NBB بنك البحرين الوطني

Enriching the lives of generations

Annual Report 2018

#TeamBahrain

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Designed and Produced by The Bridge Partnership

His Royal Highness Prince Khalifa bin Salman Al Khalifa
The Prime Minister of the Kingdom of Bahrain

His Majesty King Hamad bin Isa Al Khalifa
The King of the Kingdom of Bahrain

His Royal Highness Prince Salman bin Hamad Al Khalifa
The Crown Prince, Deputy Supreme Commander and First Deputy Prime Minister of the Kingdom of Bahrain

Your **National** Partner

In 2018, we delivered the first phase of our brand transformation, motivated by our drive to reposition National Bank of Bahrain as a contemporary, dynamic and engaging organisation sitting at the heart of the community, with a vision to enrich the lives of generations.

We created and implemented our new brand promise, 'Closer to you', clearly demonstrated through a whole new approach in creating high levels of engagement during Ramadhan, National Day, Spring of Culture, global conferences (Euromoney), and the Bahrain International Airshow. The revised brand guidelines allowed us to present a more appealing and consistent look and feel in our marketing and advertising materials. We also took the Bank to the people, holding celebratory events for our Al Watani savings scheme at various public venues. In addition, we also focused on several youth-related initiatives such as Ironkids and Irongirls, Grassroots U13 Football, and direct support to student activities at both University of Bahrain and Bahrain Polytechnic.

Scan QR code to watch the NBB new identity transformation video.

Please flip over the page to see NBB's identity transformation over the years >

The NBB brand has been standing tall for generations, providing security and stability for over 60 years. The brand legacy dates back to its inception in 1957.

Our new brand identity is an evolution of the NBB shield. It is an icon for the modernisation and realignment of our brand.
In line with the Bank's overall transformation ambitions, the new identity will accompany the Bank into the next era of banking.

بنك البحرين
BANK OF BAHRAIN

1957

بنك البحرين
Bank of Bahrain

1962

NATIONAL BANK OF BAHRAIN

1973

1975

National Bank of Bahrain
بنك البحرين الوطني

1990

NBB

2007

2019

NBB
بنك البحرين الوطني

NBB
بنك البحرين الوطني

WE ARE BAHRAIN'S FIRST NATIONAL BANK.

Since our establishment in 1957 as Bahrain's first national bank, we have been enriching the lives of generations. Throughout the years, we have developed leading services and products in retail and commercial banking with an aim to contribute positively to the Kingdom's economy and its people.

Following an ambitious growth strategy, we have expanded locally and to key GCC markets including Riyadh, Kingdom of Saudi Arabia and Abu Dhabi in the United Arab Emirates.

From providing the largest network of branches and ATMs in Bahrain to developments in omnichannel banking, we have paved the way in innovation and convenience for our customers.

With a plan to further enhance our services and product range in Bahrain and the GCC, we look forward to bringing new and improved experiences to our customers and to the market.

We have embarked on a journey of digital and internal transformation to improve our agility even further and to anticipate customer needs. Driven by our brand culture and passionate team, we focus everything we do on being closer to our customers, offering products and services that will truly enrich their lives. Introducing new tiers of products, cards, revamping mobile banking systems and re-imagining the branch experience are only a few of the initiatives currently in progress.

A proudly Bahraini brand, we are listed on the Bahrain Bourse with a strong local stakeholder profile. Our ownership is comprised of 44.94% local private and institutional investors, 44.18% Bahrain Mumtalakat Holding Company, wholly-owned by the Government of the Kingdom of Bahrain, and 10.88% by the Social Insurance Organisation.

VALUES

- **Pride:** Work with heart
- **Teamwork:** Collaborate for success
- **Respect:** Connect with respect
- **Responsibility:** Own it and embrace it
- **Ethics:** Always do the right thing
- **Transparency:** Be fearlessly transparent

Scan QR code to watch the National Day Song video.

MISSION

To always connect with you, to understand you and help give you what you need, when you need it, in a way that works for you.

PURPOSE

Enriching the lives of generations.

PROMISE

Closer to you

Maha Al Mahmood
Head - Treasury Sales

Abdulla Buali
Project Management Officer

Aref Janahi
Head - Commercial & SMEs

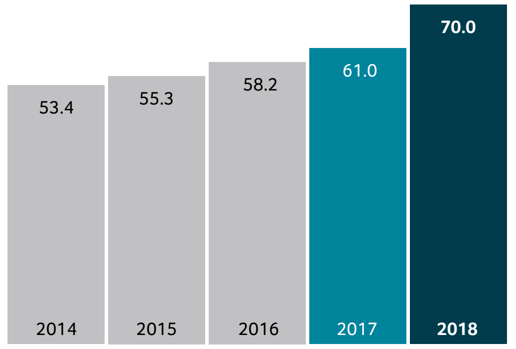
Financial Highlights

National Bank of Bahrain delivered sustained growth in revenue and profit, increased productivity and shareholder value.

	2018	2017	2016	2015	2014
Earnings (BHD millions)					
Net interest income	**87.2**	73.1	66.0	59.5	59.6
Other income	**30.2**	31.4	30.9	34.9	29.6
Operating expenses	**41.8**	33.0	34.1	30.1	29.2
Profit for the year	**70.0**	61.0	58.2	55.3	53.4
Cash dividend	**35.1**	31.9	29.0	26.4	23.5
Stock dividend	**14.0**	12.8	11.6	10.5	9.4
Financial Position (BHD millions)					
Total assets	**3,195.5**	3,101.5	2,977.1	2,999.7	2,738.5
Loans and advances	**1,190.1**	1,226.9	1,031.9	1,051.7	781.0
Investment securities	**1,132.2**	1,067.3	1,092.9	1,094.0	999.5
Earning assets	**3,020.7**	2,939.7	2,823.0	2,837.9	2,580.9
Total deposits	**2,675.9**	2,617.1	2,526.4	2,588.2	2,321.3
Customer deposits	**2,190.6**	2,165.2	2,088.4	2,247.0	2,154.9
Shareholders' equity	**475.8**	447.9	414.7	364.8	378.0
Ratios (%)					
Earnings					
Return on average equity	**15.2**	14.1	14.9	14.9	14.4
Return on average assets	**2.2**	2.0	2.0	1.9	2.0
Earnings per share (Fils)	**50**	44	42	40	38
Cost-to-income ratio	**35.6**	31.6	35.2	31.9	32.7
Earnings per full-time employee (BHD 000's)	**102.6**	98.6	102.4	98.3	96.5
Capital					
Shareholders' equity as % of total assets	**14.9**	14.4	13.9	12.2	13.8
Total liabilities to shareholders' equity (times)	**5.7**	5.9	6.2	7.2	6.2
Capital adequacy 2015 to 2018: Basel 3 (2014: Basel 2)	**33.8**	36.3	35.4	30.0	34.3

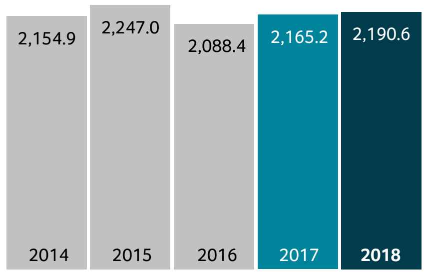
Profit for the year
(BHD millions)

70.0



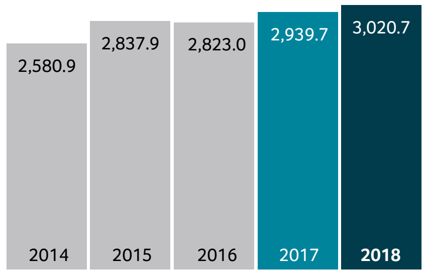
Customer deposits
(BHD millions)

2,190.6



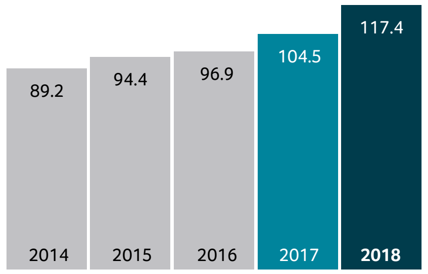
Earning assets
(BHD millions)

3,020.7



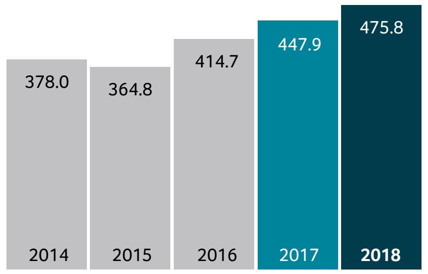
Total income
(BHD millions)

117.4



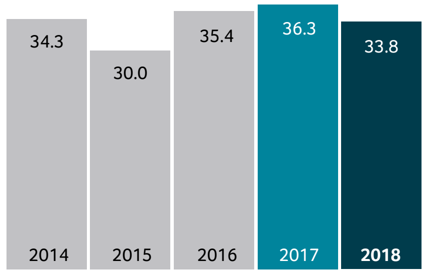
Equity
(BHD millions)

475.8



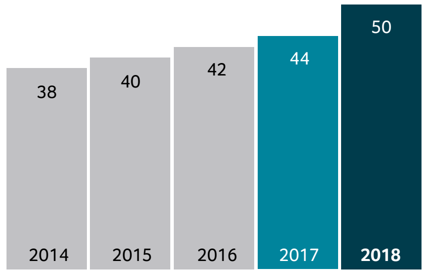
Capital adequacy
(%)

33.8



Earnings per share
(Bahraini fils)

50



Board of Directors

FAROUK YOUSUF KHALIL ALMOAYYED (Chairman)

Non-executive
Appointed to the Board in 1997
Chairman: Nomination and Remuneration Committee; Donations and Contributions Committee.

Chairman: Y. K. Al Moayyed and Sons; Al Moayyed International Group; Ashrafs; Bahrain Duty Free; Bahrain Hotels Company; Ahlia University; National Finance House; Bahrain Insurance Holding Company.
Director: Economic Development Board (EDB); Investcorp Bank B.S.C.

DR. ESSAM ABDULLA FAKHRO (Deputy Chairman)

Non-executive
Appointed to the Board in 2008
Chairman: Executive Committee
Member: Nomination and Remuneration Committee; Donations and Contributions Committee.

Chairman: Bahrain Cinema Company; Abdulla Yousif Fakhro and Sons Group; Bahrain Islamic Bank.

FAWZI AHMED KANOO (Deputy Chairman)

Independent
Appointed to the Board in 2010
Member: Executive Committee; Donations and Contributions Committee.

Chairman: Abdulrahman Jassim Kanoo Co. W.L.L.
Executive Chairman: Bahrain Ship Repairing and Engineering Co B.S.C.
Deputy Chairman: Yusuf Bin Ahmed Kanoo Group (Bahrain); Bahrain Hotels Company.

KHALID YOUSIF ABDUL RAHMAN (Director)

Independent
Appointed to the Board in 2001
Chairman: Audit Committee.

Chairman: The Food Supply Company Limited (Fosco).
Deputy Chairman: Awal Dairy Company.
Director, member of the Executive Committee and Audit Committee: Bahrain Ship Repair and Engineering Company.
Director and member of the Executive Committee: Bahrain Islamic Bank
CEO: National Transport Establishment.

HUSSAIN SULTAN AL GHANEM (Director)

Non-executive
Appointed to the Board in 2004
Member: Executive Committee.

Undersecretary, Human Resources; Prime Minister's Court.

KHALID OMAR AL ROMAIHI (Director)

Non-executive
Appointed to the Board in 2014
Chairman: Risk Committee.

Director and CEO: Economic Development Board (EDB).
Chairman: Bahrain Real Estate Investment Company (Edamah); Bahrain Development Bank.
Director: Bahrain Mumtalakat Holding Company.


Farouk Yousuf Khalil Almoayyed
Chairman


Dr. Essam Abdulla Fakhro
Deputy Chairman


Fawzi Ahmed Kanoo
Deputy Chairman


Khalid Yousif Abdul Rahman
Director


Hussain Sultan Al Ghanem
Director

SH. RASHID BIN SALMAN MOHAMED AL KHALIFA (Director)

Non-executive
Appointed to the Board in 2014
Member: Executive Committee; Nomination and Remuneration Committee.

Retired banker and independent consultant for investment and banking services.

MOHAMED TAREQ MOHAMED SADEQ MOHAMED AKBAR (Director)

Non-executive
Appointed to the Board in 2018
Member: Audit Committee.

Fellow: Institute of Chartered Accountants in England and Wales (ICAEW).

Chairman: Ibdar Bank B.S.C. (c).
Director: Ahli United Bank Kuwait K.S.C., Ahli United Bank (SAE) Egypt and Ahli United Bank Limited, Dubai (UAE), Bahrain International Golf Course Company B.S.C. (c); Al Zayani Investments B.S.C. (c).

HALA ALI HUSSAIN YATEEM (Director)

Independent
Appointed to the Board in 2018
Member: Audit Committee; Donations and Contributions Committee.

Director: Bahrain Real Estate Investment Company (Edamah); Ali and Mohamed Yateem Group of Companies W.L.L.

YUSUF ABDULLA YUSUF AKBAR ALIREZA (Director)

Independent
Appointed to the Board in 2018
Member: Executive Committee; Nomination and Remuneration Committee

Founder of ARP Global Capital Ltd., an alternative asset management firm in 2018. He was the CEO of Noble Group, the largest Asian commodity firm and a Fortune 100 company from 2012 to 2016 after working for 20 years with Goldman Sachs and Co where his last role was Co-President of Asia.

Director: Bahrain Economic Development Board (EDB), the Global Board of Room to Read and the Center for Contemporary Arab Studies Georgetown University.

The first Arab Partner in Goldman Sachs and Co and the only Arab to ever be elected to the firm's Global Management Committee.

RISHI KAPOOR (Director)

Independent
Appointed to the Board in 2018
Member: Risk Committee.

Investcorp's Co-Chief Executive Officer, responsible for overseeing activities across North America, Europe, India and the Middle East, covering private equity, real estate investments, credit management and absolute return investments.

He is the Chairman of Investcorp Investment Committees; a member of the Executive Committee, Operating Committee and the Financial Risk Management Committee.

Director: Duke University's regional advisory board for the Middle East; Gulf Air Group; Bahrain Airport Company; Gulf Aviation Academy.

In 2018, Forbes Middle East recognised Rishi as a top Indian leader in the Arab world.


Khalid Omar Al Romaihi
Director


Sh. Rashid Bin Salman Mohamed Al Khalifa
Director


Hala Ali Husain Yateem
Director


Yusuf Abdulla Yusuf Akbar Alireza
Director


Mohamed Tareq Mohamed Sadeq Mohamed Akbar
Director


Rishi Kapoor
Director

Board of Directors' Report

"The excellent results achieved in 2018 by NBB under the new management team vindicate the decision made by the Board to adapt the Bank's strategy to a fast-evolving banking industry and to our clients' new requirements".

Farouk Yousuf Khalil Almoayyed
Chairman

NET PROFIT
BHD 70.0 million

The Bank achieved strong financial results and record net profit

TOTAL ASSETS
BHD 3,195.5 million

Total assets were up by 3.0% compared to 2017 level

The Board of Directors of National Bank of Bahrain (NBB) takes pleasure in presenting the 62nd annual report of the Bank together with the financial statements for the year ended 31 December 2018, marking another year of strong growth and enhanced profitability.

Overall performance

NBB achieved strong financial results and record net profit of BHD 70.0 million (USD 186.1 million) compared to BHD 61.0 million (USD 162.3 million) for the previous year, an increase of 14.8%. Key performance indicators continue to remain strong with a return on average equity of 15.2% (2017: 14.1%) and earnings per share of 50 fils (2017: 44 fils). The financial position of the Bank remained strong. Total assets stood at BHD 3,195.5 million (USD 8,498.6 million) as at 31 December 2018 compared to BHD 3,101.5 million (USD 8,248.8 million) as at 31 December 2017, a growth of 3.0%.

Scan QR code to watch the Chairman video.

"The Bank witnessed a growing involvement in the local economy and the diversification of its expertise to serve all segments of our customer base. In 2018, the Bank increased its penetration of the SMEs segment, which is one of the major pillars of our economy".

Of particular importance is the growth of 8.7% recorded in average loans and advances to BHD 1,272.3 million (USD 3,383.8 million) compared with BHD 1,171.0 million (USD 3,114.4 million) last year. The Bank has a strong capital base with a capital adequacy ratio of 33.8% (before proposed appropriations) as at 31 December 2018.

The excellent results achieved in 2018 by NBB under the new management team vindicate the decision made by the Board to adapt the Bank's strategy to a fast-evolving banking industry and to our clients' new requirements. I am particularly satisfied to witness NBB's growing involvement in the local economy and the diversification of its expertise to serve all segments of our customer base. In 2018, the Bank increased its penetration of the SMEs segment, which is one of the major pillars of our economy. NBB also participated as arrangers in key projects for the Kingdom. The new strategy gives our Bank greater visibility in the market place and offers our clients a better quality of service, coupled with access to new financing solutions.

The Board has encouraged the team to pursue its digital strategy at all levels and I am encouraged to see the first results of this important paradigm shift. We will continue supporting the management team in their efforts to maintain the longest-serving local Bank in Bahrain in its position of leadership in its market.

Details of the Bank's financial position and performance are further elaborated in the financial review and financial statements sections that follow.

Recommended appropriations

Based on the results, the Board of Directors has recommended for approval by shareholders the following appropriations:

	BHD millions
Cash dividend (25%)	35.1
Bonus shares (10%)	14.0
Donations and contributions	3.5
Transfer to statutory reserve	7.0

Donations and contributions

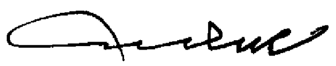
The Board is recommending the allocation of BHD 3.5 million (USD 9.3 million) to the Donations and Contributions Programme, representing 5% of the Bank's 2018 profit. The cumulative allocation under the programme, since its inception in 1980, now stands at BHD 49.2 million (USD 130.9 million).

Corporate governance

The Board recognises that good governance is integral to the success of any organisation and is fully committed to protecting the interests of all stakeholders through robust and international standard governance policies. The Bank is in compliance with the requirements of the Code of Corporate Governance issued by the Ministry of Industry and Commerce and the Central Bank of Bahrain's Rulebook. A detailed report on the Bank's compliance with the Corporate Governance Code is elaborated on in the corporate governance report section of the annual report. The report also contains disclosures on the number of shares held as at 31 December 2018 by Directors and trading during the year in the Bank's shares by Directors, senior management, approved persons and their related parties.

Acknowledgements

The Directors, on behalf of the shareholders, take this opportunity to extend their gratitude to His Majesty King Hamad bin Isa Al Khalifa, King of Bahrain, His Royal Highness Prince Khalifa bin Salman Al Khalifa, Prime Minister, His Royal Highness Prince Salman bin Hamad Al Khalifa, Crown Prince, Deputy Supreme Commander and First Deputy Prime Minister and the many government ministries and institutions. We would also like to acknowledge the ongoing support and invaluable guidance provided to us by the Ministry of Finance and National Economy, and the Central Bank of Bahrain. The Directors also express their appreciation to our loyal customers for their continued partnership with NBB and their confidence in the Bank. In concluding, I would like to congratulate our management team and all employees for their outstanding performance and their contributions to the achievements of the past year. I would like also to extend thanks and gratitude to the Board of Directors Secretary, Nasser Mohammed Nasser, who retired from his role after serving the Bank for more than 47 years, during which he served for 15 years in his latest position and I wish him all the best in his endeavours. We look forward to a strong 2019 and to keeping you apprised of NBB's progress in the year ahead.



Farouk Yousuf Khalil Almoayyed
Chairman
28 January 2019

Executive Management

JEAN-CHRISTOPHE DURAND
Chief Executive Officer

Mr. Jean-Christophe Durand joined National Bank of Bahrain (NBB) as CEO in December 2016 where he continues to focus on reinforcing and expanding the Bank's role as a driver for economic growth and development. He brings to his role over 37 years of international and regional banking and finance experience gained from senior leadership roles at leading global banking institutions of which 30 years are in the GCC. Previously, and for 20 years, he was the CEO of BNP Paribas Middle East and Africa region for Corporate and Institutional Banking and Asset Management. Mr. Durand holds several Board positions locally and regionally. He is a Director for Gulf Air, and Bahrain Telecommunications Company (Batelco) and the Deputy Chairman of Batelco's Executive Committee Nomination, Remuneration, Donations and Corporate Governance Committee. He is also the Vice Chairman for Umniah Telecommunication Company in Jordan, and a Director for Bahrain Institute of Banking and Finance (BIBF) and the Chairman of the French Chamber of Commerce and Industry in Bahrain (FCCIB). Mr. Durand received the 'Legion d'Honneur' from the Government of France and is a graduate from ESSEC (Ecole Superieure des Sciences Economiques et Commerciales) in Paris.

ABDUL AZIZ AL AHMED
Chief Executive – Retail, Commercial and SMEs

Mr. Abdul Aziz joined NBB in 1974. He has 44 years of banking experience at NBB. He assumed his present position in 2011. He is the Vice Chairman of the Automotive Board for National Motor Company W.L.L. (NMC); Tas'heelat Automotive Company S.P.C. (TAC); Tas'heelat Car Leasing Company W.L.L. (TCL), Bahrain; and Tas'heelat for General Trading and Cars W.L.L. (TGTC); ErbilKurdistan, Republic of Iraq. He holds an Executive Diploma from University of Virginia, USA.

HUSSAIN AL HUSSAINI
Chief Executive – Treasury, Capital Markets and Wealth Management

Mr. Al Hussaini joined NBB in 1982 and assumed his present position in 2017. He has 36 years of experience at NBB. He serves as Vice Chairman of the Board of Directors and Vice Chairman of the Investment Committee of the Securities and Investment Company (SICO); Board Member and Executive Committee Chairman of Esterad Investment Company; Chairman of Nomination and Remuneration Committee of Esterad; Member of Board of Trustees in Bahrain Polytechnique; Member of the Deposit Protection and Unrestricted Investor Accounts. He holds an MBA in Marketing and Management, DePaul University, USA; and a B.A. in Economics, Concordia University, Canada.

DANA BUHEJI

Chief Human Resource Officer

Ms. Buheji joined NBB in 2017 as the Chief Human Resource Officer. Her focus lies on ensuring the Bank effectively maximises its talent base, invests in the training and development of staff and effectively recruits and retains staff to support the Bank's efforts to grow and diversify. She has 18 years of extensive experience with Bahrain Economic Development Board (EDB), Bahrain Mumtalakat Holding Company, Ministry of Finance and National Economy, and Ahli United Bank. She serves as a Member of HR and Remuneration Committee of Bahrain Association of Banks (BAB). She holds a Certificate in Personnel Practice (CPP), London, UK and B.A. in Commerce, Concordia University, Canada.

IAIN BLACKLAW
Chief Operating Officer

Mr. Blacklaw joined the Bank in 2017 bringing to his role more than 30 years of experience as an international banking and finance executive who has built and run large-scale operations across various sectors including banking and technology. His focus is on helping NBB strengthen its structure and foundation to create a more competitive Bank. This includes realising greater efficiencies and the streamlining of operations through the optimisation and modernisation of practices both on the brick-and-mortar level and through the adoption of the latest technologies.

Jean-Christophe Durand
Chief Executive Officer

Abdul Aziz Al Ahmed
Chief Executive – Retail, Commercial and SMEs

Hussain Al Hussaini
Chief Executive – Treasury, Capital Markets and Wealth Management

Dana Buheji
Chief Human Resource Officer

Hisham Al Kurdi
Chief Executive – Corporate Institutions and Investment Banking

BRUCE WADE
Chief Risk Officer

Mr. Wade joined NBB in 2014. He brings to NBB more than 35 years of banking experience including roles at Saudi Hollandi Bank; Riyad Bank; Citibank; and Bank of Tokyo Group. He is Chairman of the Risk Management Committee, Bahrain Association of Banks. Mr. Wade holds an MBA and Bachelor of Applied Science from Queensland University of Technology, Australia and a Graduate Diploma, Applied Finance and Investment, Securities Institute of Australia. He is also a Fellow Australian Institute of Company Directors, Fellow Financial Services Institute of Australasia, Member Finance and Treasury Association Limited, Senior Certified Treasury Professional.

YASER ALSHARIFI
Chief Strategy Officer

Mr. Alsharifi joined NBB in 2017 as the Chief Strategy Officer, responsible for innovation, strategy development and implementation, the project management office, business development, as well as the operations in Saudi Arabia and the United Arab Emirates. Mr. Alsharifi previously worked with Al Rajhi Holdings and Ernst and Young. He has 24 years' experience in investment management and corporate finance across the GCC, Europe and the US. Additionally, Mr. Alsharifi serves as the Chairman of the Advisory Board of Bahrain Fintech Bay, Chairman of Danat Bahrain Institute for Pearls and Gemstones. He is a board member of Edamah, Bahrain Bourse, Bahrain Clear, and Bahrain Car Parks Company B.S.C. He holds a B.A. in Business Administration from the University of Massachusetts at Amherst.

RICHARD HICKS
Chief Marketing Officer

Mr. Hicks joined NBB in 2016 as the Chief Marketing Officer after more than 30 years of banking and marketing experience with Nat West, RBS and HSBC where he was part of the Global Marketing Team based in the London Head Office working across all business lines and geographies. His specialist areas are digital marketing, customer experience and digital transformation. He leads the marketing and communications team responsible for developing the NBB brand and supporting the business' goals through engaging marketing events and campaigns, targeted sponsorships and a sophisticated PR and communications strategy. He places customer insight and user experience at the heart of the Bank's initiatives with a growing focus on digital channels. He is a long-standing member of the Chartered Institute of Marketing. He has a BA (Hons) degree in Economics from De Montfort University in UK.

GABY EL HAKIM
General Counsel and Corporate Secretary

Mr. Gaby El Hakim joined NBB in 2017 as the General Counsel and Corporate Secretary. He previously worked with GFH Financial Group and BNP Paribas and has over 17 years of experience practicing law in areas including corporate and investment banking, Islamic finance, structured finance, capital markets, private equity, regulatory investigation and dispute resolutions. He is responsible for handling all legal matters and advising management and the Board with respect to all aspects of the business. Mr. El Hakim is the Vice Chairman of the Lawyer's Committee of ICC Bahrain, Chamber of Industry and Commerce, a member of ICC Paris Commission on Arbitration and ADR and serves as a board member of ICC Bahrain. He holds an LLM in Banking and Finance from Osgood Hall Law School, York University, Canada and an LLB (Licence en Droit Libanais) from Sagesse University School of Law, Beirut, Lebanon and several postgraduate qualifications.

HISHAM AL KURDI
Chief Executive – Corporate Institutions and Investment Banking

Mr. Hisham joined the Bank in 2017 as the Chief Executive – Corporate Institutions and Investment Banking, bringing to his role more than 21 years of local and international experience in capital markets and institutional coverage. In his past occupation, Mr. Hisham assumed the post of the Head of Capital Markets for the MEA region and was a member of the CIB regional board and executive committee. He holds a BEng Engineering in Systems Control from the University of Huddersfield, UK.

Bruce Wade
Chief Risk Officer

Yaser Alsharifi
Chief Strategy Officer

Richard Hicks
Chief Marketing Officer

Gaby El Hakim
General Counsel and Corporate Secretary

Iain Blacklaw
Chief Operating Officer

Statement of the Chief Executive Officer

"Visible progress has been achieved in terms of reorganisation of our business and support functions, aimed at serving our customers better and more comprehensively."

Jean-Christophe Durand
Chief Executive Officer

NET PROFITABILITY GROWTH

14.8%

This was achieved without compromising on risk management

OPERATING PROFIT GROWTH[1]

10.9%

Reflects the business development initiatives undertaken by the Bank

[1](before one-offs)

Last year was the first full year of the transformation journey undertaken by National Bank of Bahrain in order to bring it to a new level and to adapt to a fast-changing banking environment. We are pleased with the strong results achieved in a challenging economic environment and in a phase of changes. It is important to underline that the Bank has achieved these record net results without compromising on risk management and with a vastly reinforced infrastructure of controls and operations. Visible progress has been achieved in terms of reorganisation of our business and support functions, aimed at serving our customers better and more comprehensively, while offering them an enhanced range of products and services, and a better customer experience.

The 14.8% growth in net profitability for 2018, and even more importantly, the 10.9% growth in operating profits (before one-offs) reflects the business

Scan QR code to watch the CEO video.

development initiatives undertaken by the Bank, combined with a disciplined management of expenses and investments, and a well-controlled risk framework in line with the new strategy approved by the Board in 2017. The trend of the operating profits (before one-offs) shows a marked improvement of 10% compared to 5% on the historic long-term trend. From a financial strength perspective, NBB continues boasting a strong balance sheet with robust capital adequacy and liquidity ratios, ranking among the best along our regional peers.

In 2018, our teams have demonstrated a new mindset aiming at ensuring business sustainability across the activities of the Bank during this phase of growth. Each business line and support function within the organisation is focused on building a strong infrastructure at the level of the best industry standards and in line with the evolving regulatory requirements, capable of supporting the planned development of the institution. In particular, we aim to become the market benchmark in terms of compliance with regulations, corporate governance and risk management.

From a business standpoint, we have always asserted that our existing and future clients are the centre of our strategic efforts. We have also reaffirmed our strong commitment to the development of the local economy, which remains at the core of our strategy, and in which NBB has a very special role to play. These strategic directions are evident in a growing involvement with smaller companies, which constitute the backbone of the economy in the Kingdom; in our increasing role in local strategic projects financing such as power and oil; in our recent active involvement in raising debt for the Government and major local players on the international capital markets; and in the development of enhanced products and services for our retail clients.

These new developments are well-aligned with the Kingdom's 2030 vision and with our clients' evolving requirements. The National Bank of Bahrain is recognised as a pillar of the Kingdom's banking industry and it is our priority objective to further consolidate this position by providing an even broader range of services and solutions to serve all our clients better and become their bank of reference.

In 2018, NBB embarked on a digitilisation programme to make our clients' interaction with the Bank simpler and more efficient. This means being equipped with a modern and efficient platform to deliver our various products and services efficiently, simply and seamlessly. This demands a robust internal infrastructure, capable of supporting existing and ongoing development projects. Good progress has been made in 2018 in establishing that platform, with the provision of our online banking, mobile banking and an enhanced website. These initiatives will continue in 2019. The successful migration of clients to online banking is ongoing and will be accelerated. The aim is to cut down the amount of waiting and transaction time for customers, and to free up staff in the branches to serve our customers better. To achieve this objective, we are modernising and enhancing the technical features of the ATM network and expanding its footprint to remain the largest in the Kingdom.

Our human capital is fundamental to succeed in our vision and the Bank's transformation. Our commitment to continuous human capital development,

"In 2018, our teams have demonstrated a new mindset aiming at ensuring business sustainability across the activities of the Bank during this phase of growth".

to attracting the best talent, to grooming leaders from within, is a strategic priority of the management. Excellent, tangible results have been achieved in this respect and National Bank of Bahrain has become an employer of choice for Bahraini talents. At the same time, skills transfer from recent senior executive hires has been launched to ensure continuity and motivation. A comprehensive range of training programmes have been designed to enable and empower our personnel to excel in their various functions within the Bank. The amount of staff training time has been multiplied by 6 over 2 years. The vast majority of our recent hires are Bahraini talents, which confirms our position among the highest Bahrainisation rates in the industry. It is gratifying that the number of applications from high calibre and skilled talents has grown exponentially over the past year.

On behalf of the management team and the entire Bank staff, I would like to thank our Chairman and board members for their guidance, their availability and the unwavering support demonstrated throughout the year.

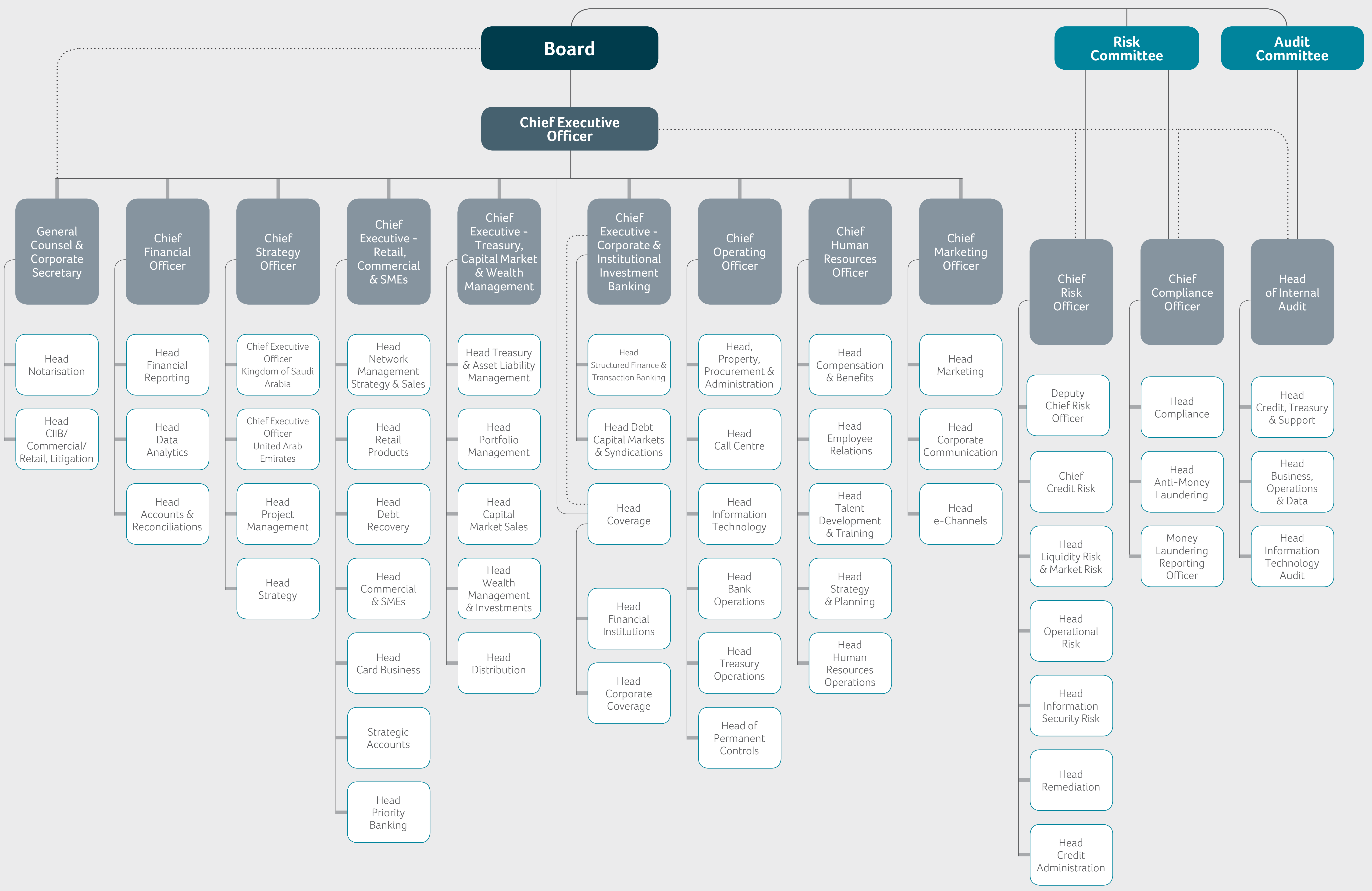
The year 2019 will certainly be another challenging year for the regional and local economies and the Banking industry in general. I strongly believe that National Bank of Bahrain is well placed to capitalise on its strengths, its committed and hard-working teams, its disciplined risk management, and its clear objectives to expand and strengthen its footprint in Bahrain and in the GCC, and to develop successfully new activities.

Jean-Christophe Durand
Chief Executive Officer

Your **National** Partner

Our human capital is fundamental to succeed in our vision and the Bank's transformation. Our commitment to continuous human capital development, to attracting the best talent, and the grooming of leaders from within, is a strategic priority of the management. Excellent, tangible results have been achieved in this respect and National Bank of Bahrain has become an employer of choice for Bahraini talent. At the same time, skills transfer from recent senior executive hires has been launched to ensure continuity and motivation. A comprehensive range of training programmes have been designed to enable and empower our personnel to excel in their various functions within the Bank. The vast majority of our recent hires are Bahraini talents, which confirms our position among the highest Bahrainisation rates in the industry. It is gratifying that the number of applications from high calibre and skilled talents has grown exponentially over the past year.

Organisation Structure



Human Resources and Talent Development

Human Resources and Talent Development at NBB is responsible for aligning strategic and business objectives with that of employees, management and shareholders. The function serves as a consultant to management on human resource-related issues whilst acting as an employee champion and change agent. It is through the understanding of NBB's strategy and needs that such knowhow translates practically and proactively into added value actions.

At NBB, we go beyond thoroughly knowing the business to understanding the dynamics through which we are able to position the business to succeed. By way of capability-building and efforts towards the creation of an aligned and sustainable culture, NBB has collectively formed its new identity.

That identity is facilitated through change championship, resulting in the ability to both initiate and sustain change at the individual, initiative, and institutional levels. As HR innovators and integrators, we design and deliver solution-focused HR practices using data to improve our decision-making.

Continuous growth and development is at the core of our belief. In order to be the leading financial institution locally and to be a significant regional player, our people must be given the opportunity to attain their highest potential and to continue to evolve with the dynamics of the industry in which we operate. With that in mind, training, development and talent management have been at the forefront of the HR activities for 2018. With great emphasis placed on regulatory and compliance-related training (constituting around 50% of all training initiatives attended for the year) we believe our employees are better equipped today to navigate in today's increasingly complex compliance environment. Amongst the various initiatives was a sanctions training provided by ICT – International Compliance Training after which 56 of our compliance and business employees received the ICA Certificate in Managing Sanctions Risk.

Innovation and creativity are believed to be the winning agents warranting leadership in the space of customer centric service and so, a training programme, 'Delivering Success in a Competitive World' , was launched across the Bank as a catalyst in support of this critical mindset.

As a practical stepping-stone towards enhancing real-world experience within a secure and challenging environment, NBB provided two simulation programmes to all its employees within branch retail banking and banking operations. This simulation method to training ensured a hands-on approach to learning whereby capabilities were enhanced in a pragmatic and practical way.

Every member of our team is believed to be a valuable contributor to this institution. With the encouraging support of Tamkeen, NBB was able to assist all its employees in exploring their leadership potential starting with self-leadership and ending with organisational influencers whose actions serve to position NBB in today's market. This was accomplished in 2018 through a bank-wide initiative that was customised to individuals' degree of influence in the organisation and rolled out across the year.

Advocates of entrepreneurship, at NBB we seek innovation and evolution. Stemming from this realisation, NBB fosters the entrepreneurial spirit within its philosophy to enable quick and dynamic transformation much required for the journey towards industry leadership. As a result, NBB has become an employer of choice for those who are creative and wish to explore means to ensure the successful positioning of this organisation as a National Champion and supporter of the local economy.

NBB is proud to be an official participant and sponsor of an employment onboarding programme which served to enrich its workforce with trained and professional employees with down syndrome. The sponsorship and onboarding programme took place in 2018 and involved the training and preparation of the new recruits, in addition to awareness sessions aimed towards enhancing our staff's knowledge of the potential sensitivities that could arise due to special needs requirements.

In addition, our training initiatives towards supporting our special needs clients extended to offering sign language training to all our retail customer-facing representatives. This has resulted in all our branches having the capability to serve those clients with ease and at an enhanced level of service.

< **Please flip over the page to see NBB organisation structure**

Your National Partner

Enhancing the digital experience

Developing our digital channel is a core focus for us, to add real benefits for our customers and making their everyday banking easier. Over the coming years, we will continue updating our digital offerings to allow our customers to bank in confidence, wherever they may be around the globe.

Registered Users

40,000+

Scan QR code to download the NBB mobile application from Google Play

Scan QR code to download the NBB mobile application from Apple store

Riyadh Yousif
Manager, Investment Advisory

Nada Hubeishi
Relationship Manager, Corporate Coverage

In pursuit of enriching the lives of generations by continuously enhancing our customer's experience, we launched our retail transformational strategy to challenge ourselves to bring best practice to every part of the Bank's business.

We have recognised the ever-increasing role of technology in the delivery of services to our customers. Hence, we have embarked on a three-year major investment programme in IT, aiming to replace our existing technologies and further raise the level of these services through more reliability and fewer systems issues.

To achieve our digital mandate, we have recognised that we have to start from within and therefore have begun deploying next generation solutions to automate internal processes and documentation.

The Bank has plans in place to remodel its branch systems, including deploying more self-service devices at each branch and better queue management technologies that will drive improvements to customer waiting times.

A comprehensive infrastructure modernisation programme is updating and upgrading all of our hardware. We have begun to migrate some of our non-customer systems onto the Cloud, in line with Bahrain's vision to be a Cloud first.

Significant investment in key banking systems is underway to support our branches to better serve our customers, for our business lines to more clearly understand our customers and their needs, and which will provide a greater level of security and control over customer data.

Other initiatives during the year include the roll out of Robotics applications; Straight Through Processing ('STP') capability for domestic and international payments; and the transfer from paper to electronic imaging for much of our customer service documentation.

Retail Banking

Our fundamental strategy of being 'Closer to you' has focused the energies of Retail Banking throughout 2018. We continued strengthening our infrastructure and expanding our conventional as well as our digital distribution footprint.

Retail Banking continued to consolidate its core segments and grew the asset book, despite the ever-present market competition and price pressure. For this purpose, new value proposition has been developed to introduce new products and services tailored towards the needs of the different segments of Bahrain society – to be launched in the near future.

In 2018, digital transformation strategy has been developed which will shape the future of retail banking offering, positioning NBB as the digital leader in Bahrain and one of the leaders in the region. This strategy envisions revamping all digital/ traditional channels of the Bank, offering state-of-the-art technology and serving the needs of the existing customer base as well as the growing segment of millennials in Bahrain's society.

We have concluded the design of the new branch service model to further expand the network presence in the Kingdom. This new model, to be implemented in the near future, offers an enhanced Retail Banking experience, with presence 'around the corner', from digital kiosks and branches to classic and flagship branches, offering a whole new experience and distinguished service/ sales flow.

The groundwork has been laid to introduce state of the art Interactive Teller Machines at flagship branches across our network. The extensive menu will give customers extended access to automated services such as higher limit cash deposits/ withdrawals, funds transfers, cheque deposit, utility bill payments, automated account opening, and requests for loans, cards and other products/ services.

Additionally, we have introduced a Meeter/ Greeter role in selected branches to facilitate the use of the alternative channels (i.e. ATMs, Internet banking, Mobile banking) by our customers. This role will continue to exist/ expand across our branch network going forward.

In our efforts to provide seamless customer experience at our branch network, a smart queue management system has been deployed with the ultimate goal of cutting customer waiting time in branches.

To be able to expand NBB's lending facilities to wider segments in Bahrain, the approved employer list has been expanded based on specific conditions to include more corporates/ multi-national organisations in Bahrain, supporting the local economy and expanding our customer reach.

Our ATM network continued to serve the Bank customers with enhanced features. In 2018, we replaced our ATM fleet with new models with increased functionality, which will continue in 2019. In addition, NBB is the first bank in Bahrain to deploy a mobile van with two ATMs aboard, which continues to be located at key events in the Kingdom.

Working with industry experts, we have been able to improve significantly the service to our call centre customers, thereby exceeding call centre service standards throughout the year. We introduced a new automated service with better menu options, as well as customer feedback surveys to measure customer satisfaction.

Commercial and SMEs

The Commercial and SME Banking department is an active player in the local economy through its distribution network across the country, specifically in areas with a strong foothold in the retail market.

During 2018, several initiatives were undertaken in order to bring us closer to our clients. A Middle Office function has been established to service daily customer needs, controls and monitoring, thereby allowing relationship managers to dedicate time to growing the business.

Business Online Banking was relaunched in April 2018 with enhanced features, enabling clients to conduct banking transactions to heighten their digital experience. The department initiated training sessions, educating customers and obtaining valuable user feedback.

Cash Deposit Machines ('CDMs') service for commercial clients is under implementation, which will provide banking convenience through access to instant credit with real time account viewing. We signed an exclusive partnership with one of the leading suppliers of cash management devices, to initiate the roll-out of cash deposit machines in major retail outlets where the cash is counted, automatically credited to our customer's account, then collected by our cash partner.

Plans for 2019 include departmental portfolio segmentation which is vital for growth and creation of expertise within different fields in order to ensure career growth from within. Given the requirements of the SME market and the challenges faced, the Bank will dedicate talent in this field to meet specific customer needs in an environment where transparency is a necessity. Aligning programme lending criteria to companies based on segments and their needs will be developed.

The department targets to achieve increased net income in 2019 by further expansion of its assets and liabilities.

Corporate and Institutional Investment Banking

Corporate and Institutional Investment Banking ('CIIB') is the natural evolution of NBB's business philosophy. The division was created to provide tailor-made solutions to large clients in Bahrain and the wider GCC. CIIB's founding principles revolve around service excellence and client centricity. With a combined experience and track record of several decades in regional and international markets, the CIIB team utilises its complementary skills to develop new products and services. We streamline and broaden the client experience through a newly introduced coverage model which focuses on our clients' needs.

Our aim is to remain close to our clients, ensuring that we understand their business. We will provide them with products and services which are relevant to their overall business objectives and market realities. While CIIB's main focus in 2018 was on building a solid infrastructure with systems and processes that can support sustainable growth, the team also made significant inroads with key clients in Bahrain, KSA, UAE and Oman. This resulted in NBB acting as arranger on strategic public mandates and high-profile transactions. The credibility gained through these transactions is already translating into new opportunities and more visibility.

In 2018, NBB financed key sectors of the domestic and GCC economies, ranging from utilities, oil and gas, health care, financial institutions and tourism, acting as a mandated lead arranger with anchor commitments on both structured finance and syndicated loan transactions. There has also been significant progress on the design of trade and cash solutions for our expanding client base.

The Bank prides itself in the tangible progress achieved by CIIB business lines, namely debt capital markets, structured finance, syndications and transaction banking.

Our keenness to align our transformational journey with the Kingdom's 2030 vision was evident in NBB's commitment to Bahrain's largest-ever project loan financing exercise. NBB also acted as a joint lead manager and/or coordinator on three international debt capital markets offerings. These milestones further cement NBB's position as a leading financing house in Bahrain and a recognised player in the GCC.

Our home market will always be our bedrock, ensuring that we play a lead role in the expansion and development of the local economy, but our horizon extends further to the region, with physical presence in the Kingdom of Saudi Arabia and the United Arab Emirates. CIIB will play an instrumental role in the way NBB is transforming, adding new dimensions in the capacity, complexity and value accretive business. In this manner, we will continue to serve our existing clients and pave the way for us to enter new markets and transact through new products.

Treasury, Capital Markets and Wealth Management

The strategy to maintain a high portion of the portfolio in floating rate notes has been justified as the Federal Reserve raised rates several times in 2018. This had a positive impact on the portfolio as the hedging strategy provided a cushion and strategically locked in our long-term funding in the rising rate environment.

Market timing strategies were utilised to take advantage of rates volatility, producing capital gains throughout the year. These strategies, coupled with high net interest income, resulted in above average returns for the year.

We anticipate diversifying and making the fixed income portfolio more dynamic. We see the evolution of the portfolio as integral to working with other new business lines to ensure the Bank's overall success.

In 2018, NBB strengthened its position in the interbank markets, working closely with local and regional counterparts in meeting requirements related to financial instruments denominated in Bahraini Dinars (BHD). In the foreign exchange market, NBB is regarded as the key bank locally, particularly during periods of increased interest and activity in the BHD. Compared to last year, the Bank more than doubled its interbank foreign exchange flows.

NBB will collaborate further with local counterparts by offering them bespoke treasury solutions to meet their needs. This will sustain NBB's position as the leading 'go-to' bank in Bahrain.

In our quest to convert NBB's motto, 'Closer to you', into reality, the unit embarked on a long-term transformation journey in terms of the various products and services crafted to cater to the various needs of our valued clientele. Together with the traditional foreign exchange and deposit flow activities, the team now offers derivatives and structured products and solutions, to address hedging and investment requirements.

The unit plays an important role in complementing the investment banking objectives of NBB in support of the bank's Debt Capital Markets and Syndications unit by distributing and marketing new bond issues to investors.

Your National Partner

Delivering service excellence

We are committed to understanding our customers and delivering what matters most to them through every stage of their financial journey.

Employees	Branches	ATMS
702	26	64

Ahmed Abdulghani
Head - Debt Capital Markets & Syndications

Maram Buallay
Manager - HR & Talent Development

Haitham Seyadi
Head - Property, Procurement & Administration

Razi Amin
Head - Information Technology

Zied Jalali
Head - Structured Finance & Transaction Banking

Financial Review

Overview

The Bank achieved a strong financial result and a record net profit for the year, generating an inflection point for the Bank results. The result was despite the tough external economic environment and internal transformational investments that were present throughout 2018. During the year, the Bank focused on further diversification of the asset and liability portfolios, augmenting the overall income by enhanced asset liability management whilst prudent risk management remained a core tenet. This resulted in the Bank recording a net profit of BHD 70.0 million for 2018, a double-digit increase of 14.8% over the previous year result of BHD 61.0 million.

At 2018 year-end, the total balance sheet stood at BHD 3,195.5 million compared to BHD 3,101.5 million as at the close of the previous financial year. The Bank has a well-diversified asset profile, with loans and advances representing 37.2% of total assets, the core remaining assets comprise of a sound liquidity base and include treasury bills at 12.1% of the total assets, placements with banks and other financial institutions representing 8.1%, and investment securities representing 35.4%. Customer deposits stood at BHD 2,190.6 million which represent 68.6% of total liabilities and equity, while shareholders' funds represent 14.9% of total liabilities and equity.

Key performance indicators continue to remain strong in relation to our regional peers and international benchmarks, with a return on average equity at 15.2% (2017: 14.1%) and a return on average assets of 2.2% (2017: 2.0%) for the year. Earnings per share improved from 44 fils in 2017 to 50 fils for 2018. The cost-to-income ratio at 35.6% compared favourably with the local and regional marketplace. The Bank continues to have a strong and stable capital adequacy ratio of 33.8% before the proposed appropriations calculated in accordance with Basel III guidelines as adopted by the Central Bank of Bahrain. Liquidity continues to be comfortable with the Bank being a net contributor of funds into the interbank markets throughout the year.

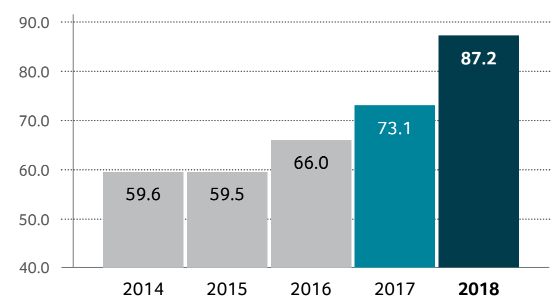
Net interest income

Net interest income for 2018 was BHD 87.2 million compared to BHD 73.1 million for 2017, reflecting a strong increase of 19.3%. The increase is attributable to positive volume and rate metrics within the loan portfolio due to active and effective internal management. Accordingly, the net interest income as a percentage of earning assets, improved to 2.9% in 2018 compared to 2.5% in 2017.

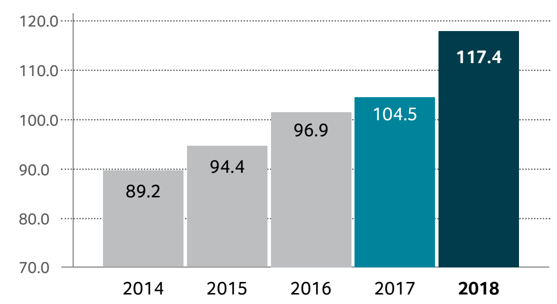
Other income

Other income recorded for the year was BHD 30.2 million compared to BHD 31.4 million recorded for the previous year. Excluding the exception income of BHD 3.3 million recorded in 2017, other income increased by 7.5%. The increase, therefore, represents an improvement in the

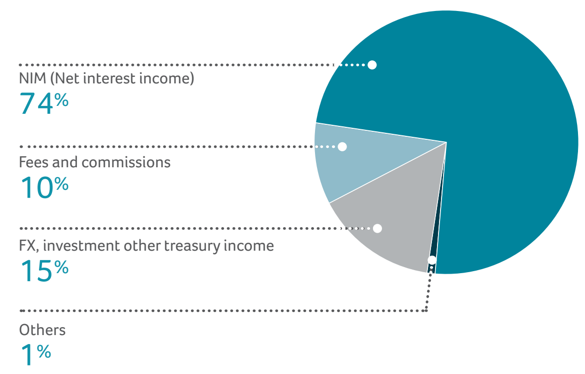
Net interest income
(BHD millions)



Total operating income
(BHD millions)



Composition of total income (%)



Bank's fundamentals rather than due to receipt of exceptional or one-off income. In line with a business diversification strategy, the fee based core banking activities represented a quarter of total income. Details of other income, with comparative figures for the previous year, are set out in note 24 of the financial statements.

Operating expenses

Operating expenses at BHD 41.8 million represented an increase of 26.7% over the previous year, reflecting the investment in people, processes and digital infrastructure required to maintain the Bank's competitive advantage of being closer to our customers whether they be within Bahrain or in the wider region. Despite the cost of the strategic investments, an element of which will reduce future expenses or contribute to increases in the future revenue opportunities, the Bank's cost-to-income ratio was contained at a low 35.6%.

Provisions

Year 2018 represents the first year since the Bank adopted International Financial Reporting Standard (IFRS) 9 on financial instruments. The new international standard, endorsed by the Central Bank of Bahrain, amended the accounting treatment of financial assets and financial liabilities, and provided a new framework for assessing the adequacy of impairment provisions for financial assets including loans and advances and off-balance sheet facilities. Provisions for individually impaired credit exposures continue to be determined by discounting expected future cash flows. However, impairment charges on the wider portfolio of financial assets which are not individually identified as impaired is now a forward-looking calculation and is established based on various factors. These factors include internal risk ratings, historical default rates adjusted considering multiple scenarios of the future macroeconomic outlook, loss ratios given an event of default, and rating migrations. Based on the ongoing assessment of the provision requirement, an amount of BHD 5.6 million was provided towards impairment during the year compared to BHD 10.5 million in 2017. Further disclosure on the impact of the accounting change is presented in note 2 of the financial statements.

Loans are classified as part of the non-performing portfolio upon an impairment event. Based on the Central Bank of Bahrain regulations, such assets will remain classified as non-performing for a one-year cure period even after the underlying facility becomes fully performing. The non-performing loan portfolio (excluding the cure period assets) of BHD 47.8 million at the end of 2018 compared to BHD 87.8 million at the end of 2017. Details of the Bank's non-performing loans, provisions and movements therein during the year are detailed in note 7 of the financial statements.

Assets

Total assets stood at BHD 3,195.5 million as at 31 December 2018, compared to BHD 3,101.5 million as at 31 December 2017. Total earning assets stood at BHD 3,020.7 million as at 31 December 2017 compared to BHD 2,939.7 million as at the previous year-end. The Bank has a well-diversified asset profile with loans and advances representing 37.2% of the total assets, while treasury bills represent 12.1%, placements with banks and other financial institutions represent 8.1%; investment securities represent 35.4% of total assets.

The loan portfolio is diversified with widespread participation in the domestic market with a constant broadening of business relationships in Bahrain and the wider region. At the year-end, the Bank's investment portfolio of BHD 1,132.2 million (2017: BHD 1,067.3 million) consisted mainly of debt securities. A major part of the debt securities comprised Government of Bahrain bonds and Islamic sukuk.

Note 29 to the financial statements provide details of the distribution of total assets by geographical region and industry.

Liabilities

Customer deposits at the year-end stood at BHD 2,190.6 million compared to BHD 2,165.2 million at the end of 2017. The Bank continues to be successful in generating core customer deposits resulting from its 'Closer to you' brand promise which entails rich product offerings, superior service and a dominant position in the domestic market. The Bank is also recognised as being the national bank, a rich pedigree that signifies the highest levels of safety and soundness of any financial services institution in the Kingdom of Bahrain.

Borrowings under repurchase agreements and due to banks and financial institutions stood at BHD 485.3 million as at 31 December 2018, compared to BHD 451.8 million at the 2017 year-end. Customer deposits continue to be the major source of funding with the ratio of customer deposits to total liabilities raising to 80.5% at the year-end, and represented the funding source for 94.3% of the combined loan and investment portfolios.

Capital strength

Shareholders' equity, inclusive of the proposed appropriations, reflected a balance of BHD 475.8 million as at the year-end, compared to BHD 447.9 million as at the close of the previous financial year. At the year-end, shareholders' equity as a percentage of total assets was 14.9%. The Bank's capital adequacy ratio as at 31 December 2018 was 33.8% with the common equity tier 1 ('CET 1') ratio at 32.8% before the proposed appropriations. The ratios have been calculated in accordance with the Basel III regulations as adopted by the Central Bank of Bahrain. The Bank's capital adequacy ratio is significantly above both the Basel Committee's requirement for internationally active banks and above the minimum level of 12.5% set by the Central Bank of Bahrain. The main factors that contribute to the Bank's strong capital adequacy ratio are the high capital base, prudent risk management practices and a low risk profile of on-balance sheet and off-balance sheet exposures. The Bank's profile includes significant exposures to low risk asset classes such as sovereigns, public sector undertakings and prime banks and financial institutions. Note 41 to the financial statements and the risk and capital management disclosures provide further details on the Bank's capital strengths.

Risk Management

Risk management has been further strengthened in 2018. During the year, we have appointed a very strong Bahraini team with new department heads for liquidity risk , market risk and operational risk. With these new appointments, we have added a wealth of knowledge and experience.

The financial sector continues to grow in complexity and sophistication with ongoing changes in the regulatory and operating environments globally. Moreover, advances and developments on the technological front are introducing new challenges and opportunities for banks. With this dynamic environment comes a growing need to continue to strengthen existing frameworks and bolster controls. NBB has over the years developed risk management into a core competence and remains well positioned to meet these challenges. The Bank evaluates risk in terms of the impact on income and asset values. The evaluation reflects the Bank's assessment of the potential impact on its business on account of changes in political, economic and market conditions and in the credit worthiness of its clients. Risk management at NBB has always been prudent and proactive with the objective of achieving the optimum balance between risk and expected returns.

The overall authority for risk management in the Bank is vested in the Board of Directors and a Board Risk Committee at Board level has been established to provide oversight and advice to the Board of Directors. The Board authorises appropriate credit, operational, liquidity, market and information security risk policies based on the recommendation of management. Approval authorities are delegated in the hierarchy depending on the amount, type of risk and collateral security. Moreover, the Bank has established an Operational Risk Management Committee ('ORMC'), Asset Liability Committee ('ALCO') and Information Security Committee ('ISC') to address different areas of risk.

Integral to the Bank's risk management system is the internal audit department that plays a role in evaluating the independence and overall effectiveness of the Bank's risk management functions. A periodic review of risk assets is conducted by the department to confirm that established policies, procedures and approved terms are complied with, to review asset quality and highlight areas of concern so that corrective action can be taken in time.

The Bank's risk management process encompasses the various dimensions of risk as follows:

Credit risk

We actively strive to manage risk to protect and enable the business.

NBB has maintained a conservative and consistent approach to risk since its inception, helping to ensure we protect customers' funds, lend responsibly and support the local economy. The team at credit risk works carefully to ensure the alignment between our credit risk appetite and vision calls of our new corporate strategy.

With regulatory and market pressures driving the industry to heightened risk controls and wise use of capital, the team continues to undertake more scrutiny in detailed reviews of our portfolios and are proactively assessing clients and sectors likely to come under stress, taking corrective risk management action plans when necessary.

An internal grading system and review process ensures prompt identification of any deterioration in credit risk and consequent implementation of corrective action. The Bank's internal ratings are based on a 16-point scale that takes into account the financial strength of a borrower as well as qualitative aspects, to arrive at a comprehensive snapshot of the risk of default associated with the borrower. Risk ratings assigned to each borrower are reviewed at least on an annual basis. Regular monitoring of the portfolio enables the Bank to exit accounts that evidence deterioration in risk profile.

The Bank follows stringent criteria in setting credit limits for countries and financial institutions. Prudent norms have also been implemented to govern the Bank's investment activities. Not only are regular appraisals conducted to judge the credit worthiness of the counterparty but day-to-day monitoring of financial developments across the globe ensures timely identification of any event affecting the risk profile.

The Bank has systems and procedures in place to generate alerts in case of past dues in any account. A stringent classification process is followed for all accounts with past dues. The Bank applies rigorous standards for provisioning and monitoring of non-performing loans.

Legal risk

The Legal Department manages and mitigates the legal risks of the Bank through prompt review and advice on transaction documents and generally advises the Bank's various departments regular review of standard documentation to ensure the Bank's interests are protected. Furthermore, they negotiate with counterparties/lawyers, keep abreast of latest developments in domestic and international banking laws, as well as corporate and other laws and regulations, and initiate corrective action when the Bank's business is likely to be affected. In-house expertise independently ensures the above objectives are properly maintained.

In addition, firms of international repute have been retained by the Bank to advise on local and foreign law related matters and represent the Bank in legal proceedings before local and foreign legal authorities as and when such representation is required.

Liquidity and market risk

Liquidity risk is classified as the potential inability of the Bank to meet its financial obligations on account of a maturity mismatch between assets and liabilities. Liquidity risk management ensures that funds are available at all times to meet the funding requirements of the Bank.

The asset/liabilities management of the Bank ensures various liquidity criteria that need to be complied with, such as minimum level of liquid assets, gap limits, ratio of liquid assets to total assets, etc.

The Bank's ability to maintain a stable liquidity profile is primarily on account of its success in retaining and growing its customer deposit base. The strategy of the Bank has ensured a balanced mix of demand and time deposits.

The Bank's goal is to achieve stable earnings growth through active management of the assets and liabilities mix while selectively positioning itself to benefit from near term changes in interest rate levels.

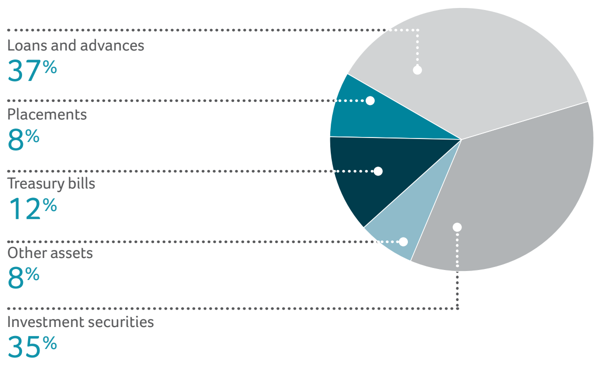
The Head of Treasury and ALM is primarily responsible for managing interest rate risk. Reports on overall positions and risks are submitted to senior management for review and positions are adjusted if deemed necessary. In addition, ALCO regularly reviews the interest rate sensitivity profile and its impact on earnings. Strategic decisions are made with the objective of producing a strong and stable interest income over time.

Market risk is classified as the risk to the value of the trading portfolio arising from changes in interest rates, foreign exchange, commodity and equity prices. The Bank's trading activities are governed by conservative policies, stringent adherence to controls and limits, strict segregation of front and back office duties, regular reporting of positions, regular independent review of all controls and limits and rigorous testing of pricing, trading and risk management systems.

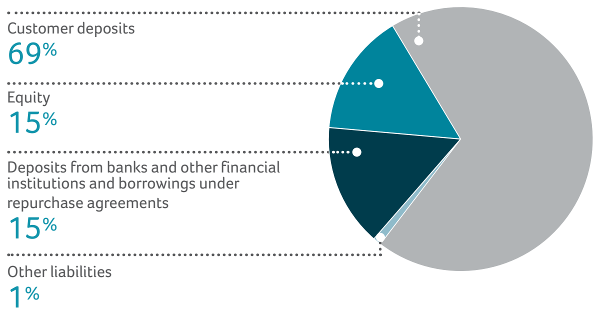
The limits are set annually and regularly reviewed. Quality and rating are the main criteria in selecting a trading asset.

The Bank uses the standardised method to calculate capital charge for market risk, the capital that is required to be held on account of the various risk factors affecting the trading book and currency positions. Capital requirement on

Composition of total assets
(%)



Composition of total liabilities and equity
(%)



account of interest rate risk, foreign exchange risk, equity risk, commodity risk and options risk are calculated separately and then summed up to arrive at the total market risk capital requirement of the Bank.

Operational risk

Operational risk is the risk to achieving our strategy or objectives as a result of inadequate or failed internal processes, people and systems or from external events. Operational risk arises from day-to-day operations or external events and is relevant to every aspect of our business.

Operational risk is:

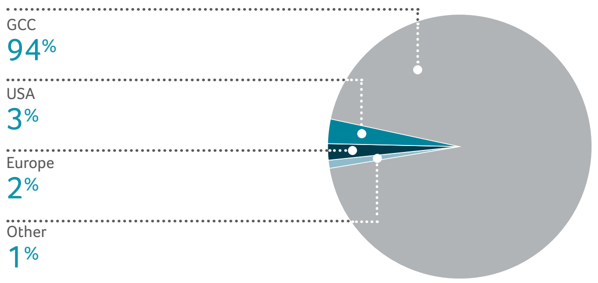
- Measured using the risk and control assessment process, which assesses the level of risk and the effectiveness of controls, and measured for capital management using risk event losses;
- Monitored using key risk indicators and other internal control activities; and
- Managed primarily by business and functional managers who identify and assess risks, implement controls to manage them and monitor the effectiveness of these controls using the operational risk management framework.

The objective of our operational risk management framework ('ORMF') is to manage and control operational risk in a cost-effective manner within targeted levels of operational risk consistent with our risk appetite.

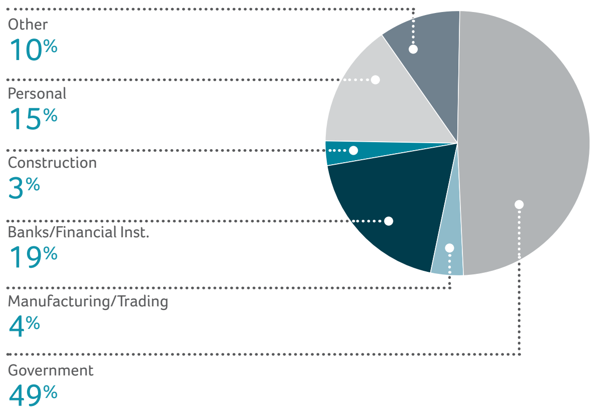
We have a dedicated Operational Risk Management Department ('ORMD') within our Risk Group Division. It is responsible for leading the embedding of the ORMF and assuring adherence to associated policies and processes across the first and second lines of defence. It supports the Chief Risk Officer and the Operational Risk Management Committee ('ORMC'), which meets on a monthly basis to discuss key risk issues and review the implementation of the ORMF.

Heads of departments and functions throughout the Bank are responsible for maintaining an acceptable level of internal control commensurate with the scale and nature of operations, and for identifying and assessing risks, designing controls and monitoring the effectiveness of these controls.

Geographical distribution of assets
(%)



Sector distribution of assets
(%)



In 2018 we continued our ongoing work to strengthen those controls that manage our most material risks. Among other measures, we are:

- Further developing controls to help ensure that we know our customers, ask the right questions, monitor transactions and escalate concerns to detect, prevent and deter fraud risk;
- Improving controls and security to protect customers when using digital channels;
- Increasing monitoring and enhancing detective controls to manage those fraud risks which arise from new technologies and new ways of banking.

Information security risk

Information security risk is the risk associated with the operation and use of information systems that support the mission and business functions of the Bank. It is defined as a function of the likelihood of a given threat-source's exercising (accidentally triggering or intentionally exploiting) a particular potential vulnerability, and the resulting impact of that adverse event on the organisation.

The Bank is implementing an Information Security Management System ('ISMS') Framework of policies and procedures, based on the ISO/IEC 27000:2018 family of standards that includes all legal, physical and technical controls involved in the organisation's information risk management processes. It is a systematic approach to managing sensitive company information so that it remains secure, by including people, processes and technology. The strategic objective is to adopt a risk based approach (Plan – Do – Check – Act) by integrating the information security risk management processes into the life cycle of all information systems and infrastructures, thus mitigating and minimising the risk to an acceptable level.

The department is also responsible for all information and cyber security activities across NBB including security event monitoring, monitoring of compliance with information security regulations, policies, standards and procedures, overseeing the investigation of information security incidents and gathering and analysing threat intelligence from internal and external sources. Information security risk assessments and reviews are also a core activity of the team as well as proactively supporting other functions on information security, defining and conducting the information security awareness programmes and measuring and reporting the information security KRIs and KPIs.

Reputation and fiduciary risk

Reputation risk is defined as the current and prospective impact on earnings and capital arising from negative public opinion that would impact the ability to establish new relationships or services or to continue servicing existing relationships. Management of reputation risk is an inherent feature of the Bank's corporate culture which is embedded as an integral part of the internal control systems. Besides identification and management of risks, the internal control system also incorporates as an ethos the maintenance of business practices of the highest quality towards its customers, shareholders, regulators, general public and fiduciary/ non-fiduciary clients. Through its policies and practices, NBB ensures that proper screening of clients' risk profiles and performance expectations are conducted prior to making investment products or services available to them.

All the aspects of risk mentioned above are reviewed regularly at meetings of the Board of Directors, the Executive Committee and Board Risk Committee based on a comprehensive risk report. This integrated approach to risk management also serves the Bank in achieving its objective of protecting the interests of shareholders and customers.

Regulatory compliance and financial crime risks

Promotion of a healthy compliance culture lies at the heart of NBB's strategy. The Bank has accordingly been focused on developing a sound framework which oversees adherence to the codes, rules, regulations and standards of the Kingdom of Bahrain, as well as other countries where it has operations.

The compliance department's key responsibilities include managing financial crime compliance. To this effect, a risk based approach has been implemented to address Know Your Client ('KYC') requirements, sanctions monitoring, and anti-money laundering and counter terrorism financing measures.

During 2018, NBB has invested in new system technology to enhance its transaction monitoring capabilities coupled with a strengthening of the compliance department resources. Furthermore, the Bank has increased its efforts with a major KYC programme kicking off in 2018, due to be complete in 2019.

The Bank also monitors the regulatory compliance risk by integrating the feedback and judgement of the first line of defence risk and control assessments vis-a-vis the results of the activities of the second line of defence functions. Appropriate policies and procedures and training programmes have been established for all of our employees in this area to ensure that both detective and preventive controls are followed at all times.

Your National Partner

Fostering our local communities

At NBB we believe that corporate social responsibility goes further than simply serving our customers banking needs. Involvement in the welfare of the families in the communities where we serve is of utmost importance.

Since

1980

Total allocation

BHD 49.2 million

Scan QR code to watch the Ramadan #ShareToCareBH video

Donations and Contributions

Since NBB's establishment in January 1957, the Bank has strived to remain at the heart of the community and has taken the community to heart. Several decades on, our commitment to supporting the Kingdom's social welfare and contributing to the betterment of the lives of its citizens continues undiminished. It is both our duty and our privilege to be serving the community beyond the banking and financial services we provide.

In line with the Bank's Donations and Contributions policy, each year NBB allocates 5% of the Bank's net annual profit in support of our social endeavours. These include programmes and foundations/ projects which are aimed at promoting social welfare, health care and education. This principle dates back to 1980 when the Bank's Donations and Contributions Programme was formalised. The Bank has allocated BHD 49.2 million since the inception of the Donations and Contributions Programme.

Our Commitments:

I. Education

Our commitment to education comprises of donations that provide support to all educational initiatives which have a direct impact on the community. These include the Crown Prince Scholarship Programme for students plus donations and contributions to schools, colleges, universities and other educational establishments.

II. Health care

Our support to the health sector comprises of donations which actively contribute to the betterment of our society in terms of health and well-being. These include direct donations and contributions to hospitals, medical centres, registered organisations and health service providers as well as for the provision of equipment and active participation in awareness campaigns.

III. Social welfare

Our dedication towards social welfare comprises of donations to associations and social and philanthropic organisations to help support activities that aim at achieving substantial social benefits for specific sectors, segments as well as the public at large. Our support extends to special programmes which specifically target disadvantaged and challenged sections of our society. All with the aim of helping to develop a better and more cohesive community.

Scan QR code to watch the visit to NBB's Rehabilitation Home for Disabled Children

IV. Development programmes

Our commitment to development programmes comprises of all initiatives and activities that place a focus on Bahrain. These include support for professional associations and specialised conferences and events focused on specific areas of strategic importance to the Kingdom.

V. Others

This category includes all other donations and contributions which are considered justified by the Donations and Contributions Committee in line with contributions towards the advancement of the Kingdom.

Scan QR code to watch the visit to NBB's Elderly Home in Eid Al Fitr

The Board of Directors is responsible for the overall governance of National Bank of Bahrain. The Board ensures that high ethical standards are established across the Bank and regularly reviews the Bank's compliance with the Central Bank of Bahrain ('CBB') regulations regarding corporate governance. The Board recognises that good corporate governance is a vital ingredient in the creation of sustainable shareholder value and protecting the interests of all stakeholders.

Maintaining the best standards of corporate governance has provided the Bank's customers, counterparties, shareholders, regulators, employees and rating agencies with a high degree of confidence in our institution; achieved an appropriate balance between long-term growth and short-term objectives; created a sound portfolio of assets, a stable customer base, income diversity as well as the ability and resources to face economic cycles and uncertainties. The Board has set the moral tone for the Bank with a high degree of intolerance for any instances of malpractice, fraud and unethical behaviour and ensured the highest degree of adherence to laws, rules and regulations.

Board of Directors:

The Board's composition is governed by the Bank's Memorandum and Articles of Association and comprises of eleven members. Four members of the Board of Directors are appointed by Bahrain Mumtalakat Holding Company, which holds 44.18% of the Bank's share capital and one member by Social Insurance Organisation, which holds 10.88% of the Bank's share capital. The remaining six members of the Board of Directors are elected by secret ballot at the ordinary general meeting of the shareholders, by a simple majority of valid votes. The five members of the Board of Directors appointed by the shareholders remain in office for a term not exceeding three years, which may be renewed. In order to be eligible for being nominated for directorship, the individuals concerned should meet the 'fit and proper' criteria established by the Central Bank of Bahrain and their appointment is subject to prior approval by the Central Bank of Bahrain. The present Board of Directors was elected at the Annual General Meeting in 2018 and their term expires at the Annual General Meeting to be held in 2021.

On joining NBB's Board, all Directors are provided with a "Directors' Kit" which includes the Bank's Memorandum and Articles of Association, key policies, terms of reference of the Board and its sub-committees and Corporate Governance guidelines. Induction sessions are also held with the Chairman and Chief Executive Officer which focuses on business profile, opportunities, challenges and risks faced by the Bank.

In accordance with the definitions stipulated by the CBB, Directors are categorised as independent, executive and non-executive. The Board currently comprises of five independent directors and six non-executive directors. The roles of the Chairman and the Chief Executive Officer are separate and exercised by different persons.

The Board's primary responsibility is to deliver sustainable value to all stakeholders by charting the strategic direction of the Bank as well as setting the risk appetite and the overall capital structure of the Bank. The Board is also responsible for monitoring Management's running of the business within the agreed framework. The Board seeks to ensure that the Management strikes an appropriate balance between long-term growth and the short-term objectives. The Board is ultimately accountable and responsible for the affairs and performance of the Bank. Accordingly, the main functions of the Board are:

- Maintain an appropriate board structure.
- Maintain an appropriate management and organisation structure in line with the Bank's business requirements.
- Plan the strategic future of the Bank, approve annual business plans, approve and monitor major initiatives.
- Monitor the operations framework of the Bank and the integrity of internal controls.
- Ensure compliance with laws and regulations.
- Monitor the Bank's performance and approve financial results, ensure transparency and integrity in stakeholders reporting including financial statements.
- Evaluate periodically the Board's own performance including that of Board sub-committees.
- Assure equitable treatment of all shareholders including minority shareholders.

The Chairman is mainly responsible for the leadership of the Board, ensuring that it operates effectively and fully discharges its legal and regulatory responsibilities.

The Board of Directors meets regularly throughout the year and maintains full and effective control over strategic, financial, operational, internal control and compliance issues. As per its terms of reference, the Board shall meet at least once every calendar quarter.

In its role as the primary governing body, the Board of Directors provides oversight for the Bank's affairs and constantly strives to improve and build on the Bank's strong corporate governance practices. The business performance of the Bank is reported regularly to the Board of Directors. Performance trends as well as performance against budget and prior periods are closely monitored. Financial information is prepared using appropriate accounting policies, in accordance with International Financial Reporting Standards as promulgated by the International Accounting Standards Board and are consistently applied. Operational procedures and controls have been established to facilitate complete, accurate and timely processing of transactions and the safeguarding of assets.

The Board of Directors has unlimited authority within the overall regulatory framework. The Board has delegated approval authorities to its sub-committees and members of Management; all transactions falling outside the delegated limits are referred to the Board for approval. In addition, the Board approves on a yearly basis the annual budget and operating limits for various activities of the Bank.

Committee of the Board of Directors:

The Board has set up several sub-committees which provide effective support to the Board in carrying out its responsibilities. These include the Executive Committee, the Audit Committee, the Donations and Contributions Committee, the Risk Committee, and the Nomination and Remuneration Committee.

Executive Committee:

The Executive Committee comprises of five Board members selected and appointed by the Board, with at least two of the members being independent directors and three of the members being Non-executive. The Executive Committee meets at least six times a year. The role of the Executive Committee is to assist the Board of Directors in fulfilling its responsibilities with regard to lending and investment, as well as any other matters not delegated to a specific Board Committee. Accordingly, the Executive Committee is empowered to approve specific credit and investment proposals, review budgets, plans and major initiatives for eventual submission to the Board for approval, and to monitor the Bank's performance against business plan objectives.

Audit Committee:

The Audit Committee comprises of three Board members selected and appointed by the Board, two of which are independent directors and one non-executive Director. The Audit Committee meets at least four times a year. The primary function of the Audit Committee is to reinforce the internal and external audit process and assist the Board in fulfilling its responsibility in ensuring an effective system of internal control and risk management. In addition, the Audit Committee is also responsible for reviewing and recommending changes to the Bank's corporate governance policy framework based on regulatory requirements or industry best practices. The Audit Committee is responsible for recommending to the Board, the appointment and compensation of the external auditors, reviewing the integrity of the Bank's financial reporting, reviewing the activities and performance of the internal audit function and reviewing compliance with relevant laws, regulations and code of conduct.

The Audit Committee is supported by the Internal Audit Department, which regularly monitors the system of internal controls. Monitoring includes an assessment of the risks and controls in each operating unit and matters arising there from are reported to the Audit Committee on a regular basis.

Donations and Contributions Committee:

The Donations and Contributions Committee consists of a maximum of four Board members and two management members as decided by the Board of Directors. It was is established to manage the affairs of the Donations and Contributions Programme and to decide on all contributions to philanthropic and social activities which generate substantial benefits and returns to the largest segment of the community. The allocated annual budget of the committee equals to 5% of the Bank's annual net profit.

Risk Committee:

The Risk Committee comprises of four members selected and appointed by the Board. It includes two directors one of which is an independent Director, one non-executive Director and two independent advisors to the Board. The Risk Committee meets at least four times a year. The role of the Committee is to identify and monitor risks within the framework of the risk appetite established by the Board of Directors including reviewing and reporting its conclusions and recommendations to the Board on the Bank's current and future risk appetite, the Bank's risk management framework and the Bank's risk culture.

Nomination and Remuneration Committee:

The Nomination and Remuneration Committee is comprised of four Board members selected and appointed by the Board, one of which is an independent Director and three non-executive Directors. The Nomination and Remuneration Committee meets at least twice a year. The role of the Nomination and Remuneration Committee is to assist the Board in fulfilling its responsibilities with regard to the nomination and remuneration policy of the Bank. The Nomination and Remuneration Committee has the mandate for identifying persons qualified to become members of the Board, CEO, CFO, corporate secretary, and any other officers positions as considered appropriate by the Board and recommending them to the Board. The Committee also has the responsibility of reviewing and recommending the remuneration policies for the Board of Directors and senior management.

Board meetings and attendance:

The Board of Directors and the sub-committees of the Board meet regularly to effectively discharge their responsibilities. For meeting the requirements of the Corporate Governance Code and the CBB Rulebook, the Bank considers attendance of Directors at Board and sub-committee meetings. A summary of the Board meetings and sub-committee meetings held during the year 2018 and attendance are detailed below:

	Board		Executive Committee		Audit Committee		Risk Committee		Nomination and Remuneration Committee		Total		
Name of the Director	Total No of meetings	Meetings attended	Total No of meetings	Meetings attended	Total No of meetings	Meetings attended	Total No of meetings	Meetings attended	Total No of meetings	Meetings attended	Total No of meetings	Meetings attended	% of Meetings attended
Farouk Yousuf Khalil Almoayyed Chairman	8	8							6	6	14	14	100%
Dr. Essam Abdulla Fakhro Deputy Chairman	7	7	4	4					6	6	17	17	100%
Fawzi Ahmed Kanoo Deputy Chairman	8	7	4	4							12	11	92%
Khalid Yousif Abdul Rahman Director	7	7			6	6					13	13	100%
Hussain Sultan Al Ghanem Director	8	8	3	3	2	2					13	13	100%
Khalid Omar Al Romaihi Director	8	7					3	3			11	10	90%
Sh. Rashid Bin Salman Al Khalifa Director	7	7	4	4					4	4	15	15	100%
Hala Ali Hussain Yateem Director	6	6			4	4					10	10	100%
Rishi Kapoor Director	6	6					3	3			9	9	100%
Mohamed Tareq Mohamed Sadeq Mohamed Akbar Director	6	6			4	4					10	10	100%
Yusuf Abdulla Yusuf Akbar Alireza Director	6	6	3	3					4	4	13	13	100%
Abdulla Yousif Akbar Alireza Deputy Chairman	2	2			2	2	Left the Board				4	4	100%
Ali Hussain Yateem Director	2	2	1	1			Left the Board				3	3	100%
Mir Zulfekar Ali Director	2	1	1	1			Left the Board				3	2	66%

Dates of meetings and attendance details:

Board Meetings: Total number of meetings held: 8

	Meeting dates							
Members	29/1/2018	07/3/2018	7/3/2018	2/5/2018	18/7/2018	17/10/2018	7/11/2018 (Ad-hoc)	21/11/2018
Farouk Yousuf Khalil Almoayyed - Chairman	✓	✓	✓	✓	✓	✓	✓	✓
Dr. Essam A Fakhro - Deputy Chairman	✓	✓	✓	✓	✓	✓	Conflict of interest	✓
Fawzi Ahmed Kanoo - Deputy Chairman	✓	✓	✓	✓	×	✓	✓	✓
Khalid Yousif Abdul Rahman - Director	✓	✓	✓	✓	✓	✓	Conflict of interest	✓
Hussain Sultan Al Ghanem - Director	✓	✓	✓	✓	✓	✓	✓	✓
Khalid Omar Al Romaihi - Director	✓	×	✓	✓	✓	✓	✓	✓
Sh. Rashid Bin Salman Al Khalifa - Director	✓	✓	✓	✓	✓	✓	Conflict of interest	✓
Hala Ali Hussain Yateem - Director	Not in Board		✓	✓	✓	✓	✓	✓
Rishi Kapoor - Director	Not in Board		✓	✓*	✓	✓*	✓	✓
Mohamed Tareq Mohamed Sadeq Mohamed Akbar - Director	Not in Board		✓	✓	✓	✓	✓	✓
Yusuf Abdulla Yusuf Akbar Alireza - Director	Not in Board		✓	✓	✓*	✓	✓	✓
Abdulla Yousif Akbar Alireza - Deputy Chairman	✓	✓	Left the Board					
Ali Hussain Yateem - Director	✓	✓	Left the Board					
Mir Zulfekar Ali - Director	×	✓	Left the Board					

* Attended by phone

Executive Committee Meetings: Total number of meetings held: 4

	Meeting dates			
Members	14/2/2018	16/5/2018	26/9/2018	11/12/2018
Dr. Essam Abdulla Fakhro - Deputy Chairman and Chairman of Executive Committee	✓	✓	✓	✓
Fawzi Ahmed Kanoo - Deputy Chairman	✓*	✓	✓	✓*
Hussain Sultan Al Ghanem - Director	Not a Member	✓	✓	✓
Sh. Rashid Bin Salman Al Khalifa - Director	✓	✓	✓	✓
Yusuf Abdulla Yusuf Akbar Alireza - Director	Not a Member	✓	✓	✓*
Ali Hussain Yateem - Director	✓	Left the Board		
Mir Zulfekar Ali - Director	✓	Left the Board		

* Attended by phone

Audit Committee Meetings: Total number of meetings held: 6

	Meeting dates					
Members	17/1/2018	8/2/2018	29/4/2018	17/7/2018	16/10/2018	4/12/2018
Khalid Yousif Abdul Rahman - Director and Chairman of Audit Committee	✓	✓	✓	✓	✓	✓
Hala Ali Hussain Yateem - Director	Not a Member		✓	✓	✓	✓
Mohamed Tareq Mohamed Sadeq Mohamed Akbar - Director	Not a Member		✓	✓	✓	✓
Abdulla Yousif Akbar Alireza - Deputy Chairman	✓	✓	Left the Board			
Hussain Sultan Al Ghanem - Director	✓	✓	Left the Audit Committee			

Risk Committee Meetings: Total number of meetings held: 3

	Meeting dates		
Members	30/5/2018	12/9/2018	29/11/2018
Khalid Omar Al Romaihi, Director and Chairman of Risk Committee	✓	✓	✓
Rishi Kapoor, Director	✓	✓	✓
Sabah Al Moayyad, Non-Director – Advisor to the Board	✓	✓	✓
Matthew Deakins, Non-Director – Advisor to the Board	✓	✓	✓

Nomination and Remuneration Committee Meetings: Total number of meetings held: 6

	Meeting dates					
Members	28/1/2018	14/2/2018	2/5/2018	18/7/2018	17/10/2018	21/11/2018
Farouk Yousuf Khalil Almoayyed - Chairman of the Board and Chairman of Nomination and Remuneration Committee	✓	✓	✓	✓	✓	✓
Dr. Essam Abdulla Fakhro - Deputy Chairman	✓	✓	✓	✓	✓	✓
Sh. Rashed Bin Salman Al Khalifa - Director	Not a Member		✓	✓	✓	✓
Yusuf Abdulla Ali Reza -Director	Not a Member		✓	✓	✓	✓
Abdulla Yousif Akbar Alireza - Deputy Chairman	✓	✓	Left the Board			
Ali Hussain Yateem - Director	✓	✓	Left the Board			

Management structure:

The management structure that clearly defines roles, responsibilities and reporting lines, is availabe on page 20 of this annual report. Within the management structure there are separate committees responsible to meet on a regular basis to discuss and decide on the various strategic and tactical issues within their respective areas.

Committee Name	Members	Objective
1- Management Committee ('MANCO')	1- Jean Christophe Durand – Chief Executive Officer **(Chairman)** 2- Abdulaziz Al Ahmed – Chief Executive, Retail, Commercial and SMEs 3- Hussain Al Hussaini – Chief Executive, Treasury Capital Markets and Wealth Management 4- Dana Buheji – Chief Human Resources Officer 5- Iain Blacklaw – Chief Operating Officer 6- Bruce Wade – Chief Risk Officer 7- Yaser Alsharifi – Chief Strategy Officer 8- Richard Hicks – Chief Marketing Officer 9- Gaby El Hakim – General Counsel and Corporate Secretary 10- Hisham Kurdi – Chief Executive, CIIB	- Meets on a weekly basis. - To share and review strategic matters among senior management. - To brief on key developments.
2- Credit Committee	1- Jean Christophe Durand – Chief Executive Officer **(Chairman)** 2- Abdulaziz Al Ahmed – Chief Executive, Retail, Commercial and SMEs 3- Hussain Al Hussaini – Chief Executive, Treasury Capital Markets and Wealth Management 4- Bruce Wade – Chief Risk Officer 5- Yaser Alsharifi – Chief Strategy Officer 6- Hisham Kurdi – Chief Executive, CIIB 7- Isa Maseeh – Deputy Chief Risk Officer 8- Ali Ehsan – Chief Credit Officer	- Meets on a weekly basis. - To oversee the effective implementation of the credit risk framework of the Bank. - To approve credit proposals and monitoring the credit portfolio in line with the defined risk appetite and policies of the Bank.
3- Operational Risk Management Committee ('ORMC')	1- Bruce Wade – Chief Risk Officer **(Chairman)** 2- Jean Christophe Durand – Chief Executive Officer 3- Dana Buheji – Chief Human Resources Officer 4- Iain Blacklaw – Chief Operating Officer 5- Hisham Kurdi – Chief Executive, CIIB 6- Isa Maseeh – Deputy Chief Risk Officer 7- Jaffar Mohammed – Head of Operational Risk 8- Nabeel Mustafa – Head - Retail Operations 9- Balu Ramamurthy – Head - Compliance (left in November 2018) 10- Moschonas Panagiotis - Head of Internal Audit (upon invitation)	- Meets on a monthly basis. - To review and assess different aspects of risk arising from the Bank's business processes (i.e. operational risks, technology risk, business continuity plan, disaster recovery, legal risk, compliance risks and compliance with internal controls) to ensure that material risks are captured, monitored and mitigated.
4- Asset Liability Committee ('ALCO')	1- Jean Christophe Durand – Chief Executive Officer **(Chairman)** 2- Abdulaziz Al Ahmed – Chief Executive, Retail, Commercial and SMEs 3- Hussain Al Hussaini – Chief Executive, Treasury Capital Markets and Wealth Management 4- Bruce Wade – Chief Risk Officer 5- Yaser Alsharifi – Chief Strategy Officer 6- Hisham Kurdi – Chief Executive, CIIB 7- Russell Bennett – Chief Financial Officer 8- Isa Maseeh – Deputy Chief Risk Officer 9- Ali Al Moulani – Head - Treasury and ALM 10- Jaafar Abdulla – Head Liquidity and Market Risk	- Meets on a monthly basis. - To discuss and evaluate key issues concerning the Bank's balance sheet structure and performance, pricing of assets and liabilities, funding and capital planning, contingency planning, market risk, interest rate risk, and liquidity risk.

Management structure: (continued)

Committee Name	Members	Objective
5- Project Steering Committee ('PSG')	1- Jean Christophe Durand – Chief Executive Officer **(Chairman)** 2- Abdulaziz Al Ahmed – Chief Executive, Retail, Commercial and SMEs 3- Hussain Al Hussaini – Chief Executive, Treasury Capital Markets and Wealth Management 4- Dana Buheji – Chief Human Resources Officer 5- Iain Blacklaw – Chief Operating Officer 6- Bruce Wade – Chief Risk Officer 7- Yaser Alsharifi – Chief Strategy Officer 8- Hisham Kurdi – Chief Executive, CIIB 9- Richard Hicks – Chief Marketing Officer 10- Russell Bennett – Chief Financial Officer 11- Mahmood Al Aali – Head of Retail Transformation 12- Razi Amin – Head of Information Technology 13- Abdulla Buali – Project Management Officer 14- Muneera Mahmood – Project Management Specialist	- Meets on a monthly basis. - To ensure that the strategic programmes and major projects as approved by the management are successfully implemented. - To monitor issues raised through the PMO, project sponsors, and other programme committees are resolved and that progress is made according to the approved plans and approved financial budgets.
6- Digital Advisory Committee ('DAG')	1- Yaser Alsharifi – Chief Strategy Officer **(Chairman)** 2- Iain Blacklaw – Chief Operating Officer 3- Hisham Kurdi – Chief Executive, CIIB 4- Richard Hicks – Chief Marketing Officer 5- Mahmood Al Aali – Head of Retail Transformation 6- Razi Amin – Head of Information Technology	- Meets on a monthly basis. - To define the digital direction of the bank, govern the digital initiatives and projects and support business transformation.
7- Information Security Steering Committee ('ISSC')	1- Bruce Wade – Chief Risk Officer **(Chairman)** 2- Jordan Savvides – Head of Information Security 3- Iain Blacklaw – Chief Operating Officer 4- Isa Maseeh – Deputy Chief Risk Officer 5- Ali AlSaegh – IT Security Assistant Manager 6- Razi Amin – Head of Information Technology 7- Husam Saoudi – Manager, Information Security Risk 8- Balu Ramamurthy – Head - Compliance (left in November 2018)	- Meets on a monthly basis. - To oversee the Information Security risks; and monitor all information security related projects and initiatives.

The Chief Compliance Officer reports directly to the Risk Committee and has access to the Board of Directors through the Audit Committee. The Corporate Secretary has direct access to the Board of Directors in accordance with Corporate Governance requirements.

Performance evaluation of Board and sub-committees:

The Board of Directors has conducted a self evaluation of the performance of the Board and its sub-committees for the year 2018. This was carried out through the completion of a structured questionnaire on the effectiveness and contribution of each member against certain pre-defined criteria as per the mandate of the Board and each Board sub-committee. The Nomination and Remuneration Committee is responsible for overseeing the process and the findings were presented to the Board of Directors in the first quarter of 2019 which confirms that NBB's Board and its sub-committees continue to operate with a high level of effectiveness.

Corporate Governance Report (continued)

Related party transactions and conflict of interest:

Directors have a duty under the Commercial Companies Law, the CBB's regulations and the Bank's corporate governance policy to avoid situations in which they may have conflicts of interest with those of the Bank, unless they are specifically authorised by the Board of Directors. This includes potential conflicts that may arise when a Director takes up a position with another company or has any material transactions with the Bank.

The Bank has policies and procedures for handling related party transactions including loans and advances to directors, senior management and their related parties, as well as transactions and agreements in which a Director or an employee has a material interest. In addition, exposures to directors and senior management are governed by the regulations of the CBB. Details of related party transactions involving the Bank in 2018 are disclosed in Note 27 of the financial statements.

As per the Bank's policy, the Directors concerned do not participate in decisions in which they have or may have a potential conflict of interest.

Related party transactions are entered into in compliance with Article 189 of the Commercial Companies Law. They are entered into following the satisfaction of the Bank's tender processes and procedures in case they relate to services provided to the Bank to ensure that the Bank receives optimal services from its counterparties at the best pricing available. Decisions relating to the approval of related party transactions, whether with connected parties of Directors, Controllers or significant shareholders of the Bank, or employees are approved after appropriate disclosures have been made and the related parties and their connected persons refrain from participating in the decision making process. The Bank's shareholders are referred to Note 27 of the financial statements setting out disclosures of related party transactions in compliance with Article 189(C) of the Commercial Companies Law. The Board of Directors is satisfied with the procedures in place for the approval of related party transactions and the outcomes of related party contracts entered into in 2018.

Employment of relatives:

The Bank has a Board approved policy in place on employment of relatives to prevent the potential favouritism and conflict of interest in decision-making due to factors of blood relationships amongst employees including Approved Persons. The Bank will not hire any candidate related up to the second degree of an employee and/or a Director of the Board of the Bank at the time of application for employment, while special consideration is made when hiring individuals related beyond the above degree to existing staff members.

Code of conduct:

The Board has adopted a comprehensive code of conduct that provides a framework for directors, officers and employees on the conduct and ethical decision making integral to their work. All officers and employees subscribe to this Code and are expected to observe high standards of integrity and fairness in their dealings with customers, regulators and other stakeholders.

Whistle blower policy:

The Board has adopted a whistle blower policy which provides all employees with the opportunity to access in good faith, the Audit Committee or the CEO (who will keep the chairman of the Audit Committee informed of the facts as received by him) any instances they observe regarding unethical and improper practices or any other wrongful conduct of a financial or legal nature in the Bank and to prohibit managerial personnel from taking adverse action against employees for doing so. The policy is available on the website of the Bank.

Communication strategy:

The Bank has a public disclosure policy approved by the Board of Directors. The Bank is committed to support the timely and accurate disclosure of material information in accordance with the requirements set out in the rules and regulations of the CBB and the Bahrain Bourse as well as other applicable laws, to facilitate efficient capital market activities. The Bank believes in the principle of transparency about its financial performance thus enabling all stakeholders to have access to such information on a timely basis. In addition to the annual audit, the external auditors conduct reviews on the Bank's quarterly financial statements. These statements are subsequently published in the newspapers and posted on the Bank's website in accordance with regulatory requirements. The annual report including the complete financial statements for the current financial year and a minimum of five preceding financial years are provided on the Bank's website.

Fines and penalties:

The following penalties were paid by the Bank to the CBB during the year: (a) BHD 540 relating to old and new currency notes sorting (b) BHD 1,200 on delay in submission of the requirement stipulated in paragraph BR-1.1.3 sub-section (m) of the CBB's rulebook.

Directors and senior management interests:

The number of shares held by directors and their related parties and trading during the year is as follows:

Name	Type of shares	31 December 2018[1]	Sales during 2018	Purchases during 2018	31 December 2017
Farouk Yousuf Khalil Almoayyed - Chairman	Ordinary	22,650,930	-	-	20,591,756
Dr. Essam Abdulla Fakhro - Deputy Chairman	Ordinary	9,867,680	-	-	8,970,620
Fawzi Ahmed Kanoo - Deputy Chairman	Ordinary	87,760	-	-	79,783
Khalid Yousif Abdul Rahman - Director	Ordinary	22,021,982	-	512,457	19,517,741
Hussain Sultan Al Ghanem - Director	Ordinary	-	-	-	-
Khalid Omar Al Rumaihi - Director	Ordinary	-	-	-	-
Sh. Rashid Salman Mohamed Al Khalifa - Director	Ordinary	-	-	-	-
Hala Ali Hussain Yateem - Director	Ordinary	4,244,285	-	-	Not a Member
Rishi Kapoor - Director	Ordinary	-	-	-	Not a Member
Mohamed Tareq Mohamed Sadeq Mohamed Akbar - Director	Ordinary	-	-	-	Not a Member
Yusuf Abdulla Yusuf Akbar Alireza - Director	Ordinary	-	-	-	Not a Member
Ali Hussain Yateem - Director [2]	Ordinary		Left the Board		11,368,860
Abdulla Yousif Akbar Alireza - Deputy Chairman[2]	Ordinary		Left the Board		13,300,714
Mir Zulfekar Ali - Director [2]	Ordinary		Left the Board		-
Total		58,872,637	-	512,457	73,829,474
As a % of the total number of shares		4.20%			3.85%

[1] Shares as at 31 December 2018 include bonus shares issued during the year (where applicable) at the rate of one additional share for every ten shares held.

[2] Ali Hussain Yateem, Abdulla Yousif Akbar Alireza and Mir Zulfekar have left the board during 2018 and did not conduct any trade in respect to their direct/indirect holding of NBB shares before they left the board.

The number of shares held by senior management and their related parties and trading during the year is as follows:

Name	Type of shares	31 December 2018[1]	Sales during 2018	Purchases during 2018[2]	31 December 2017
Jean Christophe Durand - Chief Executive Officer	Ordinary	-	-	-	-
Hussain Al Hussaini - Chief Executive, Treasury, Capital Markets and Wealth Management	Ordinary	-	332,033	201,746	118,443
Abdulaziz Al Ahmed - Chief Executive, Retail, Commercial & SMEs	Ordinary	309,073	-	168,920	127,412
Bruce Wade - Chief Risk Officer	Ordinary	47,512	60,000	60,031	43,165
Dana Buheji - Chief Human Resources Officer	Ordinary	22,924	-	22,924	-
Iain Blacklaw - Chief Operating Officer	Ordinary	-	-	-	-
Yaser Al Sharifi - Chief Strategy Officer	Ordinary	11,975	-	11,975	-
Richard Hicks - Chief Marketing Officer	Ordinary	14,536	-	14,536	-
Hisham Al Kurdi Chief Executive, CIIB	Ordinary	-	-	-	-
Moschonas Panagiotis - Head of Internal Audit	Ordinary	18,144	-	15,741	2,403
Russell Bennett - Chief Financial Officer	Ordinary	-	-	-	-
Gaby El Hakim - General Counsel and Corporate Secretary	Ordinary	-	5,988	5,988	-
Venkata Subramaniam Raju - Chief Financial Officer	Ordinary		Left NBB		76,109
Balu Ramamurthy - Head of Compliance	Ordinary		Left NBB		40,365
Total		424,164	398,021	501,861	407,897

[1] Shares as at 31 December 2018 include bonus shares issued during the year (where applicable) at the rate of one additional share for every ten shares held.

[2] Represents shares transferred during the year as part of the Employee Share Incentive Scheme.

Approved persons interests:

The total interest in the shares held by approved persons and their related parties is as follows:

	Type of shares	31 December 2018	31 December 2017
Total number of shares held	Ordinary	59,494,528	74,271,469
As a % of the total number of shares		4.24%	5.82%

Remuneration:

Board of Directors remuneration policy:

The Board of Directors are paid an annual remuneration as approved by the shareholders at the Annual General Meeting. While the amount of the remuneration is not directly linked to the performance of the Bank, factors such as the Bank's performance, industry comparison and the time and effort committed by the Directors to the Bank, are considered for determining the total remuneration. Directors' remuneration is accounted as an expense as per International Financial Reporting Standards and CBB regulations. In addition, Directors are paid sitting fees for attending the various sub-committees of the Board of Directors.

Employees remuneration policy:

The employees of the Bank are critical for the Bank's success and future business sustenance. Hence, it is imperative to recruit and retain talented resources from the competitive employment market. In order to achieve this objective, the Bank's remuneration policy is developed to attract, retain and motivate the best talent. Accordingly, employee remuneration and benefits are reviewed and revised in the context of business performance, industry and local practices. In addition to fixed monthly salary and allowances, employees are provided with several other benefits like variable remuneration in the form of bonus, medical, life insurance coverage, retirement benefits and employee savings scheme. While doing so, the Bank gives paramount importance to the interests of the shareholders and to this end, the Bank has implemented the Sound Remuneration Practices mandated by the Central Bank of Bahrain. While aligning the compensation of the employees with the risk outcomes and performance levels of the Bank, policies for variable remuneration i.e. the bonus and share incentive scheme also endeavour to align senior management's interest with shareholders' interests. The total variable remuneration paid to all employees including the share incentive scheme is within the range of 8% to 9% of the net profit before the bonus and the variable remuneration expense. The variable remuneration of senior management is reviewed and approved by the Nomination and Remuneration Committee ('NRC') of the Bank. The approaches under the revised compensation policies will be beneficial to all stakeholders of the Bank, including the shareholders, as they resolve to achieve a balance between the performance and risk outcomes.

Remuneration of Board Members, Senior Management and fees paid to external auditors:

The aggregate remuneration paid to board members and senior management personnel are disclosed in note 27 of the financial statements.

KPMG Fakhro was the Bank's external auditors for the financial year ended 31 December 2018. The details of the audit fee paid to the auditors during the year 2018 as well as the details of non-audit services and fees paid are held at the Bank's premises, which is available to eligible shareholders upon specific request.

Status of compliance with CBB's Corporate Governance guidelines (High Level Controls Module)

Banks are required to comply with the High Level Controls (HC) Module of the CBB Rulebook. The HC Module contains both Rules and Guidance; Rules must be complied with, but Guidance may either be complied with or non-compliance explained by way of an annual report to the shareholders and to the CBB.

The Bank has provided the following explanations in relation to the below Guidance items:

Guidance

1. HC 1.3.13 states that no director of a bank should hold more than three directorships in public companies in the Kingdom of Bahrain, with the provision that no conflict of interest may exist, and the Board should not propose the election or re-election of any director who does. Two of the Bank's directors, Mr. Farouk Almoayyed and Dr. Essam Fakhro hold more than three directorships in public companies in Bahrain. However, the Board is of the opinion that this does not impact the effectiveness and efficiency of the Board of Directors, as the directors provide adequate attention to their responsibilities and there are no conflict of interests between their other directorships and that of the Bank.
2. HC 1.4.6 states that the Chairman of the Board of Directors should be an independent director. The Bank's Chairman, Mr. Farouk Almoayyed is not treated as an independent director taking into account the business transactions that the Bank has with the Almoayyed Group which is controlled by Mr. Farouk Almoayyed. The Board is of the view that this does not compromise the high standards of corporate governance that the Bank maintains as (i) the business transactions are entered into on 'arms length' basis following transparent tendering and approval processes (ii) the Bank follows strict policies to manage conflicts of interest in Board decisions (iii) Directors having a business interest in proposals considered by the Bank do not participate in decisions related to such proposals.
3. HC-1.8.2 states that the Board should establish a Corporate Governance Committee of at least three independent members and HC-1.8.5 allows combination of committees. The Bank has combined the responsibility of the Corporate Governance Committee with that of the Audit Committee, which has three members two of whom are independent. The Board is of the view that this does not compromise the high standards of corporate governance as the Audit Committee has sufficient resources and time to discharge its duties and holds sufficient number of meetings to fulfil its responsibilities.

Remuneration Report

Our philosophy

NBB has adopted a total rewards philosophy which translates its vision, strategy and the values into a framework that guides its decision making when it comes to all elements of its reward. We aim through this adoption to:

1. Attract and retain the best performers.
2. Provide incentive variable pay based on the attainment of specific organisational performance goals as well as the attainment of individual performance goals in a manner which is completely aligned to our organisational values.
3. Develop industry leaders who positively impact the performance of the bank and act as catalyst for growth within the economies in which we operate.

In its elements, our philosophy encompasses the following:

1. Encourage competency building by better linking career development, performance management and rewards.
2. Support a performance-driven work culture that generates organisational growth.
3. Reward (in the form of fixed and variable compensation) performance, skills and competencies, development and growth, and effective visible commitment to the organisation.
4. Generate opportunities for individuals' growth through career development, training, and succession planning and talent development.
5. Support a work environment which is governed by our values, sound leadership, and a culture conducive of success through team-based oriented work relationships and a balanced work life mix.

The translation of this philosophy has been implemented through compliance to a strong corporate governance framework. One which is both in adherence to regulatory requirements and in alignment to industry benchmarks and best practices. In terms of oversight, the Nomination and Remuneration Committee of the Board ('NRC') is responsible for ensuring adherence to policy and regulations.

The Bank's Remuneration Policy ensures that all employees, particularly the approved persons and material risk takers, are remunerated fairly and responsibly. Approved persons are employees who undertake functions that require prior approval from the CBB. These include controlled functions named by the CBB, executive positions directly reporting to the CEO and certain heads of function requiring specialised skill sets. Material Risk Takers are employees who are heads of significant business lines and any individuals within their control who have a material impact of the bank's risk profile.

In order to ensure alignment between what we pay the employees and the Bank's business strategy, we assess individual performance against annual and long-term financial and nonfinancial objectives summarised in line with our performance management system. This assessment also takes into account adherence to the Bank's values, risk, compliance measures and above all acting with integrity. Altogether, performance is therefore judged not only on what is achieved over the short and long-term but also importantly on how it is achieved, as the Bank believes the latter contributes to the long-term sustainability of the business.

NRC role and focus

The NRC has oversight of all compensation policies for the Bank's employees. The NRC is the supervisory and governing body for compensation policy, practices and plans. It is responsible for determining, reviewing and proposing variable remuneration policy for approval by the Board. It is responsible for setting the principles and governance framework for all compensation decisions. The NRC ensures that all persons must be remunerated fairly and responsibly. The remuneration policy is reviewed on a periodic basis to reflect changes in market practices and the business plan and risk profile of the Bank.

The responsibilities of the NRC with regards to the variable compensation policy of the Bank, as stated in its mandate, include, but are not limited to, the following:

- Approve, monitor and review the remuneration system to ensure the system operates as intended.
- Approve the remuneration policy and amounts for each Approved Person and Material Risk-Taker, as well as total variable remuneration to be distributed, taking account of total remuneration including salaries, fees, expenses, bonuses and other employee benefits.
- Ensure remuneration is adjusted for all types of risks.
- Ensure that for Material Risk Takers, variable remuneration forms a substantial part of their total remuneration.
- Review the stress testing and back testing results before approving the total variable remuneration to be distributed including salaries, fees, expenses, bonuses and other employee benefits.
- Carefully evaluate practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. The NRC will question payouts for income that cannot be realised or whose likelihood of realisation remains uncertain at the time of payment.
- Ensure that for approved persons in risk management, human resources, strategy, internal audit, operations, financial controls and compliance functions the mix of fixed and variable remuneration is weighted in favour of fixed remuneration

- Recommend Board member remuneration based on their attendance and performance and in compliance with Article 188 of Bahrain's Commercial Companies Law.
- Ensure appropriate compliance mechanisms are in place to ensure that employees commit themselves not to use personal hedging strategies or remuneration-and liability-related insurance to undermine the risk alignment effects embedded in their remuneration arrangements.

The Board of Directors has established the Nomination and Remuneration Committee in order to address the above mentioned objectives. Details of the committee, including the meeting dates, are included under the Corporate Governance Report. The aggregate remuneration paid to the NRC members during the year in the form of sitting fees amounted to BHD 12,000.

External consultants

External consultants have helped the Bank in formulating its variable remuneration policy to be in line with the CBB's Sound Remuneration Practices and industry standards.

Scope of application of the remuneration policy

The remuneration policy has been adopted on a Bank-wide basis and shall apply to its overseas branches and subsidiaries.

Board remuneration

The Bank's Board's remuneration is determined in line with the provisions of Article 188 of Bahrain's Commercial Companies Law, 2001. The Board of Directors' remuneration will be capped so that the total remuneration (excluding sitting fees) does not exceed 10% of the Bank's net profit, after all the required deductions outlined in Article 188 of the Companies law, in any financial year. The Board remuneration is subject to approval of the shareholders in the Annual General Meeting. Remuneration of non-executive directors does not include performance-related elements such as grants of shares, share options or other deferred stock-related incentive schemes, bonuses or pension benefits.

Variable remuneration for staff

The variable remuneration is performance related and consists primarily of the annual performance bonus award. The variable remuneration reward is linked to individuals' contributions towards the attainment of NBB goals and targets working within a value-based culture, conducive of a highly efficient, pragmatic and delivery-oriented environment.

The Bank has a Board approved framework to develop a transparent link between performance and variable remuneration. The framework is designed on the basis that the combination of financial performance and achievement of other non-financial factors, would, all other things being equal, deliver a target bonus pool for the employees. The bonus pool is then adjusted to take account of risk via the use of risk-adjusted measures (including forward-looking considerations). In the framework adopted in determining the variable remuneration pool, the NRC aims to balance the distribution of the Bank's profits between shareholders and employees.

The key performance metrics at the bank level include a combination of short-term and long-term measures and include profitability, solvency, liquidity and growth indicators.

The NRC carefully evaluates practices by which remuneration is paid for potential future revenues whose timing and likelihood remain uncertain. NRC demonstrates that its decisions are consistent with the assessment of the Bank's financial condition and future prospects.

The Bank uses a formalised and transparent process to adjust the bonus pool for quality of earnings. It is the Bank's objective to pay out bonuses out of realised and sustainable profits. Based on the quality of earnings, the bonus base could be adjusted based on the discretion of the NRC.

For the overall Bank to have any funding for distribution of bonus pool; thresholds of financial targets have to be achieved. The performance measures ensure that the total variable remuneration is generally considerably reduced where subdued or negative financial performance of the Bank occurs. Furthermore, the target bonus pool as determined above is subject to risk adjustments in line with the risk adjustment and linkage framework. The performance management process ensures that all goals are appropriately cascaded down to respective business units and employees.

The total variable remuneration paid to all employees including the Share Incentive Scheme is within the range of 8% to 9% of the net profit before the bonus.

Remuneration of control and support functions

The remuneration level of staff in the control and support functions allows the Bank to employ qualified and experienced personnel in these functions. The Bank ensures that the mix of fixed and variable remuneration for control and support function personnel should be weighted in favour of fixed remuneration. The variable remuneration of control functions is based on function-specific objectives and is not determined by the individual financial performance of the business area they monitor.

The Bank's performance management system plays a major role in deciding the performance of the support and control units on the basis of the objectives set for them. Such objectives are more focused on non-financial targets that include risk, control, compliance and ethical considerations as well as the market and regulatory environment apart from value adding tasks which are specific to each unit.

Variable compensation for business units

The variable compensation for the business units is primarily decided by the key performance objectives set through the performance management system of the Bank. Such objectives contain financial and non-financial targets, including risk control, compliance and ethical considerations as well as market and regulatory environment. The consideration of risk assessment in the performance evaluation of individuals ensures that any two employees who generate the same short-run profit but take different amounts of risk on behalf of the Bank are treated differently by the remunerations system.

Risk assessment framework

The purpose of the risk linkages is to align variable remuneration to the risk profile of the Bank. In its endeavour to do so, the Bank considers both quantitative measures and qualitative measures in the risk assessment process. Both quantitative measures and human judgment play a role in determining risk adjustments. The risk assessment process encompasses the need to ensure that the remuneration policy is designed to reduce employees' incentives to take excessive and undue risk is symmetrical with risk outcomes and has an appropriate mix of remuneration that is consistent with risk alignment.

The Bank's NRC considers whether the variable remuneration policy is in line with the Bank's risk profile and ensures that through the Bank's ex-ante and ex-post risk assessment framework and processes, remuneration practices where potential future revenues whose timing and likelihood remain uncertain are carefully evaluated.

Risk adjustments take into account all types of risk, including intangible and other risks such as reputation risk, liquidity risk and the cost of capital. The Bank undertakes risk assessment to review financial and operational performance against the business strategy and risk performance prior to the distribution of the annual bonus. The Bank ensures that the total variable remuneration does not limit its ability to strengthen its capital base.

The NRC keeps itself abreast with the Bank's performance against the risk management framework. The NRC will use this information when considering remuneration to ensure the return, risk and remuneration are aligned.

In years where the Bank suffers material losses in the financial performance, the risk adjustment framework includes several adjustments. The NRC carefully examines the results of stress tests and back tests conducted on the variable remuneration policy framework and makes necessary corrections to the staff bonus by reduction of bonus pool, possible changes to vesting period, additional deferrals and malus or clawback provisions.

The NRC, with Board's approval, can rationalise and make the following discretionary decisions:

- Increase/ decrease the ex-post adjustment
- Consider additional deferrals or increase in the quantum of share awards
- Recovery through malus and clawback arrangements

Malus and Clawback framework

The Bank's malus and clawback provisions allows the Bank's Board of Directors to determine that, if appropriate, unvested elements under the deferred bonus plan can be forfeited/ adjusted or the delivered variable compensation could be recovered in certain situations. The intention is to allow the Bank to respond appropriately if the performance factors on which reward decisions were based turn out not to reflect the corresponding performance in the longer term. All deferred compensation awards contain provisions that enable the Bank to reduce or cancel the awards of employees whose individual behaviour has had a materially detrimental impact on the Bank during the concerned performance year.

Any decision to take back an individual's award can only be taken by the Bank's Board of Directors.

The Bank's malus and clawback provisions allows the Bank's Board to determine that, if appropriate, vested / unvested elements under the deferred bonus plan can be adjusted/ cancelled in certain situations. These events include the following:

- Reasonable evidence of willful misbehaviour, material error, negligence or incompetence of the employee causing the Bank/ the employee's business unit to suffer material loss in its financial performance, material misstatement of the Bank's financial statements, material risk management failure or reputational loss or risk due to such employee's actions, negligence, misbehaviour or incompetence during the concerned performance year.
- The employee deliberately misleads the market and/or shareholders in relation to the financial performance of the Bank during the concerned performance year.

Clawback can be used if the malus adjustment on the unvested portion is insufficient, given the nature and magnitude of the issue.

Components of variable remuneration

Variable remuneration has following main components:

Upfront cash	The portion of the variable compensation that is awarded and paid out in cash on conclusion of the performance evaluation process for each year.
Deferred cash	The portion of variable compensation that is awarded and paid in cash on a pro-rata basis over a period of 3 years
Upfront share awards	The portion of variable compensation that is awarded and issued in the form of shares on conclusion of the performance evaluation process for each year.
Deferred shares	The portion of variable compensation that is awarded and paid in the form of shares on a pro-rata basis over a period of 3 years

All deferred awards are subject to malus provisions. All share awards are released to the benefit of the employee after a six month retention period from the date of vesting. The number of equity share awards is linked to the Bank's share price as per the rules of the Bank's share incentive scheme. Any dividend on these shares is released to the employee along with the shares (i.e. after the retention period).

Deferred compensation

Employees in the grade of senior manager and above and those earning total annual compensation of BHD 100,000 and above shall be subject to deferral of variable remuneration as follows:

Element of variable remuneration	GMs and above	5 highest paid business emp.	SMs and AGMs	Deferral period	Retention	Malus	Clawback
Upfront cash	40%	40%	50%	immediate	-	-	Yes
Upfront shares	-	-	10%	immediate	6 months	Yes	Yes
Deferred cash	10%	10%	-	3 years*	-	Yes	Yes
Deferred share awards	50%	50%	40%	3 years*	6 months	Yes	Yes

* The deferral vests on a pro-rata basis over a 3 year period

The NRC, based on its assessment of role profiles and risk taken by an employee could increase the coverage of employees that would be subject to deferral arrangements.

Details of remuneration paid

(a) Board of Directors

BHD 000's	2018	2017
· Sitting fees	32	23
· Remuneration	460	420

(b) Employees

1-Employee remuneration

	2018										
	Number of staff*	Fixed remuneration		Sign on bonuses**	Guaranteed bonuses	Variable remuneration					
						Upfront		Deferred			
BHD 000's		Cash	Others	(Cash / shares)	(Cash / shares)	Cash	Shares	Cash	Shares	Others	Total
Approved persons											
- Business lines	7	1,449	349	22	-	505	8	117	614	-	3,064
- Control and support	18	1,964	449	-	-	594	112	-	448	-	3,567
Other material risk takers	14	942	157	-	-	254	43	10	220	-	1,626
Other staff	619	9,189	3,443	-	-	3,644	27	-	108	-	16,411
Overseas staff	44	649	403	4	-	161	-	-	1	-	1,218
	702	14,192	4,802	26	-	5,158	190	126	1,391	-	25,886

* This represents staff as at 31 December 2018. 45 staff who left during the year are not included in the number of staff however their respective remuneration has been disclosed in the relevant captions.

** This item is for two sign on awards which were awarded to certain strategic new hires in an overseas branch to meet the requirements of the prevailing market practice in the foreign jurisdiction of that branch, which is on an exceptional basis to the standing general policy of the Bank not to provide sign on awards.

Note: other staff costs amounting to BHD 127 thousand incurred towards recruitment are not included in the above.

Details of remuneration paid (continued)

	2017										
	Number of staff*	Fixed remuneration		Sign on bonuses	Guaranteed bonuses	Variable remuneration					
						Upfront		Deferred			
BHD 000's		Cash	Others	(Cash / shares)	(Cash / shares)	Cash	Shares	Cash	Shares	Others	Total
Approved persons											
- Business lines	6	1,137	361	-	-	441	4	106	543	-	2,592
- Control and support	16	1,468	383	-	-	341	56	10	270	-	2,528
Other material risk takers	5	225	74	-	-	66	13	-	53	-	431
Other staff	610	7,884	3,179	-	-	3,072	33	5	161	-	14,334
Overseas staff	33	721	142	-	-	126	-	-	-	-	989
	670	11,435	4,135	-	-	4,046	106	121	1,027	-	20,874

* This represents staff as at 31 December 2017. 54 staff who left during the year are not included in number of staff however their respective remuneration has been disclosed in the relevant caption.

Note: other staff costs amounting to BHD 429 thousand incurred towards recruitment and other indirect staff expense are not included in the above.

Note: The total amount of remuneration during the year includes a severance payment made amounting to BHD 37 thousand to one person. This payment was per the labour law.

2. Deferred Awards

	2018				
	Cash		Shares	Others	Total
	BHD 000's	Number	BHD 000's*	BHD 000's	BHD 000's
Opening Balance	573	4,609,222	2,819	-	3,392
Awarded during the year	123	1,791,631	1,155	-	1,278
Cash/Stock dividend awarded during the year	164	655,645	-	-	618
Paid out/released during the year	(357)	(2,459,043)	(1,289)	-	(1,646)
Service, performance and risk adjustments	-	-	-	-	-
Changes in value of unvested awards	-	-	-	-	-
Closing Balance	503	4,597,455	2,685	-	3,188

* Based on the original award price for each award period

	2017				
	Cash		Shares	Others	Total
	BHD 000's	Number	BHD 000's*	BHD 000's	BHD 000's
Opening Balance	421	3,595,666	2,293	-	2,714
Awarded during the year	189	2,175,730	1,573	-	1,762
Cash/Stock dividend awarded during the year	150	598,751	-	-	150
Paid out/released during the year	(200)	(1,760,925)	(1,047)	-	(1,247)
Service, performance and risk adjustments	-	-	-	-	-
Changes in value of unvested awards	13	-	-	-	13
Closing Balance	573	4,609,222	2,819	-	3,392

* Based on the original award price for each award period

Financial Statements

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Independent Auditors' Report to the Shareholders

National Bank of Bahrain B.S.C.
P.O. Box 106
Manama
Kingdom of Bahrain

Report on the audit of the financial statements

Opinion

We have audited the accompanying financial statements of National Bank of Bahrain B .S.C. (the 'Bank'), which comprise the statement of financial position as at 31 December 2018, the statements of profit or loss, comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' responsibilities for the audit of the financial statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements for the year ended 31 December 2018. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Impairment of loans and advances

(refer to the use of estimate and management judgement in note 2(d), impairment policy in note 2f(x), note 7 and disclosures of credit risk in note 3 of the financial statements)

Description	How the matter was addressed in our audit
We focused on this area because: • of the significance of loans and advances (representing 37% of total assets) and the related estimation uncertainty to the financial statements; and • IFRS 9 'Financial Instruments' (IFRS 9) was adopted by the Bank on 1 January 2018 and has resulted in: ◦ change in accounting policies for impairment including the need for making complex estimates and judgment over both timing and recognition of impairment; ◦ transition adjustments on 1 January 2018, being the date of adoption in retained earnings;.	Our audit procedures, amongst others, to address significant risks associated with impairment included: • Evaluating the appropriateness of the accounting policies adopted based on the requirements of IFRS 9, our business understanding, and industry practice. • Confirming our understanding of management's new or revised processes, systems and controls implemented, including controls over expected credit loss ('ECL') model development. Controls testing We performed process walkthroughs to identify the key systems, applications and controls used in the ECL processes. We tested the relevant General IT and applications controls over key systems used in the ECL process. Key aspects of our control testing involved the following: • Performing detailed credit risk assessment for a sample of performing and non-performing loans to test controls over credit rating and its monitoring process; • Testing the design and operating effectiveness of the key controls over the completeness and accuracy of the key inputs and assumptions elements into the IFRS 9 impairment models; • Testing controls over the transfer of data between underlying source systems and the impairment models that the Bank operates;

Independent Auditors' Report to the Shareholders (continued)

Impairment of loans and advances (continued)

Description	How the matter was addressed in our audit
◦ use of statistical models and methodologies for determination of expected credit losses; ◦ significant change in processes, data and control that have not been subject to testing previously; and ◦ complex disclosure requirements regarding impact of initial application of IFRS 9 and credit quality of the portfolio including explanation of key judgements and material inputs used in determination of expected credit losses.	• Evaluating controls over the modelling process, including governance over model monitoring, validation and approval; • Evaluating controls over the governance and assessment of model outputs and authorisation and review of post model adjustments and management overlays; and • Testing key controls relating to selection and implementation of material economic variables. Test of details Key aspects of our testing involved: • Sample testing over key inputs and assumptions impacting ECL calculations including economic forecasts and weights to confirm the accuracy of information used; • Re-performing key aspects of the Bank's significant increase in credit risk ('SICR') determinations and selecting samples of financial instruments to determine whether a SICR was appropriately identified; • Re-performing key elements of the Bank's model calculations and assessing performance results for accuracy; and • Selecting a sample of post model adjustments and management overlays in order to assess the reasonableness of the adjustments by challenging key assumptions, testing the underlying calculation and tracing a sample back to source data. Use of specialists For the relevant portfolios examined, we have involved KPMG specialists to assist us in assessing IT system controls and challenging key management assumptions used in determining expected credit losses. Key aspects of their involvement include: • We involved our Information Risk Management specialists to test controls over the new IT systems, recording of data in source systems and transfer of data between source systems and the impairment models; • We involved our Financial Risk Management specialists to review the reasonableness and appropriateness of the methodology and assumptions used in various components of ECL modelling by reference to our own knowledge and external market data and economic conditions. This typically included challenging key assumptions/ judgements relating to credit risk grading, significant increase in credit risk, definition of default, probability of default, recovery rates, use macroeconomic variables and probability weighted outcomes. Disclosures We assessed the adequacy of the Bank's disclosure in relation to transition impact arising from first time application of IFRS 9, new accounting policies, use of significant estimates and judgement and credit quality of loans and advances by reference to the requirements of relevant accounting standards.

Other information

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

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

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we have obtained prior to the date of this auditors' report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the board of directors for the financial statements

The board of directors is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as the board of directors determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the board of directors is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the board of directors either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Independent Auditors' Report to the Shareholders (continued)

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the board of directors.
- Conclude on the appropriateness of the board of directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Bank to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the board of directors regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

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

From the matters communicated with the board of directors, we determine those matters that were of most significance in the audit of the financial statements for the year ended 31 December 2018 and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other regulatory requirements

As required by the Bahrain Commercial Companies Law and Volume 1 of the Central Bank of Bahrain (CBB) Rule Book, we report that:

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

b) the financial information contained in the board of directors report is consistent with the financial statements;

c) we are not aware of any violations during the year of the Bahrain Commercial Companies Law, the Central Bank of Bahrain and Financial Institutions Law, the CBB Rule Book (Volume 1, applicable provisions of Volume 6 and CBB directives), the CBB Capital Markets Regulations and associated resolutions, the Bahrain Bourse rules and procedures or the terms of the Bank's memorandum and articles of association that would have had a material adverse effect on the business of the Bank or on its financial position; and

d) satisfactory explanations and information have been provided to us by management in response to all our requests.

The engagement partner on the audit resulting in this independent auditors' report is Jaafar AlQubaiti.

KPMG

KPMG Fakhro
Partner registration number 83
28 January 2019

Statement of Financial Position
As at 31 December

	Note	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
Assets					
Cash and balances at central banks	4	**107.3**	**285.4**	107.0	284.7
Treasury bills	5	**387.1**	**1,029.5**	419.9	1,116.8
Placements with banks and other financial institutions	6	**259.7**	**690.6**	174.0	462.8
Loans and advances	7	**1,190.1**	**3,165.2**	1,226.9	3,262.9
Investment securities	8	**1,132.2**	**3,011.2**	1,067.3	2,838.6
Investment in associates	9	**51.6**	**137.2**	51.6	137.2
Interest receivable and other assets	10	**50.9**	**135.4**	41.8	111.1
Property and equipment	19	**16.6**	**44.1**	13.0	34.7
Total assets		**3,195.5**	**8,498.6**	3,101.5	8,248.8
Liabilities					
Due to banks and other financial institutions	11	**381.4**	**1,014.4**	384.0	1,021.3
Borrowings under repurchase agreements	12	**103.9**	**276.3**	67.8	180.4
Customer deposits	13	**2,190.6**	**5,826.1**	2,165.2	5,758.6
Interest payable and other liabilities	14	**43.8**	**116.5**	36.6	97.2
Total liabilities		**2,719.7**	**7,233.3**	2,653.6	7,057.5
Equity					
Share capital	20	**140.3**	**373.1**	127.5	339.2
Shares unallocated under share incentive scheme	20	**(1.5)**	**(4.0)**	(1.7)	(4.4)
Share premium	21	**5.0**	**13.2**	4.0	10.7
Statutory reserve	21	**70.1**	**186.4**	63.8	169.6
General reserve	21	**32.4**	**86.2**	32.4	86.1
Other reserves and retained earnings	21	**229.5**	**610.4**	221.9	590.1
Total equity		**475.8**	**1,265.3**	447.9	1,191.3
Total liabilities and equity		**3,195.5**	**8,498.6**	3,101.5	8,248.8

The board of directors approved the financial statements consisting of pages 58 to 93 on 28 January 2019 and signed on its behalf by:

Farouk Yousuf Khalil Almoayyed	**Dr. Essam Abdulla Fakhro**	**Jean-Christophe Durand**
Chairman	Deputy Chairman	Chief Executive Officer

The accompanying notes 1 to 43 are an integral part of these financial statements.

Statement of Profit or Loss
For the year ended 31 December

	Note	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
Interest income	23	**126.8**	**337.3**	102.1	271.5
Interest expense	23	**(39.6)**	**(105.4)**	(29.0)	(77.2)
Net interest income		**87.2**	**231.9**	73.1	194.3
Other income	24	**30.2**	**80.3**	31.4	83.5
Total operating income		**117.4**	**312.2**	104.5	277.8
Staff expenses	25	**26.0**	**69.1**	21.3	56.6
Other expenses		**15.8**	**42.0**	11.7	31.1
Total operating expenses		**41.8**	**111.1**	33.0	87.7
Profit before impairment provisions		**75.6**	**201.0**	71.5	190.1
Net impairment provisions	15	**(5.6)**	**(14.9)**	(10.5)	(27.8)
Profit for the year		**70.0**	**186.1**	61.0	162.3
Basic and diluted earnings per share	38	**50 fils**	**13 cents**	44 fils	12 cents

Farouk Yousuf Khalil Almoayyed	**Dr. Essam Abdulla Fakhro**	**Jean-Christophe Durand**
Chairman	Deputy Chairman	Chief Executive Officer

The accompanying notes 1 to 43 are an integral part of these financial statements.

Statement of Comprehensive Income

For the year ended 31 December

	2018		2017	
	BHD millions	**USD millions**	BHD millions	USD millions
Profit for the year	**70.0**	**186.1**	61.0	162.3
Other comprehensive income:				
Items that are, or may be, reclassified to profit or loss:				
Fair value through other comprehensive income				
Net change in fair value	**(8.9)**	**(23.7)**	1.1	3.0
Net amount transferred to profit or loss	**-**	**-**	(0.2)	(0.6)
Items that will not be reclassified to profit or loss:				
Fair value through other comprehensive income	**5.5**	**14.6**	-	-
Total other comprehensive income for the year	**(3.4)**	**(9.1)**	0.9	2.4
Total comprehensive income for the year	**66.6**	**177.0**	61.9	164.7

The accompanying notes 1 to 43 are an integral part of these financial statements.

Statement of Changes in Equity

For the year ended 31 December 2018

						Other reserves and retained earnings			Total	
31 December 2018	**Share capital**	**Unallocated shares**	**Share premium**	**Statutory reserve**	**General reserve**	**Fair value reserve**	**Donation and charity reserve**	**Retained earnings**	**BHD millions**	**USD millions**
Balance at 31 December 2017	**127.5**	**(1.7)**	**4.0**	**63.8**	**32.4**	**26.1**	**16.0**	**179.8**	**447.9**	**1,191.3**
Impact of adopting IFRS 9 as at 1 January 2018	**-**	**-**	**-**	**-**	**-**	**(12.7)**	**-**	**9.9**	**(2.8)**	**(7.4)**
Impact of adopting IFRS 9 by associates	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(4.1)**	**(4.1)**	**(10.9)**
Balance at 1 January 2018	**127.5**	**(1.7)**	**4.0**	**63.8**	**32.4**	**13.4**	**16.0**	**185.6**	**441.0**	**1,173.0**
2017 appropriations:										
Cash dividend at 25%	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(31.5)**	**(31.5)**	**(83.8)**
Bonus shares issued 10%	**12.8**	**(0.1)**	**-**	**-**	**(12.8)**	**-**	**-**	**0.1**	**-**	**-**
Transfer to donations and charity reserve	**-**	**-**	**-**	**-**	**-**	**-**	**3.1**	**(3.1)**	**-**	**-**
Transfer to general reserve	**-**	**-**	**-**	**-**	**19.1**	**-**	**-**	**(19.1)**	**-**	**-**
Transfer to statutory reserve	**-**	**-**	**-**	**6.3**	**(6.3)**	**-**	**-**	**-**	**-**	**-**
Balance after 2017 appropriations	**140.3**	**(1.8)**	**4.0**	**70.1**	**32.4**	**13.4**	**19.1**	**132.0**	**409.5**	**1,089.2**
Employee shares allocated	**-**	**0.3**	**1.0**	**-**	**-**	**-**	**-**	**-**	**1.3**	**3.7**
Comprehensive income for the year:										
Profit for the year	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**70.0**	**70.0**	**186.1**
Other comprehensive income	**-**	**-**	**-**	**-**	**-**	**(3.4)**	**-**	**-**	**(3.4)**	**(9.1)**
Total comprehensive income for the year	**-**	**-**	**-**	**-**	**-**	**(3.4)**	**-**	**70.0**	**66.6**	**176.9**
Utilisation of donation and charity reserve	**-**	**-**	**-**	**-**	**-**	**-**	**(1.6)**	**-**	**(1.6)**	**(4.5)**
Balance at 31 December 2018 (notes 20-22)	**140.3**	**(1.5)**	**5.0**	**70.1**	**32.4**	**10.0**	**17.5**	**202.0**	**475.8**	**1,265.3**

The appropriations for the year 2018 will be submitted to the shareholders at the annual general meeting. These appropriations include BHD 35.1 million for cash dividend at 25% (2017: 25%), BHD 3.5 million for donations and contributions and a transfer of BHD 21.0 million from retained earnings to general reserve. The Board of Directors has also proposed a one for ten bonus issue through utilisation of BHD 14.0 million from general reserve and the transfer of BHD 7.0 million from general reserve to statutory reserve.

						Other reserves and retained earnings			Total	
31 December 2017	Share capital	Unallocated shares	Share premium	Statutory reserve	General reserve	Fair value reserve	Donation and charity reserve	Retained earnings	BHD millions	USD millions
Balance at 1 January 2017	116.0	(1.6)	2.5	58.0	32.4	25.2	14.6	167.5	414.6	1,102.7
2016 appropriations:										
Cash dividend at 25%	-	-	-	-	-	-	-	(28.7)	(28.7)	(76.2)
Bonus shares issued 10%	11.5	(0.2)	-	-	(11.5)	-	-	0.2	-	-
Transfer to donations and charity reserve	-	-	-	-	-	-	2.9	(2.9)	-	-
Transfer to general reserve	-	-	-	-	17.3	-	-	(17.3)	-	-
Transfer to statutory reserve	-	-	-	5.8	(5.8)	-	-	-	-	-
Balance after 2016 appropriations	127.5	(1.8)	2.5	63.8	32.4	25.2	17.5	118.8	385.9	1,026.5
Employee shares allocated	-	0.1	1.5	-	-	-	-	-	1.6	4.2
Comprehensive income for the year:										
Profit for the year	-	-	-	-	-	-	-	61.0	61.0	162.3
Other comprehensive income	-	-	-	-	-	0.9	-	-	0.9	2.4
Total comprehensive income for the year	-	-	-	-	-	0.9	-	61.0	61.9	164.7
Utilisation of donation and charity reserve	-	-	-	-	-	-	(1.5)	-	(1.5)	(4.1)
Balance at 31 December 2017 (notes 20-22)	127.5	(1.7)	4.0	63.8	32.4	26.1	16.0	179.8	447.9	1,191.3

Unallocated shares are shares that remain unallocated to employees under the employee share incentive scheme.

The accompanying notes 1 to 43 are an integral part of these financial statements.

Statement of Cash Flows
For the year ended 31 December

		2018		2017	
	Note	BHD millions	USD millions	BHD millions	USD millions
Cash flows from operating activities					
Profit for the year		**70.0**	**186.1**	61.0	162.3
Adjustments to reconcile profit for the year to net cash from operating activities:					
Depreciation		**2.0**	**5.4**	1.8	4.7
Net impairment provisions	*15*	**5.6**	**14.9**	10.4	27.6
Share of profit of associates		**(5.4)**	**(14.4)**	(3.7)	(9.8)
Profit for the year after adjustments		**72.2**	**192.0**	69.5	184.8
Changes in operating assets and liabilities					
Balances with central banks (mandatory cash reserves)		**7.8**	**20.7**	1.1	2.9
Treasury bills		**52.1**	**138.6**	18.6	49.6
Placements with banks and other financial institutions		**2.6**	**6.8**	16.3	43.4
Loans and advances		**27.7**	**73.7**	(205.3)	(546.1)
Investment securities		**(75.0)**	**(199.1)**	24.8	66.1
Interest receivable and other assets		**(0.7)**	**(1.8)**	0.3	0.8
Due to banks and other financial institutions		**(2.6)**	**(7.0)**	10.2	27.1
Borrowings under repurchase agreements		**36.1**	**96.0**	3.5	9.4
Customer deposits		**25.4**	**67.5**	76.9	204.4
Interest payable and other liabilities		**7.7**	**20.3**	0.6	1.6
Net cash from operating activities		**153.3**	**407.7**	16.5	44.0
Cash flows from investing activities					
Dividend received from associates		**1.2**	**3.1**	2.3	6.1
Purchase of property and equipment, net		**(5.7)**	**(15.2)**	(2.4)	(6.3)
Net cash used in investing activities		**(4.5)**	**(12.1)**	(0.1)	(0.2)
Cash flows from financing activities					
Dividends paid		**(31.5)**	**(83.9)**	(28.5)	(76.0)
Donations and charities paid		**(1.6)**	**(4.3)**	(1.5)	(4.2)
Net cash used in financing activities		**(33.1)**	**(88.2)**	(30.0)	(80.2)
Net increase/(decrease) in cash and cash equivalents		**115.7**	**307.4**	(13.6)	(36.4)
Cash and cash equivalents at 1 January	*4*	**195.2**	**519.1**	208.8	555.5
Cash and cash equivalents at 31 December	*4*	**310.9**	**826.5**	195.2	519.1

The accompanying notes 1 to 43 are an integral part of these financial statements.

Notes to the Financial Statements
For the year ended 31 December

1. REPORTING ENTITY

The National Bank of Bahrain B.S.C., a public shareholding company, was incorporated in the Kingdom of Bahrain by an Amiri decree in January 1957. The Bank is licensed by the Central Bank of Bahrain as a conventional retail bank.

The overseas branches in Abu Dhabi (United Arab Emirates) and Riyadh (Kingdom of Saudi Arabia) operate under the laws of those respective countries. The Bank is principally engaged in providing retail and wholesale commercial banking services, treasury and investment activities, and investment advisory services.

The Bank's registered address is National Bank of Bahrain B.S.C., P.O. Box 106, NBB Tower, Government Avenue, Manama, Kingdom of Bahrain. The shares of the Bank are listed on the Bahrain Bourse, Manama, Kingdom of Bahrain.

2. SIGNIFICANT ACCOUNTING POLICIES

a. Statement of compliance

The financial statements have been prepared in accordance with the International Financial Reporting Standards ('IFRS'), the requirements of the Bahrain Commercial Companies Law 2001 and the Central Bank of Bahrain and Financial Institutions Law 2006.

b. Basis of preparation

The financial statements of the Bank are presented in Bahraini Dinar (BHD) being the functional currency of the Bank. The US Dollar (USD) amounts are presented for the convenience of the reader. The Bahraini Dinar has been translated to US Dollar at the rate of BHD 0.376 to USD 1 (2017: BHD 0.376 to USD 1).

The financial statements have been prepared on the historical cost convention except for financial instruments classified as fair value through profit or loss, fair value through other comprehensive income investments and derivative financial instruments which are measured at fair value. The principal accounting policies applied in the preparation of these financial statements have been consistently applied to all the years presented except as described below:

i) New standards, amendments and interpretations effective from 1 January 2018:

The Bank has adopted IFRS 9 'Financial insturments' and IFRS 15 'Revenue from contracts with customers' from 1 January 2018.

A. IFRS 9 'Financial Instruments'

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement. The requirements of IFRS 9 represent a significant change from IAS 39. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

Due to the transition method chosen by the Bank in applying IFRS 9, comparative information throughout these financial statements has not been restated to reflect its requirements.

The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarised below.

i) Changes in accounting policies

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost (AC), fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-for-trading, held-to-maturity, available-for-sale and loans and receivables.

IFRS 9 removes the requirement contained in IAS 39 relating to bifurcation of an embedded derivative from an asset host contract. However, entities are still required to separate derivatives embedded in financial liabilities where they are not closely related to the host contract.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities with the exception of the treatment of the Bank's own credit gains and losses, which arise where a bank has chosen to measure a liability at fair value through profit or loss, these gains and losses are recognised in other comprehensive income. There continue to be two measurement categories for financial liabilities: fair value and amortised cost.

Impairment of financial assets

IFRS 9 replaces the incurred loss model in IAS 39 with an expected credit loss ('ECL') model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

The Bank applies a three-stage approach to measuring ECL on financial assets carried at amortised cost and debt instruments classified as FVOCI. Assets migrate through the following three stages based on the change in credit quality since initial recognition.

Stage 1: 12-months ECL

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

Stage 2: Lifetime ECL - not credit impaired

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

Notes to the Financial Statements (continued)
For the year ended 31 December

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

b. Basis of preparation (continued)

Stage 3: Lifetime ECL - credit impaired

Stage 3 includes financial assets that have objective evidence of impairment at the reporting date. For these assets, lifetime ECL is recognised based on discounted cash flow methods based on the difference between the net carrying amount and the recoverable amount of the financial asset. The recoverable amount is measured as the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted based on the interest rate at the inception of the credit facility or, for debt instruments, at the current market rate of interest for a similar financial asset.

Hedge accounting

At inception of the hedging relationship, the management undertakes a formal designation and documentation. This includes the Bank's risk management objective underlying the hedging relationship and how that fits within the overall risk management strategy. The documentation also includes an identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the entity will assess whether the hedging relationship meets the hedge effectiveness requirements. IFRS 9 also requires documentation of the hedge ratio and potential sources of ineffectiveness.

ii) Changes to significant estimates and judgements

Credit risk grades

The Bank has an internal credit rating model that uses qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower. The credit grades are calibrated such that the risk of default increases at each higher risk grade. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade. The Bank also uses external credit ratings for certain exposures.

Significant increase in credit risk

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

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

I. Downgrade in risk rating according to the approved ECL policy.

II. Facilities restructured during the previous twelve months.

III. Facilities overdue by 30 days as at the reporting date subject to rebuttal in applicable circumstances.

Measurement of expected credit losses

The estimation of credit exposure for risk management purposes is complex and requires the use of models. The exposure varies with changes in market conditions, expected cash flows, and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios, and of default correlations between counterparties. The Bank measures expected credit loss using probability of default ('PD'), exposure at default ('EAD') and loss given default ('LGD').

The Bank employs statistical models to analyse the data collected and generate estimates of PD of exposures and how these are expected to change as a result of the passage of time. This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, across the various geographies in which the Bank has exposures.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the forecasted collateral value and the associated recovery cost.

iii) Impact of adopting IFRS 9

The impact from the adoption of IFRS 9 as at 1 January 2018 has resulted in an increase in retained earnings by BHD 5.8 million and a decrease in the fair value reserve by BHD 12.7 million:

In BHD millions	Retained earnings	Fair value reserve
Closing balance under IAS 39 (31 December 2017)	179.8	26.1
Impact on reclassification and remeasurements:		
Investment securities (equity) from available-for-sale to those measured at fair value through other comprehensive income	14.2	(14.2)
	194.0	11.9
Impact on recognition of expected credit losses:		
Investment securities - (debt) at fair value through other comprehensive income	(1.5)	1.5
Loans and advances	0.3	-
Loan commitments and financial guarantees	(3.1)	-
	(4.3)	1.5
Impact of adopting IFRS 9 by associates	(4.1)	-
Opening balance under IFRS 9 on date of initial application of 1 January 2018	**185.6**	**13.4**

Notes to the Financial Statements (continued)
For the year ended 31 December

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

b. Basis of preparation (continued)

iv) Classification and measurement of financial instruments

The Bank performed a detailed analysis of its business models for managing financial assets as well as analysing their cash flow characteristics. The below table reconciles the original measurement categories and carrying amounts of financial assets in accordance with IAS 39 and the new measurement categories under IFRS 9 as at 1 January 2018:

In BHD millions	Original classification under IAS 39	New classification under IFRS 9	Original carrying amount	Impact of IFRS9 remeasurement	New carrying amount
Financial assets					
Cash and balances with central banks	Loans and receivables	Amortised cost	107.0	-	107.0
Treasury bills	Held-to-maturity	Amortised cost	419.9	-	419.9
Placements with banks and other financial institutions	Loans and receivables	Amortised cost	174.0	-	174.0
Loans and advances	Loans and receivables	Amortised cost	1,226.9	0.3	1,227.2
Investment securities			1,067.3	-	1,067.3
Debt insturments	*Available-for-sale*	*FVOCI*	1,017.9	-	1,017.9
Equity insturments	*Held-for-trading*	*FVTPL*	0.3	-	0.3
Equity insturments	*Available-for-sale*	*FVOCI*	49.1	-	49.1
Interest receivable and other assets	Loans and receivables	Amortised cost	41.8	-	41.8
			3,036.9	0.3	3,037.2

As at 1 July 2018, the Bank has reclassified debt instruments amounting to BHD 685.4 million from fair value through other comprehensive income (FVOCI) category to amortised cost category to more accurately reflect the Bank's new strategic intention for the portfolio. The Bank intends to collect the contractual cash flows which represent solely the payment of principal and interest.

All financial liabilities are measured at amortised cost.

v) Expected credit loss / impairment allowances

The following reconciles the closing impairment allowance for financial assets in accordance with IAS 39 as at 31 December 2017 to the opening ECL allowance determined in accordance with IFRS 9 as at 1 January 2018:

In BHD millions	31 December 2017	Remeasurement	1 January 2018
Loans and advances	42.7	(0.3)	42.4
Available-for-sale debt securities under IAS 39/debt securities at FVOCI under IFRS 9	-	1.5	1.5
Loan commitments and financial guarantees	-	3.1	3.1
	42.7	4.3	47.0

vi) ECL impact on exposure as at 1 January 2018

In BHD millions	Stage 1	Stage 2	Stage 3	Total
Exposure subject to ECL as at 1 January 2018				
Loans and advances	1,151.0	29.9	88.7	1,269.6
Treasury bills	419.9	-	-	419.9
Investment securities (debt)	1,017.9	-	-	1,017.9
Placements with banks and other financial institutions	174.0	-	-	174.0
	2,762.8	29.9	88.7	2,881.4
ECL as at 1 January 2018				
Loans and advances	9.4	1.6	31.4	42.4
Treasury bills	-	-	-	-
Investment securities (debt)	1.5	-	-	1.5
Placements with banks and other financial institutions	-	-	-	-
	10.9	1.6	31.4	43.9

ECL on loan commitments and financial guarantees captured under other liabilities and amounting to BHD 3.1 million.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

b. Basis of preparation (continued)

B. IFRS 15 'Revenue from contracts with customers'
IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.

The Bank initially applied IFRS 15 on 1 January 2018 retrospectively in accordance with IAS 8 without any practical expedients.The timing or amount of the Bank's fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15.

ii) New standards, amendments and interpretations issued but not yet effective:

A. IFRS 16 'Leases'
IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments into the future. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting remains similar to the current standard i.e. lessors continue to classify leases as finance or operating leases.

IFRS 16 replaces existing leases guidance including IAS 17 'Leases', IFRIC 4 'Determining whether an arrangement contains a lease', SIC-15 'Operating leases-incentives' and SIC-27 'Evaluating the substance of transactions involving the legal form of a lease'.

The Bank plans to apply IFRS 16 on 1 January 2019, using a modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

The Bank plans to apply the practical expedient to grandfather the definition of a lease on transition. This means that it will apply IFRS 16 to all contracts entered into before 1 January 2019.

The adoption of the standard will not have a significant impact on the financial position of the Bank.

c. Foreign currencies

i) Foreign currency transactions:

Foreign currency transactions are initially recorded at rates of exchange prevailing at the value date of the transactions. Monetary assets and liabilities in foreign currencies are translated to respective functional currencies at the rates of exchange prevailing at the statement of financial position date. Realised and unrealised exchange gains or losses are recognised in the statement of profit or loss and included in other income.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the spot exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in the statement of profit or loss, except for differences arising on the retranslation of fair value through other comprehensive income equity instruments which are recognised directly in other comperhensive income as part of fair value changes.

ii) Foreign operations:

The assets and liabilities of the overseas branches are translated into Bahraini Dinar at the spot exchange rate at the reporting date. The income and expenses of these overseas branches for the year are translated into Bahraini Dinar at average exchange rates. Differences resulting from the translation of the opening net investment in these overseas branches are recognised in other comprehensive income.

d. Use of estimates and management judgement
The Bank's financial statements and its financial results are influenced by accounting policies, assumptions, estimates and management judgement, which necessarily have to be made in the course of preparation of the financial statements.

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities. All estimates and assumptions required in conformity with IFRS are best estimates undertaken in accordance with the application of the standards. Estimates and judgements are evaluated on a continuous basis, and are based on past experience and other factors, including expectations with regard to future events.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure the fair value of the financal insturments.

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis to determine whether an impairment loss should be recorded in the statement of profit or loss.

Applicable from 1 January 2018

Refer to note 2.b.a.ii 'Changes to significant estimates and judgements'.

Applicable before 1 January 2018

The Bank makes judgements as to whether there is any observable data indicating an impairment trigger followed by measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the Bank. Management uses estimates based on historical loss experience for assets within credit risk characteristics and objective evidence of impairment similar to those in the portfolio to assess impairment.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period or in the period of the revision and future period if the revision affects both current and future periods.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

e. Accounting for income and expenses
i) Interest income and expenses are recognised in the statement of profit or loss on an accrual basis using the effective interest rate method.

The effective interest rate method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows through the expected life of the financial asset or liability or, where appropriate, a shorter period, to the net carrying amount of the financial asset or liability. The application of the effective interest rate method has the effect of recognising interest income and interest expense evenly in proportion to the amount outstanding over the period to maturity or repayment. In calculating the effective interest rate, cash flows are estimated taking into consideration all contractual terms of the financial instrument but excluding future credit losses.

ii) Fees and commissions that are integral to the effective interest rate of a financial asset or liability are included in the calculation of the effective interest rate. Other fees and commissions are recognised as the related services are performed or received, and are included in fee and commission income.

iii) Dividend income is recognised when the right to receive a dividend is established.

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

The Bank has different retirement benefit schemes for its employees in Bahrain and its overseas branches, which are in accordance with the relevant labour laws of the respective countries. The retirement benefit scheme is in the nature of a 'Defined Contribution Plan' for employees who are covered by the social insurance pension schemes in Bahrain and the overseas branches. Other employees are entitled to leaving indemnities payable in accordance with the employment agreements or under the respective labour laws, based on length of service and final remuneration. This liability is unfunded and is provided for on the basis of the cost had all such employees left at the statement of financial position date. The cost of providing these retirement benefits is charged to the statement of profit or loss.

The Bank has a voluntary employees saving scheme. The Bank and the employees contribute monthly on a fixed percentage of salaries basis to the scheme. The scheme is managed and administered by a board of trustees who are the employees of the Bank. The Bank's share of contribution to this scheme is charged to the statement of profit or loss.

v) Other expenses are recognised in the period in which they are incurred on an accrual basis.

f. Financial assets and liabilities

i. Recognition and initial measurement
The Bank initially recognised loans and advances and deposits on the date on which they are originated. A financial asset or financial liability is measured initially at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue.

ii. Classification
Applicable from 1 January 2018

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

– The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
– The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding ('SPPI').

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

– The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
– The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding ('SPPI').

On initial recognition of an equity investment that is not held for trading, the Bank may irrevocably elect to present subsequent changes in fair value in other comprehensive income. This election is made on an investment-by-investment basis.

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Notes to the Financial Statements (continued)
For the year ended 31 December

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Financial assets and liabilities (continued)

ii. Classification (continued)

Business model assessment
The Bank makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining practical interest rate profile, realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL.

Assessment whether contractual cash flows are solely payments of principal and interest
For the purposes of this assessment, principal is defined as the fair value of the financial asset on initial recognition. Interest is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

The Bank holds a portfolio of long-term fixed-rate loans for which the Bank has the option to propose to revise the interest rate at periodic reset dates. The reset rights are limited to the market rate at the time of revision. The borrowers have an option to either accept the revised rate or redeem the loan at par without penalty. The Bank has determined that the contractual cash flows of these loans are SPPI because the option varies the interest rate in a way that is consideration for the time value of money, credit risk, other basic lending risks and costs associated with the principal amount outstanding.

Applicable before 1 January 2018

Investments at fair value through profit or loss comprised of investments designated at inception at fair value though profit or loss and trading investments.

Investments designated at fair value through profit or loss: Investment securities which are acquired with an intent to hold for an indefinite period of time, and are managed, evaluated and reported internally on a fair value basis are designated as investments at fair value through profit or loss. These investments are carried at fair value based on quoted market prices, fund manager quotes or amounts derived from cash flow models as appropriate. Any unrealised gains and losses arising from changes in fair value are recognised in the statement of profit or loss.

Trading securities
Securities which are either acquired for the purpose of generating profit from short-term fluctuations in price or are included in a portfolio in which a pattern of short-term profit taking exists are categorised as trading securities. These securities are initially recognised at fair value and subsequently measured at fair value based on quoted market bid prices. Realised and unrealised gains and losses on trading securities are included in the statement of profit or loss.

Held-to-maturity investments
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank positively intends, and is able, to hold until maturity. Held-to-maturity investments are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest rate method, less any impairment losses.

Available-for-sale investments
Investments which are non-derivative and which are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity, changes in interest rates or concerns with respect to credit deterioration are categorised as available-for-sale investments. Available-for-sale investments which comprise both debt and equity investments are initially recognised at fair value, including transaction costs, and subsequently measured at fair value based on quoted market prices, brokers quotes or amounts derived from cash flow models as appropriate. Unrealised gains and losses arising from changes in the fair values of available-for-sale investments are recognised in other comprehensive income. The cumulative fair value adjustments on available-for-sale investments which are sold or otherwise disposed of and which had previously been recognised in other comprehensive inome are transferred to the statement of profit or loss.

The Bank classifies its financial liabilities, other than financial guarantees, as measured at amortised cost.

Notes to the Financial Statements (continued)
For the year ended 31 December

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Financial assets and liabilities (continued)

iii. Reclassifications

Applicable from 1 January 2018

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets.

Applicable before 1 January 2018

The categorisation of financial assets into fair value through profit or loss, available-for-sale and held-to-maturity is done on the basis of the management intent at the time these securities are acquired and laid down investment policies.

iv. Customer deposits
Customer deposits are initially recognised at their fair value and subsequently measured at their amortised cost using the effective interest rate method.

v. Financial guarantees
Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specific debtor fails to make payment when due in accordance with the contractual terms.

Financial guarantees are initially recognised at fair value (which is the premium received on issuance). The premium received is amortised over the life of the financial guarantee. The guarantee liability (the notional amount) is subsequently carried at the higher of this amortised amount and the present value of any expected payment (when a payment under the guarantee has become probable). The unamortised portion of the premium on these financial guarantees is included under other liabilities.

vi. Derivative financial instruments
All derivative financial instruments are initially recognised at cost, being the fair value at contract date, and are subsequently remeasured at their fair values. Fair values are obtained from quoted market prices in active markets including recent market transactions, and valuation techniques including discounted cash flow models and option pricing models as appropriate. Changes in the fair value of derivative financial instruments that do not qualify for hedge accounting are recognised in the same statement of profit or loss line as the hedged item. In the case of fair value hedges that meet the criteria for hedge accounting, any gain or loss arising from remeasuring the hedging instruments to fair value as well as the related changes in fair value of the item being hedged are recognised in the statement of profit or loss under other income.

In the case of cash flow hedges that meet the criteria of hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognised directly in equity and the ineffective portion, if any, is recognised in the statement of profit or loss.

All derivative financial instruments are recognised in the statement of financial position as either assets (positive fair values) or liabilities (negative fair values).

vii. Repos and reverse repos
Where securities are sold subject to a commitment to repurchase them at a specified future date (repo) and at a predetermined price, they are not derecognised and the consideration received is classified as borrowings under repurchase agreements. The difference between the sale and repurchase price is treated as an interest expense and accrued over the life of the repo agreement using the effective yield method. Conversely, securities purchased under a commitment to resell them at a specified future date (reverse repo) and at a predetermined price are not recognised on the statement of financial position and the consideration paid is recorded in placements with banks and other financial institutions. The difference between the purchase and resale price is treated as an interest income and accrued over the life of the reverse repo agreement using the effective interest rate method.

viii. Cash and cash equivalents
Cash and cash equivalents comprise cash, balances at central banks excluding mandatory cash reserves, placements with banks and other financial institutions that mature within three months of the date of placement, and short-term highly liquid investments that are readily convertible to cash and which are subject to an insignificant risk of change in value and mature within three months of the date of acquisition and are used by the Bank in the management of its short-term commitments.

ix. Fair value measurement
Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of a financial instrument using quoted market prices in an active market for that instrument. This includes listed equity and debt securities. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

For unlisted debt securities the fair value is based on brokers quotes, recent arm's length transactions between knowledgeable, willing parties (if available) and discounted cash flow analyses with accepted economic methodologies for pricing financial instruments.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Financial assets and liabilities (continued)

x. Identification and measurement of impairment

Applicable from 1 January 2018

The Bank recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

– Financial assets including loans and advances, debt instruments and placements;
– Financial guarantee contracts issued; and
– Loan commitments issued.

No impairment loss is recognised on equity investments.

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

– debt investment securities that are determined to have low credit risk at the reporting date; and
– other financial instruments on which credit risk has not increased significantly since their initial recognition.

Applicable before 1 January 2018

At each reporting date, the carrying amount of the Bank's financial assets not carried at fair value through profit or loss is reviewed to determine whether there is objective evidence that a specific asset may be impaired. A financial asset is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset that can be estimated reasonably. If any such evidence exists, the recoverable amount of the asset is estimated to determine the extent of impairment.

Objective evidence that financial assets are impaired include significant financial difficulty of the borrower or issuer, default or delinquency of a borrower, the restructuring of a loan or advance by the Bank on terms the Bank would not consider otherwise, indicators that a borrower or issuer will enter bankruptcy or the disappearance of an active market for a security.

Impairment losses on assets carried at amortised cost are measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset shall be reduced directly or through use of an allowance account. The amount of the loss shall be recognised in the statement of profit or loss. When a subsequent event causes the amount of impairment losses to decrease, the impairment loss is reversed through the statement of profit or loss.

The Bank considers evidence of impairment for loans and advances at both specific and collective levels.

All individually significant loans and advances are assessed for specific impairment. Specific provision for impairment, pertaining to individually significant impaired loans and advances, is determined based on the difference between the net carrying amount and the estimated recoverable amount of the loans and advances, measured at the present value of estimated future cash flows from such loans and advances and discounting them based on their original effective interest rate. If a loan has a floating interest rate, the discount rate is the current effective rate determined under the contract.

Impairment and uncollectability is also measured and recognised on a portfolio basis for a group of loans and advances with similar credit risk characteristics, that are not individually identified as impaired, on the basis of estimates of losses that have been incurred but not yet specifically identified within the loans and advances portfolio at the statement of financial position date. The estimates are based on internal risk ratings, historical default rates, rating migrations, loss severity, macroeconomic and other relevant factors with historic loss experience being adjusted to reflect the effect of prevailing economic and credit conditions.

Loans and advances are written off after all reasonable attempts at restructuring and possible courses of action to achieve recovery have been exhausted and the possibility of any further recovery is considered to be remote.

In case of debt securities classified as available-for-sale, the Bank assesses individually whether there is an objective evidence of impairment based on the same criteria as financial assets carried at amortised cost. The amount of impairment loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less impairment loss previously recognised in the statement of profit or loss. If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognised in the statement of profit or loss, then the impairment loss is reversed through the statement of profit or loss.

For an investment in an equity security classified as available-for-sale, a significant or prolonged decline in fair value below cost is an objective evidence of impairment. Where there is an objective evidence of impairment, the amount of impairment loss is measured as the difference between the acquisition cost and the current fair value, less any impairment loss previously recognised in the statement of profit or loss. Any subsequent recovery in fair value of an impaired available-for-sale equity security is recognised in other comprehensive income.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

f. Financial assets and liabilities (continued)

xi. Derecognition of financial assets and liabilities

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

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

If the terms of the financial assets are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised. If the cash flows of the renegotiated asset are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and the new financial asset is recognised at fair value. The impairment loss before an expected restructuring is measured as follows:

– If the expected restructuring will not result in derecognition of an existing asset, then the estimated cash flows arising from the modified financial asset are included in the measurement of the existing asset based on their expected timing and amounts discounted at the original effective interest rate of the existing financial asset.
– If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of derecognition. This amount is discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

g. Impairment of non-financial assets

At each statement of financial position date, the Bank reviews the carrying amounts of its non-financial assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the assets is estimated in order to determine the extent of the impairment loss, if any. Where it is not possible to estimate the recoverable amount of an individual asset, the Bank estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount.

An impairment loss is recognised in the statement of profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease. Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, such that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in the statement of profit or loss, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

h. Investment in associates

Associates are those entities in which the Bank has significant influence, but not control or joint control, over their financial and operating policies. Significant influence is presumed to exist when the Bank holds between 20 and 50 percent of the voting power of another entity. Associates are accounted for using the equity method and are recognised initially at cost, which includes the transaction costs. The financial statements of the Bank include its share of the income and expenses and equity movements of associates, after adjustments to align the accounting policies with those of the Bank, from the date that significant influence commences until the date that significant influence ceases. On cessation of significant influence, even if an investment in an associate becomes an investment in a joint venture, the entity does not re-measure the retained interest. When the Bank's share of losses exceeds its interest in an associate, the carrying amount of that interest is reduced to nil and the recognition of further losses is discontinued except to the extent that the Bank has an obligation or has made payments on behalf of the associate.

i. Property and equipment

Property and equipment are initially recorded at cost and subsequently stated at cost less accumulated depreciation and impairment losses. Land is not depreciated and is stated at cost at the date of acquisition. Where an item of property and equipment comprises major components having different useful lives, they are accounted for separately. The cost of an item of property and equipment comprises its purchase price and any costs directly attributable to bringing the asset to the location and condition necessary for it to be put to its intended use. Depreciation is charged to the statement of profit or loss on a straight-line basis over the estimated useful lives of the property and equipment. The estimated useful lives are as follows:

Buildings	20 to 40 years
Furniture and equipment	3 to 8 years

The residual value and the useful life of property and equipment are reviewed periodically and, if expectations differ from previous estimates, the change is recognised prospectively in the statement of profit or loss over the remaining estimated useful life of the property and equipment.

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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

k. Offsetting
Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank currently has a legally enforceable right to set-off the recognised amounts and the Bank intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

l. Settlement date accounting
All regular way purchases and sales of financial assets except for derivatives and assets classified as fair value through profit or loss are recognised on the settlement date i.e. the date the Bank receives or delivers the asset. Regular way purchases and sales are those that require delivery of assets within the time frame generally established by regulation or convention in the market place. Derivative and assets classified as fair value through profit or loss transactions are recognised on trade date, representing the date the Bank contracts to purchase or sell.

m. Proposed appropriations
Dividends and other proposed appropriations are recognised as a liability in the period in which they are approved by the shareholders.

n. Remuneration policy
Board of Directors - The remuneration of the Board of Directors is approved by the shareholders. In addition, directors are paid nominal fees for attending meetings of the sub-committees of the Board.

Employees - The remuneration primarily consists of monthly salaries and allowances. The Bank also has a discretionary profit sharing scheme based on the net income for the year and considering the employees' performance during the year.

The above is in compliance with the sound remuneration practices regulation of the Central Bank of Bahrain.

o. Segment reporting
An operating segment is a component of the Bank that engages in business activities from which it may earn revenue and incur expenses, including revenues and expenses that relate to transactions with any of the other components of the Bank. All operating results of the operating segments are reviewed regularly by the Chief Executive Officer to make decisions about resource allocation and assess its performance, and for which discrete financial information is available.

p. Earnings per share
The Bank presents basic earnings per share ('EPS') data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the year. Diluted earnings per share is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

q. Income tax liability
The Bank's operations in Bahrain and Abu Dhabi are not liable to income tax. The Bank's Riyadh branch is subject to income tax in accordance with the Saudi Income Tax Law. Income tax, if any, is charged to the statement of profit or loss.

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

s. Assets under management
The Bank acts as a trustee/manager and in other capacities that result in holding or placing of assets on behalf of a trust or other institution. These assets and income arising thereon are not included in the Bank's financial statements as they are not assets of the Bank.

3. FINANCIAL RISK MANAGEMENT

The Bank is exposed to the following types of risks:

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

3 . FINANCIAL RISK MANAGEMENT (CONTINUED)

Risk management framework
The overall authority for risk management in the Bank is vested with the Board of Directors. The Board authorises appropriate credit, liquidity, market, and operational risk policies based on the recommendation of the Board Risk Committee and Management of the Bank. The Bank has established various committees that review and assess all risk issues. Approval authorities are delegated to different functionaries in the hierarchy depending on the amount, type of risk and nature of operations or risk. The Risk Group of the Bank provides the necessary support to Senior Management and the business units in all areas of risk management. The Risk Group functions independent of the business units and reports directly to the Board Risk Committee and administratively to the Chief Executive Officer.

The Board Risk Committee is responsible for identifying and monitoring risks within the framework of the risk appetite established by the Board of Directors including reviewing and reporting its conclusions and recommendations to the Board on the Bank's current and future risk appetite, the Bank's risk management framework as well as the Bank's risk culture.

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

Credit risk
Credit risk represents the potential financial loss as a consequence of a customer's inability to honour the terms and conditions of a credit facility. Such risk is measured with respect to counterparties for both on-balance sheet assets and off-balance sheet items.

The Bank has well laid out procedures, not only to appraise but also to regularly monitor credit risk. Credit appraisal is based on the financial position of the borrower, performance projections, market position, industry outlook, external ratings (where available), track record, account conduct, repayment sources and ability, tangible and intangible security, etc. Regular reviews are carried out for each account and risks identified are mitigated in a number of ways, which include obtention of collateral, counter-guarantees from shareholders and/or third parties.

The Credit Risk Department of the Bank independently analyses risks and puts forth its recommendations prior to approval by the appropriate authorities for facilities above a specified threshold. In addition to rigorous credit analysis, the terms and conditions of all credit facilities are strictly implemented by the Credit Administration Department. An internal grading system and annual review process supports the identification of any deterioration in credit risk and consequent implementation of corrective action.

The Bank's internal ratings are based on a 16-point scale, which takes into account the financial strength of a borrower as well as qualitative aspects to arrive at a comprehensive snapshot of the risk of default associated with the borrower. Risk ratings assigned to each borrower are reviewed at least on an annual basis. Regular monitoring of the portfolio enables the Bank to identify accounts, which witness deterioration in risk profile. Consumer credit facilities which are granted based on pre-defined criteria such as salary assignment, maximum repayment obligation as a percentage of salary etc., are excluded from this rating system.

The Bank also uses the ratings by established rating agencies as part of the appraisal process while considering exposures to rated entities.

Liquidity risk
Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk management ensures that funds are available at all times to meet the funding requirements of the Bank.

The asset and liability management policies of the Bank define the proportion of liquid assets to total assets with the aim of minimising liquidity risk. The Bank maintains adequate liquid assets such as inter-bank placements, treasury bills and other readily marketable securities, to support its business and operations. The Treasury Department monitors the maturity profile of assets and liabilities so that adequate liquidity is maintained at all times. The Asset Liability Committee (ALCO) chaired by the Chief Executive Officer reviews the liquidity gap profile and the liquidity scenario and addresses strategic issues concerning liquidity.

Market risk
Market risk is the risk of potential losses arising from movements in market prices of interest rate related instruments and equities in the trading portfolio and foreign exchange and commodities holdings throughout the Bank. The Bank's trading activities are governed by policies that are clearly documented, by adherence to comprehensive limit structures set annually and by regular reviews. Quality and rating are the main criteria in selecting a trading asset. The Bank uses the standardised method under Basel III for allocating market risk capital based on the risk assessed for underlying factors of interest rate risk, equity risk, foreign exchange risk, options risk and commodity risk.

Operational risk
Operational risk is the risk of monetary loss on account of human error, fraud, system failures or the failure to record transactions. The Bank has well laid out procedures and systems that set out the methodologies for carrying out specific tasks. These systems and procedures are constantly reviewed and revised to address any potential risks. Additionally, new products and services are reviewed and assessed for operational risks prior to their implementation.

Capital management
The Bank's policy is to maintain sufficient capital to sustain investor, creditor and market confidence and to support future development of the business. The impact of the level of capital on the return on shareholder's equity is also recognised, and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Central Bank of Bahrain's ('CBB') Basel III guidelines outlining the capital adequacy framework for banks incorporated in the Kingdom of Bahrain. The framework emphasises common equity as the predominant component of tier 1 capital by adding a minimum common equity tier 1 ('CET') capital ratio. The Basel III rules also require institutions to hold capital buffers. For the purpose of calculating CET 1 capital, the regulatory adjustments (deductions) including amounts above the aggregate limit for significant investments in financial institutions, mortgage servicing rights, and deferred tax assets from temporary differences, will be deducted from CET1 over a phased manner to be fully deducted by 1 January 2019. The Bank's current capital position is sufficient to meet the regulatory capital requirements. The Bank ensures that the capital adequacy requirements are met on a consolidated basis and also with local regulator's requirements, if any, in the countries in which the Bank has branches. The Bank has complied with all regulatory capital requirements throughout the year.

Notes to the Financial Statements (continued)
For the year ended 31 December

4. CASH AND CASH EQUIVALENTS

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Cash and balances at central banks	**107.3**	**285.4**	107.0	284.7
Less: mandatory cash reserves	**(75.5)**	**(200.8)**	(83.3)	(221.6)
	31.8	**84.6**	23.7	63.0
Treasury bills (less than 3 months)	**19.3**	**51.2**	-	-
Placements with banks (less than 3 months)	**259.8**	**690.7**	171.5	456.1
	310.9	**826.5**	195.2	519.1

5. TREASURY BILLS

Treasury bills are short-term in nature and include treasury bills and Islamic Sukuk issued by the Government of Bahrain and the Government of Saudi Arabia.

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Government of Bahrain	**377.1**	**1,002.9**	409.9	1,090.2
Government of Saudi Arabia	**10.0**	**26.6**	10.0	26.6
	387.1	**1,029.5**	419.9	1,116.8

6. PLACEMENTS WITH BANKS AND OTHER FINANCIAL INSTITUTIONS

Placements with banks and other financial institutions are part of the Bank's money market activities and comprises short-term lending to banks and other financial institutions.

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Placements with banks	**257.8**	**685.5**	158.2	420.8
Placements with other financial institutions	**1.9**	**5.1**	15.8	42.0
	259.7	**690.6**	174.0	462.8

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Term placements	**244.5**	**650.2**	158.9	422.7
Current and call accounts	**15.2**	**40.4**	15.1	40.1
	259.7	**690.6**	174.0	462.8

7. LOANS AND ADVANCES

	2018		2017	
a) As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Loans and advances to non-banks	**1,157.3**	**3,078.1**	1,112.8	2,959.5
Loans and advances to banks	**82.2**	**218.5**	156.8	417.0
Less: provision for impairment	**(49.4)**	**(131.4)**	(42.7)	(113.6)
	1,190.1	**3,165.2**	1,226.9	3,262.9

b) As at 31 December 2018, the amount of floating rate loans for which interest was being reset by the Bank on agreed dates and based on an agreed fixed margin over a benchmark interest rate amounted to BHD 466.2 million (USD 1,239.9 million) [31 December 2017: BHD 612.7 million (USD 1,629.4 million)].

Notes to the Financial Statements (continued)
For the year ended 31 December

7. LOANS AND ADVANCES (CONTINUED)

c) In accordance with the Bank's policy and the Central Bank of Bahrain guidelines, loans on which payments of interest or repayments of principal are 90 days past due are immediately defined as non-performing. Any interest accrued is reversed and future interest is only recognised on a cash basis. The ageing schedule of non-performing loans and advances based on the time period since the last repayment of principal or interest by the customer, is as follows:

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Up to 3 months (subject to cooling off period)	**53.5**	**142.3**	-	-
Over 3 months to 1 year	**12.5**	**33.2**	25.7	68.3
1 to 3 years	**26.1**	**69.4**	13.3	35.5
Over 3 years	**9.2**	**24.5**	48.7	129.6
	47.8	**127.1**	87.7	233.4
	101.3	**269.4**	87.7	233.4
Fair market value of collateral	**132.8**	**353.2**	113.2	301.1
Stage 3/Specific provision for impairment	**(36.5)**	**(97.1)**	(30.2)	(80.5)

In accordance with the Central Bank of Bahrain guidelines, loans that have been classified as non-perfoming should remain classified as non-performing for a cooling off period of not less than 1 year from the date of becoming performing.

Loans that are past due below 90 days but not impaired are those for which contractual interest or principal payments are past due but the Bank believes that specific impairment is not appropriate on the basis of the level of security or collateral available and/or the stage of collection of amounts owed to the Bank. As at 31 December 2018, loans past due below 90 days but not impaired amounted to BHD 11.3 million (USD 29.9 million) [31 December 2017: BHD 9.9 million (USD 26.3 million)].

d) The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be de-recognised and the renegotiated loan recognised as a new loan.

The Bank renegotiates loans to customers as a result of changes in anticipated cash flows and/or in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. During 2018, credit facilities amounting to BHD 3.7 million (USD 9.8 million) were restructured (2017: BHD 0.1 million). Restructuring concessions mainly related to deferral of loan installments to assist customers overcome temporary cash flow situations or to realign the repayment with the borrower's revised cash flow projections, and amending the terms of loan covenants. Due to the minor nature of concessions, there was no significant impact on the Bank's impairment charge or the future earnings. In accordance with the Central Bank of Bahrain guidelines, loans that have been restructured should be reported as stage 2 for not less than 1 year from the date of restructuring.

e) The Bank holds collateral against loans and advances to customers in the form of lien over deposits, mortgage over properties and/or shares and sovereign/bank guarantees. Some of these collaterals are held through a special purpose vehicle. As at 31 December 2018, loans and advances amounting to BHD 292.1 million (USD 776.8 million) [31 December 2017: BHD 340.2 million (USD 904.8 million)] were fully collateralised and loans and advances amounting to BHD 44.4 million (USD 118.1 million) [31 December 2017: BHD 48.9 million (USD 130.1 million)] were partly collateralised with a collateral value of BHD 19.2 million (USD 51.0 million) [31 December 2017: BHD 29.2 million (USD 77.7 million)].

Notes to the Financial Statements (continued)
For the year ended 31 December

7. LOANS AND ADVANCES (CONTINUED)

f) Exposure to credit risk

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Total carrying amount	**1,190.1**	**3,165.2**	1,226.9	3,262.9
1. Individually impaired				
Substandard	**91.1**	**242.2**	77.7	206.8
Doubtful	**1.9**	**5.1**	1.9	5.1
Loss	**8.3**	**22.1**	8.1	21.5
Individually impaired	**101.3**	**269.4**	87.7	233.4
Stage 3/Specific provision for impairment	**(36.5)**	**(97.1)**	(30.2)	(80.5)
Individually impaired carrying amount	**64.8**	**172.3**	57.5	152.9
2. Past due below 90 days but not impaired				
Gross amount	**11.3**	**31.1**	9.9	26.3
Stage 1 or 2/Collective impairment provision	**(0.2)**	**(0.5)**	(0.1)	(0.3)
Past due but not impaired carrying amount	**11.1**	**30.6**	9.8	26.0
3. Neither past due nor impaired by internal rating				
Rated 1	**26.8**	**71.3**	55.9	148.6
Rated 2	**48.5**	**129.0**	4.9	13.0
Rated 3	**78.2**	**208.0**	81.9	217.9
Rated 4+ to 4-	**136.7**	**363.4**	107.2	285.1
Rated 5+ to 5-	**215.8**	**573.9**	199.2	529.8
Rated 6+ to 6-	**77.0**	**204.8**	129.7	345.1
Rated 7	**130.5**	**347.0**	171.9	457.2
Unrated	**413.4**	**1,098.7**	421.3	1,120.2
Gross amount	**1,126.9**	**2,996.1**	1,172.0	3,116.9
Stage 1 or 2/Collective impairment provision	**(12.7)**	**(33.8)**	(12.4)	(32.9)
Carrying amount of neither past due nor impaired	**1,114.2**	**2,962.3**	1,159.6	3,084.0
Total carrying amount	**1,190.1**	**3,165.2**	1,226.9	3,262.9

Unrated includes mainly consumer loans and other facilities that are not assigned any ratings at inception.

By staging **As at 31 December 2018**	**Stage 1 BHD millions**	**Stage 2 BHD millions**	**Stage 3 BHD millions**	**Total BHD millions**	**Total USD millions**
Loans and advances	**1,085.5**	**52.7**	**101.3**	**1,239.5**	**3,296.6**
Less: impairment provision	**(6.6)**	**(6.3)**	**(36.5)**	**(49.4)**	**(131.4)**
Net loans and advances	**1,078.9**	**46.4**	**64.8**	**1,190.1**	**3,165.2**

g) Impairment provisions on loans and advances
Impairment movement (IFRS9) - 2018

	Stage 1 BHD millions	**Stage 2 BHD millions**	**Stage 3 BHD millions**	**Total BHD millions**	**Total USD millions**
Impairment at 1 January 2018	**9.4**	**1.6**	**31.4**	**42.4**	**112.8**
Net transfer between stages	**(1.2)**	**(0.4)**	**1.6**	**-**	**-**
Write off during the year	**-**	**-**	**(2.2)**	**(2.2)**	**(5.9)**
Charge for the year (net)	**(1.6)**	**5.1**	**5.7**	**9.2**	**24.5**
Impairment at 31 December 2018	**6.6**	**6.3**	**36.5**	**49.4**	**131.4**

Notes to the Financial Statements (continued)
For the year ended 31 December

7. LOANS AND ADVANCES (CONTINUED)

g) Impairment provisions on loans and advances (continued)
Impairment movement (IAS39) - 2017

	Specific impairment provision BHD millions	Collective impairment provision BHD millions	Total impairment provisions BHD millions	Total impairment provisions USD millions
Impairment at 1 January 2017	36.5	13.0	49.5	131.7
Charge for the year (net)	9.2	1.2	10.4	27.7
Amounts written off against impairment provision	(17.3)	-	(17.3)	(46.0)
Transfers, recoveries & write backs	1.8	(1.7)	0.1	0.3
Impairment at 31 December 2017	30.2	12.5	42.7	113.7

8. INVESTMENT SECURITIES

i) Investment securities comprise the following:

As at 31 December 2018	**FVTPL BHD millions**	**FVOCI BHD millions**	**Amortised cost BHD millions**	**Total BHD millions**	**Total USD millions**
Quoted investments:					
Debt instruments	**-**	**301.6**	**-**	**301.6**	**802.1**
Equity instruments	**-**	**43.6**	**-**	**43.6**	**115.9**
Total quoted investments	**-**	**345.2**	**-**	**345.2**	**918.0**
Unquoted investments:					
Debt instruments	**-**	**-**	**775.5**	**775.5**	**2,062.4**
Equity instruments	**0.4**	**11.1**	**-**	**11.5**	**30.8**
Total unquoted investments	**0.4**	**11.1**	**775.5**	**787.0**	**2,093.2**
Total investment instruments	**0.4**	**356.3**	**775.5**	**1,132.2**	**3,011.2**

As at 31 December 2017	Held-for-Trading BHD millions	Available-for-sale BHD millions	Held-to-maturity BHD millions	Total BHD millions	Total USD millions
Quoted investments:					
Debt instruments	-	332.5	-	332.5	884.3
Equity instruments	-	52.5	-	52.5	139.7
Total quoted investments	-	385.0	-	385.0	1,024.0
Unquoted investments:					
Debt instruments	-	685.4	-	685.4	1,822.9
Equity instruments	0.2	10.9	-	11.1	29.5
Total unquoted investments	0.2	696.3	-	696.5	1,852.4
Investment instruments	0.2	1,081.3	-	1,081.5	2,876.4
Less: impairment provision	-	(14.2)	-	(14.2)	(37.8)
Net investment instruments	0.2	1,067.1	-	1,067.3	2,838.6

Notes to the Financial Statements (continued)
For the year ended 31 December

8. INVESTMENT SECURITIES (CONTINUED)

ii. Breakdown between repricing nature of debt instruments

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Fixed rate debt instruments	**484.0**	**1,287.1**	350.5	932.3
Floating rate debt instruments	**593.1**	**1,577.4**	667.4	1,774.9
	1,077.1	**2,864.5**	1,017.9	2,707.2

iii. Breakdown of debt instruments by rating

The ratings given below are by established rating agencies.

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
AAA	**13.8**	**36.7**	24.1	64.2
AA	**12.9**	**34.3**	13.3	35.3
A	**11.8**	**31.4**	21.7	57.8
BBB	**3.7**	**9.8**	3.7	9.9
BB	**7.0**	**18.6**	11.3	30.1
B	**1,014.9**	**2,699.1**	930.5	2,474.4
Unrated	**13.0**	**34.6**	13.3	35.5
	1,077.1	**2,864.5**	1,017.9	2,707.2

The debt instruments rated B primarily represent instruments issued by sovereigns.

As at 31 December 2018, all debt instruments were classified as stage 1.

iv. Investments designated as fair value through profit or loss
The Bank hold investment in managed funds designated as fair value through profit or loss amounting to BHD 0.4 million (USD 1.1 million) [2017: BHD 0.2 million (USD 0.7 million)]

9. INVESTMENT IN ASSOCIATES

The Bank has a 29.06% shareholding in Bahrain Islamic Bank B.S.C. The Bahrain Islamic Bank is incorporated in the Kingdom of Bahrain and operates under a retail banking license issued by the Central Bank of Bahrain and carries out banking and other financial trading activities.

The Bank has a 34.84% interest in The Benefit Company B.S.C. (c) incorporated in the Kingdom of Bahrain. The Benefit Company has been granted a license for ancillary services by the Central Bank of Bahrain to provide payment systems, Bahrain cheque truncation and other related financial services for the benefit of commercial banks and their customers in the Kingdom of Bahrain.

The Bank has a 24.27% interest in the units issued by the Bahrain Liquidity Fund ('BLF'). BLF was set up in 2016 as an open ended fund registered as Private Investment Undertaking ('PIU') as per Central Bank of Bahrain rulebook volume 7. The main objective of ('BLF') is to add liquidity to Bahrain Bourse, which over a period of time should result in enhancing investor confidence in the market's listed securities.

The Bank has recognised the above investments as equity accounted associates in accordance with IAS 28 'Investment in associates'.

	2018		2017	
	BHD millions	**USD millions**	BHD millions	USD millions
Opening balance	**51.6**	**137.2**	50.1	133.2
Impact of adopting IFRS 9 by associates	**(4.1)**	**(10.9)**	-	-
At 1 January	**47.5**	**126.3**	50.1	133.2
Share of profit	**5.4**	**14.4**	3.8	10.0
Dividends received	**(1.2)**	**(3.2)**	(2.3)	(6.1)
Other movements	**(0.1)**	**(0.3)**	-	0.1
At 31 December	**51.6**	**137.2**	51.6	137.2

Shares of Bahrain Islamic Bank are listed on the Bahrain Bourse and the quoted price on 31 December 2018 was BHD 0.130 (31 December 2017: BHD 0.150). The estimated fair value of the investment based on this price was BHD 40.2 million (USD 106.9 million) [(31 December 2017: BHD 44.2 million) (USD 117.5 million)].

The financial statements of the associates used for applying the equity accounting are at of 30 September which is different from the reporting date of the Bank. Accordingly, amounts have been adjusted for material transactions, if any, for the period from 30 September to the Bank's reporting date.

Notes to the Financial Statements (continued)
For the year ended 31 December

10. INTEREST RECEIVABLE AND OTHER ASSETS

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Interest receivable	**28.9**	**76.9**	24.3	64.7
Accounts receivable & prepayments	**6.4**	**17.0**	9.0	23.8
Positive fair value of derivatives	**10.2**	**27.1**	4.2	11.1
Others	**5.4**	**14.4**	4.3	11.5
	50.9	**135.4**	41.8	111.1

Others included BHD 5.2 million (USD 14.0 million) [31 December 2017: BHD 4.2 million (USD 11.1 million)] in respect of land and buildings acquired from customers and now held for disposal. The land and buildings are stated at lower of cost and net realisable value.

11. DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

Due to banks and other financial institutions consists of short-term borrowings from banks and other financial institutions.

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Current and call accounts	**30.5**	**81.2**	54.1	143.8
Term deposits	**350.9**	**933.2**	329.9	877.5
	381.4	**1,014.4**	384.0	1,021.3

As at 31 December 2018 and 31 December 2017 the Bank was a net contributor into the treasury bill and interbank money markets.

12. BORROWINGS UNDER REPURCHASE AGREEMENTS

Borrowings under repurchase agreements amounted to BHD 103.9 million (USD 276.3 million) [31 December 2017: BHD 67.8 million (USD 180.4 million)] and the fair value of the investment securities pledged as collateral amounted to BHD 119.4 million (USD 317.6 million) [31 December 2017: BHD 71.9 million (USD 191.3 million)].

13. CUSTOMER DEPOSITS

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Repayable on demand or at short notice	**1,181.5**	**3,142.4**	1,223.9	3,255.0
Term deposits	**1,009.1**	**2,683.7**	941.3	2,503.6
	2,190.6	**5,826.1**	2,165.2	5,758.6

14. INTEREST PAYABLE AND OTHER LIABILITIES

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Interest payable	**23.0**	**61.2**	18.8	50.0
Employee benefits	**10.3**	**27.4**	9.4	24.9
Creditors and account payables	**3.2**	**8.5**	3.0	8.0
Deferred income	**3.1**	**8.2**	1.4	3.6
Negative fair value of derivatives	**0.7**	**1.9**	1.1	3.0
Others	**3.5**	**9.3**	2.9	7.7
	43.8	**116.5**	36.6	97.2

15. NET IMPAIRMENT PROVISIONS

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Loans and advances (note 7g)	**9.2**	**24.5**	10.5	27.8
Investment securities – (debt instruments)	**(1.3)**	**(3.5)**	-	-
Loan commitments and guarantees	**(2.3)**	**(6.1)**	-	-
	5.6	**14.9**	10.5	27.8

Notes to the Financial Statements (continued)
For the year ended 31 December

16. CONTINGENT LIABILITIES AND BANKING COMMITMENTS

The Bank issues commitments to extend credit and guarantees the performance of customers by issuing standby letters of credit and guarantees to third parties. For these instruments, the contractual amount of the financial instrument represents the maximum potential credit risk if the counterparty does not perform according to the terms of the contract. The credit exposure for the contingent liabilities is reduced by obtaining counter guarantees and collateral from third parties. A large majority of these expire without being drawn upon, and as a result, the contractual amounts are not representative of the actual future credit exposure or liquidity requirements of the Bank.

Based upon the level of fees currently charged, taking into account maturity and interest rates together with any changes in the credit worthiness of counterparties since origination, the Bank has determined that the fair value of contingent liabilities and undrawn loan commitments is not material.

	2018		2017	
	BHD millions	USD millions	BHD millions	USD millions
Contingent liabilities				
Liabilities on confirmed documentary credits	27.9	74.2	33.6	89.3
Guarantees :				
Counter guaranteed by banks	39.9	106.1	48.7	129.4
Others	112.0	297.9	117.2	311.8
	179.8	478.2	199.5	530.5
Banking commitments				
Undrawn loan commitments	15.1	40.2	82.9	220.4
Forward commitments:				
Interbank placing	18.8	50.0	8.0	21.3
	33.9	90.2	90.9	241.7
	213.7	568.4	290.4	772.2

17. DERIVATIVE AND FOREIGN EXCHANGE FINANCIAL INSTRUMENTS

The Bank utilises various derivative and foreign exchange financial instruments for trading, asset/liability management and hedging risks. These instruments primarily comprise futures, forwards, swaps and options.

Futures and forward contracts are commitments to buy or sell financial instruments or currencies on a future date at a specified price or yield, and may be settled in cash or through delivery. Swap contracts are commitments to settle in cash on a future date or dates, interest rate commitments or currency amounts based upon differentials between specified financial indices, as applied to a notional principal amount. Option contracts give the acquirer, for a fee, the right but not the obligation, to buy or sell within a limited period a financial instrument or currency at a contracted price.

In respect of the derivative and foreign exchange financial instruments, the contract/notional principal amounts do not represent balances subject to credit or market risk. Contract/notional principal amounts represent the volume of outstanding transactions and are indicators of business activity. These amounts are used to measure changes in the value of derivative products and to determine the cash flows to be exchanged. The replacement cost is the cost of replacing those financial instruments with a positive market value, together with an estimate for the potential future change in the value of the contract, and reflects the maximum credit loss for the Bank had all these counterparties defaulted. For written options, there is no credit risk, as they represent obligations of the Bank. The fair value represents the aggregate of the positive and negative cash flows which would have occurred if the rights and obligations arising from the instrument were extinguished by the Bank in an orderly market as at the reporting date. The fair values of derivative financial instruments such as interest rate swaps and forward rate agreements were calculated using discounted cash flow models based on current market yields for similar types of instruments and the maturity of each instrument. The futures contracts, foreign exchange contracts and interest rate options were revalued using market prices and option valuation models as appropriate.

a) The following table summarises for each type of derivative and foreign exchange financial instrument, the aggregate notional amounts, the replacement cost and the fair value:

In BHD millions	Notional principal amount		Replacement cost		Fair value	
As at 31 December	**2018**	2017	**2018**	2017	**2018**	2017
Interest rate contracts						
Interest rate swaps	630.2	651.3	4.2	2.2	4.1	2.2
Foreign exchange contracts						
Outright spot and forward contracts	201.2	293.2	1.0	0.9	0.7	0.3
Swap agreements	1,874.1	490.2	5.0	1.2	4.7	0.6
Options	-	0.9	-	-	-	-
	2,075.3	784.3	6.0	2.0	5.4	0.9
Total in BHD millions	2,705.5	1,435.6	10.2	4.2	9.5	3.1
Total in USD millions	7,195.5	3,818.1	27.1	11.1	25.3	8.1

Notes to the Financial Statements (continued)
For the year ended 31 December

17. DERIVATIVE AND FOREIGN EXCHANGE FINANCIAL INSTRUMENTS (CONTINUED)

b) The remaining maturity profile by each class of derivative and foreign exchange financial instrument based on contract/notional principal amounts is as follows:

In BHD millions	2018			2017		
As at 31 December	**Up to 1 year**	**Over 1 year**	**Total**	Up to 1 year	Over 1 year	Total
Interest rate contracts						
Interest rate swaps	-	630.2	630.2	-	651.2	651.2
Foreign exchange contracts						
Outright spot and forward contracts	191.1	10.0	201.2	219.2	74.0	293.2
Swap agreements	1,874.1	-	1,874.1	490.3	-	490.3
Options	-	-	-	0.9	-	0.9
	2,065.2	10.0	2,075.3	710.4	74.0	784.4
Total In BHD millions	2,065.2	640.2	2,705.5	710.4	725.2	1,435.6
Total in USD millions	5,492.7	1,702.7	7,195.4	1,889.3	1,928.8	3,818.1

18. CAPITAL EXPENDITURE COMMITMENTS

At 31 December 2018 commitments for capital expenditure amounted to BHD 1.4 million (USD 3.7 million) [31 December 2017: BHD 1.00 million (USD 2.7million)].

19. PROPERTY AND EQUIPMENT

	Land BHD millions	Buildings BHD millions	Furniture and equipment BHD millions	Total BHD millions	Total USD millions
Cost	1.0	26.2	12.7	39.9	106.0
Accumulated depreciation	-	(18.8)	(4.5)	(23.3)	(61.9)
Net book value at 31 December 2018	1.0	7.4	8.2	16.6	44.1
Net book value at 31 December 2017	1.0	7.5	4.5	13.0	34.7

The depreciation charge for 2018 amounted to BHD 2.0 million (USD 5.4 million) [2017: BHD 1.8 million (USD 4.7 million)]. The above included capital work in progress at cost, amounting to BHD 1.4 million (USD 3.7 million) [2017: BHD 0.9 million (USD 2.4 million)]

20. SHARE CAPITAL

	2018		2017	
	BHD millions	USD millions	BHD millions	USD millions
Authorised share capital				
1,500,000,000 (2017: 1,500,000,000) ordinary shares of 100 fils each	150.0	398.9	150.0	398.9
Issued and fully paid share capital				
At 1 January 1,275,448,416 ordinary shares of 100 fils each (at 1 January 2017: 1,159,498,560 shares of 100 fils each)	127.5	339.2	115.9	308.4
Bonus issue (one for ten shares held)	12.8	33.9	11.6	30.8
At 31 December 1,402,993,257 ordinary shares of 100 fils each (at 31 December 2017: 1,275,448,416 shares of 100 fils each)	140.3	373.1	127.5	339.2

The shareholders annual general ordinary and extra ordinary meetings for the year 2017 held on 7 March 2018 approved the increase of issued and fully paid capital by the issue of bonus shares at the rate of one additional share for every ten shares held and amounted to BHD 12.8 million.

The Board of Directors has proposed to increase the authorised share capital. In addition, the Board of Directors has proposed to increase the issued and fully paid capital of the Bank to BHD 154.3 million by the issue of bonus shares at the rate of one additional share for every ten shares held amounting to BHD 14.0 million. These shares will rank pari passu with all other shares for future dividends and distribution. This bonus issue is proposed to be made through utilisation of BHD 14.0 million from the general reserve.

20. SHARE CAPITAL (CONTINUED)

The distribution of ordinary shares, setting out the number of shares and shareholders and percentage of total outstanding shares in the following categories, is shown below:

As at 31 December	2018 Number of shares	2018 Number of shareholders	2018 % of total outstanding shares	2017 Number of shares	2017 Number of shareholders	2017 % of total outstanding shares
Less than 1%	**408,928,108**	**1,202**	**29.1%**	387,002,253	1,142	30.3%
1% up to less than 5%	**221,494,305**	**9**	**15.8%**	186,109,030	8	14.6%
5% up to less than 10%	**-**	**-**	**-**	-	-	-
10% up to less than 20%	**152,666,220**	**1**	**10.9%**	138,787,474	1	10.9%
20% up to less than 50%	**619,904,624**	**1**	**44.2%**	563,549,659	1	44.2%
	1,402,993,257	**1,213**	**100.0%**	1,275,448,416	1,152	100.0%

The distribution of ordinary shares ownership based on nationality of the shareholder is shown below:

As at 31 December	2018 Number of shares	2018 Number of shareholders	2018 % of total outstanding shares	2017 Number of shares	2017 Number of shareholders	2017 % of total outstanding shares
Bahraini	**1,346,956,717**	**1,126**	**96.0%**	1,233,139,708	1,069	96.7%
Other GCC countries	**55,734,765**	**73**	**4.0%**	42,090,218	74	3.3%
Others	**301,775**	**14**	**-**	218,490	9	-
	1,402,993,257	**1,213**	**100.0%**	1,275,448,416	1,152	100.0%

44.2% of the Bank's share capital is held by the Bahrain Mumtalakat Holding Co, which is 100% owned by the Government of Bahrain. 10.9% of shares is owned by the Social Insurance Organisation, Kingdom of Bahrain. The rest of the share capital is widely held primarily by the citizens of, and entities incorporated, in the Kingdom of Bahrain.

Employee share incentive scheme

The employee share incentive scheme ('Scheme') was approved at the ordinary general meeting on 11 March 2015 in pursuant to CBB's Sound Remuneration Practices regulation. As a result, 19,104,000 ordinary shares amounting to BHD 1.91 million were issued in 2015 to an independent party to hold the beneficial interest of the shares under the scheme. Shares are allocated to the employees under the scheme. The allocated share under the scheme are entitled to cash and stock dividend and subject to malus and clawback provisions of the scheme. As at 31 December 2018 there were 15,033,197 (2017: 15,659,167) shares unallocated. These unallocated shares under the scheme are deducted from equity.

21. RESERVES

a) Statutory reserve

In accordance with the Bahrain Commercial Companies Law 2001, 10% of net profit is appropriated to a statutory reserve, which is not normally distributable except in accordance with Article 224 of the law. Such appropriations may cease when the reserve reaches 50% of paid up share capital. The Board of Directors has proposed to the shareholders to appropriate BHD 7.0 million from the general reserve to the statutory reserve.

b) General reserve

The reserve has been created in accordance with the Bank's articles of association and underlines the shareholders' commitment to enhance the strong equity base of the Bank.

c) Fair value reserve

The fair value reserve includes the cumulative net change in fair value of fair value through other comprehensive income (IAS39: available-for-sale investments, excluding impairment losses, until the investment is derecognised or impaired). The fair value reserve also includes the Bank's share of other comprehensive income of associates.

d) Donation and charity reserve

Based on the recommendations of the Board of Directors, upon shareholders' approval an amount is transferred from the profit for the year to this donation and charity reserve. The reserve represents the amount of donations pending utilisation.

e) Share premium

Under the employee share incentive scheme, the Bank has allocated 7,244,494 ordinary shares with a nominal value of BHD 0.72 million to the employees, which has resulted in share premium of BHD 5.0 million.

22. APPROPRIATIONS

The appropriations relating to the year 2017 were approved at the annual general meeting held on 7 March 2018.

23. INTEREST INCOME / INTEREST EXPENSE

a) Interest income

For the year ended 31 December	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
Loans and advances to non banks	**50.7**	**134.9**	39.1	103.7
Loans and advances to banks	**5.6**	**14.9**	4.4	11.7
Treasury bills	**15.5**	**41.2**	13.6	36.2
Placements with banks and other financial institutions	**1.4**	**3.7**	1.4	3.7
Investment securities	**51.7**	**137.5**	43.3	115.3
Derivative assets held for risk management	**1.9**	**5.1**	0.3	0.9
	126.8	**337.3**	102.1	271.5

b) Interest expense

For the year ended 31 December	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
Customer deposits	**28.0**	**74.5**	21.7	57.7
Due to banks and other financial institutions	**8.3**	**22.1**	6.1	16.1
Borrowings under repurchase agreements	**1.7**	**4.5**	0.5	1.4
Derivative liabilities held for risk management	**1.6**	**4.3**	0.7	2.0
	39.6	**105.4**	29.0	77.2

24. OTHER INCOME

For the year ended 31 December	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
a) Fees and commission income				
Fees and commission on loans and advances	**9.1**	**24.3**	11.3	30.1
Commission on sale of managed funds	**0.2**	**0.5**	0.2	0.4
Other fees and commission	**8.4**	**22.4**	7.7	20.4
Less: fees and commission paid	**(5.9)**	**(15.7)**	(5.1)	(13.4)
	11.8	**31.5**	14.1	37.5
b) Other operating income				
Profit on sale of available-for-sale investments (IAS39)	**-**	**-**	0.5	1.2
Gain on fair value through profit or loss investments	**0.8**	**2.1**	0.1	0.3
Dividend income	**3.4**	**9.0**	3.2	8.4
Profit on exchange dealing and transactions	**6.3**	**16.8**	5.2	13.7
Profit on trading securities and derivatives	**1.2**	**3.1**	0.4	1.2
Share of profit of associates	**5.4**	**14.4**	3.8	10.0
Other income	**1.3**	**3.4**	4.2	11.2
	18.4	**48.8**	17.3	46.0
	30.2	**80.3**	31.4	83.5

25. STAFF EXPENSES

For the year ended 31 December	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
Salaries, allowances and bonuses	**20.4**	**54.1**	17.1	45.4
Social security and gratuity	**2.0**	**5.3**	1.6	4.2
Housing and other benefits	**3.0**	**8.0**	2.2	5.9
Others	**0.6**	**1.7**	0.4	1.1
	26.0	**69.1**	21.3	56.6

Notes to the Financial Statements (continued)

For the year ended 31 December

26. SIGNIFICANT NET OPEN FOREIGN CURRENCY POSITIONS

As at 31 December	2018 BHD millions	2018 USD millions	2017 BHD millions	2017 USD millions
US Dollar (long position) - unhedged	**145.4**	**386.7**	65.1	173.3
Saudi Riyal (long position) - unhedged	**23.7**	**62.9**	0.6	1.7
UAE Dirhams (long position) - unhedged	**19.0**	**50.5**	1.4	3.7
Qatari Riyal (long position) - unhedged	**0.3**	**0.7**	6.6	17.5

All of the above currencies have a fixed rate of exchange against the US Dollar. The Bank did not have any significant net open positions as at 31 December 2018 or 31 December 2017.

27. RELATED PARTIES

Certain related parties (major shareholders, directors of the Bank and families and companies of which they are principal owners, key management personnel and associates) were customers of the Bank in the ordinary course of business. The transactions with these parties were made on an arm's length basis. Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Bank. Typically, key management personnel include the Chief Executive Officer and persons directly reporting to this position. Significant balances at the reporting date in regard to related parties and transactions during the year with related parties are as below:

The Bank qualifies as a government related entity under the definitions provided in IAS 24 as its significant shareholders is government owned. In addition to the government exposures reported below, in its normal course of business, the Bank provides commercial lending, liquidity management and other banking services to, and also avails services from, various semi governmental organisations and government owned companies in the Kingdom of Bahrain.

In BHD millions	Major shareholder and related entities		Directors and key personal management		Associates	
As at 31 December	**2018**	2017	**2018**	2017	**2018**	2017
Loans and advances	**162.9**	251.3	**7.1**	4.2	**-**	38.9
Treasury bills, including securities	**1,397.0**	1,353.8	**-**	-	**51.6**	51.6
Customer deposits	**186.4**	229.2	**43.7**	30.1	**9.3**	6.8
Contingent liabilities for irrevocable commitments, guarantees and other contingencies	**48.6**	92.4	**12.2**	10.7	**-**	-

In BHD millions **For the year ended 31 December**	**2018**	2017	**2018**	2017	**2018**	2017
Loans advanced	**98.9**	116.1	**1.9**	8.5	**-**	38.8
Loans repaid	**81.5**	79.6	**4.2**	14.9	**38.8**	-
Net (decrease) / increase in overdrafts	**(105.7)**	(36.5)	**5.2**	(3.4)	**-**	-
Treasury bills, bonds and equities purchased	**916.0**	742.2	**-**	-	**-**	-
Treasury bills, bonds and equities matured/sold	**872.8**	742.2	**-**	-	**-**	-
Interest income	**74.6**	59.6	**0.6**	0.2	**0.5**	0.7
Interest expense	**1.7**	1.6	**0.6**	0.2	**-**	-
Share of profit of associates	**-**	-	**-**	-	**5.4**	3.8
Dividend Income	**0.4**	0.3	**-**	-	**-**	-
Directors remuneration and sitting fees	**0.2**	0.2	**0.3**	0.3	**-**	-
Short-term employee benefits	**-**	-	**3.2**	3.0	**-**	-
Post employment retirement benefits	**-**	-	**0.3**	0.2	**-**	-

During the year, impairment provision of BHD 4.4 million (USD 11.7 million) [2017: BHD 6.4 million (USD 17.0 million)] have been recorded against outstanding balances with related parties.

Certain transactions were approved by the Board of Directors under Article 189(b) of the Commercial Companies Law in the financial year ended 31 December 2018 where the chairman, directors or managers had a direct or indirect interest in the contracts or transactions which have been approved by the Board.

28. ASSETS UNDER MANAGEMENT

Assets managed on behalf of customers to which the Bank does not have legal title were not included in the statement of financial position. At 31 December 2018, assets under management amounted to BHD 138.1 million (USD 367.3 million) [31 December 2017: BHD 107.8 million (USD 286.7 million)].

Notes to the Financial Statements (continued)
For the year ended 31 December

29. GEOGRAPHICAL DISTRIBUTION

In BHD millions	Assets		Liabilities		Off-balance sheet items	
As at 31 December	**2018**	2017	**2018**	2017	**2018**	2017
GCC	**3,020.5**	2,930.8	**2,536.8**	2,531.5	**2,128.9**	947.4
USA	**98.2**	125.6	**24.8**	26.8	**225.0**	226.4
Europe	**54.9**	8.1	**90.7**	39.1	**558.1**	540.8
Rest of the world	**21.9**	37.0	**67.4**	56.2	**7.2**	11.4
	3,195.5	3,101.5	**2,719.7**	2,653.6	**2,919.2**	1,726.0

Off-balance sheet items include contingent liabilities, banking commitments, derivatives and forward exchange contracts.

30. DISTRIBUTION BY SECTOR

In BHD millions	Assets		Liabilities		Off-balance sheet items	
As at 31 December	**2018**	2017	**2018**	2017	**2018**	2017
Government	**1,550.2**	1,606.4	**388.3**	444.0	**34.8**	70.2
Manufacturing / trading	**147.6**	134.0	**186.5**	149.7	**107.6**	73.2
Banks / financial institutions	**593.2**	605.6	**523.0**	511.5	**2,716.3**	1,517.3
Construction	**85.2**	77.6	**99.3**	97.9	**38.4**	35.6
Personal	**467.7**	422.9	**1,288.1**	1,231.7	**2.3**	2.3
Others	**351.6**	255.0	**234.5**	218.8	**19.8**	27.4
	3,195.5	3,101.5	**2,719.7**	2,653.6	**2,919.2**	1,726.0

Off-balance sheet items include contingent liabilities, banking commitments, derivatives and forward exchange contracts.

31. CONCENTRATION OF CREDIT RISK

The following is the concentration of credit risk by industry and geographical regions:

a) By Industry

In BHD millions	Government Bahrain	Government Other countries	Manufacturing / trading	Banks / financial institutions	Construction	Personal	Others	Total
Assets								
Balances at central banks	**-**	**-**	**-**	**80.3**	**-**	**-**	**-**	**80.3**
Treasury bills	**387.1**	**-**	**-**	**-**	**-**	**-**	**-**	**387.1**
Placements with banks and other financial institutions	**3.8**	**-**	**-**	**255.9**	**-**	**-**	**-**	**259.7**
Loans and advances	**114.7**	**-**	**138.0**	**103.3**	**84.2**	**466.8**	**283.1**	**1,190.1**
Investment securities - debt instruments	**1,005.8**	**20.8**	**-**	**39.3**	**-**	**-**	**11.2**	**1,077.1**
Interest receivable and other assets	**17.9**	**0.1**	**1.1**	**5.7**	**0.1**	**0.9**	**23.4**	**49.2**
Total assets	**1,529.3**	**20.9**	**139.1**	**484.5**	**84.3**	**467.7**	**317.7**	**3,043.5**
Contingent liabilities and banking commitments	**34.8**	**-**	**65.4**	**53.8**	**38.4**	**1.5**	**19.8**	**213.7**
Derivatives (replacement cost)	**2.0**	**-**	**-**	**7.9**	**-**	**0.3**	**-**	**10.2**

In BHD millions As at 31 December 2017	Government Bahrain	Government Other countries	Manufacturing / trading	Banks / financial institutions	Construction	Personal	Others	Total
Balances at central banks	-	-	-	88.2	-	-	-	88.2
Treasury bills	409.9	10.0	-	-	-	-	-	419.9
Placements with banks and other financial institutions	-	-	-	174.0	-	-	-	174.0
Loans and advances	219.4	-	123.2	186.3	76.8	422.1	199.1	1,226.9
Investment securities - debt instruments	919.4	31.7	1.9	53.4	-	-	11.5	1,017.9
Interest receivable and other assets	15.9	0.1	0.2	5.1	0.1	0.9	18.6	40.9
Total assets	1,564.6	41.8	125.3	507.0	76.9	423.0	229.2	2,967.8
Contingent liabilities and banking commitments	70.1	0.1	66.2	89.5	35.6	1.5	27.4	290.4
Derivatives (replacement cost)	-	-	0.1	3.7	-	0.3	-	4.2

The balances at the end of the year are representative of the position during the year and hence average balances have not been separately disclosed.

Notes to the Financial Statements (continued)

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31. CONCENTRATION OF CREDIT RISK (CONTINUED)

The above includes certain exposures to customers / counterparties which are in excess of 15% of the Bank's capital base. These have the approval of the Central Bank of Bahrain or are exempt exposures under the large exposures policy of the Central Bank of Bahrain. The table below gives details of these exposures as at 31 December 2018:

Counterparty	Counterparty type	Total exposure
Counterparty A	Sovereign	**1,420.4**
Counterparty B	Central bank	**176.5**
Counterparty C	Sovereign	**136.0**
Counterparty D	Sovereign	**85.5**

(b) By geographical regions:

In BHD millions As 31 December 2018	**GCC**	**USA**	**Europe**	**Rest of the world**	**Total**
Assets					
Balances at central banks	**80.3**	**-**	**-**	**-**	**80.3**
Treasury bills	**387.1**	**-**	**-**	**-**	**387.1**
Placements with banks and other financial institutions	**205.1**	**2.5**	**51.5**	**0.6**	**259.7**
Loans and advances	**1,099.0**	**83.7**	**-**	**7.4**	**1,190.1**
Investment securities-debt instruments	**1,053.9**	**9.4**	**-**	**13.8**	**1,077.1**
Interest receivable and other assets	**43.3**	**2.6**	**3.2**	**0.1**	**49.2**
Total assets	**2,868.7**	**98.2**	**54.7**	**21.9**	**3,043.5**
Contingent liabilities and banking commitments	**192.4**	**0.1**	**16.2**	**5.0**	**213.7**
Derivatives (replacement cost)	**5.4**	**0.9**	**3.9**	**-**	**10.2**

In BHD millions As at 31 December 2017	GCC	USA	Europe	Rest of the World	Total
Assets					
Balances at central banks	88.2	-	-	-	88.2
Treasury bills	419.9	-	-	-	419.9
Placements with banks and other financial institutions	163.7	3.9	5.1	1.3	174.0
Loans and advances	1,117.0	95.0	-	14.9	1,226.9
Investment securities-debt instruments	972.7	24.5	-	20.7	1,017.9
Interest receivable and other assets	35.8	2.2	2.8	0.1	40.9
Total assets	2,797.3	125.6	7.9	37.0	2,967.8
Contingent liabilities and banking commitments	264.2	0.1	22.9	3.2	290.4
Derivatives (replacement cost)	1.6	0.4	2.2	-	4.2

32. INTEREST RATE RISK

Interest rate risk is measured by the extent to which changes in the market interest rates impact margins, net interest income and the economic value of the Bank's equity. Net interest income will be affected as a result of volatility in interest rates to the extent that the re-pricing structure of interest bearing assets differs from that of liabilities. The Bank's goal is to achieve stable earnings growth through active management of the assets and liabilities mix while, selectively, positioning itself to benefit from near-term changes in interest rate levels. The Treasurer is primarily responsible for managing the interest rate risk. Reports on overall position and risks are submitted to senior management for review and positions are adjusted if deemed necessary. In addition, ALCO regularly reviews the interest rate sensitivity profile and its impact on earnings.

The Bank's asset and liability management process is utilised to manage interest rate risk through the structuring of on-balance sheet and off-balance sheet portfolios. The Bank uses various techniques for measuring and managing its exposure to interest rate risk. Duration analysis is used to measure the interest rate sensitivity of the fixed income portfolio. Duration of the portfolio is governed by economic forecasts, expected direction of interest rates and spreads. Modified duration gives the percentage change in value of the portfolio following a 1% change in yield. Interest rate swaps and forward rate agreements are used to manage the interest rate risk. The Bank uses interest rate gap analysis to measure the interest rate sensitivity of its annual earnings due to re-pricing mismatches between rate sensitive assets, liabilities and derivative positions.

Assets and liabilities are placed in maturity buckets based on the remaining period to the contractual repricing or maturity dates, whichever is earlier. Customer deposits for which no specific contractual maturity or repricing date exists are placed in ladders based on the Bank's judgement concerning their most likely repricing behaviour.

Notes to the Financial Statements (continued)

For the year ended 31 December

32. INTEREST RATE RISK (CONTINUED)

The repricing profile and effective interest rate of the various asset and liability categories are as follows:

In BHD millions As 31 December 2018	**Effective interest rate %**	**Up to 3 months**	**3 to 6 months**	**6 to 12 months**	**1 to 5 years**	**More than 5 years**	**Rate insensitive**	**Total**
Assets								
Cash and balances at central banks	**-**	**-**	**-**	**-**	**-**	**-**	**107.3**	**107.3**
Treasury bills	**3.6%**	**172.0**	**103.4**	**111.7**	**-**	**-**	**-**	**387.1**
Placements with banks and other financial institutions	**2.5%**	**244.5**	**-**	**-**	**-**	**-**	**15.2**	**259.7**
Loans and advances	**4.4%**	**364.9**	**61.4**	**130.6**	**510.4**	**122.8**	**-**	**1,190.1**
Investment securities	**4.8%**	**1.9**	**4.3**	**194.5**	**625.9**	**250.5**	**55.1**	**1,132.2**
Investment in associates, interest receivable and other assets	**-**	**-**	**-**	**-**	**-**	**-**	**102.5**	**102.5**
Property and equipment	**-**	**-**	**-**	**-**	**-**	**-**	**16.6**	**16.6**
Total assets		**783.3**	**169.1**	**436.8**	**1,136.3**	**373.3**	**296.7**	**3,195.5**
Liabilities and equity								
Due to banks and other financial institutions	**2.2%**	**350.1**	**-**	**0.8**	**-**	**-**	**30.5**	**381.4**
Borrowings under repurchase agreements	**2.4%**	**103.9**	**-**	**-**	**-**	**-**	**-**	**103.9**
Customer deposits	**1.3%**	**786.0**	**165.0**	**263.8**	**47.9**	**-**	**927.9**	**2,190.6**
Interest payable and other liabilities	**-**	**-**	**-**	**-**	**-**	**-**	**43.8**	**43.8**
Equity	**-**	**-**	**-**	**-**	**-**	**-**	**475.8**	**475.8**
Total liabilities and equity		**1,240.0**	**165.0**	**264.6**	**47.9**	**-**	**1,478.0**	**3,195.5**
On-balance sheet interest rate sensitivity gap		**(456.7)**	**4.1**	**172.2**	**1,088.4**	**373.3**	**(1,181.3)**	**-**
Off-balance sheet interest rate gap		**630.2**	**-**	**(6.3)**	**(408.1)**	**(215.8)**	**-**	**-**
Cumulative interest rate sensitivity gap		**173.5**	**177.6**	**343.5**	**1,023.8**	**1,181.3**	**-**	**-**

In BHD millions As at 31 December 2017	*Effective interest rate %*	Up to 3 months	3 to 6 months	6 to 12 months	1 to 5 years	More than 5 years	Rate insensitive	Total
Assets								
Cash and balances at central banks	-	-	-	-	-	-	107.0	107.0
Treasury bills	*3.0%*	134.4	145.8	139.7	-	-	-	419.9
Placements with banks and other financial institutions	*1.5%*	158.9	-	-	-	-	15.1	174.0
Loans and advances	*3.8%*	529.8	31.6	78.6	492.1	94.7	-	1,226.8
Investment securities	*4.4%*	47.5	-	55.4	617.0	298.0	49.4	1,067.3
Investment in associates, interest receivable and other assets	-	-	-	-	-	-	93.4	93.4
Property and equipment	-	-	-	-	-	-	13.1	13.1
Total assets		870.6	177.4	273.7	1,109.1	392.7	278.0	3,101.5
Liabilities and equity								
Due to banks and other financial institutions	*1.7%*	329.9	-	-	-	-	54.1	384.0
Borrowings under repurchase agreements	*1.8%*	67.8	-	-	-	-	-	67.8
Customer deposits	*1.1%*	695.2	167.2	269.4	48.4	-	985.0	2,165.2
Interest payable and other liabilities	-	-	-	-	-	-	36.6	36.6
Equity	-	-	-	-	-	-	447.9	447.9
Total liabilities and equity		1,092.9	167.2	269.4	48.4	-	1,523.6	3,101.5
On-balance sheet interest rate sensitivity gap		(222.3)	10.2	4.3	1,060.7	392.7	(1,245.6)	-
Off-balance sheet interest rate gap		651.3	-	-	(378.1)	(273.2)	-	-
Cumulative interest rate sensitivity gap		429.0	439.2	443.5	1,126.1	1,245.6	-	-

Notes to the Financial Statements (continued)
For the year ended 31 December

33. MARKET RISK

a) The Bank uses the standardised method for allocating market risk capital.

The following table shows the capital charges as at 31 December:

Risk type

In BHD millions	**2018**	2017
Interest rate risk	**4.0**	1.3
Foreign exchange risk	**-**	-
Total minimum capital required for market risk	**4.0**	1.3
Multiplier	**12.5**	12.5
Market risk weighted exposure under the standardised method	**50.2**	16.1

b) The principal risk to which the Bank portfolio is exposed is the risk of loss from fluctuations in future cash flows of financial instruments because of changes in the market interest rates. The interest rate risk management process is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to an interest rate shock of 200bps increase/ decrease. An analysis of the Bank's sensitivity to an increase or decrease in market interest rates on the Bank's balance sheet (assuming no asymmetrical movement in yield curves and a constant balance sheet position) is as follows:

	2018		2017	
In BHD millions	**200 bps parallel increase**	**200 bps parallel decrease**	200 bps parallel increase	200 bps parallel decrease
At 31 December	**5.6**	**(5.6)**	10.0	(10.0)
Average for the year	**6.2**	**(6.2)**	10.5	(10.5)
Minimum for the year	**3.6**	**(3.6)**	8.6	(8.6)
Maximum for the year	**10.4**	**(10.4)**	12.2	(12.2)

c) The Bank holds investments in quoted equities as part of investment securities. Equity risk is the potential adverse impact due to movements in individual equity prices or general market movements in stock markets. The Bank manages this risk through diversification of investments in terms of geographical distribution and industrial concentration.

Overall non-trading interest rate risk positions are managed by the treasury division, which uses investment securities, placements with banks, deposits from banks and derivative instruments to manage the overall position arising from the Bank's non-trading activities. The use of derivatives to manage interest rate risk is described in note 17.

34. SEGMENT INFORMATION

For management purposes, the Bank is organised into the following main strategic business units ('SBUs') - Retail Commercial and SMEs, Corporate, Institutional and Investment Banking, Overseas Branches and Treasury, Capital Markets and Wealth Management. These SBUs are the basis on which the Bank reports its operating segment information.

The Personal Banking and Bahrain Business Banking SBUs provide various banking products and services to the Bank's customers in Bahrain. The SBUs are differentiated based on their respective customer segments. Retail, Commercial and SMEs caters to individuals and commercial enterprises, while Corporate, Institutional and Investment Banking caters to governments and corporates.

The Treasury, Capital Markets and Wealth Management SBU has the overall responsibility of managing the Bank's liquidity, interest rate, foreign exchange and market risk and the Overseas Branches SBU provide various banking products and services to the Bank's customers outside Bahrain.

Notes to the Financial Statements (continued)
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34. SEGMENT INFORMATION (CONTINUED)

Financial information about the operating segments is presented in the following table:

In BHD millions	**Retail, Commercial & SMEs**		**Corporate, Institutional & Investment Banking**		**Overseas Branches**		**Treasury, Capital Markets & Wealth Management**		**Total**	
For the year ended 31 December	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017	**2018**	2017
Interest income	**28.3**	25.0	**26.1**	16.9	**2.4**	1.8	**70.0**	58.4	**126.8**	102.1
Interest expense	**(14.8)**	(10.6)	**(12.9)**	(10.8)	**(0.2)**	(0.3)	**(11.7)**	(7.3)	**(39.6)**	(29.0)
Inter-segment interest income/(expense)	**25.7**	16.8	**4.7**	4.9	**0.2**	-	**(30.6)**	(21.7)	**-**	-
Net interest income	**39.2**	31.2	**17.9**	11.0	**2.4**	1.5	**27.7**	29.4	**87.2**	73.1
Other income	**8.3**	11.5	**2.8**	5.5	**1.2**	1.2	**17.9**	13.2	**30.2**	31.4
Operating income	**47.5**	42.7	**20.7**	16.5	**3.6**	2.7	**45.6**	42.6	**117.4**	104.5
Result	**24.8**	24.6	**7.6**	1.2	**0.2**	(0.6)	**41.0**	38.6	**73.6**	63.8
Unallocated corporate expenses									**(3.6)**	(2.7)
Profit for the year									**70.0**	61.0
Other information										
As at 31 December										
Segment assets	**615.5**	544.5	**649.1**	731.0	**67.0**	69.5	**1,863.9**	1,756.5	**3,195.5**	3,101.5
Segment liabilities & equity	**1,386.3**	1,406.7	**831.3**	903.0	**38.1**	40.0	**939.8**	751.8	**3,195.5**	3,101.5
For the year ended 31 December										
Depreciation for the year	**0.7**	0.5	**0.3**	0.3	**0.3**	0.4	**-**	-	**1.3**	1.2
Provision for impaired assets	**1.4**	0.9	**5.1**	9.5	**(0.8)**	0.1	**(0.2)**	-	**5.6**	10.5

Segment revenues and expenses are directly attributable to the business segments. The benefit of the Bank's capital has been distributed across the segments in proportion to their total assets employed. Expenses of departments whose services are jointly utilised by more than one segment have been allocated to the relevant segments on an appropriate basis.

Inter-segment interest income and expense represent the interest cost on the excess funds which are transferred by all the other business segments to Treasury, Capital Markets & Wealth Management. The interest rate for calculating interest of such transfers is set once every three months separately for local and foreign currency and is based on the weighted average of market rates for various maturities for each currency.

35. MATURITY PROFILE AND LIQUIDITY RISK

a) Maturity profile

The table below shows the maturity profile of total assets and liabilities based on contractual terms.

In BHD millions As 31 December 2018	**Up to 3 months**	**3 to 6 months**	**6 months to 1 year**	**1 to 3 years**	**3 to 5 years**	**5 to 10 years**	**10 to 20 years**	**Over 20 years**	**Total**
Assets									
Cash and balances at central banks	**107.3**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**107.3**
Treasury bills	**172.0**	**103.4**	**111.7**	**-**	**-**	**-**	**-**	**-**	**387.1**
Placements with banks and other financial institutions	**259.7**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**259.7**
Loans and advances	**267.8**	**57.9**	**152.3**	**284.7**	**272.1**	**129.2**	**23.7**	**2.4**	**1,190.1**
Investment securities	**1.8**	**4.3**	**194.4**	**493.4**	**206.9**	**176.3**	**-**	**55.1**	**1,132.2**
Investment in associates, interest receivable, other assets and property & equipment	**5.7**	**0.2**	**2.3**	**12.9**	**4.6**	**3.5**	**-**	**89.9**	**119.1**
Total assets	**814.3**	**165.8**	**460.7**	**791.0**	**483.6**	**309.0**	**23.7**	**147.4**	**3,195.5**
Liabilities and equity									
Due to banks and other financial institutions	**380.6**	**-**	**0.8**	**-**	**-**	**-**	**-**	**-**	**381.4**
Borrowings under repurchase agreements	**103.9**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**103.9**
Customer deposits	**1,713.0**	**165.3**	**263.9**	**48.4**	**-**	**-**	**-**	**-**	**2,190.6**
Interest payable & other liabilities	**25.1**	**2.3**	**1.3**	**15.1**	**-**	**-**	**-**	**-**	**43.8**
Equity	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**475.8**	**475.8**
Total liabilities and equity	**2,222.6**	**167.6**	**266.0**	**63.5**	**-**	**-**	**-**	**475.8**	**3,195.5**

35. MATURITY PROFILE AND LIQUIDITY RISK (CONTINUED)

In BHD millions As at 31 December 2017	Up to 3 months	3 to 6 months	6 months to 1 year	1 to 3 years	3 to 5 years	5 to 10 years	10 to 20 years	Over 20 years	Total
Assets									
Cash and balances at central banks	107.0	-	-	-	-	-	-	-	107.0
Treasury bills	134.4	145.8	139.7	-	-	-	-	-	419.9
Placements with banks and other financial institutions	174.0	-	-	-	-	-	-	-	174.0
Loans and advances	351.7	75.2	110.9	285.5	273.8	99.5	28.7	1.6	1,226.9
Investment securities	39.8	1.8	55.4	300.5	322.4	253.0	13.2	81.2	1,067.3
Investment in associates, interest receivable, other assets and property & equipment	4.2	0.2	0.6	7.8	5.9	5.0	0.2	82.6	106.5
Total assets	811.1	223.0	306.6	593.8	602.1	357.5	42.1	165.4	3,101.5
Liabilities and equity									
Due to banks and other financial institutions	384.0	-	-	-	-	-	-	-	384.0
Borrowings under repurchase agreements	67.8	-	-	-	-	-	-	-	67.8
Customer deposits	1,680.2	167.2	269.4	48.4	-	-	-	-	2,165.2
Interest payable & other liabilities	20.5	13.8	0.7	1.6	-	-	-	-	36.6
Equity	-	-	-	-	-	-	-	447.9	447.9
Total liabilities and equity	2,152.5	181.0	270.1	50.0	-	-	-	447.9	3,101.5

b) Liquidity risk

The table below shows the undiscounted cash flows of the Bank's financial liabilities and undrawn loan commitments on the basis of their earliest contractual liability. The Bank's expected cash flows on these instruments vary significantly from this analysis; for example customers are expected to maintain stable or increased balances in demand deposits and not all undrawn loan commitments are expected to be drawn down immediately. For derivatives that have simultaneous gross settlement (e.g. forward exchange contracts and currency swaps) the gross nominal undiscounted cash inflow/(outflow) are considered while in the case of derivatives that are net settled the net amounts have been considered.

In BHD millions As 31 December 2018	**Carrying amount**	**Gross nominal inflow / (outflow)**	**Less than 3 months**	**3 to 6 months**	**6 to 12 months**	**1 to 5 years**	**More than 5 years**
Non derivative liabilities							
Due to banks and other financial institutions	**381.4**	**382.0**	**380.9**	**-**	**1.1**	**-**	**-**
Borrowings under repurchase agreements	**103.9**	**-**	**-**	**-**	**-**	**-**	**-**
Customer deposits	**2,190.6**	**2,213.5**	**1,717.3**	**168.9**	**273.8**	**53.5**	**-**
Total non derivative liabilities	**2,675.9**	**2,595.5**	**2,098.2**	**168.9**	**274.9**	**53.5**	**-**
Derivative liabilities							
Trading: outflow	**-**	**2,075.5**	**878.4**	**483.0**	**704.3**	**9.9**	**-**
Trading: inflow	**5.4**	**2,080.4**	**879.7**	**485.0**	**705.7**	**10.0**	**-**
Total derivative liabilities	**5.4**	**4,155.9**	**1,758.1**	**968.0**	**1,410.0**	**19.9**	**-**
Banking commitments	**-**	**-**	**(18.1)**	**-**	**-**	**-**	**18.1**
Financial guarantees	**-**	**(32.0)**	**(7.9)**	**(0.2)**	**(0.3)**	**(23.6)**	**-**

In BHD millions As 31 December 2017	Carrying amount	Gross nominal inflow / (outflow)	Less than 3 months	3 to 6 months	6 to 12 months	1 to 5 years	More than 5 years
Non derivative liabilities							
Due to banks and other financial institutions	384.1	385.6	385.6	-	-	-	-
Borrowings under repurchase agreements	67.8	68.0	68.0	-	-	-	-
Customer deposits	2,165.2	2,174.7	1,682.5	162.6	276.2	53.5	-
Total non derivative liabilities	2,617.1	2,628.3	2,136.1	162.6	276.2	53.5	-
Derivative liabilities							
Trading: outflow	-	782.3	533.8	183.1	65.3	0.1	-
Trading: inflow	0.9	783.4	534.3	183.3	65.8	0.1	-
Total derivative liabilities	0.9	1,565.7	1,068.1	366.4	131.1	0.2	-
Banking commitments	-	-	(82.9)	-	-	-	82.9
Financial guarantees	-	(47.6)	(6.9)	(0.3)	(0.5)	(39.9)	-

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36. RETIREMENT BENEFIT COSTS

The Bank's obligations to defined contribution pension plans for employees who are covered by the social insurance pension scheme in Bahrain and its overseas branches are recognised as an expense in the statement of profit or loss. The Bank's contribution for 2018 amounted to BHD 1.1 million (USD 2.9million) [2017: BHD 0.9 million (USD 2.4 million)].

Other employees are entitled to leaving indemnities payable in accordance with the employment agreements or under the respective labour laws. The movement in the provision for leaving indemnities during the year was as follows:

Provision for leaving indemnities

Movements during the year	2018		2017	
	BHD millions	**USD millions**	BHD millions	USD millions
At 1 January	**2.3**	**6.0**	3.1	8.4
Charge for the year	**0.9**	**2.4**	0.6	1.6
Paid during the year	**(0.6)**	**(1.6)**	(1.4)	(3.8)
At 31 December	**2.6**	**6.8**	2.3	6.2

The Bank has a voluntary staff savings scheme for eligible employees. The employees and the Bank contribute monthly on a fixed-percentage-of-salaries basis to the scheme. The scheme is managed and administrated by a board of trustees who are the employees of the Bank. The Bank's contribution to the scheme for 2018 amounted to BHD 1.0 million (USD 2.7 million) [2017: BHD 0.8 million (USD 2.1 million)]. As at 31 December 2018, after considering the employer's and employees' contributions, net income accretions and net pay-outs from the scheme, the net balance of the scheme, amounted to BHD 10.3 million (USD 27.4 million) [31 December 2017: BHD 10.0 million (USD 26.6 million)].

37. LEGAL CLAIMS

As at 31 December 2018, legal claims pending against the Bank aggregated to BHD 1.4 million (USD 3.7 million) [31 December 2017: BHD 1.2 million (USD 3.3 million)]. Based on the opinion of the Bank's legal advisors about final judgement on these claims, adequate provision as assessed by management is maintained.

38. EARNINGS AND DIVIDEND PER SHARE

	2018		2017	
	BHD millions	**USD millions**	BHD millions	USD millions
Profit for the year	**70.0**	**186.1**	61.0	162.3
Dividend proposed at 25% (2017: 25 %)	**35.1**	**93.4**	31.9	84.8
Weighted average number of shares issued (millions)				
Ordinary shares as at 1 January 2018	**1,275.4**	**1,275.4**	1,275.4	1,275.4
Effect of bonus shares issued during 2018 for 2017	**127.5**	**127.5**	127.5	127.5
Less unallocated employee shares	**(15.0)**	**(15.0)**	(15.7)	(15.7)
Weighted average number of ordinary shares (millions) as at 31 December	**1,387.9**	**1,387.9**	1,387.2	1,387.2
Earnings per share	**50 fils**	**13 cents**	44 fils	12 cents
Dividend per share	**25 fils**	**7 cents**	23 fils	6 cents

Diluted earnings per share is same as basic earnings per share as the Bank does not have any potential dilutive instruments in issue.

39. ACCOUNTING CLASSIFICATION

a) The following table provides disclosure of the accounting classification for assets and liabilities:

In BHD millions As at 31 December 2018	**Fair value through profit or loss**	**Amostised cost**	**Fair value through other comprehensive income**	**Total carrying amount**
Cash and balances at central banks	**-**	**107.3**	**-**	**107.3**
Treasury bills	**-**	**387.1**	**-**	**387.1**
Placements with banks and other financial institutions	**-**	**259.7**	**-**	**259.7**
Loans and advances	**-**	**1,190.1**	**-**	**1,190.1**
Investment securities	**0.4**	**775.5**	**356.3**	**1,132.2**
Interest receivable & other assets	**-**	**119.1**	**-**	**119.1**
Total assets	**0.4**	**2,838.8**	**356.3**	**3,195.5**
Due to banks and other financial institutions	**-**	**381.4**	**-**	**381.4**
Borrowings under repurchase agreements	**-**	**103.9**	**-**	**103.9**
Customer deposits	**-**	**2,190.6**	**-**	**2,190.6**
Interest payable & other liabilities	**-**	**43.8**	**-**	**43.8**
Total liabilities	**-**	**2,719.7**	**-**	**2,719.7**

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39. ACCOUNTING CLASSIFICATION (CONTINUED)

In BHD millions As at 31 December 2017	Fair value through profit or loss	Loans and receivables	Available-for-sale	Others at amortised cost	Total carrying amount
Cash and balances at central banks	-	107.0	-	-	107.0
Treasury bills	-	419.9	-	-	419.9
Placements with banks and other financial institutions	-	174.0	-	-	174.0
Loans and advances	-	1,226.9	-	-	1,226.9
Investment securities	0.2	-	1,067.1	-	1,067.3
Interest receivable & other assets	-	41.8	-	-	41.8
Total assets	0.2	1,969.6	1,067.1	-	3,036.9
Due to banks and other financial institutions	-	-	-	384.0	384.0
Borrowings under repurchase agreements	-	-	-	67.8	67.8
Customer deposits	-	-	-	2,165.2	2,165.2
Interest payable & other liabilities	-	-	-	27.2	27.2
Total liabilities	-	-	-	2,644.3	2,644.3

b) Fair value hierarchy

The Bank measures fair values of financial instruments using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly observable from market data.

Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes input not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation.

All financial instruments other than those disclosed in the table below are classified as level 2.

(i) Loans and advances: The fair value approximates its carrying value since the majority of loans are floating rate loans which have been disbursed at market rates, and adequate impairment provisions have been taken for those loans with doubt as to collectability.

(ii) Customer deposits: The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is deemed to equal the amount repayable on demand, which is represented by the carrying value of the deposits. For interest bearing fixed maturity deposits, the Bank estimates that fair value will approximate their book value as the majority of deposits are of short-term nature and all deposits are at market rates.

(iii) Other financial assets and liabilities: The fair value is considered to approximate their book values due to their short-term nature and negligible probability of credit losses.

The table below analyses financial assets and liabilities carried at fair value, by valuation method.

In BHD millions		**2018**				2017		
At 31 December	**Level 1**	**Level 2**	**Level 3**	**Total**	Level 1	Level 2	Level 3	Total
Fair value through profit or loss:								
Equity instruments/Managed funds	**-**	**0.4**	**-**	**0.4**	-	0.2	-	0.2
Fair value through other comprehensive income/ Available-for-sale:								
Debt instruments	**301.6**	**-**	**-**	**301.6**	332.5	685.4	-	1,017.9
Equity instruments	**43.6**	**-**	**11.1**	**54.7**	38.3	-	10.9	49.2
Derivative financial assets	**-**	**10.2**	**-**	**10.2**	-	4.2	-	4.2
	345.2	**10.6**	**11.1**	**366.9**	370.8	689.8	10.9	1,071.5
Derivative financial liabilities	**-**	**0.7**	**-**	**0.7**	-	1.1	-	1.1

The portfolio of debt instruments valued under the level 2 valuation method at 31 December 2017 amounting to BHD 685.4 million has been reclassified during the year. The Bank reclassified the portfolio as at 1 July 2018 from the fair value through other comprehensive income (available-for-sale under IAS39) category to the amortised cost category to more accurately reflect the Bank's new strategic intention for the portfolio. The Bank intends to collect the contractual cash flows which represent solely the payment of principal and interest. At the time of reclassification, the portfolio had a fair value of BHD 729.8 million. The carrying amount of the portfolio as at 31 December 2018 was BHD 775.5 million, with a fair value of BHD 778.0 million. The Bank would have recognised a positive fair value of BHD 2.5 million in other comprehensive income if the portfolio was not reclassified.

Notes to the Financial Statements (continued)
For the year ended 31 December

39. ACCOUNTING CLASSIFICATION (CONTINUED)

The following table analyses the movement in level 3 financial assets during the year. There were no transfers between level 1, level 2 and level 3 of the fair value hierarchy.

	Investment securities	
In BHD millions	**2018**	2017
At 1 January	**10.9**	10.3
Total gains in other comprehensive income	**0.2**	0.6
At 31 December	**11.1**	10.9

Total gain for the year included in the statement of profit or loss for assets/liabilities held at 31 December 2018 is nil (2017: nil)

Level 3 comprises unquoted equity investments classified as fair value through other comprehensive income (2017: available-for-sale) which are measured at their estimated fair value based on the latest financial information by the investee. Sensitivity analysis of the movement in fair value of the financial instruments in the level 3 category financial assets is assessed as not significant to the other comprehensive income and total equity.

40. AVERAGE BALANCES

The following are average daily balances for the year :	**2018**		2017	
	BHD millions	**USD millions**	BHD millions	USD millions
Total assets	**3,037.8**	**8,079.3**	3,007.9	7,999.8
Total liabilities	**2,575.2**	**6,848.9**	2,582.0	6,866.9
Total equity	**462.6**	**1,230.4**	425.9	1,132.8
Contingent liabilities and undrawn loan commitments	**211.5**	**562.4**	243.9	648.7

41. CAPITAL ADEQUACY

The Bank operates as an independent banking institution with headquarters in Bahrain and branches in Bahrain, United Arab Emirates and Saudi Arabia.

The capital adequacy ratio has been calculated in accordance with Basel III and Central Bank of Bahrain guidelines incorporating credit risk, operational risk and market risk. The Bank uses the standardised approach for computing credit risk. Operational risk is computed using the basic indicator approach. Market risk is computed using the standardised method.

The details of the Bank's capital adequacy calculations are shown below:

	2018		2017	
As at 31 December	**BHD millions**	**USD millions**	BHD millions	USD millions
Common equity	**461.3**	**1,226.9**	434.1	1,154.5
Additional tier 1	**-**	**-**	-	-
Total common equity tier 1 (CET1)	**461.3**	**1,226.9**	434.1	1,154.4
Tier 2	**13.6**	**36.2**	12.4	33.2
Total capital base	**474.9**	**1,263.0**	446.5	1,187.6
Risk weighted exposure:				
Credit risk	**1,163.8**	**3,095.3**	1,039.9	2,765.5
Market risk	**50.2**	**133.5**	16.1	42.9
Operational risk	**192.5**	**512.0**	174.8	465.1
Total risk weighted exposure	**1,406.5**	**3,740.8**	1,230.8	3,273.5
CET1 Ratio	**32.8%**		35.3%	
Total capital adequacy ratio	**33.8%**		36.3%	

42. DEPOSIT PROTECTION SCHEME

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

43. COMPARATIVES

The corresponding figures have been regrouped where necessary to conform with the current year's presentation. The regrouping did not affect previously reported profit for the year or total equity of the Bank.

Risk and Capital Management Disclosures
For the year ended 31 December 2018

EXECUTIVE SUMMARY

The Central Bank of Bahrain's ('CBB') Basel III rules outlining the capital adequacy framework for banks incorporated in the Kingdom of Bahrain became effective from 1 January 2015.

NBB has adopted the standardised approach for credit risk and market risk and the basic indicator approach for operational risk to determine the capital requirement. This report consists of the Basel Committee's Pillar 3 disclosures and other disclosure requirements as stipulated by the CBB. The report contains a description of the Bank's risk management and capital adequacy policies and practices including detailed quantitative information on capital adequacy.

As at 31 December 2018, the Bank's total risk weighted assets amounted to BHD 1,406.5 million; common equity tier 1 ('CET1') and total regulatory capital amounted to BHD 461.3 million and BHD 474.9 million respectively. Accordingly, the CET1 capital adequacy ratio and the total capital adequacy ratio were 32.8% and 33.8% respectively. These ratios exceed the minimum capital requirements under the CBB's Basel III framework.

The Bank views these disclosures as an important means of increased transparency and accordingly has provided extensive disclosures in this report that is appropriate and relevant to the Bank's stakeholders and market participants.

CBB CAPITAL ADEQUACY RULES

The CBB capital adequacy rules provide guidance on the risk measurements for the calculation of capital adequacy requirements (CAR). Conventional bank licenses are required to meet the following minimum CAR requirements:

		Components of consolidated CARs		
	Limit	Minimum ratio required	Capital conservation buffer (CCB)	CAR including CCB
Common equity tier 1 ('CET1')		**6.5 %**	2.5 % comprising of CET1	**9.0 %**
Additional tier 1 ('AT1')	1.5 %			
Tier 1		**8.0 %**		**10.5 %**
Tier 2	2.0 %			
Total capital		**10.0 %**		**12.5 %**

The regulatory adjustments (i.e. deductions) including amounts above the aggregate 15% limit for significant investments in financial institutions, mortgage service rights, and deferred tax assets from temporary differences, are fully deducted from CET1 by 1 January 2019. This regulatory adjustment was at 20% of the required adjustments to CET 1 on 1 January 2015, 40% on 1 January 2016, 60% on 1 January 2017, 80% on 1 January 2018, and reach 100% on 1 January 2019. During the transition period, the remainder not deducted from CET1, continues to be risk weighted as per the rulebook.

Banks are required to maintain a capital conservation buffer ('CCB') of 2.5%, comprising of CET1 above the regulatory minimum total capital ratio of 10.0%. Capital distribution constraints will be imposed when the CCB falls below 2.5%. The constraints imposed only relate to distribution, and not the operations of the licensed banks.

The Basel III framework consists of three mutually reinforcing pillars:

i. Pillar 1: minimum capital requirements for credit risk, market risk and operational risk.
ii. Pillar 2: supervisory review of capital adequacy including documentation of an Internal Capital Adequacy Assessment Process ('ICAAP').
iii. Pillar 3: market discipline including rules for disclosure of risk management and capital adequacy.

SCOPE OF APPLICATION

The Bank operates as an independent banking institution with headquarters in Bahrain and branches in Bahrain, United Arab Emirates and Saudi Arabia. The Bank's capital adequacy requirements are computed on a consolidated basis. The Bank does not have any subsidiaries.

RISK AND CAPITAL MANAGEMENT

The Bank is exposed to the following types of risks:

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

Risk management framework

The overall authority for risk management in the Bank is vested in the Board of Directors. The Board authorises appropriate credit, liquidity, operational, and market risk policies that form part of its risk management framework, based on the recommendation of management. The Bank has established various committees that review and assess all risk issues. Approval authorities are delegated to different functionaries in the hierarchy depending on the amount, type of risk and nature of operations or risk. The risk group of the Bank provides the necessary support to senior management and the business units in all areas of risk management. The risk group functions independent of the business units and reports directly to the Board Risk Committee and administratively to the Chief Executive Officer. The risk group comprises of a Credit Risk Department (responsible for independent pre-approval analysis of credit / investment proposals as well as risk policy and procedures management), Credit Administration Department (responsible for post approval implementation and follow up), Liquidity and Market Risk Management Department, Operational Risk Management Department, and Information Security Risk Department.

Risk and Capital Management Disclosures (continued)

For the year ended 31 December

RISK AND CAPITAL MANAGEMENT (continued)

Risk management framework (continued)

The Board Risk Committee is responsible for identifying, optimising and ensuring appropriate mitigation of risks within the framework of the risk appetite established by the Bank's board of directors. This includes reviewing and reporting its conclusions and recommendations to the board on:

- The Bank's current and future risk appetite (i.e. in relation to the extent and categories of risk which the board regards as acceptable for the Bank to bear);
- The Bank's risk management framework (embracing principles, policies, methodologies, systems, processes, procedures and people); and
- The Bank's risk culture to ensure that it supports the Bank's risk appetite. In this regard, the committee will take a forward-looking perspective, seeking to anticipate changes in business conditions.

Credit risk

Credit risk represents the potential financial loss as a consequence of a customer's inability to honour the terms and conditions of a credit facility. Such risk is measured with respect to counterparties for both on-balance sheet assets and off-balance sheet items.

The Bank acknowledges that credit risk is an inherent and substantial cost that needs to be set against income. Risk is just one aspect of the triangle for any economic capital system and must be seen in conjunction with capital requirements and returns. The Bank evaluates risk in terms of the impact on income and asset values, and the evaluation reflects the Bank's assessment of the potential impact on its business on account of changes in political, economic and market conditions and in the credit worthiness of its clients. Risk management at the Bank has always been conservative and proactive with the objective of achieving a balanced relation between risk appetite and expected returns.

The Bank monitors and manages concentration risk by setting limits on exposures to countries, sectors and counterparty groups. Stringent criteria are used by the credit risk department in setting such limits and these have ensured that the impact of any adverse developments on the Bank's income generation and capital strength is limited. Similarly, prudent norms have been implemented to govern the Bank's investment activities, which specify to the Bank's treasury department the acceptable levels of exposure to various products, based on its nature, tenor, rating, type, features, etc.

The Bank has well laid out procedures, to not only appraise but also regularly monitor credit risk. Credit appraisal is based on the financial information of the borrower, performance projections, market position, industry outlook, external ratings (where available), track record, product type, facility tenor, account conduct, repayment sources and ability, tangible and intangible security, etc. Regular reviews are carried out for each account and risks identified are mitigated in a number of ways, which include obtaining collateral, counter-guarantees from shareholders and/or third parties. Adequate margins are maintained on the collateral to provide a cushion against adverse movement in the market price of collateral. Not only are regular appraisals conducted to judge the credit worthiness of the counterparty but day-to-day monitoring of financial developments across the globe by the business units and credit risk department ensures timely identification of any events affecting the risk profile.

The business units of the Bank are responsible for business generation and initial vetting of proposals in accordance with the stipulated policy requirements. Credit facilities in excess of certain levels or falling outside pre-approved product criteria are independently reviewed by the credit risk department, which analyses the proposal and puts forth its recommendations prior to approval by the appropriate authorities. In addition to rigorous credit analysis, the terms and conditions of all credit facilities are strictly implemented by the credit administration department. An internal grading system and review process ensures identification of any deterioration in credit risk and consequent implementation of corrective action.

The Bank's internal ratings are based on a 16-point scale, which takes into account the financial strength of a borrower as well as qualitative aspects to arrive at a comprehensive snapshot of the risk of default associated with the borrower. Ratings are further sub-divided into categories, which reflect estimates of the potential maximum loss in an event of default. Risk ratings assigned to each borrower are reviewed on at least an annual basis. Regular monitoring of the portfolio enables the Bank to identify accounts, which witness deterioration in risk profile. Consumer credit facilities, which are granted based on pre-defined criteria such as salary assignment, maximum repayment obligation as a percentage of salary, etc. are excluded from this rating system.

The Bank also uses the ratings by established rating agencies as part of the appraisal process while considering exposures to rated entities.

For purposes of comparison, the Bank's internal ratings are mapped to Fitch, Moody's and Standard & Poor's ('S&P') ratings as under:

Internal ratings scale	Fitch	S&P	Moody's
1	AAA	AAA	Aaa
2	AA+	AA+	Aa1
3	AA	AA	Aa2
4+	AA-	AA-	Aa3
4	A+	A+	A1
4-	A	A	A2
5+	A-	A-	A3
5	BBB+	BBB+	Baa1
5-	BBB	BBB	Baa2
6+	BBB-	BBB-	Baa3
6	BB+	BB+	Ba1
6-	BB to BB-	BB to BB-	Ba2 to Ba3
7	B+ to B-	B+ to B-	B1 to B3
8-10	CCC+ to D	CCC+ to D	Caa1 to C

However, the above mapping is not intended to reflect a direct relationship between the Bank's internal ratings and the corresponding rating of the external agencies, since the basis and methodology differ.

Risk and Capital Management Disclosures (continued)

For the year ended 31 December

RISK AND CAPITAL MANAGEMENT (continued)

Liquidity risk

Liquidity risk is the potential inability of a bank to meet its financial obligations on account of a maturity mismatch between assets and liabilities. Liquidity risk management ensures that funds are available at all times to meet the funding requirements of the Bank.

The asset/liability management policies of the Bank define the proportion of liquid assets to total assets with the aim of minimising liquidity risk. The Bank maintains adequate liquid assets such as inter-bank placements, treasury bills and other readily marketable securities, to support its business and operations. The treasury department monitors the maturity profile of assets and liabilities so that adequate liquidity is maintained at all times.

The Bank's ability to maintain a stable liquidity profile is primarily on account of its success in retaining and growing its customer deposit base. The marketing strategy of the Bank has ensured a balanced mix of demand and time deposits. Stability of the deposit base thus minimises the Bank's dependence on volatile short-term borrowings. Further, investment securities with contractual maturities of more than three months can also be readily liquidated. Considering the effective maturities of deposits based on retention history and in view of the ready availability of liquid investments, the Bank is able to ensure that sufficient liquidity is always available. The Asset Liability Committee ('ALCO') chaired by the Chief Executive Officer reviews the liquidity gap profile and the liquidity scenario and addresses strategic issues concerning liquidity.

Market risk

Market risk is the risk of potential losses arising from movements in market prices of interest rate related instruments and equities in the trading portfolio and foreign exchange and commodities holdings throughout the Bank. The Bank's trading activities are governed by conservative policies that are clearly documented, by adherence to comprehensive limit structures set annually, and by regular reviews. Quality and rating are the main criteria in selecting a trading asset. The Bank uses the standardised method for allocating market risk capital based on the risk assessed for underlying factors of interest rate risk, equity risk, foreign exchange risk, options risk and commodity risk. Daily reports in this regard are submitted to senior management for review and decision making purposes.

Interest rate risk is measured by the extent to which changes in the market interest rates impact margins, net interest income and the economic value of the Bank's equity. Net interest income will be affected as a result of volatility in interest rates to the extent that the re-pricing structure of interest bearing assets differs from that of liabilities. The Bank's goal is to achieve stable earnings growth through active management of the assets and liabilities mix while, selectively positioning itself to benefit from near-term changes in interest rate levels. The treasurer is primarily responsible for managing the interest rate risk. Reports on overall position and risks are submitted to senior management for review and positions are adjusted if deemed necessary. In addition, ALCO regularly reviews the interest rate sensitivity profile and its impact on earnings.

The Bank's asset and liability management process is utilised to manage interest rate risk through the structuring of on-balance sheet and off-balance sheet portfolios. The Bank uses various techniques for measuring and managing its exposure to interest rate risk. Duration analysis is used to measure the interest rate sensitivity of the fixed income portfolio. Duration of the portfolio is governed by economic forecasts, expected direction of interest rates and spreads. Modified duration gives the percentage change in value of the portfolio following a 1 percent change in yield. Interest rate swaps and forward rate agreements are used to manage the interest rate risk. The Bank uses interest rate gap analysis to measure the interest rate sensitivity of its annual earnings due to re-pricing mismatches between rate sensitive assets, liabilities and derivatives positions.

Operational risk

Operational risk is the risk of monetary loss on account of human error, fraud, systems failures or the failure to record transactions. In order to manage and mitigate such risks, the Bank ensures that proper systems and resources (financial and personnel) are available to support the Bank's operations. Proper segregation of duties and other controls (including reconciliation, monitoring and reporting) are implemented to support the various operations, especially credit, treasury and electronic banking activities.

Detailed operational guidelines are covered in the Bank's procedure manuals to specify the steps to be followed in handling any transaction. These steps are designed to mitigate the risks arising from errors, omissions and oversights in dealing with customer instructions and transaction processing. The overriding principles in drawing up operational processes are that transactions must be scrutinised by a "checker" independent from the "originator" prior to booking and that there should be a clear audit trail for post facto scrutiny. The Bank's procedures provide necessary guidance to mitigate risks and ensure that adequate controls are in place for detecting suspicious transactions. Any changes to operational procedures need to be processed through the operational risk department, who ensure that satisfactory control mechanisms are in place in all procedures.

Specific limits are set up to mitigate and monitor the Bank's exposure including limits on maximum branch cash limit, maximum teller limit, maximum payment authorisation limit, signature authorities, etc. Documented policies and procedures, approval and authorisation process for transactions, documented authority letters, process of verification of transaction details and activities, reconciliation of key activities, dual custody of financial assets like demand drafts, cheques etc. and insurance coverage of various operational risks are the key pillars of the operational risk management process.

The Bank has an operational risk management department within the risk group to independently monitor and manage all aspects of operational risk on a bank wide basis. The Bank also has a dedicated Operational Risk Management Committee (chaired by the Chief Risk Officer) to supervise, monitor and review operational risk issues and to ensure that adequate mitigants are developed and implemented for all operational risk issues.

The scope of the internal audit department encompasses audits and reviews of all business units, support services and branches. The internal audit process focuses primarily on assessing risks and controls and ensuring compliance with established policies, procedures and delegated authorities. New products and services are reviewed by the internal audit department and assessed for operational risks prior to their implementation. The internal audit department is operationally independent and reports significant internal control deficiencies to the audit committee.

The Bank has a business continuity plan ('BCP') to ensure that the critical activities are supported in case of an emergency. The BCP is approved by the Board of Directors.

RISK AND CAPITAL MANAGEMENT (continued)

Risk monitoring and reporting
Systems and processes are in place to regularly monitor and report risk exposures to the board of directors and senior management to effectively monitor and manage the risk profile of the Bank.

The Board of Directors are provided with quarterly risk reports covering credit, market, liquidity, operational, concentration and other risks.

Senior management is provided with a daily report on market risk and monthly reports on other risks. Reports on capital adequacy and internal capital adequacy assessment are provided to senior management on a monthly basis. In addition, stress testing on capital adequacy is undertaken once a year or more frequently in times of need and communicated to the Board of Directors and senior management for appropriate decisions.

Capital management
The Bank's policy is to maintain sufficient capital to sustain investor, creditor and market confidence and to support future development of the business. The impact of the level of capital on return on shareholders' equity is also considered and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

The Bank's capital management framework is intended to ensure that there is sufficient capital to support the underlying risks of the Bank's business activities and to maintain a well-capitalised status under regulatory requirements. The Bank has a comprehensive Internal Capital Adequacy Assessment Process ('ICAAP') that includes board and senior management oversight, monitoring, reporting and internal control reviews, to identify and measure the various risks that are not covered under Pillar 1 risks and to regularly assess the overall capital adequacy considering the risks and the Bank's planned business strategies. The non-Pillar 1 risks covered under the ICAAP process include concentration risk, liquidity risk, interest rate risk in the banking book and other miscellaneous risks. The ICAAP also keeps in perspective the Bank's strategic plans, credit growth expectations, future sources and uses of funds, dividend policy and the impact of all these on maintaining adequate capital levels. In addition, the ICAAP process also includes stress testing on the Bank's capital adequacy to determine the capital requirement and planning to ensure that the Bank is adequately capitalised in line with the overall risk profile.

The Bank ensures that the capital adequacy requirements are met on a consolidated basis and also with local regulator's requirements, if any, in countries in which the Bank has branches. The Bank has complied with regulatory capital requirements throughout the year.

Prior approval of the Central Bank of Bahrain is obtained by the Bank before submitting any proposal for distribution of profits for shareholders' approval.

CAPITAL STRUCTURE AND CAPITAL ADEQUACY

Capital structure, minimum capital and capital adequacy
The Bank's paid up capital consists only of ordinary shares, which have proportionate voting rights. The Bank does not have any other type of capital instruments.

All amounts are presented at 31 December 2018 unless specified otherwise.

	BHD millions
Common equity tier 1 ('CET1')	
Share capital	140.3
Shares unallocated under share incentive scheme	(1.5)
Share premium	5.0
Statutory reserve	70.1
General reserves	32.4
Other reserves and retained earnings	229.5
Total equity	**475.8**
Addition unrealised loss in cash flow hedge reserve not eligible for regulatory capital	0.4
Total regulatory capital	**476.2**
Deduction from CET 1 (significant investments in common stock of financial entities)	(14.9)
Total common equity tier 1 ('CET1')	**461.3**
Additional tier 1	-
Total tier 1	461.3
Tier 2 capital	
Expected credit loss subject to 1.25% of credit risk weighted assets	13.6
Total tier 2	**13.6**
Total capital base (tier 1 + tier 2)	**474.9**

CREDIT RISK

The Bank has a diversified on and off-balance sheet credit portfolio, which is divided into counterparty exposure classes in accordance with the CBB's Basel III capital adequacy framework. A high-level description of the counterparty exposure classes and the risk weights used to derive the risk weighted assets are as follows:

Sovereign portfolio
The sovereign portfolio comprises exposures to governments and their respective central banks. The risk weights are 0 percent for exposures in the relevant domestic currency of the sovereign, or for any exposures to GCC governments. Foreign currency claims on other sovereigns are risk weighted based on their external credit ratings.

Certain multilateral development banks as determined by the CBB may be included in the sovereign portfolio and treated as exposures with a 0 percent risk weighting.

PSE portfolio
Public sector entities ('PSEs') are risk weighted according to their external ratings except for Bahrain PSEs and domestic currency claims on other PSEs that are assigned a 0 percent risk weight by their respective country regulator, which are risk weighted at 0 percent.

Banks portfolio
Claims on banks are risk weighted based on their external credit ratings. A preferential risk weight treatment is available for qualifying short-term exposures to foreign banks licensed in Bahrain. Short-term exposures are defined as exposures with an original tenor of three months or less and denominated and funded in the respective domestic currency. The preferential risk weight for short-term claims is applied on exposures in Bahraini Dinar and US Dollar in the case of Bahraini incorporated banks.

Corporates portfolio
Claims on corporates are risk weighted based on their external credit ratings. A 100 percent risk weight is assigned to exposures to unrated corporates. A preferential risk weight treatment is available for certain corporates owned by the Government of Bahrain, as determined by the CBB, which are assigned a 0 percent risk weight.

Regulatory retail portfolio
Claims on individuals or to a small business with an annual turnover below BHD 2.0 million and where the maximum aggregated retail exposure to one counterpart is below BHD 0.25 million are risk weighted at 75 percent.

Residential mortgages
Lending fully secured by first mortgages on residential property that is, or will be, occupied by the borrower or that is leased are risk weighted at 75 percent.

Equities/funds portfolio
The equities portfolio comprises equity investments in the banking book, i.e. categorised as fair value through other comprehensive income. The credit (specific) risk for equities in the trading book is included in market risk for regulatory capital adequacy calculation purposes.

A 100 percent risk weight is assigned to listed equities and funds. Unlisted equities and funds are risk weighted at 150 percent. Investments in rated funds are risk weighted according to the external credit rating. Significant investments in listed and unlisted equities of financial entities are aggregated and the excess above the 10 percent of CET1 is deducted from equity; the amount not deducted is risk weighted at 250 percent.

Investments in real estate and also in bonds, funds and equities of companies engaged primarily in real estate are risk weighted at 200 percent.

In addition to the above portfolios, other exposures are risk weighted as under:

Past due exposures
All past due loan exposures, irrespective of the categorisation of the exposure are classified separately under the past due exposures asset class. A risk weighting of either 100 percent or 150 percent is applied depending on the level of specific provision maintained against the exposure.

Other assets
Other assets are risk weighted at 100 percent. A credit valuation adjustment ('CVA') is applied to applicable derivative exposures and included under other assets.

Risk and Capital Management Disclosures (continued)

For the year ended 31 December

CREDIT RISK (continued)

External credit assessment institutions (ECAI)

The Bank uses ratings issued by external rating agencies to derive the risk weightings under the CBB's Basel III capital adequacy framework. Where ratings vary between rating agencies, the highest rating for the lowest two ratings is used to derive the risk weighting.

In BHD millions	Credit exposure before CRM	Eligible CRM	Credit exposure after CRM	Average risk weight percentage	Risk weighted exposure	Capital requirement at 12.5%
Sovereign portfolio	1,601.7	-	1,601.7	-	-	-
PSE portfolio	0.2	-	0.2	-	-	-
Banks portfolio	362.5	52.6	309.9	46%	140.9	17.6
Corporates portfolio	402.3	40.1	362.2	98%	356.2	44.5
Regulatory retail portfolio	409.7	2.7	407.0	75%	305.3	38.2
Residential mortgages portfolio	29.3	-	29.3	75%	22.0	2.8
Equities/funds portfolio	97.6	-	97.6	189%	184.3	23.0
Past due exposures portfolio	68.4	3.1	65.3	116%	75.7	9.5
Others assets	79.4	-	79.4	100%	79.4	9.9
Total credit risk exposure	3,051.1	98.5	2,952.6		1,163.8	145.5
Market risk					50.2	6.3
Operational risk					192.5	24.1
Total risk weighted assets					1,406.5	175.8
CET1 capital adequacy ratio					32.8%	
Capital adequacy ratio					33.8%	

CRM is credit risk mitigants such as lien over deposits, mortgage over properties and/or shares and financial instruments.

According to Central Bank of Bahrain rulebook, banks designated as D-SIBs must hold designated HLA (high loss absorbency) expressed as common equity tier 1 capital at 1.5% of the total risk weighted assets, as calculated for the purposes of capital adequacy. As at 31 December 2018, the Bank common equity tier 1 capital ratio was 32.8% exceeding the minimum common capital tier 1 ratio and D-SIB buffer requirement of 9.0% and 1.5% respectively.

Credit risk exposures

The following are gross credit exposures, presented before the application of any credit risk mitigation techniques:

In BHD millions	As at 31 December 2018	2018 Daily average
Balances at central banks	80.3	104.5
Treasury bills	387.1	430.6
Placements with banks and other financial institutions	259.7	113.7
Loans and advances	1,190.1	1,231.2
Investment securities	1,077.1	1,084.0
Other assets	49.2	108.7
Total assets	3,043.5	3,072.7
Non-derivative banking commitments and contingent liabilities	213.7	261.9
Derivatives (replacement cost)	10.2	6.9
	3,267.4	3,341.5

Industry or sector exposure

	Government							
In BHD millions	Bahrain	Other countries	Manufacturing / trading	Banks / financial	Construction	Personal	Others	Total
Assets								
Balances at central banks	-	-	-	80.3	-	-	-	80.3
Treasury bills	387.1	-	-	-	-	-	-	387.1
Placements with banks and other financial institutions	3.8	-	-	255.9	-	-	-	259.7
Loans and advances	114.7	-	138.0	103.3	84.2	466.8	283.1	1,190.1
Investment securities - debt instruments	1,005.8	20.8	-	39.3	-	-	11.2	1,077.1
Interest receivable and other assets	17.9	0.1	1.1	5.7	0.1	0.9	23.4	49.2
Total assets	1,529.3	20.9	139.1	484.5	84.3	467.7	317.7	3,043.5
Contingent liabilities and banking commitments	34.8	-	65.4	53.8	38.4	1.5	19.8	213.7
Derivatives (replacement cost)	2.0	-	-	7.9	-	0.3	-	10.2
	1,566.1	20.9	204.5	546.2	122.7	469.5	337.5	3,267.4

Risk and Capital Management Disclosures (continued)

For the year ended 31 December

CREDIT RISK (continued)

Industry or sector exposure (continued)

The previous table includes certain exposures to customers/counter-parties, which are in excess of 15% of the Bank's capital base. These exposures have the approval of the Central Bank of Bahrain or are exempt exposures under the large exposures policy of the Central Bank of Bahrain. The table below gives details of these exposures:

Counterparty	Counterparty type	Total exposure (In BHD millions)
Counterparty A	Sovereign	1,420.4
Counterparty B	Central bank	176.5
Counterparty C	Sovereign	136.0
Counterparty D	Sovereign	85.5

Geographic distribution of exposure

In BHD millions	GCC	USA	Europe	Rest of the world	Total
Assets					
Balances at central banks	80.3	-	-	-	80.3
Treasury bills	387.1	-	-	-	387.1
Placements with banks and other financial institutions	205.1	2.5	51.5	0.6	259.7
Loans and advances	1,099.0	83.7	-	7.4	1,190.1
Investment securities- debt instrument	1,053.9	9.4	-	13.8	1,077.1
Interest receivable and other assets	43.3	2.6	3.2	0.1	49.2
Total assets	2,868.7	98.2	54.7	21.9	3,043.5
Contingent liabilities and banking commitments	192.4	0.1	16.2	5.0	213.7
Derivatives (replacement cost)	5.4	0.9	3.9	-	10.2
	3,066.5	99.2	74.8	26.9	3,267.4

Residual contractual maturity

In BHD millions	Up to 3 months	3 to 6 months	6 months to 1 year	1 to 3 years	3 to 5 years	5 to 10 years	10 to 20 years	Over 20 years	Total
Assets									
Balances at central banks	80.3	-	-	-	-	-	-	-	80.3
Treasury bills	172.0	103.4	111.7	-	-	-	-	-	387.1
Placements with banks and other financial institutions	259.7	-	-	-	-	-	-	-	259.7
Loans and advances	267.8	57.9	152.3	284.7	272.1	129.2	23.7	2.4	1,190.1
Investment securities- debt instrument	1.8	4.3	194.4	493.4	206.9	176.3	-	-	1,077.1
Interest receivable and other assets	4.0	0.2	2.3	12.9	4.6	3.5	-	21.7	49.2
Total assets	785.6	165.8	460.7	791.0	483.6	309.0	23.7	24.1	3,043.5
Contingent liabilities and banking commitments	87.2	33.7	30.2	59.3	2.5	0.8	-	-	213.7
Derivatives (replacement cost)	1.9	1.8	2.3	-	0.2	1.3	-	2.7	10.2
	874.7	201.3	493.2	850.3	486.3	311.1	23.7	26.8	3,267.4

Shari'a compliant credit facilities

As at 31 December 2018, the Bank held Shari'a compliant credit facilities amounting to BHD 140.3 million.

Past due exposures

In accordance with the Bank's policy and Central Bank of Bahrain guidelines, loans on which payment of interest or repayment of principal are over 90 days past due, are defined as non-performing.

The Bank has systems and procedures in place to identify past dues in any account. A stringent classification process is followed for all accounts with past dues of over 90 days. The Bank applies rigorous standards for provisioning and monitoring of non-performing loans. The level of provisions required is determined based on the security position, repayment source, discounted values of cash flows, etc. and adequate provisions are carried to guard against inherent risks in the portfolio.

All non-performing loans and advances are assessed for impairment as stage 3. Under stage 3, lifetime ECL is recognised based on discounted cash flow methods based on the difference between the net carrying amount and the recoverable amount of the financial asset. The recoverable amount is measured as the present value of expected future cash flows, including amounts recoverable from guarantees and collateral, discounted based on the interest rate at the inception of the credit facility or, for debt instruments, at the current market rate of interest for a similar financial asset.

Impairment charges on the wider portfolio of financial assets which are not individually identified as impaired is now a forward-looking calculation and is established based on various factors. These factors include internal risk ratings, historical default rates adjusted considering multiple scenarios of the future macroeconomic outlook, loss ratios given an event of default, and rating migrations.

Risk and Capital Management Disclosures (continued)
For the year ended 31 December

CREDIT RISK (continued)
Past due exposures (continued)

Ageing analysis of impaired and past due loans and advances:

	BHD millions
Up to 3 months (subject to cooling off period)	53.5
Over 3 months to 1 year	12.5
1 to 3 years	26.1
Over 3 years	9.2
	47.8
	101.3
Fair market value of collateral	132.8
Stage 3/Specific provision for impairment	(36.5)

Geographical location of impaired and past due loans and advances:

In BHD millions	Loan amount	Stage 3/Specific provision for impairment	Collateral market value	ECL stage 1 and stage 2
Bahrain	96.3	36.2	132.8	12.0
Other GCC countries	5.0	0.3	-	0.9
	101.3	36.5	132.8	12.9

ECL stage 1 and stage 2 is against loan exposure classified as stage 1 and stage 2 amounting to BHD 1,138.2 million.

Industry breakdown of impaired and past due loans and advances:

In BHD millions	Impaired loans	Stage 3/Specific provision for impairment	Collateral market value	ECL stage 1 and stage 2
Manufacturing/trading	36.8	11.1	21.8	2.3
Construction	45.1	14.4	81.3	0.1
Personal	11.7	10.6		7.9
Others	7.7	0.4	29.7	2.6
Total	101.3	36.5	132.8	12.9

ECL stage 1 and stage 2 is against loan exposure classified as stage 1 and stage 2 amounting to BHD 1,138.2 million.

Movement in impairment provision for loans and advances:

In BHD millions	Stage 1	Stage 2	Stage 3	Total
Impairment at 1 January 2018	9.4	1.6	31.4	42.4
Net transfer between stages	(1.2)	(0.4)	1.6	-
Write off during the year	-	-	(2.2)	(2.2)
Charge for the year (net)	(1.6)	5.1	5.7	9.2
Impairment at 31 December 2018	6.6	6.3	36.5	49.4

Restructuring
During 2018, credit facilities amounting to BHD 3.7 million were restructured. Restructuring concessions mainly related to deferral of loan installments to assist customers overcome temporary cash flow situations or to realign the repayment with the borrower's revised cash flow projections, and amending the terms of loan covenants. Due to the minor nature of concessions, there was no significant impact on the Bank's impairment charge or the future earnings. In accordance with the Central Bank of Bahrain guidelines, loans that have been restructured should be reported as stage 2 for not less than 1 year from the date of restructuring.

CREDIT RISK MITIGATION
The reduction of the capital requirement attributable to credit risk mitigation is calculated in different ways, depending on the type of credit risk mitigation, as under:

- Adjusted exposure amount: The Bank uses the comprehensive method for eligible financial collateral such as cash and equities listed on a recognised stock exchange. The exposure amount and financial collateral, where applicable, are adjusted for market volatility through the use of supervisory haircuts (for currency mis-matches, price volatility and maturity-mismatches).

- Substitution of counterparty: The substitution method is used for eligible guarantees (sovereigns, banks or corporate entities with ECAI ratings higher than that of the counterparty; guarantees issued by corporate entities may only be taken into account if their rating corresponds to A- or better) whereby the rating of the counterparty is substituted with the rating of the guarantor.

Risk and Capital Management Disclosures (continued)
For the year ended 31 December

COLLATERAL AND VALUATION PRINCIPLES
Collaterals taken for risk mitigation on credit exposures include: deposits held by customers, pledge of quoted shares, residential/commercial property mortgages, investment securities, counter-guarantees from other banks, etc. Other risk mitigants considered include salary and end of service benefits assignment for personal loans, personal guarantees of promoters, etc. However, for purposes of capital adequacy computation, only eligible collateral recognised under Basel III is taken into consideration.

The Bank's credit policy defines the types of acceptable collateral and the applicable haircuts or loan-to-value ratio. The Bank has a policy of independent valuation of collateral. In the case of real estate, valuation is done by independent valuer at regular intervals as stipulated in the Bank's credit policy. In respect of quoted shares and other securities, the valuation is done based on the closing price on the stock exchange. The market value of the collateral is actively monitored on a regular basis and requests are made for additional collateral as required in accordance with the terms of the underlying agreements. In general, lending is based on the customer's repayment capacity and not the collateral value. However, collateral is considered as a secondary alternative to fall back on in the event of default.

Eligible financial collateral presented by portfolio is as follows:

In BHD millions	Gross credit exposure	Financial collateral	Credit exposure after risk mitigation
Sovereign portfolio	1,601.7	-	1,601.7
PSE portfolio	0.2	-	0.2
Banks portfolio	362.5	52.6	309.9
Corporates portfolio	402.3	40.1	362.2
Regulatory retail portfolio	409.7	2.7	407.0
Residential mortgages portfolio	29.3	-	29.3
Equities/funds portfolio	97.6	-	97.6
Past due exposures portfolio	68.4	3.1	65.3
Others assets	79.4	-	79.4
	3,051.1	98.5	2,952.6

On and off-balance sheet netting
The bank enters into netting agreements during the normal course of business, the agreements provide the bank with the legal rights to set off balances from specific counterparties, for both on and off-balance sheet exposure.

The amount of financial assets and financial liabilities set off under netting agreements amounted to BHD 64.2 million at 31 December 2018.

MARKET RISK
The Bank applies the standardised method for allocating market risk capital. The Bank has clearly documented policies and procedures for the management and valuation of the trading portfolio. The treasury operations department, which is independent of the treasury front office, is responsible for valuation. Valuation is performed on a daily basis, based on quoted market prices from stock exchanges, independent third parties or amounts derived from cash flow models, as appropriate.

In BHD millions		Capital Charge		
Risk type	**Amount**	**Maximum**	**Minimum**	**Average**
Interest rate risk	4.0	4.8	0.8	2.5
Foreign exchange risk	-	0.2	-	-
Total minimum capital required for market risk	4.0			
Multiplier	12.5			
Market risk weighted exposure under the standardised method	50.2			

OPERATIONAL RISK
Whilst the Bank recognises that operational risks cannot be eliminated in its entirety, it constantly strives to minimise operational risks (inherent in the Bank's activities, processes and systems) by ensuring that a strong control infrastructure is in place throughout the organisation and enhanced where necessary. The various procedures and processes used to manage operational risks are regularly reviewed and updated and implemented through effective staff training, close monitoring of risk limits, segregation of duties, appropriate controls to safeguard assets and records, regular reconciliation of accounts and transactions, and financial management and reporting. In addition, regular internal audit and reviews, business continuity planning and arrangements for insurance cover are in place to complement the processes and procedures.

The Bank applies the basic indicator approach for assessing the capital requirement for operational risk. The capital requirement of BHD 192.5 million is based on the gross operating income (excluding profit/loss on debt instruments classified as fair value through other comprehensive income, amortised cost categories and any exceptional items of income) for the last 3 years multiplied by 12.5 to arrive at the operational risk-weighted exposure.

EQUITY POSITION IN THE BANKING BOOK
The Bank holds certain investments in equity securities as part of its strategic holdings (including investment in associates) and others are held with the objective of capital appreciation and realising gains on sale thereof. The accounting policies for "FVOCI" and "Investment in associates" are described in detail in the financial statements under "Significant Accounting Policies".

Risk and Capital Management Disclosures (continued)

For the year ended 31 December

EQUITY POSITION IN THE BANKING BOOK (continued)

Details of equity investments

In BHD millions	Amount	Amount subject to risk weight	Minimum capital requirement at 12.5%
Non-significant investment in the common shares			
Listed equities	**28.6**	**28.6**	**3.6**
Unlisted equities	**3.0**	**3.0**	**0.6**
Significant investment in the common shares of financial entities >10%	**49.0**	**49.0**	**15.3**
	80.6	**80.6**	**19.5**
Unrealised gains from equities fair value	**14.7**		
Deduction from CET 1 (significant investments in common stock of financial entities)	**14.9**		

INTEREST RATE RISK IN THE BANKING BOOK

Interest rate risk positions are managed by the treasury department. Reports on overall position and risks are submitted to senior management for review and positions are adjusted if deemed necessary. In addition, ALCO regularly reviews (at least on a monthly basis) the interest rate sensitivity profile and its impact on earnings. Strategic decisions are made with the objective of producing a strong and stable interest income stream over time.

Duration analysis is used to measure the interest rate sensitivity of the fixed income portfolio. Duration of the portfolio is governed by economic forecasts, expected direction of interest rates and spreads. Modified duration gives the percentage change in value of the portfolio following a 1 percent change in yield. Modified duration of the Bank's fixed income portfolio was 1.27 percent on 31 December 2018 implying that a 1 percent parallel upward shift in the yield curve could result in a drop in the value of the portfolio by BHD 4.7 million.

Deposits without a fixed maturity are considered as repayable on demand and are accordingly included in the overnight maturity bucket. The Bank usually levies a pre-payment charge for any loan or deposit, which is repaid/withdrawn before the maturity date, unless it is specifically waived. This prepayment charge is to take care of any interest rate risk that the Bank faces on account of such prepayments and accordingly, no assumptions regarding such pre-payments are factored for computation of interest rate risk in the banking book.

The Bank uses interest rate gap analysis to measure the interest rate sensitivity of its annual earnings due to re-pricing mismatches between rate sensitive assets, liabilities and derivatives positions. The asset and liability re-pricing profile of various asset and liability categories is set out below:

In BHD million	Up to 3 months	3 to 6 months	6 months to 1 year	1 year to 5 years	Over 5 years	Rate insensitive	Total
Cash and balances at central banks	-	-	-	-	-	**107.3**	**107.3**
Treasury bills	**172.0**	**103.4**	**111.7**	-	-	-	**387.1**
Placements with banks and other financial institutions	**244.5**	-	-	-	-	**15.2**	**259.7**
Loans and advances	**364.9**	**61.4**	**130.6**	**510.4**	**122.8**	-	**1,190.1**
Investment securities	**1.9**	**4.3**	**194.5**	**625.9**	**250.5**	**55.1**	**1,132.2**
Investment in associates and other assets	-	-	-	-	-	**119.1**	**119.1**
Total assets	**783.3**	**169.1**	**436.8**	**1,136.3**	**373.3**	**296.7**	**3,195.5**
Liabilities and equity							
Due to banks and other financial institutions	**350.1**	-	**0.8**	-	-	**30.5**	**381.4**
Borrowings under repurchase agreements	**103.9**	-	-	-	-	-	**103.9**
Customers deposits	**786.0**	**165.0**	**263.8**	**47.9**	-	**927.9**	**2,190.6**
Other liabilities	-	-	-	-	-	**43.8**	**43.8**
Equity	-	-	-	-	-	**475.8**	**475.8**
Total liabilities and equity	**1,240.0**	**165.0**	**264.6**	**47.9**	-	**1,478.0**	**3,195.5**
On balance-sheet interest rate sensitivity gap	**(456.7)**	**4.1**	**172.2**	**1,088.4**	**373.3**	**(1,181.3)**	-
Off balance-sheet interest rate gap	**630.2**	-	**(6.3)**	**(408.1)**	**(215.8)**	-	-
Cumulative interest rate sensitivity gap	**173.5**	**177.6**	**343.5**	**1,023.8**	**1,181.3**	-	-

The interest rate risk management process is supplemented by monitoring the sensitivity of the Bank's financial assets and liabilities to an interest rate shock of 200 bps increase/decrease on the balance sheet. An analysis of the Bank's sensitivity to an increase or decrease in market interest rates (assuming no asymmetrical movement in yield curves and a constant balance sheet position) is as follows:

In BHD millions	200 bps parallel increase	200 bps parallel decrease
As at 31 December 2018	**5.6**	**(5.6)**
Average for the year	**6.2**	**(6.2)**
Minimum for the year	**3.6**	**(3.6)**
Maximum for the year	**10.4**	**(10.4)**

These disclosures have been prepared in accordance with the Public Disclosure Module ("PD"), CBB rule book, Volume I for conventional banks. These disclosures should be read in conjunction with the notes to the financial statements, in particular the significant accounting policies and financial risk management.

These disclosures have been reviewed by the Bank's external auditors based upon agreed-upon procedures as required under paragraph PD-A.2.4 of the PD module.