 | 1,955,297 | 1,626,494 | 221,018 |
| Owners' equity | - | 320,002 | - | - | 328,803 | - |
| | 1,656,643 | 1,656,643 | 171,597 | 1,955,297 | 1,955,297 | 221,018 |

## 31 MARKET RISK

Market risk arises from fluctuations in global yields on financial instruments and foreign exchange rates that could have an indirect effect on the Group's assets value and equity prices. The Board has set limits on the risk that may be accepted. This is monitored on a regular basis by the Asset and Liability Committee of the Group.

### 31.1 Equity price risk

Equity price risk arises from fluctuations in equity prices. The Board has set limits on the amount and type of investments that may be accepted. This is monitored on an ongoing basis by the Group's Investment Committee.

The effect on income (as a result of changes in the fair values of non-trading investments held at fair value through profit or loss and available-for-sale investments) solely due to reasonably possible changes in equity prices, is as follows:

| | 2015 | | | |
|---|---|---|---|---|
| | 10% increase | | 10% decrease | |
| | Effect on net profit BD '000 | Effect on equity BD '000 | Effect on net profit BD '000 | Effect on equity BD '000 |
| Quoted: | | | | |
| Bahrain | - | 193 | (193) | - |
| Saudi | 585 | - | (585) | - |
| Singapore | - | 284 | (284) | - |
| Frankfurt | 179 | - | (179) | - |
| Unquoted | 10,736 | 373 | (10,736) | (373) |

**31 MARKET RISK (continued)**

**31.1 Equity price risk (continued)**

| | 2014 | | | |
|---|---|---|---|---|
| | *10% increase* | | *10% decrease* | |
| | *Effect on net profit BD '000* | *Effect on equity BD '000* | *Effect on net profit BD '000* | *Effect on equity BD '000* |
| Quoted: | | | | |
| Bahrain | - | 301 | - | (301) |
| Saudi | 540 | - | (540) | - |
| Singapore | 1,155 | 372 | (1,155) | (372) |
| Frankfurt | 152 | - | (152) | - |
| Unquoted | 10,730 | 1,502 | (10,730) | (1,502) |

**31.2 Profit return risk**

The Group has exposure to fluctuations in the profit rates on its assets and liabilities. The Group recognises income on certain financial assets on a time-apportioned basis. The Group has set limits for profit return risk and these are monitored on an ongoing basis by the Group's Asset Liability Committee (ALCO).

The Group manages exposures to the effects of various risks associated with fluctuations in the prevailing levels of market profit rates on its financial position and cash flows.

The effect on income solely due to reasonably possible immediate and sustained changes in profit return rates, affecting both floating rate assets and liabilities and fixed rate assets and liabilities with maturities less than one year are as follows:

| | ***2015*** | | | |
|---|---|---|---|---|
| | ***Change in rate %*** | ***Effect on net profit BD '000*** | ***Change in rate %*** | ***Effect on net profit BD '000*** |
| Bahraini dinars | **0.10** | **(237)** | **(0.10)** | **237** |
| US dollars | **0.10** | **(191)** | **(0.10)** | **191** |

| | *2014* | | | |
|---|---|---|---|---|
| | *Change in rate %* | *Effect on net profit BD '000* | *Change in rate %* | *Effect on net profit BD '000* |
| Bahraini dinars | 0.10 | (208) | (0.10) | 208 |
| US dollars | 0.10 | (142) | (0.10) | 142 |

**31.3 Currency risk**

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on positions by currency. Positions are monitored on a periodic basis by the Asset Liability Committee to ensure positions are maintained within established limits.

Substantial portion of the Group's assets and liabilities are denominated in Bahrain dinars, US dollars or Saudi Riyals. As the Bahraini Dinar and Saudi Riyals are pegged to the US Dollars, positions in these currencies are not considered to represent significant currency risk as of 31 December 2015 and 2014.

## 32 LIQUIDITY RISK

Liquidity risk is the risk that the Group will be unable to meet its liabilities as they fall due. Liquidity risk can be caused by market disruptions or credit downgrades which may impact certain sources of funding. To mitigate this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining an adequate balance of cash, cash equivalents and readily convertible marketable securities. Liquidity position is monitored on an ongoing basis by the Asset Liability Committee.

The table below summarises the expected maturity profile of the Group's assets and liabilities as at 31 December 2015 and 2014:

| | *31 December 2015* | | | | |
|---|---|---|---|---|---|
| | *Up to 3 months BD '000* | *3 months to 1 year BD '000* | *1 to 5 years BD '000* | *Over 5 years BD '000* | *Total BD '000* |
| **ASSETS** | | | | | |
| Cash and balances with banks and the Central Bank | 135,505 | 11,215 | 5,852 | - | 152,572 |
| Sovereign Sukuk | 721 | 46,618 | 72,206 | 193,564 | 313,109 |
| Murabaha & Wakala receivables from banks | 103,345 | - | - | - | 103,345 |
| Corporate Sukuk | 675 | 16,566 | 37,238 | 9,678 | 64,157 |
| Murabaha and Mudaraba financing | 45,936 | 153,444 | 214,864 | 93,635 | 507,879 |
| Ijarah Muntahia Bittamleek | 4,272 | 6,222 | 62,881 | 81,842 | 155,217 |
| Musharaka financing | 1,951 | 819 | 2,793 | 1,591 | 7,154 |
| Assets under conversion | - | - | 22,163 | 9,869 | 32,032 |
| Non-trading investments | - | - | 123,157 | 357 | 123,514 |
| Investments in real estates | - | - | 68,786 | - | 68,786 |
| Development properties | - | - | 49,021 | - | 49,021 |
| Investment in associates | - | - | 7,525 | 2,469 | 9,994 |
| Other assets | 34,590 | 2,144 | 3,056 | 4,102 | 43,892 |
| Goodwill | - | - | - | 25,971 | 25,971 |
| | 326,995 | 237,028 | 669,542 | 423,078 | 1,656,643 |
| **LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS** | | | | | |
| Murabaha and Wakala payables to banks | 91,067 | 13,437 | 16,291 | - | 120,795 |
| Wakala payables to non-banks | - | 84,257 | 758,313 | - | 842,570 |
| Current accounts | 224,366 | - | - | - | 224,366 |
| Liabilities under conversion | 2,327 | - | - | - | 2,327 |
| Term financing | - | 7,531 | 28,455 | - | 35,986 |
| Other liabilities | 19,995 | 20,329 | 7,922 | - | 48,246 |
| Equity of investment accountholders | 18,706 | 12,470 | 31,175 | - | 62,351 |
| | 356,461 | 138,024 | 842,156 | - | 1,336,641 |

**32 LIQUIDITY RISK (continued)**

| | *31 December 2014* | | | | |
|---|---|---|---|---|---|
| | *Up to 3 months BD '000* | *3 months to 1 year BD '000* | *1 to 5 years BD '000* | *Over 5 years BD '000* | *Total BD '000* |
| ASSETS | | | | | |
| Cash and balances with banks and Central Bank | 256,575 | - | 21,176 | - | 277,751 |
| Sovereign Sukuk | 10,267 | - | 87,655 | 47,867 | 145,789 |
| Murabaha & Wakala receivables from banks | 182,110 | - | - | - | 182,110 |
| Corporate Sukuk | - | 19,902 | 52,654 | 15,637 | 88,193 |
| Murabaha and Mudaraba financing | 28,803 | 121,852 | 211,206 | 98,168 | 460,029 |
| Ijarah Muntahia Bittamleek | 28,402 | 13,044 | 59,141 | 40,465 | 141,052 |
| Musharaka financing | 3,010 | 1,774 | 3,393 | 2,674 | 10,851 |
| Assets under conversion | 30,185 | 21,326 | 257,148 | - | 308,659 |
| Non-trading investments | - | - | 145,121 | 1,975 | 147,096 |
| Investments in real estates | - | - | 65,149 | - | 65,149 |
| Development properties | - | - | 59,262 | - | 59,262 |
| Investment in associates | - | - | 7,753 | 2,739 | 10,492 |
| Other assets | 23,854 | 2,096 | 474 | 6,469 | 32,893 |
| Goodwill | - | - | - | 25,971 | 25,971 |
| | 563,206 | 179,994 | 970,132 | 241,965 | 1,955,297 |
| LIABILITIES AND EQUITY OF INVESTMENT ACCOUNTHOLDERS | | | | | |
| Murabaha and Wakala payables to banks | - | 44,179 | 77,087 | - | 121,266 |
| Wakala payables to non-banks | - | 103,405 | 930,647 | - | 1,034,052 |
| Current accounts | 226,648 | - | - | - | 226,648 |
| Liabilities under conversion | 9,637 | 14,962 | 125,022 | - | 149,621 |
| Term financing | 303 | 935 | 20,099 | - | 21,337 |
| Other liabilities | 40,568 | 4,323 | 527 | - | 45,418 |
| Equity of investment accountholders | 8,445 | 5,631 | 14,076 | - | 28,152 |
| | 285,601 | 173,435 | 1,167,458 | - | 1,626,494 |

## 32 LIQUIDITY RISK (continued)

The table below summarises the maturity profile of the Group's financial liabilities at 31 December 2015 and 2014 based on contractual undiscounted payment obligation:

| | *31 December 2015* | | | | | |
|---|---|---|---|---|---|---|
| | ***On demand BD '000*** | ***Up to 3 months BD '000*** | ***3 months to 1 year BD '000*** | ***1 to 5 years BD '000*** | ***Over 5 years BD '000*** | ***Total BD '000*** |
| **LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS, COMMITMENTS AND CONTINGENT LIABILITIES** | | | | | | |
| Murabaha & Wakala payables to banks | - | 112,366 | 8,429 | - | - | 120,795 |
| Wakala payables to non-banks | - | 384,898 | 427,200 | 30,472 | - | 842,570 |
| Current accounts | 224,366 | - | - | - | - | 224,366 |
| Equity of investment accountholders | 27,986 | 34,365 | - | - | - | 62,351 |
| Liabilities under conversion | - | - | 2,327 | - | - | 2,327 |
| Term financing | - | - | 7,531 | 28,455 | - | 35,986 |
| Unutilised commitments | 9,319 | 23,370 | 67,062 | 9,063 | 7,674 | 116,488 |
| Contingent liabilities | 40,013 | 291 | 1,037 | 2,577 | - | 43,918 |
| Other financial liabilities | - | 6,245 | 12,438 | 195 | - | 18,878 |
| Profit on financial liabilities | - | 1,037 | 5,986 | 3,063 | - | 10,086 |
| | 301,684 | 562,572 | 532,010 | 73,825 | 7,674 | 1,477,765 |

| | *31 December 2014* | | | | | |
|---|---|---|---|---|---|---|
| | *On demand BD '000* | *Up to 3 months BD '000* | *3 months to 1 year BD '000* | *1 to 5 years BD '000* | *Over 5 years BD '000* | *Total BD '000* |
| LIABILITIES, EQUITY OF INVESTMENT ACCOUNTHOLDERS, COMMITMENTS AND CONTINGENT LIABILITIES | | | | | | |
| Murabaha & Wakala payables to banks | - | 103,091 | 18,175 | - | - | 121,266 |
| Wakala payables to non-banks | - | 332,009 | 553,664 | 147,730 | 649 | 1,034,052 |
| Current accounts | 226,648 | - | - | - | - | 226,648 |
| Equity of investment accountholders | - | 28,152 | - | - | - | 28,152 |
| Liabilities under conversion | - | 58,422 | 25,511 | 51,971 | 13,717 | 149,621 |
| Term financing | 303 | 935 | 20,099 | - | - | 21,337 |
| Unutilised commitments | 33,594 | 7,337 | 50,686 | 18,358 | 7,653 | 117,628 |
| Contingent liabilities | 2,199 | 17,475 | 24,381 | 6,190 | - | 50,245 |
| Other financial liabilities | - | 5,971 | 5,855 | 427 | - | 12,253 |
| Profit on financial liabilities | 81 | 1,254 | 9,083 | 7,888 | 49 | 18,355 |
| | 262,825 | 554,646 | 707,454 | 232,564 | 22,068 | 1,779,557 |

## 33 SEGMENT INFORMATION

**Primary segment information**

For management purposes, the Group is organised into four major business segments:

| | |
|---|---|
| **Banking** | - Principally managing Shari'a compliant profit sharing investment accounts, and offering Shari'a compliant financing contracts and other Shari'a-compliant products. This segment comprises corporate banking, retail banking and private banking and wealth management. |
| **Treasury** | - Principally handling Shari'a compliant money market, trading and treasury services including short-term commodity Murabaha. |
| **Investments** | - Principally the Group's proprietary portfolio and serving clients with a range of investment products, funds and alternative investments. |
| **Capital** | - Manages the undeployed capital of the Group by investing it in high quality financial instruments, incurs all expenses in managing such investments and accounts for the capital governance related expenses. |

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:

| | *31 December 2015* | | | | |
|---|---|---|---|---|---|
| | ***Banking BD '000*** | ***Treasury BD '000*** | ***Investments BD '000*** | ***Capital BD '000*** | ***Total BD '000*** |
| **Operating income** | **32,493** | **8,969** | **7,054** | **9,295** | **57,811** |
| **Segment result** | **8,998** | **6,532** | **(4,458)** | **(524)** | **10,548** |
| **Segment assets** | **655,372** | **618,757** | **219,074** | **163,440** | **1,656,643** |
| **Segment liabilities, and equity** | **1,108,457** | **177,678** | **39,565** | **330,943** | **1,656,643** |

Goodwill resulting from BMI acquisition is allocated to banking segment.

| | *31 December 2014* | | | | |
|---|---|---|---|---|---|
| | *Banking BD '000* | *Treasury BD '000* | *Investments BD '000* | *Capital BD '000* | *Total BD '000* |
| Operating income | 30,931 | 5,757 | 8,507 | 873 | 46,068 |
| Segment result | 7,148 | 4,448 | 5,600 | (1,375) | 15,821 |
| Segment assets | 830,396 | 537,408 | 356,947 | 230,546 | 1,955,297 |
| Segment liabilities, and equity | 1,444,201 | 121,549 | 62,258 | 327,289 | 1,955,297 |

**Secondary segment information**

The Group primarily operates in the GCC and derives substantially all its operating income and incurs all operating expenses in the GCC.

## 34 FIDUCIARY ASSETS

Funds under management at the year-end amounted to BD 80,891 thousands (2014: BD 78,178 thousands). These assets are held in a fiduciary capacity and are not included in the consolidated statement of financial position.

## 35 SHARI'A SUPERVISORY BOARD

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

## 36 FAIR VALUE OF FINANCIAL INSTRUMENTS

The fair value of sovereign sukuk is BD 303,506 thousands (2014: BD 147,593 thousands). The estimated fair values of other financial instruments are not materially different to their carrying values as of 31 December 2015 and 2014.

## 37 EARNINGS AND EXPENSES PROHIBITED BY SHARI'A

During the year, the Group received Sharia' prohibited income totalling BD 189 thousands (2014: BD 211 thousands). These include, income earned from the conventional financing and investments, penalty charges from customers and income on current account balances held with correspondent banks. These funds were allocated to charitable contributions.

## 38 SOCIAL RESPONSIBILITY

The Group discharges its social responsibility through charity fund expenditures and donations to individuals and organisations which are used for charitable purposes. During the year the Group paid an amount of BD 320 thousands (2014: BD 225 thousands) on account of charitable donations.

## 39 ZAKAH

Pursuant to a resolution of the shareholders in an EGM held on 12 November 2009, it was resolved to amend the articles of association of the Bank to inform the shareholders of their obligation to pay Zakah on income and net worth. Consequently, Zakah is not recognized in the consolidated income statement as an expense. The total Zakah payable by the shareholders for 2015 has been determined by the Shari'a supervisory board as 3.9 fils (2014: 3.8 fils) per share.

## 40 CAPITAL ADEQUACY

The primary objectives of the Group's capital management policies are to ensure that the Group complies with externally imposed capital requirements and that the Group maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value. Capital adequacy for each of the group companies is also managed separately at individual company level. The Group does not have any significant restrictions on its ability to access or use its assets and settle its liabilities other than any restrictions that may result from the supervisory frameworks within which the banking subsidiaries operate.

## 40 CAPITAL ADEQUACY (continued)

In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

The regulatory capital and risk-weighted assets have been calculated in accordance with Basel III as adopted by the CBB.

| | ***2015*** |
|---|---|
| | ***BD '000*** |
| Common equity Tier 1 capital | ***268,814*** |
| Tier 2 capital | **32,240** |
| Total capital | **301,054** |
| Credit risk-weighted assets | **1,381,565** |
| Market risk-weighted assets | **19,606** |
| Operational risk-weighted assets | **99,967** |
| Total risk-weighted assets | **1,501,138** |
| Total capital ratio | **20.1%** |
| Minimum requirement | **12.5%** |

Capital adequacy ratio for 2014 was calculated to be 18.7%. This included the regulatory capital of BD 263,222 thousand and risk-weighted assets of BD 1,407,346 thousand, calculated in accordance with Basel II regulations as adopted by the CBB.

## 41 DEPOSIT PROTECTION SCHEME

Deposits held with the Group's Bahrain operations are covered by the Deposit Protection Scheme (the Scheme) which was established by the Central Bank of Bahrain concerning the establishment of Deposit Protection Scheme and Deposit Protection Board. No liability is due until one of the member commercial banks of the Scheme is unable to meet its deposit obligations.

## 42 COMPARATIVE FIGURES

Certain of the prior year figures have been reclassified to conform to the current year presentation. Such reclassifications did not affect previously reported net profit, total assets, total liabilities and total equity of the Group.